



# MANUAL TRANSMITTAL

Department of the Treasury  
Internal Revenue Service

4.23.8

APRIL 17, 2024

## EFFECTIVE DATE

(04-17-2024)

## PURPOSE

- (1) This transmits a revised IRM 4.23.8, Employment Tax, Determining Employment Tax Liability

## MATERIAL CHANGES

- (1) This IRM was revised to reflect the following changes:

SUBSECTION	MATERIAL CHANGE
IRM 4.23.8.1	Added paragraph (2) that provides for the scope of this IRM section.
IRM 4.23.8.1.2	Revised the content in paragraph (3) for searching for delegation orders issued by the Commissioner of the Internal Revenue.
IRM 4.23.8.1.3	Clarified paragraph (1) by adding “executive” to the paragraph. .
IRM 4.23.8.1.7	Updated content in paragraph (3) Taxpayer Bill of Rights (TBOR), paragraph (4) Taxpayer Advocate Service (TAS) and paragraph (5) disclosure and privacy provisions. Added paragraph (6) that provided the overall responsibility for civil penalty programs is assigned to Office of Servicewide Penalties (OSP).
IRM 4.23.8.2	Added reference to IRM 4.23.5.3, Section 530 of the Revenue Act of 1978, to paragraph (3). Removed paragraph (4) and (5) since information in IRM 4.23.5.3 and subsequent paragraphs were renumbered. Added reference to paragraph (6) to IRM 4.23.8.9.
IRM 4.23.8.3	Additional resources Note was added to paragraph (1) for additional resources that were in paragraph (4). Removed paragraph (4) with reference information moved to paragraph (1) and all subsequent paragraphs were renumbered.
IRM 4.23.8.3.1	Removed list of Forms 2504 from paragraph (1). Modified paragraph (3) example 2 to incorporate guidance provided in IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022. Removed paragraph (4) since duplicated information in IRM 4.23.8.3 paragraph (7).

SUBSECTION	MATERIAL CHANGE
IRM 4.23.8.3.2	Modified paragraph (1) to facilitate electronic case file and incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022 and IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022.
IRM 4.23.8.4	Revised paragraphs (1) and (2) removing outdated tax rates. Revised paragraph (3) for clarity. Split paragraph (4) into two paragraphs and all subsequent paragraphs are renumbered.
IRM 4.23.8.4.1	Removed first sentence from paragraph (2) for clarity.
IRM 4.23.8.4.2	Revised paragraph (2) to facilitate electronic case file and to incorporate guidance provided in IGM SBSE-04-0722-0048, Emailing documents to Employment Tax -Workload Selection and Delivery, dated July 15, 2022.
IRM 4.23.8.4.3	Revised paragraphs (2), (4) and (6) for clarity. Modified paragraph (7) to incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022. Revised paragraph (8) to incorporate guidance provided in IGM SBSE-04-0722-0048, Emailing documents to Employment Tax -Workload Selection and Delivery, dated July 15, 2022. Removed the note after paragraph (9) to incorporate IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022, that eliminated the requirement of completing Form 5599.
IRM 4.23.8.5.1	Removed references to Form 1099-MISC throughout the subsection. Removed outdated examples in paragraphs (1) and (2).
IRM 4.23.8.5.2	Revised paragraph (4) to incorporate IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022, that eliminated the requirement of completing Form 5599.
IRM 4.23.8.5.2.1	New subsection providing instructions applying IRC 3509 on adjustments to compensation paid to corporate officers.
IRM 4.23.8.5.3	Revised paragraphs (4) and (5) to remove out of date instructions.

<b>SUBSECTION</b>	<b>MATERIAL CHANGE</b>
IRM 4.23.8.6	Revised paragraphs (1) and (4) for clarity.
IRM 4.23.8.6.1	Added paragraph (2) to provide clarity and all subsequent paragraphs are renumbered.
IRM 4.23.8.6.1.1	Revised paragraph (3) to provide instruction for eFaxing the material to Accounts Management.
IRM 4.23.8.7	Modified paragraph (4) for clarity.
IRM 4.23.8.7.4	Modified paragraph (2) to incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022 and IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022.
IRM 4.23.8.7.5	Revised paragraphs (2) and (3) to incorporated IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022, that eliminated the requirement of completing Form 5599.
IRM 4.23.8.8.2	Modified paragraph (1) clarifying instruction.
IRM 4.23.8.9	Added new subsection regarding grossing up of employment taxes during examination. All subsequent subsections are renumbered.
IRM 4.23.8.10.1	Revised paragraph (1) clarifying the content.
IRM 4.23.8.11	Updated subsection for clarity, removed outdated content, and added content on information return electronic filing requirement effective on or after January 1, 2024.
IRM 4.23.8.11.1	Revised paragraph (1) and (5) to clarify the content and instructions. Added to paragraph (6) that employer must provide confirmation that SSA has received the electronic submission due to change of information return electronic filing requirement effective on or after January 1, 2024. Revised paragraph (7) annotation language on Form 3198. Modified paragraphs (6) and (7) to incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022 and IGM TEGE-04-0322-0009, Interim Guidance on Fully Electronic (100% Paperless) Cases, dated March 15, 2022.

SUBSECTION	MATERIAL CHANGE
IRM 4.23.8.11.2	Revised paragraph (1) to clarify the instructions. Revised the rest of the subsection to incorporate guidance provided in IGM SBSE-04-0722-0048, Emailing documents to Employment Tax -Workload Selection and Delivery, dated July 15, 2022. Provided the components of a “tickler file” and changed instructions to email the documents to ET- WSD in lieu of mailing.
IRM 4.23.8.11.3	Modified paragraph (1) to facilitate electronic case file and incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022.
IRM 4.23.8.11.4	Added paragraph (2) on procedures on IRS received date stamping and postmark date stamping to be consisted with IRM 3.10.72.6. All subsequent paragraphs are renumbered. Modified paragraphs (5) and (6) to facilitate electronic case file.
IRM 4.23.8.12	Added note to paragraph (1) to provided additional information and resources. Added note to paragraph (2) to be consisted with IRM 4.7.3. Removed paragraph (3) and all subsequent paragraphs are renumbered. Insert a note into paragraph (4) to remind examiners that the Information Return Penalty Application will generate Letter 5005 and 5005-P and Form 886-A. Revised paragraph (6) to facilitate electronic case file. Modified paragraph (11) to incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022.
IRM 4.23.8.12.1	Subsection has been retitled. Modified the subsection to facilitate electronic case file and incorporate guidance provided in IGM TEGE-04-0222-0006, Elimination of requirement to post Form 3198-A as a separate workpaper in RCCMS Office Documents folder, dated February 23, 2022.
IRM 4.23.8.12.2	Subsection has been retitled. Modified the subsection to facilitate electronic case file.
IRM 4.23.8.13	Updated title of subsection for clarity. Moved paragraph (3) to paragraph (1) and all subsequent paragraphs are renumbered.

<b>SUBSECTION</b>	<b>MATERIAL CHANGE</b>
IRM 4.23.8.14	Split paragraph (2) creating paragraph (2) and (3) and clarified content. All succeeding paragraphs were adjusted accordingly. Added paragraph (9) to provide explanation regarding a nonresident alien.
IRM 4.23.8.14.1	Added a reminder to paragraph (2) a taxpayer is required to backup withhold during the period during which the TIN has not been furnished in the manner required, regardless of whether the payor receives and complies with a CP2100 or CP2100A notice.
IRM 4.23.8.14.2	Modified paragraph (6) since IRM 4.23.8.14.2.1 was added.
IRM 4.23.8.14.2.1	Added subsection on procedures requesting recreated of CP2100 and CP2100A.
IRM 4.23.8.15	Modified paragraph (8) to facilitate electronic case file.
Exhibit 4.23.8-1	Replaced exhibit with a simplified table that provides the same information.
Exhibit 4.23.8-2	Modified the table for 508 compliance.
Exhibit 4.23.8-3	Replaced exhibit with two simplified tables for IRC 3509(a) rates and IRC 3509(b) rates.

- (2) Editorial changes made throughout the IRM for clarity. Reviewed and updated grammar, plain language, titles, IRM references, IRS organization or organization terminology to business unit and reorganized content.

## **EFFECT ON OTHER DOCUMENTS**

IRM 4.23.8, dated March 19, 2021 is superseded. This IRM incorporates Interim Guidance Memorandum SBSE-04-0722-1148, Emailing documents to Employment Tax - Workload Selection and Delivery, dated July 15, 2022.

## **AUDIENCE**

This sections contains instructions and guidelines for all Large Business & International (LB&I), Tax Exempt and Government Entities (TE/GE), and Small Business/Self-Employed (SB/SE) employees dealing with employment tax issues.

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4.23.8

Determining Employment Tax Liability

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4.23.8.1  
(03-19-2021)  
**Program Scope**

- (1) **Purpose:** IRM 4.23.8 discusses the factors to consider when determining an employment tax liability, including interest-free provisions.
- (2) **Scope:** This IRM, Determining Employment Tax Liability, is for all examiners conducting examinations of employment tax returns
- (3) **Audience:** This section contains instructions and guidelines for all Large Business & International (LB&I), Tax Exempt/Government Entities (TE/GE), and Small Business/Self-Employed (SB/SE) employees dealing with employment tax issues.
- (4) **Policy Owner:** Director, Specialty Examination Policy of the Small Business/Self-Employed Division.
- (5) **Program Owner:** Program Manager - Employment Tax Policy.
- (6) **Primary Stakeholders:**
  - Employment Tax – Workload Selection and Delivery (SE:S:D-CE:E:HQ:ECS:S:ETEGCS:EWSD).
  - Specialty Examination - Employment Tax (SE:S:DCE:E:SE:ET).
  - Specialty Examination Policy - Employment Tax Policy (SE:S:D-CE:E:HQ:SEP:EMTP).
  - Other areas that may be affected by these policies and procedures include Appeals, Counsel, SB/SE Examination, LB&I, and TE/GE.
- (7) **Program Scope:** The mission of Employment Tax Policy is to establish effective policies and procedures, and to support compliance with employment tax laws.

