

# *Mashgichim:* Independent Contractors Or Employees?

**Nathan H. Lichtenstein**  
**Aronberg Goldgehn**  
**330 North Wabash, Suite 1700**  
**Chicago IL 60611**  
**312-755-3148**  
**[nlichtenstein@agdglaw.com](mailto:nlichtenstein@agdglaw.com)**  
**[www.agdglaw.com](http://www.agdglaw.com)**



# Who Cares?

- IRS
  - More difficult to collect income taxes from independent contractors
- HHS
  - More difficult to collect payroll taxes from independent contractors
- Department of Labor
  - Potential abuse of minimum wage and overtime laws
  - Potential abuse of anti-discrimination laws

# Who Cares?

- State Department of Revenue
  - More difficult to collect income taxes from independent contractors
- State Unemployment Agency
  - Employers are not contributing to the UI fund
- State Workers' Compensation Agency
  - Workers are not protected
  - Employers are not contributing to the WC Fund

# Who Makes the Determination?

- IRS
- Department of Labor
- NLRB
- State Agencies

# The 20 Common Law Factors (Rev. Rule 87-41 and DOL)

1. Level of instruction
  - Direct when, where and how the work is done.
2. Amount of training
  - Employees typically receive training
3. Degree of business integration
  - Is there a continuing working relationship?
4. Extent of personal services
  - Does the worker provide services personally?
5. Control of assistants
  - who hires, supervises and pays assistants

# The 20 Common Law Factors (continued)

## 6. Continuity of relationships

- A continuous relationship usually means an employment relationship is present

## 7. Flexibility of Schedules

- Independent contractors generally set their own hours

## 8. Demands for full-time work

- Full time generally suggests an employment relationship

## 9. Need for on-site services

- Work on the company's premises suggests an employment

## 10. Sequence of work

- If required to work in a certain order or sequence

# The 20 Common Law Factors (continued)

## 11. Requirement for reports

- Report his or her progress usually demonstrates an employment relationship

## 12. Method of payment

- Paid hourly, weekly or monthly

## 13. Payment of business or travel expenses

- If travel and business expenses are reimbursed

## 14. Provision of tools and Services

- Provides tools and materials in order to perform their jobs?

## 15. Investment in facilities

- Independent contractors typically invest in and maintain their own work facilities.

# The 20 Common Law Factors (continued)

## 16. Realization of profit or loss

- Employees receive a salary do not have the risk of a loss.

## 17. Work for multiple companies

- Contractors can be working for multiple companies at once.

## 18. Availability to public

- An independent contractor generally makes his or her services available to the general public.

## 19. Control over discharge

- Contractor's termination usually depends on the contract terms.

## 20. Right of termination

- Employees can quit their job at any time without incurring a liability, whereas independent contractors have contract terms.



# IRS Test

- The IRS looks at the degree of control the employer exerts over the worker and the degree of independence exhibited by the worker.
- The IRS considers facts that provide evidence in the following three categories:
  - Behavioral Control
  - Financial Control
  - Type of Relationship

# Behavioral Control

- Control over when and where the work will be done
- Whether or not the employer provides instruction on how the work will be done
- Whether the worker uses the employer's or his/her own tools and equipment
- Whether or not the employer provides training to the worker
- How the worker is evaluated (details or end result)

# Financial Control

- Extent of unreimbursed business expenses
- Extent of worker's investment in equipment and facilities
- Extent to which the worker's services are made available to the relevant market
- Extent to which the worker can realize a profit or loss
- Method of payment

# Type of Relationship

- Whether or not the employer provides the worker with employee-type benefits
  - Insurance
  - Pension plan
  - Vacation, holiday, or sick pay
- Whether or not the worker is provided a copy of the employee handbook
- Whether or not the worker is engaged with the expectation that the relationship will continue indefinitely
- The extent to which the worker's services are a key aspect of the employer's regular business

# United States Supreme Court

In resolving disputes under the Fair Labor Standards Act, the United States Supreme Court [*Rutherford Food Corp. vs. McComb*, 331 U.S.722 (1947)] has said that no single factor is determinative, but depends upon the whole activity.

- The factors the Court has considered significant include:
  - The extent to which the worker's services are an integral part of the employer's business
  - The permanency of the relationship

# The U.S. Supreme Court (continued)

- The amount of the worker's investment in facilities and equipment
- The nature and degree of control by the principal
- The worker's opportunities for profit and loss
- The level of skill require in performing the job and the amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent enterprise

# Other Factors Supporting “Employee” Status

- Worker Receiving Benefits
- Company Equipment
  - (computer, iPhone, e-mail address, etc.)
- Employee Directory
- Business Cards

# Other Factors Supporting “Employee” Status

- Job Descriptions
- Personnel Files
- Performance Evaluations
- Employee Handbooks



# New Jersey Unemployment Standards

- New Jersey uses a regulatory scheme for unemployment contributions called the “ABC Test”:
  - Freedom from employer control; and
  - Service is outside normal course of business or performed outside place of business; and
  - Individual is engaged in independently established trade, occupation or business.

