



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

OFFICE OF  
CHIEF COUNSEL

UIL: 3401.06-04

August 16, 2006

Number: **INFO 2006-0072**

Release Date: 9/29/2006

The Honorable Mike DeWine  
United States Senator  
37 West Broad Street, Suite 300  
Columbus, OH 43215

Dear Senator DeWine:

I apologize for the delay in responding to your letter dated June 7, 2006, on behalf of your constituents, [REDACTED] wrote to you about an IRS ruling that an individual worker [REDACTED] used in his business in 2002 and 2003 was an employee.

We hope the following is helpful to you in responding to the [REDACTED].

**Definition of Employee and Imposition of Employment Taxes**

The law defines an employee as any individual who, under the usual common law rules for determining the employer-employee relationship, has the status of employee. (Sections 3121(d), 3306(a), and 3401(c) of the Internal Revenue Code (the Code) and sections 31.3121(d)-1, 31.3306(l)-1, and 31.3401(c)-1 of the Employment Tax Regulations (the Regulations).)

Generally, the relationship of employer and employee exists when the person for whom the individual performs the services has the right to control and direct not only as to the results of that individual's work, but also as to the details and means by which he or she accomplishes the result. (Section 31.3121(d)-1(c)(2) of the Regulations.) *Publication 15-A, Employer's Supplemental Tax Guide*, found at [www.irs.gov](http://www.irs.gov/pub/irs-pdf/p15a.pdf) (<http://www.irs.gov/pub/irs-pdf/p15a.pdf>), explains this further. I am enclosing a copy for your convenience.

Generally, an employer must withhold, deposit, report, and pay employment taxes, including federal income tax withholding, FICA tax, and FUTA tax on wages he or she pays to employees.

An individual who is not an employee may be self-employed. A self-employed individual includes someone who carries on a trade or business as an independent contractor. An individual who is self-employed pays Self-Employment Contributions Act (SECA) tax on net earnings from self-employment using Schedule SE (Form 1040).

## **Form SS-8 Process**

Apparently, [REDACTED] received a determination letter from us following the worker's submission of a Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding. Both workers and businesses may use the Form SS-8 to request a determination of a worker's past status.

When we receive a request from a worker on Form SS-8, we try to get additional information by asking the business to complete Form SS-8. We give each party an opportunity to present a statement of the facts because any decision may affect the tax liabilities of both parties. If the business does not give us information, we can only consider the worker's statement of facts in making the status determination. Our written determination for any worker will apply to other workers of the same class if the facts are not materially different for these workers.

We assign each Form SS-8 case to a technician who reviews the facts, applies the law, and issues a decision.

The Form SS-8 determination process is not an examination (audit) of any federal tax return. Therefore, the appeal rights available for an examination do not apply to a Form SS-8 determination. However, if a business or a worker disagrees with a determination and has additional information concerning the work relationship that we may not have previously considered, either party can ask us to reconsider our decision.

## **Employment Tax Relief for Taxpayers Under Section 530 of the Revenue Act of 1978**

If a business has a reasonable basis for not treating a worker as an employee, the law provides relief for that business from having to pay employment taxes for that worker under section 530 of the Revenue Act of 1976. A reasonable basis for not treating a worker as an employee could be that the business:

- Reasonably relied on a court case about federal taxes or an IRS ruling issued to the business
- Underwent an IRS audit at a time when the business treated similar workers as other than employees and the IRS did not reclassify those workers as employees
- Treated the workers as other than employees because of knowledge that a significant segment of the same industry treated similar workers as other than employees
- Relied on some other reasonable basis, such as the advice of an accountant who knew the facts about the business

In addition, the business must have treated the workers, and any similar workers, as other than employees. Finally, the business must have filed all required federal tax returns (including information returns) for the individual for the period consistent with the individual's not being an employee. For example, if the business treated the individual as an independent contractor, the business must have filed required Forms 1099 for the individual.

If the business meets the requirements of section 530, the individual will be deemed not to be an employee for purposes of the business's federal employment tax responsibilities. Our determination

of a worker's status under Form SS-8 does not change the business's entitlement to section 530 relief.