4.23.8.1.1  
(05-17-2018)  
**Background**

- (1) A determination of employment tax liabilities requires finding that there is an employer, an employee, and a payment of wages or compensation. Federal employment taxes consist of five separate employment taxes, items (a) through (e). This subsection will also discuss the income tax on self-employment income, item (f).
  - a. Federal Insurance Contributions Act (FICA): IRC 3101 through IRC 3128
  - b. Railroad Retirement Tax Act (RRTA): IRC 3201 through IRC 3233
  - c. Federal Unemployment Tax Act (FUTA): IRC 3301 through IRC 3311
  - d. Railroad Unemployment Repayment Tax (RURT): IRC 3321 and IRC 3322
  - e. Federal Income Tax Withholding (FITW): IRC 3401 through IRC 3406
  - f. Self-Employment Contributions Act (SECA): IRC 1401 through IRC 1403
- (2) The FICA, RRTA, FUTA, RURT, and FITW are imposed by Chapters 21, 22, 23, 23A, and 24, respectively, of Subtitle C - "Employment Taxes." SECA tax is imposed by Chapter 2 of Subtitle A - "Income Taxes" of the IRC, and is not an employment tax.
- (3) Subtitle C also includes Chapter 25 of the IRC entitled "General Provisions Relating to Employment Taxes." This chapter includes eleven additional code sections relating to miscellaneous employment tax provisions.

4.23.8.1.2  
(04-17-2024)

#### Authority

- (1) Employment tax provisions are found at Internal Revenue Code (IRC) Subtitle C:
  - Chapter 21, Federal Insurance Contributions Act (FICA),
  - Chapter 22, Railroad Retirement Tax Act (RRTA),
  - Chapter 23, Federal Unemployment Tax Act (FUTA),
  - Chapter 23A, Railroad Unemployment Repayment Tax,
  - Chapter 24, Collection of Income Tax at Source (FITW), and
  - Chapter 25, General Provisions relating to employment taxes and collection of income taxes at source.
- (2) The Employment Tax Program is governed by Policy Statements and other internal guidance that apply to all IRS personnel regardless of operating division. The Policy Statements found in IRM 1.2.1, *Servicewide Policy Statements*, apply to all employment tax issues and examinations. Examiners should review these Policy Statements to properly perform their examination duties.
- (3) A website, Search Servicewide Delegation Orders, located at <https://irm.web.irs.gov/imd/del/search.aspx> provides a searchable list of Servicewide Delegation Orders issued by the Commissioner of the Internal Revenue, or on their behalf by either of the deputy commissioners. Delegation Orders pertaining to each IRS business process can be found in IRM 1.2.2, *Servicewide Delegations of Authority*.
- (4) IRM 4.23 provides Servicewide instructions for all operating divisions with employees involved with the correct filing, reporting, and payment of employment taxes. IRM 4.23 serves as the foundation for consistent administration of employment taxes by various IRS operating divisions. By providing one source of authority for all operating divisions, the IRS greatly reduces philosophical and procedural inconsistencies.

4.23.8.1.3  
(04-17-2024)

#### Responsibilities

- (1) Director, Specialty Examination Policy is the executive responsible for the procedures and updates addressed in this IRM.
- (2) Director, Specialty Examination is the executive responsible for examination operational compliance.

4.23.8.1.4  
(05-17-2018)

#### Program Objectives and Review

- (1) Program Goals: The processes and procedures provided in this IRM are consistent with the objectives or goals that are addressed in IRM 1.1.16.5.3.3, *Employment Tax Examination*, and IRM 1.1.16.5.5.2.2, *Employment Tax Policy*.
- (2) Program Effectiveness: Program goals are measured with Employment Tax Embedded Quality Performance Reports that monitor whether quality attributes are applied uniformly and consistently.
- (3) Annual Review: Program Manager of Employment Tax Policy is responsible for reviewing the information in this IRM annually to ensure accuracy and promote consistent tax administration.

4.23.8.1.4.1  
(05-17-2018)  
**Program Reports**

- (1) Program Reports: Information regarding the reporting of program objectives are included on, but not limited to, the following reports:
  - Headquarters Examination Monthly Briefing,
  - Program Manager Monthly Briefing,
  - Examination Operational Review, and
  - Business Performance Reviews.
- (2) Quarterly Business Performance Review (BPR) provides updates on the status of the Whistleblower claims in Operating Division status.

4.23.8.1.5  
(05-17-2018)  
**Terms and Definitions**

- (1) The following table lists Terms and Definitions found in this IRM:

Term	Definition
Section 530	Section 530 of the Revenue Act of 1978 provides employers with relief from federal employment tax liabilities resulting from the reclassification of individuals as employees if three requirements are met.
Section 530 - Reporting Consistency	The first requirement a taxpayer must meet to obtain section 530 relief is timely filing of all required federal tax returns consistent with the worker being treated as a non-employee.
Section 530 - Substantive Consistency	The second requirement is that the taxpayer (or a predecessor) must not have treated the worker, or any worker holding a substantially similar position, as an employee for any period after 1977.
Section 530 - Reasonable Basis	The third requirement is that a taxpayer will be treated as having a reasonable basis for not treating a worker as an employee if the treatment was in reasonable reliance on a prior audit, judicial precedence, industry practice, or other reasonable basis.

4.23.8.1.6  
(04-17-2024)  
**Acronyms**

- (1) The following table lists commonly used acronyms and their definitions:

Acronym	Definition
AdMT	Additional Medicare Tax

Acronym	Definition
Appeals	Independent Office of Appeals
AIMS	Audit Information Management System
BCD	Board Coverage Decision
BMF	Business Master File
BOD	Business Operating Division
CCP	Centralized Case Processing
CFO	Chief Financial Officer
CSP	Classification Settlement Program
DOL	Department of Labor
EEE	Employee Benefits, Exempt Organizations, and Employment Tax
EIN	Employer Identification Number
EO	Exempt Organization
ERCS	Examination Returns Control System
ET-WSD	Employment Tax - Workload Selection and Delivery
FICA	Federal Insurance Contributions Act
FITW	Federal Income Tax Withholding
FMS	Financial Management Service
FTD	Failure to Deposit
FTF	Failure to File
FTP	Failure to Pay
FUTA	Federal Unemployment Tax Act
IDRS	Integrated Data Retrieval System
IMF	Individual Master File
IMS	Issue Management System
ITM	Integrated Talent Management
IRC	Internal Revenue Code
LB&I	Large Business & International
RCCMS	Reporting Compliance Case Management System
RRB	Railroad Retirement Board

Acronym	Definition
RRTA	Railroad Retirement Tax Act
RUIA	Railroad Unemployment Insurance Act
RURT	Railroad Unemployment Repayment Tax
SAIN	Standard Audit Index Number
SB/SE	Small Business/Self-Employed
SECA	Self-Employment Contributions Act
SETA	Specialty Employment Tax Application
SFR	Substitute for Return
SSA	Social Security Administration
TAS	Taxpayer Advocate Service
TBOR	Taxpayer Bill of Rights
TEGEDC	Tax Exempt/Government Entities/Division Counsel
TE/GE	Tax Exempt/Government Entities
TIN	Taxpayer Identification Number
WBDOC	Wilkes-Barre Data Operations Center

4.23.8.1.7  
(04-17-2024)

#### Related Resources

- (1) The following table lists the primary sources of guidance:

Source	Title	Description of Guidance
IRM 4.23	Employment Tax IRM	IRM sections, the majority of which are owned by SB/SE - Specialty Examination Policy, provide Servicewide instructions for employees of all operating divisions involved with the correct filing, reporting, and payment of employment taxes. IRM 4.23 serves as the foundation for consistent administration of employment taxes by various IRS operating divisions.

- (2) Other helpful information sources include:

- The SBSE Employment Tax Small Business Knowledge Base (main page) is located at <https://irsgov.sharepoint.com/sites/ETD-KMT-KB014>.
- The Specialist Referral System home page: <https://srs.web.irs.gov/>.
- A list of SB/SE Employment Tax Policy Analysts, their contact information and program assignments, are found at *Employment Tax Policy Contacts*.

- (3) The Taxpayer Bill of Rights (TBOR) lists rights that already existed in the IRC, putting them in simple language and grouping them into 10 fundamental rights. Employees are responsible for being familiar with and acting in accord with taxpayer rights. See IRC 7803(a)(3). For additional information about the TBOR see IRC 7803(a)(3). For additional information about TBOR, see Pub 5170, *Taxpayer Bill of Rights*, [www.irs.gov/taxpayer-bill-of-rights](http://www.irs.gov/taxpayer-bill-of-rights) or <https://irssource.web.irs.gov/SitePages/TaxpayerBillOfRights.aspx>.

- (4) The Taxpayer Advocate Service (TAS) is an independent organization within the IRS, led by the National Taxpayer Advocate, that helps taxpayers and protects taxpayer rights. TAS offers free help to taxpayers when a tax problem is causing a financial difficulty, when they've tried and been unable to resolve their issue with the IRS, or when they believe an IRS system, process, or procedure just isn't working as it should. TAS strives to ensure that every taxpayer is treated fairly and knows and understands their rights under the TBOR. TAS has at least one taxpayer advocate office located in every state, the District of Columbia, and Puerto Rico.

- (5) Employment tax examiners should consider the disclosure provisions when preparing agreed and unagreed case reports. For further information, see the

Privacy, Government Liaison and Disclosure (PGLD) maintained knowledge base at <https://irs.gov.sharepoint.com/sites/ETD-KMT-KB003>.

