

Assessing the Tricky Status of Your “Independent Contractors”

Rules You Should Know

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<u>Table of Contents</u>	<u>Page</u>
Benefits of Independent Contractors	1
Complicated Guidelines	1
Guidelines	1
Contract	2
Pay	2
Work Method	3
Miscellaneous	3
Conclusion and Future Action	4

Benefits of Independent Contractors

Independent Contractors (“ICs”) are an everyday resource for many companies in the U.S. In a mutually beneficial relationship, the company gets a highly qualified person who is an expert in their field. The worker has the flexibility to provide services to more than one company and can provide services when he or she chooses. The company does not have the legal responsibilities of an employer and has dramatically lower costs due to other savings.

Complicated Guidelines

You must manage Independent Contractors completely differently from employees. If a company does not follow the legal guidelines for use of Independent Contractors, a variety of problems can befall you. The government can seek to reclassify the Independent Contractors to employees, you may have to pay back-employment taxes to the government, and you may be required to offer similar benefits to the IC that have been offered to employees if your employee claims unemployment benefits or sues you. This can cause unexpected, significant losses and needless time in fighting adverse findings by government agencies such as the Illinois Department of Employment Security (“IDES”).

By law, an Independent Contractor rela-

tionship must be structured and operated completely differently from an employer-employee relationship. Independent Contractors are independent mini-businesses. Independent Contractors must be allowed to provide services in methods they choose. As their customer, you can set requirements and deadlines. However, the requirements must be quantitative goals and the Independent Contractor must be allowed to choose the way in which they conduct the work – not according to your methods. Do not manage an Independent Contractor using traditional employee supervision methods.

An employee, on the other hand, is fully controlled by the employer. Employees are supposed to follow every instruction and are required to follow any lawful workplace rule, no matter how detailed. In addition, you provide a costly range of financial support for the employee and assume much greater legal liability towards the employee.

Guidelines

Fortunately, there are known guidelines to avoid problems. The below guidelines must be interpreted in a matrix-like manner. Some guidelines can be critical and some can be less meaningful. It depends on your business and how all the factors interrelate as a whole. The degree or existence of each factor will differ depending on your particular situation. No factor is necessarily decisive, but you should take into account all factors. If you need further help on these issues, we can help you.

We strongly suggest you follow our Do’s and Don’ts of using and managing Independent Contractors.



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With creative, cost-effective re-structuring of your Independent Contractor rules, minor modifications may dramatically increase your legal compliance and avoid problems.

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Contract

Do's	Don'ts	Why?
Do have a written agreement with your Independent Contractors (the "IC").	Do not rely on a "hand shake" agreement.	A written agreement is not common in the rank-and-file employer-employee relationship
Do include a provision to transfer to your company all ownership of copyrighted material produced by an IC.		Failure to do this means an IC will own any materials her or she creates for you.

Pay

Do's	Don'ts	Why?
Do pay an Independent Contractor contingent upon completing tasks or upon completing the job.	Do not pay an Independent Contractor wages or amounts measured by regular intervals (i.e., per hour, week, month).	Paying by the hour, week or month tends to show an employer-employee relationship.
	Do not pay their expenses.	An independent business would naturally pay all its expenses
	Do not pay Independent Contractors from a payroll account.	Only employees should be paid from a payroll account.
Do obtain an Independent Contractor's taxpayer ID number or social security number if an Independent Contractor will make over \$600 a year.		If you do not report Independent Contractor payments, the IRS will require you to withhold 31% of all payments to Independent Contractors above \$599.
	Do not give IC's similar benefits as are given to employees.	Explain to the IC that this is necessary. Your employees will also appreciate that they are receiving greater benefits.
Do file a Form 1099-MISC with the IRS and give a copy to the Independent Contractor.		Filing a Form 1099-MISC will ensure that IRS Safe Harbor protections are retained.

Work Method

Do's	Don'ts	Why?
Do allow an Independent Contractor to work when she wants.	Do not require an Independent Contractor to work "full-time" for you and do not require set hours.	Allowing an Independent Contractor to choose their own hours of work tends to show no employer-employee relationship.
Do allow an Independent Contractor to work off premises.		An Independent Contractor should have some office space separate from the company. Usually, only employees are provided with free office space.
Require results from the Independent Contractors, not a method for completing the work. Detailed requirements including deadlines are absolutely allowed and actually beneficial.	Do not control the order and sequence of an Independent Contractor's work.	<ul style="list-style-type: none"> • Controlling an Independent Contractor's order and sequence of work tends to show control, which is consistent with an employer-employee relationship. • Of course, you can require the Independent Contractor to follow job and company rules.

Miscellaneous

Do's	Don'ts	Why?
	Do not have Independent Contractors and regular employees do similar work.	Allowing an Independent Contractor to do the typical repetitive work performed by other employees shows an employer-employee relationship. The closer the work of an Independent Contractor is to the core business operations, the more likely it is that the work should be done by an employee.
Do hire an incorporated Independent Contractor.		Since an incorporated Independent Contractor is already an employee, he cannot be your employee. Usually, this is a lesser factor.
Do keep good records of all transactions with IC's.		Good recordkeeping will support your case.
	Do not provide continuing career education to an Independent Contractor.	You can provide training specific to your company procedures.

Miscellaneous (continued)

Do's	Don'ts	Why?
Do allow Independent Contractors to use other people to render services.		An Independent Contractor rendering service through another person or entity tends to show that the company lacks control over the work methods of the Independent Contractor.
Give Independent Contractors specific project completion dates.	Do not hire Independent Contractors for indefinite or extended periods.	An indefinite term of work is a hallmark of an employee. IC's can be used regularly, it's just that each project should have clear beginning and end dates.
	Do not give an Independent Contractor the tools and materials for completion of the job.	Providing tools and materials is something done for employees, not independent parties.
Do allow Independent Contractors to work for more than one person at your company.		If more than one person at the company uses the Independent Contractors work, this tends to show they lack close supervision.
Do require the Independent Contractors to have their own business cards.		Independent business people have their own cards. This is important. IC's should be offering their services regularly to other companies.

Conclusion and Future Action

If you use Independent Contractors, the above rules may seem unrealistically restrictive for your business. Yes, it is difficult to follow all of the rules simultaneously. Nevertheless, I have seen first-hand how businesses have borne losses for not following these rules.

With creative, cost-effective re-structuring of your Independent Contractor rules, minor modifications may dramatically increase your legal compliance and avoid problems. You should compare the above rules to your Independent Contractor work methods and make sure you comply with the law.

If you need help interpreting these rules, we would be glad to help you.

This article does not constitute the giving of legal advice. Please seek legal counsel who can assess your individual legal situation in compliance with the law.

About CorpLaw Associates LLC

CorpLaw Associates LLC is a law firm of experienced business attorneys who deeply understand their clients' businesses and who use best practices to achieve their clients' business goals. The firm provides full support for businesses. For clients who need on-site legal help, CorpLaw is one of only a few firms that specialize in this model. Our mailing address is CorpLaw Associates LLC, 400 Central Avenue, Suite 150, Northfield, Illinois 60093. We can be contacted at 847.784.1300 or at firm@corplaw.com. Our web address is www.corplaw.com.

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Charlie is an accomplished business legal adviser, having practiced corporate law for 23 years. He has held senior Law Department roles in major companies, including as General Counsel. While specializing in IP (patent management, trademarks and trade secrets), he counsels company boards and executives in the U.S. and abroad in a wide range of business issues. His experience spans a number of industries; Charlie has served in leadership roles in different bar associations. He is active in civic affairs. Charlie's e-mail address is charlie@corplaw.com.