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## **CCA 200948043**

### ISSUE

Whether Taxpayer qualifies for relief under Section 530 of the Revenue Act of 1978 (Section 530) with respect to its Category A Workers for [Redacted Text] the year [Redacted Text]?

### CONCLUSION

For the year [Redacted Text], Taxpayer qualifies for relief under Section 530 with respect to its Category A Workers, based on the following:

- (1) Taxpayer meets the reporting consistency requirement as to Category A Workers because it filed Forms 1099 with respect to all Category A Workers for the year [Redacted Text];
- (2) Taxpayer meets the substantive consistency requirement as to Category A Workers because it did not treat any Category A Worker or individual in a substantially similar position as an employee; and
- (3) Taxpayer meets the reasonable basis requirement with respect to Category A Workers. Taxpayer relied on a prior audit of tax years [Redacted Text], for which the Service issued a no-change letter with respect to Category A Workers. Further, Taxpayer may also succeed in its claim that it reasonably relied on judicial precedent, letter rulings, its closing agreement [Redacted Text], or some other reasonable basis for not treating the Category A Workers as employees.

### FACTS

#### I. Background

The Service is currently conducting an employment tax examination of Taxpayer for employment tax periods ending in the year [Redacted Text]. The examination includes the worker classification of Category A Workers that Taxpayer uses in its business, as explained more fully below.

#### A. Taxpayer's Corporate History

Taxpayer has a complex corporate history. In brief, Taxpayer [Redacted Text]

#### B. General Facts Regarding Use of Category A Workers in Taxpayer's Business

Based upon the available evidence, the facts regarding Taxpayer's use of Category A Workers in its business during [Redacted Text] follows.

Taxpayer is in the [Redacted Text] business. In [Redacted Text], Taxpayer serviced its [Redacted Text] clients generally through its Category A Workers, who [Redacted Text].

Taxpayer provided these services by directly contracting with Category A Workers via the use of standardized [Redacted Text] agreements and by contracting with temporary staffing services for the use of temporary [Redacted Text]. Taxpayer has been using some form of this [Redacted Text] agreement with its Category A Workers since it started its business operation. Taxpayer has modified the agreements over the years, but it continues to use them as the main contracting method to obtain [Redacted Text] services. All evidence obtained by the Service indicates that the [Redacted Text] agreements are mandatory for the Category A Workers and include no negotiable terms. There are options within the agreements from which the Category A Workers can choose, but the choices are restricted to those contained in the standardized agreements. All [Redacted Text] agreements the Service has been provided and has reviewed are in this standardized/mandatory format.

The general terms of all of the [Redacted Text] agreements are that the Category A Worker [Redacted Text], must provide at the Category A Worker's own expense a Taxpayer-approved [Redacted Text], wear a Taxpayer uniform and adhere to Taxpayer appearance standards. Each Category A Worker is paid via a standardized [Redacted Text] formula with additional consideration for [Redacted Text]. In addition, the Category A Worker is paid [Redacted Text], and can be paid as a [Redacted Text]. There is a daily payment for the Category A Worker who elects the [Redacted Text] program and there are [Redacted Text].

[illegible]

The [Redacted Text] agreements are additionally modified by addendums, signed or initialed by the Category A Worker and the [Redacted Text] manager. Some addendums are for each Category A Worker, some are specific, such as [Redacted Text], for the [Redacted Text].

The terms of the [Redacted Text] agreements are discussed in greater detail in sections I.C.4 and I.D.

### 1. Category A Workers

Under their respective [Redacted Text] agreements, each Category A Worker had to provide a Taxpayer-approved [Redacted Text]. The [Redacted Text] had to meet Taxpayer's requirements for the [Redacted Text].

If the Category A Worker had more than one [Redacted Text] or [Redacted Text], he had to have a Taxpayer-approved [Redacted Text] for each [Redacted Text]. The Category A Worker was required to wear a Taxpayer uniform that identified him with Taxpayer. Each Category A Worker used a [Redacted Text]. Taxpayer offered the Category A Workers, for a fee, an optional

[Redacted Text], [Redacted Text], Taxpayer [Redacted Text]. The [Redacted Text] equipment was included as part of the [Redacted Text]. The Category A Worker was not required to have a [Redacted Text]. A Category A Worker was required to have [Redacted Text] liability coverage [Redacted Text] and work accident and/or worker's compensation insurance. Category A Workers generally were provided coverage through policies negotiated by Taxpayer.

Many Category A Workers had [Redacted Text] agreements to service [Redacted Text]. In [Redacted Text], there were approximately [Redacted Text] Category A Workers with [Redacted Text] areas and [Redacted Text] Category A Workers with [Redacted Text] areas. According to Taxpayer, since [Redacted Text], more and more Category A Workers have taken on [Redacted Text] areas.

Both [Redacted Text] and [Redacted Text] Category A Workers had the right to sell their [Redacted Text] to others. 1 The record contains no information on number of [Redacted Text] offered for sale, number of [Redacted Text] actually sold, or any final [Redacted Text] sales prices in [Redacted Text], or any other year.

Taxpayer issued Forms 1099 to all Category A Workers performing services for Taxpayer during [Redacted Text], without regard to whether the Category A Workers were incorporated. The examination revealed that there were a few instances where Taxpayer issued both a Form W-2 and Form 1099 to certain Category A Workers. This was explained by Taxpayer as isolated instances where an employee, such as a [Redacted Text], became a Category A Worker. The Form W-2 would have been issued for the period the worker was an employee performing [Redacted Text] duties, and a Form 1099 issued for the period of time where the worker was a Category A Worker.

In [Redacted Text], Category A Workers worked under the [Redacted Text] and the [Redacted Text] Agreements or continued work under an [Redacted Text] agreement signed in an earlier year for multiple years. The [Redacted Text] and the [Redacted Text] Agreements were nearly identical. A comparison provided by Taxpayer in response to IDR ET [Redacted Text] shows that there were only [Redacted Text] differences, which amounted to typographical changes.

The examination team conducted an analysis of changes between the [Redacted Text] Agreement, which was referenced in the [Redacted Text] Closing Agreement (discussed later), and the [Redacted Text] Agreement. Examples include changes made to arbitration rights for asserted wrongful termination, the compensation structure, the duration of the agreement, and the addition of [Redacted Text].

The [Redacted Text] of a Category A Worker were generally set by Taxpayer, as each Category A Worker had a set schedule of [Redacted Text] customers, times and locations. In [Redacted Text], the basic duties of a Category A Worker included [Redacted Text].

## 2. Temporary [Redacted Text] 2 [Redacted Text]

Temporary [Redacted Text] are [Redacted Text] who [Redacted Text] but do not [Redacted Text]. Temporary [Redacted Text] do not [Redacted Text] and are not required to provide any tools or equipment. They do not have [Redacted Text] agreements with Taxpayer. They are paid an hourly or daily rate. The Taxpayer uses temporary [Redacted Text] to [Redacted Text] that are temporarily without Category A Workers, to assist with [Redacted Text] is too great for the

Category A Workers to handle, or for other duties, such as [Redacted Text]. When temporary [Redacted Text] are not being used by the Taxpayer, they can be hired by Category A Workers who want to take time off, or who need additional assistance with their [Redacted Text].

Taxpayer [Redacted Text] recruited some temporary [Redacted Text]. When the individuals arrived at the [Redacted Text], Taxpayer personnel would have them fill out applications and Forms W-4. The temporary [Redacted Text] were treated as employees of temporary staffing services, such as TSS1 and TSS2. Sometimes the [Redacted Text] understood that they were being employed by the temporary staffing service; sometimes they did not understand this until they received a paycheck from the temporary staffing service.

#### a.Contracts for Temporary

##### (i)TSS1

A contract between Taxpayer and TSS1 was executed on [Redacted Text]. This contract provides that TSS1 was to pay all wages to these [Redacted Text], as well as withholding and paying all required federal, state, county, and local taxes.

Pursuant to this contract, two days prior to TSS1 paying these [Redacted Text], Taxpayer was to list all [Redacted Text] and the amounts each [Redacted Text] was to be paid, and to forward these funds, with the agreed upon taxes and fees, to TSS1. The contract is silent as to what happens if such funds were not so forwarded two days prior. The contract was binding on successors to either party.

On [Redacted Text], TSS1 sent Taxpayer a letter stating that TSS1 should now be referred to as "[Redacted Text]". In [Redacted Text], some of the temporary [Redacted Text] were provided by TSS1.

##### (ii)TSS2

The file contains an [Redacted Text], contract between TSS2 and Taxpayer. TSS2 is part of the [Redacted Text] company that provides HR services. TSS2 provides temporary staffing workers to many companies nationwide, not merely [Redacted Text] for Taxpayer.

Under this contract, entitled "Temporary [Redacted Text] Services Agreement," TSS2 provides employees for use by Taxpayer for use at its Taxpayer [Redacted Text]. 3 Pursuant to this contract, TSS2 ensures that all personnel it sends to Taxpayer meet the minimum [Redacted Text] eligibility requirements listed in Attachment [Redacted Text] of the Contract ("[Redacted Text] Eligibility Requirements"). These requirements include ensuring each worker had not been convicted of a felony, is at least 21 years of age, [Redacted Text], a physical examination completed by a qualified physician, drug screening, a scored written examination pertaining to [Redacted Text], and successful completion of a [Redacted Text] test meeting minimum [Redacted Text] standards.

Under the contract, TSS2 is also required to train [Redacted Text] in six specific areas prior to the [Redacted Text] arriving at a Taxpayer facility. These areas are [Redacted Text] This training is also required under the Occupational Safety and Health Act.

The contract provides that the workers that TSS2 provides to Taxpayer are at all times employees of TSS2, and that Taxpayer may not engage in any actions that would make TSS2's employees those of Taxpayer. Taxpayer agrees to adequately instruct and oversee TSS2's personnel in performing their agreed upon duties. 4

Under the contract, TSS2 invoices Taxpayer weekly. Term [Redacted Text] of the contract provides that "[t]he terms of payment are net 30 days." Taxpayer agreed to promptly pay these invoices. TSS2's billing rates were [Redacted Text] above employee payroll for workers assigned to Taxpayer. TSS2 reports payments to [Redacted Text] on Form W-2, using its EIN.

The contract required Taxpayer to maintain certain insurance coverage in specific amounts (e.g., [Redacted Text]), which covered TSS2 and its employees. The contract also required TSS2 to maintain additional identical insurance coverage in specific amounts (e.g., [Redacted Text]).

The contract provides that TSS2 maintains workers' compensation coverage. [Redacted Text] The contract also prohibits Taxpayer from employing, contracting with, soliciting for employment or as a contractor, directly or indirectly, any TSS2-recruited worker, without the prior written consent of TSS2. The contract also provides a fee schedule that Taxpayer would pay to TSS2 should Taxpayer hire such a worker. The contract further provides that the fee schedule and liquidated damages provision do not apply in the case of workers directly recruited by Taxpayer.

The contract further provides that Taxpayer will not change the assignment of a TSS2 provided worker without prior written consent by TSS2. No TSS2 employee assigned to Taxpayer is entitled to any benefits or compensation from Taxpayer and each TSS2 employee must acknowledge in writing that they are not entitled to participate in any Taxpayer benefit plan.

The record reflects that Taxpayer recruited both Category A Workers and temporary [Redacted Text].

b. [Redacted Text] Program

Category A Workers can elect to participate in a [Redacted Text] ("Program") which provides two weeks off during the year. The selection of weeks for the [Redacted Text] program is according to length of time as a Category A Worker. Taxpayer provides the replacement [Redacted Text]; the Category A Worker's [Redacted Text]; and the Category A Worker will not receive any [Redacted Text] for the work performed by the replacement [Redacted Text] during the time off. Prior to taking time off, the Category A Worker will provide the replacement [Redacted Text] with advice concerning serving the [Redacted Text]. This is included in the Program. Taxpayer charges Category A Workers electing the optional Program an additional charge of [Redacted Text] per day added to the [Redacted Text] for the program. The [Redacted Text] Program was instituted for Category A Workers in [Redacted Text].

c. Temporary Replacement [Redacted Text]

If a Category A Worker (or one of their additional [Redacted Text]) is sick or otherwise unable to [Redacted Text] on a given day, he is required to provide a Taxpayer approved replacement [Redacted Text], either through his own contacts or the contacts of other [Redacted Text].

Taxpayer requires that the Category A Worker have Form [Redacted Text], signed by Taxpayer before a substitute [Redacted Text] can [Redacted Text].

If the Category A Worker is unable to provide a replacement [Redacted Text], Taxpayer will [Redacted Text] or use a [Redacted Text] or provide a temporary replacement [Redacted Text] through one of the temporary staffing services. In the latter case, the replacement [Redacted Text] and the Category A Worker does not receive any [Redacted Text] for use of the temporary replacement [Redacted Text]. The cost of the temporary [Redacted Text] is charged to Taxpayer by the temporary staffing service provider.