- (6) Overall responsibility for civil penalty programs is assigned to Office of Service-wide Penalties (OSP). OSP is charged with coordinating policy and procedures concerning the civil penalty program administration, ensuring consistency with the penalty policy statement, reviewing and analyzing penalty information, re-searching penalty effectiveness on compliance trends, and determining appropriate action necessary to promote voluntary compliance. For further understanding of the civil penalty program and penalty relief refer to the *Penalties Knowledge Base Homepage* (<https://irs.gov.sharepoint.com/sites/ETD-KMT-KB015>).

## 4.23.8.2 (04-17-2024) Introduction

- (1) A worker's status or classification (that is employee, independent contractor, or other non-employee) determines what taxes are paid and who is responsible for reporting and paying these taxes. Generally, if an employer-employee relationship exists, the employer is liable for FICA, FUTA, and FITW under IRC 3101, IRC 3102, IRC 3111, IRC 3301, IRC 3402, and IRC 3403, respectively. But there are special rules that may apply. For example, certain workers are subject to FICA taxes even though they are independent contractors under the common law test. These workers are commonly called "statutory employees." See Exhibit 4.23.5-2, *Employment Tax Treatment for Various Categories of Workers*.
- (2) Controversies arising from a worker's classification may be prompted by the firm's concern for the potential increase in tax liability. Although there are relief provisions available under IRC 3102(f)(3), IRC 3402(d), IRC 3509, and IRC 6521, employers may not be aware of them and, with respect to IRC 3102(f)(3), IRC 3402(d) and IRC 6521, employers sometimes find it difficult to locate and get the cooperation of former employees in order to avail themselves of the relief.
- (3) If certain requirements are met, Section 530 of the Revenue Act of 1978 (section 530) provides relief to taxpayers for federal employment tax purposes only. The effect of section 530 is to provide employers relief from federal employment tax obligations imposed on the employer under FICA, FUTA, RRTA, and FITW. For more information, see IRM 4.23.5.3, *Section 530 of the Revenue Act of 1978*. For information regarding examination procedures and report writing when the taxpayer qualifies for section 530 relief, see IRM 4.23.10.10.3.1, *No-Change Reports for Section 530 Eligible Taxpayers*.
- (4) IRC 3509 provides a "statutory offset mechanism that will apply in reclassification cases" and provides reduced tax rates in certain circumstances for determining an employer's liability for an employee's share of FICA tax and FITW on wages paid to the employee. The employer is still liable for the full employer's share of FICA and FUTA taxes. The employee's liability for FICA tax under IRC 3101 is not affected by IRC 3509 and the employer is not entitled to recover from the employee any part of the employee tax assessed under this section. The relief provisions of IRC 3402(d), concerning income taxes paid by the recipient, and IRC 6521, containing the mitigation provisions with respect to employee FICA tax and self-employment tax, do not apply to the tax computed under IRC 3509. For more information see IRM 4.23.8.5, *IRC Section 3509*.

- (5) Both the FITW and Additional Medicare Tax (AdMT) not withheld but paid by the employer after December 31 of the year in which the wages are paid cannot be taken as a credit for withheld income taxes or withheld AdMT on the employee's income tax return. The FITW not withheld but assessed against the employer is subject to the abatement provisions of IRC 3402(d). The AdMT not withheld but assessed against the employer is subject to the abatement provisions of IRC 3102(f)(3). These sections and regulations under these sections afford relief to the employer providing the employer can show that the employee filed a return, reported the wages, and paid the tax. Generally, Form 4669, *Statement of Payments Received*, and Form 4670, *Request for Relief of Payment of Certain Withholding Taxes*, are utilized for this purpose. For more information on relief for an employer when employees have paid income tax or AdMT on wages see IRM 4.23.8.4, *IRC 3402(d) - Relief for Employer When Employees Have Paid Income Tax on Wages*.
- (6) The FICA and FITW not withheld from an employee's wages but paid by the employer on behalf of the employee by December 31 of the year in which the wages are paid constitutes gross income to the employee in the year paid and is wages subject to FICA, FUTA, and FITW. If such taxes are not withheld, the wages need to be grossed up. See Rev. Proc. 81-48, 1981-2 C.B. 623 and IRM 4.23.8.9, *Gross Up of Employment Taxes*.

4.23.8.3  
(05-17-2018)  
**Interest-Free  
Adjustments - In General**

- (1) IRC 6205(a) provides that an employer who makes, or has made, an under-collection or underpayment of employment taxes (FICA, RRTA, or FITW), may make interest-free payments of the tax due when certain conditions are met. This provision does not apply to FUTA or penalties.

**Note:** For more information refer to Treas. Reg. 31.6205-1 and Rev. Rul. 2009-39, 2009-52, I.R.B. 951.

- (2) IRC 6413(a) provides that an employer who paid more than the correct amount of employment taxes (FICA, RRTA, or FITW) may make interest-free adjustments of the amount overpaid when certain conditions are met. This provision does not apply to FUTA.
- (3) IRC 6402 permits the IRS, within the applicable period of limitations, to credit or refund any overpayments. However, regulations under IRC 6402 permit the IRS, within the applicable period of limitations, to credit or refund overpayments of AdMT to the employer only to the extent such overpayments were not deducted and withheld by the employer. Similarly, IRC 6414 permits the IRS, within the applicable period of limitations, to refund an overpayment of FITW to the employer only to the extent such overpayment was not deducted and withheld by the employer.
- (4) The "X" forms are used to report adjustments to employment taxes and to claim refunds of overpaid employment taxes. The "X" forms correspond and relate line-by-line to the employment tax return they are correcting. The "X" forms affect taxpayers that file:
  - Form 941, *Employer's QUARTERLY Federal Tax Return*,
  - Form 943, *Employer's Annual Tax Return for Agricultural Employees*,
  - Form 944, *Employer's ANNUAL Federal Tax Return*,
  - Form 945, *Annual Return of Withheld Federal Income Tax*, and
  - Form CT-1, *Employer's Annual Railroad Retirement Tax Return*.

**Note:** Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, does not have an "X" form.

- (5) The regulations under IRC 6205 provide that if a return is filed and less than the correct amount of employee or employer portions of FICA or RRTA tax is reported and the employer discovers such error after filing the return, the employer will adjust the resulting underpayment of tax by reporting the additional amount due on an "adjusted return" for the return period in which the error was ascertained. The "X" form is an adjusted return. An error is ascertained when the employer has sufficient knowledge of the error to be able to correct it.
- (6) An adjusted return (for example, Form 941-X, *Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund*) correcting an underpayment must be filed by the due date of the return for the return period in which the error is ascertained and **the amount of the underpayment must be paid by the time the adjusted return is filed**, or interest will begin to accrue from that date. For underpayments of AdMT and FITW where the incorrect amount was withheld, the regulations under IRC 6205 provide that an adjustment may be made only for errors ascertained during the calendar year in which the wages were paid unless IRC 3509 applies or the adjustment is being made in the context of an examination.
- (7) Interest-free adjustments may not be made if:
  - a. The amounts under-reported relate to an issue that was raised in a prior period examination,
  - b. The taxpayer knowingly under-reports an employment tax liability,
  - c. The taxpayer receives notice and demand for payment after assessment and prior to filing the adjusted return,
  - d. The taxpayer receives Letter 3523, *Notice of Employment Tax Determination Under IRC Section 7436*, prior to filing the adjusted return (refer to Treas. Reg. 31.6205-1(a)(2) and (a)(6)), or
  - e. The adjusted return is not timely filed. That is by the due date of the return for the return period in which the error was ascertained.
- (8) The regulations permit an interest-free adjustment to be made in situations where a return was not filed because:
  - The employer failed to treat any individuals as employees, or
  - The wrong return was filed (for example, employer was required to file Form CT-1 reporting RRTA tax, but erroneously filed Form 941 reporting FICA instead).

**Note:** The employer will make the interest-free adjustment by filing an original return and an attached adjusted return reporting the correct amount of tax, in accordance with the instructions for the adjusted return.

- (9) For Form 945, interest-free adjustments procedures may only apply if a return has been previously filed and an error is subsequently discovered. Interest-free does not apply to non-filed Forms 945.
- (10) An employer making an interest-free adjustment of an underpayment must pay the amount of the underpayment by the time it files the adjusted return, for example, Form 941-X. Such timely payment will satisfy the employer's deposit obligations with respect to the adjustment. Conversely, if the amount of the ad-

justment is not paid by the time the adjusted return is filed, a penalty under IRC 6656 for failure to deposit may apply because the deposit obligation for such taxes is not deemed to be satisfied and the employer may not have otherwise satisfied the deposit obligations. Interest will also begin to accrue from the time the adjusted return is filed.

- (11) Under Treas. Reg. 31.6205-1(a)(6), an interest-free adjustment generally may not be made after receipt of notice and demand for payment or receipt of a Letter 3523. In order to provide a mechanism for taxpayers to make an interest-free adjustment yet receive Letter 3523 enabling them to petition the U.S. Tax Court, Treas. Reg. 31.6205-1(a)(6)(ii) permits employers, prior to receipt Letter 3523, to make an IRC 6205 deposit in lieu of making a payment to stop the accrual of any interest. The IRS treats an IRC 6205 deposit made prior to receipt of Letter 3523 as an interest-free adjustment. Without this rule, an employer would not be able to both make an interest-free adjustment and receive Letter 3523 enabling it to seek U.S. Tax Court review under IRC 7436. Moreover, this IRC 6205 deposit is the only way an employer can make an interest-free adjustment other than filing an adjusted return.
- (12) The regulations under IRC 6413 provide that interest-free adjustments to over-payments may be made at any time after the error is ascertained within the applicable period of limitations for credit or refund. An error is ascertained when the employer has sufficient information to be able to correct it.
- (13) An employer is required to repay or reimburse the employee in the amount of the over-collection prior to filing the adjusted return. For adjustments of FICA tax over-collected in prior years, the employer must also secure the employee's written statement confirming that the employee has not made any previous claims (or the claims were rejected) and will not make any future claims for refund or credit of the amount of the over-collected FICA tax.

