

IRS Tempts Employers Who Have Been Misclassifying Employees

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Employers have a strong withholding and employment tax incentives to classify their workers as independent contractors instead of employees. Such a course avoids income tax withholdings and FICA, FUTA, and Medicare taxes and withholdings, shifting responsibility of such items to the worker.

As such, employers may have aggressively or inappropriately classified employees as independent contractors. An IRS settlement program known as the "Voluntary Classification Settlement Program," or VCSP, provides a semi-painless way for employers to correct their classifications and come into the fold of compliant taxpayers. A recent set of FAQs provides details on the new program. Below is a summary of the key provisions.

WHO CAN USE THE PROGRAM?

Businesses, tax-exempt organizations, and government entities.

BASIC ELIGIBILITY REQUIREMENTS

To be able to apply, the employer must:

- 1) have consistently treated the subject workers as nonemployees,
- 2) have filed all required Forms 1099 for the workers for the previous three years, and
- 3) not be under audit by IRS, or currently under audit concerning the classification of the workers by the Department of Labor or a state government agency.

EFFECT OF PROGRAM

The employer will have to pay a relatively small sum to enter the program, but will then receive absolution for its mischaracterizations for past years. More particularly, the employer will:

(1) owe 10% of the employment tax liability that may have been due on compensation paid to the workers for the most recent tax year, applying the special reduced rates of Code Section 3509, and without interest or penalties being imposed on that liability,

(2) be safe from an employment tax audit for the worker classification of the subject workers for prior years, and

(3) have to agree to extend the period of limitations on assessment of employment taxes for three years for the first, second and third calendar years beginning after the date on which the taxpayer has agreed under the VCSP closing agreement to begin treating the workers as employees.

Of course, the employer will begin classifying the subject workers as employees and paying appropriate employment and withholding taxes.

Given the relatively small amount that is due, the program provides an excellent opportunity for taxpayers to put themselves into compliance. In an example provided in the FAQ, an employer who paid \$1,500,000 to workers in the subject tax year owed only \$16,020 for the required 10% payment.

Application for the program is made on Form 8952, Application for Voluntary Classification Settlement Program. More information on the VCSP is available in [Announcement 2011-64](#).

Voluntary Classification Settlement Program (VCSP) Frequently Asked Questions

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