

How You "Treat" Your Music Teachers



Presented by

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Session Objectives:



- “Pros & Cons” between classifying music teachers as **employees vs. independent contractors**
- “Criteria” used by most tax authorities to determine the **employment status** of a worker
- Classification **guidance**

Classified as “Employees”



Pros –

- Control over their work schedule
- Control over their teaching methods
- Control over their teaching rates
- Control over their compensation & benefits offered
- Never have an issue with any tax authority

Cons –

- Significantly “higher” worker costs, including payroll and unemployment taxes, health, liability and workers comp insurance, and retirement benefits (Remember – you can’t discriminate between owners and employees, or between employees, with regard to employment benefits)

Classified as “Independent Contractors”



Pros –

- Complete elimination of any payroll taxes
- Complete elimination of any insurance costs
- Complete elimination of any retirement benefits
- Complete elimination of employment benefits
- Complete elimination of payroll accounting
- Minimized tax reporting (1099-MISC at year-end)

Cons –

- No control over their work schedule
- No control over their teaching methods
- No control over their teaching rates

BEWARE:



Incorrect classification can cause you to be held responsible for...

- All "back" federal & state payroll taxes
- All "back" unemployment taxes
- All "back" employment benefits

BAD...VERY BAD !!

IRS Guidelines



- In 1987, the IRS issues the “20 Factor Test” under Revenue Ruling 87-14
- These rules were strictly (and unfairly) enforced in court cases, as the IRS would focus on the violation of 1 or 2 rules to win its case against an employer
- In 1996, the IRS issued a new set of guidelines which directed agents to focus on the “overall” set of circumstances, rather than one or two factors

The **20 Factor** Test

Factor #1 - Instructions



Employee: Must follow mandatory instructions as to where, when and /or how to perform work

Contractor: Performs work based upon independently established procedures or industry specs

Factor #2 - Training



Employee: Receives and/or is required to receive training

Contractor: Skilled professional requiring no training to adequately perform services

Factor #3 – Integration of Services



Employee: Provides essential services which meld into overall business operation

Contractor: Work performed is not an “integral part” – it is a “unique” service

Factor #4 – Services Rendered Personally



Employee: Required to render services personally

Contractor: Has assistants or employees while retaining the right to hire others to perform the required work

Factor #5 – Hiring, Supervising and Paying Assistants



Employee: Does not supervise or hire others

Contractor: Hires assistants at his/her expense to perform all or part of project

Factor #6 – Regular and Continuous Relationship



Employee: Services are part of a continuing relationship

Contractor: Provides services and contracts for separate and distinct projects, not on continuing basis

Factor #7 – Set Hours of Work



Employee: Required to work set hours

Contractor: Retains right to complete work at any time

Factor #8 – Full Time Required



Employee: Required to devote full-time to a job on a non-project basis

Contractor: Contract specifies what is to be accomplished by what date; free to choose to work for other clients

Factor #9 – Doing Work on Employer's Premises



Employee: Required to work on-site, when alternatives exist

Contractor: Rents or leases location where work is performed

Factor #10 – Order or Sequence Set



Employee: Required to perform task in a set manner, routine or schedule

Contractor: Has full discretion over routine or manner in which to perform services

Factor #11 – Oral or Written Reports



Employee: Required to submit regular oral and/or written work reports where work is evaluated

Contractor: Has few or no obligations to file regular written or oral reports

Factor #12 – Payment by Hour, Week, Month



Employee: A person paid at regular intervals

Contractor: Compensation determined separately by project or based on fixed fee

Factor #13 – Payment of Business / Training Expenses



Employee: Business or training expenses are paid or reimbursed

Contractor: No reimbursement for business or training expenses

Factor #14 – Furnish Tools or Equipment



Employee: Tools and materials are furnished

Contractor: Furnishes own tools and materials

Factor #15 – Significant Investment



Employee: Does not invest in facilities and/or equipment used to perform work

Contractor: Possesses and invests in facilities and equipment to perform services

