

Independent Contractors or Employees?

Law firms, just like any other business, must be sure that the lawyers, paralegals and other individuals providing services to the firm are correctly classified as either independent contractors or employees. If the firm is audited by a federal or state agency or challenged by a worker and is determined to have incorrectly classified a lawyer, paralegal or other service provider as an independent contractor rather than an employee, the consequences could be severe. The law firm could be responsible for unpaid federal and state income and employment taxes; pension and profit sharing, health, life, disability, and other employee benefits; workers' compensation benefits; and unemployment benefits. The firm also could be exposed to potential liability for failure to provide protected family medical or sick leave, violation of discrimination or wage and hour laws, failure to comply with I-9 requirements, and a host of other employment-related claims.

Agencies and Tests Governing Independent Contractors

Several state and federal agencies audit businesses to determine whether they have correctly classified individuals as independent contractors or employees. In Oregon, some of the state agencies that evaluate whether a person is correctly classified as an independent contractor include the Department of Revenue, the Employment Department, the Oregon Bureau of Labor and Industries, the Construction Contractors Board, the Landscape Contractors Board and the Workers' Compensation Division.

At the federal level, the IRS and the Department of Labor both independently audit employers to ensure that the workers are correctly classified as independent contractors. The IRS has adopted a 13 factor test broken down into three categories: behavioral control, financial control, and relationships. The Department of Labor has issued an interpretive memorandum entitled "Administrator's Interpretation No. 2015-1," which is intended to provide guidance to employers in determining who should be classified as an employee rather than an independent contractor under the Fair Labor Standards Act.

The various state and federal agencies auditing these relationships each apply different tests and factors in analyzing whether a person is an employee or independent contractor. The Department of Labor and the Bureau of Labor, Wage and Hour Division, apply an "economic reality" test; the Oregon Department of Revenue applies the factors listed in ORS 670.600; the Oregon Civil Rights Division and the Workers' Compensation Division apply the "right-to-control" test. (See the accompanying Resources sidebar of federal and state websites.)

The Contract

Given the complexity of classification and the risks of incorrect classification, law firms wanting to retain lawyers or paralegals as independent contractors should consider drafting a written agreement setting forth the factors that legally establish an independent contractor relationship. Provisions the parties may want to consider include the following:

- The lawyer/paralegal is responsible for their own income taxes, including estimated tax payments, and self-employment taxes (in lieu of Social Security and Medicare taxes), professional liability insurance, and excess coverage.
- The firm will issue a Form 1099-MISC for the services performed by the lawyer/paralegal unless the firm determines that such Form is not required to be issued.
- The firm and lawyer/paralegal agree that they are not entering into a joint venture and do not have a shared business interest.

- The lawyer is currently licensed and in good standing with the Oregon State Bar, has current professional liability coverage, and has no pending malpractice claims or ethics complaints.
- The lawyer does not have a conflict with any of the parties involved in the assigned project.
- The lawyer agrees to at all times fulfill his or her professional duties to protect information that is proprietary, privileged, work product and/or confidential.
- The lawyer will at all times comply with his or her ethical and legal responsibilities as a lawyer licensed to practice law in the state of Oregon.
- The lawyer/paralegal will return or shred all client documents, including all electronic and hard copies of the documents, when the project is complete.
- The lawyer/paralegal will not receive any employee benefits, unemployment compensation or workers' compensation coverage.

The Working Relationship

Lawyers/paralegals working as independent contractors should have their own office, business cards, e-mail account (separate from the law firm's e-mail), online research tools, computer and copying capability, and tax ID number. The contract lawyers/paralegals should not be integrated into the law firm or expected to regularly work at the firm or attend firm meetings because they are not employees of the firm. Independent contractors set their own rates and fees, making their own determination as to what they will charge to complete a specific project; at the completion of the project, the contract lawyer/paralegal should submit an invoice to the firm for the work performed. Independent contractors set their own hours and perform their work without supervision; the law firm should not be exercising control over or closely monitoring how the work is performed. While the independent contractor and the firm may agree on the specific requirements and deadlines for the assigned project, the firm should not be supervising the project.

A lawyer/paralegal working as an independent contractor should be contracting to work for more than one firm and should not be economically dependent on any one firm as a source of business. While independent contractors may work regularly with one firm, they must also work with other firms; the working relationship can be frequent but not constant, allowing some intervals when the contract lawyer is not doing work for the firm. The firm's financial success should not be dependent on the work of the independent contractor. As independent contractors work for several firms, they cannot be subject to non-compete agreements.

