



OFFICE OF
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR DISTRICT COUNSEL CC:

FROM: Branch Chief CC:EBEO:BR2

SUBJECT: Field Service Advice

This Field Service Advice responds to your memorandum dated December 10, 1998. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND:

City =

State =

ISSUE:

Whether members of advisory boards appointed by the City are "officers" under State law for purposes of section 3401(c) of the Code.

CONCLUSION:

Whether the members of the advisory boards are "officers" under state law is properly determined by District Counsel. If the board members are determined to be officers for federal income tax withholding purposes, it does not automatically follow that they are employees FICA tax purposes. For FICA tax purposes, the Service must determine whether the board members are common law employees.

FACTS:

Acting under authority granted by State statute, the City Council appoints citizens to several advisory boards, including the

. The City pays the board members for each meeting attended.

The City does not withhold income taxes from payments it makes to the board members. Nor does the City withhold or pay OASDI or Medicare tax from the payments. The City issues a Form 1099 to each board member who receives \$600 or more in a calendar year. The board members are not participants in the City's employee pension plan.

LAW AND ANALYSIS

Section 3401(a) of the Code provides that the term "wages" means all remuneration (other than fees paid to a public official) for services performed by an employee for his employer.

Section 31.3401(a)-2(b)(1) of the Employment Tax Regulations provides that authorized fees paid to public officials such as notaries public, clerks of courts, sheriffs, etc., for services rendered in the performance of their official duties are excepted from wages and hence are not subject to withholding. However, salaries paid to such officials by the Government, or by a Government agency or instrumentality, are subject to withholding. Section 31.3401(a)-2(b)(2) provides that amounts paid to precinct workers for services performed at election booths in State, county, and municipal elections and fees paid to jurors and witnesses are in the nature of fees paid to public officials and are therefore not subject to withholding.

Section 3402(a) provides that every employer making a payment of wages shall deduct and withhold federal income taxes.

Section 3401(c) provides that the term "employee" includes an officer, employee, or elected official of the United States, a state, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing.

Section 31.3401(c)-1(a) of the Employment Tax Regulations provides, in part, that the term "employee" includes officers and employees, whether elected or appointed, of the United States, a state, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing.

Under section 1402(c)(1), for purposes of the Self-Employment Compensation Act (SECA), the term “trade or business” generally does not include the performance of the functions of a public office. An exception exists for a public office that is compensated solely on a fee basis. Under Revenue Ruling 74-608, 1974-2 C.B. 275, the exception applies only with respect to fees received directly from the public.

Section 1.1402(c)(2) of the Income Tax Regulations provides guidance on the types of positions that are considered to be a public office. This section provides, in part, that the term "public office" includes any elective or appointive office of a state or its political subdivisions. Further, this section provides that, for example, a governor, a mayor, the Secretary of State, a county commissioner, a judge, a justice of the peace, a county or city attorney, or a notary public perform the services of a public office.

Revenue Ruling 61-113, 1961-1 C.B. 400, considers whether individuals serving as members of a hearing board of an air pollution control district are performing the functions of a public office. The members are appointed by the county board of supervisors, take an oath of office, hold public hearings, and submit their decisions to the county. They are not under the control and direction of the county board of supervisors or any other body. Their compensation is based upon the number of meetings they attend. The ruling concludes that the board members' services constitute the performance of the functions of a public office and therefore do not constitute a “trade or business” under section 1402(c)(1).

Whether the board members are officers under section 3401(c) is determined by reference to local law. Analysis of local law is properly handled by the Office of District Counsel. However, we provide the following information on the employment tax consequences if it is determined that the board members are officers under local law.

If the board members are determined to be officers under local law, then section 3401(c) provides that they are employees for income tax withholding purposes. However, fees paid to a public official are not wages subject to income tax withholding. Moreover, whether the board members are officers under section 3401(c) does not affect whether they are employees for OASDI or Medicare (FICA) tax purposes. Rather, whether the board members are employees for FICA purposes is determined based upon the common law standard. I.R.C. § 3121(d)(2).

Notwithstanding that a worker is an employee under the common law, the taxpayer may be entitled to relief from employment taxes under section 530 of the Revenue Act of 1978. We wish to draw your attention to two provisions under

section 530 that were added by section 1122 of the Small Business Job Protection Act of 1996 (SBJPA), Pub. L. No. 104-188. First, section 530(e)(3) provides that the availability of the safe harbors is not dependent upon the worker otherwise being an employee. Based upon this provision, the Service has taken the position that the first step in a worker-classification case is to determine whether the taxpayer is entitled to relief under section 530. Second, section 530(e)(2)(B) provides that the "industry practice" safe harbor under section 530(a)(2)(C) shall not require a reasonable showing of the practice of more than 25 percent of the industry. We note this provision because taxpayers often claim reliance on industry practice as a reasonable basis for treating a worker as a nonemployee. For further information on section 530 and worker-classification, see the training materials on employee versus independent contractor status. "Independent Contractor or Employee?" Training 3320-102 (Rev. 10-96) TPDS 842381.

If section 530 relief is not available, a state or local government employer will be subject to FICA with respect to a common law employee unless the employee is a member of a qualified retirement system or some other exception applies. I.R.C. § 3121(b)(7)(F). Under section 3121(b)(7)(F), to be excluded from the FICA, the employee must be a participant in a plan; it is not enough that the employer maintains a plan. For further information, see Publication 963, Federal-State Reference Guide (Social Security Coverage and FICA Reporting by State and Local Government Employers).

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS:

The guidelines under the State and Local Government Compliance Initiative provide that prospective treatment is the preferred approach to gaining taxpayer compliance. [REDACTED]

If you have any further questions, please call the branch telephone number.

Jerry E. Holmes
Branch Chief

Associate Chief Counsel (Employee
Benefits & Exempt Organizations)