



To: Clients, Associates & Friends of Pro@ctive CPA  
From: Mark L. Wyssbrod, Managing Member  
Date: December 6, 2010  
Re: Employees Verses Independent Contractors

During the past several months tax publications and update courses have informed and warned tax professionals that the Internal Revenue Service (IRS) and state taxing authorities (including Georgia Department of Revenue and Georgia Department of Labor) are looking into employment tax audits. The warnings have become louder over each of the following years for about a decade. The audits are to review you are remitting your payroll tax payments timely, filing your payroll tax returns timely and accurately and you are you classifying your employees and contractors correctly?

Please note this information is to be received as general tax information and not specific tax advice. Please contact us at (770) 664-8583 should you have any questions.

In our transmittal letters which accompany our tax returns we remind our clients of this classification with the following paragraph:

Recent articles and tax updates indicate the IRS is targeting employers for misclassifying contractors and employees. Please review the IRS's Publication 15-A Employers Supplemental Tax Guide (<http://www.irs.gov/pub/irs-pdf/p15a.pdf>). Please contact me to discuss.

The real test is if you have behavior control, financial control and the type of relationship between the parties.

Behavior Control is if you have the right and control for how the worker completes a task. This includes when and where they complete the task, what equipment or tools they use to complete the task, which workers will assist them, where to purchase supplies or services, what work must be completed by specific individuals and what order or sequence is to be followed.

Financial Control is the facts that show whether the business has the right to control the business aspects of the worker's job. This includes the extent to which the worker will be reimbursed for business expenses, the extent of the worker's investment, the extent the worker's business is offered to the relevant market, how the business pays the worker and the extend the worker can realize a profit.

Types of Relationship is the facts that define the relationship. This includes written documents defining the relationship, whether the worker is provided employee-type benefits (insurance, etc.), permanency of relationship and the extent to which the services performed by the worker are a key aspect of the regular business of the company.



**Why is this important to you as a business owner?** This is really important to you as a business owner because a contractor can complete Form 8919 if they believe they should have been an employee. This will trigger the IRS to complete a full audit of the business, even if the contractor is incorrect. This could lead to a large Social Security and Medicare liability and a distraction of an audit. **The audit can result in thousands, tens of thousands, perhaps even hundreds of additional Social Security and Medicare taxes due!**

Several case studies have ended with the small business filing for bankruptcy protection. Unfortunately, payroll taxes are not forgiven in bankruptcy and the officers of the company can be held personally liable for the “trust” portion of the taxes.

**How can you protect your business?** You can protect your business from having contractors reclassified to employees by taking a few pro-active steps, including, but not limited to:

- Contract only with legal entities (must has an LLC, LP or a Inc. at the end of it name)
  - Have your current individual contractor form a legal business
  - Be careful that the facts and circumstances do not trump the legal entity payment system
    - i.e. if you have a bunch of single owner legal entities the IRS may view them as employees instead of contractors, especially if you are the single source of revenue
- Set up Vender Files for each relationship
  - Have a written document stating the type of the relationship
    - i.e. Contract
  - Complete Form W-9
    - <http://www.irs.gov/pub/irs-pdf/fw9.pdf?portlet=3>
  - Complete Form SS-8 and have the IRS determine the relationship for you
    - <http://www.irs.gov/pub/irs-pdf/fss8.pdf>
  - If any individual, be certain to retain a copy of the contractors:
    - Driver’s license
    - Social Security Card
- Be certain to issue all required 1099-MISC
  - You are required to issue a 1099-MISC
    - At least \$600 in rents, services (including parts and materials), prizes, awards, other income, medical and health care payments, crop insurance proceeds, cash payments for fish, or, generally the cash paid from a notional principal contract *to an individual, partnership or estate*;
    - If you paid \$10 or more in Royalties;
    - Any fishing boat proceeds; and/or
    - Proceeds to an attorney



- To review the instructions for issuing 1099-MISC visit <http://www.irs.gov/pub/irs-pdf/i1099misc.pdf>
- Follow the aforementioned rules!

Sometimes the differences between employees and contractors can be tricky. Please contact your Pro@ctive CPA team should you have any questions (770) 664-8583 or [mark@pro-active-cpa.com](mailto:mark@pro-active-cpa.com).

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