**Note:** The rules for adjusting over-collections in prior years do not apply to AdMT because over-collection of AdMT generally cannot be adjusted for prior years.

- (14) The employer is required to certify on its adjusted return that it has repaid or reimbursed the employee in the amount of the over-collection. For adjustments of FICA tax over-collected in prior years, the employer must also certify that it has secured the required written statement from the employee. However, these requirements do not apply to the extent that the taxes were not withheld from the employee. If, after having made reasonable efforts, the employer cannot locate the employee or, for prior year FICA tax, the employee will not furnish the required written statement, the employer may make an adjustment of the overpaid **employer share** of FICA tax. Generally, interest-free adjustments to AdMT and FITW may be made only for overpayment errors discovered and repaid during the calendar year in which the wages were paid.
- (15) The regulations under IRC 6402 and IRC 6414 provide that an employer may file a claim for refund at any time after the error is ascertained within the applicable period of limitations. Per the regulations under IRC 6402, refunds of AdMT shall be made to the employer only to the extent that the amount of such overpayment was not deducted and withheld by the employer. Similarly, per IRC 6414, refunds of FITW will be made to the employer only to the extent that the amount of such overpayment was not deducted and withheld by the employer. As part of the claim for refund process, the employer must repay or

reimburse the employee in the amount of the over-collection or secure the employee's consent to the filing of the claim for refund. The employer must certify that it has repaid or reimbursed its employee or has secured the employee's consent. For refund claims for FICA tax over-collected in prior years, the employer must also certify that it has obtained the employee's written statement confirming that the employee has not made any previous claims (or the claims were rejected) and will not make any future claims for refund or credit of the amount of the over-collection.

**Note:** The rules for claiming refunds of over-collections in prior years do not apply to AdMT because refunds of AdMT are available only to the extent it was not deducted and withheld from the employee.

**Note:** However, these requirements do not apply to the extent that the taxes were not withheld from the employee. If, after having made reasonable efforts, the employer cannot locate the employee, or the employee will not provide consent, or the employee will not provide the required written statement, the employer may claim a refund of the overpaid **employer share** of FICA tax.

**Note:** See Rev. Proc. 2017-28, I.R.B. 2017-14 for the requirements for employee consent used by an employer to support a claim for credit or refund of overpaid taxes under FICA and the Railroad Retirement Tax Act (RTTA) pursuant to IRC 6402.

## 4.23.8.3.1 (04-17-2024) Interest-Free Audit Adjustment

- (1) An error is ascertained when the employer has sufficient knowledge of the error to be able to correct it. Such knowledge may be obtained in the course of an examination. In an agreed case, this is when the employer submits one of the Form 2504 series agreements. For an unagreed case, it could be at the conclusion of an Appeals conference or when the taxpayer declines to exercise its right to go to Appeals.

**Reminder:** For additional information of what constitutes an adjusted return refer to Rev. Rul. 2009-39, 2009-52, I.R.B. 951.

- (2) If one of the exceptions listed in IRM 4.23.8.3(7) is not applicable, the submission of one of the Form 2504 series agreements at the close of an examination or Appeals conference (and prior to the issuance of a notice and demand for payment) fulfills the requirements for correcting a return for purposes of the interest-free adjustment provisions of IRC 6205 and the regulations. For errors discovered on or after January 1, 2009, full payment of the tax must be made at the time of the submission of the agreement in order to receive complete interest-free treatment and avoid failure to deposit (FTD) penalties. If the tax adjustment is not paid when the signed agreement is submitted, interest and penalties accrue. It is important that the examiner clearly explain the various penalty and interest-free rules when soliciting an agreement in an agreed case or closing an unagreed case. The interpretation of this paragraph is illustrated by the following examples:

**Example:** (1) An employer files and pays the tax for a timely filed employment tax return that is incorrect. During an audit, an error in the FICA tax liability is discovered by the examiner and an adjustment is proposed to the employer on September 15th. The employer submits a signed Form

2504 and pays the additional tax on November 10th. As the amount was paid at the time the agreement was secured, the taxpayer is entitled to a complete interest-free adjustment.

**Example:** (2) Same situation as Example 1 above, except that the taxpayer submits the signed agreement on November 10th but does not pay the tax at that time. The interest computation date entered on line 11 of Form 5344 or the Individual/Bus (1 of 3) tab of the closing record in Reporting Compliance Case Management System (RCCMS) for TE/GE is November 10th, and interest begins to accrue starting November 11th.

- (3) Under the regulations, an adjusted return must be filed to get an interest-free adjustment. If the taxpayer elects to pay the full adjustment amount (taxes and penalties) at any time prior to the closing of the examination but does not agree by submitting a signed Form 2504, the case will be processed as an unagreed case without an interest-free adjustment. If, after the case is closed unagreed, the taxpayer submits a signed Form 2504 or files Form 941-X prior to the due date of the return for the period in which the payment was made, the taxpayer will be entitled to an interest-free adjustment.

**Note:** If the taxpayer submits a signed Form 2504 but does not pay the tax at that time resulting in the issuance of a notice and demand for payment, the taxpayer would still be entitled to an interest-free adjustment. However, interest will be due from the date the Form 2504 was submitted until full payment is made.

#### 4.23.8.3.2 (04-17-2024)

#### Processing Interest-Free Employment Tax Cases

- (1) In all employment tax cases which involve a restriction on the payment of interest, Form 3198, *Special Handling Notice for Examination Case Processing* is used to notify the Support and Processing function not to assess interest. TE/GE employees will prepare RCCMS Form 3198-A, *TE/GE Special Handling Checklist*. Note the type of tax, the tax periods, and the section of the IRC or Regulations which authorizes the restriction of interest. Check the appropriate block on Form 3198 or RCCMS Form 3198-A and enter the interest computation date, that is, the date the Form 2504 was date-stamped **received**. Also, enter this date in Item 11 of Form 5344 or the Individual/Bus (1 of 3) tab of the closing record in RCCMS for TE/GE. Enter transaction code "308" in Item 12 of Form 5344 or the Individual/Bus (1 of 3) tab of the closing record in RCCMS for TE/GE to identify the tax as interest-free. There are **no** interest-free adjustments for underpaid FUTA taxes. The IRC provisions restricting and prohibiting assessment or payment of interest are listed in Exhibit 4.23.8-2, *Code Provisions Restricting and Prohibiting Interest — Employment Taxes*. Additional instructions on the preparation of Form 5344 for employment tax closures are provided in IRM 4.23.10.20, *Form 5344/Form 5599 - Additional Entries for Completion of Employment Tax Closures*, and in IRM 4.4.12, *AIMS Procedures and Processing Instructions, Examined Closings, Surveyed Claims, and Partial Assessments*.
- (2) If the taxpayer agrees with the examination findings for the years under examination and the current year returns reflect similar errors as adjusted in the examination, advise the taxpayer they must correct the current year errors using Forms 941-X (or other corresponding "X" form), for all periods to be adjusted before the end of the current filing period to receive an interest-free adjustment for any underpayments.

- (3) If the case is unagreed and a Notice and Demand for payment is issued, interest generally begins to accrue starting on the due date of the return. See IRC 6601.

4.23.8.4  
(04-17-2024)  
**IRC 3402(d) - Relief for Employer When Employees Have Paid Income Tax on Wages**

- (1) When FITW is involved and IRC 3509 is not applicable, the withholding is either computed under ordinary FITW requirements under Treas. Reg. 31.3402(a)-1 or using the supplemental withholding rate in Treas. Reg. 31.3402(g)-1. The supplemental rate is 22 percent effective January 1, 2018.
- (2) Supplemental wage payments in **excess of \$1,000,000** for any one employee are subject to withholding that is computed at the maximum federal income tax withholding rate in effect for the given year, without regard to the employee's Form W-4. The supplemental rate for wage payments in excess of \$1,000,000 is 37 percent effective January 1, 2018.

**Note:** Total supplemental wages paid to the employee for the year include: (a) supplemental wages previously included in the employee's wages, plus; (b) the employee's share of the employment tax adjustment. Examiners must consider payments to the employee from all businesses under common control, and the employee's share of the employment tax adjustments for all issues. See Rev. Rul. 2008-24 2008-1 C.B. 861 and Treas. Reg. 31.3402(g)-1(a)(2).

- (3) IRC 3402(d) provides that if the employer failed to deduct and withhold FITW but the employee reported the income and paid the tax, the FITW shall not be collected from the employer. Examiners may adjust amounts subject to FITW prior to closing the employment tax case.
- (4) FICA and FUTA taxes are not abatable under IRC 3402(d).
- (5) Any applicable penalties or interest are not abated when FITW is abated under IRC 3402(d). A partial assessment process is used to ensure the correct assessments are made. See IRM 4.23.8.4.3, *Procedures for Relief Under IRC 3402(d) and/or IRC 3102(f)(3) in Examination*, below.
- (6) IRC 3402(d) is **not** available for employers who deducted and withheld income taxes but failed to report the withheld income taxes to the IRS.
- (7) The actual amount of tax credit available for abatement is included on line 11 of Form 4668. See IRM 4.23.10.15.3, *Examination Report Forms for IRC 3402(d) and IRC 3102(f)(3) Abatements*.

4.23.8.4.1  
(04-17-2024)  
**IRC 3102(f)(3) - Relief for Employer When Employees Have Paid Additional Medicare Tax on Wages**

- (1) If an employer deducts less than the correct amount of AdMT, it is nevertheless liable for the correct amount of tax that it was required to withhold, unless and until the employee pays the tax. Under IRC 3102(f)(3), if an employee subsequently pays the tax that the employer failed to deduct, the tax will not be collected from the employer.
- (2) An employer is not relieved of its liability for payment of any AdMT required to be withheld unless it can show that the tax has been paid by the employee or that the employee did not owe the tax because the employee filed a joint tax return and did not have total Medicare wages and tips and self-employment income of more than \$250,000 or total railroad retirement (RRTA) compensation of more than \$250,000. Form 4670 is used to request relief from the

employee AdMT withholding obligation with the Form 4669 attachments. These are the same forms used for requesting federal income tax withholding relief.

