

Cynthia Marcotte **S**tamer, P.C. OLUTIONS LAWYER™

Primary Office
16633 Dallas Parkway, Suite 600
Addison, Texas 75001
Mobile Telephone: (469) 767.8872

Helping Management Manage

Plano/Mail Room
3948 Legacy Drive
Suite 106, Box 397
Plano, Texas 75023

September 22, 2011

New IRS Voluntary Worker Classification Settlement Program Signals Growing Worker Misclassification Audit & Enforcement Emphasis

Businesses Urged To Strengthen Their Worker Classification Defenses

The September 22, 2011 launch by the Internal Revenue Service of a new Voluntary Worker Classification Settlement Program (“Settlement Program”) is the latest warning to businesses using independent contractors, leased employees or other non-employee workers of the need to review critically within the scope of attorney-client privilege the defensibility of their existing classification and treatment of those workers as non-employees in light of the in light of stepped up scrutiny and enforcement emphasis by the IRS and other federal and state regulators as well as workers and others in private litigation.

If this review raises concerns about the defensibility of the business’ classification of existing workers or those employed within relevant statute of limitations periods for income, employment or other Federal tax purposes, the business should consult with qualified counsel within the scope of attorney-client privilege about the advisability of using the Settlement Program to resolve these tax related risks and options for coordinating these activities with efforts by the business to manage worker classification related exposures under other relevant laws and regulations.

To guard against these and other growing risks of worker classification, employers should review within the scope of attorney-client privilege the defensibility of their existing worker classification, employee benefit, fringe benefit, employment, wage and hour, and other workforce policies and consult with qualified legal counsel about the advisability to adjust these practices to mitigate exposures to potential IRS, Labor Department or other penalties associated with worker misclassification.

New Settlement Program Offers Opportunity To Resolve Payroll Tax Risks Of Worker Misclassification

The new Settlement Program established under [Announcement 2011-64](#) reflects the widespread emphasis by the IRS and other federal and state regulators on uncovering and redressing misclassification of workers as non-employees by businesses for purposes of tax and other laws. IRS scrutiny of worker classification practices by businesses has risen significantly over the past decade. The IRS’ launch of the Settlement Program follows its announcement in September, 2010 of plans to conduct approximately 6,000 payroll tax audits over a three year period focusing on the appropriateness of employer worker classification and other payroll tax practices. The announcement of the new Settlement Program signals that the IRS perceives that worker misclassification by business in violation of Federal tax laws is sufficiently widespread and pervasive to merit both efforts to incentive voluntary correction through participation in the

Settlement Program, as well as stiff enforcement against businesses that fail to self-correct worker classification compliance concerns.

The new Settlement Program is designed to increase tax compliance and reduce burden for employers by providing greater certainty for employers, workers and the government. Under the program, eligible employers can obtain substantial relief from federal payroll taxes they may have owed for the past, if they may a “minimal payment” to settle past payroll tax liability and prospectively appropriately treat workers as employees.

Available to a broad range of businesses, tax-exempt organizations and government entities that currently erroneously treat their workers or a class or group of workers as nonemployees or independent contractors, the Settlement Program offers eligible employers concerned about potential worker misclassification exposures that might arise from a payroll tax audit the opportunity to come into compliance by making the required filing, adjusting their practices and paying the required settlement fee effectively equaling just over one percent of the wages paid to the reclassified workers for the past year. Businesses wishing to use the Settlement Program to resolve pre-existing payroll taxes must apply for Settlement Program admission by filing [Form 8952](#), Application for Voluntary Classification Settlement Program at least 60 days before they want to begin treating the workers as employees. If this settlement fee is paid and the other requirements of the Settlement Program are met, the Settlement Program specifies that employers accepted into the program will not be assessed interest or penalties and not be audited on payroll taxes related to these workers for prior years.

