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Agricultural Employees vs. Independent Contractors

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One of the most commonly seen mistakes among clients of ours is misclassification of employees and independent contractors. Many agricultural employers find it much easier to classify those who help them as independent contractors, rather than paid employees, in order to avoid paying employment taxes. We will evaluate how to determine the difference between an employee or independent contractor, tax implications of both, and the ramifications of misclassifying as an independent contractor.

One of the main deciphering factors to look at is how much control an employer has over what the worker does, and what their means are to carry out a job. The IRS previously used a Common Law, 20-factor test to determine the relationship between an employer and employee or contractor. It has now been broken down into three categories to take a close look at: Behavioral Control, Financial Control, and Relationship Control.

When evaluating Behavioral Control, it is important to look at whether the employer decides what the worker does, and how it is done. If the employer mandates the task, and the worker uses tools and machinery owned by the employer, it is likely done by an employee. If the worker has his own way of doing the job using his own materials/machinery, it is more likely done by an independent contractor. Another factor to look at is how much training it takes for the worker to get the job done. When an employer has to provide on the job training, a high degree of instruction, and further evaluation after that, the worker classifies as an employee. An independent contractor should already specialize in the job to be done, and not need excessive instruction. If the employer hires assistants to help a worker do a job, they are also employees; however, if the independent contractor hires assistants, they are then likely an employee of the contractor.

Financial control takes a look at how much and how often a worker is paid. Employees typically receive an hourly or salary wage within a pay period that consistently stays the same, until formally changed. An independent contractor usually receives a flat fee at a specified time, or simply when the job is finished. An independent contractor also does not often receive payment until a bill is sent and received by the owner. An employee is reimbursed for expenses such as supplies or travel costs, whereas an independent contractor is responsible for his own

expenses that go unreimbursed. Independent contractors face the biggest opportunity for profit or loss.

Relationship control evaluates how the employer and the worker distinguish their services to one another. An employee usually signs a written contract with his employer specifying a wage they will be paid, along with the benefits available to them, such as a retirement plan, health insurance, or vacation pay. Independent contractors are much more at liberty to seek out several employment opportunities with different employers at the same time, and to advertise their services to the general public.

Putting this all into consideration when looking at agricultural operations, the most common misuse of treating employees as independent contractors occurs during big events such as harvesting or branding. Many people gather to help and are paid a wage, but they aren't independent contractors with their own business. Often times a worker will help an employer for a few weeks at a time, until they do it again the following year. They are instructed by the employer what to do and when, often using the employer's machinery and equipment, and are typically told by the employer when they are to work. While it is much easier to write them a check, send them on their way, and call it custom work, legally this would be considered an employee working a job, and they should have employment taxes deducted from their pay.

While it is okay to deduct employee meals in the correct cases, deducting them is a commonly made mistake we see taxpayers attempting to put as a farm expense on their tax returns. When you have true employees paid a consistent wage, you can deduct 50% of the employee meals you provide for them. This was implemented in the new tax law starting on 2018 tax returns, whereas before that you could deduct the full cost. Providing meals for those who help with harvesting or branding for example, is not a deductible expense. If you're not paying them a wage and are instead regarding them as an independent contractor, buying their meals would not qualify as an employee meal.

In some cases, the ramifications of misclassifying a worker can have big consequences. According to The CPA Journal, "Federal employment withholding taxes represent nearly 70% of all federal tax revenue to be paid to the IRS. Unreported or underreported employment taxes contribute to the overall federal tax gap. The IRS seeks back taxes and penalties from employers that wrongly treat workers as self-employed contractors." Consequences to employers for misclassifying are based heavily on the degree to which the employer misreported. In some cases, employers can avoid paying back taxes or penalties if the misclassification is minor, and simply reclassify their workers as employees or prove why they're paying a worker as an independent contractor. In much larger cases, penalties can include 20% of all wages paid, as well as 100% of FICA taxes owed, and even jail time can be sentenced in extreme circumstances.

When trying to determine between an independent contractor and an employee, if it is very undecided, the IRS usually errs on the side of the worker being an employee. There is no one thing that specifies whether a worker is one or the other, but there are points to look at in order to decide. The best thing to do if you're unsure is to simply consult your tax preparer or accountant and have them help you figure out the best way to perceive your workers. It is always best to be proactive and more cautious than to risk being caught and targeted for an employment tax audit.

Works Cited

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