### 3.[Redacted Text] Owners and [Redacted Text]

A [Redacted Text] owner is a Category A Worker who owns two or more [Redacted Text]. These Category A Workers have the right under their contracts to hire their own workers, and many do. The Category A Workers make their own arrangements and pay their own workers separate from any agreement that Taxpayer has with any temporary staffing service. Their workers must be approved by Taxpayer and meet the training and drug testing requirements of Taxpayer. Some Category A Workers treat these additional [Redacted Text] as their employees; others treat them as independent contractors. These additional [Redacted Text] are paid pursuant to independent agreements with the Category A Workers for whom they work, and the [Redacted Text] owners receive compensation for each [Redacted Text]. We are aware of no standard pay agreement for this type of arrangement and have no information regarding the details of the pay that this category of [Redacted Text] receives.

A [Redacted Text] differs significantly from a [Redacted Text] Category A Worker. A [Redacted Text] may be a Category A Worker, but is contracted to service one [Redacted Text]. Due to growth in his [Redacted Text], however, this [Redacted Text] is required to provide additional [Redacted Text] to meet the service needs of his [Redacted Text]. Although the [Redacted Text] hires his own assistants and enters into pay arrangements with his assistants independently of Taxpayer, the [Redacted Text] does not receive additional compensation, such as [Redacted Text]. [Redacted Text] do, however, receive payments for the additional [Redacted Text].

## C.The [Redacted Text] Closing Agreement History

### 1.[Redacted Text] Audit and Litigation

Taxpayer was examined by the Service for the [Redacted Text] tax years and assessed employment taxes for its Category A Workers. Taxpayer contested the assessment in [Redacted Text].

### 2.[Redacted Text] Closing Agreement

In settling the employment tax [Redacted Text] litigation for the tax years [Redacted Text], Taxpayer and the Service entered into a closing agreement in [Redacted Text], under which Taxpayer paid the Service [Redacted Text], which included an amount already paid for years [Redacted Text]

The closing agreement did not merely detail the way Taxpayer treated the Category A Workers for the [Redacted Text] years. Rather, the closing agreement, along with documents the parties

exchanged in working out the settlement, detailed the way the parties agreed that Taxpayer would treat the Category A Workers for future periods. Indeed, to be as specific as possible, the parties incorporated the then new [Redacted Text] Agreement into the [Redacted Text] Closing Agreement, along with numerous attachments, exhibits, and addenda.

The closing agreement contains the following relevant terms: 1) Taxpayer paid the Service the total sum of [Redacted Text] for employment tax deficiencies for the [Redacted Text] tax years; the Service abated the remainder of any assessments in relation to those deficiencies for the years [Redacted Text]. 2) [Redacted Text] 3) Taxpayer agreed that the Service may audit Taxpayer operations to confirm Taxpayer's continued compliance with the [Redacted Text] Agreement. Taxpayer also agreed that the Service could interview [Redacted Text] without Taxpayer officials present and that Taxpayer would maintain records for the Service to review upon request. 4) The Service agreed not to reclassify Taxpayer's [Redacted Text] as employees, unless it determined that Taxpayer exercised control in a manner that conflicts with the [Redacted Text] Agreement [Redacted Text] (described below) and was not a sporadic or isolated incident. Taxpayer had all the legal rights to dispute such a reclassification. 5) Taxpayer was to file Forms 1099 at the Service Center [Redacted Text]. 6) [Redacted Text] Taxpayer was to issue a tax obligation letter to the [Redacted Text] each year.

The closing agreement has prospective application and no specified date for termination. The closing agreement contains the standard Form 906 text stating that it is final and conclusive except that the matter it relates to may be reopened in the event of fraud, malfeasance, or misrepresentation of material fact. There is no indication of fraud, malfeasance, or misrepresentation of any material fact with respect to the [Redacted Text] closing agreement.

The Closing Agreement contains no terms regarding whether the Category A Workers continue as independent contractors if Taxpayer and the Category A Workers modify the contract terms between them from the contract terms reviewed by the Service as set forth in the [Redacted Text] Agreement.

Term [Redacted Text] of the closing agreement places no limit on the number of audits the Service can conduct to verify compliance with the [Redacted Text] Agreement. Specifically, it provides:

The Internal Revenue Service may audit [Taxpayer] operations to confirm [Taxpayer's] continued compliance with the [Redacted Text] Agreement. In connection with such audit, [Taxpayer] agrees to the following specific procedural undertakings: [(a) Service may interview [Redacted Text], (b) [Taxpayer] to maintain written record of disagreements over interpretation of [Redacted Text] Agreement, and (c) [Taxpayer] to maintain list and files re arbitration decisions]. (emphasis added)

Section 530 is not addressed in the closing agreement. However, during the settlement negotiations in the [Redacted Text], the parties addressed the issue of Section 530 waiver. A [Redacted Text] letter to counsel for Taxpayer from the Department of Justice, which enclosed the proposed closing agreement, contains the sentence: "Paragraph [Redacted Text] has been added at our request to serve as a guideline for both [Taxpayer] and the Service in the event of a breach of this agreement." Paragraph [Redacted Text] in the proposed closing agreement provides that if the Service determines that Taxpayer has breached the terms of the closing agreement, and the breach is not cured within 30 days of written notification by the Service, the

Service may immediately assess "based on treatment of the Contractors as employees for purposes of the Internal Revenue Code." Taxpayer could contest the assessment by paying the tax and filing a claim for refund ( IRC § 7436 did not take effect until 1997). Unless the Service notified Taxpayer that the breach had been cured or there was a final judicial decision that there had been no breach, the Service's written notification "shall be determinative in requiring tax treatment of the Contractors as employees." The proposed Paragraph [Redacted Text] ended with the sentence: "Such written formal notification by the Service of a breach (or a judicial decision to that effect) shall also preclude [Taxpayer] from raising any claim for relief under Section 530 of the Internal Revenue Act of 1978 [sic], or such other law existing on the date of the execution of this agreement."

In a [Redacted Text] letter to the Department of Justice, Taxpayer's counsel responded:

As we have discussed, our principal concerns are with the proposed paragraph ([Redacted Text]), which, as written, would be a 'deal-breaker' to [Taxpayer]. We have, throughout our discussions, recognized the right of the Service to audit [Taxpayer] operations under the [Redacted Text] Agreement. Our fundamental understanding of the agreement with the Service is that, so long as [Taxpayer] operations are conducted as described in the [Redacted Text] Agreement, the Service will not propose to reclassify the Contractors. . . . We have, however, understood that in all events [Taxpayer] would have the same procedural and legal rights as any other taxpayer if for some reason the Service concluded on audit that [Taxpayer] operations had departed in some material way from the terms of the [Redacted Text] Agreement, so that the Service was no longer bound [Redacted Text], and further that the asserted departure by [Taxpayer] was so significant as to warrant a proposed reclassification.

The letter states Taxpayer's understanding that the Department of Justice would withdraw or substantially restate the paragraph. In the draft enclosed with that letter, paragraph [Redacted Text] was deleted. The language from the proposed paragraph ([Redacted Text]) was not included in the closing agreement executed by the parties.

3. [Redacted Text]

4.[Redacted Text] Agreement

Under the [Redacted Text] Agreement executed between Taxpayer and its Category A Workers, the Category A Workers ([Redacted Text] or [Redacted Text] in the [Redacted Text] Agreement) were responsible for providing their own [Redacted Text] and for the operating expenses. Taxpayer reserved the right to approve each [Redacted Text]. [Redacted Text] There were extensive "[Redacted Text]" provisions, as well as [Redacted Text] appearance standards. Taxpayer provided a [Redacted Text] providing the [Redacted Text] various items at-cost such as [Redacted Text], uniforms, [Redacted Text], and critical [Redacted Text] equipment. There was also an optional [Redacted Text] program. [Redacted Text] electing to participate in the [Redacted Text] program were paid an additional [Redacted Text]. [Redacted Text] were permitted, with Taxpayer's consent, to [Redacted Text] more than one [Redacted Text]. These additional [Redacted Text] were required to meet the same standards as the other [Redacted Text]. These additional [Redacted Text] would be the workers of the [Redacted Text]. [Redacted Text] could also have a qualified replacement [Redacted Text] should the [Redacted Text] be



absent on a given day. These replacement [Redacted Text] would also be workers of the [Redacted Text]. Insurance obligations were divided between Taxpayer and the [Redacted Text]. The compensation formula had several components, including [Redacted Text] and various [Redacted Text]. [Redacted Text] could sell their [Redacted Text] at whatever price a departing [Redacted Text] and purchasing [Redacted Text] agreed upon. This sale could include the sale of the [Redacted Text] and other equipment used in the business. There were numerous contractual rights under the [Redacted Text] Agreement including the right to arbitration before a neutral arbiter under the rules of the American Arbitration Association. Additionally, Taxpayer maintained a [Redacted Text]. The Agreement acknowledged and incorporated the numerous state and federal regulatory agency requirements associated with such operations. Taxpayer also agreed to provide training for new [Redacted Text] to provide an introduction to the company, an overview of the Agreement, training regarding the required documentation, the use of the electronic equipment, and a review of the safety requirements. Taxpayer was permitted to [Redacted Text] and additionally if the [Redacted Text] so requested.

Since [Redacted Text], Taxpayer has made some changes in its relationship with and treatment of Category A Workers.

#### D.[Redacted Text] Agreements in Use Since [Redacted Text]

Since the execution of the [Redacted Text] Closing Agreement, the [Redacted Text] Agreement between Taxpayer and its Category A Workers has been modified and new [Redacted Text] agreements were entered into. Most of the provisions of the subsequent agreements remained the same as the [Redacted Text] agreement, with some modifications to the original reflected therein.

Category A Workers covered by the [Redacted Text] Agreement have since signed new [Redacted Text] agreements. Thus, none of the Category A Workers in [Redacted Text] would have been [Redacted Text] under the [Redacted Text] Agreement. Much of the basic structure of the [Redacted Text] Agreement is found in the subsequently executed [Redacted Text] Agreements. Some of the terms and addenda, however, have changed over the years. For example, the compensation structure that was available under the [Redacted Text] Agreement was subsequently altered such that a Category A Worker's ability to participate in the company's [Redacted Text] Program and the [Redacted Text] Program was based on the type of [Redacted Text] the Category A Worker used to fulfill his duties.

Like the [Redacted Text] Agreement, the subsequent [Redacted Text] Agreements create and describe the relationship between Taxpayer and its Category A Workers. As in the [Redacted Text] Agreement, each subsequent agreement defines Taxpayer as [Redacted Text] "[Redacted Text]. Each describes the Category A Workers as contractors who [Redacted Text] Id. Under the Agreements, the Category A Workers are required to provide, [Redacted Text]. The most obvious differences among the agreements are in [Redacted Text] and relate to compensation rates.

There are three primary differences between the [Redacted Text] Agreement and the [Redacted Text] Agreement. First, the [Redacted Text] Agreement provides for shorter maximum initial contract terms than the [Redacted Text] Agreement. Category A Workers may choose a maximum [Redacted Text] term rather than a maximum [Redacted Text] term. Second, the [Redacted Text] and the [Redacted Text] Agreement require the cooperation of the Category A

Workers in the legal defense of claims brought against Taxpayer. 6 Three, [Redacted Text] Agreements entered into subsequent to the [Redacted Text] Agreement, as well as the [Redacted Text] and [Redacted Text] Agreements, alter the financial rewards available to the Category A Workers depending on the type of [Redacted Text] used.

## II. History of Prior Service Inquiries

It is our understanding that both the Service's records and Taxpayer's records of employment tax inquiries between [Redacted Text] and [Redacted Text] are incomplete. We summarize below a history of the relevant tax-related inquiries from available Service records, records provided by Taxpayer in response to an informal request, and Taxpayer's response to IDR ET [Redacted Text]. It appears that numerous EINs were involved with each of these examinations and that not all the records in the Service's files are EIN-specific. Other records are clearly EIN-specific. We note that we have considered those records that are specific to Taxpayer, EIN [Redacted Text] as well as those records that contain no EIN and appear to include multiple EIN's, including EIN [Redacted Text]. The files suggest that the inquiries were coordinated.

As a general observation relating to all the records, we are unable to locate in any file a copy of the Service's standard employment tax compliance check notification letter, or any other letter suggesting the Service had opened compliance checks regarding Taxpayer. The Service files also contain no clear examination opening letters for any prior period. Some files include an examination plan and Information Document Requests (IDRs). Each inquiry was closed without change (i.e., without an employment tax proposal or assessment relating to the treatment of Category A Workers as employees rather than independent contractors). The file contains a copy of a no-change letter (Letter 590) dated [Redacted Text] issued to Taxpayer concerning the Form 941 for all periods in [Redacted Text] and [Redacted Text].

### A. Taxpayer 7

Taxpayer name: Taxpayer

EIN:

Date begun: The Master File Transcript reflects the exam of Taxpayer's [Redacted Text] year began on [Redacted Text] and the exam of Taxpayer's [Redacted Text] year began on [Redacted Text].

Date ended: No-change letter issued [Redacted Text].

The audit files for Taxpayer ([Redacted Text]) are included in the [Redacted Text] Audit Plan files.

For the examination of the [Redacted Text] and [Redacted Text] tax years, the letter commencing the examination was issued to the Taxpayer on [Redacted Text]. The opening conference was held on [Redacted Text]. ET IDR [Redacted Text] was issued to [Redacted Text] on [Redacted Text], which was prior to these dates. It appears that pre-audit planning for the examination started in [Redacted Text].

