

IRS INDEPENDENT CONTRACTOR VS. EMPLOYEE TEST

The IRS has replaced its 20 factor test with a revised model that essentially groups those 20 factors into three main focus areas: Behavioral Control, Financial Control, and Type of Relationship.

BEHAVIORAL CONTROL

1. Type of Instructions Given - If the agency gives a producer instructions about how, when, and where the producer is to work and with whom, this would indicate employee status. Ordinarily, an agency does give such instructions to its producers and would not want to relinquish its right to do so to any significant extent.

2. Degree of Instructions – If the agency gives a producer detailed instructions about how, when, and where the producer is to work and with whom, this would indicate employee status. The degree of instructions on these topics given to producers usually varies from agency to agency, but the more detailed the instructions given the more likely the producer would be considered an employee.

3. Training - If the agency provides training to a producer, this would indicate employee status. If the training provided is of a periodic ongoing nature, this is considered by the IRS to be strong evidence of employee status. In the case of producers with no previous experience, such training would normally be provided by the agency and may also be provided to any producer who switches or expands from personal to commercial lines or vice versa. In many instances, agencies also provide periodic ongoing training to producers to help them maintain their skills and knowledge. If the agency pays the cost of such training by outside providers, this is the same as if the agency itself provided the training, especially if the agency selects the outside training programs.

4. Evaluation System - If the agency has a procedure for evaluating the performance of its producers that is based on how the producer performs his or her job, this would indicate employee status. If the evaluation procedure focuses on the end results of the producer's performance, this would indicate independent contractor status. Most agencies are probably more concerned with how many sales its producers make than with how they make the sales. This would indicate independent contractor status for such producers.

FINANCIAL CONTROL

1. Method of Payment - If a producer is paid a salary or other fixed amount of compensation on a hourly, weekly, or monthly basis, that would indicate employee status. Most producers are paid on a commission basis, and thus, this factor would indicate independent contractor status for such producers.

2. Unreimbursed Expenses - If the agency pays a producer's business, travel, and other expenses, that would indicate employee status. This factor is subject to wide variation among agencies and thus, the employment relationship could probably be structured to require a producer to pay his or her own business expenses in most instances.

3. Significant Investment - If the agency provides business facilities, such as an office, office supplies, and other materials for use by a producer in performing services on its behalf, this would indicate employee status. Most agencies do provide office space, supplies, and other materials for a producer's use. However, the employment relationship could probably be structured to permit a producer to work out of an office in his or her home or at some location other than the agency's offices. A potential problem with such an arrangement would be the necessity of the producer paying for the expense of setting up and operating such an office.

4. Opportunity for Profit or Loss - If a producer is not subject to a risk of economic loss as a result of the performance of services for the agency, that would indicate employee status. A producer that was being compensated on a draw against commissions basis (where repayment of excess draws was actually required) and/or was required to pay for the expenses referred to paragraphs 2 and 3 above would have such a risk. However, whether such an employment relationship could be implemented would depend on a case by case analysis of the producer's financial condition and prospects for success.

5. Services Available to the Market - If a producer makes his or her services available to the general public on a regular basis, that would indicate independent contractor status. But if a producer works for only one agency and can not place business elsewhere without the agency's permission, that would indicate employee status. This is almost always the case and would be difficult, if not impossible, to change.

TYPE OF RELATIONSHIP

1. Written Contracts - If the producer has a written contract that says he or she is an independent contractor this is helpful, but does not control the final determination of independent contractor status. That determination will be made based on how the producer and agency actually work together in light of all the other factors mentioned.

2. Benefits - If the agency provides the producer with insurance coverage of any kind (life, health, disability, E&O), retirement plans, paid vacations, or other "fringe benefits", that would indicate employee status. This will vary from agency to agency, but the more such benefits a producer is required to pay the full cost of, the more that producer will appear to be an independent contractor.

3. Services Provided as Key Activity of Business - If a producer is being used to perform normal business functions, the performance of which would largely determine

the success of the agency's business, that would indicate employee status. Producers are an integral part of, and essential to, the success of an agency.

4. Permanency of the Relationship - If the relationship existing between the producer and the agency is of an indefinite and continuing nature, that would indicate employee status. Producers usually work continuously for an agency on an "at will" basis for an indefinite time. This practice would be difficult, if not impossible, to change.