



## New Ruling on Independent Contractors Impacts Many Employers

By Richard Warner, CPA, Smith Dickson, An Accountancy Corporation

Determining whether a California worker is an independent contractor or an employee has always been difficult. However, for many years the laws have been interpreted to mean that the key to distinguishing between employees and independent contractors was whether the company had the right to control the manner and means by which the worker accomplished the desired result. Recently, a ruling by the California Supreme Court changed that understanding.

Earlier this year, the Court revised the guidelines that are used to identify individuals who work with a business as independent contractors. The Court ruled in *Dynamex Operations West, Inc. v. Superior Court* that employers bear the burden of proving classification of an individual as an independent contractor. These three "ABC test" factors must all be met to qualify:

- The employer does not control/direct how the individual performs the work;
- The individual provides a service that is outside the employer's usual business; and
- The individual is customarily engaged in an established business, trade, or profession that is independent of the employer's business.

On a related note, California's SB 459 law signifies the government's intent to closely monitor worker misclassification. Here are a few key aspects of the law:

- Employers may face fines of \$5,000 to \$10,000 for first violations and up to \$25,000 for repeat violations for "voluntarily and knowingly" misclassifying workers as independent contractors.
- Extensive IRS and state agencies audits of a business may be conducted in order to determine whether workers are properly classified. If it has been officially determined that independent contractors should have been classified as employees, then the businesses could face back taxes, interest, penalties, and CPA/legal fees for representation.
- An employer who violates the new law must post a notice to employees detailing the misclassification on its website, or, if it does not have a website, another prominent area.

As a result of Dynamex and SB 459, employers will need to reevaluate the nature of the relationship with many of their workers; it has been estimated that millions of workers in the state who were considered independent contractors will now be deemed employees. Some businesses may have to revise their operational model on a major level, since the costs of providing benefits, workers' compensation and potential legal liability may be substantial.

Under this new ruling, businesses have minimal leniency and should evaluate classification of their workforce. The potential penalties and fines for misclassification are severe. This new law is very serious — it is advisable to seek guidance from your CPA or attorney to help evaluate your current classification, examine your business structure, and avoid complications that can seriously damage your ongoing operational status. Please contact Smith Dickson CPAs if you need further assistance with employee classifications, 1099s and related tax issues.

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