



IRS to tighten Compliance with Voluntary Program to Classify Workers as Employees

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The Tax Inspector General for Tax Administration (TIGTA) has issued a report on IRS's Voluntary Classification Settlement Program (VCSP). The report provided a number of recommendations to improve compliance with the program on the part of participating employers, all of which were agreed to by IRS.

Background on the VCSP:

The VCSP allows many businesses, tax-exempt organizations, and government entities that currently treat their workers, or a class or group of workers, as nonemployees or independent contractors, to prospectively reclassify workers as employees under generous settlement terms. Participation in the program is voluntary.

Taxpayers must meet certain requirements to participate in the program, including:

- (1) they must have consistently treated the workers in the past as nonemployees;
- (2) they must have filed all required 1099 forms for the workers for the previous three years;
- (3) they must not be currently under audit for employment taxes by IRS; and
- (4) they must not be currently under audit by the federal Department of Labor (DOL) or a state agency with respect to the classification of these workers.

Interested employers apply for the program by filing Form 8952, *Application for Voluntary Classification Settlement Program (VCSP)*. Employers accepted into the program will pay an amount effectively equaling just over 1% of the wages paid to the reclassified workers for the past year. Employers accepted into the program will not be audited for prior years on payroll taxes related to these workers.

Report findings:

TIGTA found that IRS does not obtain the information that it needs to verify the accuracy of applications and payments. Specifically, IRS does not require employers to provide information on the VCSP application that identifies the specific workers who are being reclassified, such as the workers' names and Social Security numbers. Without the specific worker identification numbers, IRS cannot determine if the applicant met the VCSP eligibility requirements. In addition, IRS is unable to verify the accuracy of the compensation amount reported on the application, and, ultimately, the applicant's computation of the VCSP payment amount owed. Without identifying information for the workers being reclassified, IRS is also unable to establish an effective process to monitor VCSP agreements to ensure employer compliance.

The report noted that the VCSP verification detailed in IRS procedures is not the same as the requirement that must be met for an employer to participate in the VCSP, which is that the employer filed all 1099 forms for the previous three years for the workers to be reclassified. IRS internal procedures only instruct tax compliance officers reviewing VCSP applications to ensure that the employer filed 1099 forms for each of the three previous years, rather than all 1099 forms for each of the previous three years *for the workers to be reclassified*. The verification process is also hampered by the fact that the tax compliance officer reviewing the application is not expected to validate the taxpayer's computations.

In addition, TIGTA found that IRS processes to track and monitor program applications are ineffective and not always accurate, and the follow-up review control logs do not always reflect accepted agreements.

IRS agrees with report findings:

IRS agreed with all of TIGTA's recommendations to improve the program. IRS plans to revise the VCSP application to instruct employers to provide worker identification information. IRS will also revise its internal procedures to use this worker identification information to evaluate eligibility for the program and compliance with VCSP agreements. In addition, IRS plans to implement reporting capabilities for the Reporting Compliance Case Management System to allow for a single inventory system for inventory tracking and monitoring program performance. IRS also noted that it has developed and implemented internal procedures to ensure that inventory is accurately input and agreements are transferred to the appropriate business units for compliance monitoring.

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