

GUIDELINES FOR DETERMINING EMPLOYEE OR INDEPENDENT CONTRACTOR RELATIONSHIPS

Under University policy, contracts will generally only be entered into with independent contractors (IC). Independent contractors are individuals or firms that (1) are engaged to perform specific services for a stated fee or contracted amount, (2) provide services to the public, and (3) are subject to University control only as to the end results, and not the methods of obtaining them. Individuals who are not independent contractors should be placed on the University's payroll.

The determination of an individual's status as an employee or independent contractor should be made **prior to** an engagement to perform services. Such determination is critical in accurately assessing the University's tax obligation. Where an individual is classified as an employee, the University must meet the overhead costs of withholding income and FICA/Medicare taxes and match the employer's share of these taxes. In addition, other obligations such as vacation, sick pay, worker's compensation insurance, health insurance and pension plan contributions may be incurred by the University for employees. Conversely, if the worker is classified as an IC, the University has no obligation to withhold income or FICA taxes on amounts paid to an IC. However, if an IC does not furnish a correct taxpayer identification number (TIN), i.e., social security number or employer identification number, or does not certify that the TIN is correct, the backup withholding rules require that income tax be withheld at a rate of 31%. The University must report remuneration of \$600 or more per calendar year on Form 1099-MISC, if the contractor is not a corporation.

To determine how to treat payments for services by individuals, the business relationship that exists between the University and the individual performing the services must be evaluated. Assessing the degree of control and independence is dependent on all the facts and circumstances of a particular situation. The Internal Revenue Service (IRS) does not consider any one factor or set of factors as necessarily controlling or decisive. Rather, the IRS stresses, "All information that provides evidence of the degree of control and the degree of independence must be considered".

The courts have considered many facts in deciding whether a worker is an independent contractor or an employee. These relevant facts fall into three main categories that are defined below: behavioral control; financial control; and relationship of parties. As noted above, in each case, it is very important to consider all the facts – no single fact provides the answer.

BEHAVIORAL CONTROL: Facts that show whether the University has a right to direct and control how the worker does the task for which the worker is hired include the type and degree of:

- **Compliance with Instructions** – An individual who must comply with another person's instructions about when, where or how to work, generally is considered an employee. This applies even if the person simply has the right to require compliance, but does not exercise that right. The more detailed the instructions are that the worker is required to follow, the more control the business exercises over the worker, and the more likely the business retains the right to control the methods by which the worker performs the work. The absence of detail in instructions reflects less control.

- **Training** – Providing a worker with training about required procedures and methods is indicative that the business wants the work done in a certain way, and this suggests that the worker may be an **employee**.

- **Personal Services Required** – Employee status is suggested if an individual is required to personally render the services in question. Such an arrangement, says the IRS, indicates the employer is interested in controlling the methods used to accomplish the results. By contrast, an individual's right to substitute another's services without the employer's knowledge suggests the existence of an independent contractor relationship.

- **Control Over the Hiring, Supervising and Paying of Assistants** – An employer that hires, supervises and pays an individual's assistants usually is viewed as controlling the work (and the individual performing the services) in question. On the other hand, individuals who hire, supervise and pay other workers in accordance with an arrangement in which they have agreed to provide the labor needed to attain a certain result are generally treated as independent contractors.

- **Set Hours of Work** – A requirement that individuals adhere to certain work hours established by the employer generally is viewed as a factor indicating employer control. Independent Contractors set their own work hours.

- **Full-time Work Requirement** – Employee status is suggested if an individual must work on a substantially full-time basis for the employer since this indicates that the employer controls the amount of time the individual spends working and thus essentially restricts the worker's ability to perform for someone else. By contrast, independent contractors are free to work when and for whom they choose.

- **Working on the Employer's Premises** – Performance of the work on employer's premises may be viewed as evidence of employer control, especially if the work could be done elsewhere. While performance at an off-premises site demonstrates some freedom from employer control, it does not by itself mean that the worker is an independent contractor. Employer control is suggested when the employer has the right to have the worker work at a specific place.

- **Furnishing of Tools and Materials** – An employer-employee relationship is indicated where an employer supplies a worker with a significant amount of tools, materials or other equipment. Moreover, in some occupations and industries where it is customary for individuals to provide their own tools, these workers also may be treated as employees.

- **Required Work Order Sequence** – A degree of control is suggested, says the IRS, where an individual is required to submit regular oral or written reports to the employer.

FINANCIAL CONTROL: Facts that show whether the University has a right to control the business aspects of the worker's job include:

- **Payment by the Hour, Week or Month** – Employees generally are paid by the hour, day or month, while independent contractors typically are paid by the job or on a lump sum or straight commission basis.

- **Payment of Business or Travel Expenses** – Employer payment of work related business or travel expense generally indicates employee status.

- **Investment in Facilities** – Workers are likely to be viewed as independent contractors if they have a significant investment in facilities they use in the course of performing services.

