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I. OBLIGATION OF EMPLOYER TO WITHHOLD GROSS INCOME TAX FROM WAGES PAID TO RESIDENT EMPLOYEES

18:35-7.2: Employers maintaining an office or transacting business in New Jersey must *withhold gross income tax* from wages paid to resident employees equal to the tax reasonably estimated to be due on the basis of the wages received by the employee during the calendar year.

II. DEFINITION OF EMPLOYEE

18:35-7.1(a): The term employee means every individual performing services if the relationship between him and the person for whom he performs such services is the legal relationship of employer and employee.

III. DETERMINING WORKER STATUS – KEY FACTORS

18:35-7.1(b): When determining whether an individual is in an employer-employee relationship, relevant factors shall be considered, including the following:

18:35-7.1(b)1: The relationship which the parties believe they have created;

18:35-7.1(b)2: The extent of control exercisable by the person receiving the benefit of the services over the *manner* and *method* of performance. It is not necessary that the employer *actually* direct or control the manner of performance, but it is sufficient if he has the *right* to do so;

18:35-7.1(b)3: Whether the person rendering the service undertook substantial costs to perform the service;

18:35-7.1(b)4: Whether the service required special training or skill, and whether the person receiving the benefit of the services provided such special training;

18:35-7.1(b)5: The duration of the relationship between the parties;

18:35-7.1(b)6: Whether the person rendering the service had a risk of loss;

18:35-7.1(b)7: Whether the person who received the benefit of the services could discharge without cause the person who performed the services;

18:35-7.1(b)8: The method of payment, such as by time or by job;

18:35-7.1(b)9: Whether the person rendering services regularly performs the same services for *other* persons and is not protected to any degree from competition;

18:35-7.1(b)10: Whether the person for whom services are performed furnishes tools, equipment, support staff and a place to work to the individual rendering the services;

18:35-7.1(b)11: Whether the individual rendering the services is eligible for *employer provided benefits* such as pension, bonuses, paid vacation days and sick pay;

18:35-7.1(b)12: Whether the person receiving the benefits of the services rendered carries workmen's compensation insurance on the individual performing the services;

18:35-7.1(b)13: Whether the IRS determines that an individual performing services is an employee; and

18:35-7.1(b)14: Any other information deemed to be relevant by the Division.

IV. 18:35-7.1(c):

No *single* factor in (b) shall necessarily be conclusive in determining whether an individual is an employee or self-employed. The final determination as to whether an individual is either an employee or self-employed shall be based upon the review of the circumstances of the *entire* relationship and the evaluation of any special facts in a particular case.

V. Laws taken from NJ tax cases that have particular significance to the relationship that D & B has formed with its salesmen

a. Extent of Control

i. Rule: A person is an independent contractor if he is subject to the control or direction of another *only* as to the **result to be achieved** but *not* as to the **means to accomplish it**. In other words, if an employer is interested not only in the end result of a salesman's work, but also in the way in which it is done, that is indicative of an employer-employee relationship. *Landwehr v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 66 (citing *Wilson v. Kelleher Motor Freight Lines, Inc.*, 12 N.J. 261 (1953)).

ii. Rationale: The fact that an employer intervenes to some degree is not conclusive of the employment relationship – so does a general building contractor intervene in the work of his subcontractors. He decides how the different parts of the work must be timed, and how they fit together. If he finds it desirable to cut out this or that from the specifications, he does so. Some supervision is inherent in any joint undertaking, and does not make the contributing contractors employees. *Boudrot v. Director, Division of Taxation* (1982, NJTaxCt) 4 NJTax 268 (citing *Radio City Music Hall Corp. v. United States*, 135 F.2d 715, 717-18 (2d Cir. 1943)).

** Basic responsibilities such as maintaining customer satisfaction, preserving the "good name" of D & B, and making a profit are indicative of nothing more than D & B's control over the *result* to be achieved, not the *means* to accomplish it.

iii. Pursuant to *Boudrot*, the test is one of control that *could* be exercised rather than of *actual* exercise. In other words, the issue is whether there exists the *potential* for a great degree of supervision by the employer.

b. Whether the person rendering services regularly performs the same services for *other* persons

i. A person rendering services *exclusively* to another may nevertheless be an independent contractor. *Landwehr v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 66

ii. Under no circumstances should a salesperson be *prohibited* from engaging in any other work, activity, or occupation for financial remuneration during the workweek. *Poppe v. Taxation Division Director* (1983, NJTaxCt) 6 NJTax 108

c. Whether the individual rendering the services is eligible for employer-provided benefits