Service files for the employment tax inquiry of Taxpayer for tax years [Redacted Text] contain an undated Form [Redacted Text], which is part of all formal [Redacted Text] audit plans and specific to employment taxes. This form contains a brief summary of the previous examination and resolution for years through [Redacted Text]. It states, "If [Taxpayer] conducts its operations in accordance with the aforementioned agreement [the [Redacted Text] closing agreement], then IRS will consider the [Redacted Text] to be independent contractors." The procedures outlined to conduct this analysis included securing from the taxpayer copies of relevant company manuals, procedures, and/or policy statements; reviewing the revised [Redacted Text] agreement; obtaining an analysis of [Redacted Text] comprised of payees and annual dollar amounts; considering "NAR Form 2-114, Employment Tax Referral To Collection Division;" and "Ascertaining if [Taxpayer] is conducting its operations in accordance with the revised [Redacted Text] Agreement. If it is, then the [Redacted Text] are to be considered independent contractors. If it is not, then determine if there is an employer-employee relationship." This Service Form [Redacted Text] contained EIN [Redacted Text] typed at the top and in the center of handwritten page number [Redacted Text].

This file also contained a handwritten note dated [Redacted Text], entitled "Independent Contractor Status" regarding the [Redacted Text] examination of [Taxpayer], noting "Settlement of Employee/Independent Contractor Status Closing Agreement." After a summary of the settlement agreement terms, the note concludes:

Does not appear that much can be done in this area except to verify that the terms of agreement are being adhered to. May want to request documents shown on pg. - and - of Closing Agreement. Will make referral for employment tax specialist. If none assigned, we will handle.

On [Redacted Text], IDR ET- [Redacted Text] was issued to Taxpayer. IDR ET-[Redacted Text] requested various documents, including but not limited to copies of manuals, procedures and policy statements pertaining to [Redacted Text] as well as the [Redacted Text] Agreement, attachments thereto, letters from the Taxpayer's President to [Redacted Text] managers, examples of [Redacted Text] agreements, etc. IDR ET[Redacted Text] was issued as a follow-up to IDR ET[Redacted Text], and was issued to Taxpayer on [Redacted Text]. IDR ET[Redacted Text] requested copies of "any memorandums, notices, bulletins, policies, announcements, rules, regulations, etc., issued, written, and/or posted pertaining to contractors, [Redacted Text]."

On [Redacted Text], the Service issued a no-change letter (Letter 590) to Taxpayer concerning the Form 941 for all periods in [Redacted Text] and [Redacted Text].

Later correspondence from Taxpayer to the Service indicates Taxpayer believes it was subject to an employment tax audit for this period. In connection with the current examination, Taxpayer asserted in a [Redacted Text] letter to the IRS Team Coordinator, [Redacted Text]:

As noted, under Section 530(a)(2)(B), a reasonable basis for treating workers as independent contractors is established by prior IRS audits which specifically considered the issue and did not make an adjustment. [Redacted Text] history is replete with such audits.

The letter continued:

Audit of [Redacted Text] and [Redacted Text] - The IRS audit team assigned an employment tax specialist to the audit and she reviewed the closing agreement and [Taxpayer's] compliance with the closing agreement. She issued information document requests regarding the [Redacted Text] and the closing agreement. The employment tax specialist agreed that the [Redacted Text] were independent contractors and no adjustment was made with respect to this issue.

Also in connection with the current examination, Taxpayer asserted in a [Redacted Text] letter to the IRS Team Coordinator, [Redacted Text]:

Audit of [Redacted Text] and [Redacted Text]. .. Three specific employment tax information document requests ("IDRs") were issued to [Taxpayer] requesting additional information. A. ET[Redacted Text] requested the companies "manual, procedures, and/or policy statement pertaining to the reimbursement of expenses incurred when the [Redacted Text], who are employees, are away from homes overnight." [Taxpayer's] response was that there were no employee [Redacted Text]. [Taxpayer attached a copy of IDR and response.] B. ET[Redacted Text] requested copies of certain documents, such as the [Redacted Text] Agreement, any changes and/or modifications to the Agreement, etc. [Taxpayer attached a copy of the IDR and response.] C. ET[Redacted Text] requested copies of "any memorandums, notices, bulletins, policies, announcements, rules, regulations, etc. issued, written, and/or posted pertaining to contractors, [Redacted Text]. " The Company is still looking for the information provided in response to this IDR. [Taxpayer attached a copy of the IDR.]

Taxpayer's letter concludes:

The audit of [Redacted Text] was an actual employment tax audit that reviewed the worker classification issue with respect to the [Redacted Text]. No adjustment was made. We believe that the copies of the IDRs should be sufficient proof to sustain that [Taxpayer] had a reasonable basis under Section 530.

Taxpayer's letter to IRS Counsel dated [Redacted Text], and Taxpayer's response to IDR ET[Redacted Text] also cite to this audit as a reasonable basis under Section 530.

B. [Redacted Text]

Taxpayer name: [Redacted Text]

EIN: Appears global; includes some IDR's specific to EIN [Redacted Text] (Taxpayer)

Date begun: Unknown and unclear. Possible dates include [Redacted Text], and [Redacted Text]. The first ET IDR is listed on the IDR log as having been issued [Redacted Text].

Date ended: Unknown and unclear. Latest ET IDR response was logged in as received by the Service on [Redacted Text]. Possibly before [Redacted Text] (date of Appeals Case Memorandum). Exam team confirms this audit was closed as a no change.

The file contains various indicia that an employment tax examination was conducted. The Service's [Redacted Text] file contains an undated copy of a Form [Redacted Text] examination plan with a category called "Worker Classification." The file contains a memorandum dated [Redacted Text], regarding years [Redacted Text], which states: "The examination plan is attached" and includes a chart showing that 5 days are planned for the employment tax portion of the three-year examination cycle. The opening conference list of attendees dated [Redacted Text], includes an employment tax specialist and an employment tax manager.

The Service file contains an [Redacted Text], IDR "EMP[Redacted Text]" to "[Redacted Text]," requesting a copy of an examination report from [Redacted Text] State Department of [Redacted Text] in which an employment tax issue was raised. Taxpayer responded on [Redacted Text], that [Redacted Text] audit of [Redacted Text] was on-going and that no report had yet been issued.

The [Redacted Text] employment tax examination file contained an undated copy of a Form [Redacted Text] (part of the "Audit Procedures Section Coordinated Examination Program Audit Plan") regarding [Redacted Text]. This form is specific to employment taxes and appears to cover the tax years [Redacted Text] (much of the years covered section is illegible). The first category of this plan was a category entitled "Worker Classification," and included four areas stating as follows:

- a. Are all individuals providing services to and receiving remittance from the taxpayer properly classified as either employees or independent contractors?
- b. Are there any statutory employees for FICA tax purposes?
- c. Are there any statutory non-employees I.R.C. § 3506 AND 3508?
- d. Is the taxpayer properly withholding on and reporting all payments made to resident and non-resident aliens?

The [Redacted Text] employment tax examination file contained an [Redacted Text] memorandum to file regarding the [Redacted Text] examination for years [Redacted Text] stating that "[t]he employment tax specialist would do a 5-day compliance check along with a review of [Redacted Text] adherence to a closing agreement concerning contract [Redacted Text]."

The [Redacted Text] employment tax examination file contained a later memorandum dated [Redacted Text] regarding the [Redacted Text] examination for years [Redacted Text]. It states that a limited scope examination utilizing streamlined procedures has been chosen and that a total of 140 days have been planned for this three year exam cycle including 5 days allocated to employment tax.

On [Redacted Text], employment tax manager [Redacted Text] signed a Coordinated Examination Program Audit Plan for "[Redacted Text]" for tax years [Redacted Text] and

[Redacted Text]. The scope of the employment tax section of the audit was summarized "all entities or as needed."

Taxpayer's files for the employment tax inquiry of [Redacted Text] for [Redacted Text] show that the Service provided [Redacted Text] with an examination plan, which stated that the employment tax specialist would do a 5-day compliance check along with a review of [Redacted Text] adherence to a closing agreement concerning contract [Redacted Text], and that the Service issued employment tax IDR's and [Redacted Text] responded. There is no closing letter in Taxpayer's file.

Taxpayer asserted in its [Redacted Text] letter to the IRS Team Coordinator:

Audit of [Redacted Text], [Redacted Text], and [Redacted Text] - The IRS audit team assigned an employment tax specialist, [Redacted Text]. The planning memorandum indicates that she would review the closing agreement. It is our understanding that she did. No adjustments were made to [Taxpayer's] employment tax returns or liabilities.

Taxpayer asserted in its [Redacted Text] letter to the IRS Team Coordinator:

Audit of [Redacted Text], [Redacted Text], and [Redacted Text] - The IRS audit team assigned an employment tax specialist, [Redacted Text]. The planning memorandum states: "The employment tax specialist would do a 5-day compliance check along with a review of [Redacted Text] adherence to a closing agreement concerning contract [Redacted Text]. " (Emphasis added by Taxpayer.) [Taxpayer attached a copy of the [Redacted Text] planning memorandum as Exhibit [Redacted Text]. ] The company provided a copy of the closing agreement to the audit team in response to an IDR request. It is our understanding that the employment tax specialist did what the planning memo provided. No adjustments were made to [Taxpayer's] employment tax returns or liabilities.

Taxpayer stated in its [Redacted Text] letter that the Service concluded this examination with no classification change.

C. [Redacted Text] 8

Taxpayer name:

EIN: None specifically noted

Date begun:

Date ended: after [Redacted Text] (date of latest report in file--re IDR)

Service files for the employment tax inquiry of Taxpayer for [Redacted Text] show an undated employment tax audit plan for [Redacted Text]. The files also show that an employment tax

specialist was assigned to the [Redacted Text] examination and that the Service issued worker classification IDRs (although it is not clear if the IDRs covered [Redacted Text]). The files contain copies of three court opinions, one US Dept. of Labor Administrative Review Board opinion, and two state workers compensation board opinions, all finding that [Redacted Text] were not employees of Taxpayer. Specific relevant items in this file are summarized below.

The file contains memoranda dated [Redacted Text], requesting an employment tax specialist be assigned to the [Redacted Text] examination of [Redacted Text], and show that by [Redacted Text], employment tax specialist [Redacted Text] was assigned. [Redacted Text] audit notes dated [Redacted Text], list numerous employment tax audit issues to be covered (covering more than one page), including "5 days package audit" and "comparison W-2 + 1099's." An [Redacted Text], employment tax Quarterly Status Report for the [Redacted Text] examination notes worker classification IDR numbers [Redacted Text] and [Redacted Text] dated [Redacted Text], were outstanding.

An undated examination note page by [Redacted Text] notes that she was "looking at worker classification (still need to follow up with IDR [Redacted Text] employee got both 1099 + W-2 sample large." 9 This document also notes regarding [Redacted Text] "closing agreement follow up on prior exam agreement."

An undated examination note regarding IDR number [Redacted Text], Terminated Employees/Contractors, states that "To complete IDR #[Redacted Text] - individuals who got a 1099 for [Redacted Text] - questions to determine whether employees or not - those who received 50,000 or more in [Redacted Text]. I am getting her info on disk."

An examination note regarding a [Redacted Text], quarterly meeting with the taxpayer stated: "[Redacted Text]. .. Closing agreement will take time file [Redacted Text] audit (we looked at closing agreement last cycle & approved method no proposed). " A typed examination note, with a handwritten date of 10 , states that [Redacted Text] employment tax examination consisted of four broad areas, one of which was listed as worker classification.

An IDR log dated [Redacted Text], regarding employment taxes shows that the Service issued several IDR's on a variety of employment tax issues to [Redacted Text], including IDR's entitled: [Redacted Text]; contractors; fringe benefits; [Redacted Text]; employee questionnaire; follow-up employee questionnaire; FPRM 941; and W-2 wages.

The [Redacted Text] employment tax examination file contained an undated copy of a Form [Redacted Text] regarding employment taxes for years [Redacted Text]. The first category of this plan was a category entitled "Worker Classification," and included four areas stating as follows:

- a. Are all individuals providing services to and receiving remittance from the taxpayer properly classified as either employees or independent contractors?
- b. Are there any statutory employees for FICA tax purposes?
- c. Are there any statutory non-employees I.R.C. § 3506 AND 3508?

d. Is the taxpayer properly withholding on and reporting all payments made to resident and non-resident aliens?

The file contains an [Redacted Text], IRS Quarterly Status Meeting report noting that two IDRs regarding worker classification were then outstanding. A similar report dated [Redacted Text], stated that, as to employment taxes, there were potential adjustments resulting from the response to "IDR #[Redacted Text]- regarding worker classification (independent contractor status). " It also states "no issues related to [Redacted Text]."

