



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
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The Honorable Lois Capps  
U.S. House of Representatives  
Washington, DC 20515

Attention:

Dear Mr. Capps:

I apologize for the delay in responding to your inquiry dated June 4, 2013, on behalf of your constituent, . asked about the applicability of employment taxes to the compensation of disabled individuals who perform services through a program operated by a certain non-profit entity.

Due to disclosure and privacy laws, we cannot provide specific tax information to anyone other than the taxpayer or the taxpayer's authorized representative without that individual's or organization's written authorization. However, I can provide general information on the applicability of employment taxes to "sheltered workshop programs" in which disabled individuals receive compensation for training or work.

Employment taxes include Federal Insurance Contributions Act (FICA) tax and federal income tax withholding. "Employment" means any service, of whatever nature, performed by an employee for the person employing him, with certain exclusions. An "employee" is any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee [Section 3121(d)(2) of the Internal Revenue Code]. Generally, an employment relationship exists for federal tax purposes if the service recipient has the right to direct and control the worker. [See Treasury Regulation sections 31.3121(d)-1, 31.3401(c)-1]. The question of whether an employment relationship exists is highly factual and must consider all the facts and circumstances of each particular case. Generally, if an employment relationship exists, the employer must withhold and pay federal employment taxes.

Our position on the applicability of employment taxes to compensation received by an individual performing services in a sheltered workshop is in Revenue Ruling 65-165, 1965-1 C.B. 466. In the first fact pattern in the ruling, individuals were given orientation and training for 16 weeks in a program designed to prepare them to work in private industry. The ruling found the individuals were not employees of the workshop for federal employment tax purposes while they were being trained.

In the second fact pattern, individuals who completed the training continued to work in the workshop, either while awaiting placement in private industry, or permanently if they could not find a job. The workshop paid the individuals, provided working conditions and pay scales comparable to those in private industry, and had fixed working hours and production schedules. The workers also received some benefits, and the workshop could discharge them if the work was not satisfactory. The ruling found that, under these facts, the individuals were employees for federal employment tax purposes.

In 1997, we issued a memorandum [PMTA-00171] affirming that Revenue Ruling 65-165 applies to sheltered workshops and similar programs, and that the ruling should be applied strictly to the facts of each particular case. Therefore, generally, the key in determining the employment status of disabled individuals is to determine which fact pattern the case at issue most closely resembles.

Taxpayers who employ individuals with disabilities can find information on the IRS.gov web site by entering the search term "sheltered workshop" and clicking on the link, "*Tax Benefits for Businesses Who Have Employees with Disabilities*." This page specifically addresses the classification of workers in sheltered workshops for employment tax purposes. Taxpayers whose dependent is a disabled individual working at a sheltered workshop can find information in Publication 17, *Your Federal Income Tax*.

We are aware that in certain cases other government agencies administer laws that require the determination of or presuppose that an employment relationship exists. However, we must make an independent determination of whether an employment relationship exists for federal tax purposes. Therefore, other federal agency's findings, such as a Department of Labor certificate on the applicability of the minimum wage, are not determinative for federal tax purposes.

I hope this information is helpful. Please contact me or  
if we can further assist you.

of my staff

Sincerely,

Paul J. Carlino  
Chief, Employment Tax, Branch 1  
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Chief Counsel (Tax Exempt & Government  
Entities)