- **Worker’s Availability to the General Public** – Individuals who make their services available to the public on a “regular and consistent basis” are generally treated as independent contractors.

- **Working for More Than One Firm** – Individuals who perform services for a number of businesses or people at the same time usually are considered independent contractors. IRS cautions however, that “a worker who performs services for more than one person may be an employee of each of the persons, especially where such persons are part of the same service arrangement”.

THE TYPE OF RELATIONSHIP OF THE PARTIES: Facts that show the parties’ type of relationship include:

- **Employer’s Discharge Rights** – If an employer has the right to discharge an individual, that worker is viewed as an employee. Independent contractors cannot be fired as long as they perform in accordance with their contract specifications.

- **Integration into the Business** – The fact that an individual’s services are so integrated into an employer’s operations that the success or continuation of the business depends on the performance of the services generally indicates that the individual is subject to a certain amount of control by the owner of the business.

- **Worker’s Termination Rights** – Employees typically can end their employment relationship at any time without incurring liability, whereas independent contractors might be liable for a breach of contract if they leave without completing their work.

- **Written Contracts** – Written contracts describe the relationship the parties intended to create.

- **Employee Type Benefits** – Whether or not the University provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay, will determine the type of relationship that exists. Employees typically are paid benefits while Independent Contractors are not.

- **Permanency of the Relationship** – A worker engaged with the expectation that the relationship will continue indefinitely, rather than for a specific project or period, is generally considered evidence that the intent was to create an employer-employee relationship. Independent Contractors are hired to perform a service over a limited and specified amount of time which is spelled out in the written contract.

It is irrelevant that the employer allows the individual considerable discretion and freedom in deciding how to perform or carry out the work of the job. Rather, the decisive factor is that the employer possesses the legal right to control or direct both the results and the method of the work or services in question. As long as the employer is entitled to control both, what must be done and how it gets done, the individual worker is **NOT** an independent contractor.

The following basic guidelines, applicable specifically to Extension and Public Service instructors, may be used to help University administrators determine whether an individual hired for temporary service with University Extension should be hired as an employee or retained as an independent contractor:

1. All University faculty and other academic appointees retained to provide teaching services to University Extension must be hired as employees, irrespective of the length of the course or program. Non-academic personnel may be retained as independent contractors to provide such services pursuant to 3. and 4. below.

2. Except as provided below, an instructor or other person who is in charge of a University Extension or Public Service course or program must be hired as a University employee. This classification applies whether or not credit is given.
3. Individuals retained to provide the following temporary services should be treated as independent contractors:
 - a. A person who is to participate as a guest lecturer on one or more occasions in a University Extension course or program,
 - b. A person who is to participate on one or more occasions as a panelist or workshop participant in a University Extension course or program,
 - c. A panelist for a University Extension course or program that consists exclusively of one or more panel discussions, and
 - d. An instructor retained to teach a course or courses of short duration, provided that the total number of days that the person teaches does not exceed 5 calendar days in one calendar year. Each day devoted to teaching would count as one calendar day regardless of the number of teaching hours worked in any of those days.
4. An instructor who is retained to teach a course of *longer duration* than that specified in 3.d. above may be retained as an independent contractor only if he or she is either (i) a bona fide employee of a company or organization that provides similar teaching services to others, or (ii) operating an independent business that provides similar teaching services to others. In determining whether the individual is operating an independent business, the following factors should be considered:
 - a. Does the individual provide more than *de minimus* services to other clients at the same time?
 - b. Does the individual appear to be operating a bona fide business (e.g., is the individual incorporated or does he or she have a taxpayer identification number, business license, business letterhead, a separate business location, etc.)?
 - c. Does the individual receive payment based on a flat fee for services performed, as opposed to being paid on an hourly basis?
 - d. Does the individual advertise his or her services?

In addition to the federal regulations pertaining to the determination of independent contractor or employee status, the State of Tennessee may also be involved in this determination for purposes such as unemployment compensation. According to the State of Tennessee Employment Security, an individual is considered to be an **independent contractor** if all three of the following criteria are met.

- a. The individual has been and will continue to be free from control or direction over the performance of such services under their contract of service; and
- b. The service is either outside the usual course of the business for which such service is performed or outside of all places of business of the enterprise for which such service is performed; and
- c. The individual is customarily engaged in an independently established trade, occupation or business.

In some instances, a worker can qualify as an independent contractor for federal income tax purposes but determined to be an employee for state unemployment insurance purposes.

Misclassification of employees as independent contractors carries significant penalties. An employer who classifies an employee as an independent contractor, with no reasonable basis for doing so, may be held liable for employment taxes for that worker. While an employer’s liability may be mitigated by Section 530 safe harbor provision, the safety net extends only to employment taxes and provides no relief in other employment areas such as potential retirement benefits issues.

FLOWCHART TO DETERMINE SERVICE PROVIDER STATUS