The file contains IDR EMP[Redacted Text], Subject: Terminated Employees Re-hired as Independent Contractors, dated [Redacted Text], seeking the names, former position, former compensation, former job description, and duties and compensation as consultant for any employees in [Redacted Text] that were terminated for any reason and who later provided consulting services and were treated as independent contractors. Also included in this tranche of IDR's was a [Redacted Text], IDR Emp-[Redacted Text], Subject: [Redacted Text] Worker Classification. The purposes noted on this IDR was "[t]o determine if services performed by workers were that of an employee or independent contractor. This IDR attached a three-page spreadsheet listing selected payees for tax years [Redacted Text] to whom Taxpayer had issued Forms 1099, and requested any underlying written service contracts (or summaries of oral contracts). This IDR also asked for additional information, including whether the worker provided with instructions on who, when, where, or how the services are to be performed; whether tools, equipment, or training was provided in order to perform the services; whether the worker was reimbursed for expenses; whether any fringe benefits provided to the worker; and for the Taxpayer to provide an explanation on its rights to terminate or discharge the worker.

The file contained responses to IDR Emp-[Redacted Text], EMP-[Redacted Text], and Emp-[Redacted Text] concerning various worker classification issues that were received in [Redacted Text].

The file contains a [Redacted Text], response from [Redacted Text] to the Service regarding Employment tax IDR's EMP-[Redacted Text], EMP-[Redacted Text], EMP-[Redacted Text], and EMP-[Redacted Text] in the [Redacted Text] examination.

D.

Taxpayer name:

EIN: [Redacted Text] separate EIN's listed in the file, including EIN

Date begun:

Date ended:

This file contains records describing some of the Service's prior inquiries as audits.

A [Redacted Text], memorandum to employment tax specialist [Redacted Text] from [Redacted Text], informing [Redacted Text] that it would be best not to issue proposed IDR [Redacted Text] for Taxpayer and reiterating that the result of the previous audit for compliance with the closing agreement resulted "in a no-change, i.e., they are doing everything in compliance."



Taxpayer's file shows that the Service issued an IDR regarding classification of workers and section 530 relief and that Taxpayer responded to this IDR, which requested that Taxpayer "provide a written explanation on how this relief is applicable for the [Redacted Text] within your company." Taxpayer's response by letter dated [Redacted Text], was that it relied on continuing compliance with the [Redacted Text] Closing Agreement [Redacted Text]. Taxpayer also noted that a prior audit of [Redacted Text] issued IDRs regarding compliance with the agreement, to which [Redacted Text] responded, and that the examination was closed without adjustment to that issue. Taxpayer's files include a Form 2504 which stated, regarding employment taxes under IRC 3101 and 3111, "No change per attached agreement subject to Area Director's approval." The attachment to the Form 2504 states:

The IRS agrees to close the [Redacted Text] and [Redacted Text] employment tax examination and open the employment tax periods encompassing the [Redacted Text] calendar year. Since prior examinations have not resulted in material changes in the employment tax area and to help expedite this review, the [Redacted Text] employment tax periods for [Redacted Text] will not be opened for examination and the examination of the [Redacted Text] periods will be limited to the review of worker classification issues.

The attachment is signed for the Service by [Redacted Text], Employment Tax Manager, dated [Redacted Text]; by [Redacted Text], Team Manager, dated [Redacted Text] [year not legible]; and for Taxpayer by [Redacted Text], [Redacted Text], undated.

### III. Court and Administrative Decisions Relied Upon by Taxpayer, and SS-8 Determinations

#### A. Court and Administrative Decisions Relied Upon by Taxpayer

In its letter dated [Redacted Text] Taxpayer contended that it relied on [Redacted Text], a National Labor Relations Board (NLRB) Regional Director's decision that found that [Redacted Text] were not common law employees [Redacted Text] for National Labor Relations Act purposes. Taxpayer stated: "The NLRB ruling, if not in and of itself decisive, clearly provides a reasonable basis for [Redacted Text] position in this matter. We have provided the following additional judicial precedent in support of the reasonable basis standard. . . ." The letter lists the following [Redacted Text] court and administrative decisions:

[Redacted Text]

[Redacted Text] In an [Redacted Text] letter to IRS Counsel, Taxpayer states: "... in determining to classify Contractors as independent contractors, [Taxpayer] relied on long-standing authority for treating [Redacted Text] as non-employees." It cites [Redacted Text] court decisions. In its response to IDR ET-[Redacted Text], Taxpayer cites the same [Redacted Text] cases, plus [Redacted Text] additional court decision. These court decisions are [Redacted Text]

#### B. SS-8 Determinations

The Service has received numerous requests from Taxpayer's workers for worker status determinations through the SS-8 process. We learned from the Service's SS-8 Unit that [Redacted Text] SS-8 cases with Taxpayer's EIN were closed in [Redacted Text], but the Service no longer has access to those records. The SS-8 Unit believes that those cases were closed with a letter to the worker but without a letter to Taxpayer. We understand that one letter issued during

[Redacted Text] was correspondence (not a determination letter) to one worker stating that, based on the facts the worker presented, it appeared the worker was an employee.

Taxpayer states in its [Redacted Text] response to IDR ET [Redacted Text]: "The Internal Revenue Service has issued determinations in response to classification requests on Forms SS-8 that contractors were independent contractors rather than employees." In its [Redacted Text] letter to IRS Counsel, Taxpayer states:

On [Redacted Text] the IRS issued [Redacted Text] SS-8 determination letters that said '[t]he Internal Revenue Service maintains that [Taxpayer] is adhering to the [Redacted Text] Agreement of [Redacted Text] that is not inconsistent with treatment of the [Redacted Text] as independent contractors. Accordingly, it is held that the worker was not an employee of the firm...' See [Redacted Text] letter to [Redacted Text], attached as Exhibit [Redacted Text].

The attached letter was addressed to Taxpayer and responded to a Form SS-8 regarding Taxpayer, referred to as the firm, and a worker named [Redacted Text]. The letter stated:

Information submitted indicates that the firm is in the [Redacted Text] business and the worker was engaged to perform [Redacted Text] services. The Internal Revenue Service maintains that [Taxpayer] is adhering to the [Redacted Text] Contractor [Redacted Text] Agreement of [Redacted Text] that is not inconsistent with treatment of the [Redacted Text] as independent contractors. Accordingly, it is held that the worker was not an employee of the firm for purposes of the [FICA, FUTA], or for collection of income tax at the source of wages.

From [Redacted Text] through [Redacted Text], the Service issued [Redacted Text] letters to Category A Workers, stating that the Service declined to rule due to the [Redacted Text] closing agreement and noting that the agreement says that operations conducted in accordance with the terms of the [Redacted Text] Agreement will not be inconsistent with treatment of the Category A Workers as independent contractors. We understand that these letters were not sent to Taxpayer.

## LAW

### I. [Redacted Text] Closing Agreement

#### A. Whether [Redacted Text] Closing Agreement Applies

The IRS is authorized by IRC § 7121 to enter into closing agreements. Section 7121 provides as follows:

#### Sec. 7121. Closing Agreements

(a) AUTHORIZATION. -The Secretary is authorized to enter into an agreement in writing with any person relating to the liability of such person (or of the person or estate for whom he acts) in respect of any internal revenue tax for any taxable period.

(b) FINALITY. - If such agreement is approved by the Secretary (within such time as may be stated in such agreement, or later agreed to) such agreement shall be final and conclusive, and, except upon a showing of fraud or malfeasance, or misrepresentation of a material fact -

(1) the case shall not be reopened as to the matters agreed upon or the agreement modified by any officer, employee, or agent of the United States, and

(2) in any suit, action, or proceeding, such agreement, or any determination, assessment, collection, payment, abatement, refund, or credit made in accordance therewith, shall not be annulled, modified, set aside, or disregarded.

Section 7121(a) provides that the Secretary may enter into an agreement in writing with any person relating to the tax liability of such person for any taxable period. Section 7121(b) provides that closing agreements are final and conclusive and defines what final and conclusive means. Section 7121(b) provides that unless there is a showing of fraud, malfeasance, or misrepresentation of a material fact, a closing agreement cannot be changed, or modified or altered in any way by a party to the agreement. Section 7121(b) provides that closing agreements are final and conclusive with respect to the matters addressed therein. A closing agreement does not extend to facts or issues not explicitly described. Thus, if a closing agreement applies prospectively to certain facts, and the facts change from what is described, the closing agreement no longer applies.

The finality of a closing agreement as provided under § 7121(b) differs from the finality of contracts under contract law principles that generally provide for flexibility between the parties. Under contract law principles, parties to a contract are not locked into a contract's terms forever. Parties to a contract are ordinarily as free to change the contract terms after making them as they were to make the contract in the first instance. Restatement (First) of Contracts § 408 (1932). Conversely, the closing agreement statute requirement of finality prohibits changing the agreement. Closing agreements are authorized, and limited by, the language of the statute. *Marathon Oil Co. v. United States*, 42 Fed. Cl. 267, 274 (1998), *aff'd* 215 F.3d 1343 (Fed. Cir. 1999). As a result, where the closing agreement "statute conflicts with general and otherwise governing contract law principles, the statute governs." *Id.*, at 274. Once a closing agreement is made "it is final, conclusive and binding upon both the taxpayer and IRS, for the purpose of the agreement is to terminate and dispose of tax controversies once and for all," barring one of the statutory exceptions of fraud, malfeasance, or a misrepresentation of material fact. *S&O Liquidating Partnership v. Commissioner*, 291 F.3d 454, 458 (7th Cir. 2002). "The notion being that where the taxpayer agrees that the determination is just and the department thinks it is just they can come to an agreement and clean it up forever." Hearings on H.R. 8245 before the Senate Committee on Finance, 67th Congress, 1st Sess. 129 (1921) (statement of T.S. Adams, Tax Advisor, Treas. Dept., discussing the final nature of these agreements, a concept that was adopted and written into law in section 1312 of the Revenue Act of 1921, and later adopted in current section 7121(b)). In practice, this means that once a closing agreement is executed, barring fraud or one of the other exceptions, it is final, and it cannot be changed.

While the finality of closing agreements is expressly controlled by statute, the interpretation of the terms of closing agreements is generally governed by federal common law contract principles. *United States v. National Steel Corp.*, 75 F.3d 1146, 1150 (7th Cir. 1996). Because a closing agreement's terms are interpreted under ordinary principles of contract law, it is limited on its face. *Smith v. United States*, 850 F.2d 242, 245 (5th Cir. 1988) (a closing agreement that was silent as to interest and penalties did not bar a later claim for them by the IRS). If a closing agreement's terms are clear and unambiguous, the language of the agreement will be enforced as written. *S&O Liquidating Partnership*, 291 F.3d at 459. If an issue is not specifically stated in the closing agreement, that issue is not resolved. *Ellinger v. United States*, 470 F.3d 1325, 1337 (11th Cir. 2006) (quoting *Geringer v. Commissioner*, 61 T.C.M. (CCH) 1738 (Jan. 28, 1991) (citing *Zaentz v. Commissioner*, 90 T.C. 753, 766 (1988))). Moreover, the parties to a closing agreement are bound to the terms agreed upon and not to the premises underlying their agreement. *Park v. United States*, 992 F.2d 955, 959-60 (9th Cir. 1993).

## B. Waiver of Section 530 Relief

Section 530 gives taxpayers important rights. Accordingly, a waiver of Section 530 rights cannot be implied. A waiver must be explicit, clear, and unmistakable. See e.g. *Long v. United States*, 69 Fed. Cl. 566, 570 (Fed. Cl. 2006) (stating that waivers must be "clear and unmistakable" when dealing with substantive rights, in this case labor rights); see also, *Wright v. Universal Maritime Service Corp.*, 525 U.S. 70, 80 (1998) and *Metro. Edison Co. v. NLRB*, 460 U.S. 693, 709-10 (1983). The terms of an agreement are construed narrowly against the Service as a drafting party. *Restatement (Second) of Contracts* § 206; *Royal Ins. Co. of Am. v. Orient Overseas Container Line Ltd.*, 525 F.3d 409, 423 (6th Cir. 2008); and *Savedoff v. Access Group, Inc.*, 524 F.3d 754, 764 (6th Cir. 2008).

## II. Section 530

### A. Generally

Section 530 generally provides a taxpayer relief from Federal employment tax liability with respect to any individual for any period, regardless of the legal relationship between the taxpayer and the individual, if the taxpayer meets each of three requirements with respect to that individual:

(1) The taxpayer (or predecessor) did not treat the individual or any individual holding a substantially similar position as an employee for any period beginning after December 31, 1977 ("substantive consistency requirement," Sections 530(a)(1)(A) and 530(a)(3));

(2) For periods after December 31, 1978, the taxpayer filed all Federal tax returns (including information returns) required to be filed with respect to that individual for that period on a basis consistent with the taxpayer's treatment of that individual as not being an employee ("reporting consistency requirement," Section 530(a)(1)(B)); and

(3) The taxpayer had a reasonable basis for not treating the individual as an employee ("reasonable basis requirement," Section 530(a)(1)).

For purposes of the reasonable basis requirement, Section 530(a)(2) provides that a taxpayer is treated as having a reasonable basis if the treatment of the individual was in reasonable reliance on one of three safe harbors:

(A) judicial precedent, published rulings, technical advice with respect to the taxpayer, or a letter ruling to the taxpayer (Section 530(a)(2)(A));

(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 (Section 530(a)(2)(B)); or  
(C) long-standing recognized practice of a significant segment of the industry in which such individual was engaged (Section 530(a)(2)(C)).

A taxpayer who fails to meet any of the three safe harbors may nevertheless be entitled to relief if the taxpayer can demonstrate, in some other manner, a reasonable basis for not treating the individual as an employee. Rev. Proc. 85-18, sec. 3.01, 1985-1 C.B. 518.

