

Updated Procedures for Processing Employment Tax Cases Involving Worker Classification and Section 530 of the Revenue Act of 1978 Under Section 7436 of the Internal Revenue Code

Notice 2002-5

PURPOSE

Section 314(f) of the Community Renewal Tax Relief Act of 2000 (“CRTRA ’00”) (H.R. 5662, incorporated in H.R. 4577, the Consolidated Appropriations Act 2001), Pub. L. No. 106-554, 112 Stat. 2763, 2762A-643 (2000), amended § 7436 of the Internal Revenue Code (Code) to expand, retroactively to August 5, 1997, the subject matter jurisdiction of the Tax Court in employment status proceedings. This notice provides information about when and how the Internal Revenue Service (Service) will issue a Notice of Determination of Worker Classification (Notice of Determination) and how taxpayers petition for Tax Court review of the determinations under Code § 7436. This notice modifies and supercedes Notice 98-43 (1998-2 C.B. 207).

BACKGROUND

The Taxpayer Relief Act of 1997 (“TRA ’97”), Pub. L. No. 105-34, 111 Stat. 788, created § 7436 of the Code, which provides Tax Court review rights concerning certain employment tax determinations. As originally enacted, § 7436 authorized the Tax Court only to review determinations by the Service that a taxpayer’s workers should be classified as employees for purposes of subtitle C (which governs employment taxes) of the Code, or that the taxpayer for whom the services were performed is not entitled to treatment under section 530(a) of the Revenue Act of 1978 (which relieves a

taxpayer of employment tax liability in certain circumstances)¹. Section 7436(a) requires that the determination(s) involve an actual controversy and that the determination(s) be made as part of an examination.

By § 314(f) of CRTRA ’00, Code § 7436(a) was amended retroactively to August 5, 1997. The jurisdiction given to the Tax Court by the original legislation was retained, but CRTRA ’00 also authorized the Tax Court to determine the proper amount of employment tax under the determinations of worker status and section 530 treatment.

ISSUES TO WHICH § 7436 APPLIES

Section 7436(a) provides that for purposes of subtitle C of the Code, the Tax Court has jurisdiction to:

- (1) review the Service’s determination that one or more individuals performing services for the taxpayer are employees;
- (2) review the Service’s determination that the taxpayer is not entitled to treatment under § 530(a) of the Revenue Act of 1978 with respect to those individuals; and
- (3) determine the proper amount of employment tax under the above determinations.

The employment taxes imposed by subtitle C of the Code are Federal Insurance Contributions Act (FICA) taxes (under Code §§ 3101-3128), the Railroad Retirement Tax Act (RRTA) taxes (under Code §§ 3201-3232), the Federal Unemployment Tax Act (FUTA) taxes (under Code §§ 3301-3311), the Railroad Unemployment Repayment Tax (RURT) taxes (under Code §§ 3321-3322), and the collection of income tax at source on wages (under Code §§ 3401-3406). “Employment tax” under the statutory language includes the additions to tax, additional amounts, and penalties provided by chapter 68A of the Code (§§ 6651-6665). Thus, the Tax Court has jurisdiction to determine the proper amount of the additions to tax, additional amounts, and penalties that relate to the employment tax

imposed by subtitle C with respect to determinations of worker classification and § 530 treatment.

Section 7436(a) does not provide the Tax Court with jurisdiction to review any employment tax determinations other than the three listed in the statute. The procedures set forth in § 7436 do not apply to employment status issues not arising under Subtitle C, such as the classification of individuals for purposes of pension plan coverage or the proper treatment of individual income tax deductions. Nor is Tax Court review available when there is no controversy with respect to the classification of workers, such as where the taxpayer itself treated the workers as employees by issuing them Forms W-2 (*Wage and Tax Statements*). Additionally, since § 7436(a) only confers jurisdiction upon the Tax Court to review determinations that are made by the Service as part of an examination, other Service determinations of employment status (including those that are made in the context of private letter rulings, technical advice memoranda or Forms SS-8 [*Determination of Employee Work Status for Purposes of Federal Employment Taxes and Income Tax Withholding*]) that are not made as part of an examination are not subject to review by the Tax Court under § 7436(a).

The Service will issue a Notice of Determination only after the Service has determined *both* that the taxpayer is not entitled to § 530 treatment and that one or more individuals performing services for the taxpayer are employees for purposes of subtitle C. The amount of employment tax under those determinations will also be determined and set forth in the Notice of Determination.

