IRS Presenters

Marvina Dail
Revenue Agent
Small Business/Self Employed
Exam Operations, Specialty Exam

Rebecca Wilson
Acting Branch Chief
Employment Tax
IRS Office of Chief Counsel
Mail to:

sbse.webinars@irs.gov
Employment Tax Issues

• Worker Classification
• Voluntary Classification Settlement Program (VCSP)
• Fringe Benefits
• Officer Compensation
• Back-up Withholding and Information Return Penalties
Worker Classification

• Workers can be either employees or independent contractors

• Business has different reporting responsibilities for each
  — ET returns and Forms W-2 for employees
  — 1099 MISC for independent contractors
Form 1099-MISC
(Independent Contractor)

PAYER’S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.

<table>
<thead>
<tr>
<th>PAYER’S federal identification number</th>
<th>RECIPIENT’S identification number</th>
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RECIPIENT’S name

Street address (including apt. no.)

City or town, state or province, country, and ZIP or foreign postal code

Account number (see instructions) | FATCA filing requirement | 2nd TIN not. |
----------------------------------|-------------------------|-------------|

15a Section 403A deferrals

15b Section 409A income

16 State tax withheld

17 State/Payer’s state no.

18 State income

19 Federal income tax withheld

Miscellaneous Income

2015

Copy A For Internal Revenue Service Center

File with Form 1096, For Privacy Act and Paperwork Reduction Act Notice, see the 2015 General Instructions for Certain Information Returns.
Employee vs. Independent Contractor

• Determination based on facts & circumstances of each case. No *single* factor determines classification

• Right to direct & control is key:
  - Behavioral control
  - Financial control
  - Relationship of the parties

• See IRS Publication 1779, *Independent Contractor or Employee*
Behavioral Control

• Instructions can cover a wide range of topics, for example:
  • How, when or where to do the work
  • What tools or equipment to use
  • What assistants to hire to help with the work
  • Where to purchase supplies and services
  • What work must be performed by a specified individual
  • What order or sequence to follow when performing the work
Training

Training – If the business provides you with training about required procedures and methods, this indicates that the business wants the work done in a certain way and this suggests that you may be an employee.
Financial Control

Facts showing whether there is a right to direct or control the business part of the work include:

• Significant Investment
• Expenses
• Opportunity for Profit or Loss
• Insurance Coverage
• Responsible for Correcting a Mistake
• Availability of Services
• Method of Payment
Relationship of the Parties

Facts that illustrate how the business and the worker perceive their relationship include:

• Written Contracts
• Employee Benefits
Relationship of the Parties

Other Questions to Determine Employer-Employee Relationship:
• How permanent is the relationship?
• Are the services provided a crucial activity of the business?
IRS Resources

• Publication 1779, *Independent Contractor or Employee*

• Publication 15-A, *Employer's Supplemental Tax Guide*

• IRS podcast and training material at www.irs.gov
Audience Question #1

What are important factors in determining proper worker status?
A. Potential employment tax liabilities
B. Right to direct and control
C. Considering all aspects of relationship
D. Whether worker is seasonal or permanent
Form SS-8

Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding

Information about Form SS-8 and its separate instructions is at www.irs.gov/formss8.

| Name of firm (or person) for whom the worker performed services | Worker’s name |
| Firm’s mailing address (include street address, apt. or suite no., city, state, and ZIP code) | Worker’s mailing address (include street address, apt. or suite no., city, state, and ZIP code) |
| Trade name | Firm’s email address | Worker’s daytime telephone number | Worker’s email address |
| Firm’s fax number | Firm’s website | Worker’s alternate telephone number | Worker’s fax number |
| Firm’s telephone number (include area code) | Firm’s employer identification number | Worker’s social security number | Worker’s employer identification number (if any) |

Note. If the worker is paid for these services by a firm other than the one listed on this form, enter the name, address, and employer identification number of the payer. 

Disclosure of Information

The information provided on Form SS-8 may be disclosed to the firm, worker, or payer named above to assist the IRS in the determination process. For example, if you are a worker, we may disclose the information you provide on Form SS-8 to the firm or payer named above. The information can only be disclosed to assist with the determination process. If you provide incomplete information, we may not be able to process your request. See Privacy Act and Paperwork Reduction Act Notice in the separate instructions for more information. If you do not want this information disclosed to other parties, do not file Form SS-8.
**Form 8919**

**Uncollected Social Security and Medicare Tax on Wages**

Information about Form 8919 and its instructions is at www.irs.gov/form8919.

Attach to your tax return.

Name of person who must file this form. If married, complete a separate Form 8919 for each spouse who must file this form.

<table>
<thead>
<tr>
<th>Social security number</th>
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**Who must file.** You must file Form 8919 if all of the following apply.

- You performed services for a firm.
- You believe your pay from the firm was not for services as an independent contractor.
- The firm did not withhold your share of social security and Medicare taxes from your pay.
- One of the reasons listed below under Reason codes applies to you.

