

**Office of Chief Counsel  
Internal Revenue Service  
Memorandum**

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subject: State agent reporting and payment of employment taxes for home health care service recipients

This Chief Counsel Advice responds to your request regarding a state agency that provides in-home personal assistance services to low income, disabled individuals. This advice may not be used or cited as precedent.

LEGEND

State X =  
Taxpayer =  
Corporation Z =  
Quantity T =

ISSUE

Whether Taxpayer may remit employment taxes paid on behalf of in-home health care service recipients who receive services under Taxpayer's in-home personal service program with timely filed IRS Form 941 or Form 940?

## CONCLUSION

Yes, the applicable employment taxes may be remitted with a timely filed return. Taxpayer is a state agency serving as a Section 3504 agent for domestic service recipients and is a "state agent" within the meaning of Revenue Procedure 80-4 as modified and amplified by Notice 2003-70. As a state agent, Taxpayer is permitted to remit taxes with a timely filed return and is not subject to the deposit schedule otherwise applicable in section 31.6302-1 of the Employment Tax Regulations.

## FACTS

Taxpayer, an agency of State X, administers a statewide federal and state funded program providing personal assistance services to low-income elderly and disabled individuals who need such assistance to remain living in their own homes. Taxpayer provides services for over Quantity T home health care service recipients (HHCSRs) in State X. Under Taxpayer's program each HHCSR is authorized to select, hire, supervise, and fire his or her home health care service provider (HHCSP). However, Taxpayer takes responsibility for withholding, reporting, and paying the applicable employment taxes.

Taxpayer and Corporation Z entered into a contract under which Corporation Z performs certain payroll-type activities, but Taxpayer pays employment taxes directly to the Internal Revenue Service (the Service) and pays wages to the HHCSPs. Under the contract, Corporation Z files all required tax returns, such as Forms 940, *Employer's ANNUAL Federal Unemployment (FUTA) Tax Return*, and Forms 941, *Employer's QUARTERLY Federal Tax Return*, for Taxpayer's in-home personal services program. Corporation Z files the returns using Taxpayer's name and the separate Employer Identification Number (EIN) that Taxpayer obtained to report employment taxes withheld and paid for HHCSRs. Taxpayer pays the taxes directly to the Service via an electronic bank transfer coincident with the filing due date for the applicable return, Form 940 or Form 941. Taxpayer does not deposit any of these withheld employment taxes in advance of the return due date.

Since the late 1990s the Service has repeatedly assessed penalties under Code section 6656 against the Taxpayer for failure to deposit employment taxes. The assessed penalties are subsequently abated when Taxpayer advises the Service that it is a state agent described in Revenue Procedure 80-4 and provides a copy of a 1997 memorandum from the Office of Chief Counsel indicating that Taxpayer may remit its taxes with a timely filed return. We understand the reason the penalties continue to be assessed is that Taxpayer is not identified by the Service as an entity not required to make employment tax deposits.

This Office was asked to determine whether Taxpayer may be identified as an entity permitted to remit employment taxes with a timely filed return.

## LAW AND ANALYSIS

Section 3504 of the Code provides that the Service is authorized to designate an agent to perform such acts as are required of employers under the Code. All provisions of law applicable with respect to an employer, including penalties and liability for employment taxes, are applicable to the agent. The employer for whom the agent acts remains liable for the employment taxes as well. The general procedures for designating an agent are found in Revenue Procedure 70-6, 1970-1 C.B. 420. Under Rev. Proc. 70-6 the agent files one tax return per period, regardless of the number of employers for whom he is acting as an agent, and it files returns using its name and employer identification number. An agent designated under section 3504 agrees to be jointly liable for the employment taxes of the employer for whom he acts as an agent.

Simplified procedures apply with respect to state and local health and welfare agencies (state agents) wishing to act as agents under section 3504 on behalf of participants enrolled in a state program that provides in-home domestic services and is partially funded with federal grants under Titles XIX and XX of the Social Security Act, as amended by 42 U.S.C. §§ 1396 and 1397 (1976). See Rev. Proc. 80-4, 1980-1 C.B. 581, as modified and amplified by Notice 2003-70, 2003-2 C.B. 916. If the service recipient is considered the employer of the service provider, Rev. Proc. 80-4 provides that no Form 2678 is required for the state agent to act as an agent under section 3504 on behalf of the service recipient. When a state agent files returns pursuant to 80-4 the returns are filed using the EIN acquired specifically to report and pay taxes with respect to HHCSRs. See Notice 95-18, 1995-1 C.B. 300, Q&A 5. A 1997 memorandum issued by the predecessor to this office concluded that a state agent may remit employment taxes paid on behalf of HHCSRs with a timely filed return and penalties for failure to deposit such taxes should not be assessed. See also Notice 95-18, Q&A 5, and Notice 2003-70, Q&A 14.

