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Safe Harbor Rule

An employer in danger of being assessed back taxes for certain workers may avoid liability if it qualifies for "Section 530 relief."

Oct. 20, 2023



It never seems to end: The IRS continues to contest classifications of workers who are treated by employers as "independent contractors" instead of employees. And no wonder: There are often thousands of tax dollars — or maybe more—at stake. Fortunately, some employers can rely on a special safe-harbor rule to bail them out of a tough situation.

Here's the crux of the matter: If a worker is classified as an employee, the employer

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How can you tell them apart? To distinguish independent contractors from employees, employers should examine the relationship between the worker and the business, factoring in the degree of control and independence in the relationship. The evidence fall into three basic categories: behavioral control, financial control, and relationships of the parties.

1. Behavioral control covers facts that show whether the employer has a right to direct and control what work is accomplished and how the work is done, through instructions, training, or other means.
2. Financial control covers facts that show whether the employer has a right to direct or control the financial and business aspects of the worker's job. This includes:
 - The extent to which the worker has unreimbursed business expenses;
 - The extent of the worker's investment in the facilities or tools used in performing services;
 - The extent to which the worker makes his or her services available to the relevant market;
 - How the employer pays the worker; and
 - The extent to which the worker can realize a profit or incur a loss.
3. Relationship of the parties covers facts that show the type of relationship the parties had. This includes:
 - Written contracts describing the relationship the parties intended to create;
 - Whether the employer provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay;
 - The permanency of the relationship; and

- The extent to which services performed by the worker are a key aspect of the

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In summary: Taking all these factors into account, employers should protect themselves from potential challenges by the IRS. Your professional advisors can provide the necessary guidance.

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