

ARE YOU AN EMPLOYEE OR AN INDEPENDENT CONTRACTOR?

Sometimes, a worker may be incorrectly classified as an **independent contractor** instead of an **employee** by an employer who doesn't understand or wants to avoid labor laws and tax responsibilities.

➔ What is the difference between an "employee" and an "independent contractor"?

If you are an employee, both you and your employer pay Social Security Tax and Medicare Tax on your wages. These amounts are shown on your W-2 forms and your paycheck stubs and are deducted from your paychecks. However, if you are an independent contractor or self-employed, you are responsible for paying **all** of the Social Security and Medicare Tax (also called self-employment tax). These taxes are in addition to the income tax that you pay on your income when you file your return. For 2011 and 2012, the tax for Social Security and Medicare is 13.3% of the net profit that you earned from your work or business.

➔ How do I know if I'm an independent contractor?

Generally, if your employer treats you as an independent contractor, he/she will give you a Form 1099-Misc to show what you earned (instead of a Form W-2). Similarly, if you are paid in cash and taxes are not withheld from those payments, you are considered an independent contractor. If you are unsure if you are an independent contractor, ask yourself the following questions:

- Do you set your own hours, or are you required to report for work at the same time each day?
- Do you bring your own tools and equipment to the job site?
- Do you decide how to complete the job or project, or does your employer control the job site?

The more **control** you have over your work hours and the way you perform your job, the more likely it is that you are an independent contractor. See IRS Publication 1779 for more information.

➔ What are my tax responsibilities if I am an independent contractor?

If you earn more than \$400 in **net self-employment income** (the income you receive as an independent contractor), you must file a Federal income tax return and report your income.

- Example: You provide daycare in your home. You received \$5,000 in payments from parents for children that you cared for while the parents worked. You spent \$3,000 in food, toys, diapers, and other items for the children. Your net self employment is \$2,000 (the \$5,000 payments received, minus \$3,000 in expenses to care for the children). You must file a Federal income tax return.

If you think that you will owe \$1,000 or more in tax, including self-employment tax, you must make **quarterly estimated payments** towards your taxes. Even if you are not authorized to work in the United States, you are required to make estimated quarterly payments towards your tax liability. These estimated payments will prevent you from owing a large amount of tax at the end of the year.

- You may be able to avoid making estimated payments if you have another job and you have enough taxes withheld from your other wages to cover your tax liability at the end of the year. You can use **IRS Form 1040-ES** to figure out the amount of your estimated quarterly payments.
- You must have a social security number or an ITIN to make estimated payments. If you are not eligible for a social security number, you must complete IRS Form W-7 to request an ITIN and attach it to a federal income tax return. Contact the IRS for more information.

➔ What kinds of records should I keep?

It is very important to keep accurate records to track your self-employment income and expenses, particularly if you are paid in cash. If you are an independent contractor, you should keep track of all payments you receive for your work, including all cash payments. Consider getting a notebook to keep track of your information. Each time you are paid, write down the following:

- The date you were paid
- How much you were paid
- Who paid you, and
- A brief description of the work you completed.

If you deposit your payments into a bank account, be sure to keep copies of all your bank statements. You should also save the receipts for any supplies or other items that were purchased in order to carry out your work. You may be able to deduct these items as business expenses when you file your return. Good record-keeping can protect you from exploitation by employers, and support you if you are audited or have a worker classification dispute with the IRS.

➔ I don't think I'm an independent contractor but my employer is treating me as one. What now?

First: Make sure that you should be classified as an employee and not as an independent contractor. Call our Tax Clinic Help Line for assistance.

Second: Complete IRS Form SS-8 and ask the IRS to decide on your correct worker status. The IRS will then contact your employer and ask for information about your job to decide whether you should be an employee.

Tax Clinic Help Line:
(312) 630-0241
taxclinic@economicprogress.org



The Center for Economic Progress (CEP) helps low-income individuals and families move from financial uncertainty to financial security.

www.economicprogress.org

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