In 2003 the Service issued Notice 2003-70, a proposed revenue procedure regarding home-care service procedures, to provide updated guidance to state agents serving as agents under section 3504 for HHCSRs. Specifically, it provides, through a series of questions and answers, the procedures that apply when a state agent appoints another agent to perform payroll and employment tax functions for the HHCSRs. Notice 2003-70 takes into account that it had become a common practice for state agents to appoint another party as an agent of the state agent to handle certain of the employment tax responsibilities that the state agent had been performing for the service recipient. Notice 2003-70 identifies these other agents that are appointed as either a “subagent” or a reporting agent”. A “subagent” is defined as an individual or entity designated as an agent by a state agent in accordance with Rev. Proc. 70-6 and Notice 2003-70, and a “reporting agent” is defined as an accounting service, franchiser, bank, service bureau or other entity authorized to perform one or more acts on behalf of an employer, including sign and file Forms 940 and 941 and make Federal tax deposits for the taxes reported on those forms. Notice 2003-70 is consistent with the conclusion in the 1997

memorandum that state agents acting on behalf of HHCSRs may remit employment taxes paid on behalf of HHCSRs with a timely filed tax return.

To resolve whether Taxpayer is permitted to remit these employment taxes with timely filed returns depends upon whether Taxpayer is a state agent. Taxpayer receives all of its funding from federal, state and local government programs. Primary federal funding comes through Medicaid programs under Title XIX and XX of the Social Security Act administered by the Department of Health and Human Services. Taxpayer acts as agent directly for the HHCSRs. The program requires HHCSRs to employ individuals to provide services in their own home. All the program participants are low-income individuals with chronic and disabling conditions who need such assistance to remain living in their homes. In all respects, Taxpayer has complied with Rev. Proc. 80-4 and Notice 2003-70. Thus, Taxpayer is a state agent as contemplated in Rev. Proc. 80-4 and Notice 2003-70 and is permitted to remit employment taxes on behalf of HHCSRs when the employment tax return is due.

#### CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

Since the 1997 memorandum, two important changes occurred that required this office to examine whether Taxpayer may continue to remit with return. First, Taxpayer engaged a third-party, Corporation Z, to file the employment tax returns Taxpayer was filing as agent on behalf of the HHCSRs. Second, Notice 2003-70 was issued. Taxpayer confirmed that it has not filed with the Service a Form 2678, *Employer/Payer Appointment of Agent*, with respect to its relationship with Corporation Z.

It was necessary to examine the relationship of Corporation Z and Taxpayer in order to conclude that Corporation Z was not acting as subagent (as described in Notice 2003-70) for Taxpayer. If Corporation Z was acting in the capacity of a subagent, it would not be permitted to remit employment taxes with a return. See Notice 2003-70, Q&A 30.

Based on the provisions of the contract, the absence of a Form 2678, and the direct payment of the taxes by the Taxpayer, we conclude that Corporation Z is not acting as a subagent of the Taxpayer. The payroll functions that Corporation Z performs satisfy the definition of reporting agent in Notice 2003-70. Thus, Taxpayer's contractual arrangement with Corporation Z does not affect its authorization to remit taxes with the return.

We also understand that Taxpayer is currently not identified in the Service's systems as a government entity under the jurisdiction of the Tax-Exempt/Government Entities operating division. We recommend that appropriate steps be taken to identify the Taxpayer as a government entity and further to assign Taxpayer a Code A which should preclude the assessment of failure to deposit penalties. We note the Service's general caution in connection with the use of Code A and support taking steps to ensure that only appropriate entities are assigned Code A.

Our conclusion is based upon our understanding of the facts, our discussions with the Revenue Officer assigned to the case, and our interpretation of the contract between Taxpayer and Corporation Z. This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call me at (202) 622-6010 or Selvan Boominathan at (202) 622-0047 if you have any further questions.