

The Independent Contractor Status Draws Scrutiny

Independent contractors are valid in various industries given the proper circumstances, including dentistry. However, the government has and will continue to look for abuses of the classification where employers attempt to use the classification to avoid employment taxes.

People who wish to be considered independent contractors (IC) should arrange their circumstances so that their case as an IC is defensible. Some of these circumstances may include: being able to perform work duties freely in the facilities of the owner, getting paid by the project or service (not hourly), paying for their own materials or supplies, using their own equipment, providing service not otherwise offered by the business owner, hiring and paying their own staff and control the result of their product or service. If these circumstances are not in place with the owner of the business, the general IC may not be an IC at all, they may be an employee.

One of our client's is a dental specialist. They don't own their own practice, they work in offices of other practitioners. They bring their own staff, they control their work process and the outcomes, their services are billed separately, they decide the days they work and because they're a specialist, the owner can't supervise their work (tell them how to do it). They also operate from their own entity so the contract is between two entities, an individual is not involved, other than the person providing the service.

Businesses must weigh the degree of the behavioral and financial relationships with workers when classifying them. The consequences for the owner who misclassifies an employee as an independent contractor could be: A) they're assessed the employer's portion of the social security and Medicare tax, B) federal unemployment tax, and, if the owner cannot prove the independent contractor reported the income on their return, they may also assess the employee's portion of social security and Medicare tax, plus penalties and

interest. If the owner had any employee benefit plans that should have covered the IC (health and retirement plans), there could be negative consequences there as well.

If you are an independent contractor, you are self-employed. To find out what your tax obligations are, visit the [Self-Employed Tax Center](#) on the IRS website.

You are not an independent contractor if:

- You perform services that can be controlled by the owner (what will be done and how it will be done)
- You use the owner's equipment and supplies
- You service the owner's patients or clients and they tell you when to work. (This applies even if you are given freedom of action). What matters is that the owner has the right to control the details of how the services are performed.

For example, a general dentist is working for another general dentist as an associate. The associate uses the dental staff, the associate is being supervised by the owner, they are told the hours they are working, they use the owner's equipment and supplies, and this is the only office they work for. This associate would likely be classified as an employee.

If an employer-employee relationship exists (regardless of what the relationship is called), you are not an independent contractor.

This is a serious issue for owners who are either intentionally or unintentionally misrepresenting relationships with workers. In cases of abuses, the owner is the party that will likely take the beating.

I recall back in the late 80's when I consulted with a stock broker who worked for a small brokerage firm where all brokers who worked for the firm were being treated as independent contractors. The IRS audited the brokerage firm for several years for the very issue being discussed. The brokers had to submit returns to prove that they were reporting their income correctly and paying the self-employment tax while the brokerage firm got slammed for hundreds of thousands of back payroll taxes, penalties, and interest. Ultimately, the brokerage went belly up, many people became unemployed and many clients

had to find new brokers or move their money to a new brokerage where their broker landed.

We've had similar stories on a much smaller scale where IRS reclassified independent contractors as employees and made the client pay back-payroll taxes, interest, and penalties. I have only heard of one case where the independent contractor themselves got audited and reclassified as an employee and they got hammered income-tax wise because schedule C expenses became miscellaneous itemized deductions subject to limits and their self-employed retirement plan deduction got thrown out.

The bottom line is in just about every IRS audit of a business, one issue the agent must take a look at is the employee vs. independent contractor issue to ensure employers aren't trying to evade employment taxes.

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