A self-employed salesman does not enjoy many of the following benefits: (1) *life and health insurance*, (2) *a pension*, (3) *worker's compensation insurance*, (4) *paid vacation*, and (5) *unemployment compensation benefits*. **Indeed, the self-employed salesman provides for his *own* vacation, life and health**

**insurance, and retirement benefits**. *Domenick v. Taxation Div. Director*, 176 N.J. Super. 121 (App. Div. 1980)

d. Force of agreement between parties

18:35-7.1(d): If the relationship of employer and employee exists, the designation or description of the relationship by the parties as anything *other* than that of employer and employee shall be *immaterial*, including designation as a … independent contractor, or similar designations or descriptions.

e. Method of Payment

i. The issuance of a W-2 form and the withholding of taxes are consistent with an employer-employee relationship. *Poppe v. Taxation Division Director* (1983, NJTaxCt) 6 NJTax 108

ii. Independent contractors should not be given a salary. Instead, they should be compensated strictly on a commission basis. Such a commission can be based upon a *formula* calculated on sales and services of the taxpayer. This demonstrates the creation of an independent contractor relationship. *Miller v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 118

f. Risk of Loss

i. Independent contractors should have some "skin in the game." In other words, they should be required to have a cash reserve. See *Miller v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 118 (worker required to have a $ 10,000 cash reserve)

ii. An independent contractor should bear the risk of loss, at least when it comes to the *manner in which inventory is treated*. *Miller v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 118 (worker that received goods on consignment had to account for inventory regularly; to the extent there was any shortfall, worker was held liable)

1. Does D & B consign inventory to its salesmen? By consignment, I mean foregoing any obligation on the part of its Salesforce to put up cash for products that are later sold to D & B customers. To the extent that inventory is consigned to its salesmen, D & B should consider

placing a clause in the contract holding each salesman responsible for any "loss, damage or expense to D & B in connection [therewith]."

2. The following procedure should be enacted. Every few months, all salesmen should account to D & B for their inventory – i.e., what items were sold and paid for and what items remained on hand. To the extent there is any difference between the amount of items sold and paid for, on the one hand, and the salesman's inventory balance, on the other, the salesman should be required to pay for the shortfall. In other words, to the extent there are any deficiencies, the salesman must reimburse D & B.

3. Such a requirement would set the employer-worker relationship apart from an employer-employee relationship. There are three reasons. As a preliminary matter, it is a rare occasion that goods are consigned to employees in the first place. Second, an employer may not withhold or divert any portion of an employee's wages, unless expressly provided by statute. N.J.S.A. 34:11-4.4. And third, absent a showing of negligence, an employee is *not* responsible for an employer's loss.

VI. Significant Cases

a. *Boudrot v. Director, Division of Taxation* (1982, NJTaxCt) 4 NJTax 268

i. **Synopsis of case**: The Taxpayer was an announcer for television and radio commercials. The Court held that he was an independent contractor rather than an employee. Therefore, he was entitled to deduct from gross income the costs and expenses incurred in conducting his business. Although the employer withheld state and federal income taxes, as well as FICA taxes from the taxpayer's earnings, the court did not find this indicative of an employer-employee relationship. Instead, this was the product of collective bargaining between the taxpayer's union and his producers. In addition, the producers receiving the taxpayer's services had only a *limited* right of control over the manner in which he performed his services. Further, the taxpayer could not be discharged once his services were engaged: he was paid even if the commercials were not aired. Finally, the taxpayer's services required special skills and there was a *high risk of loss* incident to the performance of his services.

ii. **Issue**: Is the taxpayer an independent contractor or a common law employee? An independent contractor.

iii. **Facts**:

1. Most of the taxpayer's personal service income was derived from his occupation as an announcer for commercials on radio and television. He is the "voice-over." The balance of his personal service income was derived from infrequent "on-camera" appearances on soap operas and commercials and occasional voice-over narration of training films. The taxpayer was a member of three unions. Compensation paid to the taxpayer for services rendered as a radio and television announcer to parties who *were* signatories to the collective bargaining agreements was reflected on IRS Form W-2 and FICA, and income taxes were withheld. Compensation paid to the taxpayer for services rendered as an announcer or film narrator to parties who were *not* signatories to the collective bargaining agreements was reflected on IRS Form 1099, and no taxes were withheld.

