One HR Practice Could Be Wasting Hundreds of Thousands of Dollars!

Most large corporations have a compliance process in place to screen their extended workforce to determine if the workers are contractors or legitimate micro-businesses. This makes sense -- most "on-demand" or "gig" workers are not self-employed professionals running their own business and directing their own work. The problem lies in the fact that most legitimate "solopreneurs" (e.g., independent consultants) get lumped into this broader category of gig workers and they are paid as temporary employees on a W-2 basis through a third party. This is a very common mistake yet most HR leaders are unaware that this practice has them over-paying to only partially mitigate their company's risk.

1. **Paying a consultant like a temp employee does not fully mitigate the risk of joint employment!** Paying someone through a third party mitigates the client company's tax risk, but not the risk of being sued as a joint employer. (Joint employer liability exists when a worker is paid by one company like a staffing firm but their work is directed by another company. The largest joint employment case was when Microsoft settled its lawsuit in December 2000 for $97 million.)

   The best way to ensure that the client corporation will not be found to be the individual's employer or "joint employer" is *to clearly document the type of relationship that exists between the client corporation and the individual*. In other words, have a written contract between the two parties, not between a staffing agency and the consultant.

   Of course, when a staffing agency pays a consultant on a W-2 tax basis there is a contract but it's with the staffing agency, not the client corporation. The bigger problem with this, however, is that these contracts are usually full of fuzzy language like calling the consultant a "self-employable associate" or a "special employee". Undoubtedly this nebulous language would raise a lot of questions with the National Labor Relations Board or a judge if a co-employment lawsuit were filed.

   > ***Bottom line***: **How a person is paid has nothing to do with who controls or directs the work, or the real relationship between the parties.** In other words, paying a consultant through a staffing agency does very little to mitigate the client corporation's vertical co-employment risk.

The client corporation can still be sued as the joint employer because the relationship between the parties is so unclear. (The consultant is being paid like an employee on a W-2 basis but they are not being called an employee in their contract. So what type of worker are they and who is the real employer?)

2. **Paying a consultant like a temp employee is expensive!** Most staffing agencies charge 15-18% on top of the consultant's billing rate in order to pay the consultant on a W-2 basis through their agency. For example, on a $100,000 contract the client corporation will pay an additional $15,000 to $18,000 for the W-2 service, which by the way, *does not fully mitigate the client corporation's risk of joint employment!*

   A less expensive alternative is to hire the consultant on a professional services contract based on a clear statement of work. Client corporations can do this through their own indirect procurement function or through a professional services company.

   Case Study

   Over a 12-month period a Fortune 500 tech company had PrōKo Consulting handle 20 contracts for independent consultants. **Paying these self-employed professionals on a 1099 basis saved the tech company over $130,000 in administrative fees *while fully mitigating their co-employment risk.***

3. **Paying self-employed consultants on a W-2 basis is bad for the consultant.** Being paid on a W-2 basis really muddles a self-employed professional's tax deductions, costing them thousands of dollars. (We know; PrōKo's founder did her taxes twice one year using TurboTax® to compare W-2 vs 1099 and she saved over $8,000 in tax!)

   It's for this reason that most professional consultants won't do projects if it pays on a W-2 basis. (For more information, see the 70-second video, "Friends Don't Let Friends W-2".) It's common to hear clients complain that they can't hire the consultant they want because the consultant won't work on a W-2 basis. The compliance processes at some companies are so restrictive it makes a 1099 based contract all but impossible so the consultant declines the work. Which brings up another good point: **Insisting on paying consultants on a W-2 limits your access to the truly professional talent!**

It doesn't have to be this way. Client corporations shouldn't be over-paying to partially mitigate their risk! Professional consultants shouldn't be penalized for being self-employed!

There is a better way to hire independent consultants that is a win/win for all parties involved. It's a professional services contract with a clear statement of work.

HR Leaders: Here are three ideas to save your company thousands of dollars while doing a better job of mitigating your risk.

1. Talk with your indirect procurement team. They are contract experts who should be thrilled to help you tackle this potential change because it's a better option for less money.
2. Talk with your compliance company if you have one. Are your hurdles for independent contractors to qualify as a legitimate business too high? (For example, requiring three or more employees; this has nothing to do with being a legitimate business.)
3. Explore other options like establishing a relationship with a professional services partner designed to represent independent professionals. This is definitely a better alternative for fully mitigating your co-employment risk for a lot less money!

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This white paper was written by Liz Steblay, the founder and Managing Officer of PrōKo Consulting, a modern talent model that brings together top-tier independent consultants and client corporations in a way that fully mitigates co-employment risk while protecting the consultant's independent status. As a result clients save considerable money and consultants are more profitable. Prior to creating PrōKo she was a professional independent consultant.

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