

IRS Announces New Voluntary Worker Classification Program

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Publication Date: September 27, 2011

On September 21, 2011, the Internal Revenue Service announced the Voluntary Classification Settlement Program (the "VCSP"), allowing eligible employers to voluntarily resolve past worker classification issues and reclassify workers as employees for federal employment tax purposes. Reclassifying workers as employees, however, raises many issues other than employment tax issues, including, for example: retirement benefit plan issues; health and welfare benefit plan issues; and state tax classification, unemployment tax, and workers' compensation issues. Employers should consider all potential ramifications before participating in the VCSP.

Prior to the VCSP, employers who voluntarily reclassified workers could still be exposed to federal back taxes, penalties, and interest for open years. The only relief that was available was under the IRS's Classification Settlement Program (the "CSP"), which is only available to employers already under IRS examination. The VCSP, in contrast to the CSP, provides employers the opportunity to voluntarily reclassify workers outside of the examination context.

The VCSP is available to eligible employers who satisfy the following requirements:

- The employer must consistently have treated the workers as non-employees in the past.
- The employer must have filed all required Forms 1099 for the workers for the previous three years.
- The employer must not currently be under audit by the IRS, the U.S. Department of Labor (the "DOL"), or a state agency concerning classification of the workers. (If an employer was previously audited by the IRS or the DOL concerning the classification of the workers, the employer will only be eligible if it has complied with the results of that audit.)

Employers can apply for the VCSP by filing Form 8952 at least 60 days before they want to begin treating the workers as employees. Employers accepted into the VCSP must enter into a closing agreement with the IRS whereby they agree to (i) prospectively treat the workers as employees, (ii) pay 10 percent of the



federal employment tax liability that may have been due on compensation paid to the workers for the most recent year, and (iii) allow a six-year statute of limitations on assessment of employment taxes for the first three calendar years after the employer has entered into the VCSP closing agreement. In exchange, the employers will not be liable for any interest or penalties on the amount they are required to pay under federal law, and the IRS will not conduct employment tax audits of the employers for prior years with respect to classification of the workers.

While the VCSP may be worth considering, as mentioned above, reclassifying workers as employees could also raise numerous other issues that should be considered as part of an overall compensation strategy.

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