TAXPAYERS ELIGIBLE TO SEEK TAX COURT REVIEW

Section 7436(b) of the Code provides that a pleading seeking Tax Court review of the Service’s determinations may be filed only by “the person for whom the services are performed.” Thus, workers

¹ That statutory language of section 530 of the Revenue Act of 1978, as amended, although not codified in the Internal Revenue Code of 1986, can usually be found in the publisher’s notes following Code § 3401(a).

may not seek review of the Service's determinations under § 7436. In addition, because the statute specifies that there be an actual controversy that the workers performing services "for such person" are employees "of such person," review may not be sought by a third party that has not been determined by the Service to be the employer of the workers.

NOTICE OF DETERMINATION OF WORKER CLASSIFICATION

The Service will provide taxpayers with notice of a determination described in § 7436(b) of the Code by sending the taxpayer, by certified or registered mail, a "Notice of Determination of Worker Classification."² A copy of the new Notice of Determination is attached hereto as Exhibit 1.

The Notice of Determination advises taxpayers of the opportunity to seek Tax Court review and provides information on how to do so. The Notice of Determination will include a schedule describing which workers the Service has determined should be classified as employees. The Notice of Determination will also show each kind of tax with its proposed employment tax adjustment by taxable period.

In most cases, a taxpayer who receives a Notice of Determination will have previously received a "thirty-day letter," which the Service sends to taxpayers in unagreed examination cases. The thirty-day letter lists the proposed employment tax adjustments to be made, and describes the taxpayer's right either to agree to the proposed employment tax adjustments or, alternatively, to protest the proposed adjustments to the Appeals function ("Appeals") of the Service within thirty days of the date of the letter. If the taxpayer does not respond to the thirty-day letter by agreeing to the proposed adjustments or, alternatively, by filing a protest to Appeals, the taxpayer will receive, by certified or registered mail, a Notice of Determination. Under normal procedures, if the taxpayer does not respond to the thirty-day letter, the taxpayer should generally expect to receive the Notice of

Determination within sixty days after expiration of the thirty-day period beginning with the date on the thirty-day letter. If no Notice of Determination is received during this period, the taxpayer may wish to contact the Internal Revenue Service office that issued the thirty-day letter to check on the status of the case.

If the taxpayer responds to the thirty-day letter by filing a protest to Appeals (or if the case proceeds to Appeals by way of the employment tax early referral procedures, *see* Announcement 97-52, 1997-21 I.R.B. 22, Announcement 96-13, 1996-12 I.R.B. 33, Rev. Proc. 96-9, 1996-1 C.B. 575) and the worker classification and § 530 treatment issues are not settled on an agreed basis in Appeals, the taxpayer will thereafter receive a Notice of Determination. Taxpayers are encouraged to resolve cases in nondocketed status by requesting use of the early referral procedures in appropriate cases.

PREREQUISITE FOR SEEKING TAX COURT REVIEW

Because the Notice of Determination constitutes the Service's determination described in § 7436(a), the Notice of Determination is a jurisdictional prerequisite for seeking Tax Court review of the Service's determinations regarding worker classification, § 530 treatment, and the proper amount of employment tax under those determinations. Tax Court proceedings seeking review of these determinations may not be commenced prior to the time the Service sends the Notice of Determination by certified or registered mail.

TIME BY WHICH PETITION MUST BE FILED

Section 7436(b)(2) provides that a taxpayer's petition for review must be filed with the Tax Court before the 91st day after the Service mails its Notice of Determination by certified or registered mail. On the first page of the Notice of Determination, the Service will specify the last date by which the taxpayer may timely file a petition in the Tax Court. If

the taxpayer discusses the case with the Service during the period before the 91st day following the mailing of the Notice of Determination, the discussion will not extend the period during which the taxpayer may timely file a petition with the Tax Court.

A taxpayer who does not file a Tax Court petition within the allotted time retains the right to seek judicial review of the Service's determinations by paying the tax and filing a claim for refund, as required by § 7422 of the Code. If the claim for refund is denied, or if after six months the Service has not responded to the claim for refund, the taxpayer may file a refund suit in district court or the Court of Federal Claims.

APPEALS CONSIDERATION

Cases docketed in the United States Tax Court will be referred by Area Counsel to the Appeals function for consideration of settlement unless the Notice of Determination was issued by Appeals. Cases in which Appeals issued such a Notice of Determination may be referred to Appeals unless Area Counsel determines that there is little likelihood that a settlement of all or a part of the case can be achieved in a reasonable period of time.