2. The taxpayer had an agent, who received 10% of gross compensation paid to the taxpayer for each job he performed. The job-finding process was initiated when the producer of an advertising agency called the taxpayer's agent to invite the taxpayer to an audition. The taxpayer attended auditions at his own expense. The purpose of the audition was to select one announcer for a particular commercial. If the taxpayer was the winning candidate, his agent called him to tell him when and where to appear to make the commercial.

3. The taxpayer performed his services for a large number of advertising agencies. Compensation was made within 15 days after completion of each commercial by the advertising agency engaging him. He could not be discharged from his engagement. If the producer or casting director was dissatisfied with the taxpayer's performance, he was nevertheless entitled to be paid the agreed-upon compensation.

4. The taxpayer was free to exercise his own artistic discretion as to the manner of performance. The only control over that performance was exercised by the casting director, who indicated the desired mood or tone of the commercial and the time within which it was to be recorded.

5. The advertising agency paid the taxpayer's airfare and hotel accommodations directly. He was reimbursed for other out-of-pocket expenses. At no time did he receive a nonrefundable expense allowance. The taxpayer maintained a personal officer at his own expense.

6. Just as the taxpayer was not protected from competition for commercial announcing assignments, so too was he under no competitive restraints in selecting the advertising agencies or product manufacturers for whom to work. The only restraint in this regard was that he could not make commercials for competing products which were likely to be aired at the same time.

iv. Analysis

1. The relationship which the parties believe they have created

   Reasoning: While at first blush it might appear that the relationship which the parties *intended* to create is indicative of an employer-employee relationship (based on the issuance of IRS Form W-2, the form customarily used when the recipient of gross income is an employee), the evidence refutes that conclusion. Form W-2 was merely the product of collective bargaining between the unions and the advertising agencies, and the treatment of compensation paid under such agreements was designed to facilitate the payment of the union members' tax obligations and to preserve their Social Security coverage.

2. The extent of control exercisable by the person receiving the benefit of the services over the manner and method of performance

   Reasoning: The advertising agency was the beneficiary of the taxpayer's services as a commercial announcer. And it only had a *limited* right of control over the *manner* in which the taxpayer performed those services. That control was limited to the direction of the casting director in the recording studio with respect to mood and tone. On the other hand, the mode and manner of execution were left entirely up to the taxpayer.

3. Whether the person rendering the service undertook substantial costs to perform the service

   Reasoning: The taxpayer incurred substantial expenses incident to the performance of his services. He maintained an office in Manhattan. The taxpayer spent a large part of his time in self-promotion. He entertained producers at lunches and dinners and even sent them cards and gifts at Christmas time. He also disseminated demonstration tapes, made at some expense, in an effort to obtain more assignments in this intensely competitive field.

4. Whether the person rendering the service had a risk of loss

   Reasoning: There was no guarantee that the taxpayer would ever recover the expenditures associated with his promotional efforts. Therefore, the risk of loss was substantial.

5. Whether the service required special training or skill, and whether the person receiving the benefit of the services provided such special training

   Reasoning: Taxpayer's services required special skills. The court found that he was a person of impressive artistic talent and versatility.

6. The duration of the relationship between the parties

   Reasoning: The duration of the relationship between the parties was extremely short. The taxpayer's services were generally completed in one hour.

7. The method of payment, such as by time or by job

   Reasoning: The taxpayer was paid by the job, not be time. Indeed, after he completed a commercial, he was entitled to be paid and he was in fact so paid within fifteen days.

8. Whether the person rendering services regularly performs the same services for other persons and is not protected to any degree from competition

   Reasoning: During the years in issue, the taxpayer performed services for a number of advertising agencies, so he was under no competitive restraints in selecting the advertising agencies for whom to work. The only restraint is that he could not make commercials for competing products which were likely to be aired at the same time. The taxpayer was not insulated from competition for commercial announcing assignments.

