



Best Practices for Working with Independent Contractors

Are your Independent Contractors putting you at risk? The IRS is taking the practice of hiring independent contractors very seriously and so should you.

Independent Contractors (ICs) are self-employed, hired to do a specific job and receiving payment only for the work performed. Unlike a regular employee, they pick their jobs and regularly move from client to client, business to business. Also referred to as freelancers, consultants and “1099’s”, they report the payments received as business income and pay self-employment taxes.

Hiring an IC is attractive to those companies looking for outside creative resources, and who want to outsource work that is not central to their main line of business. The work is project-oriented and is typically completed in a short amount of time. And, you are better able to meet budget by paying your IC as a vendor, not as an employee.

But there’s a big catch. The IRS has very strict guidelines that define true business-to-business relationships. These guidelines are meant to prevent firms from misclassifying would-be employees and thereby avoid, either knowingly or unknowingly, a bounty of state and federal taxes.

So again the question, **is your IC really an Independent Contractor?** This is a complex question that’s important to answer “yes” because the risk of your company facing an IRS audit has never been greater.

Key things to require when working with an IC:

- Your contractor has an established business entity, with a business name and EIN to which invoice payment is made.
- Your contractor provides services to other businesses outside your firm.
- Your IC provides certificates of insurance, including at the least coverage for general liability insurance and work comp insurance.
- You have a signed per project Agreement for Services between your company and the contractor.

continued on next page

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Watch out for:

- A situation where the contractor works only, or primarily, for your business. Independent contractors should work for multiple clients throughout the year.
- No contract or agreement for work performed. Each project should have a contract specifying project length, compensation and liability.
- Reimbursements for travel, phone, meals and overtime wages. Independent contractors should be including these expenses in their day rate.
- When an IC's work is integral to your business. An independent contractor's services should not impact the day-to-day functioning of your business. They should not be functioning as a division of your company and have no identity separate from their contract with you.
- Open ended, on going work. The longer a contractor is with you on a full time basis, the more they take on the role of an employee.

When working with your contractors:

- Do not train a contractor, direct their work responsibilities or define their work schedules. Specific instructions on how a job should be completed imply an employee relationship.
- You cannot control any aspect of their work; only the right to judge the results.
- Independent contractors should, when feasible, be using their own equipment. This includes computers and phones.
- Do not provide any employment benefits. Independent contractor's should have their own health insurance, pay their own employment taxes and not receive any corporate stock options.
- You contract on a per project basis.
- Above all, keep in mind that this is a business-to-business relationship.

Getting audited can be scary even for businesses that do everything by the book. How much are you willing to pay for employee misclassification? If you have any questions about independent contractor status, trust PayReel to help you make the determination. We screen each employment situation carefully to assess the entire relationship to make sure you are in complete compliance.

If you have questions about compliance and hiring Independent Contractors, you should take our **PayReel Self Audit**, located at www.payreel.com. The ten minutes of your time it takes to complete the Self Audit may save you years of headaches.

PayReel and sister company Crew Connection have 35 combined years of experience helping companies navigate the complex issue of compliance and working with Independent Contractors. Call us at 303-526-4900 or email info@payreel.com. Let us help you.