The Voluntary Classification Settlement Program

What is the Voluntary Classification Settlement Program (VCSP)?
The VCSP enables taxpayers to resolve past worker classification issues and achieve certainty under federal employment tax law at a low cost by voluntarily reclassifying workers for future tax periods.

Who can participate in the VCSP?
The VCSP is available to taxpayers who want to voluntarily change the prospective classification of their workers. The program is described in Announcement 2012-45 and provides an opportunity for taxpayers who are currently treating their workers (or a class or group of workers) as independent contractors or other nonemployees to reclassify their workers as employees for employment tax purposes for future tax periods with partial relief from federal employment taxes.
The VCSP is available for all businesses, including tax-exempt organizations and government entities.

What are the eligibility requirements?
The VCSP applies to taxpayers who are currently treating their workers (or a class of workers) as independent contractors or other nonemployees and want to prospectively treat the workers as employees. A taxpayer must have consistently treated the workers as nonemployees, and must have filed all required Forms 1099 for the workers being reclassified for the previous three years. The taxpayer cannot currently be under employment tax audit by the IRS or under audit concerning the classification of the workers by the Department of Labor or by a state government agency. A taxpayer who was previously audited by the IRS or the Department of Labor concerning the classification of the class or classes of workers will only be eligible if the taxpayer has complied with the results of that audit and is not currently contesting the classification in court.

How does a business apply for the VCSP?
Taxpayers apply for the VCSP by filing Form 8952, Application for Voluntary Classification Settlement Program, at least 120 days before the taxpayer wants to begin treating the workers as employees.

What happens after the taxpayer sends in the application?
The IRS will review the application and verify eligibility. Taxpayers whose application has been accepted will enter into a closing agreement with the IRS to finalize the terms of the VCSP and will simultaneously make full and complete payment of any amount due under the VCSP closing agreement. If the IRS rejects a VCSP application because the taxpayer is not eligible, the taxpayer may reapply at a future date.

What do the IRS and the taxpayer agree to under the VCSP closing agreement?
A taxpayer who participates in the VCSP and enters into a closing agreement with the IRS agrees to prospectively treat the class or classes of workers as employees for future tax periods. In exchange, the taxpayer:

a. Will pay 10 percent of the employment tax liability that may have been due on compensation paid to the workers for the most recent tax year, determined under the reduced rates of section 3509(a) of the Internal Revenue Code (this equates to a little over 1% of the amount paid to these workers);

b. Will not be liable for any interest and penalties on the liability; and

c. Will not be subject to an employment tax audit with respect to the worker classification of the workers being reclassified under the VCSP for prior years.

Where can I get more information about this attractive program?
There is more information about the VCSP in Form 8952 and its instructions, the VCSP pages of IRS.gov, including VCSP Frequently Asked Questions, and in Announcement 2012-45.