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What Agencies Should Know About Using Freelancers (ICs)

Disclaimer

Disclaimer: This is intended to be a general guide. The authors are **not** attorneys, accountants, or tax advisors. Every effort has been made to offer current and accurate information, but errors can occur. We assume no liability for errors, omissions, or information that may be different in your area or change over time. References to certain laws, regulations, and practices may change over time and should be interpreted only in light of particular circumstances. Information is presented “as is” with no guarantees of completeness, accuracy, or timeliness. *Please consider the appropriateness of any information for you and your business.*

Please consult your attorneys, CPAs, business advisors, or tax advisors with questions or when making business or legal decisions. No portion of this is to be construed, under any circumstances, as legal advice!

When selecting advisors, be sure they are familiar with current state and federal independent contractor law.

Terms

- Independent Contractor (IC)
- Freelancer

Please note that we will use the terms independent contractor, IC, and freelancer interchangeably, as they mean the same thing for our purposes.

Have and Use Business Advisors

- Seek the advice of an attorney
 - One that specializes in IC law and is current with the changes that are happening
 - Have them develop your IC service agreements (contracts)
- Use a CPA or an accountant

A Changing Environment

Due to changes in the legal environment in the last few years, state and federal governments are showing an increased interest in workers with independent contractor status. This is partly because they obtain less revenue from ICs than employees and partly because of their interest in protecting workers from exploitation.

Is a worker an IC?

It is imperative to understand that you **cannot** make someone an IC just because *you want them to be (or they want to be) a freelancer*. They can only be an independent contractor when and if it is legal to be one -- more precisely when your relationship with them does **not** meet the definition of employment. Otherwise, the government may consider them misclassified by the business, **regardless of what you (or the worker) want or intend**.

Laws vary from state to state. Know yours.

Is a worker an IC?

This website may help you better understand:

<https://www.dol.gov/agencies/whd/flsa/misclassification/myths/detail>

Note: The above website was written from the viewpoint that unless specifics are met, the worker should be an employee; and that to be an IC it is crucial that the worker is in business for themselves not just on paper, but in fact; and that the relationship with the entities they work with does not meet the legal definition of employment.

Know how to contract with ICs

This list presents the most important things an agency can do to demonstrate that they are using ICs properly and are complying with IC law.

Note: While partly inspired by recent changes to California law, this information also applies to all states with similar laws and to the IRS. These checklist items will aid agencies anywhere in the US. However, be aware that laws vary from state to state.

ICs are a Business

To start, you need to understand this:

Freelancers (aka Independent Contractors) are self-employed, which means they run their own businesses.

ICs are not like employees in any way, shape, or form.

Whether sole proprietor, LLC, or corporation, an IC owns a business, runs a business, and performs services through their business.

As an agency, you do not **hire** them. You **contract** with them. They are not your employee; they are a vendor. They contract **with** you. They do **not** work **for** you.

Independence

ICs should be independent businesses. The answer to these questions should therefore be “Yes”:

- Is the person performing work engaged in an occupation or business that is distinct from that of the agency?
- Are they willfully and knowingly running an independent business?
- Do they work with multiple agencies and/or directly for clients/consumers?
- Is there a contract between the agency and the worker?
- Do both parties agree they are creating a vendor or independent contracting relationship?

Contracts

Freelancers are independent businesses. When you contract with freelancers, you are not their employer. They do not work for you. You should have a written independent contractor or vendor contract with each freelancer.

Contracts (sometimes called agreements) should specify items such as pay rates and terms, services to be performed, and other elements specific to the work and relationship.

Contracts should be drawn up by an attorney specializing in Independent Contractor law.

Termination

Unlike employees, agencies do not have the right to discharge ICs at will, without cause.

Once you contract with an IC for a job, you and they are contractually bound. If you take that job away from them without cause, you are in breach of contract and may be sued for damages. The only exception is if the freelancer breaches the contract beforehand. As there are times that are out of your control (the client cancels the job or prefers a different service provider, etc.), it is suggested that your IC contracts include a clause that allows for these possibilities.

Distinct Business Function

In our industries (captioning and deposition or freelance court reporting), it is a crucial characteristic that agencies using independent contractors do not provide the actual services. Instead, the agencies contract with and coordinate service providers. They refer or match providers with clients. So an agency's core business is referring, matching, or coordinating service providers with clients, customers, or consumers. It is **not** their business to actually provide the services.

The ICs must provide a service distinct from your agency's core business. You should not have employees who perform the same job as ICs. This is a red flag that you are using contractors to conduct your regular business; therefore, those contractors should instead be employees.

A note for owner/operators

Do you provide services yourself as well as contract with ICs?

- As stated above, an agency should not have employees and ICs who both provide the same services.
 - If you have an LLC or corporation, you are an employee of that company
 - If you contract out to other IC providers, you are functioning as an agency.
 - If you provide the same services as those ICs, you are running a risk by using ICs instead of making them employees.

