

# What You Need to Know About Hiring Independent Contractors

From every corner of the District and colleges, projects, assignments and duties have to be performed utilizing specialized services...from construction and maintenance projects, architectural services, testing services, horticultural projects (building greenhouses), legal experts, investigators, bookkeeping, legislative advocates, mandated cost services, timekeepers for sports activities, Risk Management services, business advisors for the International Trade program, interpreters for the hearing impaired, etc., these are to name just a few of the categories that the District seeks through the hiring of independent contractors.

As many of you know, Independent Contractors are *not employees* of the District but are individuals or companies providing specific/specialized services to the District that are not controlled by the District in terms of worksite location or method service is performed, such as in the case of an employee (method of work is controlled, instruction/supervision is controlled, and time and location is controlled). Additionally, Independent Contractors are responsible for paying their own taxes.

When contracting with an individual or company for services, the District must establish the nature of the service relationship. This *should occur prior* to any services being performed and the *issuance of any payment*. Once the *legal* relationship is determined, the method of payment is prescribed by law. The *major issue* is in the grey area of *who is or is not an employee*. Instead, there are the twenty common law factors that must be analyzed to make the determination.

According to the Employment Development Department of the State of California, an independent contractor is the following:

*A service-provider is defined as an independent contractor; an independent contractor is any individual or sole proprietor who is not an employee of the service-recipient for California purposes and who receives compensation or executes a contract for services performed in or outside California.*

The Internal Revenue Service's description is:

## Who Is an Independent Contractor?

*A general rule is that the tax exempt organization, as the payer, has the **right to control or direct only the result of the work** done by an independent contractor, and **not the means and methods of accomplishing the result.***

Other definitions from the 'Lectric Law Library state:

*Independent Contractor – A person or business who performs services for another person under an express or implied agreement and who is not subject to the other's control, or right to control, the manner and means of performing the services; not as an employee. One who engages an independent contractor is not liable to others for the acts or omissions of the independent contractor.*

*A person or business which provides goods or services to another entity under terms specified in a contract. Unlike an employee, an independent contractor does not work regularly for a company.*

Consider reviewing IRS Publication SWR 40, *Public Schools and Employment Taxes*, lists workers that have already been determined by the IRS to be employees. These are individuals performing the duties of:

Administrators	Instructors
Substitutes	Clerical Staff
Athletic Coaches	Tutors
Counselors	Examination/Monitors
Proctors	Librarians

In addition to the above categories, the IRS has reclassified the following categories as employees:

Nurses  
Psychologists  
Specialty Teachers (Art, Poetry, Music, etc.)  
Individuals "filling-in" on an "Interim Basis"

The District has developed a document to assist in determining if an individual meets the criteria for becoming an independent contractor for the District. Please contact Kashi Yamashita, Executive Assistant, at (510) 466-7265 to request a copy of the guidelines.

**What are the Procedures for Hiring an Independent Contractor/Consultant?**

The originating manager must complete the independent contractor/consultant services agreement (completing with full detail) and securing the signature of the contractor, Business & Administrative Manager and the College President before sending to the District for final approval. Please make sure the following items are handled before sending the agreement to the Finance Division for approval:

**DO**

√ **plan and allow at least two (2) weeks advance timeframe for hiring Independent Contractors. This allows the proper routing and approval process to occur before a contractor begins work**

√ **have Independent Contractor form signed by contractor and include business license, social security or tax identification no. listed, service-recipient name/business name, address, and telephone number, beginning and ending date (expiration date) of services to be performed, hourly rate and the **not to exceed dollar amount on the agreement****

√ **cover memo justifying the hire of the contractor, why this contractor was selected, duration of agreement, type of service to be performed, dollar amount of contract, etc.**

√ **resume or scope of services statement from the contractor must be attached to agreement**

√ **have vendor application submitted if one has not been filed with the Purchasing Department before**

√ **have contractor obtain workers' compensation insurance for any employees he/she may employ**

