

Triangle Business Journal - May 29, 2006

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TRIANGLE BUSINESS JOURNAL

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Walking a contractor-employee tightrope

Triangle Business Journal - May 26, 2006 by [Clint Johnson](#)

WINSTON-SALEM - It's a snare that's tripped up major employers such as Microsoft, IBM, Coca-Cola and Federal Express, but legal experts say it more often foils small to midsize businesses that can easily be caught unaware.

It's the thin line between independent contractors and employees, and it's increasingly a dilemma for employers. Studies estimate the number of contingent workers is growing anywhere from three to five times the pace of full-time workers, making the employee-contractor distinction a growing challenge.

For example, more than five years ago, Microsoft paid nearly \$100 million to settle a case involving differences in how it was treating contractors and employees who, the plaintiffs contended, were doing comparable work.

In December, FedEx lost a six-year-old case in California where the company claimed that people driving leased delivery trucks with its logos on the sides of the trailers were contractors just like other independent truckers. Thirty similar suits filed against FedEx in 25 states have been consolidated into a class action suit to be tried in Indiana.

Charlot Wood, a labor attorney with Bell, Davis & Pitt law firm in Winston-Salem, says small employers simply are not familiar with even the basic rules. "Smaller employers tend to commit this kind of violation," Wood says.

"These people have been doing things the same way for a long time and it hasn't occurred to them that it is against the law," Wood says.

The Internal Revenue Service's Form 15-A and an article on its Web site describe the conditions under which workers are employees and contractors.

Twenty are listed and are called "common law," with the number one rule being that if an employer tells someone how to do the job and when it needs to be done, as most managers do, they could be employees.

The rules are clear, at least in the view of the IRS. "You don't have options as to how you treat employees," says Gloria Wajciechowski, a spokesperson for the IRS. "The rules are specific. The major thing is if the employer has 'behavioral control' over how the person does the task."

If the employer sets down the rules on when and where to do the work, provides the tools to do the work, tells the person what other workers can be hired to assist in the work and where supplies must be purchased, then the person is almost certainly an employee rather than a contractor.

"If you are controlling the hours someone works and telling him how you want the job done, you have an employee," Wajciechowski says.

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It is then the company's responsibility to follow expected routines such as withholding taxes, paying Social Security and workers' compensation costs.

One of the IRS' examples defining an employee versus a contractor describes a woman who hires subcontractors to build a house. The woman tells the subcontractors how she wants her house to be built and from where to buy building materials, which fits the definition of employer.

Pay now or pay later

When the IRS catches violators, it can increase the number of audits, levy open-ended penalties and interest, and in extreme cases, even file criminal charges.

Wood, the labor attorney, says the N.C. Industrial Commission has become more sensitive to contractors versus employees when dealing with workers' compensation claims.

"It is much easier to deal with something like this on the front end, because both criminal and civil penalties can apply on the back end," Wood says.

Kathy Bowman Atkins, president and co-owner of The Lattitude Group, a business strategy and coaching firm in Greensboro, says she sometimes finds contractors and employees working side by side doing the same thing - a clear violation of the law.

"I think 80 percent of the small businesses are violating the rules because they have not been exposed to them like the major companies have," Atkins says. "I think one key to avoiding problems is having the right accountant. Companies should find a CPA who has experience in this field, not just someone who can figure out the taxes and keep the books."

Atkins says that employers should make no effort to blur the differences between contractors and employees. She urges that

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