Not So Fast

What you need to know before hiring independent contractors

By Masarah Van Eyck

Many businesses — the computer industry at the top of the list — know the benefits of hiring independent contractors well. Independent contractors work in their own space with their own equipment, cutting down on a business's overhead; they are hired per task, ensuring efficiency; and the contracts are finite, meaning you don't have commitments beyond each project. Most appealing, businesses are not usually required to provide the health insurance or worker's compensation, or withhold the taxes that employee relationships require. They also don't have to pay the employer's portion of an independent contractor's FICA taxes.

But, while many businesses understand the benefits of hiring independent contractors, they may not fully understand the legalities. And without full compliance with the requirements set by the IRS and state of Wisconsin, businesses put themselves at risk of liability and fines.

This isn't to say that the benefits aren't still as great — you just want to take some preventive measures to ensure your relationship is legitimate.

Playing by the rules

"The most common misunderstanding that businesses have about hiring independent contractors is that the IRS will consider the person an independent contractor simply because the business labels the person as such," says attorney **Jennifer Kreuger**, who practices in the area of business law and is a shareholder at **Murphy Desmond S.C.**


Jennifer Krueger
Murphy Desmond S.C.

Just signing a contract — even if you both agree to it — isn't enough to legitimize an independent contractor relationship. In fact, the IRS will presume a worker is your employee unless the worker can prove otherwise. This requires that the relationship comply with a 20-factor test. The state of Wisconsin has its own 9-point test to do the same.

"The biggest factor is control," Kreuger says. "As a general rule, the business has the right to control or direct only the result of the work done by an independent contractor and not the means and methods of accomplishing the result."

In other words, it is the independent contractor who decides where and how the work gets done. A business owner cannot direct, for instance, what tools to use or whom the independent contractor hires to assist with the work. In turn, the independent contractor is responsible for all of his or her operating expenses, and for the profit or loss of such work.

Beyond control, other factors have equal weight in determining independent contractor

Resources for ensuring independent contractor status

IRS: www.irs.gov/govt/fslg/article/0,,id=110344,00.html

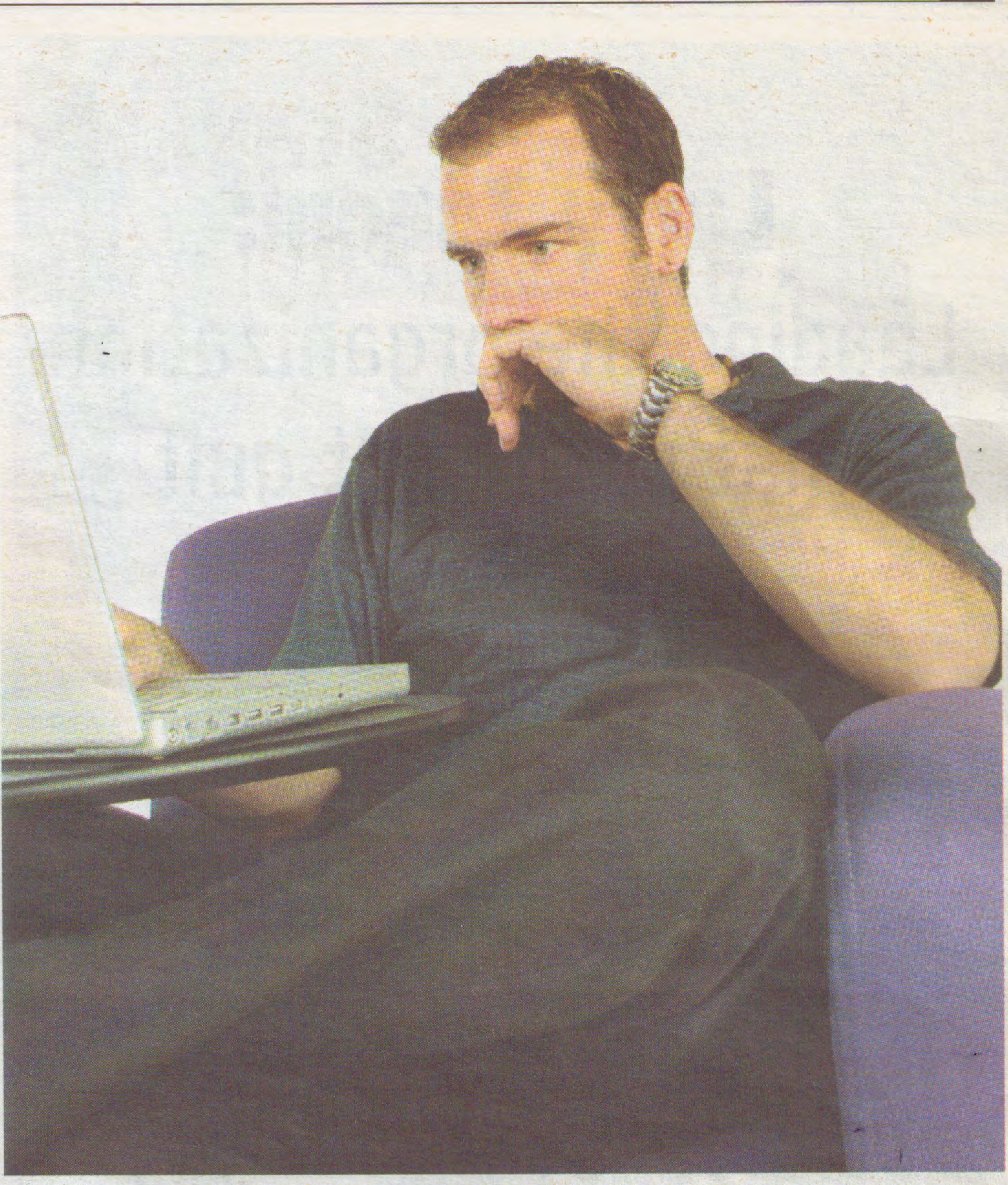
Small Business Association: www.sba.gov/wi/WI_STARTUP.html

