

WHY SIGN OUR INDEPENDENT CONTRACTOR AGREEMENT?

As you prepare to provide services as an Independent Contractor (IC) to our firm's clients, you may have some questions about some of our requirements. For example, "Do I really need to sign this formal, multi-part, IC Agreement?" or, "Why is so much information required from me?" These are reasonable questions – ones asked many times by many professionals in similar situations. We think it may be helpful to provide you with some background information about our IC Agreement and why it is so important in confirming your IC relationship with us.

Our IC Agreement is based upon a model agreement used by hundreds of companies that belong to North America's largest trade association of staffing firms that specialize in providing highly-skilled professionals to work with clients in need of temporary project support. That model agreement has been reviewed by several attorneys to assure that the proposed IC relationship complies with the ever-changing laws and regulations applied by the IRS and state tax agencies. By using this IC Agreement, the IC (your business), the staffing firm (us), and the client are able to demonstrate a valid relationship in which each party is in a business-to-business relationship, as contrasted to an employer-employee relationship.

The nature of a relationship – business-to-business vs. employer-employee – has many important consequences for the IC, the staffing firm and the client. Over the years, the IRS and state tax agencies have conducted random tax audits in order to "re-classify" many ICs as employees of either a staffing firm or its clients. For example, the IRS can assess potentially large amounts of taxes, penalties and interest on the staffing firm and the ICs if it "re-classifies" the IC as an employee – and even if the IC has paid all of its taxes in full, the IRS can and will make these assessments. In these situations, a "re-classified" IC could also have its pension plan disqualified or its valid business expenses disallowed.

It is important to operate properly under the law to avoid these negative consequences. And the current IC Agreement and procedures that we are using have stood the test of time in many IRS audits where firms like ours and ICs like you have been able to demonstrate that the IC is in a valid business-to-business relationship with the staffing firm and the client – and not in an employer-employee relationship. In fact, to our knowledge in all cases where a staffing firm has used this model IC Agreement, no IC who followed valid business practices and operated under the terms of this IC Agreement has been "re-classified" as an employee by the IRS. For these reasons, the IC Agreement should be signed – it is for our mutual protection.

Now that you have an understanding of some of the reasons for the IC Agreement, below are some frequently asked questions and answers about specific parts of it. If the tax laws were different, our firm and many others would surely use shorter, simpler agreements. But because of IRS activity and the serious consequences of "re-classifying" ICs, the IC Agreement is longer and more detailed we would really prefer. However, the comments below are brief and do not present a complete explanation of the IC Agreement. Because this summary may not have all the details that you want, be sure to read the full IC Agreement carefully before you sign it.

DURATION OF SERVICES

Paragraph 2 of the IC Agreement, entitled Duration of Services, requires an IC to remain with a client project through the agreed upon "end date" in the Purchase Order. This means that if an IC

promises to provide professional services on a client project through that “end date”, the IC must be prepared to honor that commitment as long as we do not breach our agreement with the IC. In the same way that the IC is bound by this “end date”, our firm is also bound by it – that is, we cannot unilaterally terminate your services unless you are in breach of our agreement with you. The reason for an “end date” is that the IRS has historically stated that if a worker can be unilaterally terminated at any time or if a worker can unilaterally quit at any time, then the relationship seems more like an at-will employment relationship between employer and employee, rather than a business-to-business relationship between a firm and an IC. In other words, the IRS is much more likely to “re-classify” an IC as an employee if the parties have not established an “end date” for the services. However, in the IC Agreement there is an exception to the requirement that the “end date” must be honored, and that exception is where the client itself confirms that the project is completed before the “end date” or the client no longer needs or wants the IC’s services. Although neither you nor we like a situation in which the client has the right to terminate at any time, the reality is that clients insist on keeping that right and will not agree to retain your services if they do not have that right.

RESTRICTIONS REGARDING CLIENTS, EMPLOYEES & OTHER CONTRACTORS

Paragraph 3 of the IC Agreement, entitled Restrictions Regarding Firm’s Clients, Employees And Other Contractors, clarifies that an IC has the right to provide services for whichever clients and other staffing firms that the IC desires – with one exception: if an IC contracts with our firm to provide services for one of our clients, then the IC cannot provide services for that one client either directly or through another firm until the passage of one year after the time that the IC stopped providing services to that client through our firm. This is a very narrow restriction that leaves the IC in a position to provide services to thousands of potential clients, and yet protects our firm’s business relationships and confidential information with the particular client that the IC serviced through our firm. In addition, so our firm can reasonably protect our goodwill with our employees and other ICs, for a similar one year period the IC Agreement prohibits the IC from hiring or trying to hire any of our employees or other ICs with whom the IC was involved while providing services through our firm.

INSURANCE

Paragraph 11 of the IC Agreement, entitled Insurance, requires the IC to provide both General Liability insurance and Worker’s Compensation insurance. These types of insurance are required by our clients from us and from all ICs. In addition, the IRS has often taken the view that if an IC is covered under a staffing firm’s insurance plans, and not under the IC’s own plans, then that is one sign that the IC should be “re-classified” as an employee. This is consistent with the IRS view that legitimate businesses insure against their own risks by buying their own insurance, at their own expense.

PAYMENTS

Paragraph 5 of the Contractor Agreement, entitled Payment for Services, and the Purchase Order require that the IC must assume the business “risk of nonpayment”. In a key legal ruling, the IRS specifically identified the “risk of nonpayment” as one of the most important factors to distinguish ICs from employees: if a client refuses to pay the staffing firm for services, an employee must still receive his or her guaranteed wages, but in these circumstances the staffing firm cannot guarantee payment of fees to the IC. If the firm guarantees payment to the IC regardless of the client’s payment to the firm, the IRS would likely “re-classify” the IC as an employee.

In closing, please keep in mind that although a proper IC Agreement is essential to establishing a valid IC relationship, the parties to the IC Agreement must also operate in a manner which indicates that the IC is conducting a valid business. Additional items to which the IRS and state agencies pay particular attention in an audit are:

- Business name of incorporated IC (or other entity) and Employer Identification Number on IRS Form W-9 (EIN)
- Business letterhead, stationery, cards, and invoices of IC
- Brochures and advertising by IC (e.g., directories, yellow pages, newspapers, trade journals, web postings)
- Separate business telephone line for IC
- Office and other itemized non-reimbursed expenses incurred by IC
- Business insurance policies in IC's name
- Maintenance of separate IC business books, records and checking account
- Simultaneous generation of income by IC from more than one source/client
- Proper tax filings by IC (e.g., IRS Form 1120/1120S and Forms 940/941/W-2 for incorporated ICs)

¹ This summary is not part of the IC Agreement, but instead highlights some key issues and answers some common questions. This summary is not legally binding in any way. Completeness and accuracy can only come from reading the IC Agreement carefully.