Businesses Must Manage Other Worker Classification Risks When Considering Use Of Settlement Program

As welcome as the opportunity to resolve potential payroll tax exposures through participation in the Settlement Program, businesses considering using the Program need to understand and prepared to address various challenges. Because worker misclassification tends to impact on a broad range of legal obligations and risks, businesses evaluating or planning to use the Settlement Program are act quickly, but carefully, to evaluate and determine whether and how to use the Settlement Program and to identify and take appropriate steps to address both the tax-related liabilities targeted for resolution under the Settlement Program, as well as misclassification exposures likely to arise with respect to workers to be reclassified in connection with the use of the Settlement Program.

For instance, businesses electing to use the Settlement Program need to understand the implications of that participation on the Statute of Limitations on their payroll tax liabilities. For instance, certain employers may not be eligible to participate. For the first three years of participation in the program, the Settlement Program specifies that participating employers will be subject to a special six-year statute of limitations, rather than the usual three years that generally applies to payroll taxes.

Also, not all businesses will qualify to participate in the Settlement Program. To be eligible, the business at the time it applies for admission to the Settlement Program must:

- ✓ Consistently have treated the workers in the past as nonemployees,
- ✓ Have filed all required Forms 1099 for the workers for the previous three years,
- ✓ Not currently be under audit by the IRS, the Department of Labor or a state agency concerning the classification of these workers

Furthermore, businesses also may face challenges determining the specific workers to reclassify in connection with the use of the Settlement Program. Subject to certain special rules, the determination of whether a worker is properly classified by an employer as an employee for most purposes under the Internal Revenue Code's income tax withholding and reporting, payroll tax and most other purposes typically depends upon a determination of whether the facts and circumstances associated with the performance of services by the worker meet the Internal Revenue Code's definition of a common law employee. When an analysis of the evidence reflects a high degree of certainty that the classification of a worker as a non-employee was not defensible under existing tax authorities, the decision to use the Settlement Program to redress the payroll tax exposure likely will carry great attraction. Where room for debate exists, however, many businesses may find it harder to decide whether correction is needed and if so, whether to use the Settlement Program. When making these assessments, businesses are cautioned to carefully take into account the burdens of proof typically allocated by the Internal Revenue Code and other laws to businesses electing to treat a worker as a non-employee.

When conducting this evaluation and deciding whether to use the Settlement Program, businesses also need to keep the wider implications of the analysis and their decisions regarding how to handle a potential aggressive or misclassification as a worker as a non-employee. A determination of potential aggressive or misclassification for purposes of the Internal Revenue Code's payroll tax rules generally will necessitate the need to evaluate potential exposures that may arise from the worker misclassification under other federal and state laws.

Typically, in addition to treating a worker as a non-employee for tax purposes, a business also will treat the worker as a non-employee for immigration law eligibility to work, wage and hour, employment discrimination, employee benefits, fringe benefits, worker's compensation, workplace safety, tort liability and insurance and other purposes. Consequently, a determination that reclassification is advisable for tax purposes generally will prompt the need to consider how to address the worker reclassification and attendant risk for purposes of other legal risks and requirements, as well as those covered by the Settlement Program. Businesses will need to consider how the voluntary reclassification of workers and settlement under the Settlement Program may impact their exposures and obligations under other laws. As the Settlement Program does not provide relief from the exposures arising from misclassification under other laws, businesses should be prepared to evaluate the advisability of reclassification of the worker for purposes of these other laws, the potential exposures attendant to misclassification of workers under those laws, and risks, challenges and opportunities for mitigating these exposures.

Businesses Cautioned To Conduct Evaluations & Discussions In Attorney-Client Privilege Due To Complexity & Significance of Potential Exposures

Conducting and discussing the Settlement Program and other related concerns within the scope of attorney-client privilege is particularly important because of the potentially significant civil and even criminal liability exposures that may arise from misclassification of workers for purposes of the various relevant laws. Because of the broad reaching and potentially significant non-tax exposure inherent in these discussions, business leaders are cautioned that the evidentiary privileges that often provides protection against disclosure of certain discussions with accountants and certain other non-attorney tax advisors for purposes of certain tax laws may be inadequate in scope to protect discussions against discovery for purposes of these other laws. Accordingly, while businesses definitely should incorporate appropriate tax advisors into the evaluation process, most businesses before commencing meaningful discussions with or

engaging assessments by their accounting firm or other non-attorney tax advisor will want to engage counsel and coordinate the involvement of their accounting and other non-attorney tax advisors through qualified legal counsel to protect and maximize the ability to conduct the analysis of their risks and options within the protection of attorney-client privilege.