9. Whether the person who received the benefit of the services could discharge without cause the worker

   a. Rule: The right to discharge the person rendering the services is indicative of an employment relationship.

   b. Reasoning: Here, the taxpayer could not be discharged once he was hired to do a particular commercial. The advertising agency was obligated to pay him even if the commercial was not aired.

b. *Miller v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 118

   i. **Synopsis of case**: The taxpayer operated a franchise cleaning business. The court held that he was a self-employed independent contractor rather than an employee. Therefore, he was allowed to deduct from his income all expenses of operating the business. The determination that he was self-employed was a factual issue based upon all of the relevant circumstances. Although the taxpayer signed an employment agreement with the company that referred to him as an "employee," that was *not* indicative of his relationship. Supporting the taxpayer's position that he was self-employed are the following facts. He began the cleaning business after answering a newspaper advertisement that sought individuals interested in running their *own* business. He risked substantial capital investment in the operation. Further, he took partial responsibility for his employees' salaries, he incurred substantial unreimbursed travel expenses, and he took personal responsibility for the inventory of cleaning supplies. Therefore, the facts – when taken as a whole – indicated that the taxpayer was self-employed.

ii. Issue: Was the taxpayer engaged in an independent business or was he an employee? The former.

iii. Holding: Because the taxpayer was engaged in operating a business, he was entitled to deduct all costs and expenses incurred in conducting that business.

iv. Facts:

1. The taxpayer entered into an agreement with S-K to operate a franchise cleaning business. S-K was a company that specialized in leasing and servicing cleaning equipment to various businesses, primarily gas stations. The equipment was used to wash, clean, and remove grease from tools and machines. S-K also sold products, such as hand soap and garage floor soap.

2. S-K supplied the taxpayer with a car and leased a warehouse building from which the taxpayer worked. S-K provided the taxpayer with an inventory of its sale products. S-K also provided the taxpayer with an inventory of its cleaning products that were to be used in servicing the equipment that was leased to its customers.

3. The taxpayer was required to have a cash reserve of $ 10,000, which he met. He was also required to advance all operating expenses for the first month before receiving any commissions.

4. S-K leased four trucks and placed them under the control of the taxpayer. The taxpayer was required to pay all costs associated with operating and maintaining these trucks, including monthly rentals owed to the leasing company, costs of normal repairs, operation and maintenance, licenses, fuel, oil, registration fees, and cost of repairs due to collision damage. Upon return of the trucks, any cost and expense incurred by S-K to make repairs or for general upkeep would be deducted from any balance due the taxpayer.

5. As far as inventory goes, the taxpayer did not have to put up any cash for these items. Instead, he merely signed a receipt for them. Every few months, he had to account to S-K for the inventory – that is, what items were sold and paid for and what items remained on hand. If there was any difference between the amount of items sold and paid for and

his inventory balance, the taxpayer was held accountable and was required to pay for them.

6. The taxpayer had sole responsibility for hiring salesmen-drivers. Further, it was his responsibility to train and supervise these salesmen. He soon hired three. The main job of these salesmen was to service equipment and to supply cleaning chemicals to customers. The taxpayer divided his area into territories, which he assigned to different salesmen.

7. The taxpayer opened up a bank account, which was in the name of S-K. All deposits from customers were credited to that account. Upon making a deposit into the account, the bank would automatically transfer the money from that account to an S-K account.

8. By the terms of the written agreement, S-K could not terminate its relationship with the taxpayer, except for proper cause. It provided that he must devote at least 40 hours a week to the business.

9. Regarding compensation, the taxpayer was not paid an hourly rate. Instead, he received compensation strictly on a commission basis. That compensation was based upon a formula calculated on sales and services by him and the driver-salesmen. Although the taxpayer was not entitled to a salary, it was agreed that he would receive $ 300 every two weeks *charged as a draw against his potential earnings*.

10. S-K made all of the usual salary deductions for the taxpayer that it did for its own employees and filed all of the necessary employer returns, including social security, unemployment, and income tax withholdings. The taxpayer carried no workers' compensation insurance for either himself or his employees.

11. Regarding the salesman's salary, the taxpayer was responsible for 50% of their base salary, which was paid from his gross commissions. S-K contributed a total of only 50% or $ 150 of the salary, whichever sum was less.

12. S-K paid the salesmen directly. In doing so, it made all of the usual salary deductions and filed all of the necessary employer returns.

13. The taxpayer had to keep daily records of the names and addresses of all customers serviced, the services performed, and what products, if any, were sold. This information had to be forwarded – daily – to the main office.

14. As part of the agreement, the taxpayer had to operate "within the limits of the established corporate policies and procedures."

