

# THE JOB DESCRIPTION

## 1099 Misclassification and IRS Amnesty Program

Worker misclassification occurs when a worker is not classified as an employee, but should be. Some forms of misclassification occur when workers are not reported at all, such as when working off the books or being paid under the table in cash. Misclassification also occurs when workers are classified incorrectly as independent contractors.

Employers that misclassify employees as independent contractors cut costs by not paying unemployment contributions, workers' compensation insurance, payroll taxes, or social security withholdings.

The consequences for knowing misclassification are harsh. Missouri employers that knowingly misclassify their employees face penalties in the amount of \$50 to \$1,000 per day per misclassified worker, and/or up to six months in jail per violation.

The Missouri Division of Employment Security can penalize an employer 25% of the amount the state has been defrauded. If an employer classifies an employee as an independent contractor and does not have a reasonable basis for doing so, the employer will be held liable for unemployment taxes for that worker. Knowingly failing to insure workers' compensation liability under the law is a Class A misdemeanor, and is also punishable by a civil penalty of up to three times the annual premium the employer would have paid had it been insured or up to \$50,000, whichever is greater.

While there are many factors that assist in the determination of whether a worker is an employee or independent contractor, there is no clear definition of what constitutes an independent contractor. Whether a worker is performing services as an employee or as an independent contractor depends upon the facts and circumstances and is generally determined under the common-law test of whether the service recipient has the right to direct and control the worker as to how to perform the services. Understandably, companies sometimes misclassify workers as independent contractors as they attempt to navigate through the current

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rules. To determine whether a worker is classified correctly, the best guide is the IRS 20-factor test to identify his or her legal status.

In Missouri in 2011, 5,899 misclassified workers were identified. These workers were employed by 874 employers. Those employers owed an additional \$837,593.23 due to misclassification.

The Missouri Department of Labor Director has joined forces with the U.S. Department of Labor and the IRS to tackle 1099 fraud. Congress also has introduced a bill that would create new record-keeping requirements for employers that hire independent contractors and impose stricter penalties for misclassification.

Meanwhile, the IRS has announced a Voluntary Classification Settlement Program, which will be attractive to some employers who have been misclassifying workers as independent contractors. The Program provides taxpayers a new opportunity to reclassify as employees workers who have been incorrectly treated as independent contractors for employment tax purposes, with partial relief from back federal employment taxes.

The Program permits the prospective reclassification of workers as employees, with reduced federal employment tax liabilities for past nonemployee treatment. The Program allows business and tax examiners to resolve the worker classification issues as early in the administrative process as possible, thereby reducing taxpayer burden and providing efficiencies for both the taxpayer and the government.

The Program is available to companies who currently treat a worker or group of workers as independent contractors or other nonemployees and want to treat the workers as employees going forward. To be eligible, companies must have consistently treated the workers they wish to reclassify as nonemployees or independent contractors for tax purposes. This means the company must have filed Forms 1099 for each of the workers for the previous three tax years. In addition, the company cannot be under audit by the IRS, Department of Labor, or state government agency. A taxpayer who was previously audited by



the IRS or the Department of Labor concerning the classification of the workers (or class of workers) in question will only be eligible if the taxpayer has complied with the results of that audit.

Under the Program, if a company agrees to voluntarily reclassify a worker (or class of workers), the company will pay 10% of the employment tax liability that may have been due on compensation paid to the worker for the most recent tax year as determined by Internal Revenue Code Section 3509. The taxpayer will not be liable for any interest and penalties on the liability, and will not be subject to an employment tax audit with respect to the worker classification of the workers for prior years.

If a company wishes to enter into the Program, it must complete the appropriate application with the IRS. Companies that are accepted by the IRS into the Program will enter into a closing agreement with the IRS and simultaneously make full and complete payment of any amount due under the closing agreement.

Companies should review their independent contractor arrangements to determine if they have properly classified their workers. If a company believes that workers are improperly classified, the IRS's new Program may be a good option. Reclassifying workers through the Program or other means, however, can have additional nontax ramifications that should also be considered, such as workers' compensation coverage and entitlement to unemployment benefits.

