American Institute of Family Relations v. U.S.

44 AFTR 2d 79-5043

[1] This action involves a dispute between the American Institute of Family Relations ("the Institute") and the Internal Revenue Service ("the Government") as to whether the Institute's marriage counselors, guest speakers, and lecturers were "employees" for purposes of the federal employment taxes. The case was tried to the Court on stipulated facts. The parties have filed supplemental briefs regarding newly enacted section 530 of the Internal Revenue Code [sic; should be Revenue Act of 1978], entitled "Controversies Involving Whether Individuals are Employees for Purpose of the Employment Taxes," which governs this action.

(1.) Background: The Institute was organized in 1930 and, through the date of trial, had been engaged in marriage education, marriage counseling, child guidance, training and research. During the years 1968, 1969, and 1970, the Institute paid fees to marriage counselors, guest speakers, and lecturers. The Institute considered these persons to be independent contractors for purposes of the federal employment taxes and paid no withholding taxes on the fees paid to them.In 1972 the Government audited the Institute's records and determined that the marriage counselors, guest speakers, and lecturers were "employees" for purposes of the federal employment taxes. The Government assessed withholding taxes on fees paid by the Institute to these persons, pursuant to the Federal Insurance Contribution Act, the Federal Unemployment Tax Act, and provisions for collection of income tax at the source, in the amounts of $35,968.67 for 1968, $43,071.11 for 1969, and $38,250.16 for 1970. The Institute paid the $35,968.67 assessed for 1968 under protest, after which it timely filed a claim for refund. The claim was denied by the Internal Revenue Service, and the Institute filed this action for refund. The Government counterclaimed for the unpaid amounts assessed for 1969 and 1970.

(2.) Section 530 Section 530 of the Internal Revenue Code [sic; should be Revenue Act of 1978] provides that if, for purposes of the federal employment taxes, a taxpayer did not treat an individual as an employee for any period ending before January 1, 1980, then for purposes of applying such taxes for that period with respect to the taxpayer, the individual shall be deemed not to be an employee unless the taxpayer had no reasonable basis for not treating such individual as an employee. 1 The section's "reasonable [pg. 79-5045]basis" requirement is to be construed liberally in favor of the taxpayer. Congressional Conference Report, Revenue Act of 1978, Section 530. Termination of employment tax liabilities under the section is available to taxpayers who are under audit by the Internal Revenue Service or who are involved in administrative or judicial proceedings with respect to assessments based on employment status reclassifications. Id. The section therefore requires that if the Institute had any reasonable basis for treating its marriage counselors, guest speakers, and lecturers as other than "employees" during the years 1968, 1969, and 1970, judgment must be entered in favor of the Institute.

(3.) Application of Section 530The "reasonable basis" requirement of section 530 may be satisfied either on general evidence or by meeting any one of three statutory standards which constitute "safe havens." Conference Report, supra. The first statutory "safe haven" is that the

taxpayer reasonably relied on judicial precedent, published rulings, technical advice or a letter ruling. §530(a)(2)(A). The Government relies at length on the Treasury Regulations regarding the meaning of the term "employee" under the income tax laws. Treas. Regs. §31.3401(c)-(1). That regulation provides:

("(b)) Generally the relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work to the individual who performs the services. In general, if an individual is subject to the control or direction of another merely as to the result to be accomplished by the work and not as to the means and methods for accomplishing the result, he is not an employee.

((c)) Generally, physicians, lawyers, dentists, veterinarians, contractors, subcontractors, public stenographers, auctioneers, and others who follow an independent trade, business, or profession, in which they offer their services to the public, are not employees." Treas. Reg. §31.3401(c)-(1).

The Court finds that, on the basis of Treasury Regulations §31.3401(c)-(1), the Institute had a reasonable basis for not treating its marriage counselors as "employees" for purposes of the federal employment taxes.

The stipulated facts upon which the Court primarily relies in reaching this conclusion are the following:

("8.) [Outlining the requirements for various levels of counselors, including possession of a graduate degree in an appropriate field of study and examination by a "Professional Standards Committee."]

(11.) The Institute had no formal written or oral contracts of employment with any counselors. [pg. 79-5046]

(12.) Counselors received no salaries or draws and were paid on the basis of a percentage of fees paid by the Institute's clients. If the client did not pay the counselor was not paid. The Institute guaranteed no minimum fees or minimum number of clients to any counselors.

(13.) Counselors received no bonuses or vacation pay, nor did they participate in any profit or pension sharing programs.

(14.) The Institute did not furnish any health, accident or other types of insurance to the counselors ....

(17.) The Institute did not control or attempt to control the counselor's conduct of counseling sessions with the client which was accomplished in private and on a confidential

basis. The counselor was free to select his own counseling methods and/or techniques of which there are more than fifty.

(17A.) The Institute did not furnish secretaries, typewriters, dictating machines, Xerox or duplicating equipment to counselors who prepared their own client reports.

(19.) It had always been the expressed policy of the Institute to direct counselors not to take the Institute's clients to their private practice, and in early 1969, the Institute conformed to the position taken by the American Psychological Association that counselors seeing clients at associations such as the Institute should not have any contemporaneous private practice.

