

IRS Common Law Rule and Twenty Factors

For use in determining consultant or employee status

Since there are no explicit statutory standards for determining a worker's status under the employment tax laws, the IRS has identified twenty classification factors, based on common law standards, that can be used to determine whether the employer has the right to *direct* and *control* the detail and means of a worker's duties. However, because business relationships change over time, the IRS and the courts have determined that some of the twenty factors are no longer as relevant as they once were.

The primary factors listed below include key facts that illustrate *the right to direct and control*, or its absence. Although every factor is not necessarily present in every case, generally an employer-employee relationship exists when a worker:

- 1) Must comply with the employer's **instructions** about when, where, and how to do the job. (The weight of "instructions" depends on the degree to which instructions apply to *how to get the job done* rather than to the *end result*. However, instructions imposed by the employer in compliance with governmental or governing body regulations should be given little weight. Instructions may be in the form of manuals or written procedures.)
- 2) Receives **training** from or at the direction of the employer. (Periodic or on-going training about procedures to be followed and methods to be used indicates that the employer wants the services performed in a particular manner and is strong evidence that an employer-employee relationship exists.)
- 3) Lacks a **significant investment** in facilities used to perform services. (A significant investment is evidence that an independent contractor relationship may exist; however it is *not* required for independent contractor status.)
- 4) Receives payments for business and/or traveling **expenses**. (Independent contractors are more likely to have unreimbursed expenses. In addition, the opportunity for profit or loss exists if expenses are unreimbursed.)
- 5) Does not offer **services** to the general public. (Any requirement that the individual work exclusively for one employer detracts from the argument that the worker is an independent contractor.)
- 6) Receives payments of regular amounts at set intervals. (Performance of a task for a flat fee is generally evidence of independent contractor status. **Payment by the hour, week, or month** usually indicates an employer-employee relationship.)
- 7) Cannot make a **profit** or suffer a **loss** from services. (The ability to realize a profit or incur a loss is probably the strongest evidence that a worker controls the business aspects of services rendered and is an independent contractor.)
- 8) Can be **terminated** by the employer. (Since employers rarely have complete flexibility in discharging an employee, the inability to freely discharge a worker, *by itself*, does not constitute sufficient evidence that the worker is an independent contractor.)
- 9) May quit work at any time without incurring liability. (The presence or absence of limits on a worker's ability to **terminate**, *by itself*, does not constitute sufficient evidence in determining a worker's status. On the other hand, an employer's ability to refuse payment for unsatisfactory work is characteristic of independent contractor status.)
- 10) Has a **continuing working relationship** with the employer. (The relationship is considered continuing, even if the services

are rendered on a part-time basis, are seasonal in nature, or if the individual actually works for only a short time.)

- 11) Provides services that are **integrated into the business**, i.e., the success or continuation of the employer's business depends significantly on the performance of certain services that the worker provides.

The following factors are generally considered less important in determining a worker's status:

- 12) Provides services that must be rendered personally.
- 13) Hires, supervises, and pays assistants on behalf of the employer, or if the employer hires, supervises, or pays assistants for the worker. (An independent contractor usually determines whether to hire assistants and, if so, whom to hire and what to pay them.)
- 14) Must do the work in a sequence set by the employer.
- 15) Must submit regular oral or written reports to the employer. (If a contract between the employer and an independent contractor specifies that the job must be completed to the satisfaction of the customer, the employer may avoid the need for reports from the independent contractor. *Reports are usually an indication of employee status, since the worker must account for his or her actions.*)
- 16) Relies on the employer to furnish tools and materials.
- 17) Works for only one employer at a time.
- 18) Must follow set hours of work.
- 19) Works full-time for the employer.
- 20) Does the work on the employer's premises, or on a route or at a location designated by the employer.

In addition, the fact that an individual's *relationship with a business is temporary* should be given little weight in making an employee/independent contractor determination. Although an independent contractor will typically have a temporary relationship with a business, so too will employees engaged on a seasonal, project, or an "as needed" basis.

APPLYING THE TWENTY FACTORS

Using the common law classification factors is not a simple or straightforward process since the IRS's position is that the classification factors should be used only as guidelines and that *every piece of information that helps determine the extent to which the employer retains the right to control the worker is important*.

Applying the 20 factors to a particular situation can be difficult and confusing because the importance assigned to each factor can vary significantly depending on the facts and circumstances of each case. The fact that more than half of the factors may point to one result does not necessarily mean that it is the correct result; rather, *all of the facts must be analyzed to determine whether certain factors may be more important than others under the particular circumstances*. The weight given to a particular classification factor depends on the worker's occupation and the context in which the services are performed. No one factor is determinative; the IRS will consider the answers to all relevant questions when making its decision. However, ***the IRS leans toward classifying individuals as employees rather than as independent contractors.***