

Household Help: Employee or Contractor?

Article Highlights:

- Household Employee Definition
- Employee Control Factors
- Self-employed or Employee
- Withholding Requirements
- Reporting Requirements

Frequently taxpayers will hire an individual or firm to provide services at the taxpayer's home. Because the IRS requires employers to withhold taxes for employees and issue them W-2s at the end of the year, the big question is whether or not that individual is a household employee.

Whether a household worker is considered an employee depends a great deal on circumstances and the amount of control the person hiring has over the job and the hired person. Ordinarily, when someone has the last word about telling a worker what needs to be done and how the job should be done, then that worker is an employee. Having a right to discharge the worker and supplying tools and the place to perform a job are primary factors that show control.

Not all those hired to work in a taxpayer's home are considered household employees. For example, an individual may hire a self-employed gardener who handles the yard work for a taxpayer and others in the taxpayer's neighborhood. The gardener supplies all tools and brings in other helpers needed to do the job. Under these circumstances, the gardener isn't an employee and the person hiring him/her isn't responsible for paying employment taxes. The same would apply to the pool guy or to contractors making repairs or improvements on the home.

Contrast the following example to the self-employed gardener described above: The Smith family hired Lynn to clean their home and care for their 3-year old daughter, Lori, while they are at work. Mrs. Smith gave Lynn instructions about the job to be done, explained how the various tasks should be done, and provided the tools and supplies; Mrs. Smith, rather than Lynn, had control over the job. Under these circumstances, Lynn is a household employee, and the Smiths are responsible for withholding and paying certain employment taxes for her and issuing her a W-2 for the year.

If an individual you hire is considered an employee, then you must withhold both Social Security and Medicare taxes from the household employee's cash wages if they equal or exceed the \$2,000 threshold for 2016.

The employer must match from his/her own funds the FICA amounts withheld from the employee's wages. Wages paid to a household employee who is under age 18 at any time during the year are exempt from Social Security and Medicare taxes unless household work is the employee's principal occupation.

Although the value of food, lodging, clothing or other noncash items given to household employees is generally treated as wages, it is not subject to FICA taxes. However, cash given in place of these items is subject to such taxes.

A household employer doesn't have to withhold income taxes on wages paid to a household employee, but if the employee requests such withholding, the employer can agree to it. If income taxes are to be withheld, the employer can have the

employee complete Form W-4 and base the withholding amount upon the federal income tax and FICA withholding tables.

The wage amount subject to income tax withholding includes salary, vacation and holiday pay, bonuses, clothing and other noncash items, meals and lodging. However, meals are not taxable, and therefore they are not subject to income tax withholding if they are furnished for the employer's convenience and on the employer's premises. The same goes for lodging if one additional requirement applies—that the employee lives on the employer's premises. In lieu of withholding the employee's share of FICA taxes from the employee's wages, some employers prefer to pay the employee's share themselves. In that case, the FICA taxes paid on behalf of the employee are treated as additional wages for income tax purposes.

A household employer who pays more than \$1,000 in cash wages to household employees in any calendar quarter of either the current or the prior year is also liable for unemployment tax under the Federal Unemployment Tax Act (FUTA)."

Although this may seem quite complicated, the IRS provides a single form (Schedule H) that generally allows a household employer to report and pay employment taxes on household employees' wages as part of the employer's Form 1040 filing. This includes Social Security, Medicare, and income tax withholdings and FUTA taxes.

If the employer runs a sole proprietorship with employees, the household employees' Social Security and Medicare taxes and income tax withholding may be included as part of the individual's business employee payroll reporting but are not deductible as a business expense.

Although the federal requirements can generally be handled on an individual's 1040 tax return, there may also be state reporting requirements for your state that entail separate filings.

If the individual providing household services is determined to be an independent contractor, there is currently no requirement that the person who hired the contractor file an information return such as Form 1099-MISC. This is so even if the services performed are eligible for a tax deduction or credit (such as for medical services or child care). The 1099-MISC is used only by businesses to report their payments of \$600 or more to independent contractors. Most individuals who hire other individuals to provide services in or around their homes are not doing so as a business owner.

Please call this office if you need assistance with your household employee reporting requirements or need information related to the reporting requirements for your state.