A note for owner/operators

- A possible solution is:
 - As an employee (W-2 income), limit your activities to your administrative duties.
 - When you provide services to your clients, do it as an IC contracting with your company (1099 income).
 - Set up a sole proprietorship or other structure with its own EIN and an IC contract (just like every other IC you contract with).
 - This way, only ICs (no employees) will provide services to your clients because you will also be an IC to your company for these duties.
- **Reminder: We are not attorneys or accountants. We recommend discussing this with your advisors.**
- Of course, this does not pertain if you do not use other ICs. If you are a sole proprietor (not an LLC or a corporation), you may want to discuss this with your advisors, just in case.

Equipment, Tools, & Venue

Agencies should not supply the equipment, tools, software, or a place of business for the job. Freelancers are independent businesses and, as such, are expected to provide this for themselves.

Agencies may use administrative tools, such as email, scheduling software, billing software, etc.

Skilled Professionals

Freelancers should only be used when you require skilled professionals with extensive, specialized education or training. These professionals have time and money invested in their field of work, skill sets, continuing education, materials and tools, etc.

Training

Agencies may not pay for or provide any education or training for ICs.

Freelancers are expected to be skilled professionals who come to the job ready to perform. Thus they should know everything necessary for the job and have all the required equipment.

However, orientation to your agency's procedures, such as billing, scheduling, etc., is acceptable.

Control

When using ICs, agencies do not have the right to control the manner and means of accomplishing the work. ICs should be specialists that do not need supervision or management and must be treated as such.

Agencies work with clients and offer jobs to contractors. They cannot tell the IC how to do the work. Beyond the scheduling process, an agency cannot assist or do anything for the contractor concerning the job.

However, the agency may “pass through” information about the job from the client or consumer to the contractor.

Control

Agencies should not review or evaluate IC work performance.

Agencies should refrain from requiring ICs to submit reports, attend meetings, or follow policies and procedures regarding their work.

Know that the ICs are not representatives of your company. This means no uniforms, no business cards, and no ID badges.

However, as they should be professionals, it is OK to expect them to act like professionals and to conform to industry standards (such as Codes of Conduct) and any legal requirements of the profession.

Working Relationship

ICs can and should contract with multiple agencies and/or directly with clients. This may include working with your competitors or directly with your clients. Neither of these can be discouraged or forbidden.

ICs have the right to choose their jobs, including clients, dates, and times. Of course, clients can specify ICs they prefer or do not wish to work with. Agencies cannot dictate these factors.

ICs have the right to set and negotiate their rates.

Records Checklist

The background features a light blue gradient on the left side, transitioning into a series of concentric, semi-circular arcs in various shades of blue on the right. Small, solid blue dots are scattered across these arcs, creating a pattern reminiscent of a fingerprint or a stylized data visualization.

Legitimate Businesses

As with all businesses, agencies need to protect themselves. When working with freelancers, they should keep records of the independent contractors they contract with that demonstrate that each IC is a legitimate, bona fide business.

To this end, agencies should obtain and keep current copies of the following items.

1) Business License

Many cities, towns, or counties require a business license, aka tax registration or tax certificate.

Having this license demonstrates that the IC is functioning properly as a business.

1) Business License

Since 2021, California has required referral agencies to have on file a signed statement from each freelancer attesting that they have any required business licenses for their municipality.

It is suggested that agencies maintain a file of current business licenses for the ICs they contract with. Get a copy of the certificate as well as the signed statement.

2) Written Contract

All independent contracting agreements should be in writing. Ideally, they should be drawn up by an attorney specializing in employment and contracting law for your state (as well as federal).

Contracts should specify items such as pay rates and terms, services to be performed, and other elements specific to the work and relationship.

3) Federal Employer ID Number

A Federal Employer ID Number (EIN or FEIN), aka Tax ID Number (TIN), is the business equivalent of a Social Security Number. It is used by the IRS and state governments to uniquely identify a company for tax purposes, etc.

It is true that businesses organized as sole proprietorships may legally work using the owner's Social Security number. However, legitimate businesses should have an EIN.

3) Federal Employer ID Number

An EIN is an indicator of a separate business. Working under a Social Security number implies working as an individual rather than a business. Agencies are most protected by giving preference to ICs with an EIN over those using their Social Security numbers.

A note about EIN and SS# in California

- California law requires that for some ICs who must receive a 1099 (an individual or sole proprietor paid more than \$599), the agency must also submit a form DE 542.
- This form is used for purposes of child support issues.
- It doesn't matter if the IC is not divorced or does not have children, or lives in another state. It must be submitted for all above-indicated freelancers each calendar year.
- DE 542 requires a social security number.
- Thus, for these ICs, California agencies will require both their EIN and your SS# -- the former for tax purposes, the latter for form DE 542.

4) Formal business structures

Agencies should also give preference to formal business structures such as corporations or Limited Liability Companies (LLCs) because these further indicate that the IC is well aware and has demonstrated that they are a separate business and functioning as such.