**Reason codes:** For each firm listed below, enter in column (c) the applicable reason code for filing this form. If none of the reason codes apply to you, but you believe you should have been treated as an employee, enter reason code G, and file Form SS-8 on or before the date you file your tax return.

<table>
<thead>
<tr>
<th>A</th>
<th>I filed Form SS-8 and received a determination letter stating that I am an employee of this firm.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>I received other correspondence from the IRS that states I am an employee.</td>
</tr>
<tr>
<td>G</td>
<td>I filed Form SS-8 with the IRS and have not received a reply.</td>
</tr>
<tr>
<td>H</td>
<td>I received a Form W-2 and a Form 1099-MISC from this firm for 2014. The amount on Form 1099-MISC should have been included as wages on Form W-2. (Do not file Form SS-8 if you select reason code H.)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(a) Name of firm</th>
<th>(b) Firm’s federal identification number (see instructions)</th>
<th>(c) Enter reason code from above</th>
<th>(d) Date of IRS determination or correspondence (MM/DD/YYYY) (see instructions)</th>
<th>(e) Check if Form 1099-MISC was received</th>
<th>(f) Total wages received with no social security or Medicare tax withholding and not reported on Form W-2</th>
</tr>
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Trust Fund Penalty

• The trust fund recovery penalty may apply if federal income tax, social security and Medicare tax are either not deposited or paid.

• Trust fund penalty may be assessed on those persons found by the IRS to be responsible for collecting, accounting for, and remitting these taxes and who acted willfully in not doing so.
Definitions

• A responsible person includes an officer or employee of a corporation, a partner or employee of a partnership, an accountant, a volunteer director or trustee, or an employee of a sole proprietorship. A responsible person also may include someone who signs checks for the business or otherwise has authority to cause the spending of business funds.

• Willfully means voluntarily, consciously, and intentionally. A responsible person acts willfully if the person knows the required actions are not taking place.
Section 530

• Section 530 provides relief from federal employment taxes if requirements are met:
  — Taxpayer did not treat worker as an employee
  — Taxpayer filed all required federal tax returns (like Form 1099-MISC) consistently with non-employee treatment
  — Taxpayer had a reasonable basis for not treating the worker as an employee (prior audit, case law, etc.)

• See IRS Publication 1976, *Do You Qualify for Relief Under Section 530*, for additional information.
Section 3509

- Section 3509 provides reduced rates for the employee’s share of FICA taxes and for the federal income tax that should have been withheld, if you treated an employee as a non-employee.
- Section 3509 does not provide relief for the employer’s share of FICA taxes.
- The applicable rates depend on whether you filed required Forms 1099.
Classification Settlement Program (CSP)

- The IRS Classification Settlement Program (CSP) establishes procedures to be used by Exam to resolve worker classification audits.
- CSP agreements are closing agreements that bind the taxpayer to treat workers as employees for future tax periods.
- If the business meets the CSP qualifications, it may be entitled to a reduced amount of tax.
- CSP is available only in an audit setting.
- See IRM 4.23.6 for more information.
Voluntary Classification Settlement Program (VCSP)

• Voluntary Classification Settlement Program (VCSP) – IRS launched program in 2011
• The VCSP is a voluntary program that provides an opportunity for taxpayers to reclassify their workers as employees for employment tax purposes for future tax periods with partial relief from federal employment taxes.
• Use Form 8952, Application for Voluntary Classification Settlement Program to apply
VCSP-Eligibility

Eligibility:

• A taxpayer must have consistently treated the workers as nonemployees and filed all required Forms 1099 for the previous three years.

• The taxpayer cannot currently be under employment tax audit by the IRS and cannot be currently under audit by the Department of Labor or by a state government agency.

Note: Exempt organizations and government entities may also participate in VCSP.
Voluntary Classification Settlement Program (VCSP)

- Application Form 8952 should be filed at least 60 days before the date the taxpayer wants to begin treating their workers as employees. New requirements require taxpayers to include a list of names and SSNs for the workers being reclassified.
- Taxpayers pay 10% of the employment tax liability determined under 3509(a) rates and will not be liable for any interest and penalties on the amount due.
- See Announcement 2012-45 and the IRS website for additional guidance.
Audience Question #2

To be eligible for a VCSP, one of the criteria is that the taxpayer:

A. Must have consistently treated the workers as nonemployees and must have filed all required Forms 1099 for the workers to be reclassified for the previous five years

B. Is currently under audit concerning the classification of workers by the Department of Labor or by a state government agency

C. Is not currently under an employment tax audit by the IRS

D. Is not an exempt organization
Fringe Benefits

• Wages if provided as compensation for employment
• Included in worker’s income and subject to FICA & FUTA taxes
• Employee – Fringe benefits reported on Form(s) 941 and W-2
• Non-employee – Fringe benefits reported on Form 1099-MISC for independent contractors or on Schedule K-1 (Form 1065) for partners
Fringe Benefit Valuation

• Generally – Fair Market Value of benefit
• Separate rules for meals, aircraft use, and automobile use
• Rules for noncash valuation and withholding
• Employer must determine the actual value of noncash fringe benefits no later than January 31 of the year after the year in which the benefit was received
Fringe Benefit Valuation

• If an employer chooses to pay an employee's social security and Medicare taxes on taxable fringe benefits without deducting them from his or her pay, the employer must include the amount of those tax payments in the employee's income.