With respect to the prior audit safe harbor of section 530(a)(2)(B), a taxpayer may not rely on an audit commenced after December 31, 1996, unless that audit included an examination for employment tax purposes of whether the individual involved (or any individual holding a position substantially similar to the position held by the individual involved) should be treated as an employee of the taxpayer. Section 530(e)(2)(A).

The determination of whether an individual holds a position substantially similar to a position held by another individual must include consideration of the relationship between the taxpayer and such individuals. Section 530(e)(6).

If a taxpayer establishes a prima facie case that it meets the reporting consistency requirement, the substantive consistency requirement, and one of the reasonable basis safe harbors, and the taxpayer has fully cooperated with reasonable requests from the Secretary of the Treasury or his delegate, then the burden of proof with respect to the treatment is on the Secretary. Section 530(e)(4)(A) and 530(e)(4)(B). See Small Business Job Protection Act of 1996, Conference Report, H.R. Rep. No. 104-737, 104th Congress, 2d Sess., at 203-04 (1996).

Congress intended "reasonable basis" to be construed liberally in favor of the taxpayer. Tax Reform Act of 1978, H.R. Rep. No. 95-1748, 95th Cong., 2d Sess., at 5 (1978), 1978-3 (Vol. 1) C.B. 629; Rev. Proc. 85-18, sec. 3.01; *Smoky Mountain Secrets, Inc. v. United States*, 910 F. Supp. 1316, 1323 (E.D. Tenn. 1995); *Veterinary Surgical Consultants, P.C. v. Commissioner*, 117 T.C. 141, 147 (2001), *affd. sub nom., Yeagle Drywall Co. v. Commissioner*, 54 Fed. Appx. 100 (3d Cir. 2002).

A taxpayer is entitled to relief from employment taxes if it meets the requirements of Section 530. Section 530(e)(3) provides that nothing in Section 530 shall be construed to provide that the relief of Section 530(a) only applies where the individual involved is otherwise an employee of the taxpayer. This provision applies to periods after December 31, 1996. Congress intended to make clear that there does not first have to be a determination that a worker is an employee under the common law standards before application of Section 530. See Conference Report, H.R. No.

104-737, 104th Congress, 2d Sess. at 202 (1996). The Service has interpreted this provision to mean that the section 530 issue must be examined first and, if Section 530 relief applies, the Service does not examine whether the individuals are employees. 11

If a taxpayer does not meet the requirements of Section 530 with respect to the individuals at issue, the inquiry turns to whether the individuals are employees of the taxpayer under the common law. See IRC § 3121(d)(2); Employment Tax Regulations sections 31.3121(d)-1, 31.3306(i)-1, and 31.3401(c)-1.

## B. Section 530 - Reporting Consistency

Section 530(a)(1)(B) provides that a taxpayer must have correctly and consistently adhered to the formalities of the reporting requirements. The reporting consistency requirement requires the filing of all required Federal tax returns, including information returns such as Forms 1099, on a basis that is consistent with the taxpayer's treatment of an individual as a nonemployee. Any required Forms 1099 must be filed on a timely basis. Rev. Proc. 85-18, 1985-1 C.B. 518, sec. 2.02. The focus of the reporting consistency requirement is on the reporting that a taxpayer has done: the reporting consistency requirement does not consider the underlying substance of the relationship between the taxpayer and the individual.

In determining whether a taxpayer treated an individual as an employee for any period within the meaning of Section 530(a)(1), generally the filing of an employment tax return, including a Form W-2 (Wage and Tax Statement), for a period with respect to the individual is "treatment" of the individual as an employee for that period. Rev. Proc. 85-18, 1985-1 C.B. 518, sec. 3.03(B).

## C. Section 530 - Substantive Consistency

### 1. Generally

A taxpayer satisfies the substantive consistency requirement of Section 530 if the taxpayer (or predecessor) did not treat the individual at issue or any individual in a substantially similar position as an employee. Section 530 provides relief to a taxpayer with respect to all individuals holding a substantially similar position to the individual at issue. The substantive consistency requirement looks to how the taxpayer at issue treated the individual and individuals in substantially similar positions. Section 530(e)(6) provides that "the determination as to whether an individual holds a position substantially similar to a position held by another individual shall include consideration of the relationship between the taxpayer and such individuals."

Whether workers are substantially similar is a factual determination. *McLaine v. United States*, 83 A.F.T.R.2d 99-1225 (W.D. Pa. 1999); *Lambert's Nursery and Landscaping, Inc. v. United States*, 894 F.2d 154, 156 (5th Cir. 1990); H.R. Rep. No. 104-737, 104th Cong., 2d Sess., at 201 (1996).

The Fifth Circuit affirmed a magistrate's decision that landscape workers and janitorial workers, workers performing different functions in different industries, were "substantially similar" for purposes of the prior audit safe harbor rule of section 530(a)(2)(B) under the facts in *Lambert's Nursery and Landscaping, Inc. v. United States*, 894 F.2d 154, 156, 157 (5th Cir. 1990). The court explained:

The magistrate found that both groups of workers were treated similarly 'in terms of control, supervision, pay and demands.' The workers were all supervised by persons other than Lambert, although Lambert inspected the work periodically and could control the ultimate result of the work. Lambert provided both groups with some of the materials and tools needed for their work. Both groups were paid by the job, and neither was paid overtime or given fringe benefits. All of the workers were allowed to work for other employers in their time away from their employment with Lambert. None were required to punch in and out on a time clock or to keep a time sheet, and all of Lambert's workers had to provide their own transportation to and from the job site. \*\*\* The relationship of the taxpayer to his workers is the most important element of the § 530(a)(2)(B) analysis, and a taxpayer may reasonably rely on a prior audit pursuant to § 530(a)(2)(B) even though he later employs substantially similar workers in a different industry.

Congress amended Section 530 subsequent to the Lambert's Nursery opinion by adding Section 530(e)(6) under the Small Business Job Protection Act of 1996, Pub. Law 104-188, Sec. 1122, 110 Stat. 1766. Section 530(e)(6) provides that "For purposes of this section, the determination as to whether an individual holds a position substantially similar to a position held by another shall include consideration of the relationship between the taxpayer and such individuals."

In the legislative history of Section 530(e)(6), Congress noted the inconsistency of application of Section 530 in court decisions, specifically citing to the cases of REAG, Inc. v. United States, 801 F. Supp. 494 (W.D. Okla. 1992), and Lowen Corp. v. United States, 785 F. Supp. 913 (D. Kan. 1992). 12 The legislative history also showed disfavor for the Service's position, expressed in its draft training materials, that a "substantially similar position exists if the job functions, duties, and responsibilities are substantially similar and the control and supervision of those duties and responsibilities is substantially similar." Conference Report, H.R. Rep. No. 104-737, 104th Cong., 2d Sess., at 201-202, 204, and 205 (1996) (citing IRS draft training materials). Section 530(e)(6) was added with the intent of providing both the Service and taxpayers with clearer uniform standards for determining which workers could be considered substantially similar in order to reduce the number of disputes between the Service and taxpayers over the application of Section 530, thus reducing unnecessary and costly litigation. General Explanation of Tax Legislation Enacted in the 104th Congress, JCS-12-96, at 87-88.

## 2. Temporary Staffing Services - Temporary

Whether a temporary staffing service is the employer of the workers that it provides to its clients to work at their job sites is based on application of the common law test. As expressed in longstanding revenue rulings, the Service has supported the view that it is appropriate for a temporary staffing service to be the employer of the workers it provides. In Rev. Rul. 56-502, 1956-2 C.B. 688, the Service concluded that a "domestic service agency" that engaged workers to perform services for its clients was the employer. In Rev. Rul. 70-630, 1970-2 C.B. 229, the Service concluded that sales clerks trained by an "employee service" company that assigned them to retail stores to perform temporary sales services were employees of the company. In looking at whether the company directed and controlled the sales clerks, the Service stated that 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.

In Rev. Rul. 75-41, 1975-1 C.B. 323, a physician's professional service corporation provided workers, such as secretaries and nurses, to perform services for its clients. The corporation recruited these workers, paid their wages, provided them with various benefits, and assigned the workers to its clients. The workers agreed that they would not contract directly with the clients for at least three months after cessation of their contract with the corporation. The clients relied on the corporation to provide workers with the needed skills. The ruling held that the corporation was the employer for federal employment tax purposes. Similarly, in Rev. Rul. 75-101, 1975-1 C.B. 318, a professional nursing services corporation engaged the services of licensed practical nurses, ensured they were fully trained and licensed, and assigned them to perform services for the corporation's clients. The corporation provided some instructions, paid the workers weekly, periodically reviewed services provided, and could terminate their services. The ruling held that the corporation had the right to exercise sufficient control that the workers were employees of the corporation for federal employment tax purposes. As illustrated by the accumulated rulings, temporary staffing companies are the employers of the workers where they have the right to direct and control the performance of services, even if the client also performs a supervisory role at the job site.

### 3. Section 3401(d)(1)

A "section 3401(d)(1) employer" is a party who is not the common law employer of employees, but who, rather than the common law employer, has legal control of the payment of wages to the common law employer's employees. Examples of this unusual three-party arrangement include a trustee in bankruptcy paying wages to former employees of the bankrupt company and a surety covering payroll under a surety contract. See *Otte v. United States*, 419 U.S. 43 (1974); *Reliance Insurance Co. v. United States*, 82 A.F.T.R.2d 98-5482, 98-2 U.S.T.C. (CCH) P50,609 (D. Or. 1998); § 31.3401(d)-(1)(f).

## D. Section 530 - Reasonable Basis

### 1.Safe Harbors

Section 530(a)(2) provides for three statutory safe harbors (judicial precedent/ruling, prior audit, and industry practice) for establishing reasonable basis. Given the facts of this case and Taxpayer's position as stated in its letters to the Service, this memo focuses primarily on the prior audit and judicial precedent/ruling safe harbors. A taxpayer that fails to meet any of the three safe harbors may still be entitled to relief if it can demonstrate some other reasonable basis, as discussed below in II.D.2. Provided the other requirements of Section 530 are met, a taxpayer need only qualify for reasonable basis under one of the safe harbors or another reasonable basis in order to establish that it is entitled to relief under Section 530.

#### a.Prior Audit Safe Harbor

Section 530(a)(2)(B) provides that 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 "(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."



Neither the Code nor the regulations provide an express definition of "examination" or "audit." Section 7602 of the Code addresses examination of books and witnesses. Section 7602(a) sets forth the parameters of the authority to conduct an examination of books and witnesses and in this context implicitly defines an examination as an inspection of the taxpayer's books and records, the summoning of persons and documents, and the taking of testimony for the purpose of determining a taxpayer's correct tax liability or collecting such liability. Specifically, § 7602(a) provides:

(a) Authority to Summon, Etc. - For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary is authorized-

(1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;

(2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person... to appear before the Secretary at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.

Section 601.105 of the Statement of Procedural Rules (26 CFR Part 601) addressing examination of returns uses the term "examination" in describing the inspection of the taxpayer's books and records for the purpose of determining the taxpayer's correct tax liability. When the Service exercises its authority under § 7602(a) to conduct an "examination," there are some procedural requirements including a general prohibition against second examinations under § 7605(b) of the Code. Section 7605(b) provides: (b) Restrictions on Examination of Taxpayer. - No taxpayer shall be subjected to unnecessary examination or investigations, and only one inspection of a taxpayer's books of account shall be made for each taxable year unless.... Case law under § 7605(b) provides discussion of what constitutes an examination. Courts have held that an examination would require at a minimum that respondent have access to and physically view the taxpayer's books and records. *Grossman v. Commissioner*, 74 T.C. 1147 (1980); *Benjamin v. Commissioner*, 66 T.C. 1084 (1976), *aff'd* on another issue, 592 F.2d 1259 (5th Cir. 1979); *Curtis v. Commissioner*, 84 T.C. 1349 (1985). Revenue Procedure 2005-32, 2005-1 C.B. 1206, provides, for purposes of § 7605(b), that certain actions by the Service do not constitute examination. For example, narrow, limited contacts or communications between the Service and a taxpayer that do not involve the Service inspecting the taxpayer's books of account are not examinations. See Rev. Proc. 2005-32, sec. 4.03(1).

The Conference Report for the Small Business Job Protection Act of 1996 amendments to Section 530 ratified the Service's position, as stated in its draft training materials, that, for purposes of the Section 530 prior audit safe harbor, a prior audit must involve the examination of a taxpayer's books and records. Mere inquiries from a service center or a compliance check to

determine if a taxpayer filed returns are not audits. Conference Report, H.R. Rep. No. 104-737, 104th Cong., 2d Sess., at 200 (1996). See also S. Rep. No. 104-281, 104th Cong., 2d Sess., at 22 (1996).

