

New IRS Program Limits Liability for Misclassified Workers

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"What's in a name? That which we call a rose By any other name would smell as sweet."

- William Shakespeare

On the subject of "independent contractors," the law would have us heed William Shakespeare's famous line. An employer that labels a worker as an independent contractor accomplishes nothing in the eyes of the law if the facts do not support the label. When an employer misclassifies a worker as an independent contractor, the employer exposes itself to a host of potential claims and liabilities, including but not limited to those related to payroll taxes, income tax withholding, workers compensation, unemployment insurance, overtime pay, and benefits.

To encourage employers to voluntarily fix worker classification errors, the IRS has created a new voluntary compliance program—the Voluntary Classification Settlement Program (VCSP)—through which eligible employers can significantly decrease their exposure for misclassifications.

With the advent of the VCSP, employers that use independent contractors should re-evaluate their independent contractor relationships and confirm whether the facts support the independent contractor label. If an eligible employer determines that one or more independent contractors should have been classified as employees, it may apply for relief under the VCSP. The following are highlights of participating in the VCSP:

- The employer agrees to prospectively treat a class of workers as employees;
- The employer pays to the IRS an amount equal to 10% of the employment tax liability that would have been due on compensation paid to the misclassified workers for the most recent tax year;



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and

- The employer becomes exempt from an employment tax audit with respect to the worker classification for the group of workers reclassified under the VCSP.

Employers should keep in mind that the VCSP provides relief only from federal payroll tax liabilities. The program does not address other potential claims and liabilities, such as those arising in connection with state taxes, workers compensation, overtime pay, and benefits. Before taking advantage of the VCSP, employers should consult with legal counsel to make sure they understand both the benefits and the potential risks of participating in the program.



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