

## CONTRACTORS VS. EMPLOYEES FAST FACTS TIP SHEET

### OVERVIEW

Classifying workers as an independent contractors (ICs) is appealing to many employers because it eliminates the need to pay an assortment of taxes, insurance premiums, and benefits. However, the act of classifying a worker as an IC should be undertaken with caution. At the end of the day, most workers – per the IRS and the Department of Labor – are employees.



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### THE TESTS

The IRS and the Department of Labor (DOL) each have their own test for determining whether a worker is an IC or employee. Both tests are factors tests, meaning they ask numerous questions and require employers to look at the answers as a whole to see if the scale tips more in favor of the worker being an employee or IC.

The IRS calls their test the “Right-to-Control Test,” while the DOL calls theirs the “Economic Reality Test.” The tests are extremely similar and should yield the same result. However, if you apply both tests and come to different conclusions, erring on the side of “employee” is the safe bet.

Which test is applied if a classification is challenged will depend on what kind of claim the worker is bringing. For instance, if a worker goes to the Oregon Bureau of Labor and Industry (BOLI) with a wage and hour claim, BOLI will use the Economic Reality Test; if they go to BOLI with a civil rights claim, the Right-to-Control Test will be applied. Let’s take a look at the tests.

### ECONOMIC REALITY TEST

The Economic Reality Test focuses on who bears the financial burden for overhead as well as whether the worker is financially dependent upon the employer. The DOL presents this as a six-part analysis:

- 1. Work is Integral to the Business:** Is the work an essential part of the business’s offering or operations? The work of a fundraiser at a non-profit is integral to the business, whereas the work of someone who was hired to redesign the NPO’s website is not. The more integral, the more likely the worker is an employee.
- 2. Managerial Skill:** Do the worker’s managerial skills (either self-management or management of others) impact their personal profit or loss? If so, that is a mark in favor of the IC classification.
- 3. Relative Investment and Risk of Loss:** Who spends the most and has the most to gain or lose if the worker is successful? If the worker bears more of the burden, they are more likely an IC.

- 4. Skill and Initiative:** Does the worker use skill and initiative to sell and provide their services on the open market? If so, they are more likely an IC.
- 5. Permanency of Relationship:** Is there an agreement indicating the worker has been hired for a specific period of time or project? If so, that’s a mark in favor of an IC classification.
- 6. Nature and Degree of Control:** How much control does the employer have over the work – specifically when, where, and how it gets done? The more control the employer has, the more likely the worker is an employee.

### RIGHT TO CONTROL TEST

This test looks at the level of control over the work held by the worker and the employer. There are three areas of evaluation:

- 1. Behavioral Control:** Does the company control, or have the right to control what the worker does and how they do it? If yes, they are more likely an employee.
- 2. Financial Control:** Are the business aspects of the worker’s job controlled by the employer? Does the employer reimburse expenses, provide tools, or pay the professional liability insurance of the worker? If yes, they are more likely an employee.
- 3. Type of Relationship:** If there is a written contract, what does it say? If it’s indefinite, the worker is more likely an employee. And does the worker receive benefits usually given to employees, such as health insurance, vacation time, or profit sharing? If yes, they are more likely an employee.

### IN CONCLUSION

These tests can be tough, since the answers are often not cut and dry. But when in doubt, err on the side of “employee” and pay the appropriate taxes and insurance premiums.

### FOR MORE INFORMATION

Need one-on-one help determining worker classification? Mammoth HR can help! To learn more, visit: [mammothhr.com/nao](http://mammothhr.com/nao) or call (844) 455-8706.