According to IRM 4.23.3.6 and 4.23.3.6.1 ([Redacted Text]) 13 , compliance checks:

- 1) Are opportunities to educate and encourage compliance;
- 2) Do not seek to make a determination of a tax liability;
- 3) Inform taxpayers up front, via canned letters, that a compliance check is not an inspection for § 7605(b) or an audit for Section 530 (see IRM Exhibit 4.23.3-3, Sample Letter Advising Taxpayer of an Employment Tax Compliance Check);
- 4) Only consider documents a taxpayer has already voluntarily supplied to the Service;
- 5) Do not request or examine taxpayer books and records;
- 6) Should require no more than two contacts with TP (if more than two contacts are required, an exam should be opened); and
- 7) Are closed out with standard form letters (see IRM Exhibit 4.23.3-4, Sample Follow-up Letter Advising Taxpayer That an Employment Tax Examination Will Not Be Conducted). 14

The leading case involving the prior audit safe harbor provision under Section 530(a)(2)(B) is *Lambert's Nursery and Landscaping, Inc. v. United States*, 894 F.2d 154 (5th Cir. 1990), in which the Fifth Circuit discussed the requirements a taxpayer must satisfy to meet the prior audit safe harbor. From that opinion, it can be determined that a taxpayer must establish (1) that the IRS conducted a prior audit of the taxpayer for a particular tax year; (2) that the IRS determined in the prior audit that the taxpayer's workers were independent contractors; (3) that the workers who were the subject of the prior audit are "substantially similar" to the workers at issue; and (4) that the taxpayer treated the two groups of workers in a "substantially similar" fashion. The Fifth Circuit found that the taxpayer could reasonably rely on a prior audit regarding landscape workers in treating as independent contractors the janitorial workers it hired in later years when it expanded the business. In *Smoky Mountain Secrets, Inc. v. United States*, 910 F. Supp. 1316 (E.D. Tenn. 1995), the Court cited to and followed *Lambert's Nursery* in determining whether the prior audit safe harbor provision applied under the facts of that case (court held that prior audit safe harbor provision did not apply due to failure of taxpayer to establish the existence of a past IRS audit).

A taxpayer may not rely on an audit commenced after 1996 for purposes of the prior audit safe harbor unless the audit included an examination for employment tax purposes of whether the individual involved (or any individual holding a position substantially similar to the position held

by the individual involved) should be treated as an employee of the taxpayer. Section 530(e)(2)(A).

To come within a safe harbor of section 530(a)(2), the taxpayer must have relied on the alleged authority for the entire period in question. "The statute does not countenance ex post facto justification." *Nu-Look Design, Inc. v. Commissioner*, T.C. Memo. 2003-52, aff'd, 356 F.3d 290 (3d Cir. 2004), cert. den., 543 U.S. 821 (2004) (citing to 303 W. 42nd St. Enters., Inc. v. IRS, 181 F.3d 272, 277, 279 (2d Cir. 1999) and *Select Rehab, Inc. v. United States*, 205 F. Supp. 2d 376, 380 (M.D. Pa. 2002)). See also, *Peno Trucking, Inc. v. Commissioner*, 296 Fed. Appx. 449, 102 A.F.T.R.2d 2008-6433 (6th Cir. 2008) (opinion not recommended for full-text publication).

#### b. Judicial Precedent/Ruling Safe Harbor

Section 530(a)(2)(A) provides that 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 "judicial precedent, published rulings, technical advice with respect to the taxpayer, or a letter ruling to the taxpayer."

As to technical advice or letter rulings, Section 530(a)(2)(A) provides, in part, that to satisfy the safe harbor, there must be reasonable reliance on "technical advice with respect to the taxpayer, or a letter ruling to the taxpayer." The SBJPA of 1996 Conference Report in H.R. No. 104-737, 104th Cong. 2d. Sess., at 200, also provides that the reliance must be on "technical advice with respect to the taxpayer or a letter ruling to the taxpayer." The TRA 1978 legislative history in H.R. No. 95-1748, 95th Cong. 2d. Sess., at 5, provides that the reasonable reliance must be on "technical advice with respect to the taxpayer, or a ruling (for example, a "letter ruling" or a "determination letter") issued to taxpayer." Rev. Proc. 2009-1, 2009-1 I.R.B. 1, and its predecessors define a "determination letter" as a written determination issued by a Director that applies the principles and precedents previously announced by the Service to a specific set of facts. IRM 7.1.2.2.2(1). Thus, a taxpayer may only reasonably rely upon technical advice or letter rulings relating specifically to the taxpayer.

As to judicial precedent or published rulings, the Service will look to whether the facts of the judicial precedent or published rulings are sufficiently similar to the taxpayer's facts. See SBJPA of 1996 Conference Report, H.R. No. 104-737, 104th Cong. 2d Sess., at 200 (1996); General Explanation of Tax Legislation Enacted in the 104th Congress, Joint Committee on Taxation, JCS-12-96 at 85 (1996). Under this test, the judicial precedent or published ruling upon which a taxpayer reasonably relied does not have to relate, necessarily, to the particular industry or business in which the taxpayer is engaged. General Explanation of the Revenue Act of 1978, Joint Committee on Taxation at 302 (1979); H.R. Rep. No. 95-1748, 95th Cong., 2d Sess., at 5 (1978).

The reasonable basis requirement is to be construed liberally in favor of the taxpayer. H.R. Rep. No. 95-1748, 95th Cong., 2d Sess., at 4 (1978), 1978-3 (Vol. 1) C.B. 629 and 633. Whether a taxpayer may reasonably rely upon favorable judicial precedent where there are both favorable and unfavorable precedent has not been squarely considered by the courts or in formal guidance. But IRS training materials provide that one case may be sufficient to establish a judicial precedent to create a safe harbor. 15 The IRM also contains this provision. IRM 4.23.5.2.2.4(2).

For a taxpayer to have a reasonable basis for not treating an individual as an employee under the judicial precedent safe harbor, the judicial precedent relied upon must have evaluated the employment relationship through a Federal common law analysis. *Peno Trucking, Inc.* (citing *Nu-Look Design, Inc. v. Commissioner*, T.C. Memo 2003-52, *affd.*, 356 F.3d 290 (3d Cir. 2004)). Furthermore, to come within the safe harbor, "the taxpayer must have relied on the alleged authority during the periods in issue, at the time the employment decisions were being made. The statute does not countenance *ex post facto* justification." *Nu-Look Design*, *supra*.

## 2. Other Reasonable Basis

A taxpayer that fails to meet any of the three safe harbors may nevertheless be entitled to relief if the taxpayer can demonstrate, in some other manner, a reasonable basis for not treating the individual as an employee. *Rev. Proc. 85-18*, 1985-1 C.B. 518, sec. 3.01. *Smoky Mountain Secrets, Inc. v. United States*, 910 F. Supp. 1316, 1323 (E.D. Tenn. 1995) (reliance on the advice of two professional tax advisors, both CPAs, was sufficient to show reasonable basis); *Veterinary Surgical Consultants, P.C. v. Commissioner*, 117 T.C. 141, 147 (2001) (no reasonable basis where taxpayer cited rulings and cases that did not support its position), *affd. sub nom.*, *Yeagle Drywall Co. v. Commissioner*, 54 Fed. Appx. 100 (3d Cir. 2002).

## E. Section 530 - Burden of Proof

Generally, it is the taxpayer's burden to establish by a preponderance of the evidence that it meets the requirements of Section 530. *Boles Trucking, Inc. v. United States*, 77 F.3d 236, 241 (8th Cir. 1996); *Springfield v. United States*, 88 F.3d 750, 753 (9th Cir. 1996). The Small Business Job Protection Act of 1996 amended Section 530 to add the burden of proof provision, now contained in Section 530(e)(4), that provides that once the taxpayer makes a *prima facie* case and the taxpayer has cooperated with reasonable requests from the IRS, the burden of proof shifts to the IRS.

Thus, a taxpayer must first establish a *prima facie* case that it met each of the substantive consistency, reporting consistency, and reasonable basis requirements in order for the burden to shift to the Service. See Conference Report, H.R. No. 104-737, 104th Congress, 2d Sess., at 203-204, footnote 24 (1996) and *Ramirez v. Commissioner*, T.C. Memo 2007-346 at 5. This burden of proof shift does not apply to the catchall "other reasonable basis" category of the reasonable basis requirement. Section 530(e)(4)(B).

The burden of proof provision added in 1996 is generally intended to codify the holding in *McClellan v. United States*, 900 F. Supp 101 (E.D. Mich. 1995). In *McClellan*, the court held that Section 530 requires the "taxpayer to come forward with an explanation and enough evidence to establish *prima facie* grounds for a finding of reasonableness. ... This threshold burden is relatively low, and can be met with any reasonableness showing. Once the taxpayer has made this *prima facie* showing, the burden then shifts to the IRS to verify or refute the taxpayer's explanation." See H.R. No. 104-737, 104th Congress, 2d Sess., at 203, footnote 25.

## ANALYSIS

Our analysis begins by addressing the status of the closing agreement that the Service executed with Taxpayer. We consider both whether the closing agreement applies to [Redacted Text] (or any subsequent year) and also whether the closing agreement affects the availability of Section

530 relief. Next we consider whether Taxpayer meets the requirements for relief under Section 530 for the Category A Workers.

## I. [Redacted Text] Closing Agreement

### A. Whether [Redacted Text] Closing Agreement Applies

The [Redacted Text] Closing Agreement is clear and unambiguous on its face. It binds the Service as to its determination and agreement that the relationship between Taxpayer and the Category A Workers is not inconsistent with an independent contractor relationship so long as the Taxpayer and the Category A Workers operate in accordance with the terms of the [Redacted Text] Agreement. The closing agreement only applies to operations under the provisions of the [Redacted Text] Agreement. The scope of a closing agreement is limited by statute. The closing agreement does not extend to a situation where Taxpayer and the Category A Workers operate under the terms of another (or altered) agreement. In other words, the closing agreement binds the Service for the finite time frame in which Taxpayer and the Category A Workers agreed to operate and did in fact operate in accordance with the terms of the [Redacted Text] Agreement.

Over the years, Taxpayer has changed the terms of the [Redacted Text] agreement it uses with Category A Workers from what was in the [Redacted Text] Agreement, mainly by addenda. The differences between the [Redacted Text] Agreement and the agreements in use in [Redacted Text] were substantive, not superficial. In light of these changes, the [Redacted Text] Closing Agreement no longer applies. The addenda to the [Redacted Text] Agreement and the new [Redacted Text] and [Redacted Text] agreements executed between Taxpayer and the Category A Workers constitute a modification of the terms of [Redacted Text] Agreement. The changes were not merely cosmetic changes to names or addresses, but rather changes to terms and conditions of the agreement. For example, one modification changed the compensation structure by altering the financial rewards available to the Category A Workers depending on the type of [Redacted Text] used. Another change shortened the [Redacted Text] agreements' duration from a maximum [Redacted Text] term to a maximum [Redacted Text] term, which meant that Taxpayer effectively had the power to dismiss Category A Workers without cause sooner than under the previous [Redacted Text] agreement. And yet another change added an additional duty, requiring Category A Workers to cooperate in taxpayer's defense of legal claims or have to indemnify Taxpayer for the claims. These were changes to the substantive terms of the [Redacted Text] Agreement. Under the legal standards applicable to closing agreements, any substantive change from the specific facts described terminates the future application of the [Redacted Text] Closing Agreement.

### B. Waiver of Section 530 Relief

It has been suggested that the closing agreement can be read to mean that Taxpayer waived its rights under Section 530 for future periods because the closing agreement is specific to the issue of worker classification, and term [Redacted Text] of the agreement places no limit on the number of audits the IRS can conduct. Section 530 is a significant tax provision that gives taxpayers important rights. Accordingly, a waiver cannot be implied. It must be explicit. Moreover, as the IRS was a drafting party to the closing agreement, the terms would be construed narrowly against the IRS. The closing Agreement is silent as to the applicability of Section 530. The provision authorizing audits says nothing about the implication of those audits for the prior audit safe haven or any other aspect of Section 530. Finally, correspondence

exchanged at the time the closing agreement was being drafted indicates the intent of the parties to avoid limiting any rights to Section 530 relief. Therefore, Taxpayer has sound legal support for the position that it did not waive its rights under Section 530 for any future period when it entered into the closing agreement. We do not see sound legal support for an argument to the contrary.

## II. Section 530

### A. Generally

If Taxpayer meets each of the three requirements of reporting consistency, substantive consistency, and reasonable basis, it is entitled to relief from Federal employment tax liability under Section 530, regardless of how the Category A Workers would otherwise be classified for employment tax purposes.

### B. Section 530 - Reporting Consistency

To meet the requirement of reporting consistency under Section 530, a taxpayer must have filed all Federal tax returns consistent with its treatment of the workers in question as not being employees of the taxpayer. In this case, Taxpayer filed Forms 1099 with respect to each of the Category A Workers at issue. The examination revealed that there were a few instances where Taxpayer issued both Form W-2 and Form 1099 to certain Category A Workers. Taxpayer explained that these were isolated instances where an employee, such as a [Redacted Text], became a Category A Worker. It would have issued Form W-2 for the period the worker was an employee performing [Redacted Text] duties and Form 1099 for the period of time where the worker was a Category A Worker. There is no factual basis in the exam record to the best of our knowledge to contradict Taxpayer's explanation. Accordingly, the record supports the conclusion that Taxpayer meets the reporting consistency requirement necessary for relief under Section 530 for Category A Workers.