- (3) Penalties or interest adjustments are not abated by these procedures. A partial assessment process is used to ensure the correct assessments are made. See IRM 4.23.8.4.3, *Procedures for Relief Under IRC 3402(d) and/or IRC 3102(f)(3) in Examination*, below.
- (4) The actual amount of tax credit available for abatement is included on line 12 of Form 4668.

4.23.8.4.2  
(04-17-2024)  
**Forms 4669/4670**

- (1) Form 4669 is used by the taxpayer to secure statements from payees that the income tax and/or AdMT on the payments in question has been satisfied. Form 4670 is used to summarize and transmit the Forms 4669 to the Campus.
  - In examinations where the taxpayer **has not paid** the tax and will request an **abatement** after completion of the examination, (see IRM 4.23.8.4, *IRC 3402(d) - Relief for Employer When Employees Have Paid Income Tax on Wages*) an extra copy of Form 4668 or Form 4668-B, *Report of Examination of Withheld Federal Income Tax for Withholding Reported on Forms 1099 and W-2G*, should be provided to the taxpayer. Instruct the taxpayer to mail the copy of the report form along with Forms 4669/4670 to the appropriate Campus. It is not necessary to submit an "X" form, for example, Form 941-X or Form 945-X, (however, the taxpayer may find use of the form helpful for calculation).
  - If the taxpayer **has paid** the additional employment tax examination assessment after the examination and later wants a refund (for instance, additional payees have been contacted and new Forms 4669 have been secured), the **claim** would be filed using the appropriate "X" form (for example, Form 941-X or Form 945-X,) with the attached examination report copy of Forms 4668/ 4668-B.
- (2) Examiners are authorized to accept and consider any Forms 4669 submitted to the examiner before the examination is closed. A separate Form 4669 must be obtained by the taxpayer from each payee for each year. These forms must be completed correctly by the payee and are attached to the Form 4670 prepared by the taxpayer. These completed forms must have every appropriate line item completed by the payee and accompanied by Form 4670 prepared by the payor. If any information is omitted, Form 4669 is returned to the payor for correction. The Form 4669 is signed by the payee under penalties of perjury.

4.23.8.4.3  
(04-17-2024)  
**Procedures for Relief Under IRC 3402(d) and/or IRC 3102(f)(3) in Examination**

- (1) A Form 4669 may be rejected by the examiner on the basis of incomplete or inaccurate information on the face of the document. Any questionable Form 4669 (for example, possible unreported income, false information, forged signatures) should be referred to Planning and Special Programs (PSP) for appropriate follow-up action. TE/GE employees follow the referral process in IRM 4.70.11.15.3, *General Referral Process within the IRS*.

**Note:** For additional instructions on requests for relief under IRC 3402(d) and/or IRC 3102(f)(3), see IRM 21.7.2.5.8.1, *Processing Procedures for Forms 4669 and 4670*.

- (2) Form 4669 may be subsequently reviewed by Campus after completion of the examination to determine if the income was properly reported by the payee. Where a payee is found either to have not filed income tax returns or not included the income in question, appropriate action will be considered. Payees found to have perjured themselves by providing false information, or Forms 4669 found to have forged signatures of the payee, may also be referred to the appropriate function for enforcement action.
- (3) The examiner should provide the taxpayer with Forms 4669 and a Form 4670 when the issue is identified in the examination and inform the taxpayer as early as possible in the examination to begin soliciting these forms from the payees. The examiner should allow a reasonable amount of time for the forms to be returned. Subsequent submissions of Form 4669 by the taxpayer after the case is closed from the group will be processed under existing guidelines by the Campus. See IRM 4.23.8.4.2, *Forms 4669/ 4670*.
- (4) The abatement will be based on the lesser of the tax applicable to:
  - The amount shown on the Form 4669 that each payee included on the payee's income tax return, or
  - The amount paid to each payee by the taxpayer.
- (5) At the close of the examination, the examiner should advise the taxpayer that although the FITW and/or AdMT may be abated under IRC 3402(d) and IRC 3102(f)(3), the taxpayer remains liable for any penalties or interest attributable to the original assessment.
  - If penalties are assessed, or interest-free provisions are not granted, the Modified Partial Assessment "Two-Step" report-writing procedures at IRM 4.23.10.15.2, *Examination Procedures for IRC 3402(d) and IRC 3102(f)(3) Relief*, must be followed. TE/GE employees will follow the process outlined in IRM 4.70.14.2.1.4.6.2, *TE/GE- IRC 3402(d) When Penalties are Proposed*.
  - If the examination does not propose penalties and the interest-free provisions of IRC 6205 are to be allowed, the "Two-Step" process is not to be used. The examiner will compute the tax due on Form 4668 or Form 4668-B based on the net payment adjustment using the accepted amounts from the secured Forms 4669.
- (6) In order to avoid duplicate processing of Forms 4669, clearly indicate on each accepted form in bold print "DO NOT PROCESS — ADJUSTMENT CONSIDERED BY EXAMINER ON \_\_\_\_\_(mm/dd/yy)".
- (7) Prepare a list of all payees and amounts where adjustment may be applicable and prominently identify those payees where adjustment was granted. This action precludes duplicate abatements if additional Forms 4669 are submitted to Appeals or to the Campus at a later date. This list should identify the payee, the amount paid to each payee, the amount of payment eligible for IRC 3402(d) and IRC 3102(f)(3) consideration, and the Forms 4669 accepted in the examination. In addition, if computed using a quarterly report, the IRC 3402(d) and IRC 3102(f)(3) credits allowed should be identified by quarter on the list, and the total should match the IRC 3402(d) and IRC 3102(f)(3) credit amount listed on the Form 2504/Form 2504-S/Form 2504-T. The list must remain in the case file as a summary sheet of the Forms 4669. Mark in bold print "**FORM 4669 – ADJUSTMENTS ALLOWED BY EXAMINATION**" on Form 3198 (TE/GE employees will notate RCCMS Form 3198-A).

- (8) All completed Forms 4669 secured by SB/SE Employment Tax Examiners will be scanned, if not already in an electronic format, and emailed to Employment Tax – Workload Selection and Delivery (ET-WSD). Scanned documents should be reviewed to confirm they are complete and legible prior to emailing to ET-WSD. Copies of the forms must also be uploaded as a workpaper in Issue Management System (IMS) to the relevant issue Standard Audit Index Number (SAIN). Secure email the completed Forms 4669 and Form 4670 to **\*SBSE ET WSD Case Closing Packages** (sbse.et.wsd.case.closing.packages@irs.gov) with the subject “Forms 4669 – Tax Period(s) 20XX12.” TE/GE employees keep secured Forms 4669 and Form 4670 with the case file. For further instructions TE/GE employees refer to IRM 4.70.13.9.5.6.1, *Delinquent Forms 1099 Identified in Examination*.
- (9) For instructions on report writing, processing, and Form 5344 completion for IRC 3402(d) examination abatements, see:
- IRM 4.23.10.15.2, *Examination Procedures for IRC 3402(d) and IRC 3102(f)(3) Relief*,
  - IRM 4.23.10.15.3, *Examination Report Forms for IRC 3402(d) and IRC 3102(f)(3) Abatements*, and
  - IRM 4.23.10.17, *General Procedures for Adjusting the Employee Share of FICA/RRTA Taxes Including Additional Medicare Tax (AdMT) for Form 1040*.

4.23.8.5  
(05-17-2018)  
**IRC Section 3509**

- (1) When an employer erroneously treats an employee as a non-employee and does not withhold federal employment taxes, the employer is liable under IRC 3102 and IRC 3403 for the employee’s share of FICA and FITW.
- (2) IRC 3509 provides reduced rates for FITW and the employee’s share of FICA if an employer failed to withhold employment taxes by reason of treating such employee(s) as a non-employee(s). A “non-employee” includes, but is not limited to, an independent contractor. The provision does not relieve the employer of any portion of the employer’s share of FICA and FUTA taxes.
- (3) IRC 3509 applies only to worker classification adjustments, it **does not** apply to wage adjustments including IRC 7436 wage adjustments. When a wage issue falls under IRC 7436, it does not become a worker classification issue; it remains a wage issue and IRC 3509 rates are not applicable. See IRM 4.23.5.2.1, *Classification of Employment Tax Issues*, for guidance on when employment tax issues are considered wage or worker classification issues. Also, see IRM 4.23.5.2, *IRC 7436*, for guidance on when issues are considered IRC 7436 issues.
- (4) If IRC 3509 applies, the offset provisions of IRC 3402(d) and IRC 6521 **do not** apply. Application of IRC 3509 is mandatory if the criteria are satisfied. The examiner and the taxpayer do not have a choice regarding its application. See IRC 3509(c) and (d) for exclusion criteria.

4.23.8.5.1  
(04-17-2024)  
**Reduced Tax Rates  
Under IRC 3509**

- (1) If Forms 1099-NEC, *Nonemployee Compensation* were timely filed with respect to workers who were reclassified as employees, IRC 3509(a) generally applies:
- a. FITW is computed at the rate of 1.5 percent with no abatement available under IRC 3402(d).

- b. The employer's liability for FICA is computed at the rate of 20 percent of the employee's share, plus the entire employer's share.
- c. Relief under IRC 6521 does not apply.

IRC 3509(a) Example:	Percentage
Employer share of FICA	7.65%
20% of Employee share of FICA (.20 * 7.65%)	1.53%
Total FICA	9.18%
FITW = 1.50% of wages	1.50%
<b>Total IRC 3509(a) Percentage</b>	<b>10.68%</b>

**Reminder:** If the wages paid exceed the social security wage base, this rate will need to be separated between the rate for social security tax and Medicare tax.