√ **inform contractor that he/she must have liability insurance and that signing the agreement they will agree to hold the District harmless (review liability/indemnification language on the back of the NCR Independent Contractor's Agreement)**

√ **have budget reviewed by the campus Business & Administrative Services Manager and signature (if this step is not completed at the campus level, the contract will be held until the funds are available in the appropriate budget); also, make sure the **budget code is accurate****

√ **route to the President's office for approval before sending to District Finance Department**

√ **send Agenda Blue Blurb language for Independent Contractor agreements over \$25,000 and over \$60,900 for restricted fund and bond fund projects to the attention of the Board of Trustees for approval—contracts must still be routed first to the Budget & Finance Department**

**The Finance Department will:**

√ **have contract reviewed/approved/forwarded by the Executive Assistant and the Finance, Budget & Attendance Analyst and will forward agreement to **Chancellor for final approval****

√ **log and to keep track of budget cap which has been established by the Board of Trustees, which is currently \$25,000 from unrestricted funds. Restricted fund and Bond fund limit is \$60,900. This information will be sent to the Accounts Payable Unit, Purchasing Unit and the original copy will be maintained on file in the Budget & Finance office**

√ **will send copies of the contract to the **originating manager** (copy for the contractor should be forwarded from originating manager)**

**DO NOT**

√ **send contracts unsigned by the Business & Administrative Services Manager, Unit Manager, and/or the College President**

√ **start the services of a contractor without the **Chancellor's prior approval****

√ **send unauthorized contracts long after the service is completed. The District has a **legal** responsibility to forward payment to the contractor within ten (10) days of invoicing**

√ **pay a contractor without an approved agreement on file**

√ **exceed the annual dollar limit allowable by the District and authorized by the Board of Trustees. Any contract over \$25,000 for professional or specialized services or \$60,900 for contractors to be paid out of bond funds**

The District Finance Department sends, for 1099-MISC reporting purposes, information regarding the hiring of independent contractors (contractors must be paid \$600 or more) to the State of California, Employment Development Department (EDD). **This is a state mandated process that the District is bound to comply with, therefore, timely submittal of contracts are important, particularly establishing the beginning of the service provided by the contractor.** This information must be remitted to EDD within 20-days of contractor's beginning service with the District.

To get a copy of **Frequently asked questions and answers about the California Independent Contractor's Reporting Law**, please contact Kashi Yamashita, Executive Assistant, Office of Budget & Finance, at extension 7265.

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## Frequently asked Q&A's:

### Q1. Who has to report?

A1. Any business or government entity (defined as a "service-recipient") that is required to file a federal Form 1099-MISC for services performed by an independent contractor (defined as a "service-provider") must report.

### Q2. Who is a service-recipient?

A2. A service-recipient is any business or government entity that is required to file a federal form 1099-MISC for services performed by an independent contractor. A service-recipient means any individual, person, corporation, association, or partnership, or agent thereof, doing business in this State, deriving trade or business income from sources within this State, or in any manner in the course of trade or business subject to the laws of this State. A service-recipient also includes the State of California or any political subdivision thereof, including the Regents of the University of California, any charter city, or any political body not a subdivision or agency of the State, and any person, employee, department, or agent.

### Q3. Who is a service-provider?

A3. A service-provider is defined as an independent contractor; an independent contractor is any individual who is not an employee of the service-recipient for California purposes and who receives compensation or executes a contract for services performed in or outside California.

### Q4. What information do I report?

A4. You are required to provide the following information. Business or government entity's (service-recipient): Federal employer identification number or social security number; California employer account number (if applicable); Business name, address, and telephone number; Independent contractor's (service-provider): First name, middle initial, and last name, Social security number, Address, Start date of contract (if no contract, date payments equal \$600 or more); Amount of contract, including cents (if applicable); Contract expiration date (if applicable); Ongoing contract (check box if applicable)

### Q5. When do I have to report?

A5. As of January 1, 2001, you must report information to EDD within twenty (20) days of either making payments totaling \$600 or more or entering into a contract for \$600 or more with an independent contractor in any calendar year, whichever is earlier. Report each independent contractor once each year.

