

IRS Fact Sheet

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General Employment Tax Issues

FS-2015-25, November 2015

The Internal Revenue Service reminds business owners how critical it is to understand the various types of employment-related taxes they may be required to deposit and report.

This fact sheet provides information on some of the more common employment tax topics posed by business owners, including:

- Worker Classification
- Voluntary Classification Settlement Program
- Fringe Benefits
- Officer Compensation
- Backup Withholding and Information Return Penalties

Worker Classification

A common error is not correctly classifying a worker.

The IRS classifies workers as either independent contractors or employees. Tax responsibilities are different based on how the worker is treated; an employee requires employment tax withholding and matching by the business on wages paid to them while payments made to an independent contractor do not.

Contractors and subcontractors who are engaged in an independent trade, business or profession, in which they offer their services to the public, are generally not employees. However, whether such people are employees or independent contractors depends on the facts and circumstances of each case.

More information is available in [IRS Publication 1779, *Independent Contractor or Employee*](#) and at IRS.gov.

Voluntary Classification Settlement Program

Worker classification can greatly affect a business well beyond the initial determination. The Voluntary Classification Settlement Program, commonly called VCSP, is a program that allows taxpayers to voluntarily reclassify their workers as employees for future tax periods for federal employment tax purposes and to obtain partial relief from the federal employment taxes due during the misclassified periods of employment.

The [VCSP](#) process is simple. To participate, the taxpayer must meet certain eligibility requirements, apply to participate in the VCSP and, if accepted, enter into a closing agreement with the IRS.

Taxpayers should file [Form 8952, Application for Voluntary Classification Settlement Program](#) at least 60 days before the date that they want to begin treating their workers as employees. In order for their application to be considered, taxpayers must attach a list of names and Social Security numbers of all workers to be reclassified as part of the VCSP agreement.

Refer to [IRS Announcement 2012-45](#) and IRS.gov for additional guidance.

Fringe Benefits

A fringe benefit is a form of payment for the performance of services. Businesses provide fringe benefits to all types of workers, including employees, independent contractors, partners and directors. Any fringe benefit is taxable and must be included in the worker's income unless the law specifically excludes it or the recipient pays for the benefit.

See Fringe Benefit Exclusion Rules provided in Section 2 of [Publication 15-B, Employer's Tax Guide to Fringe Benefits](#).

Officer Compensation

Corporate officers are, by statute, employees. Although the statutes are clear, many S Corporations and closely held C Corporations fail to treat payments to their officers for services as wages. Instead, they improperly treat the payments as corporate distributions, loans and payments of personal expenses.

See [S Corporation Employees, Shareholders and Corporate Officers](#) on IRS.gov for more information.

Form 1099-MISC, Backup Withholding and Information Return Penalties

Most businesses use [Form 1099-MISC](#) to report payments to non-employees to the IRS. The Internal Revenue Code (IRC) requires a business to report payments to the IRS for services rendered by non-employees if the business paid the non-employee \$600 or more during the calendar year.

A business should always secure the Taxpayer Identification Number, commonly called TIN, for any workers to whom the business makes reportable payments, so they can properly report those payments on Form 1099-MISC. A TIN is often, though not always, a Social Security number. Businesses can use [Form W-9, Request for Taxpayer Identification Number and Certification](#), to obtain the worker's TIN.

Certain reportable payments to individuals may be subject to backup withholding, currently at a rate of 28 percent, when a payee's TIN is missing or incorrect on an information return. See [Backup Withholding "B" Processes](#) on IRS.gov for more information.

Information return penalties apply to the failure to file correct information returns, including 1099-MISC, W-2 and Schedule K-1. The penalties per information return depend on when the business correctly filed the information return, and there is a maximum penalty per year.

For current IRC Code Section 6721 and 6722 penalty rate information, see Section O of the [General Instructions for Certain Information Returns \(Forms 1097, 1098, 1099, 3921, 3922, 5498, and W-2G\)](#).

Visit IRS.gov for more information on any of these topics.

