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IN THIS ISSUE

Independent Contractors: What You Need to Know

Independent contractor status provides innumerous benefits, including profitability, to both federal and state governments. Since the status eliminates the need for employers to withhold taxes — and provide other employee perks such as workers' and unemployment compensation, 401k, and health programs— governments have found this status to be most beneficial.

Why Use Independent Contractors?

Luckily for them, advances in technology have coincided with the increased need for independent contractors. As more home-based businesses arise, the need for full-time employees has lessened.

As an alternative, home-based business owners have sought the assistance of independent contractors: these are workers that they can use on a more limited basis and to whom they do not have to provide the aforementioned benefits.

Although the independent contractor status is more favorable to both governments and certain employers, the designation is not exactly attractive to those seeking a stable, long-term source of income.

What Challenges Accompany this Status?

In fact, an abundance of companies that originally opt for hiring independent contractors often find themselves ultimately being challenged legally by those they hired. On the other hand, well-known organizations, such as FedEx, previously designated their drivers as independent contractors. These drivers fought to be recognized as employees for quite some time.

As governments seek to hone in on the precise definition of an "independent contractor," the characteristics of individuality are crucial to consider. For example, FedEx workers sought employee status based on the fact that they are required to sport FedEx uniforms, drive trucks with the FedEx logo, and deliver only FedEx packages.

Independent Contractors: What You Need to Know (cont.)

The company, however, argued that the drivers purchase their own vehicles and even have the ability to sell their delivery routes. Therefore, workers seeking more corporate "freedom" are often drawn to independent contractor roles where they are not required to report to a supervisor.

Ultimately, FedEx settled this independent contractor mislabeling case for $228 million in 2015 after a Ninth Circuit ruling. This epic class action settlement paid claims that were made by thousands of FedEx workers. Some of these claims even dated back to 2000. Needless to say, FedEx was not happy to find out that they were misclassifying independent contractors for so many years.

Here are some other helpful differentiators between employees and independent contractors:

Key Characteristics of Employees:

- Typically work under one employer on a full- or part-time basis
- Are often offered benefits, such as paid time off & employer contributions to Social Security, Medicare, healthcare, & 401k programs
- Are usually managed by other employees of the same organization
- Often fulfill one static role at a time, with promotional potential
- Are provided tools to use under the employer's rules & regulations, such as a desktop computer
- Have one boss
- Are often provided at least some level of job-specific training
- File a W2 at tax time
- Typically adhere to a job offer letter & the company's guidelines

Key Characteristics of Independent Contractors:

- Often fulfill a performance-based role & are self-employed, such as salespeople
- Are sometimes hired on merely a short-term basis
- Sometimes fulfill a smaller portion of a larger project, i.e. an electrician outsourced by a general contractor to properly wire a newly constructed building
- Provide & utilize their own tools
- Are not offered extensive training— nor are they managed— by the hirer
- Are entrusted to perform tasks due to their niche and expertise
- May work on behalf of multiple companies at one time
- File a 1099 form at tax time
- Typically adhere to a verbal agreement or written contract

It is interesting to note that in July 2015, the U.S. Department of Labor issued new guidelines that are intended to prevent misclassifications. "A worker who is economically dependent on an employer is suffered or permitted to work by the employer. Thus, applying the economic realities test in view of the expansive definition of "employ" under the Act, most workers are employees under the Fair Labor Standards Act."

The Top 7 Factors That Can Weaken a Company's Value

A company's worth is not only determined by its financial history and revenue. In fact, two companies can be nearly identical in terms of net worth, but additional factors could greatly impact a dramatic cost difference in consideration of acquiring one over the other. A company worth $10 million could strive to make some internal adjustments and ultimately sell for millions more.

Let's take a look at some potentially damaging weaknesses that some companies suffer from:

1. Are Customers Too Concentrated?

An analysis of the company's customer base can help define the amount of risk involved in the company's potential acquisition.

