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Employers Considering Using New IRS Worker Classification Settlement Program Also Must Manage Other Legal Exposures

Program Shows Growing Risks, 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 signal to businesses using independent contractors, leased employees or other non-employee workers of the need to take steps to confirm and strengthen the defensibility of their existing non-employee and exempt employee classifications in response to rising scrutiny and challenging of these characterizations the IRS and a host of other federal and state regulators, as well as workers and others in private litigation.

To guard against these and other growing risks of worker classification, employers receiving services from workers who are not considered employees for purposes of income or payroll 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.

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.

Settlement Program & Other Enforcement Highlights Growing Need For Businesses To Manage Tax & Other Worker Misclassification Risks

Echoing the growing scrutiny by the IRS and other agencies on monitoring and enforcing worker classification compliance, the IRS says the new Settlement Program established under [Announcement 2011-64](#) will increase tax compliance and provide greater certainty for employers, workers and the government.

The new Settlement Program 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. The IRS’ launch of the Settlement Program follows its September, 2010 kickoff of a three-year audit program under which the IRS planned to audit the appropriateness of employer worker classification and other payroll tax practices of approximately 6000 employers. By following up with the establishment of the Settlement Program, the IRS is sending another strong signal to employers to use the Settlement Program to clean up questionable worker classification practices now to avoid significant payroll tax liability from an IRS audit or other enforcement action.

Under the program, eligible employers can obtain substantial relief from federal payroll taxes and penalties owing from past misclassification of workers by reclassifying workers under the program, filing and paying the required settlement fee to the IRS and meeting other Settlement Program requirements. When applicable, the required settlement fee effectively equals just over one percent (1%) 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 must file for admission to the program at least 60 days before reclassifying workers as employees and meet other requirements.

Worker Classification Risk Management Requires Holistic Handling

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 in the program, as well as its interaction with worker classification risks under other laws. 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.

Many employers may face challenges deciding the applicability and using the Settlement Program to address payroll tax issues. 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. As a starting point, many businesses may face challenges determining the specific workers to reclassify in connection with the use of the Settlement Program given the highly fact specific common law tests used to decide a worker's classification. 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 hard 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.

For Help With These Or Other Matters

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

Board Certified in Labor & Employment Law by the Texas Board of Legal Specialization, Ms. Stamer is nationally and internationally recognized for more than 24 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.

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.

Her experience includes extensive work 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 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.

Additional Resources

If you found this update of interest, you also may be interested in reviewing some other recent publications or other resources of Ms. Stamer including:

- [HHS Projects Medicare Advantage Enrollment Will Rise As Premiums Decline In 2012; Plans Face Increased Regulation & Enforcement](#)
- [Participant Notification Added To Required Procedures For Church Plan Determination Letter Requests](#)
- [Employers Considering Using New IRS Voluntary Worker Classification Settlement Program To Resolve Payroll Tax Risks Must Also Manage Other Legal Exposures](#)
- [4th Circuit Rejects Two Challenges To Affordable Care Act Constitutionality](#)
- [Stamer Named Fellow In American College of Employee Benefits Counsel Unions Get New Tool As NLRB Changes Bargaining Units Certification Rules For Non-Acute Health Care Facilities](#)
- [ABA TIPS Section Appoints Cynthia Marcotte Stamer Vice Chair of Employee Benefits General Committee](#)
- [Affordable Care Act To Require Health Plans Cover Contraception & Other Women’s Health Procedures Beginning In 2012](#)
- [Affordable Care Act To Require Health Plans Cover Contraception & Other Women's Health Procedures In 2012](#)
- [Labor Department 2011 Stats Show Employer Health Coverage & Other Benefit Statistics](#)
- [Company Executives, Plan Sponsors & Others May Face Personal Liability When Others Defraud Plans or Mismanage Employee Benefit Plan Responsibilities](#)
- [EEOC Finalizes Updates To Disability Regulations In Response to ADA Amendments Act: Employers Should Manage Risks](#)
- [Extended Grace Period For Some, But Not All New Affordable Care Act Health Claims & Appeals Rules Gives Qualifying Plans, Insurers Limited & Imperfect Relief](#)
- [UCLA Health Systems Payment of \\$865,500 To Settle HIPAA Charges Shows Rising HIPAA Risk](#)
- [DOL Considers Easing Rules For Electronic Benefit Communications](#)
- [Improving the Effectiveness of Compliance & Risk Management By Getting HR On The Compliance Team](#)
- [IRS Establishes Safe Harbor Election for Allocating Success-Based Fees Paid On Certain Business Transactions](#)
- [Plan Sponsors, Their Owners & Management & Others Risk Personal Liability If Others Defraud Plans or Mismanage Employee Benefit Plan Responsibilities](#)
- [Agencies Clarify Affordable Care Act Grandfathered Health Plan Rules](#)
- [Time to Tighten Health Plan Claims and Appeals Practices](#)
- [EEOC Finalizes Updates To Disability Regulations In Response to ADA Amendments Act](#)
- [NLRB Settlement Shows Care Necessary When Using Social Networking & Other Policies Restricting Employee Communications](#)

- [Safeguarding Yourself From Liability For Another's Employee Benefit Plan Embezzlement Or Other Misconduct](#)
- [DOL Wage & Hour Settlements Highlight Rising Wage & Hour Enforcement Risks](#)

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.

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