

# Independent Contractors versus Employees: The Costs and Benefits for Your Practice

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**E**very business is interested in reducing costs. Payroll and employee benefit costs can be reduced through the use of independent contractors, because they are not employees to whom training, overtime wages, and benefits must be provided. Using the services of an independent contractor presents some disadvantages, however, as an independent contractor cannot be controlled and disciplined in the same fashion as an employee. There are a variety of tests applied under various statutes to determine whether an individual is an employee or an independent contractor, and it is important to carefully analyze all of the facts of a given situation in light of these tests before entering into an independent contractor relationship. If you engage an individual as an independent contractor, and that individual is found to actually be an employee, your business may be subject to significant financial penalties.

**Key words:** Advantages; disadvantages; employee; independent contractor; hazards; savings.

Payroll and employee benefit costs are major concerns for most healthcare providers. These costs can be reduced by utilizing independent contractors. But there are disadvantages to using independent contractors—for all the cost savings, your practice will face the challenges of maintaining quality control, the confidentiality of medical and practice information, and penalties that may arise if state or federal authorities determine that your independent contractor is really an employee. In this article, we discuss the advantages, disadvantages, and hazards associated with the use of independent contractors, how to distinguish between employees and independent contractors, and factors to consider in determining what makes the most sense for your practice.

## ADVANTAGES OF INDEPENDENT CONTRACTORS

Independent contractors are not employees, a fact that can help reduce overhead and increase profitability.

Many businesses periodically need additional manpower; and when help is needed to satisfy demand, independent contractors can be used without incurring all of the costs associated with employees. For example, a business is not responsible for the expense of training independent contractors or supplying them with the tools and materials necessary for them to perform their work. In addition, independent contractors do not have to be paid overtime. Further, a business is not responsible for withholding taxes on monies paid to independent contractors, and may enjoy reduced taxes by utilizing them.

***The bottom line is that your practice may be able to save money by using independent contractors, and engaging independent contractors makes good business sense in the appropriate circumstances.***

Every business bears the expense of obtaining workers' compensation insurance for its employees. There is no such expense associated with independent contractors, as they are not entitled to that benefit. Similarly, there is no related expense for unemployment insurance benefits, as they are not entitled to that benefit.

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There are additional incentives for using independent contractors. For example, a business must withhold amounts for garnishments or child support from its employees' earnings. That is not the case with independent contractors. In addition, a business is not responsible for Social Security and Medicare for independent contractors, and it does not have to provide them with fringe benefits (pension and health benefits, etc.). And because independent contractors are not "employees," they cannot bring claims—which can be very expensive to defend—against a business under statutes designed to protect employees from various forms of alleged discrimination. Further, in the event of patient injury or death, liability may be avoided if the injury or death is caused by the actions of the independent contractor, and not an employee of the business.

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The bottom line is that your practice may be able to save money by using independent contractors, and engaging independent contractors makes good business sense in the appropriate circumstances.

## **DISADVANTAGES OF INDEPENDENT CONTRACTORS**

The advantages of utilizing independent contractors must be weighed against the disadvantages presented by their use. One disadvantage to using independent contractors is loss of control—an independent contractor's activities cannot be regulated like the activities of an employee. While a business can define the work that needs to be done and dictate when it needs to be completed, it cannot supervise an independent contractor as if he or she was an employee. Doing so may result in the independent contractor being deemed to be an employee, which can have serious financial consequences.

Another disadvantage is that an independent contractor generally cannot be prevented from performing services for a competitor without calling into question whether he or she is really an employee. And while an employee is prohibited from soliciting patients for or diverting patients to a competing business, an independent contractor, generally speaking, is under no such prohibition, and a business that engages an independent contractor may be putting its patient base at risk.

Further, while an employee may be disciplined or discharged for a violation of a work rule, such as those

frequently found in employee handbooks or manuals, an independent contractor is not subject to such discipline. For example, a business may discipline an employee for taking excessive breaks from work, wearing inappropriate attire, or insubordination. An independent contractor cannot be disciplined for engaging in such acts, because he or she is not deemed to be under the control of the business. That is to say, a master-servant relationship is presumed not to exist between an independent contractor and his or her employer. Disciplining or discharging an independent contractor may establish that the relationship of employer-employee existed and result in serious financial penalties.