Independent contractors generally should not be former employees who are performing the same job they had when they worked as an associate or a paralegal in the firm, nor should they be performing the same job duties as employees currently working for the firm. As they are not employees, independent contractors cannot be "fired at will." Instead, the terms of the contract determine the consequences if the contract lawyer/paralegal fails to satisfactorily complete the project they contracted to perform according to the contract specifications.

Summary

In summary, firms wishing to establish an independent contractor relationship with a lawyer, paralegal or other service provider may want to consider the following guidelines:

- **Right to Control** – The firm should provide information necessary for the contract lawyer/paralegal to perform the work assignment, including the date when the work

needs to be completed, but should not micromanage the “means and manner of providing the services.”

- **Scheduling** – The contract lawyer/paralegal should be allowed to set his or her own work hours.
- **Location** – To the extent possible, contract lawyers/paralegals should perform the work outside the firm, using their own computer and research tools.
- **Compensation** – Payment should be made on a project basis; contract lawyers/paralegals should invoice the firm for the work performed.
- **No Employee-Type Benefits** – The firm should not pay for or provide benefits such as insurance for the contract lawyer/paralegal. The firm should review its employee benefit plan documents and consider an exclusion for workers classified by the firm as non-employees, even if they are later reclassified, even retroactively, as employees.
- **1099 Tax Form** – A Form 1099-MISC (not a Form W-2) should be issued to the independent contractor at the end of the year if the payment amount is at least \$600.

For the contract lawyer, the overall goal is to maintain an “independently established business,” which is the test codified in ORS 670.600 and utilized by the Oregon Department of Revenue. While no single factor is conclusive, contract lawyers/paralegals should consider the following steps to maintain their independent contractor status:

- **Independent Office** – Contract lawyers/paralegals should have their own place of business.
- **Assignments** – Contract lawyers/paralegals should work on a project or assignment basis and invoice firms for the work performed.
- **Diversify** – Contract lawyers/paralegals should strive to work for more than one firm, seeking work through appropriate legal and business publications, speaking engagements, and professional networking opportunities.
- **Business Expenses** – Contract lawyers/paralegals should pay for their own supplies, office expenses, staffing and copying assistance, online research tools, business cards, stationery, and business expenses.
- **Bar and Licensing Requirements** – Contract lawyers/paralegals should pay for their own professional licensing expenses, memberships, fees, CLE requirements, and business licenses.
- **Insurance** – Contract lawyers should maintain legal malpractice insurance.
- **Taxes** – Contract lawyers/paralegals must pay their own income taxes, including estimated taxes, and self-employment taxes; they should request that a Form 1099 be issued reflecting payments for their services.

While there is not a bright-line test for determining whether a lawyer/paralegal is an independent contractor or an employee, carefully defining the terms of the relationship in a written contract may be helpful in avoiding an obvious misclassification and limiting the potential risks associated with this type of business relationship. Although this article describes the basic issues to consider, law firms are encouraged to consult employment counsel with respect to specific situations relating to their contracts with lawyers, paralegals or other service providers.

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Editor’s Note: This article should not be construed as legal advice. Please consult qualified employment counsel with respect to specific situations.

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Resources [Sidebar]

Federal:

- Internal Revenue Service

<https://www.irs.gov/businesses/small-businesses-self-employed/independent-contractor-self-employed-or-employee>

<https://www.irs.gov/businesses/small-businesses-self-employed/independent-contractor-defined>

Oregon:

- State Agency Criteria for Independent Contractors Chart

<https://www.oregon.gov/ic/Documents/State%20Agency%20Criteria%20TABLE.pdf>

- Department of Revenue / Employment Department / Construction Contractors Board / Landscape Contractors Board

www.oregon.gov/IC/pages/12-definition.aspx

- Bureau of Labor and Industries – General

https://www.oregon.gov/boli/TA/pages/t_faq_independent_contractors_11-2010.aspx

- Bureau of Labor and Industries – Wage and Hour Division

https://www.oregon.gov/boli/TA/docs/boli-whd_test_11-2010.pdf

- Bureau of Labor and Industries – Civil Rights Division

www.oregon.gov/boli/TA/docs/boli-crd_test-11-2010.pdf

- Workers' Compensation Division

www.cbs.state.or.us/wcd/compliance/indcon.html

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