

**Letter of Findings Number: 03-20150085**  
**Withholding Tax**  
**For Tax Years 2011-2013**

**NOTICE:** IC § 6-8.1-3-3.5 and IC § 4-22-7-7 requires the publication of this document in the Indiana Register. The document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

### **HOLDING**

Business owner owed withholding tax for individuals, wrongfully hired as independent contractors, because the individuals should have been treated as employees.

### **ISSUE**

#### **I. Withholding Tax-Independent Contractors/Employees.**

**Authority:** Snell v. C.J. Jenkins Enterprises, Inc., 881 N.E.2d 1088 (Ind. Ct. App. 2008); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); IC § 6-8.1-5-1; [45 IAC 3.1-1-97](#); 41 Am. Jur. 2d Independent Contractors § 1 (2009); IC § 6-3-4-8; Longmire v. Indiana Dep't of State Revenue, 638 N.E.2d 894 (Ind. Tax Ct. 1994); Rev. Rul. 87-41, 1987-1 C.B. 296; IRS Publication 15-A (2011).

Taxpayer protests imposition of withholding tax based upon the Department's classification of individuals as employees.

### **STATEMENT OF FACTS**

Taxpayer is an Indiana business. Taxpayer employs two general managers that Taxpayer treated as independent contractors. Taxpayer also employs a number of individual workers that Taxpayer treats as employees. As the result of an investigation, the Indiana Department of Revenue ("Department") determined that Taxpayer had under-remitted on its state and county withholding tax for the tax years 2011 through 2013. The Department determined that the two general managers were employees and employee withholding tax was due on their wages. The Department therefore issued proposed assessments for state and county withholding tax for those years. Taxpayer protests these proposed assessments. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as required.

#### **I. Withholding Tax-Independent Contractors/Employees.**

### **DISCUSSION**

The Department classified the two individuals Taxpayer hired as general managers as employees. Department based its determination of employee status on several factors which included how the individuals were paid, their stake in the business, and the Taxpayer's control over the individuals.

Taxpayer protests the imposition of withholding tax on the payment made to its two general managers for the tax years 2011-2013. The Taxpayer maintains that the individuals in question were independent contractors and that it was not responsible for collecting and remitting withholding tax on them.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong.

IC § 6-3-4-8(a) provides that employers must "withhold, collect, and pay over income tax on wages paid to . . . employees." The relevant regulation [45 IAC 3.1-1-97](#), states that employers must "withhold [F]ederal taxes pursuant to the Internal Revenue Code", and are also "required to withhold from employees' wages Adjusted Gross and County Adjusted Gross Income Tax."

If Taxpayer hired individuals as independent contractors it would not have been required to withhold or remit withholding tax. According to the American Jurisprudence, an "independent contractor is one who, in exercising an independent employment, contracts to do certain work according to his or her own methods, without being subject to the control of the employer, except as to the product or result of the work." 41 Am. Jur. 2d Independent Contractors § 1 (2009). The employment relationship determines whether an individual worker is an independent contractor or an employee. An employer-employee relationship "exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished." Longmire v. Indiana Dep't of State Revenue, 638 N.E.2d 894, 897 (Ind. Tax Ct. 1994).

The federal Internal Revenue Service ("IRS") provides some guidelines to determine if an individual is an employee or an independent contractor. The guidelines, set forth in Rev. Rul. 87-41, 1987-1 C.B. 296, provides for the following twenty factors:

