**FAQ Series: Employee or Independent Contractor?**

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**UUA Office of Church Staff Finances**

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**Topic: Employee or Independent Contractor?**

**Question: Ministerial compensation is complicated and can be quite confusing. Since ministers are considered self-employed for social security purposes, but employees for income taxes, should ministers receive a 1099 or a W2? Are they properly classified as an independent contractor or an employee? And does it matter whether the minister is settled, interim, consulting, or developmental? Finally, what about other staff?**

**UUA Office of Church Staff Finances Response:** Ministerial compensation is truly complicated, but IRS rulings over time do make it clear. Let’s unpack how clergy compensation should be treated:

1. The IRS expects clergy (whether called, hired, interim, consulting, or developmental) to be treated as employees for income tax purposes and self-employed for social security. This has been standard practice for decades. A W2 should be issued by the congregation. A 1099 should only be issued in rare circumstances such as a minister who leads worship only once a month and has no leadership responsibilities. So the vast majority of ministers are appropriately classified an employee and not an independent contractor.
2. The IRS has a 20-point test to help employers determine whether a compensated individual is an employee or independent contractor. In comparing the duties of most congregational staff, most should be classified as employees including religious educators, music directors, and administrative staff. This is understandably a social justice issue. Classifying an individual as self-employed when they are really an employee is a way for the employer to evade paying the employer share of social security, which is not only illegal, but inconsistent with UU values that promote fairness and economic justice. The IRS has also been going after employers misclassifying individuals. If a wrongly classified individual is audited by the IRS, then the congregation may be held liable for tax evasion.
3. In the rare circumstance where a minister (or another congregational staff member) is rightfully classified as an independent contractor, then they are NOT eligible for any employee benefits – no health insurance, retirement benefits, dental, life, or long-term disability insurance. Neither can the employer pay the employer share of FICA nor forward the employee share. It is against the law to provide such benefits to non-employees. Independent contractors must purchase/secure such benefits on their own – not through the congregation.
4. Because ministers are considered self-employment for social security purposes, they must file their own self-employment taxes. They do so quarterly. The UUA expects that congregations will provide an “in-lieu-of-FICA” payment to their minister(s). This payment is in lieu of the EMPLOYER share of FICA. This amount is currently 7.65 percent of salary and housing. The vast majority of congregations do so. This is a requirement for a congregation to be considered a “fair compensation” congregation.
5. Whether income tax is withheld is optional (although many ministers find it helpful). But s/he will still have to file quarterly taxes sufficient to cover their self-employment tax (SECA) obligation. The congregation must not include the minister’s self-employment tax/social security tax when forwarding payroll (income) taxes.
6. All parish ministers (and some community ministers) are entitled to a housing allowance which should be established prospectively by the Board and not included in the calculation of withholding. The housing allowance is not subject to income taxes, but subject to SECA (15.3 percent). The housing allowance should be paid separately, or itemized out if only one check is issued. The amount of the housing allowance is NOT reported in the taxable compensation box of the minister’s W2. The amount of the housing allowance is the LOWER of actual expenses (mortgage/rent, taxes, utilities, and furnishings) or the fair rental value of the residence including utilities and furnishings.
7. The UUA, together with the UU Ministers Association, provides a model agreement that is quite comprehensive and includes provisions such as sick/disability/parental leave. We recommend using this language to avoid confusion/problems if the match doesn't work for either the congregation, Senior Minister, or the new minister. It’s found on the UUA Transitions website at: <http://www.uua.org/documents/mpl/transitions/ministerial_agreements.pdf>
8. OCSF Staff are able to assist congregational leaders in evaluating how individual staff members may best be classified. We also recommend that congregations purchase a copy of **"*The Church & Clergy Tax Guide,*"** from Church Law and Tax Report, www.churchlawtoday.com, 800/222-1840. This annually updated volume, currently $49.95, answers almost all tax questions relevant to religious bodies and ordained clergy. The organization also publishes several monthly newsletters pertaining to financial management of congregations.

**While we understand the above information to be correct, the staff of the UUA Office of Church Staff Finances are not tax or legal professionals, and we encourage congregations to seek the services of their own tax and/or legal experts in dealing with unusual cases or individual circumstances.**