



Joint IRS and USDOL Initiative to "Crack Down" on the Misclassification of Workers

A recent initiative at the federal level may have an impact on the determinations of states with respect to whether individuals are "employees" to be covered for state workers' compensation and/or are in "employment" for purposes of state unemployment tax liability.

In the last few weeks, the Department of Labor and the Internal Revenue Service signed an MOU of cooperation <http://www.wage-hour.net/file.axd?file=2011%2f10%2fDOL+IRS+Memodandum+of+Understanding.pdf>. Seven states have joined the effort and more are expected to participate in the program to identify and potentially prosecute employers who intentionally misclassify workers as independent contractors in order to evade compliance with labor laws.

"We're here today to sign a series of agreements that together send a coordinated message: We're standing united to end the practice of misclassifying employees," said Labor Secretary Hilda Solis during a signing ceremony on Sept. 19.

Two days later, the IRS announced a "[Voluntary Classification Settlement Program](#)," as an amnesty program for employers with freelancers and independent contractors who want to convert them to employees.

Employers who agree to the voluntary reclassification and meet the eligibility requirements will pay 10 percent of the employment tax that otherwise was likely to have been due on the compensation for the most recent tax year. They also won't have to pay any interest and penalties on the federal employment tax liability, and, they won't be audited for back taxes on the employee classification of prior years.

The voluntary program is similar to the current [Classification Settlement Program](#), with the key exception being that it applies to businesses that are **not** now under audit by the IRS.

Employers and states should review the details of these agreements and the voluntary classification settlement program to avoid unintended consequences under the state unemployment and workers' compensation law of "settlements". Determinations under federal unemployment tax law may be inconsistent with definitional determinations under state UI law and result in mismatches for purposes of FUTA offset credit or determinations of taxable wage upon which state unemployment taxes are applied.

Determinations under the Fair Labor Standards Act or for federal employment tax law may impact determinations as to whether individuals are "employees" under state workers' compensation law.