If you need assistance in conducting a risk assessment of or responding to an IRS, Labor Department or other legal challenges to your organization's existing workforce classification or other labor and employment, employee benefit or compensation practices, please contact the author of this update, attorney Cynthia Marcotte Stamer.

Board Certified in Labor & Employment Law by the Texas Board of Legal Specialization, management attorney and consultant Ms. Stamer is nationally and internationally recognized for more than 23 years of work helping employers; employee benefit plans and their sponsors, administrators, fiduciaries; employee leasing, recruiting, staffing and other professional employment organizations; and others design, administer and defend innovative workforce, compensation, employee benefit and management policies and practices.

For Help With These Or Other Matters

The author of this update, attorney Cynthia Marcotte Stamer has more than 24 years experience advising and representing employer, employee benefit and other clients before the Internal Revenue Service, the Department of Labor, Immigrations & Customs, and other agencies, private plaintiffs and others on worker classification and related human resources, employee benefit, internal controls and risk management matters.

A board certified labor and employment attorney widely known for her extensive and creative knowledge and experience worker classification and other employment, employee benefits and workforce matters, Ms. Stamer works extensively with employers, employee benefit plan sponsors, insurers, administrators, and fiduciaries, payroll and staffing companies, technology and other service providers and others to develop and operate legally defensible programs, practices and policies that promote the client's human resources, employee benefits or other management goals.

A featured presenter in the recent "Worker Classification & Alternative Workforce: Employee Plans & Employment Tax Challenges" teleconference sponsored by the American Bar Association Joint Committee on Employee Benefits, Ms. Stamer also is a widely published author and highly regarded speaker on these and other employee benefit and human resources matters who is active in many other employee benefits, human resources and other management focused organizations.

The immediate past Chair and current Welfare Benefit Committee Co-Chair of the American Bar Association (ABA) RPTE Employee Benefits & Other Compensation Committee, a Council Representative on the ABA Joint Committee on Employee Benefits, the Vice Chair of the ABA TIPS Employee Benefits Committee, the Gulf States Area TEGE Council Exempt Organizations Coordinator, past-Government Affairs Committee Legislative Chair for the Dallas Human Resources Management Association, past Chair of the ABA Health Law Section Managed Care & Insurance Interest Group, and the editor and publisher of [Solutions Law Press HR & Benefits Update](#) and other Solutions Law Press Publications, She also is recognized for her publications, industry leadership, workshops and presentations on these and other human resources concerns and regularly speaks and conducts training on these matters. Her insights on these and other matters appear in the Bureau of National Affairs, Spencer Publications, the Wall

Street Journal, the Dallas Business Journal, the Houston Business Journal, and many other national and local publications.

You can learn more about Ms. Stamer and her experience, find out about upcoming training or other events, review some of her past training, speaking, publications and other resources, and register to receive future updates about developments on these and other concerns from Ms. Stamer at www.CynthiaStamer.com.

For important information concerning this communication click [here](#). THE FOLLOWING DISCLAIMER IS INCLUDED TO COMPLY WITH AND IN RESPONSE TO U.S. TREASURY DEPARTMENT CIRCULAR 230 REGULATIONS. ANY STATEMENTS CONTAINED HEREIN ARE NOT INTENDED OR WRITTEN BY THE WRITER TO BE USED, AND NOTHING CONTAINED HEREIN CAN BE USED BY YOU OR ANY OTHER PERSON, FOR THE PURPOSE OF (1) AVOIDING PENALTIES THAT MAY BE IMPOSED UNDER FEDERAL TAX LAW, OR (2) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY TAX-RELATED TRANSACTION OR MATTER ADDRESSED HEREIN.

©2011 Cynthia Marcotte Stamer, P.C.