### **Reduced Employment Tax Rates for Taxpayers Under Code Section 3509**

When a business is not eligible for relief under section 530 of the Revenue Act of 1978, other relief may be available. Generally, when a business erroneously classifies a worker as a nonemployee and does not withhold federal employment taxes, the business is not only liable for the FUTA tax and the employer share of the FICA tax but also for the employee's share of the FICA tax and the employee's federal income tax withholding. However, reduced rates for these employee taxes may be available under section 3509 of the Code.

If the business filed Forms 1099 for the workers, then we compute the federal income tax withholding at 1.5 percent of the wages paid and reduce the employee share of the FICA tax to 20 percent of the tax amount. We do not reduce the employer share of the FICA tax and the FUTA tax.

### **Worker's Tax Responsibility**

If we determine that a worker is an employee, the worker is responsible for filing an amended return for any corrections related to the decision. A determination that a worker is an employee does not necessarily reduce any current or prior tax liability. An employee is liable for the employee's share of the FICA tax regardless of payment of a tax liability by the employer. (Section 3509 of the Code). An employee is not liable for self-employment taxes. The employee must deduct any business expenses on Schedule A rather than Schedule C of Form 1040, Individual Income Tax Return, and reduce them by 2 percent of the employee's adjusted gross income.

### **Taxpayer Advocate Service**

The \_\_\_\_\_ appear to have already contacted the IRS Taxpayer Advocate Service. If they have not, they may wish to consider doing so. If a taxpayer has an ongoing issue with the IRS that has not been resolved through normal processes, or a taxpayer has suffered, or is about to suffer a significant hardship/economic burden as a result of the administration of the tax laws, the Taxpayer Advocate Service may be able to help. As an independent organization within the IRS, the Taxpayer Advocate Service helps taxpayers resolve problems with the IRS. I am enclosing contact information for the Taxpayer Advocate Service in Ohio.

I hope this information is helpful in responding to the \_\_\_\_\_ . If you have any questions, please contact me or \_\_\_\_\_ at (\_\_\_\_) \_\_\_\_\_. .

Sincerely,

Nancy J. Marks  
Associate Chief Counsel  
Tax Exempt and Government Entities

Enclosures (2)



OFFICE OF  
CHIEF COUNSEL

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

UIL: 3401.06-04

August 16, 2006

The Honorable George Voinovich  
United States Senator  
37 West Broad Street, Suite 300  
Columbus, OH 43215

Dear Senator Voinovich:

I apologize for the delay in responding to your letter dated June 7, 2006, on behalf of your constituents, wrote to you about an IRS ruling that an individual worker used in his business in 2002 and 2003 was an employee.

We hope the following is helpful to you in responding to the

**Definition of Employee and Imposition of Employment Taxes**

The law defines an employee as any individual who, under the usual common law rules for determining the employer-employee relationship, has the status of employee. (Sections 3121(d), 3306(a), and 3401(c) of the Internal Revenue Code (the Code) and sections 31.3121(d)-1, 31.3306(l)-1, and 31.3401(c)-1 of the Employment Tax Regulations (the Regulations).)

Generally, the relationship of employer and employee exists when the person for whom the individual performs the services has the right to control and direct not only as to the results of that individual's work, but also as to the details and means by which he or she accomplishes the result. (Section 31.3121(d)-1(c)(2) of the Regulations.) *Publication 15-A, Employer's Supplemental Tax Guide*, found at [www.irs.gov](http://www.irs.gov) (<http://www.irs.gov/pub/irs-pdf/p15a.pdf>), explains this further. I am enclosing a copy for your convenience.

Generally, an employer must withhold, deposit, report, and pay employment taxes, including federal income tax withholding, FICA tax, and FUTA tax on wages he or she

pays to employees.

An individual who is not an employee may be self-employed. A self-employed individual includes someone who carries on a trade or business as an independent contractor. An individual who is self-employed pays Self-Employment Contributions Act (SECA) tax on net earnings from self-employment using Schedule SE (Form 1040).

### **Form SS-8 Process**

Apparently, received a determination letter from us following the worker's submission of a Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding. Both workers and businesses may use the Form SS-8 to request a determination of a worker's past status.