# Test Under California's Division of Labor Standards Enforcement

*S. G. Borello & Sons, Inc. v. Dept. of Industrial Relations*

- Rebuttable presumption worker is an "employee"
- 11 Factors
  - Whether the person performing services is engaged in an occupation or business distinct from that of the principal;
  - Whether or not the work is part of the regular business of the principal or alleged employer;
  - Whether the principal or the worker supplies the instrumentalities, tools, and the place for the person doing the work;
  - The alleged employee's investment in the equipment or materials required by his or her task or his or her employment helpers;
  - Whether the service rendered requires special skill;
  - The kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the principal or by a specialist without supervision;
  - The alleged employee's opportunity for profit or loss depending on his or her managerial skill;
  - The length of time for which the services are to be performed;
  - The degree of permanence of the working relationship;
  - The method of payment, whether by time or by the job; and
  - Whether or not the parties believe they are creating an employer-employee relationship may have some bearing on the question, but is not determinative.

# Painter Bob



# A Straightforward Example – Part 1

- Painter Bob
  - Bob advertises in the local newspaper to get jobs
  - He maintains his own brushes, ladders, and drop cloths, and buys his own paint
  - He is paid by the job
  - When the paint job is complete, Bob no longer works for the customer/employer

**Bob is an independent contractor**

# Painter John



# A Straightforward Example – Part 2

- Painter John
  - John reports to work at the same company every day
  - The company provides John with the paint, brushes, ladders and other materials to do the job
  - The company sets John's working hours
  - John works for the company full time

**John is an employee of the company**

# Painter Paul



# A Little Murky

- Painter Paul
  - Paul reports to work at the same company 3 or 4 days a week. He works only 3-4 hours each evening.
  - Paul advertises in the local newspaper to get additional day jobs.
  - The company provides Paul with the paint, brushes, ladders and other materials to do the job.
  - The company pays Paul by the hour and Paul has some discretion on the days he works.
  - Paul has worked for the company in this capacity for several years.



Rev. Rul. 57-79

vs.

Rev. Rul. 57-80

When is a *schochet* considered an employee or an independent contractor?

Are *schochetim* considered employees of the slaughterhouse and packing plant?

*Aurora Packing Co. vs. NLRB*

904 F.2d 73 (D.C. Cir. 1990)

Is a *Mashgiach* an employee  
of a kosher caterer?

*Altman vs. Sterling Caterers, Inc.*  
879 F.Supp.2d 1375 (S.D. Florida 2012)(FLSA)

# Section 530 Safe Harbor

- Independent contractors will not be reclassified as employees if:
  - a) The company treats individuals with similar job duties as independent contractors
  - b) The company filed all required information returns (Forms 1099); and
  - c) The company had a reasonable basis for treating the worker as an independent contractor

# IRS Voluntary Classification Settlement Program

- **Eligibility**

- Are currently treating the workers as non-employees
- Have satisfied Form 1099 requirements for the workers for the past 3 years
- Have no current dispute with the IRS or the DOL regarding the workers' status
- Have not been previously audited by the IRS or if so, have complied with the results of the previous audit.

# IRS Voluntary Classification Settlement Program

- **Requirements**

- Employer agrees to prospectively treat the workers as employees in the future
- Employer agrees to extend the period of limitations on assessment of employment taxes for 3 years beginning after the date of the agreement

# IRS Voluntary Classification Settlement Program

- **Benefits**

- Employer will pay 10% of employment tax liability that may have been due on compensation paid to workers for the most recent tax year
- No interest or penalties on the liability

# What May Trigger An Inquiry or Audit?

- Worker Files For Unemployment
  - Employer disputes eligibility, claiming worker is an independent contractor
- Review of 1099-MISC filings (IRS data sharing)
- Change in Employee Status/Classification (from W-2 to 1099)
- Worker Complaint



# Avoiding Litigation

## What can companies do?

- Review all written agreements with *mashgichim*;
- Make contracts results-oriented as opposed to setting open-ended terms;
- Provide the contractor with the right to set hours of work and schedules and to determine what tools and materials to use;
- Do not restrict the contractor's ability to work on other projects;
- Provide contractual requirements for:
  - insurance;
  - indemnification; and
  - risk of loss.
- When possible contract with a corporation or company as opposed to an individual;
- Do not compensate the contractor as an employee, *i.e.*, weekly or bi-weekly payments;
- Require the contractor to seek reimbursement for expenses.

# Disclaimer

This presentation is a summary and is not intended as tax or legal advice. You should consult with your tax advisor to obtain specific advice with respect to your fact pattern.

Based on the most recent "best practice" standards for tax advisors issued by the Treasury Department, commonly referred to as Circular 230, we wish to advise you that this presentation has not been prepared to be used, and cannot be used, to provide assurance that penalties which may be assessed by the IRS or other taxing authority (including specifically section 6662 understatement penalties) will not be upheld.

# Questions?

**Nathan H. Lichtenstein**  
**Member, Aronberg Goldgehn**  
**[nlichtenstein@agdglaw.com](mailto:nlichtenstein@agdglaw.com)**