

Federal Government Announces New Amnesty Program for Misclassified Workers

October 19, 2011

For the past four years, New York employers have had to look over their shoulder to see if the New York State Labor Department was knocking on their door to review the classification of their employees. That is because in 2007, New York formed a Task Force to deal with the issue of worker misclassification - - that is, improperly classifying a W-2 employee as a 1099 independent contractor. Since then, hundreds of businesses have faced audits and penalties as a result of misclassification.

The Federal government has followed suit, announcing that it is committing additional funds to investigate and prosecute employers who misclassify their workers as independent contractors.

On September 21, 2011, the IRS announced that it would be offering a new program to businesses which would permit them to voluntarily reclassify their workers as W-2 employees for federal employment tax purposes. The Voluntary Classification Settlement Program (VCSP) permits eligible businesses to voluntarily reclassify their workers as W-2 employees for future tax periods, with limited federal employment tax liability for previously misclassifying these workers as independent contractors. To participate, the business must meet eligibility standards, apply to participate, and enter into an agreement with the IRS.

To be eligible, a business must have consistently treated the workers as independent contractors, and must have filed all required Forms 1099 for the workers for the previous three years. The business cannot currently be under audit by the IRS, or by the federal Department of Labor or any state agency. A previously audited business will only be eligible if the business has complied with the results of the audit.

The participating business must voluntarily agree to prospectively treat the class of workers as employees for tax purposes. In exchange, the business will pay only ten percent of the employment tax liability that may have been due on compensation paid to the workers for the most recent tax year, will not be liable for any interest and penalties on the liability, and will not be subject to an employment tax audit concerning misclassification for prior years. However, the participating business must agree to extend the statute of limitations for the three calendar years after which the business signs the agreement to treat the workers as employees, thus lengthening the potential period of prosecution for future violations. Information about the program and applications will be available on <http://www.irs.gov/>.

One note of caution -it is unclear whether the IRS will be sharing information about the reclassification with other governmental agencies, and it is unclear how other agencies will treat it. For example, if the IRS shared information with the [New York State Department of Labor](#) without some concomitant New York State amnesty, it would be possible for New York State to come back against the business for unpaid unemployment taxes and workers compensation coverage, along with interest and penalties. This firm has contacted the Acting Chair of the Misclassification Task force to ascertain how the New York authorities

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will treat participation in this program, but has not yet received an opinion. Therefore, our best advice is to proceed cautiously, should you choose to take advantage of this new program. When we obtain more information, we will let you know.

If you have any questions about this or any other employment-related issues, please contact [Sharon P. Stiller](#), Esq. in our [Employment Law Group](#), or your attorney contact at our firm.

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