

Properly Classifying Workers for Arkansas UI Tax Purposes

Employee vs. Independent Contractor

ACA § 11-10-210(e) defines **employment** for unemployment insurance purposes as:

Service performed by an individual for wages shall be deemed to be employment subject to this chapter irrespective of whether the common-law relationship of master and servant exists, unless and until it is shown to the satisfaction of the Director that:

- (1) Such an individual has been and will continue to be free from control and direction in connection with the performance of such service, both under his contract for the performance of service and in fact, and
- (2) Such service is performed either outside the usual course of the business for which the service is performed or is performed outside of all the places of business of the enterprise for which the service is performed; and
- (3) Such individual is customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the service performed.

The law is written in the conjunctive so unless the business paying the individual for services can establish all three of the elements it must classify the worker as an **employee** for UI purposes.

CONTROL (e)(1)

<p>An employee receives instructions about when, where and how the work is to be performed.</p> <p><i>An independent contractor does the job his way with few, if any, instructions as to the details or methods of the work.</i></p>	<p>An employee may work on call or during hours and days as set by the employer.</p> <p><i>An independent contractor is the controller of his own time and works the days and hours he chooses.</i></p>
<p>Employees are often trained by a more experienced employee or are required to attend meetings or take training courses.</p> <p><i>An independent contractor uses his own methods and thus need not receive training from the purchaser of those services.</i></p>	<p>An employee performs services in the order or sequence set by the employer.</p> <p><i>An independent contractor is concerned only with the finished product and sets his own order of sequence of work.</i></p>
<p>An employee may be required to submit regular oral or written reports about the work in progress.</p> <p><i>An independent contractor is usually not required to submit regular oral or written reports about the work in progress.</i></p>	<p>An employee is typically paid by the employer in regular amounts at stated intervals, such as by the hour, week or month.</p> <p><i>An independent contractor is normally paid by the job, either a negotiated flat rate or upon submission of a bid.</i></p>
<p>Employees perform services at a location mandated by the employer.</p> <p><i>Independent contractors ordinarily work where they choose.</i></p>	<p>An employee ordinarily works for one employer at a time and may be prohibited from joining a competitor.</p> <p><i>An independent contractor often works for more than one client or firm at the same time and is not subject to a non-competition rule,</i></p>
<p>An employee can be discharged at any time without liability on the employer's part.</p> <p><i>If the work meets the contract terms, an independent contractor cannot be fired without liability for breach of contract.</i></p>	<p>An employee can be required to wear a uniform displaying the employer's business name.</p> <p><i>An independent contractor wears the name and/or logo of his own business, not that of the business that purchased his services.</i></p>

SERVICE PERFORMED (e)(2)

<p>Services of an employee are usually merged into the firm's overall operation; the firm's success depends on those employee's services.</p> <p><i>An independent contractor's work is usually separate from the client's business and is not integrated or merged into it.</i></p>	<p>An employee's services must be rendered personally. Employees do not hire their own substitutes or delegate work to them.</p> <p><i>An independent contractor is able to assign another to do the job in his place and need not perform services personally.</i></p>
<p>An employee may act as a foreman for the employer but, if so, helpers are paid with the employer's funds.</p> <p><i>An independent contractor may select, hire, pay and supervise any helpers used and is responsible for the results of the helper's labor.</i></p>	<p>An employee often continues to work for the same employer month after month or year after year.</p> <p><i>An independent contractor is usually hired to do one job of limited or definite duration and has no expectation of continuing work.</i></p>
<p>An employee's business and travel expenses are either paid directly or reimbursed by the employer.</p> <p><i>Independent Contractors normally pay all of their own business and travel expenses without reimbursement.</i></p>	<p>An employee may quit work at any time without liability on the employer's part.</p> <p><i>An independent contractor is legally responsible for job completion and, on quitting, becomes liable for breach of contract.</i></p>

INDEPENDENTLY ESTABLISHED TRADE OR BUSINESS (e)(3)

<p>An employee generally has little or no investment in the business. Instead, an employee is economically dependent upon the employer.</p> <p><i>The independent contractors usually have a substantial financial investment in their independent business.</i></p>	<p>An employee does not ordinarily realize a profit or loss in the business. Rather, employees are paid for services rendered.</p> <p><i>An independent contractor can either realize a profit or suffer a loss depending on the management of revenues and expenses.</i></p>
<p>An employee does not make his services available to the public except through the employer's company.</p> <p><i>An independent contractor may advertise, carry business cards and hold a separate business license.</i></p>	<p>The employer furnishes employees the necessary tools and equipment.</p> <p><i>An independent contractor ordinarily provides all of the tools and equipment necessary to complete the job.</i></p>
<p>An employee's taxes are withheld from his check by the employer and are covered by the employer's worker's compensation plan. The employer provides a W-2 to the employee.</p> <p><i>An independent contractor does not have taxes withheld from his pay for services rendered and provides his own worker's compensation plan. A 1099 is provided by the purchaser of the services as an expense.</i></p>	<p>Insurance is normally an option provided by an employer and depending on the type business, an employer may get the employee bonded.</p> <p><i>An independent contractor provides his own insurance and ordinarily provides proof of having had his business bonded to the purchaser of the services.</i></p>
<p>An employee ordinarily does not have a place of business of his own separate from the employer's.</p> <p><i>An independent contractor normally has a place of business where he works from even if it is out of his own private home.</i></p>	<p>An employer would normally represent the worker as an employee of the firm to its customers.</p> <p><i>The person who purchased the services would not present the independent contractor to the customer. The contractor would present himself to the customer.</i></p>

What does all this mean and how important is it?

It is critical that you, the business owner, correctly determine whether the individuals providing services are employees or independent contractors. Generally, you must withhold and pay Social Security and Medicare Taxes, and pay unemployment insurance tax on wages paid to an employee. You generally do not have to withhold or pay any taxes on payments to independent contractors. You will want to carefully review the information in the previous pages of this document to determine whether individuals you hire are independent contractors or employees.

W-2 or 1099? Be aware of the consequences of misclassification.

You, the employer, should provide your "employee" a Form W-2 allowing them to file their personal income tax with the Internal Revenue Service (IRS) each year as required by Law. If you do not report and pay your obligations as an employer, the IRS will immediately be aware of your failure to do so with the filing of your employee's return. If you provided your employee with a Form 1099 purposely to avoid the tax obligation that goes with having an employee and knowingly misclassified your employee as contract labor violating the rights they are entitled to as an employee, you could be charged with and convicted of crimes, including but not limited to, tax evasion, mail and insurance fraud, theft and wage and hour violations.

Employer and employee agreement or contract, is it binding?

If an employer makes it known to a potential worker that he will only hire someone that agrees to work under a contract labor agreement and yet intends to exercise employer rights of the worker that would normally be afforded to an employee, the worker cannot legally waive, release or commute his rights. It is stated that any employer found in violation of this Law could be fined not less than \$100, or more than \$1,000 or be imprisoned for not more than six months or both. Department of Workforce Services Law and Regulations, A.C.A. § 11-10-107

Still uncertain?

If, after reading the previous information, you are still uncertain and want to be absolutely sure that you are reporting correctly and in compliance with the laws governing classification of your employees for unemployment insurance purposes, please call the Division Chief of the Department of Workforce Services at **(501) 682-3253** or one of two Contribution Operation Managers at **(501)682-1190** or **(501) 682-3265**.