


— MEMO #2 —

Church Employees or Independent Contractors?







Dear NBUSA: The only employee we have besides our pastor is a part-time custodian (or secretary). Do you know of any way we could pay them by contract and save the trouble of withholding income taxes and Social Security/Medicare (FICA) taxes?

In one form or another, this question has been asked hundreds of times in financial seminars, emails, and telephone conversations. The question comes in response to the increasing responsibilities of churches and other employers for reporting employee compensation information to the IRS. Fortunately, the answer is fairly straightforward; however, it is seldom the answer the questioner would like to hear.

The information in this Memo is gleaned from the actual experiences of pastors and churches.



Who Are Employees?

There are basically two types of employees defined by the Internal Revenue Code: statutory and common law. Statutory employees have specifically defined jobs that, on the surface, might appear to be self-employed positions were it not for the statutes that define the work as that of an employee. The common law employee is the category which most often affects local churches.

A common law employee is generally anyone who performs services that can be controlled by the employer. That is, the employer has the legal right to control (even if not exercised) the means, methods, and results of the services provided. If the employer/employee relationship is deemed to exist based on the facts in each case, it does not matter what the relationship is called, nor how the payments are measured or paid, nor if the services are performed full-time or part-time. The employer must determine any taxable amounts paid, withhold appropriate taxes for lay employees, make appropriate tax payments, and report them to the IRS. Virtually all pastors, associate ministers, church custodians, church secretaries, paid choir directors, paid nursery workers, etc., are viewed by the IRS as common law employees. Their compensation is reported on Form W-2. See Memo #3: Tax and Reporting Procedures for a discussion of the difference between lay employees and ministerial employees for tax purposes.

Who Are Independent Contractors?

Independent contractors generally work for more than one organization. Examples would be janitorial services, snow removal services, roofing contractors, etc., that are advertised city-wide. No employer/employee relationship exists between the church and persons performing such services. Therefore, no withholding is required. However, the local church may still be required to report to the IRS those payments made to an unincorporated independent contractor.



REMEMBER!

If the employer has the legal right to control the services provided by any worker, the IRS considers that worker to be an employee, and it expects the employer to withhold and report appropriate taxes.



SEE

Memo #3
Tax and Reporting Procedures

The Tax Code provides that payments for services to an unincorporated, independent contractor in excess of \$600 per year must be reported to the IRS on Form 1099-NEC and transmittal Form 1096.

An unincorporated evangelist would be considered an independent contractor. Any payments of \$600 or more in a calendar year, (excluding any housing allowance properly designated in advance by the board, Nazarene 403(b) Retirement Savings Plan contributions, or reimbursed expenses) would require the issuing of forms 1099-NEC and transmittal Form 1096.

What If We Do Not Withhold and Report?

There are criminal and civil penalties for willful failure to comply with the requirements for withholding and reporting. In addition, the amount of certain taxes not withheld at the time of payment from an employee's salary (that must later be paid) becomes the responsibility of the employer. The employee has no obligation to reimburse the employer later for such amount. Further, in some cases, an officer or responsible employee may become personally liable for the taxes and penalties involved.

The IRS has flagged for special review the tax returns of individuals reporting a significant proportion of income on Form 1099-NEC from one source. Such persons are usually reclassified as employees. This results in additional cost—including penalties—for both the individual and the now-determined employer. It is best to make the proper determination prior to such a review by the IRS.



REMEMBER!

If any unincorporated, independent contractor (including an unincorporated evangelist) is paid in excess of \$600 in one year, Forms 1099-NEC and 1096 must be completed.



CAUTION

Serious penalties apply to employers who willfully fail to comply with withholding and reporting requirements.





What If We Are Not Sure Which Employment Relationship Exists?

The local church should carefully consult IRS Publication 15 (Circular E), Employer's Tax Guide, and 15-A, Employer's Supplemental Tax Guide, for examples that might be similar to their situation. Both are available from [irs.gov](https://www.irs.gov) or at [800.829.3676](tel:8008293676). Also, a local legal and/or tax counselor can be consulted for advice. If questions still arise, a special form is available from the IRS to request that they determine if someone has an employment relationship with the local church. In no case should the questions be ignored, nor should there be willful failure to abide by legal requirements for withholding and reporting either wages paid to employees or payments of \$600 or more to unincorporated, independent contractors.

More details and tax information may be found in Memo #3: Tax and Reporting Procedures



SEE

IRS Publication 15 and 15-A for additional information. Both are available from [irs.gov](https://www.irs.gov) or [800.829.3676](tel:8008293676).

**Memo #3
Tax and Reporting
Procedures**

The information contained in this memo series is of a general nature reflecting USA Nazarene Church polity.

It is not offered as specific legal or tax advice. Each person, local church board, and district should evaluate their own unique situation in consultation with their local legal and tax advisors.



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NBUSA
Nazarene Benefits

17001 Prairie Star Pkwy, Lenexa, KS 66220-7900

888.888.4656 | (FAX) 800.334.0634 | nbusa.org | benefits@nazarene.org