Department of the Treasury

Internal Revenue Service

Office of Chief Counsel

N o t i c e

N(35)000-141a

November 12, 1998

Subject: Litigation Strategy for Certain Insurance Agents Claiming Independent Contractor Status - Update

Cancellation Date: May 11, 1999

This Notice updates the December 2, 1996 Notice N(35)000-141. The purpose of this notice is to assist District Counsel attorneys with cases in which individual insurance agents, who were treated as common law employees by their employers, claim independent contractor status.

These taxpayers claim independent contractor status for purposes of deducting business expenses based upon several court decisions including Butts v. Commissioner, T.C. Memo 1993-478, *aff'd per curiam*, 49 F.3d 713 (11th Cir. 1995), Ware v. United States, 850 F. Supp. 602, (W.D. Mich. 1994), *aff'd*, 67 F.3d 574 (6th Cir. 1995), and Feivor v. Commissioner, T.C. Memo 1995-107. In these cases the taxpayer's claim of independent contractor should not be challenged. *See* Lozon v. Commissioner, T.C. Memo 1997-537 (Lozon II).

The taxpayer should, however, be treated as an independent contractor for all purposes under the Internal Revenue Code. As an independent contractor, the taxpayer may not exclude certain benefits from income and will be subject to Self-Employment Contributions Act (SECA) taxes on net earnings from self-employment. To calculate the taxpayer's net earnings from self-employment, the amount of wages, tips and compensation reported by the employer in Box 1 of the Form W-2 should be treated as gross income from a trade or business. In addition, the following benefits that are not excludable from the income of an independent contractor must be included in income: (1) elective contributions made to an I.R.C. § 401(k) plan; (2) elective contributions made to an I.R.C. § 125 plan; and (3) employer contributions (premiums) for dental, health or life insurance policies, or, if the employer's medical plans are self-insured, the benefits under such plans. The taxpayer may not rely on Lozon v. Commissioner, T.C. Memo 1997-250 (Lozon I), to exclude elective contributions made to an I.R.C. § 401(k) plan from gross income. However, the value of other accrued benefits should not be treated as includible in the taxpayer's gross income.

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The taxpayer's Form W-2, Box 13, should include the amount of any elective contributions made to an I.R.C. § 401(k) plan. Other information concerning the additional income items may be obtained from the taxpayer or the company that engaged the taxpayer to perform services.

The taxpayer is liable for all SECA tax due on net earnings from self-employment, even if the Form W-2 shows that the taxpayer paid the maximum FICA tax for the year. As an independent contractor, the taxpayer may claim a refund for the employee portion of the FICA tax paid under I.R.C. § 3101 or receive a credit for that amount under I.R.C. § 6521, if a refund is barred by the statute of limitations. However, the taxpayer cannot claim credit against SECA liability for the portion of the FICA tax paid by the employer under I.R.C. § 3111.

The additional income items and SECA tax liability should be included in the Statutory Notice of Deficiency. However, if they are not, the District Counsel attorney should

(1) Include the income items and assert SECA tax liability in the answer as an affirmative allegation;

(2) Amend answers already filed to reflect the concession of the classification issue, include the additional income items and assert SECA tax liability; or

(3) In an S-case follow the district counsel office procedure for raising affirmative allegations under Tax Court Rule 175(b) and CCDM (35)160.

District Counsel attorneys should also refer to Chief Counsel Notice N(35)000-141b. If you have questions concerning this notice, please contact Marie Cashman at (202) 622-6040.

/s/
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(Employee Benefits and Exempt Organizations)