## Illinois Workers' Compensation System Overhauled

Each year in Illinois, roughly 200,000 work-related accidents occur, according to the Illinois Workers' Compensation Commission. Employers pay for workers' compensation benefits through insurance policies or self-insurance, but they have long complained about the high costs of treating employees.



### Legislative Update

To help commemorate National Domestic Violence Awareness Month, U.S. Rep. Lynn Woolsey (D-CA) introduced the Domestic Violence Leave Act (H.R. 3151), which would allow an employee to take Family and Medical Leave Act ("FMLA") leave to address acts of domestic violence, sexual assault, and stalking aimed at themselves, a spouse, parent, or child. FMLA leave could be used to seek medical attention for injuries, obtain legal assistance, participate in legal proceedings, attend support groups or therapy, and participate in safety planning.

Another leave bill, the Healthy Families Act (H.R. 1876, S. 984) would require employers to provide paid sick leave and paid leave for employees who are the victims of domestic violence, sexual assault, or stalking.

Recently, Governor Pat Quinn signed into law amendments to the Illinois Workers' Compensation Act in an effort to reduce workers' compensation costs. In 2010, Illinois had the third highest workers' compensation premium costs in the nation, the Belleville News-Democrat reported. Highlights of this new system include:

- **Medical Payments:** Reimbursements to doctors and hospitals were cut by 30% from the current fee schedule. The Illinois State Medical Society warns that reducing reimbursements will discourage physicians from treating injured workers. If fewer doctors are willing to treat injured workers, care becomes more complicated and more expensive, the Society said. The Department of Insurance expects up to 10% reductions on employer insurance premiums because of the 30% cut in medical fees.
- **Medical Care:** An employer may establish preferred provider programs, or PPPs, of medical providers approved by the Department of Insurance. Employees have two choices of doctors in the employer's network. Employees may opt out of the PPP in writing at any time. If employees opt out, they only have one doctor choice outside the network. An employer has first dibs on medical treatment by adopting a PPP, but employees' choice of doctor would be limited. Restricting doctor choice could result in delayed care or prolonged treatment.
- **Disability:** Before, when an employee returned to regular work but had a permanent limitation or restriction, Illinois provided for an assessment known as permanent partial disability ("PPD"). An employee's complaints and factors such as age and nature of the injury were considered in the analysis. Under the new system, to determine PPD, an arbitrator will look at five factors: occupation, age, future earning capacity, evidence of disability, and level of impairment based on American Medical Association guidelines. Critics say AMA guidelines have not been used before to determine PPD and are designed to rate impairment, which is not the same as disability. For example, the guidelines give a 55-year-old man with a torn bicep a 4% impairment rating. For an office worker, a 4% impairment may be acceptable. For someone using a jackhammer or screwdriver, that person may be considered work disabled.

Additionally, Gov. Quinn removed eight of Illinois' 31 workers' compensation arbitrators, as part of a reform package. Gov. Quinn promised that a new group of arbitrators "will be the most credentialed and experienced group of professionals Illinois has ever had in place to judge workers' compensation cases."



## Military Spouses Who Relocate Can Now Get Unemployment Benefits in Missouri

A new Missouri law allows the accompanying spouse of an active member of the military to be eligible for unemployment benefits in the event of a military transfer.

“Missouri is the proud home of Fort Leonard Wood and Whiteman Air Force Base. Each year, our military families face moves from base to base for the good of our national defense and these transfers cause unique financial pressures. In many cases, the

non-military spouses may have to leave their employment due to a military transfer. Generally, individuals in Missouri that voluntarily quit their employment to move with a spouse are ineligible for unemployment benefits. This new law recognizes that spouses of military service personnel who must quit their jobs due to a military transfer are not quitting voluntarily but for the good of our nation. With this new law, the state is recognizing the sacrifices of military families who are relocating,” said Missouri Department of Labor Director Larry Rebman.

Before this new law, military spouses were not able to collect unemployment in Missouri if they left their jobs to travel with their spouses to a new duty station. Missouri is the 39th state to allow military spouses to file for unemployment benefits until they find full-time work. Illinois already has a similar law.

Based on 2010 figures, this new law will provide benefits to more than 200 military families a year.



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