**Note:** An employer is responsible for withholding 0.9 percent AdMT from wages or compensation it pays to an employee in excess of \$200,000 in a calendar year. There is no employer share of AdMT. Under IRC 3509(a), 20 percent of the AdMT rate of 0.9 percent equals 0.18 percent of wages subject to AdMT (that is, wages that exceed \$200,000).

- (2) If required Forms 1099-NEC were not filed as required, IRC 3509(b) applies:
  - a. The FITW rate becomes 3 percent with no abatement available under IRC 3402(d).
  - b. The FICA liability is the employer's share plus 40 percent of the employee's share. Relief under IRC 6521 does not apply.

**Note:** If the employer's failure to file Forms 1099-NEC was due to reasonable cause and not willful neglect, the higher rates of IRC 3509(b) do not apply and the lower rates of 3509(a) are applied. See IRC 3509(b)(1). This application may include the failure to file Forms 1099-NEC for a corporate officer or in the case of employees being treated as partners.

IRC 3509(b) Example:	Percentage
Employer share of FICA	7.65%
40% of employee share of FICA (.40 * 7.65%)	3.06%
Total social FICA	10.71%
FITW = 3.0% of wages	3.00%
<b>Total IRC 3509(b) Percentage</b>	<b>13.71%</b>

**Reminder:** If the wages paid exceed the social security wage base, this rate will need to be separated between the rate for social security tax and Medicare tax.

**Note:** An employer is responsible for withholding 0.9 percent AdMT from wages or compensation it pays to an employee in excess of \$200,000 in a calendar year. There is no employer share of AdMT. Under IRC 3509(b), 40 percent of the AdMT rate of 0.9 percent equals 0.36 percent of wages subject to AdMT (that is, wages that exceed \$200,000).

(3) Penalties:

- a. For substitute for return (SFR) cases, the failure to file penalty (FTF) under IRC 6651(a)(1) and the failure to pay penalty (FTP) under IRC 6651(a)(2) are applicable if there is no reasonable cause for the employer's failure to treat the workers as employees and to file any employment tax returns. See IRM 20.1.2, *Failure to File/Failure to Pay Penalties*, of the Penalty Handbook for further instructions. See also IRM 4.8.10.5.3.3, *Amount of Underpayment and Penalties for Reclassified Workers - Table 3 and Table 4*.
- b. The FTD penalty under IRC 6656 will apply to delinquent employment taxes unless there is reasonable cause. See IRM 20.1.4, *Failure to Deposit Penalty*, for further instructions. However, the deposit penalty does **not** apply to FICA and income taxes which should have been, but were not, withheld from compensation paid to employees.

**Note:** Treas. Reg. 31.6302(c)–1 states the taxes required to be deposited are those which were withheld, together with any employer tax imposed by FICA. Typically, in a reclassification situation, no taxes were actually withheld from the workers, so the deposit penalty is computed only on the employer's share of FICA. See Rev. Rul. 75–191, 1975–1 C.B. 376.

- c. If a taxpayer has not filed a return, the accuracy-related penalty does not apply as a substitute for return is not considered a return for this purpose.
- d. If reasonable cause relief is available, a determination as to whether reasonable cause exists must be based on a careful consideration of the facts and circumstances of each case prior to the assertion of a penalty. Employment tax examiners should consider any reason a taxpayer provides in conjunction with the guidelines, principles, and evaluating factors. See IRM 20.1.1.3, *Criteria for Relief From Penalties*, as well as the applicable IRC section and Treasury Regulations relating to the specific penalty.

**Note:** Refer to IRM 20.1.1.3.3.2.1, *First Time Abate (FTA)*, for all eligibility criteria for penalty relief under the FTA administrative waiver. If eligibility criteria are met FTA provides administrative relief from FTF (IRC 6651(a)(1), IRC 6698(a)(1), and IRC 6699(a)(1)); FTP (IRC 6651(a)(2) and IRC 6651(a)(3)); and/or FTD (IRC 6656).

4.23.8.5.2  
(04-17-2024)

**Application of IRC 3509**

- (1) Consideration of the provisions of IRC 3509 is **mandatory** for **all** determinations involving worker reclassification assessments. This includes cases involving the reclassification of corporate officers.
- (2) A taxpayer cannot waive IRC 3509 when its conditions are met. However, the lower rates of IRC 3509(a) and IRC 3509(b) do not apply:

- a. In cases of the employer's intentional disregard of the requirement to deduct and withhold employment taxes (IRC 3509(c)),
  - b. In cases where the employer deducts income tax from the wages of an employee but does not deduct FICA tax (IRC 3509(d)(2)), or
  - c. In cases of certain statutory employees for FICA tax purposes (IRC 3509(d)(3)).
- (3) In agreed and unagreed cases, the provisions of IRC 3509 will be applied to all quarterly returns required to be filed for any completed calendar year under examination. If different rates under IRC section 3509 are applied to the same employer, the case file/workpapers should be documented to explain the reasoning for using the different rates. If the employer's failure to file Forms 1099-NEC was due to reasonable cause and not willful neglect, apply the rates of IRC 3509(a) rather than the higher rates of 3509(b).
- (4) If **all** assessments in an examination are made using IRC 3509 rates, in addition to the required entries for Item 15 of Form 5344 (or the Individual/Bus (1 of 3) tab of the closing record in RCCMS for TE/GE), also enter reference code "079" with an adjustment amount of "0". Inputting reference code "079" with an amount of zero causes the literal "3509" to print on the transcript account. This notifies Collection that the Trust Fund Recovery Penalty is not applicable, as the assessment was made using IRC 3509 rates and there are no employee withholding taxes subject to penalty. See IRM 4.4.12, *AIMS Procedures and Processing Handbook - Examined Closings, Surveyed Claims, and Partial Assessments*, and various updated job aids for instructions on the completion of Form 5344.

#### 4.23.8.5.2.1 (04-17-2024)

#### **Application of IRC 3509 - Corporate Officer**

- (1) In the examination of corporate officers, including an officer of an S corporation, the applicable employment taxes will depend on the nature of the payments and whether any payments were already reported on Form W-2.
- (2) If the taxpayer treated the officer as an independent contractor (Form 1099-NEC was filed with the IRS and furnished to the worker), then the taxpayer would be entitled to the reduced rates under IRC 3509(a) because this is a worker classification adjustment.
- (3) Reduced rates under IRC 3509 could also be applicable where the officer received compensation only through distributions (or loans or personal expenses) with no Form W-2. The basis for using the reduced rates in these cases is that the taxpayer treated the officer as a "non-employee." The conversion of the officer from a non-employee to an employee is a worker reclassification adjustment. The reduced rates under IRC 3509 would be applicable.

**Reminder:** For distributions reported on Schedule K-1 (Form 1120S), Shareholder's Share of Income, Deductions, Credits, etc., IRC 3509(a) rates are applicable because the Schedule K-1 is considered the information return required to be filed consistent with the taxpayer's position that the officer was a "non-employee." For loans and personal expenses, IRC 3509(b) rates are applicable since those payments would not have been reported on any information return.

- (4) If the taxpayer filed and furnished Form W-2 for some wages, and distributions, loans, or personal expenses are being recharacterized to additional wages, reduced rates under IRC 3509 are not applicable. Generally, this is a

reasonable compensation issue and not a worker classification issue. Full rates should be used for FICA and FITW. FUTA may also be applicable to the adjustment under IRC 3306 if the wages reported on Form W-2 were less than \$7,000.

- (5) If the examiner determined there was intentional disregard for not treating the officer as an employee, the reduced rates would not be applicable per IRC 3509(c). FUTA would also be applicable to these adjustments per IRC 3306.

**Reminder:** Significant evidence of intentional disregard should be clearly present before IRC 3509 rates are denied. However, the court has found intentional disregard exists in a worker classification issue involving officers, “in light of the established law in this area.” Refer to *Fred R. Esser, P.C. v. United States*, 750 F. Supp 421 (D. Ariz. 1990).

#### 4.23.8.5.3 (04-17-2024) Effect of IRC 3509 on Employee Liability

- (1) The employee’s liability for FICA tax under IRC 3101 is not affected by IRC 3509. The employer is not entitled to recover from the employee any part of the tax assessed under IRC 3509. Treas. Reg. 31.3102–1(d) provides that an employee is responsible for the employee’s share of FICA until it is collected from them by the employer. Since IRC 3509 bars the employer from collecting the tax from the employee, the employee remains liable for the FICA tax on their individual Form 1040 return. See Rev. Rul. 86-111, 1986-2 C.B. 176.
- (2) The employee may file a claim for refund of any self-employment tax which is attributable to the reclassification. Notice 989, *Commonly Asked Questions When IRS Determines Your Work Status is “Employee”*, provides instructions to the reclassified worker on how to file a claim for refund.
- (3) The amount of SECA tax refund is offset by the amount of the employee’s share of the tax imposed on the employee under IRC 3101 as a result of the application of Treas. Reg. 31.3102–1(d). The reclassified worker can use Form 8919, *Uncollected Social Security and Medicare Tax on Wages*, to compute the amount of FICA taxes due. It should be used as an attachment to Form 1040 or 1040X. Ultimate liability is on the employee until collected from either the employee or the employer. See Rev. Rul. 86–111.

