



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

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The Honorable Dianne Feinstein
United States Senate
Washington, DC 20510

Attention:

Dear Senator Feinstein:

This letter responds to your request for information dated December 11, 2010, on behalf of your constituent, . asked how to determine if he is an employee for income tax withholding purposes.

The question of whether an individual is an employee or an independent contractor (non-employee) depends on the facts and the application of law and regulations to a particular case. The regulations that provide the criteria for determining an individual's status as an employee or independent contractor for income tax withholding purposes are found in section 31.3401(c)-1 of the Employment Tax Regulations.

These regulations provide that, in general, the employer-employee relationship exists when the person for whom the individual performs services has the right to direct and control that individual not only as to the result to be accomplished by the work, but also as to the details and means by which that result is accomplished. The employer does not have to actually direct or control the manner in which the individual performs the services, but must have the right to do so. [Regulation section 31.3401(c)-1(b)].

If the relationship of an employer and employee exists, the parties' designation or description of the relationship as anything other than that of employer and employee is not important. [Regulation section 31.3401(c)-1(d)]. This means that, if an employer-employee relationship exists, whether the parties designate the employee as partner, co-adventurer, agent, independent contractor, or the like does not matter. [Regulation section 31.3401(c)-1(e)]. These rules reflect common law principles, developed and affirmed over decades by the courts, that govern Internal Revenue Service policy in this area.

In determining whether an individual is an employee or independent contractor under the common law, one must consider all evidence of both control and lack of control or autonomy. In doing so, one must examine the relationship of the work and the business. Relevant facts generally fall into three categories: (1) behavioral controls, (2) financial controls, and (3) the relationship of the parties.

Behavioral controls refer to facts that indicate whether the service recipient has a right to direct and control how the worker performs the specific task for which the individual is hired. Facts that illustrate whether there is a right to control how a worker performs a task include the provision of training, the issuance of instructions, or the completion of a job performance evaluation.

Financial controls refer to facts that indicate whether the service recipient has a right to direct or control the financial aspects of the worker's activities. These factors include the method of payment, the worker's opportunity for profit or loss, and whether a worker has made a significant investment, incurs unreimbursed expenses, or makes services available to the relevant market.

The relationship of the parties is generally evidenced by the parties' agreements and actions with respect to each other, including facts which show not only how they perceive their own relationship but also how they represent their relationship to others. Facts which illustrate how the parties perceive their relationship include the intent of the parties as expressed in written contracts, the provision of or lack of employee benefits, the right of the parties to terminate the relationship, the permanency of the relationship, and whether the services performed are part of the service recipient's regular business activities.

I am enclosing a copy of Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding. _____ can file a Form SS-8 to request a determination of his worker status for purposes of federal employment taxes and income tax withholding. However, we cannot issue a determination letter on a hypothetical situation.

If an individual is an employee under the common law rules, the individual's employer must ask the individual for a withholding exemption certificate that an employee uses to claim federal income tax withholding exemptions. Employees claim these exemptions using a Form W-4, Employee's Withholding Allowance Certificate. If an employee does not furnish his employer with a Form W-4, the employer will treat the employee as single and claiming no exemptions. I am also enclosing a copy of Form W-4, Employee's Withholding Allowance Certificate.

This letter outlines certain general principles of the law, which I hope are helpful in responding to _____. It is intended for informational purposes only and does not

constitute a ruling. See Rev. Proc. 2010-1, section 2.04, 2010-1 Internal Revenue Bulletin 1 (Jan. 4, 2010). If you have any questions, please contact me or
at .

Sincerely,

Nancy Marks
Division Counsel/Associate Chief Counsel
(Tax Exempt & Government Entities)

Enclosures (2)