• More benefit information is in Publication 15-B, *Employer’s Tax Guide to Fringe Benefits*
Cafeteria Plans

• Must be written plan
• Option of receiving cash or taxable benefits versus certain qualified benefits excludable from wages
• Further information - See IRS Publication 15-B, Employer’s Tax Guide to Fringe Benefits
Fringe Benefit-Exclusions

Examples of Fringe benefits whose value is all or partially excluded from recipient's pay:

• Accident and health benefits
• Adoption Assistance
• Dependent care assistance
• Group term life insurance
• No-additional-cost services
• Transportation benefits (for example, bus pass, metro card) subject to limitations
Audience Question #3

When are fringe benefits includible in income and subject to employment taxes?

A. Never for employees
B. Always for independent contractors
C. Always, unless exempted by law
D. Fringe benefits are never included in anyone’s income
Officer Compensation

- Corporate officers are employees for FICA purposes under Internal Revenue Code §3121(d)(1).
- Corporate officers are employees for Federal Income Tax Withholding purposes under Internal Revenue Code §3401(c).
- Corporate officers are employees for FUTA purposes under Internal Revenue Code §3306(i).
Officer Compensation

Corporate officers are employees by statute. Some examples of an officer’s compensation being wages:

- If an officer performs services, their compensation is wages and subject to employment tax.
- President of a corporation generally performs more than minor services.
- Because a corporate officer is an employee by statute, the courts have found that taxpayers had no reasonable basis for treating a corporate officer as anything other than an employee.
Court finds Officers are Employees

Court cases finding officers are employees:
• Nu-Look Design, Inc. (3d Cir. 2004),
• Joly (6th Cir. 2000),
• Joseph Radtke, S.C. (7th Cir. 1990),
• Spicer Accounting, Inc. (9th Cir. 1990),
• Western Management, Inc. (Ct Fed Cl 2000),
• Dennis Katz D.D.S., P.C. (Tax Court 2002).
Compensation

• Determination based on facts and circumstances of each case
• Some of the considerations:
  ─ Position held by each officer
  ─ Duties performed by each officer
  ─ Hours worked by each officer
  ─ Compensation paid
Websites

• BizMiner - www.bizstats.com
• Salary Expert - www.salaryexpert.com
• Salary Estimator - www.salaryestimator.com
• Salary - www.salary.com
• Monster - www.monster.com
Audience Question #4

Which of the following are factors in determining a reasonable salary for corporate officers?

A. The officer’s lifestyle  
B. The duties the officer performs  
C. The Internal Revenue Code provides pay scales for corporate officer compensation  
D. The hours the officer works
Form 1099-MISC

• Payments to non-employees of $600 or more per calendar year
• Payments reported in Box 7 of Form 1099-MISC (non-employee compensation)
• Form 1099-MISC: Furnish copy to the worker and file a copy with the IRS
• Form 1099-MISC reporting is not required for payments to LLCs that are treated as a C or S corporation unless payments are for legal or medical and health care services.
Backup Withholding

• Currently the rate is 28%
• Required if no TIN or incorrect TIN was secured for the worker
• Continues until correct TIN provided
• Reported on Form 1099-MISC
• Payer files Form 945, Annual Return of Withheld Federal Income Tax
Penalties

- Penalties: Section 6721 Failure to File Correct Information Returns & Section 6722 Failure to Furnish Correct Payee Statements
- Recent increase in penalties for returns & statements required to be filed after 12/31/2015
- Revised penalty is $50, $100 or $250 per information return
- Revised maximum penalty is $500,000, $1,500,000 or $3,000,000 per year-with lower caps for small businesses
Which of these indicates a situation that would require backup withholding?

A. The worker gives a nine digit SSN
B. The IRS notified the payer that the worker TIN is invalid
C. The worker’s TIN contains an alpha character
D. All of the above
Summary

• Worker Classification
• Voluntary Classification Settlement Program (VCSP)
• Fringe Benefits
• Officer Compensation
• Back-up Withholding and Information Return Penalties
Resources

- IRS website (www.irs.gov)
- IRS Publication 1779, *Independent Contractor or Employee*
- IRS Publication 15 (Circular E), *Employer’s Tax Guide*
- IRS Video Portal (www.irsvideos.gov)