



The IRS 20-Factor Test Used by the UIA to Determine Classification as Independent Contractor versus Employee

IRS 20-Factor Test Announced in IRS Revenue Ruling 87-41

Michigan unemployment insurance law requires the Unemployment Insurance Agency (UIA) to use the IRS 20-factor test (discussed in IRS Revenue Ruling 87-41) for purposes of determining if a person performed services during 2013 and beyond, as an employee or as an independent contractor. If a person performing services is an employee, then the employee's wages are subject to state unemployment taxation and the employee may be eligible for unemployment benefits. If, however, the person is found to be an independent contractor, then the employer pays no state unemployment taxes on the individual's earnings and the person's services are not covered employment. To simplify this new analysis, the Agency has, similar to the IRS, grouped the factors into three general categories: (1) Behavioral Control; (2) Financial Control; and (3) Relationship Factors. While no one category or factor is controlling, the categories are intended to provide characteristics of each individual factor. Depending on the specific facts, a particular factor may straddle one or more of the three categories.

A. Behavioral Control Factors:

- (1) **Instructions** An employee is required to follow instructions about when, where and how to do the work. The employer maintains control if the employer can require the instructions to be followed.
- (2) **Training**: An employee receives initial and continuing training from the employer or the employer's agent. Independent contractors are not trained by the business for which they provide services.
- (3) **Services rendered personally** An employee must perform the work directly for the business entity and cannot contract it out because the business entity wishes to direct and control the method and means by which the work is accomplished and the final product or service.
- (4) **Hiring, supervising and paying assistants** An assistant hired, supervised, and paid by a business entity is generally an employee; an independent contractor can hire, supervise and pay its own assistants under a contract that directs and controls how the assistants perform the job and that provides for the independent contractor to provide materials to the assistants.
- (5) **Continuing relationship** If there is a continuing relationship (even if occurring at frequent but irregular intervals it is likely that there is an employment relationship).
- (6) **Set hours of work** If the business entity sets the workers' hours of work, the worker will generally be an employee; an independent contractor would set his or her own schedule.
- (7) **Full time required** An employee would usually work full-time for an employer while an independent contractor can work hours and days of his or her own choosing.
- (8) **Work done on premises** If the work is required to be, or is usually, performed on the premises of the business entity, it is likely that the entity exercises direction and control over the worker as an employee; an independent contractor is required to fulfill the requirements of the contract but may work whenever he or she wishes to work to fulfill those requirements.
- (9) **Order or sequence set** Evidence of direction or control would be when a worker is required to perform the work in the order or sequence set by the business entity, while an independent contractor works in the sequence of his or her own choosing.
- (10) **Oral or written reports** An employee will be required to submit regular reports to the business entity, often in writing, to show the completion of work, evidencing control by the business entity.

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B. Financial Control Factors:

- (11) **Payments by hour, week or month** An employee will usually be paid for specified intervals of work, such as hourly, weekly, or monthly. An independent contractor is more likely to be paid as aspects of the total project are completed, but at no specific time interval.
- (12) **Payment of expenses** Reimbursement to the worker by the business entity of expenses incurred by the worker in completing the job indicates the existence of an employment relationship.
- (13) **Furnishing of tools and materials** Furnishing necessary tools, materials, and other equipment such as office equipment is generally an indication of an employment relationship.
- (14) **Significant investment** If the worker has a significant investment in the facilities where the work is performed, the worker is more likely to be an independent contractor.
- (15) **Profit or loss** While an employee generally is paid for the time to complete the required work, and bears no liability for business expenses associated with completing the work, an independent contractor can generally make a profit or suffer a loss as a result of performing the service.

C. Relationship Factors:

- (16) **Integration** An employee performs services that are integral or essential to the operation of the employer, rather than merely incidental to the business operation.
- (17) **Working for more than one firm at a time** If a worker performs the service for multiple, unrelated business entities on currently, the worker is likely an independent contractor.
- (18) **Making services available to the general public** If a worker holds him- or herself out to the public as being regularly and consistently available to perform the service for anyone contracting with him or her, the worker is likely to be an independent contractor.
- (19) **Right to discharge** If the employer retains the right to fire the worker, the worker is likely to be an employee.
- (20) **Right to terminate** If the worker can quit work without breaching any contractual agreement, the worker is likely to be an employee.

IRS Has Summarized these Factors in the Following Way:

- (1) **Behavioral Control** - Factors to consider are whether the employing entity gives instructions to the worker about how, when, or where to do the work and provides training to the worker. Implicit in this factor is whether the business retains the right to direct and control the worker's performance.



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(2) **Financial Control** – The significant factor is the right of the business entity to control the business aspects of the worker’s job.

(3) **Relationship Of Parties** - The nature of the relationship may be evidenced by the existence of a written contract; by any benefits provided by the business entity such as vacation pay or health insurance; whether the position is of indefinite duration or will cease when the work project is completed; and whether the service is a critical aspect of the business entity.

The above test applies only to services performed by an individual on or *after* January 1, 2013. If the services for which a determination is needed were performed prior to January 1, 2013, then the previously used “economic reality test” must be applied. In cases where an individual has performed services both before *and* after January 1, 2013, it may be necessary to apply both the new and old test. Further, where the nature of the services changed as of January 1, 2013, it is possible to have different determinations applicable to services performed before January 1, 2013 as compared to services performed after January 1, 2013. In such cases, the effective date of the determination applying the new test will be the date on which the nature of the services changed.

For further information about how the UIA applies the IRS 20-Factor test, call UIA’s **Office of Employer Ombudsman (OEO)**, 1-855-484-2636 (4-UIAOEO) or 313-456-2300, or email OEO@michigan.gov.