15. Over the course of the relationship, the taxpayer hired additional salesmen and leased more vans. In addition, he borrowed $ 25,000 for various costs and expenses incurred in this operation. When he terminated his relationship, he was personally indebted to a finance company for $ 15,000. Moreover, S-K claimed that the taxpayer was indebted to it for $ 11,000 in inventory shortages.

v. Factors that the court found were illustrative of an **employer-employee** relationship

1. The written agreement was entitled, "Employment Agreement" and it named the taxpayer as "employee." It referred to him throughout as "employee." S-K designated its payments as commissions and withheld state and federal income taxes together with unemployment and disability deductions. S-K supplied the taxpayer with a W-2 form.

2. The taxpayer had to operate "within the limits of established corporate policies and procedures."

3. The taxpayer was required to devote no fewer than 40 hours a week to this job.

4. The contract provided a formula intended as *reimbursement* to the taxpayer for (1) truck lease payments and (2) maintenance and operation expenses incurred.

5. The taxpayer used S-K trucks and materials exclusively and the bank account was in the sole name and control of S-K.

6. The taxpayer could be discharged *only* for good cause.

vi. Factors that the court found were illustrative of an **independent contractor** relationship

1. The taxpayer believed that he had been offered an opportunity to engage in a business. As such, he had to advance a $ 10,000 cash reserve.

2. The taxpayer had the authority to hire, discipline, and fire salesmen. He was required to train them as well as to schedule, assign, and supervise their duties.

3. The taxpayer contributed a minimum of 50% of the salesman's salaries and supplied them with delivery trucks. The trucks were leased and the cost – i.e., for operation, maintenance, and repair – were charged to him.

4. The taxpayer received S-K's products by consignment and he was responsible for all shortages.

5. The taxpayer did not receive a minimum salary or a paid vacation.

vii. Analysis

1. The relationship which the parties believe they have created

Reasoning: The taxpayer believed that he was operating a business. It is inconceivable that he would have secured a $ 10,000 loan for an initial reserve; rented trucks and paid for their operating costs; paid substantial portions of the salaries of salesmen that he personally hired; and invested upwards of $ 25,000 of his own money into this venture without such a belief. A prospective employee would never be expected to meet these financial prerequisites.

The fact that the taxpayer deposited receipts into S-K's bank account does not change this conclusion. Since S-K forwarded its materials on consignment to the taxpayer *without* requiring him to advance any money, this arrangement was nothing more than a way for S-K to protect its investment.

2. The method of payment, such as by time or by job

    a. Compensation for taxpayer: The taxpayer was not entitled to draw a salary. Instead, he received an amount equal to "gross branch commissions" less "sales representative compensation" based upon a *formula* calculated on sales and services by him and the driver-salesmen. This demonstrates the creation of an independent business.

    b. Compensation for driver-salesmen: It is contrary to any notion of an employer-employee relationship for an employee to be responsible for any part, let alone more than 50%, of a co-employee's salary. Here, the taxpayer contributed 50% of the base salary of six drivers who were paid $200/week and $ 250 of a $ 400 base weekly salary paid to four drivers. That amounted to a total weekly contribution of $ 1,000 toward a $ 1,850 payroll. That demonstrates the creation of an independent business.

3. Whether the person rendering the service undertook substantial costs to perform the service

    Reasoning: This militates in favor of an independent business. The taxpayer had to travel, on six occasions, at his own expense from NJ to Illinois to pick up trucks for his co-employees. He then had to drive them back to NJ, also at his own expense, and pay for their registration and licensing. In addition, the taxpayer paid for the cost of collision damage. This liability was not predicated upon the taxpayer's own negligence. Indeed, it was his responsibility regardless of whether it was caused by the negligence of the driver or a third party.

4. Whether the person rendering the service had a risk of loss

    a. Court's decision: The taxpayer bore the risk of loss, at least when it came to the *manner in which inventory was treated*.

    b. Reasoning: S-K consigned certain products to the taxpayer, holding him responsible for any "loss, damage or expense of the company in connection [therewith]," regardless of how it was

caused. Under the terms of the agreement, the parties agreed that S-K had the *unconditional* right to ***reduce*** **any payment otherwise due the taxpayer by an amount sufficient to reimburse S-K for any shortage**. Every three months, the taxpayer was required to take an inventory. And to the extent there were any deficiencies, the taxpayer had to reimburse S-K.

c. Such a requirement is *not* characteristic of an employer-employee relationship. For three reasons. As a preliminary matter, it is a rare occasion that goods are even consigned to employees in the first place. Second, an employer may not withhold or divert any portion of an employee's wages, unless expressly provided by statute. N.J.S.A. 34:11-4.4. And third, absent a showing of negligence, an employee is *not* responsible for an employer's loss.

