

Independent Contractor or Employee? Understanding the Laws and Evaluating the Trade-Offs

Save to myBoK

By Linda Yaniszewski

We all know the state of the economy. Cutting costs has been a mantra in healthcare for years, but recent pressures have been more demanding than ever.

In HIM, the downward pressures in cost conflict with the upward forces in workload. Additional tasks related to recovery audits, ICD-10, quality data reporting, and clinical documentation improvement are being assigned to HIM departments every day. Department directors and outsourced service companies alike are asked to do more with less. One potential area for cost savings lies in "how" human resources are categorized: independent contractors or employees.

Provider organizations and outsourced service companies can achieve savings when they use independent contractors (ICs) rather than full-time employees. This has been particularly common in the areas of transcription and coding. Savings in taxes, insurance, and other benefits can be substantial.

However, with the returns come risks and trade-offs. HIM directors must be certain they fully understand state and federal employment laws and explore the trade-offs fully.

New York Experience Sheds Light on Concerns

When medical transcription services operator ExecuScribe launched in 1989, the New York-based company used a complete IC model, the standard hiring model at the time. Adhering to published IC rules, the company was careful to explain the various benefits and limitations to the independent transcriptionists it contracted with:

- The company did not control their time (they could work for other companies).
- There was no required work schedule (flexible time schedules were permitted).
- The company provided no training or continuing education.
- There was no direct deposit of paychecks. ICs submitted invoices and the company paid them directly.

In addition, the limitations to the IC and the cost-savings to the employer were clear:

- No FICA paid
- No health insurance coverage
- No paid time off (PTO)
- No 401(k) plans or matching funds
- No unemployment taxes paid

Categorizing medical transcriptionists as ICs was working well for ExecuScribe and its staff until the State of New York Unemployment Commission requested a full audit of the company and its practices. The audit permanently changed the company's IC strategy and served as fair warning for many well-intentioned HIM directors and medical transcription services operators.

ExecuScribe provided all contractor files requested by auditors, including all demographic information for its ICs. It also included quality assurance results for each IC, which the company maintained to track performance and ensure quality work. Much to the company's surprise, the state commission considered the demographic information as a legal "employee file."

Furthermore, the quality assurance information was looked upon as employee training. At the end of the audit process, all ICs were declared ExecuScribe employees.

A New Direction-Converting ICs to Employees

Initially the company was required to pay back FICA, unemployment taxes, penalties, and interest. It was a financial disaster and a bleak year. Over the next several months it became clear that the ExecuScribe audit was part of a new state agenda. From 2002 to 2005 a state task force determined that up to 10 percent of workers in New York state were misclassified by their employers.¹

As if the state audits weren't enough, there was also a risk of the federal government getting involved. A company could incur more than \$1 million in penalties and fines if the federal government conducted an audit and reclassified its ICs as employees. Clearly, it was time to make a change.

For ExecuScribe, the only viable solution was to transition to an employee model. The company announced its intentions and within 90 days had successfully converted 98 percent of its ICs to employees.

The trade-off for ICs was that ExecuScribe would pay a lower line rate for transcription but provide complete benefits. In addition, the company assigned and enforced set hours. Initially ExecuScribe expected to see a huge drop in profits, but this did not occur.

As with most changes, communication was the first and most important step. The management team explained the need to transition from ICs to employees. ICs were provided with frequently asked questions, company documents, webinars, and face-to-face meetings. It was explained that the decrease in line rates would be more than offset by the benefits they would receive as ExecuScribe employees. In fact, the benefits worked as a tool to enhance recruitment efforts and minimize turnover.

The few transcriptionists who remained ICs were educated on the state regulations, which required them to:

- Form an independent corporation
- Have multiple clients
- Advertise in some form of media (e.g., a telephone directory)
- Carry workers' compensation insurance

At the federal level, IRS guidelines can be used to determine whether an individual is an employee under the common law rules. HIM directors and outsourced service companies should ensure they are as compliant as possible with this guidance (see sidebar).

The IRS Independent Contractor Test

The IRS offers guidelines for determining whether an individual is an independent contractor or an employee. The guidelines consider 11 factors divided across three categories. Following is a high-level summary; the full version provides a description for each factor.

Behavioral Control

Facts that show whether the business has a right to direct and control how the worker does the task for which the worker is hired include the type and degree of:

1. Instructions the business gives the worker
2. Training the business gives the worker

Financial Control

Facts that show whether the business has a right to control the business aspects of the worker's job include:

1. The extent to which the worker has unreimbursed business expenses
2. The extent of the worker's investment
3. The extent to which the worker makes services available to the relevant market
4. How the business pays the worker
5. The extent to which the worker can realize a profit or loss

Type of Relationship

Facts that show the parties' type of relationship include:

1. Written contracts describing the relationship the parties intended to create
2. Whether the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay
3. The permanency of the relationship
4. The extent to which services performed by the worker are a key aspect of the regular business of the company

Source: Internal Revenue Service. "Employer's Supplemental Tax Guide." Publication 15-A. January 25, 2010. Available at www.irs.gov/pub/irs-pdf/fss8.pdf.

Surprising Results, Safer Outcomes

Following the conversion, ExecuScribe experienced surprising results. Productivity rose dramatically. Transcriptionists received assignments and designated hours to complete their work. Quality improved, and turnaround time was reduced.

ExecuScribe managers also saw a boost in productivity and accountability. In the past they had been required to manage 40 ICs doing the work of 20 employees. Because coordinating work for full-time employees is much easier, the same managers now oversee up to 50 full-time employees.

Results of the change were communicated back to the entire team: morale improved, there was a new sense of company loyalty, and medical transcriptionists began competing for work. Company profits increased, and everyone was able to do more with less.

Robin Agan was an IC who joined the company as an employee. She values the stability of her new employee status.

"The security of knowing I would have work when the recession began provided stability and peace of mind, and the 401(k) is a huge factor," she says. "I was also provided much more company information and felt very involved as an employee versus just being a contractor. I feel much more connected to the company."

Lisa Bird, also a former IC adds, "[Paid time off] has been a big help, plus disability benefits give my family more peace of mind knowing that if something were to happen we have financial security. I am very pleased with the transition to an employee."

While using only ICs may be tempting from a cost-saving perspective, most HIM directors and outsourced service companies today use a mix of ICs, employees, and outsourced services as necessary. Should organizations choose to use ICs—even just a few of them—they must ensure they understand and abide by state and federal requirements.

ICs who sit in front offices, receive benefits, are assigned specific work hours, or get paid via paychecks will be considered employees. HIM directors, human resource directors, and company executives must be aware of these risks.

Note

1. Joint Enforcement Task Force on Employee Misclassification. "Report of the Joint Enforcement Task Force on Employee Misclassification to Elliot Spitzer, Governor State of New York." February 1, 2008. Available online at www.labor.state.ny.us.

Linda Yaniszewski (lyaniszewski@execuscribe.com) is CEO of ExecuScribe and immediate past chairperson of the Medical Transcription Industry Association.

Article citation:

Yaniszewski, Linda. "Independent Contractor or Employee? Understanding the Laws and Evaluating the Trade-Offs" *Journal of AHIMA* 82, no.1 (January 2011): 32-34.

Driving the Power of Knowledge

Copyright 2022 by The American Health Information Management Association. All Rights Reserved.