**Example:** If a worker paid self-employment tax on a net profit of \$35,100 (\$45,000 less \$9,900 related business expenses) and during a subsequent examination of the payor, the IRS reclassified those earnings from self-employment income to gross wages of \$45,000, the worker would be entitled to a SECA tax refund calculated as follows for the year 2022 in table below:

Description	Computation	Result
Net earnings from self-employment	\$35,100 x 92.35%	\$32,4515.00
SECA tax	\$32,415 x 15.3%	\$4,959.50
Employee share of FICA Tax	\$45,000 x 7.65%	\$3,442.50
Allowable SECA tax refund	\$4,959.50 - \$3,442.50	\$1,517.00

- (4) Expenses that the reclassified worker claimed on Schedule C, *Profit or Loss From Business (Sole Proprietorship)*, are eliminated by the worker's reclassification, but may be deductible for certain employees on Form 2106, *Employee Business Expenses*. Due to the suspension of miscellaneous itemized deductions subject to the 2 percent floor under IRC 67(a), only Armed Forces reservists, qualified performing artists, fee-basis state or local government officials, and/or employees with impairment-related work expenses, may file Form 2106. The employee's adjustments to income for self-employed health insurance, self-employed SEP, SIMPLE, and qualified plans, and one-half of the self-employment tax, are also eliminated.
- (5) The disallowance of business expenses for a reclassified worker will potentially increase taxable income and federal income tax.
- (6) Any additional federal income tax will offset the SECA tax refund.
- (7) If the period of limitations for the SECA tax or FICA tax is expired, IRC 6521 mitigates this by allowing the refund/payment.

**Note:** The employer may be entitled to the abatement of the employee share of FICA tax under IRC 6521 if the employee paid self-employment tax and the statute has expired for claiming a refund of such tax.

**Reminder:** The employer is not entitled to an abatement of the employee share of FICA if IRC 3509 rates were used to calculate the adjustment.

#### 4.23.8.6 (04-17-2024) FICA Tax

- (1) For purposes of FICA, all wages (cash or non-cash) derived from employment, unless specifically excluded by statute, are subject to tax. It is immaterial what the wages are called as long as the payment is for services performed as an employee. FICA tax includes both social security and Medicare tax (including Additional Medicare tax). Wages subject to social security taxes do not include amounts paid to an employee that are in excess of the taxable wage base. As of 1994, there is a wage base for the social security portion but not for the Medicare portion. For the social security wage limits for each year see Exhibit 4.23.8-3, *Employment Tax Rate Chart under IRC 3509*.
- (2) In addition to withholding Medicare tax at 1.45 percent, an employer must withhold a 0.9 percent AdMT from wages it pays to an employee in excess of \$200,000 in a calendar year. The employer is required to begin withholding AdMT in the pay period in which it pays wages more than \$200,000 to an employee and continue to withhold it each pay period until the end of the calendar year. AdMT is only imposed on the employee. There is no employer share of AdMT. All wages that are subject to Medicare tax are subject to AdMT withholding if paid in excess of the \$200,000 withholding threshold.
- (3) Wages are considered to be paid when they are made available to the employee; that is, when they are actually or constructively received by the employee. Wages are constructively received when credited to the account of the employee or when set apart to permit the employee at his or her discretion to draw upon the account or take possession of the amount without substantial limitations or restrictions.
- (4) An employer may not, in determining the social security wage limit and wages subject to AdMT, take into consideration wages paid to an employee by

another employer (except a predecessor employer) in a calendar year. Rev. Rul. 55-584, 1955-2 C.B. 394, and Rev. Rul. 57-32, 1957-1 C.B. 301. The employee can recover any excess employee social security tax and/or AdMT withheld by multiple employers on their individual income tax return. See IRM 4.23.5.12, *Related Corporations Providing Concurrent Employment—Common Paymaster*, and IRM 4.23.5.12.1, *Wages Paid by Predecessor Attributed to Successor*, for additional information.

4.23.8.6.1  
(04-17-2024)  
**Special Rules Relating  
to FICA, FUTA, and  
RRTA Taxes**

- (1) The IRS is responsible for enforcement of the filing of tax returns as well as collection of taxes under the Railroad Retirement Tax Act (RRTA). See Chapter 22, "Railroad Retirement Tax Act", of the IRC.
- (2) Under the Railroad Retirement Act (RRA), creditable compensation and retirement-survivor benefits are based on a two-tier structure: Tier 1 and Tier 2. Railroad retirement taxes under the RRTA are also computed using the tier structure. Tier 1 is the railroad retirement equivalent of social security wages and benefit amounts. Tier 2 resembles private pensions.
- (3) Instead of paying FICA, railroad employers and employees pay RRTA taxes. These taxes are collected and deposited throughout the year but are not reported quarterly on Form 941. They are reported annually on Form CT-1, Employer's Annual Railroad Retirement Tax Return. Railroad employee representatives file Form CT-2, *Employee Representative's Quarterly Railroad Tax Return*, to pay Tier 1 and Tier 2 taxes as provided in IRC 3211 and IRC 3213 on compensation received for services performed as an employee representative. FITW is not reported on the Form CT-1 or Form CT-2. Railroads are required to report FITW on the quarterly Form 941.
- (4) The IRS is responsible for assessing and collecting FICA, FUTA, and RRTA taxes. However, it is not responsible for Railroad Unemployment Insurance Act (RUIA) taxes. A railroad employer is subject only to RUIA and not FUTA for railroad employees. If an employer audit results in a conversion from FICA tax to RRTA tax and FUTA tax returns have been filed up to that point, the examiner may only correct the FUTA liabilities. It is the railroad employer's responsibility to reconcile both unemployment accounts and correct the RUIA.
- (5) There are times when the employer status as a railroad may be unclear. The employer, employees, or others may ask either the Railroad Retirement Board (RRB) or the IRS to determine its status as a railroad. The RRB issues a Board Coverage Determination (BCD) to outline this opinion. The IRS may also render an opinion on the status of an employer as a railroad. The Office of the Associate Chief Counsel - Employee Benefits, Exempt Organizations, and Employment Tax (EEE) may rule on the employer status as a railroad in a Private Letter Ruling (PLR). In addition, the Office of the Associate Chief Counsel (EEE) had previously issued informal opinions to the appropriate campus function indicating if it concurred with RRB BCD opinions, so that the appropriate filing requirements could be entered. However, beginning in 2009, this task was transferred to the Campus function to make the independent determination regarding the taxpayer's filing requirements based on the information provided by the RRB. In most cases, the Office of Associate Chief Counsel had concurred with RRB's determination regarding railroad status based on the information provided. The Campus function will consult with the Office of Division Counsel (TEGEDC) in any unclear cases.

- (6) IRC 6103(l)(1)(C) authorizes disclosure of returns and return information concerning RRTA to the RRB for administering the RRA. If the adjustment is for RRTA, Campus Compliance Services, Centralized Case Processing (CCP), will forward copies of all RRTA tax audit results, assessments, or abatements to the RRB Chief Financial Officer. Only RRTA information is permitted to be disclosed to the RRB. Contact your local IRS disclosure office if you need to disclose additional information.
- (7) If a taxpayer erroneously pays RRTA tax when it should have paid FICA tax, or vice versa, the erroneous payment of the one tax is credited against the other. See IRC 3503. Treas. Reg. 31.3503-1 and the regulations under IRC 6205, IRC 6402, and IRC 6413 provide the proper procedures for correcting these errors. Note that Treas. Reg. 31.3503-1 has not been updated to refer to Form 941-X instead of Form 843. See Treas. Reg. 31.3503-1.
- (8) If an employer erroneously paid FICA taxes with respect to the remuneration of employees for services which are held to be covered under the Railroad Retirement Tax Act, RRTA returns must be filed for each return period involved. The taxable compensation paid to all employees involved and the employer tax and employee tax applicable must be reported on such returns. The correct original Form CT-1 and/or Form CT-2, adjusted Form CT-1X, amended Form CT-2, or an employment tax report must be prepared. In addition, credit must be claimed for the amount of FICA tax (both the employer and the employee portions) erroneously paid for corresponding return periods, and all of the wages erroneously reported for the employees on FICA returns must be corrected on an accompanying Form 941-X for each period. See Treas. Reg. 31.6205-1(b)(2)(ii) and the Instructions for Form 941-X. In addition, the employer will be required to file Form W-2c, *Corrected Wage and Tax Statement*, in order for the Social Security Administration (SSA) to correct the employee's earnings record.
  - a. Treas. Reg. 31.3503-1 requires the employer to file a claim for the FICA tax in accordance with Treas. Reg. 31.6402(a)-2. Though the regulation states the claim should be filed on Form 843, Form 941-X should be used instead. If the employer fails to file a claim or files a protective claim for FICA tax, then the examiner should recommend the assessment of the full amount of RRTA tax to avoid statute problems.
  - b. Only the net RRTA tax liability will be assessed after the credit for FICA tax has been applied. The delinquency penalty provisions do not apply as long as the taxpayer mistakenly and in good faith paid FICA taxes on the remuneration involved. For the same reason, and in order to avoid double taxation, it has been the practice of the IRS to grant relief in such cases by permitting the crediting of one tax against another when the period of limitations on refunds or credits has expired with respect to any erroneously or mistakenly paid taxes. The rates under RRTA are higher than under FICA. Therefore, no net refund is generally involved in this transaction.
  - c. If Form 940 returns have been filed for years that are the subject of conversion from FICA tax to RRTA tax, see IRM 4.23.8.7.3 below.
- (9) If an employer erroneously paid RRTA taxes with respect to the compensation of employees for services which are held to be covered under the FICA, FICA tax returns must be filed for each return period involved. The wages paid to all the employees involved and the applicable tax must be reported on the appropriate return, either an original Form 941 and/or Form 941-X. In addition, credit

must be claimed for RRTA employer and employee taxes erroneously paid for the corresponding return periods using Form CT-1X. See Treas. Reg. 31.6205-1(b)(2)(iii) and the instructions for Form CT-1X. To the extent the credit for RRTA tax exceeds the liability for FICA tax, the excess will be refunded to the extent that refund is not barred by the statutory period of limitations on refunding of tax. See IRC 3503 and Treas. Reg. 31.3503-1 and 31.6402(a)-2. To the extent the underpayment of FICA tax exceeds the credit for RRTA tax, the net FICA tax will be assessed.

