# The Worker Classification Flowchart

A COMPLIANCE FRAMEWORK FOR W-2 EMPLOYEES VS. 1099 CONTRACTORS

**The Audit Risk:** Misclassifying employees as independent contractors is one of the single largest audit triggers for both state Departments of Labor and the IRS. Simply having a signed "Independent Contractor Agreement" means nothing if the operational reality violates federal guidelines. Follow this structured compliance logic map to verify classification status.

## STEP-BY-STEP STATUTORY LOGIC MAP

### Test 1: Behavioral Control & Autonomy

Does your company set the exact working hours, mandate specific sequence methods, dictate strict software tools, or supervise the worker's execution daily?

➔ **If YES:** This worker strongly leans toward a **W-2 Employee** status. Employers cannot micromanage an independent contractor's execution methods, only the final project delivery.

### Test 2: Financial Control & Capital Investment

Does the worker use their own specialized tools, computers, and licensing? Do they maintain an active, distinct business entity that services multiple separate clients? Do they realize a true opportunity for profit or financial loss?

➔ **If YES:** This worker aligns with a **1099 Independent Contractor** framework. If they rely on your internal laptops and have zero other commercial clients, they are likely an employee.

### Test 3: Core Integration & Nature of Relationship

Is the worker executing the fundamental, core service your company sells to customers? (e.g., hiring a graphic designer to build your logo vs. hiring a software developer to build the core app your tech firm sells).

➔ **If YES:** Regulatory agencies almost always classify core business functions as **W-2 Employee** roles.

## OPERATIONAL SUMMARY MATRIX

| OPERATIONAL FACET | 1099 INDEPENDENT CONTRACTOR | W-2 EMPLOYEE |
|---|---|---|
| **Payment Basis** | Flat project fee or milestone rate invoiced directly by the worker's business. | Hourly wage or consistent salary processed via recurring corporate payroll. |
| **Tax Structures** | No corporate withholdings. Issued a 1099-NEC at year-end; handles self-employment tax. | Company handles automatic federal, state, FICA, and local payroll tax withholdings. |
| **Business Tools** | Supplies their own independent operational software, hardware, and licensing. | Uses company-provided physical equipment, systems, and email setups. |

Misclassification penalties can carry crippling retroactive tax, overtime, and benefit liabilities.

**Let Centioli Compliance Services clean up your contractor and payroll structures.**