### C. Section 530 - Substantive Consistency

A taxpayer satisfies the substantive consistency requirement of Section 530 if the taxpayer (or predecessor) did not treat the workers at issue or any individual in a substantially similar position as an employee for employment tax purposes. Taxpayer did not treat any of the Category A Workers as its employees (exception being the limited cases where Taxpayer issued both Form W-2 and Form 1099 to certain Category A Workers, explained above). Nor did it treat other [Redacted Text] with [Redacted Text] agreements, including [Redacted Text], as employees.

We have been asked whether the temporary staffing services' treatment of [Redacted Text] as employees should be taken into account for evaluating whether Taxpayer meets the substantive consistency requirement. Although Taxpayer made use of temporary [Redacted Text] to perform some functions comparable to functions performed by the Category A Workers, Taxpayer secured their services through its contracts with TSS1 and TSS2. While the record contains little information about the size and scope of TSS1, TSS2 is a large temporary staffing service that serves many unrelated clients in different industries. Taxpayer did not treat any of the temporary [Redacted Text] as its workers, let alone its employees for federal employment tax purposes. Conversely, both temporary staffing services treated the temporary [Redacted Text] as their

employees for Federal employment tax purposes at all times and in accord with the contractual agreements negotiated between Taxpayer and the temporary staffing services.

IRS published guidance has repeatedly confirmed that it is appropriate for a temporary staffing service to treat its workers as its employees where the temporary staffing service has the right to direct and control their work, even though the workers are receiving day to day direction and supervision from the client company at the work site. See for example, Rev. Rul. 75-101, Rev. Rul. 75-41, and Rev. Rul. 70-630. The facts with respect to Taxpayer's contracts with TSS1 and TSS2 appear to be consistent with the published guidance. The facts indicate that TSS1 and TSS2 treated the temporary [Redacted Text] as their employees at all times, reporting and paying employment taxes and issuing Forms W-2. Accordingly, the published rulings establish that the temporary staffing services are the common law employers of the temporary [Redacted Text].

The facts indicate that at least some of the temporary [Redacted Text] may not have been aware that they were employed by TSS1 or TSS2 rather than Taxpayer. They applied for employment at one of Taxpayer's facilities, interacted entirely with Taxpayer's employees in being hired and trained, and worked exclusively for Taxpayer. They may have become aware of TSS1 or TSS2 only when they received paychecks or Forms W-2 that identified TSS1 or TSS2 as their employer. Although some temporary [Redacted Text] may have had the impression that Taxpayer was their employer, under the Service's published guidance, workers may be employees of a temporary staffing service. The facts with respect to Taxpayer are consistent with treating TSS1 and TSS2, rather than Taxpayer, as the common law employer. Accordingly, the temporary [Redacted Text] are not taken into account for purposes of the substantive consistency requirement as it related to the Category A Workers for Taxpayer.

Thus, we conclude that Taxpayer has satisfied the substantive consistency requirement of Section 530(a)(3).

Additionally, we note that even if the temporary [Redacted Text] were taken into account for purposes of evaluating whether Taxpayer meets the substantive consistency requirement, the facts indicate that the temporary [Redacted Text] are not substantially similar to the Category A Workers. The temporary [Redacted Text] do not have [Redacted Text] agreements with Taxpayer, the temporary [Redacted Text] are not required to [Redacted Text], and they do not [Redacted Text]. They are paid for time worked rather than under the formulas used for Category A workers. Under section 530(e)(6), it is not only the function performed by two sets of workers but also the relationships between the workers and the firm that must be taken into account in determining whether the two sets are substantially similar. These differences for the temporary [Redacted Text] are significant and lead us to conclude that, even if the temporary [Redacted Text] were taken into account, they are not substantially similar to the Category A Workers.

Thus, overall, based on the facts developed in the examination, Taxpayer has satisfied the substantive consistency requirement with respect to Category A Workers.

#### D. Section 530 - Reasonable Basis

To meet the third requirement for Section 530 relief, a taxpayer must have a reasonable basis for not treating the workers in question as employees. As noted above, Congress intended for Section 530, including the "reasonable basis" requirement, to be construed liberally in favor of the taxpayer. Taxpayer takes the position in its letters to [Redacted Text] IRS Team Coordinator,

of [Redacted Text], to [Redacted Text] IRS Team Coordinator, of [Redacted Text], and to IRS Counsel, [Redacted Text], and in its [Redacted Text], response to IDR ET[Redacted Text], that it is entitled to the prior audit safe harbor based on the Service's audits of the [Redacted Text] and [Redacted Text] tax years, and to the judicial precedent/ruling safe harbor based on (a) the [Redacted Text] Closing Agreement [Redacted Text], (b) a PLR and a TAM issued to other taxpayers, (c) SS-8 determinations, (d) an [Redacted Text] NLRB decision in which [Redacted Text] the worker classification of [Redacted Text] was at issue, and (e) other court and administrative cases. Given the facts of this case and Taxpayer's position, we have focused on whether the prior audit or judicial precedent/ruling safe harbors are a means for Taxpayer to establish reasonable basis.

## 1.Safe Harbors

### a.Prior Audit Safe Harbor

To come within the terms of the safe harbor of 530(a)(2)(B), a prior Service investigation must have been an audit that considered worker classification. Under the Tax Court's opinion in Benjamin, an audit involves an inspection of a taxpayer's books of account. ("To inspect the 'books of account' would require, at a minimum, that the respondent have access to and physically view a taxpayer's books and records.") 66 T.C. at 1098; Grossman, *supra*; Curtis, *supra* . Also, a taxpayer must have relied on the results of the audit, meaning that the audit must have closed before the beginning of the year for which Section 530 relief is claimed.

There were several employment tax investigations of Taxpayer between [Redacted Text] and [Redacted Text]. Taxpayer asserts that the audits for the tax years [Redacted Text] and [Redacted Text] were prior audits that entitle it to the safe harbor. See letters dated [Redacted Text] response to IDR ET[Redacted Text]. We consider each one separately.

During [Redacted Text] and [Redacted Text], the Service conducted an employment tax examination of Taxpayer for tax years [Redacted Text]. Although the files with respect to the examination are incomplete, the material they contain supports the conclusion that this was an examination and not a compliance check. The Service's examination plan for [Redacted Text] specifically discussed the previous examination of Taxpayer and resolution for years through [Redacted Text], as well as the [Redacted Text] closing agreement. The files do not show that the Service provided Taxpayer with a letter stating that the inquiry was a compliance check and not an examination, as would have been required by the IRM in effect at that time for a compliance check. IRM 4.23.3.6.1 ([Redacted Text]). The Service issued an employment tax IDR and reviewed Taxpayer books and records to determine whether Taxpayer was conducting its operations in accordance with the [Redacted Text] agreement. The Service reviewed Taxpayer company manuals, procedures, and policy statements and the revised [Redacted Text] agreement. It obtained an analysis of [Redacted Text] comprised of payees and dollar amounts. The Service issued a no-change letter (Letter 590) dated [Redacted Text] to Taxpayer concerning Form 941 for all periods in [Redacted Text] and [Redacted Text]. The audit was closed before [Redacted Text], the year for which Taxpayer claims relief. The nature of the materials requested and reviewed and the issuance and contents of the no-change letter show that the Service conducted an audit of Taxpayer's books and records for tax years [Redacted Text]. The review of material related to the closing agreement show that the Service considered the classification of the Category A Workers, comparing actual operations to the terms of the [Redacted Text] agreement.



During [Redacted Text], the Service conducted an examination of [Redacted Text] for tax years [Redacted Text]. Again, the files are incomplete. However, they are consistent with an audit. The examination plan describes a category entitled "Worker Classification." While the files indicate that this was an examination of [Redacted Text], the [Redacted Text], the files include IDRs specific to Taxpayer. Although the last employment tax IDR response was received by the Service in [Redacted Text], it is not clear from the facts that this examination was concluded before [Redacted Text] or whether any employment tax portion concerned only the [Redacted Text]. There is no closing letter, and there is an Appeals Case Memorandum in the file dated [Redacted Text].

Beginning in [Redacted Text], the Service also audited [Redacted Text] and its subsidiaries for tax years [Redacted Text]. It is not clear when this audit closed; the latest document in the file is dated [Redacted Text]. The files show that the Service issued IDRs for names of workers who received a Form 1099. A note regarding a [Redacted Text], meeting stated "[Redacted Text]. .. Closing agreement will take time file [Redacted Text]audit (we looked at closing agreement last cycle & approved method no proposed). " These facts indicate that the Service may have considered the worker classification of the Category A Workers. Thus, the content of this audit may provide Taxpayer with a reasonable basis for not treating Category A Workers as employees under the prior audit safe harbor, but it is not clear from the facts that this examination was concluded before [Redacted Text].

An employment tax audit of [Redacted Text] and its subsidiaries for tax years [Redacted Text] was begun in [Redacted Text]. It was closed in [Redacted Text] as indicated in an attachment to the Form 2504, which states: "The IRS agrees to close the [Redacted Text] employment tax examination and open the employment tax periods encompassing the [Redacted Text] calendar year. Since prior examinations have not resulted in material changes in the employment tax area and to help expedite this review, the [Redacted Text] employment tax periods for [Redacted Text] will not be opened for examination and the examination of the [Redacted Text] periods will be limited to the review of worker classification issues." Even if this audit had gone forward to conclusion, the timing of the examination means that Taxpayer could not have relied on its result to supply reasonable basis under the prior audit safe harbor.

Taxpayer has the necessary elements to make a prima facie case that it qualifies for the prior audit safe harbor with respect to the Category A Workers based on the prior audit of Taxpayer for tax years [Redacted Text]. Rebutting the Taxpayer's position requires that the Service show that the workers examined in [Redacted Text] are not substantially similar to the workers examined in [Redacted Text]. The Service bears the burden of proof to rebut Taxpayer's claim to the prior audit safe harbor for Category A Workers.

A comparison between the [Redacted Text] agreement used in [Redacted Text] and the [Redacted Text] agreement used in [Redacted Text] shows some substantive changes. As discussed above, these substantive changes are sufficient to terminate any further application of the [Redacted Text] Closing Agreement under the legal standards applicable to closing agreements. However, these changes were limited in scope. The items changed were as follows: the compensation structure was made dependent on the type of [Redacted Text] used; the contracts' duration was reduced from a maximum [Redacted Text] term to a maximum [Redacted Text] term; and Category A Workers were required to cooperate in Taxpayer's defense of legal claims or indemnify Taxpayer for the claims. These amendments did not change the fundamental relationship between Taxpayer and the Category A Workers. Category A Workers still must

supply their own [Redacted Text] and still are paid using a standardized [Redacted Text] formula with additional consideration for [Redacted Text]. Category A Workers are still permitted to [Redacted Text] and provide a [Redacted Text]. Insurance obligations are still split the same way as they were in the [Redacted Text] Agreement.

Under section 530(e)(6), the relationship between the workers and a taxpayer is a critical element in determining whether any two groups of workers are substantially similar. The records in this case are incomplete and not clear as to what the [Redacted Text] audit found with respect to Taxpayer's operations during [Redacted Text]. The issuance of a no-change letter implies that the Service concluded that operations were consistent with the [Redacted Text] agreement as required under the closing agreement. The facts developed in this examination, as we understand them, do not establish differences in operation between the [Redacted Text] years and the [Redacted Text] year, nor do they show that operations are different from what the Service reviewed in the prior audit. Based on the facts in the audit record with respect to the [Redacted Text] agreements and actual operations, we conclude that the positions of the Category A Workers in [Redacted Text] were substantially similar to those of Category A Workers in [Redacted Text]. Thus, relying on the audit of the [Redacted Text] years, Taxpayer qualifies for the prior audit safe harbor to establish reasonable basis for treating the Category A Workers as independent contractors for [Redacted Text].

#### b. Judicial Precedent/Ruling Safe Harbor

Taxpayer takes the position that it also qualifies for the safe harbor based on judicial precedents or rulings. In letters dated [Redacted Text], Taxpayer states that its treatment of the Category A Workers is reasonable based on [Redacted Text] a determination of the National Labor Relations Board from the year [Redacted Text] which considered [Redacted Text], and a number of other NLRB and court decisions. Subsequently, in its response to IDR ET[Redacted Text] dated [Redacted Text], Taxpayer claimed that it relied on the [Redacted Text] Closing Agreement [Redacted Text], a number of additional court decisions, SS-8 rulings issued to its Category A Workers, rulings issued to two other taxpayers, and industry practice. We consider each of these in turn.

##### (i) [Redacted Text] Closing Agreement

Taxpayer lists as one of its reasonable bases the [Redacted Text] Closing Agreement [Redacted Text] While the closing agreement may provide "other reasonable basis," it was not a ruling that Taxpayer could rely upon to satisfy the criteria for this safe harbor. [Redacted Text]

##### (ii) PLR and TAM

In connection with the closing agreement [Redacted Text], Taxpayer states in its response to IDR ET[Redacted Text]: "The IRS has also issued guidance to other taxpayers consistent with such classification." It lists PLR [Redacted Text] and TAM [Redacted Text]. We note that those determinations were not issued to Taxpayer. The PLR and TAM do not provide a safe harbor to Taxpayer under Section 530(a)(2)(A), because that safe harbor requires that technical advice be "with respect to the taxpayer" and that a letter ruling be "to the taxpayer." Neither PLR [Redacted Text] nor TAM [Redacted Text] was issued to Taxpayer.