When we receive a request from a worker on Form SS-8, we try to get additional information by asking the business to complete Form SS-8. We give each party an opportunity to present a statement of the facts because any decision may affect the tax liabilities of both parties. If the business does not give us information, we can only consider the worker's statement of facts in making the status determination. Our written determination for any worker will apply to other workers of the same class if the facts are not materially different for these workers.

We assign each Form SS-8 case to a technician who reviews the facts, applies the law, and issues a decision.

The Form SS-8 determination process is not an examination (audit) of any federal tax return. Therefore, the appeal rights available for an examination do not apply to a Form SS-8 determination. However, if a business or a worker disagrees with a determination and has additional information concerning the work relationship that we may not have previously considered, either party can ask us to reconsider our decision.

### **Employment Tax Relief for Taxpayers Under Section 530 of the Revenue Act of 1978**

If a business has a reasonable basis for not treating a worker as an employee, the law provides relief for that business from having to pay employment taxes for that worker under section 530 of the Revenue Act of 1976. A reasonable basis for not treating a worker as an employee could be that the business:

- Reasonably relied on a court case about federal taxes or an IRS ruling issued to the business
- Underwent an IRS audit at a time when the business treated similar workers as other than employees and the IRS did not reclassify those workers as employees

- Treated the workers as other than employees because of knowledge that a significant segment of the same industry treated similar workers as other than employees
- Relied on some other reasonable basis, such as the advice of an accountant who knew the facts about the business

In addition, the business must have treated the workers, and any similar workers, as other than employees. Finally, the business must have filed all required federal tax returns (including information returns) for the individual for the period consistent with the individual's not being an employee. For example, if the business treated the individual as an independent contractor, the business must have filed required Forms 1099 for the individual.

If the business meets the requirements of section 530, the individual will be deemed not to be an employee for purposes of the business's federal employment tax responsibilities. Our determination of a worker's status under Form SS-8 does not change the business's entitlement to section 530 relief.

### **Reduced Employment Tax Rates for Taxpayers Under Code Section 3509**

When a business is not eligible for relief under section 530 of the Revenue Act of 1978, other relief may be available. Generally, when a business erroneously classifies a worker as a nonemployee and does not withhold federal employment taxes, the business is not only liable for the FUTA tax and the employer share of the FICA tax but also for the employee's share of the FICA tax and the employee's federal income tax withholding. However, reduced rates for these employee taxes may be available under section 3509 of the Code.

If the business filed Forms 1099 for the workers, then we compute the federal income tax withholding at 1.5 percent of the wages paid and reduce the employee share of the FICA tax to 20 percent of the tax amount. We do not reduce the employer share of the FICA tax and the FUTA tax.

### **Worker's Tax Responsibility**

If we determine that a worker is an employee, the worker is responsible for filing an amended return for any corrections related to the decision. A determination that a worker is an employee does not necessarily reduce any current or prior tax liability. An employee is liable for the employee's share of the FICA tax regardless of payment of a tax liability by the employer. (Section 3509 of the Code). An employee is not liable for self-employment taxes. The employee must deduct any business expenses on Schedule A rather than Schedule C of Form 1040, Individual Income Tax Return, and reduce them by 2 percent of the employee's adjusted gross income.

## **Taxpayer Advocate Service**

The \_\_\_\_\_ appear to have already contacted the IRS Taxpayer Advocate Service. If they have not, they may wish to consider doing so. If a taxpayer has an ongoing issue with the IRS that has not been resolved through normal processes, or a taxpayer has suffered, or is about to suffer a significant hardship/economic burden as a result of the administration of the tax laws, the Taxpayer Advocate Service may be able to help. As an independent organization within the IRS, the Taxpayer Advocate Service helps taxpayers resolve problems with the IRS. I am enclosing contact information for the Taxpayer Advocate Service in Ohio.

I hope this information is helpful in responding to the \_\_\_\_\_. If you have any questions, please contact me or \_\_\_\_\_ at (\_\_\_\_\_.)

Sincerely,

Nancy J. Marks  
Associate Chief Counsel  
Tax Exempt and Government Entities

Enclosures (2)