Q6. What do I do if it is difficult to determine when the contract will equal or exceed \$600 or if there is no set contract amount?

A6. If you are unable to determine when total payments made equal or exceed \$600, you may estimate the dollar amount of the contract and check the box on the DE 542 that indicates "ongoing." If there is no set contract amount, you may report when the aggregate payments in a calendar year equal or exceed \$600 and check the "ongoing" box.

Q7. If the cost of parts and materials is included in the contract or payments, is this cost included in determining if the \$600 threshold has been met?

A7. Yes. If either the contract amount or amount paid includes the cost of parts or materials, that cost is to be included in determining whether the service-provider has been paid \$600 or more.

### Q8. How do I report?

A8. Report independent contractors on the Report of Independent Contractor(s) (DE 542). If you are hiring a large number of independent contractors, you are encouraged to send the information via magnetic media. If you report on magnetic media, you do not need to send a DE 542. For details, contact the Magnetic Media Unit at (916) 651-6945.

Q9. How do I obtain the Report of Independent Contractor(s) (DE 542) and/or whom do I contact if I have questions?

A9. For assistance or to order forms, please call our hotline number (916) 657-0529, Monday through Friday from 8 a.m. to 5 p.m. (PT). You may also call our toll-free number 1-888-745-3886, visit your local Employment Tax Office, order forms on-line at [www.edd.ca.gov/taxordn2.htm](http://www.edd.ca.gov/taxordn2.htm), or download them at [www.edd.ca.gov/taxform.htm](http://www.edd.ca.gov/taxform.htm).

### Q10. Where do I report?

A10. Mail to:  
Employment Development Department  
PO Box 997350 MIC 99  
Sacramento CA 95899-7350  
Fax to: (916) 255-3211

Q11. What is the purpose of the independent contractor reporting law?

A11. The information you provide to EDD will increase child support collection by helping to locate parents who are delinquent in their child support obligations.

Q12. What type of penalty is charged if the report is late?

A12. The EDD may assess a penalty of \$24 for each failure to comply within the required time frames. Also, a penalty of \$490 may be assessed for the failure to report independent contractor information if the failure is

the result of conspiracy between the service-recipient and service-provider

**Q13.** Do I report independent contractors who work in another state? If my business is not in California, do I report the independent contractors?

**A13.** Under California law, "service-recipients" must report "service-providers." By definition, a service-provider is an independent contractor who provides services (rather than goods) to a business or government entity; a service-recipient must meet one of these three tests: 1) Does business in California; 2) Derives trade or business income from sources within California; and 3) In any manner in the course of a trade or business is subject to the laws of California.

If your business/government entity meets one or more of the three service-recipient tests, you must report independent contractors whose services are performed for any of your business operations that also meet at least one of the three tests.

*Example #1 – Your business is headquartered in California and therefore meets one of the service-recipient tests. Your California office hires an independent contractor (IC) who lives and works in New York. You must report this IC to EDD since the IC performs services for your California business operation.*

*Example #2 – Your business is headquartered in California and therefore meets one of the service-recipient tests. You also have a business operation in Massachusetts. The Massachusetts location hires a Massachusetts-based IC to perform janitorial services in Massachusetts. You do not have to report this IC to EDD since the IC performs services for a business operation that does not meet any of the service-recipient tests.*

*Example #3 – Your business is headquartered in North Dakota and has a branch office in California that uses ICs. Those ICs should be reported since the California office meets the service-recipient test. However, if the North Dakota office hires an IC to perform services for the North Dakota location, those services would not be reported because the IC performs services for an office that does not meet any of the service-recipient tests.*

*Example #4 – Your business is headquartered in Indiana and does not have any branch offices in California. Your business registered with a California state agency to have independent sales agents (ICs) sell your products in California. You must report these ICs to EDD since they perform services for a business operation deriving income from California and subject to some California laws, thereby meeting two of the service-recipient tests.*

**Q14.** Do any other states require independent contractor reporting?

**A14.** Yes. According to the U.S. Department of Health and Human Services, Iowa, Massachusetts, Minnesota, New Hampshire, and New Jersey require some sort of independent contractor reporting.

