

February 24, 2010

MEMORANDUM TO CLIENTS

RE: Obama Budget Proposes Major Worker Classification Reforms

Following closely on the recent IRS announcement of a 3-year worker classification study affecting 6,000 employers, the 2011 Obama Administration Budget includes new legislative proposals to "increase certainty with respect to worker classification." Sending a strong signal that it supports potential groundbreaking changes – which are likely to have ripple effects on employee benefit programs, wage and hour laws and many other areas – the Administration proposals would –

- repeal the section 530 relief that benefits companies that had a "reasonable basis" to treat workers as independent contractors (and meet certain other standards) where IRS later reclassifies them as employees – effective after the year ending one full calendar year after enactment (i.e., effective January 2012 if enactment occurred this year),
- immediately repeal the 1978 revenue act restrictions on new IRS guidance on worker classification – thus opening the door to new IRS guidelines potentially classifying more workers as employees,
- limit reduced retroactive tax rates under current law (Code sec. 3509) to employers who voluntarily reclassify workers – and not where reclassification occurs through an IRS audit,
- require businesses to notify independent contractors of their status and explain the tax, compensation, and wage and hour implications of this classification, and
- allow independent contractors receiving at least \$600 in payments to require the payor/business to withhold federal tax at a flat rate selected by the contractor.

These proposals would increase revenues by more than \$7 billion over 10 years. Several of the proposals resemble ones included in proposed reforms Obama sponsored as a Senator and that are currently included in pending legislation (S. 2882, HR 3408) sponsored by Senator Kerry (D-MA) and Congressman McDermott (D-WA), both members of the Congressional tax-writing committees.

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Please call one of the following, or the Groom attorney you regularly contact, if you have any questions about this or any other matter.

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