...

As a result of this private practice directive the Institute lost 15 or 16 counselors, and notwithstanding the directive approximately 8 or 10 counselors who already had private practices in 1969 continued to maintain their own practice while counseling at the Institute.

29. ... The marriage counselors' Summaries and Reports were not reviewed by the Institute's staff, except in the case of complaints, and were sent to file.

33. Counselors at the Institute were free to utilize any system or method of counseling within the generally accepted theories of the time."

These facts demonstrate that the Institute had a reasonable basis for not treating its marriage counselors as "employees" for employment tax purposes. The Institute could reasonably conclude that the counselors were under the Institute's control merely as to the result to be accomplished and not as to the means and methods for accomplishing the result. The Institute could further reasonably conclude that it did not furnish "tools" to the marriage counselors. Finally, the Institute could reasonably conclude that the marriage counselors were professionals to be treated similarly to physicians, lawyers, or dentists. Thus, the Institute could reasonably have relied on Treas. Regs. §31.3401(c)-(1) in not treating its counselors as "employees."

The Court also finds that, considering all the stipulated facts, the relevant statutory and regulatory provisions, and the judicial and administrative decisions cited by the parties, the Institute satisfies the "reasonable basis" requirement of section 530. The Institute had a reasonable basis to conclude that the marriage counselors, guest speakers, and lecturers were independent contractors and not employees. 2

The foregoing are to be deemed findings of fact and conclusions of law.

Accordingly, judgment will be entered in favor of the American Institute of Family Relations and against the United States of America.

Judgment

This matter came on for trial before the Court without a jury on stipulated facts. Based upon the Findings of Fact and Conclusions of Law filed in the form of a memorandum opinion in this matter, and upon argument of counsel and all other matters properly a part of the record in this case,

It Is Hereby Ordered, Adjudged and Decreed that plaintiff shall have judgment on its complaint in the amount of $38,250.16, plus interest in accordance with law.

It Is Hereby Further Ordered, Adjudged and Decreed that defendant shall take nothing by its counterclaim, and the counterclaim shall be dismissed.

1 Section 530 provides:
"Controversies Involving Whether Individuals are Employees for Purposes of the Employment Taxes.

((a)) Termination of Certain Employment Tax Liability for Periods Before 1980.-

((1)) In general.-If-

((A)) for purpose of employment taxes, the taxpayer did not treat an individual as an employee for any period ending before January 1, 1980, and

((B)) in the case of periods after December 31, 1978, all Federal tax returns (including information returns) required to be filed by the taxpayer with respect to such individual for such period are filed on a basis consistent with the taxpayer's treatment of such individual as not being an employee, then for purposes of applying such taxes for such period with respect to the taxpayer, the individual shall be deemed not to be an employee unless the taxpayer had no reasonable basis for not treating such individual as an employee.

((2)) Statutory standards providing one method of satisfying the requirements of paragaraph (1).-For purposes of paragraph (1), a taxpayer shall in any case be treated as having a reasonable basis for not treating an individual as an employee for a period if the taxpayer's treatment of such individual for such period was in reasonable reliance on any of the following:

((A)) judicial precedent, published rulings, technical advice with respect to the taxpayer, or a letter ruling to the taxpayer;

((B)) a past Internal Revenue Service audit of the taxpayer in which there was no assessment attributable to the treatment (for employment tax purposes) of the individuals holding positions substantially similar to the position held by this individual; or

((C)) long-standing recognized practice of a significant segment of the industry in which such individual was engaged.

((3)) Consistency required in the case of 1979 tax treatment.-Paragraph (1) shall not apply with respect to the treatment of any individual for employment tax purposes for any period ending after December 31, 1978, and before January 1, 1980, if the taxpayer (or a predecessor) has treated any individual holding a substantially similar position as an employee for purposes of the employment taxes for any period beginning after December 31, 1977.

((4)) Refund or credit of overpayment.-If refund or credit of any overpayment of an employment tax resulting from the application of paragraph (1) is not barred on the date of the enactment of this Act by any law or rules of law, the period for filing a claim for refund or credit of such overpayment (to the extent attributable to the application of paragraph (1) shall not expire before the date 1 year after the date of the enactment of this Act.

((b)) Prohibition Against Regulations and Rulings on Employment Status.-No regulation or Revenue Ruling shall be published on or after the date of the enactment of this Act and before January 1, 1980 (or, if earlier, the effective date of any law hereafter enacted clarifying the employment status of individuals for purposes of the employment taxes) by the Department of the Treasury (including the Internal Revenue Service) with respect to the employment status of any individual for purposes of the employment taxes.

((c)) Definitions.-For purposes of this section-

((1)) Employment tax.-The term 'employment tax' means any tax imposed by subtitle C of the Internal Revenue Code of 1954.

((2)) Employment status.-The term 'employment status' means the status of an individual, under the usual common law rules applicable in determining the employer-employee

relationship, as an employee or as an independent contractor (or other individual who is not an employee)."

2 The Government has not contended at trial that the Institute's guest speakers and lecturers were "employees" for purposes of the employment taxes.