Factor #16 – Realization of Profit or Loss



Employee: Compensation for services at fixed rate regardless of profitability

Contractor: Shoulders the possibility of incurring a loss and realizing a profit

Factor #17 – Major Source of Income



Employee: Performs services for only one firm at a time, on a non project basis

Contractor: Has numerous concurrent clients and is not financially dependent on any one

Factor #18 – Services Available to General Public



Employee: Services are not offered to general public and points toward control

Contractor: Offers services to public

Factor #19 – Right to Discharge



Employee: Can be discharged at any time with no liquidated damages

Contractor: Cannot be discharged other than for failure to perform contracted service

Factor #20 – Right to Terminate



Employee: May terminate relationship at any time

Contractor: May terminate work relationship only upon completion of contract or breach by other party

Some Advice and Guidance



Structuring the Relationship Between You & Your Teachers



To best assure a favorable outcome in the event of an IRS or labor department scrutiny, employers should:

- Have “written” contracts or arrangements with their music teachers
- Have an attorney review all documents
- If need be, request assistance from the IRS in determining status by filing a Federal Form SS-8

Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding

Name of firm (or person) for whom the worker performed services <i>Clients of Friedman, Kannerberg + Co., P.C.</i>		Worker's name	
Firm's address (include street address, apt. or suite no., city, state, and ZIP code) <i>91 South Main Street West Hartford, CT 06107</i>		Worker's address (include street address, apt. or suite no., city, state, and ZIP code)	
Trade name		Telephone number (include area code) ()	Worker's social security number : : : :
Telephone number (include area code) <i>(860) 521-3790</i>	Firm's employer identification number <i>06:1146038</i>	Worker's employer identification number (if any) :	

If the worker is paid by a firm other than the one listed on this form for these services, enter the name, address, and employer identification number of the payer.

Important Information Needed To Process Your Request

We must have your permission to disclose your name and the information on this form and any attachments to other parties involved with this request. Do we have your permission to disclose this information? Yes No
 If you answered "No" or did not mark a box, we will not process your request and will not issue a determination.

You must answer ALL items OR mark them "Unknown" or "Does not apply." If you need more space, attach another sheet.

- A** This form is being completed by: Firm Worker; for services performed _____ to _____
(beginning date) (ending date)
- B** Explain your reason(s) for filing this form (e.g., you received a bill from the IRS, you believe you received a Form 1099 or Form W-2 erroneously, you are unable to get worker's compensation benefits, you were audited or are being audited by the IRS).
We are a CPA firm that specializes in the music retail industry. In order to better advise our clients with employee vs. independent contractor issues, we are requesting an informational letter based on a typical scenario routinely presented to us by our music retailing clients.
- C** Total number of workers who performed or are performing the same or similar services *Varies (1-50)*
- D** How did the worker obtain the job? Application Bid Employment Agency Other (specify) *Networking*
- E** Attach copies of all supporting documentation (contracts, invoices, memos, Forms W-2, Forms 1099, IRS closing agreements, IRS rulings, etc.). In addition, please inform us of any current or past litigation concerning the worker's status. If no income reporting forms (Form 1099-MISC or W-2) were furnished to the worker, enter the amount of income earned for the year(s) at issue \$ *N/A*
- F** Describe the firm's business.
Music Retail - sale and rental of musical instruments, equipment and print music, as well as music lessons/instruction services.
- G** Describe the work done by the worker and provide the worker's job title.
Music Teacher - offers musical instruction to students, who are also retail customers of the music retail store.

IRS Guidance



In a 1970 Court Case, the IRS challenged the worker status of music teachers at a music conservatory. These teachers taught students in accordance with a **curriculum** provided by the school, as well as provided **private instruction** to students as part of a lesson program administered by the school.

IRS Guidance



- Upon completion of their audit, the IRS issued Revenue Ruling 70-338 which stated *“Teachers instructing regular classes at a music conservatory for regular remuneration are **employees** of the school; however, teachers who instruct pupils in private lessons in return for a percentage of the fees collected by the conservatory are **not employees**. ”*
- Essentially, the determining issue was “who” had **control** over “how” the student was taught



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