1. INSTRUCTIONS. A worker who is required to comply with other persons' instructions about when, where, and how he or she is to work is ordinarily an employee. This control factor is present if the person or persons for whom the services are performed have the RIGHT to require compliance with instructions.
2. TRAINING. Training a worker by requiring an experienced employee to work with the worker, by corresponding with the worker, by requiring the worker to attend meetings, or by using other methods, indicates that the person or persons for whom the services are performed want the services performed in a particular method or manner.
3. INTEGRATION. Integration of the worker's services into the business operations generally shows that the worker is subject to direction and control. When the success or continuation of a business depends to an appreciable degree upon the performance of certain services, the workers who perform those services must necessarily be subject to a certain amount of control by the owner of the business.
4. SERVICES RENDERED PERSONALLY. If the services must be rendered personally, presumably the person or persons for whom the services are performed are interested in the methods used to accomplish the work as well as in the results.
5. HIRING, SUPERVISING, AND PAYING ASSISTANTS. If the person or persons for whom the services are performed hire, supervise, and pay assistants, that factor generally shows control over the workers on the job. However, if one worker hires, supervises, and pays the other assistants pursuant to a contract under which the worker agrees to provide materials and labor and under which the worker is responsible only for the attainment of a result, this factor indicates an independent contractor status.
6. CONTINUING RELATIONSHIP. A continuing relationship between the worker and the person or persons for whom the services are performed indicates that an employer-employee relationship exists. A continuing relationship may exist where work is performed at frequently recurring although irregular intervals.
7. SET HOURS OF WORK. The establishment of set hours of work by the person or persons for whom the services are performed is a factor indicating control.
8. FULL TIME REQUIRED. If the worker must devote substantially full time to the business of the person or persons for whom the services are performed, such person or persons have control over the amount of time the worker spends working and impliedly restrict the worker from doing other gainful work. An independent contractor on the other hand, is free to work when and for whom he or she chooses.
9. DOING WORK ON EMPLOYER'S PREMISES. If the work is performed on the premises of the person or persons for whom the services are performed, that factor suggests control over the worker, especially if the work could be done elsewhere. Rev. Rul. 56-660, 1956-2 C.B. 693. Work done off the premises of the person or persons receiving the services, such as at the office of the worker, indicates some freedom from control. However, this fact by itself does not mean that the worker is not an employee. The importance of this factor

depends on the nature of the service involved and the extent to which an employer generally would require that employees perform such services on the employer's premises. Control over the place of work is indicated when the person or persons for whom the services are performed have the right to compel the worker to travel a designated route, to canvass a territory within a certain time, or to work at specific places as required.

10. ORDER OR SEQUENCE SET. If a worker must perform services in the order or sequence set by the person or persons for whom the services are performed, that factor shows that the worker is not free to follow the worker's own pattern of work but must follow the established routines and schedules of the person or persons for whom the services are performed. Often, because of the nature of an occupation, the person or persons for whom the services are performed do not set the order of the services or set the order infrequently. It is sufficient to show control, however, if such person or persons retain the right to do so.

11. ORAL OR WRITTEN REPORTS. A requirement that the worker submit regular or written reports to the person or persons for whom the services are performed indicates a degree of control.

12. PAYMENT BY HOUR, WEEK, MONTH. Payment by the hour, week, or month generally points to an employer-employee relationship, provided that this method of payment is not just a convenient way of paying a lump sum agreed upon as the cost of a job. Payment made by the job or on a straight commission generally indicates that the worker is an independent contractor.

13. PAYMENT OF BUSINESS AND/OR TRAVELING EXPENSES. If the person or persons for whom the services are performed ordinarily pay the worker's business and/or traveling expenses, the worker is ordinarily an employee. An employer, to be able to control expenses, generally retains the right to regulate and direct the worker's business activities.

14. FURNISHING OF TOOLS AND MATERIALS. The fact that the person or persons for whom the services are performed furnish significant tools, materials, and other equipment tends to show the existence of an employer-employee relationship.

15. SIGNIFICANT INVESTMENT. If the worker invests in facilities that are used by the worker in performing services and are not typically maintained by employees (such as the maintenance of an office rented at fair value from an unrelated party), that factor tends to indicate that the worker is an independent contractor. On the other hand, lack of investment in facilities indicates dependence on the person or persons for whom the services are performed for such facilities and, accordingly, the existence of an employer-employee relationship.

16. REALIZATION OF PROFIT OR LOSS. A worker who can realize a profit or suffer a loss as a result of the worker's services (in addition to the profit or loss ordinarily realized by employees) is generally an independent contractor, but the worker who cannot is an employee. See Rev. Rul. 70-309. For example, if the worker is subject to a real risk of economic loss due to significant investments or a bona fide liability for expenses, such as salary payments to unrelated employees, that factor indicates that the worker is an independent contractor. The risk that a worker will not receive payment for his or her services, however, is common to both independent contractors and employees and thus does not constitute a sufficient economic risk to support treatment as an independent contractor.