##### (iii) SS-8 Determinations

The Service has received numerous requests from Taxpayer's workers for worker status determinations through the SS-8 process. We learned from the Service's SS-8 Unit that [Redacted Text] SS-8 cases with Taxpayer's EIN were closed in [Redacted Text], but the Service no longer has access to those records. The SS-8 Unit believes that those cases were closed with a letter to the worker but without a letter to Taxpayer. We understand that one letter issued during [Redacted Text] was correspondence (not a determination letter) to one worker stating that, based on the facts the worker presented, it appeared the worker was an employee.

Taxpayer states in its [Redacted Text], response to IDR ET[Redacted Text]: "The Internal Revenue Service has issued determinations in response to classification requests on Forms SS-8 that contractors were independent contractors rather than employees." In its [Redacted Text], letter to IRS Counsel, Taxpayer states:

On [Redacted Text], the IRS issued [Redacted Text] SS-8 determination letters that said '[t]he Internal Revenue Service maintains that [Taxpayer] is adhering to the [Redacted Text] Agreement of [Redacted Text] that is not inconsistent with treatment of the [Redacted Text] as independent contractors. Accordingly, it is held that the worker was not an employee of the firm....' See [Redacted Text] letter to [Redacted Text], attached as Exhibit [Redacted Text].

The attached letter was addressed to Taxpayer and responded to a Form SS-8 regarding Taxpayer, referred to as the firm, and a worker named [Redacted Text]. The letter stated:

Information submitted indicates that the firm is in the [Redacted Text] business and the worker was engaged to perform [Redacted Text] services. The Internal Revenue Service maintains that [Taxpayer] is adhering to the [Redacted Text] Agreement of [Redacted Text] that is not inconsistent with treatment of the [Redacted Text] as independent contractors. Accordingly, it is held that the worker was not an employee of the firm for purposes of the [FICA, FUTA], or for collection of income tax at the source of wages.

From [Redacted Text], the Service issued [Redacted Text] letters to Category A Workers, stating that the Service declined to rule due to the [Redacted Text] closing agreement and noting that the agreement says that operations conducted in accordance with the terms of the [Redacted Text] Agreement will not be inconsistent with treatment of the Category A Workers as independent contractors. We understand that these letters were not sent to Taxpayer.

Determination letters issued to workers but not to Taxpayer do not provide a safe harbor under Section 530(a)(2)(A) because they are not a letter ruling to the taxpayer. However, if the [Redacted Text] letters claimed were in fact issued to Taxpayer holding that individual Category A Workers were independent contractors, they would be letter rulings sufficient to provide a safe harbor under Section 530(a)(2)(A).

#### (iv) NLRB Decision

Taxpayer also contends that it relied on [Redacted Text] NLRB Regional Director's decision holding that [Redacted Text] were not common law employees [Redacted Text] for NLRA purposes. Taxpayer cites this case separately because the NLRB Regional Director carefully

[Redacted Text] and found that [Redacted Text] were not employees. Taxpayer also cites to this case as the NLRB Regional Director considered [Redacted Text].

The opinion notes that "[Redacted Text].

The NLRB Regional Director's opinion states that [Redacted Text] The opinion states that it applied the common law agency test as interpreted by the Supreme Court in *NLRB v. United Insurance Co. of America*, 390 U.S. 254 (1968). This is the same test used to determine whether a worker is an employee for purposes of Federal employment taxes. *Nationwide Mutual Insurance Co. v. Darden*, 503 U.S. 318 (1992) (citing *Community for Creative Non-Violence v. Reid*, 490 U.S. 730 (1989) ("... when Congress has used the term 'employee' without defining it, we have concluded that Congress intended to describe the conventional master-servant relationship as understood by common-law agency doctrine." )); *Weber v. Commissioner*, 103 T.C. 378 (1994).

As explained above, in determining whether a taxpayer falls within the judicial precedent safe harbor, the Service will look to whether the facts of the judicial precedent are sufficiently similar to the taxpayer's facts. One case may be sufficient to establish a judicial precedent to create a safe harbor. The precedent relied on must have evaluated the employment relationship through a Federal common law analysis. Taxpayer must have relied on the authority during the periods in issue. It appears that all of these criteria, including similarity of the facts, are met. We can think of three possible arguments to the contrary, although we do not find them persuasive.

First, while it might be argued that it is not reasonable for Taxpayer to rely on an opinion that considered such a small sample [Redacted Text]. Second, it might be argued that it is not reasonable to rely on an opinion by a different Federal agency to establish a reasonable classification for employment tax purposes because that agency may be applying different law. But the NLRB stated that it applied the common law of agency; this is the same standard used for worker classification for employment tax purposes. Third, it might be argued that competing precedents from the NLRB and state courts have reached divergent conclusions about whether [Redacted Text] are employees or independent contractors, 16 and thus it is not reasonable to rely on a single lower level precedent covering a handful of workers when there are a number of precedents with competing conclusions. However, the Service's IRM and training materials state that one case is sufficient to establish a precedent that creates a safe harbor. Further, the NLRB opinion shows an exhaustive inquiry into the facts and thoughtful consideration of the contrary arguments before concluding that [Redacted Text] were not employees. Although this is a novel question, and selection of a [Redacted Text]. [Redacted Text] single opinion from a mixed record may not always be sufficient, we think a court would likely find Taxpayer's reliance on this opinion reasonable.

#### (v) Other Court and Administrative Decisions

In its letter dated [Redacted Text], Taxpayer contended that it relied on [Redacted Text] (discussed previously). Taxpayer stated: "The NLRB ruling, if not in and of itself decisive, clearly provides a reasonable basis for [Taxpayer's] position in this matter. We have provided the following additional judicial precedent in support of the reasonable basis standard...." The letter lists the following [Redacted Text] court and administrative decisions:

[Redacted Text].

Additionally, in an [Redacted Text], letter to IRS Counsel, Taxpayer states: "... in determining to classify Contractors as independent contractors, [Taxpayer] relied on long-standing authority for treating [Redacted Text] as non-employees." It cites [Redacted Text] court decisions. In its response to IDR ET[Redacted Text], Taxpayer cites the same [Redacted Text]cases, plus [Redacted Text] additional court decision. These court decisions are: [Redacted Text]

Instead of considering each case one by one, we will consider them under the criteria applied in determining whether they can provide a basis for the judicial precedent safe harbor.

Criterion 1. Taxpayer must have relied on the cited authority during the period at issue, in this case the year [Redacted Text]. The authority cannot provide an ex post facto justification. Thus, if the authority is dated after [Redacted Text], Taxpayer could not have relied on it for the [Redacted Text] tax year, and it cannot provide a basis for the safe harbor. Cases in this category include:

[Redacted Text]. 17

Criterion 2. The authority must have evaluated the employment relationship using a Federal common law analysis. The following cases meet that requirement. [Redacted Text]. It must still be considered whether these cases meet the third requirement.

Criterion 3. The facts of the cited authority must be sufficiently similar to the taxpayer's facts. [Redacted Text]

Taxpayer did not set forth adequate facts to establish that it relied on these cases. Accordingly, we cannot with certainty project whether Taxpayer could establish that it qualifies for this safe harbor on the basis of these opinions in this context. However, with multiple precedents available to cite, Taxpayer is likely to at least establish that it has made a prima facie case and therefore shift the burden of proof to the Service.

## 2.Other Reasonable Basis

Even if Taxpayer falls short of meeting one of the safe harbors, it may still potentially show it has some other reasonable basis for treating the Category A Workers as other than employees. Thus, even if the Service's review of the years [Redacted Text] were viewed as a compliance check rather than an examination, [Redacted Text] and even if the NLRB Regional Director's decision were not considered suitable judicial precedent, Taxpayer may still raise all of these items to claim that it had "other reasonable basis" for treating its Category A Workers as independent contractors.

For example, Taxpayer can say that regardless of whether the Service's review of the [Redacted Text] years was an audit or a compliance check, at its conclusion, the Service did not express any concerns or questions about Taxpayer's compliance with the [Redacted Text] Closing Agreement. In fact, to this day the Taxpayer continues to act in a way that shows it believes the closing agreement is applicable when it files copies of Forms 1099 for all Category A Workers ([Redacted Text]) [Redacted Text]. [Redacted Text]. Taxpayer may argue that it relied on the Service's acceptance of these continued filings with no notice to the Taxpayer that past changes to the [Redacted Text] Agreement were sufficient to terminate the closing agreement as

implicitly indicating that the closing agreement still applied, and that Taxpayer was in compliance with it.

Taken cumulatively, the sheer volume of cases and rulings, combined with the Service's course of conduct in light of Taxpayer's unique history with the [Redacted Text] Closing Agreement, [Redacted Text] and the repeated audits, would likely support a showing of other reasonable basis for purposes of Section 530 relief.

In conclusion, looking at the total set of arguments Taxpayer makes for reasonable basis against the backdrop of legislative history, Lambert's Nursery, section 530(e)(6), multiple audits specific to the Category A Workers, the closing agreement, [Redacted Text] and the fallback category of other reasonable basis, we conclude that on balance the law as applied to the facts supports Taxpayer's claim that it had a reasonable basis for treating its Category A Workers as independent contractors.

If you have any questions, please contact [Redacted Text] or me at (202) 622-0047.

Office of Division Counsel/[Redacted Text]

Associate Chief Counsel

(Tax Exempt and Government Entities)

1 Although the [Redacted Text] agreement permits the Category A Workers to sell their [Redacted Text], we note that the [Redacted Text] agreement also requires that each [Redacted Text] must be approved by Taxpayer.

2 A "temporary [Redacted Text]" should not be confused with a [Redacted Text]. " A [Redacted Text] is a contract [Redacted Text]who may or may not have a [Redacted Text]. The [Redacted Text] is generally one who has a lengthy history as a contract [Redacted Text] for Taxpayer and who fills in for [Redacted Text] that are not being covered on a given day. A [Redacted Text] receives pay for his services directly from Taxpayer. A temporary [Redacted Text] is one who does not [Redacted Text], is not covered under contract with Taxpayer, and who reports to [Redacted Text] each day for purposes of performing his work. A temporary [Redacted Text] receives his pay from a temporary staffing service. Both [Redacted Text] and temporary [Redacted Text] must first be approved by Taxpayer before being allowed to [Redacted Text].

3 The parties amended this contract in [Redacted Text], indicating that the prior agreement was between Taxpayer [Redacted Text] and TSS2, and states that the parties agree that the terms of the prior contract do apply to [Redacted Text].

4 See Section [Redacted Text] of TSS2 contract. Under the contract, Taxpayer is also required to review and approve the time records submitted by the temporary [Redacted Text] employed by TSS2. See Section [Redacted Text] of contract.

5 The closing agreement stated that it did not preclude the Service from issuing a determination letter or ruling in response to the filing of a Form SS-8 by a [Redacted Text].

6 Paragraph [Redacted Text], [Redacted Text], in the [Redacted Text] Agreement, provides that the [Redacted Text]: [Redacted Text]

7 [Redacted Text]

8 [Redacted Text]

9 It is not clear from the record which entity this relates to.

10 Since this record is clearly one page of a much larger report and refers to a meeting held after the date written on the page, the [Redacted Text] date is likely erroneous.

11 See Training Materials, "Independent Contractor or Employee?", Department of the Treasury, Internal Revenue Service, Training 3320-102 (Rev. 10-96), TPDS 84238I, at p. 1-1; IRM 4.23.5.2(3); IRM 4.23.5.2.1(1); and IRM 4.23.5.2.2(6).

12 In REAG, Inc., the court held that the position of appraisers who were owner-officers of the business was not substantially similar to that of appraisers who were not owners since the owner-officers had managerial responsibilities. In contrast, the court in Lowen found that all workers engaged in the business of selling real estate signs had substantially similar positions even though some were salaried and had to file daily reports while others were paid by commission and did not have to file such reports.

13 This is the version that was in effect during [Redacted Text]. The material regarding compliance checks was removed from the IRM in March 2009 with an explanation that compliance checks are no longer used. However, these provisions were in place in [Redacted Text], the year at issue.

14 See also, Publication 3114 (Rev. 1-2005), Compliance Checks: Compliance Check, Audit, Examination, or Review? and Publication 4386 (Rev. 4-2006), Compliance Checks: Examination, Audit or Compliance Check?, Tax Exempt and Government Entities Division.

15 IRS training materials provide that one case is sufficient to establish a precedent that creates a safe harbor. These materials also provide that this is true even if case law can be found to support either side of the independent contractor/employee issue. Training Materials, "Independent Contractor or Employee?", Department of the Treasury, Internal Revenue Service, Training 3320 -102 (Rev. 10-96), TPDS 84238I, at p. 1-24. The Training Materials, however, do not consider the effect of an unfavorable precedent in the taxpayer's jurisdiction compared to a favorable precedent outside the taxpayer's jurisdiction.

16 See, e.g., [Redacted Text]

17 We are aware of additional contrary authority which was not cited by Taxpayer. Because Taxpayer could not have known of these post [Redacted Text] cases in [Redacted Text], these cases do not cast doubt on the reasonableness of Taxpayer's reliance on its cited authority.