While it may seem impressive on the surface to have just a few major clients, such as the U.S. government or General Motors, everyone knows that buying circumstances and purchasing agents can change. As a result, customer concentration can dramatically reduce the value of a company.

Take a look at an interesting case study of a major office tools manufacturer. With over $20 million in total sales, their biggest client was Staples, which represented over 75% of all deals.

The manufacturer was ultimately faced with a decision to either continue with all of their eggs in the Staples basket, acquire direct buys from another—yet different—company, or sell out to a competitor of their own. They opted for the latter. However, the acquirer was unable to establish the same business relationship with Staples. The office store came to represent just 10% of the newly formed company's customer concentration.

However, there is much less concern in acquiring a company now worth $125 million, with Staples making up just 10% of their buys, versus acquiring the original $20 million company, which nearly completely relied on the office superstore's purchases.

2. Are there Too Few Products?

For every company, there is a product or service and for nearly every product or service, there is a competitor. To reference, yet again, the eggs-in-one-basket concept, there is significant risk in investing the majority of your company's time, money, and focus into just one product.

A famous example of this weakness was when Henry Ford nearly lost his company by believing in society's universal ability to purchase Ford's "Model A" vehicle. In opposition, General Motors' long-time chairman and CEO, Alfred Sloan, opted to create and sell multiple models of cars that appealed to varying income thresholds, seeing much more success.

3. Is the Focus Too Limited?

There is limited ability to grow companies that found comfort selling locally and only within their own domain. Organizations that perform national and global deals have significantly more opportunity to flourish. Further, companies that have a large consumer base on the Internet have a nearly unlimited opportunity to grow.

4. Is the Workforce Too Old?

Unfortunately, today's youth are more likely to advance their education academically, not trade-specifically. As a result, as skilled workers age and leave the workforce, these employees are often not being replaced by equally experienced workers. Over time, this issue contributes to the deterioration of the quality of the organization.

5. Is the Industry in Decline?

Fortunately, some companies are able to adapt to

The Top 7 Factors That Can Weaken a Company's Value (cont.)

advances in society and continue to flourish. For example, Walmart was able to compete with the convenience of shopping for everyday products on websites, such as Amazon, by providing their own online shopping experience with competitive shipping promotions and prices. On the other hand, unfortunately, other organizations are left with no choice but to falter, such as what book stores endured in the wake of digital reading alternatives.

6. Are Costs Rising?

Companies that have faced rising costs in efforts to continuously produce their own commodities are often unable to pass these increases on to consumers. This is the exact situation that the steel industry encountered prior to greater demand from China and a colossal industry merging. In the end, these new factors aided the circumstances, enabling the steel industry to thrive.

7. Is that Company Too Reliant on the CEO?

Many companies depend on the CEO that founded and paved its success path, and rightfully so. For years, companies effectively rely upon this "one-man-band" without preparing a succession plan to sustain the business beyond his or her tenure.

As Kenneth Freeman tried to remind CEOs in "The CEO's Real Legacy" (Harvard Business Review, November 2004), "Succession planning is one of the best ways for you to ensure the long-term health of your company."

The alternate to submitting to a company's weaknesses is to evaluate all of these aspects of the organization and actively work to increase its value. The CEO and his or her Board of Directors would be the foundation for this positive movement. However, the current CEO may struggle to envision the company's existence beyond his or her length of employment.

Freeman summarizes this priority: "Your true legacy as a CEO is what happens to the company after you leave the corner office. Begin early. Look first inside your company for exceptional talent. See that candidates gain experience in all aspects of the business; help them develop the skills they'll need in the top job."

Keeping reality top of mind, he adds, "During good times, most boards simply don't want to talk about CEO succession. During bad times, when the board is ready to fire the CEO, it's too late to talk about a plan for smoothly passing the baton."

With a little motivation and, hopefully, with his or her assistance, a CEO succession plan can be executed as a major step in the right direction towards increasing the company's overall worth.