**Q15.** Can other states report their independent contractors to California and vice versa?

**A15.** No. There are no reciprocal agreements between the states for this purpose.

**Q16.** If my business contracts with a service-provider that is a corporation, general partnership, or limited liability company, must this service-provider be reported?

**A16.** No. The legislative requirements only call for the reporting of service-providers who are individuals working as independent contractors. In general, independent contractors who are sole proprietors are to be reported to EDD.

**Q17.** My service-providers have federal employer identification numbers (FEINs) and business names. How do I determine if they are sole proprietors? Can I report their FEINs instead of their social security numbers (SSNs)?

**A17.** By statute, you are required to obtain the first name, last name, and SSN of any service-providers that are sole proprietors. The federal Form W-9 was recently revised and now requires sole proprietors to list their first and last names. You may want your service-providers to complete new Forms W-9. If the SSN is still not known after reviewing the W-9, ask the service-provider for the SSN. If the service-provider does not provide it, fill out the SSN box with zeroes (000000000).

**Q18.** If my business contracts with a service-provider on more than one occasion during a year, are the individual contracts cumulative in reaching the \$600 reporting threshold? Also, if I report a service-provider during the year and then enter into another contract that again calls for at least \$600 in compensation, must the service-provider be reported a second time?

**A18.** The threshold for requiring reporting is \$600 in a year on an aggregate basis. Therefore, you would only report once a year for each service-provider, and there is no basis to require reporting each time a service-provider receives \$600 in a year.

**Q19.** My business doesn't have employees. Do I have to register with EDD solely for purposes of reporting my service-providers?

**A19.** No. Service-recipients who are not registered with EDD are not required to register and receive a California employer account number solely for purposes of reporting independent contractor service-providers. Unregistered service-recipients complete the Report of Independent Contractor(s) (DE 542) using their social security or federal employer identification numbers.

**Q20.** For purposes of independent contractor reporting, must the contract be in writing or would a verbal contract also qualify?

**A20.** A contract may be either written or verbal.

**Q21.** My business engages the services of a worker who is my acknowledged employee, and I reported this employee under the New Employee Registry when first hired. This same worker also performs work for my business as a valid independent contractor and receives a federal Form 1099-MISC which reflects this compensation. Must I also report the worker for the independent contractor compensation?

**A21.** Yes.

**Q22.** If my business engages workers whose services are by statute not in subject employment, should I report the workers as independent contractors to EDD?

**A22.** To answer this question, one must first determine if the workers are performing services for the business or government entity as employees or independent contractors. If the workers are engaged as employees, their services would not be reported as independent contractors. However, the business or government entity may be required to report the employees as part of the New Employee Registry (under Section 1088.5 of the California Unemployment Insurance Code) if the requirements of that section are met. When a service-recipient hires workers who are not employees and is required to provide the workers with a Form 1099-MISC, the service-recipient is required to report the workers (service-providers) as independent contractors (under the provisions of Section 1088.8 of the California Unemployment Insurance Code).

**Q23.** Are churches or nonprofit organizations required to report independent contractors they engage for services?

**A23.** Yes. Title 26, Code of Federal Regulations, Section 1.6041-1(b) defines the term "trade or business," which includes churches and nonprofit organizations. Therefore, reporting independent contractors is required.

**Q24.** How can I get a copy of Section 1088.8 of the California Unemployment Insurance Code (CUIC)?

**A24.** You can view the code section at [www.leginfo.ca.gov/calaw.html](http://www.leginfo.ca.gov/calaw.html). Click on "Unemployment Insurance Code," then click on "Search." The CUIC Table of Contents will appear; the code sections are grouped in numerical order on the right side of the page. Scroll down to "1085-1098," click on the link, then scroll down to 1088.8.