17. WORKING FOR MORE THAN ONE FIRM AT A TIME. If a worker performs more than de minimis services for a multiple of unrelated persons or firms at the same time, that factor generally indicates that the worker is an independent contractor. See Rev. Rul. 70-572, 1970-2 C.B. 221. However, a worker who performs services for more than one person may be an employee of each of the persons, especially where such persons are part of the same service arrangement.

18. MAKING SERVICE AVAILABLE TO GENERAL PUBLIC. The fact that a worker makes his or her services available to the general public on a regular and consistent basis indicates an independent contractor relationship.

19. RIGHT TO DISCHARGE. The right to discharge a worker is a factor indicating that the worker is an employee and the person possessing the right is an employer. An employer exercises control through the threat of dismissal, which causes the worker to obey the employer's instructions. An independent contractor, on the other hand, cannot be fired so long as the independent contractor produces a result that meets the contract specifications.

20. RIGHT TO TERMINATE. If the worker has the right to end his or her relationship with the person for whom the services are performed at any time he or she wishes without incurring liability, that factor indicates an employer-employee relationship.

These factors supplement the common-law factors determining whether an individual is a common-law employee or independent contractor. See IRS Publication 15-A (2011).

The Department notes that the Court of Appeals of Indiana addressed the problem of determining if a person is an employee or an independent contractor in the case *Snell v. C.J. Jenkins Enterprises, Inc.*, 881 N.E.2d 1088 (Ind. Ct. App. 2008). In that case, the plaintiff (Snell) wanted to be considered an employee in order to recover some money, which he believed was owed by the defendant (Enterprises), using Indiana wage statutes. The court determined that the plaintiff was an independent contractor. The court explained:

Because the question at issue here is whether Snell was Jenkins's employee or an independent contractor, we too will employ the ten-factor test pursuant to the Supreme Court's direction in *Moberly*. These ten factors are as follows:

- (a) the extent of control which, by the agreement, the master may exercise over the details of the work;
  - (b) whether or not the one employed is engaged in a distinct occupation or business;
  - (c) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the employer or by a specialist without supervision;
  - (d) the skill required in the particular occupation;
  - (e) whether the employer or the workman supplies the instrumentalities, tools, and the place of work for the person doing the work;
  - (f) the length of time for which the person is employed;
  - (g) the method of payment, whether by the time or by the job;
  - (h) whether or not the work is a part of the regular business of the employer;
  - (i) whether or not the parties believe they are creating the relation of master and servant; and
  - (j) whether the principal is or is not in business.
- Id. at 1091.

The court discussed each factor and determined whether that particular factor weighed towards Snell's status as an employee or an independent contractor. The court also considered how strongly each factor weighed in which direction. Ultimately, the court determined that enough factors weighed strongly enough to rule that Snell was an independent contractor.

In the instant case, Taxpayer discussed the IRS factors but provided little documentation in support of its position that the general managers were independent contractors and not employees. There was no written agreement laying out the terms of employment or whether the Taxpayer would treat the general managers as employees or independent contractors. The Taxpayer paid the general managers a flat weekly fee, and Taxpayer also paid any persons hired by the general managers. Also, Taxpayer could terminate the general managers' employment at any time. The general managers' accountant informed Taxpayer that the individuals were independent contractors and would file their taxes accordingly. Taxpayer provided copies of the general managers' tax returns which showed they filed their income as independent contractors rather than employees. Taxpayer's issuance of the 1099s weighs in Taxpayer's favor as explained in factors (a) and (i) in *Snell*. However, factors (c), (d), (g), (h) and (j) weigh against Taxpayer.

There is no documentation to establish the status of the remaining factors and, as previously mentioned, the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as required by IC § 6-8.1-5-1(c). In this case, Taxpayer has only shown that two of ten factors weigh in its favor. Therefore, Taxpayer has not met the burden of proving the proposed assessments wrong.

**FINDING**

Taxpayer's protest is denied.

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