



# CONTRACTORS VS. EMPLOYEES:

How to Decide Which is Right for Your Business

by Dori Soukup

**W**hen deciding whether to staff your spa business with independent contractors or full time employees, there are many factors to take into consideration. This article clarifies the pros and cons of each to help you make the right choice for *your* business.

**Consider the differences according to the IRS:**

## AN EMPLOYEE STATUS

Under common law rules, anyone who performs services for you is your employee if you can control what will be done and how it will be done. This is so that even when you give the employee freedom of action, you have the right to control the details of how the services are performed.

**Example:** Donna is a massage therapist employed on a full-time basis by Blue Spa. She works five assigned days a week and is scheduled to work at certain times on those days. She performs massages based on the spa's protocols and she must follow the systems and policies of the spa. She is paid a commission and is eligible for awards and bonuses offered by Blue Spa. Donna is an employee of Blue Spa.

## INDEPENDENT CONTRACTOR STATUS

An individual is an independent contractor if the payer has the right to control or direct only the result of the work — and not what will be done or how it

will be done. The earnings of an individual working as an independent contractor are subject to self-employment tax.

**Example:** Lisa is an esthetician hired by Blue Spa to provide facials as an independent contractor. She has the flexibility to set her own hours and come and go as she pleases. She can follow her own protocols and dress however she likes. She doesn't have to follow Blue Spa's operational guidelines and procedures.

Lisa is an independent contractor because the payer does not have the legal right to control the details of how she performs the services.

✦ Keep in mind that if an employer-employee relationship exists (regardless of what the relationship is called), one is not an independent contractor, and their earnings are generally not subject to self-employment tax. However, their earnings as an employee may be subject to FICA (Social Security tax and Medicare) and income tax withholding.

**ESSENTIAL FILING AND FORMS**

**Independent contractors:** An independent contractor must complete Form W-9, Request for Taxpayer Identification Number and Certification.

**Employees:** At the end of the year, you as the employer must prepare and file a W-2 form wage and tax statement to report to the IRS wages, tips and other compensation paid to an employee.

**AVOID COMMON CONFUSION**

Many spas and salons hire independent contractors and then expect them to act as employees. That crosses the line and may be a violation of IRS laws. Do



you have independent contractors who are acting as employees? To be safe, view the differences in detail on [irs.gov](http://irs.gov) and follow the guidelines. Also, consider the following statement on the IRS website:

"Businesses must weigh all these factors when determining whether a worker is an employee or independent contractor. Some factors may indicate that the worker is an employee, while other factors indicate that the worker is an independent contractor. There is no 'magic' or set number of factors that 'makes' the worker an employee or an independent contractor, and no one factor stands alone in making this

determination. Also, factors that are relevant in one situation may not be relevant in another. The key is to look at the entire relationship, consider the degree or extent of the right to direct and control, and finally, to document each of the factors used in coming up with the determination."

Taking the following factors into consideration, only you can decide which path is right for your business. Whichever one you choose, it's imperative to ensure you stay within the IRS guidelines to avoid putting your business at risk.

*"There is no 'magic' or set number of factors that 'makes' the worker an employee or an independent contractor."*



**Employee Status Pros**

- When you hire an employee, you are making an investment in them as well as your business; therefore the selection process becomes more important in your attempt to hire the best candidate.
- Having employees allows you to raise your performance standards and enforce them without crossing the line. You are able to effectively manage your team instead of them managing you.
- In most cases, employees are more invested in their careers and committed to having a long-term relationship. Retention is also more likely with employees than contractors.

**Employee Status Cons**

- You must guarantee a minimum wage to employees. That means that even if they're not busy, they're making money, even though you are not. It is essential to have traffic coming to your spa to justify the cost of employees.
- It's more expensive to hire employees than independent contractors. Employees are more costly due to the fact that the employer has to pay taxes, workers compensation, insurance and possibly unemployment.



**Independent Contractor Pros**

- You don't have to guarantee an hourly wage.
- It's less expensive to hire independent contractors, as you can eliminate the aforementioned costs associated with employees.

**Independent Contractor Cons**

- You can't control contractors' behavior, nor do you have the right to direct and control what work is accomplished and how the work is done.
- You cannot give independent contractors an official schedule. They can come and go as they please. This makes your job as a leader difficult when you're trying to cover all shifts.
- You don't have control over the contractors' training, policies, procedures, uniforms, etc.
- Independent contractors are free agents — they can work for you in the morning, go to another spa in the afternoon and have their own clients at home. This is a lot of co-mingling, which may not be a good thing.



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