SMALL TAX CASE PROCEEDINGS

At the option of the taxpayer, and with the concurrence of the Tax Court, employment status proceedings under § 7436 may be conducted pursuant to the Tax Court's simplified procedures for small tax cases, if the amount of employment taxes placed in dispute is \$50,000 or less for each calendar quarter involved. The simplified procedures for small tax cases are set forth in § 7463 of the Code and Rule 295 of the Tax Court's Rules of Practice and Procedure.

SUSPENSION OF STATUTE OF LIMITATIONS

Section 7436(d)(1) provides that the suspension of the limitations period for assessment in Code § 6503(a) applies in

² The original notice was called "Notice of Determination Concerning Worker Classification Under § 7436." The title has now been simplified to "Notice of Determination of Worker Classification."

the same manner as if a notice of deficiency had been issued. Thus, the mailing of the Notice of Determination by certified or registered mail will suspend the statute of limitations for assessment of taxes attributable to the worker classification and § 530 treatment issues. The statute of limitations for assessment is suspended for the 90-day period during which the taxpayer can begin a suit in Tax Court, plus an additional 60 days thereafter. Moreover, if the taxpayer does file a timely petition in the Tax Court, the statute of limitations for assessment will be suspended until the decision of the Tax Court becomes final and for 60 days thereafter.

RESTRICTIONS ON ASSESSMENT

Section 7436(d)(1) provides that various restrictions on assessment in Code § 6213 apply in the same manner as if a notice of deficiency had been issued.³ Thus, after the Notice of Determination is mailed, the Service is precluded from assessing the taxes identified in the Notice of Determination prior to expiration of the 90-day period during which the taxpayer may file a timely Tax Court petition.⁴ If the taxpayer does not file a timely Tax Court petition before the 91st day after the Notice of Determination was mailed, the employment taxes identified in the Notice of Determination shall thereafter be assessed.

AGREED SETTLEMENTS

If the taxpayer wishes to settle the worker classification, § 530 treatment, and amount of employment tax issues on an agreed basis, either before issuance of the Notice of Determination, or after issuance of the Notice of Determination but before expiration of the 90-day period for filing a Tax Court petition, the taxpayer must formally waive the restrictions on assessment contained in Code §§ 7436(d)(1) and 6213(a). This will generally be accomplished by execution of an agreed settlement that contains the following language:

I understand that by signing this agreement, I am waiving the restrictions on assessment provided in section 7436(d) and 6213(a) of the Internal Revenue Code of 1986.

The Service will not assess employment taxes attributable to worker classification or § 530 treatment issues unless either the Service has issued a Notice of Determination to the taxpayer and the 90-day period for filing a Tax Court petition has expired, or, alternatively, the taxpayer has waived the restrictions on assessment. If the Service erroneously makes an assessment of taxes attributable to worker classification and § 530 issues without first either issuing a Notice of Determination or obtaining a waiver of restrictions on assessment from the taxpayer, the taxpayer is entitled to an auto-

matic abatement of the assessment. However, once any such procedural defects are corrected, the Service may reassess the employment taxes to the same extent as if the abated assessment had not occurred.

EFFECTIVE DATE

Section 1454 of TRA '97 and § 314(f) of CRTRA '00 are effective as of August 5, 1997. Assessments that were made prior to the August 5, 1997, effective date are not subject to the procedures discussed above. All employment tax examinations involving worker classification and/or § 530 treatment issues that were pending as of August 5, 1997, are subject to Code § 7436, as amended.

COMMENTS

The Service invites comments with respect to the attached Notice of Determination, as well as with respect to any procedural issues contained in this notice. Written comments should be submitted to

Linda E. Mosakowski
Office of Chief Counsel,
Internal Revenue Service
1111 Constitution Avenue, N.W.
(CC:TEGE:EOEG:ET2)
Washington, D.C. 20224.

For further information regarding this notice contact Linda E. Mosakowski at (202) 622-6040 (not a toll-free call).

³ Only the principles of subsections (a), (b), (c), (d), and (f) of § 6213 apply to the employment status proceedings under § 7436.

⁴ The Service may immediately assess proposed employment tax amounts that do not arise as a result of a determination by the Service that an individual is an employee of the taxpayer. To the extent the employment taxes relate to individuals the taxpayer was already treating as employees, those tax amounts would not be included in the Notice of Determination and thus, assessment of those taxes would not be restricted by section 6213 (a).

EXHIBIT 1

Internal Revenue Service

IRS Contact Person

Name:

Telephone Number:

Identification Number:

Location Symbols:

Last Day to File a Petition With the United States Tax Court:

Taxpayer Identification Number:

NOTICE OF DETERMINATION OF WORKER CLASSIFICATION

Dear

This letter is your Notice of Determination of Worker Classification (“Notice”), as required by law, to notify you (before assessment) that we have determined that you owe additional employment tax, additions to tax, and/or penalties for the tax periods identified below.