Department of Workforce Development: dwd.wisconsin.gov

For **Workers Compensation**: 608-266-3046, dwd.wisconsin.gov/wc

For **Labor Standards** information: Equal Rights Division: 608-266-6860, dwd.wisconsin.gov/er

For questions on **unemployment insurance:** 608-261-6700, dwd.wisconsin.gov/ui



status. The state of Wisconsin, for example, requires an independent contractor to have his or her own business and a Federal Employer Identification Number (FEIN) to show for it. And the parameters around what an independent contractor is — and isn't — hired for are strict. This is where things can get sticky.

Why all the fuss?

Take the issue of worker's compensation. If an injury occurs in covered employment, the injured worker is automatically entitled to compensation for wage loss and medical benefits. However, an independent contractor is limited to those benefits and the employer is protected from any other lawsuit by the worker, thanks to Wisconsin's Worker Compensation Act.

As an example, if your business hires someone to do electrical work, but then that person is asked to perform something else, such as drop off equipment at another site on the way home. While seemingly minor, the second task is not under the independent contractor's agreement. What if that individual is injured during the delivery? Your business is liable and will likely have to pay worker's compensation.

In many ways, the tight stipulations are meant to protect your business from these claims. As **Rose Lynch**, director of communications for the **Department of Workforce Development**, says, "the Worker's Compensation Act provides protection for the employer as well as the worker."

Rose Lynch
Department of Workforce Development

How to be sure

Resources that lay out the basic rules of the relationship are readily available on the Web, but a quick phone call can save hours and dollars in the end. "Each situation can be different," says Lynch, "so we strongly suggest that employers contact us so we can discuss their specific circumstances." Her office can answer most of your questions about worker's compensation, labor standards and unemployment insurance.

For really tricky issues, consulting your lawyer isn't a bad idea either. "In the best-case scenario, a client will come to me when he or she is thinking about contracting with someone on an independent contractor basis," says Krueger. "If lawyers are involved in the early stages, we can educate the parties and structure the relationship to minimize the risk of the IRS later objecting to the classification of the relationship." ■