

# PUBLICATION

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## IRS Announces Voluntary Worker Classification Settlement Program

September 26, 2011

On September 21, in Announcement 2011-64, the Internal Revenue Service (IRS) announced a new Voluntary Classification Settlement Program (VCSP), under which partial amnesty is offered to businesses utilizing the services of service providers who have been previously treated as independent contractors for federal employment tax purposes. The purpose of this VCSP is to allow eligible taxpayers (that is, service recipients) to voluntarily, and at least for federal employment tax purposes prospectively, reclassify their workers as employees. In exchange for the payment of a significantly reduced potential employment tax liability for past periods, service recipients must agree to treat a class of workers as employees going forward. In addition to the eligibility requirements for the VCSP, as briefly outlined below, there are a myriad of other implications outside the scope of federal employment tax that all taxpayers should consider prior to reclassifying any independent contractor as an employee.

### Eligibility and Effect

The VCSP is available to any service recipient that is willing to begin treating a class(es) of workers as employees for federal income tax purposes. This status change could apply to any worker(s) that the service recipient has previously treated as an independent contractor rather than as an employee. In order to be eligible for VCSP, the service recipient must have consistently not treated the worker(s) as employees in the past, and must have filed all required Forms 1099 for such workers in each of the past three years. Additionally, the taxpayer cannot be under audit by the IRS, nor can the taxpayer be under audit concerning worker classification by the Department of Labor or by a state government agency. Taxpayers who have previously been under any such audits will only be eligible if they are found to be compliant with the results of that audit.

By participating in VCSP and agreeing to prospectively treat the affected class of workers as employees, taxpayers are possibly able to insulate themselves from a federal tax audit risk, insofar as employment taxes for the workers to which the reclassification applies. In exchange, the service recipient must pay 10 percent of the employment tax liability that would otherwise be due on compensation paid to workers in the relevant class(es) in the most recent year, and to treat the class of workers as employees in the future. Taxpayers entering the VCSP must also agree to extend the period of limitations on assessment by three years for each of the first three calendar years that begin after the date which the taxpayer agrees under the VCSP to begin treating workers as employees.

### Application for the VCSP

Participation in the VCSP requires an application to the IRS through the filing of Form 8952. An application is required to be made at least 60 days in advance of a proposed date for a change in status of the class of service providers. The Form must be signed under penalties of perjury, generally by a sole proprietor, general partner of a partnership, fiduciary of a trust or estate, or certain corporate officers listed in the Form 8952 Instructions. The amount payable is calculated on Form 8952, with the 10% payment rate being applied to a portion of what both an employer and an employee would owe in payroll taxes for the relevant period. Any required payment is not to be made with the application to the IRS, but rather is to be remitted with a signed Closing Agreement which will be prepared by the IRS after acceptance of the application.

## Risks Associated With Worker Reclassification

Any taxpayer that is considering applying to the VCSP should carefully assess and weigh all potential risks associated with any worker reclassification, whether or not as part of the VCSP. Although some may consider the VCSP rather generous, it is important to remember that the IRS does not speak for the federal government as a whole, nor does the Service speak for any state governmental agency, nor for the workers themselves. A service recipient entering the VCSP certainly takes on risks. For example, what is the scope of the "class" which will be treated as employees? What is the effect of a failure to adhere strictly to a VCSP closing agreement with the IRS? What are the nature and extent of other economic exposures which may arise as a result of VCSP participation?

It should be noted that on September 19, 2011 the IRS and the U. S. Department of Labor (DOL) signed an agreement to share information regarding worker misclassification. The DOL, in turn, has indicated that it has similar agreements in place to share information with the Occupational Safety & Health Administration, the Office of Federal Contract Compliance Programs, the Office of the Solicitor, and several states. It is thus possible that the details of a taxpayer's participation in the VCSP will be shared by the IRS with the DOL and, in turn, shared by the DOL with other federal and state agencies, none of which has any apparent amnesty program for VCSP participants. Conversely, information provided to the DOL by other federal and state agencies may be shared with the IRS for audit and enforcement purposes. Remaining to be determined is whether these other federal and state agencies will interpret such prospective reclassification for VCSP purposes, and payment of the associated past employment taxes required under VCSP, as an admission that workers were classified incorrectly for other purposes in prior years.

For a more in-depth discussion of the issues and exposures associated with worker classification and reclassification, please see our [March 9, 2010](#) and [June 8, 2010](#) Tax Alerts, respectively.

## Conclusion

Although amnesty type programs requiring voluntary disclosures, such as the VCSP, can seem appealing at first sight, it is important to consider both the tax and the non-tax consequences of entering such a program. In the case of VCSP, other consequences could far outweigh any employment tax benefit gained by entering into the VCSP. The issues will involve not only whether, but also how, to structure any reclassification. Prior consultation with labor and employee benefit counsel is also advisable. To discuss the VCSP, or any of the ancillary tax consequences or other effects the VCSP may have based on your own, unique tax situation, please feel free to contact any of the attorneys within the Firm's Tax Department.