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1099 Or W-2?

This time of year that seems a logical question. It's short for "independent contractor or employee?" If you're an employee, you must be paid via a net check—on which tax withholdings are taken. That means you'll receive an [IRS Form W-2](#) from your employer in January the following year.

In contrast, if you're an independent contractor, you'll get full pay with no deductions, but are liable for your own taxes. Come January, assuming your total pay was \$600 or more, you'll receive an [IRS Form 1099](#). But is it that simple, and what if you're the employer rather than the recipient?

It turns out this is one of the more momentous decisions in the tax world. Yet this decision is made literally thousands of times a day all over America, often, it seems, without much thought. Some employers ask "1099 or W-2?" as if they were asking how you take your coffee.

If you're the worker, you may be tempted to say "1099," figuring you'll get a bigger check that way. Of course, you will in the short run, but you'll actually owe **higher** taxes. As an independent contractor, you'll owe not only the income tax, but self-employment tax too. On the first \$106,800 of income, that's a whopping 13.3% rate. Beyond \$106,800, the rate drops to 2.9%.

In contrast, if you're an employee, up to \$106,800 of pay, you pay only one half the Social Security tax, (your half is 4.2%) plus one half the Medicare rate (your half is 1.45%). Your employer pays the rest. Beyond

\$106,800, you pay only the 1.45%. This is an even more striking comparison in 2011, due to payroll tax changes made in President Obama's end-of-the-year tax bill. See [Extended Individual Tax Benefits In Compromise Bill](#).

That's not the only thing to keep in mind, of course, but it does suggest that it can be shortsighted to turn down employee status. Apart from tax law, employee status carries a host of nondiscrimination laws, pension and benefits laws and wage and hour protections that apply to employees but not to independent contractors.

For all of these reasons, employers have considerable incentives to try to pay independent contractors rather than employees. Often this can be done within the confines of the law in ways that are perfectly proper. Yet some employers clearly push the envelope to treat workers as "independent contractors" who rather clearly are employees if anyone would bother to look.

That's where the IRS and many other agencies come in. They can ferret out the truth according to various legal standards that often boil down to how much control the company has over the worker. See [Some Control Won't Convert Independent Contractors To Employees](#). The IRS has much to say on this. For example, see [Employee v. Independent Contractor—Seven Tips For Business Owners](#).

The area is heating up in a big way, with many believing that inappropriate worker status determinations are a major tax loophole. If you're an employer, be careful.

For more, see:

[Criminal Penalties For Misclassifying Independent Contractors?](#)

[White House On Contractor vs. Employee: There Will Be Blood](#)

[Miranda-Like Warnings To Independent Contractors?](#)

[Publication 15-A, Employer's Supplemental Tax Guide](#)

[Publication 1779, Independent Contractor or Employee](#)

[Publication 1976, Do You Qualify for Relief under Section 530?](#)

[Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding](#)

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