



Robert W. Wood

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Higher Minimum Wage Means More Independent Contractors-- And Disputes

Did President Obama just make independent contractor v. employee issues even bigger? Arguably, yes. His State of the Union Address noted that he would sign an executive order increasing the minimum worker wage for federal contracts from \$7.25/hour to \$10.10. But he made it clear that he wants a broader minimum wage increase in the private sector too.

The fact that the President and First Lady invited some fast food workers to see the State of the Union surely underscores the message. But for some, an increased cost for employees could have a safety valve: treating workers as independent contractors.

In some cases, those might be new workers. In some cases, they may be existing workers, as where an employer holds on to a pre-existing independent contractor classification. In some cases, the employer may know the independent contractor classification is aggressive.



President Obama standing before the President of the Senate and Speaker of the House. (Photo credit: Wikipedia)

There's no one size fits all solution for worker status problems. Even the IRS doesn't expect every single worker to be an employee. But there's no question that some employers push the envelope.

Higher payroll taxes can mean more pressure on companies to use independent contractors. So can higher benefit costs and mandated health insurance. And so can higher mandated wages.

And while it certainly doesn't give employers a pass to mislabel employees as independent contractors, there are considerable grey areas. Of course, from an economic viewpoint, it can be tempting indeed. There's no tax withholding on independent contractors—the contractor pays his own taxes.

Although it's unlikely that higher taxes on the worker's share will motivate employers to treat workers as independent contractors, there is a connection. Employers have a duty to withhold taxes from employees. That's one reason the IRS likes employees better than independent contractors. The IRS gets its tax money sooner and more reliably by withholding.

Does that mean everyone is an employee? Clearly not, but be reasonable. If you use independent contractors, consider the strength of your case and how

many workers you have. Tally the cost of fighting reclassification or giving in. If your case isn't strong, you may be able to revise your contract to improve it.

But you are better off considering these issues before an audit or litigation. A [Department of Labor \(DOL\) study](#) says up to 30% of employers misclassify workers, and a [GAO report](#) says the IRS is losing billions. But change is on the way. The DOL announced in 2010 that it would issue regulations requiring companies to write a classification analysis for all workers, including independent contractors. Plus, the IRS, DOL and state governments are swapping information.

[Business](#) owners and other “[responsible persons](#)” have personal liability and excuses are rarely accepted. The IRS can assess a [Trust Fund Recovery Assessment](#), also known as a 100% penalty, against every “responsible person.” See [Section 6672\(a\)](#). You can be liable even if have no knowledge the IRS is not being paid.

There can even be liability if you thought your workers were independent contractors and failed to withhold for that reason. If it turns out you did have a payroll after all, the company is liable for all the employment taxes and for failure to withhold income taxes. And even if the company is insolvent and can't pay, the responsible persons are on the hook personally.

You can reach me at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.