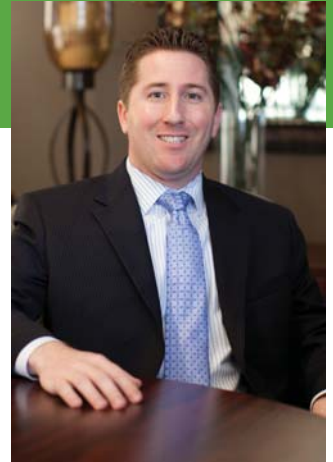


Are You Misclassified? 1099 versus W2 Employees

By Frank Plum, Partner at PayDay Payroll Resources Inc.



“The only things certain in life are death and taxes.”

The first time I heard this quote by Benjamin Franklin was from my father when I was just a child growing up in Marlton, NJ. Later I heard this same quote from teachers and professors. And finally I heard this quote from leaders of industry and colleagues in business. The irony behind this quote is that society consistently tries to cheat the two things that Benjamin Franklin knew to be certain. Modern science has given us the capability to live longer, but not forever. As we have seen from the “Occupy Campaigns” all over the country this past year, individuals and business owners continually find loop holes to avoid paying taxes.

While the top 1% of our countries wealth has teams of high powered lawyers and accountants to assist them in taking advantage of every loophole they can find, every day I see local small business owners make the mistake of trying to avoid paying their employer tax expenses by misclassifying their employees as 1099 independent contractors and not W2 employees.

Business owners benefit by classifying an individual as a 1099 independent contractor because they avoid paying the employer tax expense (6.2% social security, 1.45% Medicare, .06 % FUTA, and State UI/DI 3% avg.). They also avoid having to pay overtime, health and safety insurances, and unemployment and workers compensation benefits. The IRS, as well as the State of New Jersey, set very strict guidelines on the classification of a 1099 independent contractor. Some of the guidelines have been broken out into three categories, including:

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1. Behavioral: Does the company control or have the right to control what the worker does and how the worker does his or her job?

2. Financial: Are the business aspects of the worker's job controlled by the payer? (This includes things like: Does the worker use his or her own tools? How is the worker paid and are expenses reimbursed?)

3. Type of Relationship: Are there written contracts or employee type benefits (i.e. pension plan, insurance, vacation pay, etc.)? Will the relationship continue after the work is complete and is the work performed a key aspect of the business?

A 1099 independent contractor should have their own Tax ID number and carry their own insurance. They should be able control their own work environment and how and when they get paid. The job that they were contracted to do should have a completion date and the job should end. Finally a 1099 independent contractor is considered self employed and is subject to Self-Employment Tax. If none of this applies, you are not an independent contractor and you should be classified as a W2 employee.

Employers that misclassify employees are subject to a civil penalty of up to \$1,100 for each violation. Those employers who are found to have repeat violations would be subject to a civil penalty of up to \$5,000.

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