5. The extent of control exercisable by the person receiving the benefit of the services over the manner and method of performance

   Reasoning: S-K exercised no control whatsoever over the taxpayer's day-to-day operations. While the contract expressly delegates certain duties to the taxpayer, the fact remains that such provisions are merely guidelines. The taxpayer had broad discretion in *implementing* these guidelines. His basic responsibilities were to maintain customer satisfaction, preserve the "good name" of S-K, and make a profit. These were general guidelines which the taxpayer was required to implement by his own chosen methods.

c. *Landwehr v. Director, Division of Taxation* (1983, NJTaxCt) 6 NJTax 66

   i. **Synopsis of case**: The taxpayer provided services for a manufacturing company. The court held that he was an independent contractor and not an employee. Therefore, he could use his net business income for purposes of determining his state gross income tax. Because of his freedom to conduct his business according to his own schedule and in his own manner without geographical restrictions and because he received very limited benefits from the manufacturing company (other than his contractual minimum plus commissions), the taxpayer was classified as an independent contractor.

ii. **Facts**: Everlasting was to pay the taxpayer $ 850 per week for a one-year term. During that term, the taxpayer was prohibited from engaging in any other business. The agreement between the parties did not use the words employee, employer, or independent contractor. Instead, it referred to the taxpayer as "Landwehr" and to Everlasting Products as "Everlasting." Also, the agreement acknowledged that Landwehr had "certain expertise in the business as conducted by" Everlasting, that he would "undertake to assist" Everlasting and that he had "the right … to engage himself with 'Everlasting' in the conduct of business." The agreement provided that "if desired" by the taxpayer, Everlasting would deduct from his payments withholding taxes, social security taxes, "employment tax and such other taxes as may be payable." Everlasting did deduct certain taxes from the payments made to the taxpayer, but only on his written request.

iii. Analysis:

1. The extent of control exercisable by the person receiving the benefit of the services over the *manner* and *method* of performance

    a. Rule: A person is an independent contractor if he is subject to the control or direction of another *only* as to the **result to be achieved** but *not* as to the **means to accomplish it**. *Wilson v. Kelleher Motor Freight Lines, Inc.*, 12 N.J. 261 (1953).

    b. Reasoning: Everlasting had only limited control over the *manner* in which the taxpayer performed his services. That control was Everlasting's right to call upon him for his assistance with its dyeing processes, based on his experience as a former manufacturer. On one occasion, for approximately one week, he so assisted Everlasting.

    c. In selling Everlasting's products, the taxpayer had no territory assigned to him. He was free to go "clear across" the country.

    d. The taxpayer was not obligated to report to Everlasting on any specified schedule.

    e. The taxpayer never attended any sales meetings. In fact, he never even had to set foot into the office.

f. The taxpayer arranged his own work schedule and was not bound to work any schedule prepared by Everlasting; he even fixed his own vacation schedule.

g. Although the agreement allowed Everlasting to give the taxpayer instructions and directions, the fact remains that during the period that the taxpayer worked for Everlasting, Everlasting never issued any directions to him "as to what to do or how to go about his job and duties." This lends credibility to the taxpayer's understanding that Everlasting would *not* exercise control over him in the performance of his duties.

h. The taxpayer also retained control over the sales methods. For example, he was responsible for soliciting customers over the phone and calling on customers. In rendering his services, the taxpayer took samples which Everlasting gave him to wholesale florists and display houses. He then took orders and sent those orders to Everlasting. The orders were filled and shipped directly to the customers. He also opened new accounts for Everlasting.

2. Whether the person rendering services regularly performs the same services for other persons and is not protected to any degree from competition

   Reasoning: While the taxpayer worked for no company other than Everlasting, the fact remains that a person rendering services exclusively to another may nevertheless be an independent contractor.