If the IC chooses to remain a sole proprietorship, the preference is for them to use a business name and, if necessary, register it as a Fictitious Business Name (FBN), aka “Doing Business As” (DBA).

As with the SSN, a freelancer working under their personal name implies working as an individual rather than as a legitimate business.

4) Formal business structures

The combination of an EIN and a corporation, LLC, or sole proprietor using a business name, along with any applicable business license, poses a solid argument that the IC knows they are operating a business and is operating it legitimately.

(While this is the freelancer's concern, be aware that the requirements for registering a business name as an FBN vary from state to state and city to city.)

Note that business licenses should be in the business name, regardless of the business structure.

5) Paid Advertising

Real businesses advertise. Paid advertising demonstrates investment in the business and an IC's ability to choose their own clients. Websites are a relatively cheap way to accomplish this.

It is highly recommended that agencies request and keep records of website URLs for the ICs they contract with.

6) Other Business Artifacts

Other items that agencies can collect from freelancers:

- URLs from free advertising
 - Company Facebook Page
 - Company LinkedIn Page
- Print Matter
 - Business Card
 - Rate Sheet
 - Advertising Flyer
 - Business Bio/Work History
- Certificates of Insurance

7) Certifications

Having certifications from professional organizations demonstrates that the IC is working in an industry that requires specialized skills.

Agencies should collect current copies of certifications from contractors and consider giving preference to those that are certified.

Contractor Information File

For each IC they contract with, agencies should collect as many previously mentioned items as practical. Building and maintaining a file of the above information for each IC provides a record demonstrating that the freelancers have knowingly and willingly entered into an IC relationship and are properly running legitimate, independent businesses.

While it may be an administrative challenge, your records should be updated periodically to keep current with any changes or renewals, such as business names, licenses, insurance, certifications, etc.

Appendix: Appropriate Language Regarding Freelancers

Employees	Freelancers	Explanation
Employee	Freelancer, independent contractor, contractor, vendor, or IC	Service providers are not employees. They are independent contractors, which means they are independent businesses.
Employer	Agency, client	Agencies do not employ ICs. ICs are vendors; agencies are their clients.
Wage, salary	Agreed-upon rate or fee, negotiated rate or fee	ICs are not paid a wage or salary. They are paid a rate, fee, or amount negotiated with the agency.
Raise, promotion	Rate Renegotiation	ICs do not get raises or promotions (or demotions). Rates are renegotiated for an increase (or decrease).
Hire, employ	Agree to send job offers or assignments, contract with; accept job offers or assignments	Agencies do not hire ICs; they contract with them. Typically, the agreement is to send ICs job or assignment offers they might be interested in and accept.
Quit, resign	Stop contracting with, request to no longer receive job offers, terminate agreement or contract	As they are not employees, ICs do not quit or resign; they choose to stop contracting with the agency. They may request to stop receiving job offers, or they may ignore them and stop accepting any jobs.
Fire, terminate, let go, or lay off	Stop sending job offers, stop contracting with, terminate agreement or contract	As they are not employees, Agencies cannot fire or terminate ICs. An agency can stop contracting with them or perhaps stop sending them job offers.
Payroll/paycheck	Invoice payment, billing payment	Paychecks are for employees. Agencies pay invoices or bills submitted by ICs.
Pay Period	Billing cycle, billing period	ICs are paid from invoices. Invoices are processed in billing cycles, not pay periods.
Resume	Business biography or history	Resumes are for individuals/employees. ICs are businesses.

Employees	Freelancers	Explanation
Working with, working for	Contracting with	“Working with” is ambiguous as to who is in control because it does not specify the working relationship. “Working for” implies control by the agency and an employment relationship.
Assign Jobs, schedule jobs	Agencies offer jobs or assignments; Freelancers accept or reject jobs or assignments	The verb “assign” and the verb “schedule” have connotations of control, i.e., the agency “requiring” the IC to do something. Agencies offer jobs; ICs respond with their choices. Agencies refer or match ICs and jobs. They do not dictate what an IC will or can do.
Schedule (noun)	List of accepted jobs/assignments, schedule report (of accepted jobs)	As per above, “schedule” implies something the agency has demanded of or created for the IC.
Employment or work policies	<i>Not applicable – “pass-through information” only</i>	Agencies cannot have policies dictating how ICs perform their work or how the end result is achieved. They can only pass along such policies or guidelines from the client or consumer. However, agencies may have procedures regarding the tendering and acceptance of job offers, invoicing, etc. – in other words, how the IC and the agency interact. The agency may only have policies covering those types of matters, never about the job itself.
Employee training	<i>Not applicable</i>	Agencies may not educate or train ICs or pay for any training for ICs. They may have policies regarding the type of education, training, or certification they require or prefer.
Performance reviews or testing; supervising, monitoring, or controlling the work.	<i>Not applicable</i>	As agencies may not control how work is performed, they are not allowed to supervise or monitor the IC nor give performance reviews or testing.



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