

# ONCAMPUS

Presented by the Higher Education Law Team of Whyte Hirschboeck Dudek S.C.

## COLLEGES AND UNIVERSITIES MAY VOLUNTARILY RECLASSIFY WORKERS AS EMPLOYEES UNDER NEW IRS SETTLEMENT PROGRAM

*Institutions may have unknowingly incurred hidden tax liabilities over time*

Colleges and universities have long struggled with the legal issues surrounding whether certain service providers for the institution should be properly classified as an employee or an independent contractor. In particular, senior administrators have been perplexed in applying the various tax rules to the unique service provider relationships found on many campuses, such as those involving the following:

- Part-time temporary faculty
- Instructors in non-degree professional development programs
- Consultants who perform management or supervisory functions
- Coaches, including assistant and part-time coaches
- Teaching and research assistants
- Laborers performing temporary or seasonal work
- Interns and research fellows
- Dual status workers (those considered both an employee and a contractor)
- Foreign students performing services on campus

To the extent that colleges and

universities have misunderstood or misapplied the various tax rules relating to the classification of service providers, such institutions have been incurring “hidden” tax liabilities year after year.

On September 21, 2011, the Internal Revenue Service (IRS) issued Announcement 2011-64 describing a new voluntary compliance program to permit institutions – including colleges and universities – to voluntarily reclassify workers as employees for federal employment tax purposes. The Voluntary Classification Settlement Program (VCSP) allows eligible institutions to voluntarily reclassify their workers for federal employment tax purposes and obtain relief similar to that obtained in the current Classification Settlement Program (CSP).

For institutions under examination, the current CSP is available to resolve federal employment tax issues related to worker misclassification, if certain criteria are met. In general, the CSP allows prospective reclassification of workers as employees, with reduced federal employment tax liabilities for past nonemployee treatment.

Under the VCSP, the IRS seeks to



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facilitate voluntary disclosure and resolution of worker classification issues and achieve compliance and certainty for employers. The VCSP allows for voluntary reclassification of workers as employees outside of the examination context and without implementing the typical correction procedures applicable to employment taxes.

### **Program Eligibility**

The VCSP is optional and voluntary. In order to request prospective reclassification of workers as employees with limited federal employment tax liability for the past independent contractor treatment, the institution must:

- Meet certain eligibility requirements;
- Apply to participate in VCSP; and
- Enter into a closing agreement with the IRS.



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In particular, the institution must be treating the workers as independent contractors and must have consistently treated the workers as nonemployees, including having filed any required Forms 1099 with respect to each of the workers for the past three years. In addition, the institution cannot be currently under audit by the IRS and cannot be under audit by the Department of Labor or any state agency regarding the classification of the workers. However, an institution that was previously audited by the IRS or the Department of Labor concerning the classification of the workers may be eligible for the VCSP if the institution has complied with the results of the IRS or Department of Labor audit.

### Application Process

Applying for the VCSP is relatively straightforward. The institution must complete and submit an application, using [Form 8952, Application for Voluntary Classification Settlement Program](#). The application should be filed at least 60 days from the date the institution wants to begin treating its workers as employees. No payments are due with the submission of the VCSP. Once submitted, the IRS will review the application and verify the institution's eligibility. If accepted, the IRS will contact the institution (or the institution's authorized representative if an executed power of attorney was submitted with Form 8952) to execute a closing agreement with the IRS. After execution of the closing agreement, the institution must make full and complete payment of the amount due under the VCSP.

### Computing the Amount Due

In general, payment under the VCSP is 10% of the amount of employment taxes calculated with certain reduced rates under the Internal Revenue Code for the compensation paid for the most recent tax year to the workers being reclassified under the VCSP. The effective tax rate for compensation up to the Social Security wage base is 10.68% in 2010 (applies under the VCSP in 2011) or 10.28% in 2011 (applies under the VCSP in 2012), and 3.24% for compensation above the Social Security wage base (applies under VCSP in 2011 and 2012).

Example: in 2010 WI College paid \$150,000 to workers that are the subject of the VCSP. All of the workers that are the subject of the VCSP were compensated at or below the Social Security wage base (e.g., under \$106,800 for 2010). WI College submits the VCSP application on October 1, 2011 and WI College wants the beginning date of the quarter for which its want to treat the class or classes of workers as employees to be January 1, 2012. WI College looks to amounts paid to the workers in 2010 for purposes of calculating the VCSP amount. The employment taxes applicable to \$150,000 would be \$16,020 (10.68% of \$150,000).

Under the VCSP, WI College's payment would be 10% of \$16,020, or \$1,602.

### Action Steps

We recommend that senior administrators immediately consult with legal counsel to determine the advantages and disadvantages of the

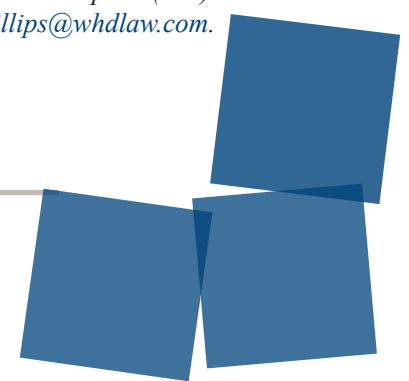
VCSP. A decision to apply for the VCSP may hinge upon a detailed analysis of the following:

1. The institution's federal employment tax liability exposure for prior years for individuals classified as independent contractors.
2. Additional future costs of treating the workers as employees, such as costs associated with unpaid wages (e.g., overtime), employee benefit eligibility and workers compensation.
3. Application and possible extension of the statute of limitations.
4. The institution's history of filing Forms 1099 to report compensation of individuals as independent contractors.
5. The potential exposure to tax and non-tax claims by state regulatory agencies.

### Conclusion

The VCSP may offer a viable approach to resolving worker classification issues and eliminating uncertainty in exchange for a significantly reduced employment tax liability for past years. WHD's Higher Education Law Team includes tax, employee benefit and employment attorneys who can assist institutions in identifying current exposure for prior misclassification of service providers and evaluate whether the VCSP is an appropriate remedy.

*For more information, please contact Arthur Phillips at (414) 978-5382 or [aphillips@whdlaw.com](mailto:aphillips@whdlaw.com).*



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