3. Whether the person rendering the service undertook substantial costs to perform the service

   a. Reasoning: According to the agreement, the taxpayer was "responsible for all of his own expenses" and he did, in fact, pay all of his expenses. Although "fairly substantial," Everlasting never reimbursed the taxpayer for any of his selling expenses. They included (1) automobile, (2) telephone, (3) telephone answering service, (4) airfare, (5) hotel, (6) car rental expenses,

and (7) expenses incurred in the use of part of his home for business purposes.

b. The taxpayer also paid for his own stationary with a letterhead which read, "Landwehr Enterprises." Employees do not normally have their own stationary.

c. In one of the tax years in question, the taxpayer spent 42% of his gross income on services rendered to Everlasting.

4. Whether the person for whom services are performed furnishes … a place to work to the individual rendering the services

   Reasoning: The taxpayer did not have an office at Everlasting's place of business. Instead, he maintained an office at home with a business phone and telephone answering service. All of his files were stored at his home office.

5. Whether the person rendering the service had a risk of loss

   Reasoning: The agreement between Everlasting and the taxpayer provided for a minimum sales production with monthly review of the taxpayer's performance. In the event that the minimum sales required were not met, Everlasting had the right to terminate the taxpayer under the terms of the agreement and without further notice. This term allowing for discharge by Everlasting created a substantial risk of loss to the taxpayer who might spend considerable sums for airfare, car rentals, and hotel accommodations and still be discharged.

d. *Poppe v. Taxation Division Director* (1983, NJTaxCt) 6 NJTax 108

   i. **Synopsis of case**: The taxpayer was a licensed sales representative who worked for a major insurance company. The court held that he was an employee and not a self-employed independent contractor. Therefore, he could not deduct the expenses of doing business from his income. Whether the taxpayer was an employee or an independent contractor was a factual question based on all relevant factors. Significantly, the representative and his company *intended* to create an employer-employee relationship by virtue of the issuance of W-2 forms to the representative, the withholding of his taxes, and the

considerable benefits that were extended to him, including vacation pay. Further, the insurance company required the representative to conduct business consistent with rules and regulations that *prohibited employment with other companies*, and otherwise controlled the agent's activities in much the same way that an employer would control an employee. Although the taxpayer undertook substantial costs to maintain his business and was paid by commission, both typical of an independent contractor, the relationship – when viewed as a whole – was more analogous to an employer-employee relationship.

ii. Issue: Was the taxpayer an independent contractor or an employee? An employee.

iii. Holding: The taxpayer was an employee. Therefore, he was not entitled to deduct from his gross income the expenses incurred in his sales activities.

iv. Facts:

1. Poppe was a sales representative for Metropolitan Life Insurance. He was authorized to sell life insurance, health insurance, and annuities. As a sales representative, he was not limited to any particular geographical sales territory. Instead, he could solicit and sell insurance and annuities anywhere in the state of NJ on behalf of Metropolitan.

2. Metropolitan provided Poppe with his own office and a secretary. Metropolitan imposed no sales quotas. Poppe was not required to submit any reports regarding his activities, other than a weekly report on policies sold.

3. Poppe was compensated on a commission basis. Metropolitan withheld federal and state income and social security taxes from his compensation.

4. Poppe was never reimbursed for any expenses incurred in servicing existing business or in soliciting new business. Metropolitan provided Poppe with various benefits, including a health care package, disability benefits, retirement benefits, and a savings and investment plan.

5. Under the terms of the employment manual, Poppe was subject to the general supervision and direction of a district sales manager. In

performing the services of a sales representative, Poppe was obligated to follow Metropolitan's rules and regulations. He was required to maintain books, records, and accounts in a manner prescribed by Metropolitan.

6. Poppe was prohibited from engaging in any other work, activity, or occupation for financial remuneration during the workweek. He was also forbidden to solicit insurance for any other company.

7. Poppe was entitled to vacations with compensation. He also attended training courses offered by Metropolitan and was reimbursed for attending certain company-approved courses.

8. Poppe worked from Metropolitan's office at least once per week. Finally, Poppe could be terminated by Metropolitan without advance notice for breach of any of the conditions of his appointment, and at any time with two weeks' notice. Similarly, Poppe could terminate his association with Metropolitan at any time on not less than two weeks' notice.

v. Analysis:

1. The relationship which the parties believe they have created (the court considered this factor to be one of the most persuasive)

    a. Reasoning: Regardless of Poppe's contention that he never considered himself an employee, Poppe and Metropolitan intended to create an employer-employee relationship. As a preliminary matter, Metropolitan issued Poppe a IRS W-2 form, and withheld state and federal income taxes. While these facts are not conclusive evidence of an employer-employee relationship, the issuance of a W-2 form and the withholding of taxes is *consistent* with such a relationship.

    b. Metropolitan provided Poppe with several benefit plans. Poppe argued that the only reason he received benefits was because the commission paid to him was substantially less than that paid to an insurance broker. However, there was no evidence in the record to support this.