We have made three determinations:

- we have determined that for purposes of federal employment taxes, the individual(s) described or listed in Table 1 below are to be legally classified as employees for the tax periods indicated;
- we have determined that with respect to such individual(s) you are not entitled to relief from employment tax under the treatment described in section 530(a) of the Revenue Act of 1978; and
- we have determined that for the tax periods indicated, you owe additional employment tax, additions to tax, and/or penalties in the amounts set forth in Table 2 following the list of re-classified individuals. (Please be aware that the figures on Table 2 do not include the interest that is required by law to be imposed on underpayments of tax.)

EXHIBIT 1

Table 2 indicates the proper amount of employment tax, additions to tax, and/or penalties that arises from the classification of the above-listed individuals as employees. Please note that these figures do not include the interest that accrues on the underpayment of tax.

TABLE 2

Tax Period Ending

Year	Type of Tax	March 31	June 30	Sept 30	Dec. 31	TOTAL
	Old Age, Survivor, Disability Insurance	\$	\$	\$	\$	\$
	Hospital Insurance					
	Income Tax Withholding					
	Federal Unemployment Tax Act					
	Addition to Tax I.R.C. §					
	Addition to Tax I.R.C. §					
	Penalty I.R.C. §					
	TOTAL					
	Old Age, Survivor, Disability Insurance					
	Hospital Insurance					
	Income Tax Withholding					
	Federal Unemployment Tax Act					
	Addition to Tax I.R.C. §					
	Addition to Tax I.R.C. §					
	Penalty I.R.C. §					
	TOTAL					
	Old Age, Survivor, Disability Insurance					
	Hospital Insurance					
	Income Tax Withholding					
	Federal Unemployment Tax Act					
	Addition to Tax I.R.C. §					
	Addition to Tax I.R.C. §					
	Penalty I.R.C. §					
	TOTAL					

If you want to contest any or all of our three determinations in the United States Tax Court, you must file a petition with the United States Tax Court by the date indicated on the first page of this letter as the “Last Day to File a Petition With the United States Tax Court.” You may mail the petition to the Tax Court (and/or write to the court with questions about the Tax Court proceedings) at the following address:

United States Tax Court
 400 Second Street, N.W.
 Washington, DC 20217

The time you have to file a petition with the Tax Court (that is, before the 91st day after the letter is mailed) is set by law and cannot be extended or suspended. Therefore, contacting the Internal Revenue Service (IRS) or contacting the Tax Court for more information, or receiving other correspondence from the IRS, will not change the period for filing a petition with the Tax Court.

We have enclosed several documents with this Notice of Determination of Worker Classification. Forms 4666, 4667, and/or 4668 provide details on how we calculated the amount of your additional employment tax liability. Form 2504–WC is a waiver form that you may use if you decide not to file a petition in the Tax Court. Sending us a signed Form 2504–WC gives us permission to assess the proposed amounts quickly and can help limit the accumulation of interest. Publication 3953, “*Questions & Answers About Tax Court Proceedings for Determination of Employment Status Under I.R.C. § 7436*” provides details about this Notice and the Tax Court proceedings.

If you have any questions about this letter, you may write to the person whose name and IRS address are shown on the front of this letter. If you write, please include your telephone number, the best time for us to call you if we need more information, and a copy of this letter to help us identify your account. Keep the original letter for your records.

If you prefer, you may call the IRS contact person at the telephone number on the front page of this letter. If this number is outside your local calling area, there will be a long distance charge to you. You may call the IRS telephone number listed in your local directory. An IRS employee there may be able to help you, but the contact person at our address shown on this letter is most familiar with your case.

You also have the right to contact a Taxpayer Advocate. If you believe that your tax matter is not being resolved through established IRS procedures or you are suffering or about to suffer a significant hardship, a Taxpayer Advocate may assist you in getting your tax matter addressed in a prompt and proper manner. A Taxpayer Advocate, however, does not have the ability to reverse legally correct tax determinations, extend the time fixed by law for filing a petition in the United States Tax Court, or act as a substitute for established IRS procedures, such as the formal appeals process. If you would like to contact a Taxpayer Advocate for assistance, please refer to section 12 of the enclosed Publication 3953 for the address and telephone number of your local Taxpayer Advocate.

Thank you for your cooperation.

Sincerely,

Commissioner
By