***Miscalculating how much training and support can be provided to and/or how much control can be exerted over an independent contractor without transforming him or her into an employee can have disastrous results.***

The same concern exists with regard to integrating an independent contractor's services into business operations, because providing substantial amounts of training on policies and procedures to meet regulatory guidelines and quality standards, or providing a substantial amount of the tools and materials necessary to perform the work at hand may be deemed to be indicative of an employer-employee relationship and result in serious financial penalties.

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## **WHAT IS AN INDEPENDENT CONTRACTOR?**

There is no easy way to determine whether an individual is a true independent contractor, as the various courts and governmental agencies have articulated different tests to be applied to any given factual situation. On the surface, the various tests are similar, but a uniform result in any given situation cannot be guaranteed because of the application of differing precedential opinions and the various interpretations of fact that may be reached by differing decision-makers.

Under Title VII (a federal law prohibiting certain types of discrimination against employees, but not independent contractors) the following factors are ordinarily considered: (1) the extent of the employer's control and supervision over the worker, including directions on scheduling and performance of work; (2) the kind of occupation and nature of skill required, including whether

skills are obtained in the workplace; (3) responsibility for the costs of operation, such as equipment, supplies, fees, and licenses; (4) the method and form of payment and benefits; and (5) the length of the job commitment.

Under the Fair Labor Standards Act (a federal law pertaining to the payment of wages) and the Employee Retirement Income Security Act (a federal law pertaining to pension and other benefits), the following factors are generally considered: (1) the extent of control the employer may exercise over the work; (2) whether or not the one employed is engaged in a distinct occupation or business; (3) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the employer or by a specialist without supervision; (4) the skill required in the particular occupation; (5) whether the employer or the workman supplies the instrumentalities, tools, and the place of work for the person doing the work; (6) the length of time for which the person is employed; (7) the method of payment, whether by the time or by the job; (8) whether or not the work is a part of the regular business of the employer; (9) whether or not the parties believe they are master and servant; and (10) whether the one employed is an actual business entity.

***The financial benefits of engaging independent contractors are substantial. However, given the variety of tests that may be applied to any given situation, prior to entering into what is perceived to be a true independent contractor relationship a business should consult with counsel in order to minimize the risk of incurring any of the substantial penalties that may be imposed if the relationship is ultimately found to be that of employer and employee.***

Under the Illinois Workers' Compensation Act, the following factors are examined: (1) the right to control the manner in which the work is done; (2) the right to discharge; and (3) the nature of the claimant's work as it relates to the employer's business, and who provides the tools, material, or equipment (of these factors, the right to control the work is the single most important factor in determining the parties' relationship).

Under the Illinois Unemployment Insurance Act, the following test is employed: service performed by an individual shall be deemed to be employment unless it is proven that the individual has been and will continue to be free from control or direction over the performance of the work, the work is either outside the usual course

of the business for which such service is performed or that such service is performed outside of all the places of business of the enterprise for which such service is performed, and the individual is engaged in an independently established business.

Under the federal tax code, the Internal Revenue Service examines behavioral control, financial control, and the "type of relationship" to determine whether a true independent contractor relationship exists. Behavioral control concerns facts that show whether the employer has the right to direct or control how the work is done. Financial control concerns facts that show whether the employer has the right to direct or control the financial and business aspects of the worker's job. "Type of relationship" concerns facts that evidence how the employer and the worker perceive their relationship (for example, whether or not a written independent contractor agreement exists). While all of these factors are considered, the most important is whether the employer can direct or control only the result of the work to be done, but not the means and methods of accomplishing the work.

## **HAZARDS OF IMPROPER INDEPENDENT CONTRACTOR RELATIONSHIPS**

The adverse financial consequences for entering, even mistakenly, into an independent contractor agreement that is not in conformance with any of the above-referenced laws can be substantial. If an "independent contractor" is deemed to be an employee, a business may be exposed to substantial liability: (1) under employee anti-discrimination statutes (including punitive damages and attorneys' fees); (2) for failure to pay taxes, plus penalties; (3) for workers' compensation benefits, such as doctor and hospital expenses, plus penalties; (4) for unemployment insurance benefits, plus penalties; (5) for unpaid wages and overtime, plus penalties; (6) for fringe benefits, plus penalties; and (7) for personal injury.

## **CONCLUSION**

The financial benefits of engaging independent contractors are substantial. However, given the variety of tests that may be applied to any given situation, prior to entering into what is perceived to be a true independent contractor relationship a business should consult with counsel in order to minimize the risk of incurring any of the substantial penalties that may be imposed if the relationship is ultimately found to be that of employer and employee. While all risk cannot be eliminated, it can be minimized by carefully crafting an independent contractor agreement. ■