



## Worker Classification from the Worker's Viewpoint



Dawn Greenberg, CPA  
Tax Principal  
Construction Services Group  
Cowan, Guteski & Co., P.A.

With worker classification issues, we look at the related federal and state statutes to see what tests are enumerated in the law and how we can properly comply. It is also important to contemplate these issues from the worker's point of view to determine what planning opportunities exist. Depending on the worker's financial needs and goals, one classification may be preferred over the other. Once all the relevant issues are analyzed, proper planning may help the employer and worker to achieve the desired result.

### **TAX CONSIDERATIONS**

A worker engaged in a trade or business in which significant travel or other expenses are incurred may prefer to be treated as an independent contractor in order to get the most benefit from those deductions for income tax purposes. While employees can deduct their unreimbursed business expenses as itemized deductions on their tax returns, the amount must exceed two percent of their adjusted gross income in order to provide any tax benefit. Depending on the amount of income earned, the expenses may have to be substantial, and only the amount exceeding the limitation is deducted in computing income tax. The benefit may even be further limited if the taxpayer's income is high enough to cause itemized deductions to phase-out. Treatment as an independent contractor allows the worker to use all substantiated business expenses to directly offset income. Examples of deductible business expenses include office supplies, marketing expenses, uniforms and special clothing required for the trade, the greater of standard auto mileage or actual auto expenses (including depreciation) based on business miles traveled, and an allocation of expenses and depreciation for a portion of the worker's home used in the business. On the other hand, workers without many out-of-pocket expenses may receive a greater benefit from classification as an employee for other reasons unrelated to taxes.

In addition to income tax, the independent contractor is subject to self-employment tax, Social Security and Medicare tax that is paid on wages if the worker is classified as an employee. The independent contractor is charged with both the employee's and employer's portion of these taxes but receives a deduction for half the self-employment tax calculated. Like the income tax, the self-employment tax is based on the independent contractor's net income from the trade or business as opposed to the gross wages on which an employee pays taxes.

For purposes of New Jersey income taxes, the state generally allows the same deductions as the Internal Revenue Service. However, it gives the taxpayer a deduction for 100 percent of any business meals and entertainment expenses. The deduction is limited to 50 percent at the federal level. If significant tools and equipment are purchased for the business, there may be differences in depreciation as well.

**THIS ARTICLE WAS PUBLISHED IN THE  
DECEMBER 2008 ISSUE OF BUILDER/ARCHITECT MAGAZINE**

## **BENEFITS AND OTHER COMPENSATION**

Employee benefits and other financial incentives available to employees may play a large role in determining the desired status. Employers frequently offer a pension plan, 401(k) or other employer-paid benefits, such as group-term life insurance, health insurance, or a stock purchase plan. An independent contractor should consider this and negotiate a fee high enough to justify the forgone compensation. This can be possible, especially if the employer does not need a full-time employee.

## **LEGAL ISSUES**

Many workers that want independent contractor status fail to consider the additional costs associated with the legal liabilities that may arise in connection with their businesses. In most trades in New Jersey, workers of any kind, including unincorporated independent contractors, are required to be covered by worker's compensation insurance even if the contractor has no other employees. In addition, general liability insurance may be necessary to protect the worker in the case of a lawsuit. Premiums for these types of policies can be a significant cost to the worker.

Jurisdictional issues may also come into play. If the employer requires work to be performed in a neighboring state, the worker's ability to file a lawsuit in that state may be hindered if the worker is not properly registered. One advantage of employee status is that these issues generally become a concern for the employer, not the worker. A worker in a high-risk industry may find it beneficial to let the employer absorb these costs.

## **PLANNING**

When we look to the payroll statutes, we see a common theme that is applied by the taxing authorities – control. Those statutes should be carefully analyzed in order to ensure that all necessary conditions for the desired status are in place. For instance, if the employer exercises control over when and how a worker performs a task, the worker has no other source of income than that employer, and the worker has not made a significant financial investment in equipment needed to perform the job, all indications point to employee status. One important thing to remember is that no one factor out-weighs the others in the determination. Given the right circumstances, a worker could perform services for two or three different employers but still be considered an employee of each of those employers if each one exercises overall control. At the same time, a worker can demonstrate that an employer does not exercise control, even if that employer is the only source of the worker's income. These examples are somewhat over-simplified. The law should be carefully studied in any given situation.

## **WHEN EMPLOYER AND WORKER DO NOT AGREE**

The 2001 Microsoft case and the more recent FedEx Ground case have shown us employers and workers often have different interests. In both cases, the employer took the position that the workers in question were independent contractors. In the Microsoft case, both the tax and civil courts ruled that the facts and circumstances proved the workers to be employees, entitling them to back benefits. Although the FedEx cases have not yet been concluded, many do not hold out much hope for the company.

So what can be done to settle the matter without an expensive lawsuit? If there is a disagreement between the employer and worker regarding the worker's status, either party can file a Form SS-8 with the Internal Revenue Service. The form consists of several questions regarding the worker's employment. The IRS will review the form and render a determination of worker status. Since the determination will be predicated on the facts provided, it is important to be very accurate in completing the form. Recently, the IRS has released a new Form 8919 that is only filed by the worker. Form 8919 is used when a worker who is treated by an employer as an independent contractor does not agree with that classification. The



form allows the worker to pay only the employee share of federal payroll taxes, as well as identify the employer who is not withholding.

There are many, often complicated factors that surround the issue of worker classification. As evidenced by the litigation in this area, workers have as much reason for concern as employers. Proper research and planning with the help of a qualified professional can help protect and benefit both.

As one of the leading accounting and consulting firms for the construction industry and a Master Sponsor of the New Jersey Builders Association, Cowan, Guteski & Co., P.A. provides clients with advice and counsel on how federal and state tax laws could impact your business. Our goal is to position your construction company to take advantage of all legitimate strategies to minimize your tax obligation. Contact Dawn Greenberg, CPA, Tax Principal, at 732-349-6880 extension 118 or [dgreenberg@cowanguteski.com](mailto:dgreenberg@cowanguteski.com) to discuss your particular situation.

#### **ABOUT COWAN, GUNTESKI & COMPANY, P.A.**

As a diversified certified public accounting firm, Cowan, Guteski & Co., P.A. is committed to being an active partner in their client's growth by delivering value beyond accounting, innovative solutions and consistent exceptional service. Visit [www.cowanguteski.com](http://www.cowanguteski.com) for more information on the services available to meet the unique needs of the construction industry.

The technical information in this article is necessarily brief. No final conclusion on this topic should be drawn without further review and consultation. Please be advised that, based on current IRS rules and standards, the advice contained herein is not intended to be used, nor can it be used, for the avoidance of any tax penalty assessed by the IRS.