2. The extent of *control* exercisable by the person receiving the benefit of the services over the manner and method of performance (the court considered this factor to be one of the most persuasive)

    a. Holding: Regardless of Metropolitan's *actual* control over Poppe's activities, there existed the *potential* for a great degree of supervision by Metropolitan.

    b. Reasoning: On the one hand, Poppe did *not* have to report his sales activities or account for his time to Metropolitan. In addition, he had no sales quota to meet, he was not confined to any particular sales territory, and he did not follow a prescribed sales presentation.

    c. On the other hand, Poppe was subject to the general supervision of the district sales manager; he was forbidden to engage in any other activity for financial remuneration; he could not solicit insurance for any other company except as specified by Metropolitan; he was required to spend some time in his office; and he had to maintain books, records, and accounts in a manner prescribed by Metropolitan. Most importantly, Poppe was required to perform his services in accordance with Metropolitan's rules and regulations.

    d. While Metropolitan may not have exercised a substantial degree of *actual* control over the way in which the work was done, that is not the test. Pursuant to *Boudrot*, the test is one of control that *could* be exercised rather than of *actual* exercise. Here, Metropolitan retained the *ability* to exercise a considerable amount of control over Poppe's activities.

3. The duration of the relationship between the parties

    Reasoning: Poppe worked for Metropolitan for seven years. That is indicative of an employer-employee relationship.

4. Whether the person who received the benefit of the services could discharge without cause the person who performed the services

Reasoning: Metropolitan could discharge Poppe without cause with only two weeks' notice.

5. Whether the person for whom services are performed furnishes …equipment, support staff and a place to work to the individual rendering the services

   Reasoning: Metropolitan provided Poppe with his own office, a secretary, and a phone. In addition, it provided certain business supplies, including letterhead stationery and business cards.

6. Whether the person rendering services regularly performs the same services for other persons …

   Reasoning: Poppe was prohibited from engaging in any other work, activity, or occupation for financial remuneration during the workweek. In addition, he was forbidden to solicit insurance for any other company, except as specified by Metropolitan.

7. Whether the service required special training or skill, and whether the person receiving the benefit of the services provided such special training

   Reasoning: Whatever special training or skill Poppe possessed, one thing is clear. It was supplied by Metropolitan, either in the form of his initial training or as reimbursement for approved courses.

8. Whether the person rendering the service had a risk of loss

   Reasoning: Poppe undertook substantial costs to perform his service. Indeed, he spent more than $ 16,000 during the '78 tax year. If Poppe had been less successful in his sales efforts, his expenses might well have exceeded his commission income, thus exposing him to the risk of loss.

9. Whether the individual rendering the services is eligible for employer provided benefits such as pension, bonuses, paid vacation days and sick pay

Reasoning: Metropolitan provided Poppe with various benefits, including a health care package, disability benefits, retirement benefits, and a savings and investment plan. He was also allowed to take paid vacations. Vacation pay is indicative of an employer-employee relationship.

e. *Domenick v. Taxation Div. Director*, 176 N.J. Super. 121 (App. Div. 1980)

**Synopsis of case**: The Appellate Division held that the taxpayer was an employee, and not an independent contractor. Therefore, he was not entitled to deduct from his gross income costs and expenses incurred in the course of his employment. By agreement, the taxpayer was required to work full time and attend biweekly sales meetings. He was restricted as to the customers he could call upon, although he was protected from competition by his co-employees. He could also be discharged if his sales fell below a specified minimum. More importantly, he was entitled to a monthly expense allowance. Finally, he had the benefit and protection for himself and his family of (1) *life and health insurance*, (2) *a pension program*, (3) *worker's compensation insurance*, and (4) *unemployment compensation benefits*. As the Appellate Division pointed out, a self-employed salesman does not enjoy many of these benefits. **Indeed, the self-employed salesman provides for his own vacation, life and health insurance, and retirement benefits**. Nor is such a worker protected from competition from other salesmen. Instead, he is generally free to conduct his business as he sees fit without the restrictions and limitations imposed on employee salesmen.