4.23.8.6.1.1  
(04-17-2024)

**Processing and  
Submission of Forms for  
FICA and RRTA  
Adjustments**

- (1) After an employer has learned they are a railroad and have erroneously reported and paid FICA taxes, the employer may correct the previous actions taken by following the steps below:

- a. RRB has determined that Employer is a railroad - effective date: "\_\_\_\_\_."
- b. Employer previously filed Form 941 reporting all wages under the FICA system.
- c. Employer requests to file Form CT-1 to comply with the RRB's decision.
- d. Employer requests that the amounts of FICA previously paid be **CREDITED** against the RRTA due.
- e. Employer attaches the following forms pursuant to this request:

Attached Forms
1. Forms W-2c for each year for each employee showing zero FICA wages and taxes. Employer requests that these be forwarded to the SSA so each employee's record can be corrected.
2. Corrections to Form 941 prepared on Forms 941-X for each quarter showing the elimination of FICA wages and FICA taxes.
3. Form 941-X for each quarter showing total amount of FICA overpayment. Employer requests that these FICA amounts erroneously paid <b>NOT BE REFUNDED</b> , but be credited on Form CT-1.
4. Form CT-1 for each year showing total RRTA tax amounts on Line 13, "Total Tax Based on Compensation," offset by total FICA already paid on Line 14, "Adjustments to employer and employee railroad retirement taxes based on compensation."
5. If applicable, a statement such as: "Employer requests that late filing and late payment penalties be waived as, prior to the RRB decision dated "_____", employer did not realize it was subject to RRTA taxes."
Note: Employer must be able to explain the circumstances that justify its mistaken understanding.

- (2) The above package of forms should be aggregated together by year. A cover sheet summarizing each year's results should be attached to each year's package of returns.
- (3) The entire package including all years should be submitted under a cover letter briefly explaining the above to the Accounts Management using eFax number 855-307-3090 with the subject line **Processing and Submission of Forms for FICA and RRTA Adjustments**.

**Note:** If the examiner is submitting multiple packages, a separate eFax should be sent for each distinct Employer Identification Number (EIN).

4.23.8.6.2  
(10-26-2015)  
**Specific Instructions -  
FICA Overpayments in  
Examinations**

- (1) If the examination of multiple periods results in an over-assessment for any period, the examiner will follow these procedures:
  - a. Verify that the error causing the over-assessment was not corrected in a subsequent period.
  - b. If the error was properly corrected by the employer in another quarter, verify this fact and make comments in the workpapers or the examination report.
  - c. If the error was not corrected, inform the taxpayer of the option to make an adjustment or file a claim for refund using Form 941-X.
  - d. If the employer elects to file a claim, secure the claim and determine the amount allowable. The secured claim may be on Form 941-X or may be an informal claim. Procedures for the examination of claims should be followed in these cases. See IRM 4.23.13, *Employment Tax - Adjusted Returns, Abatements and Claims*. The amount of claim allowable will be reflected on Form 4668. An explanation of adjustment will be prepared to inform the employer of the amount of the claim allowed. The explanation may be in the other information of Form 4666 or prepared on Form 886-A.
  - e. If the employer does not agree with the over-assessment, prepare the report to show that the taxpayer does not wish the adjustment to be made.

4.23.8.6.3  
(10-26-2015)  
**Additional Medicare Tax  
(AdMT) Withholding  
Overpayments - Current  
Year**

- (1) If, during any return period, an employer:
  - a. Collects from an employee more than the correct amount of AdMT withholding (IRC 3102),
  - b. Repays the amount of the over-collection to the employee, and
  - c. Obtains a written receipt showing the date and the amount of the repayment before the return for such period is filed with the IRS and before the end of the calendar year in which the over-collection was made,

the employer shall not report on any return or pay to the IRS the amount of the over-collection.

- (2) If, in any return period in a calendar year, an employer collects from any employee more than the correct amount of AdMT under IRC 3102 and the employer pays the over-collection to the IRS, and if the employer discovers the error within the calendar year in which the wages were paid, the employer may correct the error. The employer must repay or reimburse its employees in the amount of the over-collection prior to the end of the calendar year in which the wages were paid. See Treas. Reg. 31.6413(a)-1(a)(2). The employer may correct the overpayment through an interest-free adjustment by filing an adjusted return (for example, Form 941-X). See Treas. Reg. 31.6413(a)-2(b)(2). Form W-2 or Form W-2c shall be prepared so as to adequately reflect the adjustments.

4.23.8.6.4  
(05-17-2018)  
**Additional Medicare Tax  
(AdMT) Withholding  
Overpayments  
Discovered in an  
Examination**

- (1) Any overpayment of AdMT withholding paid to the United States Treasury during the return periods of one calendar year is not adjustable if the error is discovered in a subsequent year, or if the employer does not repay or reimburse its employees in the amount of the over-collection before the end of the calendar year in which the wages were paid, unless it is attributable to an administrative error. An administrative error is any error that does not change the amount of AdMT that was withheld. Only transposition or basic math errors, such as addition, subtraction, and multiplication computations, in which the amount reported does not agree with the amount withheld from an employee's wages, are administrative errors. In addition, the employer may not claim a refund or credit of the overpayment on a Form 941-X unless the amount of such overpayment was not withheld from an employee's wages.

**Note:** For examples of administrative errors, see IRM 21.7.2.4.6.3.1, *Administrative Errors*.

- (2) If an examiner discovers an overpayment in a prior calendar year and no adjustment was made and no claim filed, the examiner will allow the overpayment for refund only to the extent the overpayment was an administrative error and not deducted or withheld from an employee's wages.
- (3) If an adjustment was made on a return for a period in one calendar year to correct an overpayment on a return for a period in another calendar year, where the overpayment was not actually withheld the examiner will:
  - a. Adjust the return on which the adjustment was made by increasing the AdMT withholding reported by the amount of the adjustment, and
  - b. Include the overpayment on the examiner's report for the period in which the overpayment was made.

4.23.8.6.5  
(05-17-2018)  
**Trustee in Bankruptcy  
Acting as Employer**

- (1) In accordance with IRC 3401(d)(1) and the holding of the Supreme Court in *Otte v. U.S.*, 419 U.S. 43 (1974), 1975-1 C.B. 329, a trustee in bankruptcy is an employer for purposes of income tax withholding and withholding the employee's share of FICA. This is because the trustee in bankruptcy has control of the payment of wages.
- (2) As the payer, the trustee is obligated to prepare and file Form 941 and to prepare, file, and distribute the related Form W-2 for each wage claimant. Furthermore, *Otte* has been extended to provide that the person having control of the payment is also an employer for purposes of the employer's share of FICA and FUTA. See *Lane Processing Trust v. United States*, 25 F.3d 662 (8th Cir. 1994), and *re Armadillo Corp.*, 410 F. Supp. 407 (D. Col. 1976), *aff'd*, 561 F.2d 1382 (10th Cir. 1977). Withholding and employment taxes incurred by the bankruptcy estate are entitled to be paid as administrative expenses under Bankruptcy Code section 503(b)(1)(B).

4.23.8.7  
(04-17-2024)  
**Federal Unemployment  
Tax**

- (1) When there is additional liability for FUTA tax for a calendar year, secure the taxpayer's agreement on the appropriate Form 2504. See IRM 4.23.10.10.10, *Form 2504*, *Form 2504-S*, and *Form 2504-T*. FUTA, FICA, and FITW may be included on the same Form 2504 agreement, but separate lines should be used for each type of tax. FUTA tax due for one calendar year may not be adjusted in a return filed for another calendar year.

- (2) When making any worker classification adjustment, the de minimis exception standards of IRM 4.10.2.3.1, *Large Unusual or Questionable (LUQ) Items Defined*, **do not apply**. The reclassification of an independent contractor to an employee would be considered to be a special situation where the assessment would be made regardless of the amount.
- (3) The credit under IRC 3302(a) for contributions paid to a state unemployment fund will be allowed if the contributions are timely. If contributions are not timely, only 90 percent of the credit that would otherwise be allowable for timely contributions is available to the taxpayer. See IRC 3302(a)(3). Therefore, if there are additional FUTA wages and the taxpayer pays the additional tax due to the state on these wages, the taxpayer may receive only 90 percent of the credit that would have been allowed if the taxes had been paid timely.
- (4) The additional credit under IRC 3302(b) is allowable only for the wages for which contributions are required to be paid to the state by the taxpayer, and where the taxpayer paid such required contributions. If the examiner discovers additional FUTA wages which are not required to be reported to the state, no additional credit under IRC 3302(b) is available to the taxpayer with respect to such wages. In this instance, assess the full FUTA rate on the additional wages.

**Note:** If the taxpayer paid state contributions in excess of the maximum credit allowable against the previously reported FUTA wages, that is in excess of 5.4 percent, there may be additional state contributions to credit against the FUTA tax on the additional wages. See the worksheet in the Form 940 Instructions.

- (5) When an issue is identified that affects FUTA taxes during an examination, the taxpayer should report the additional adjusted wages to the state if they are subject to state contributions.

**Caution:** Before allowing any credit for additional contributions paid or additional credit under IRC 3302(b), see IRM 4.23.10.11, *Credit for FUTA Tax in Examination*, for an in-depth discussion of taxpayer obligations and examiner procedures.

- (6) In some cases, a 30-day period is granted for the purpose of submitting evidence of payment to a state fund, yet the taxpayer may disagree with the finding that a delinquent tax liability exists or with the correctness of the amount of such liability. Issuance of a preliminary letter affording the taxpayer an opportunity to request an Appeals conference should be delayed until the expiration of the 30-day period mentioned or receipt of the evidence of payment into the state fund, whichever is earlier.
- (7) For information on Substitute for Return procedures for FUTA, see IRM 4.23.10.11.1, *IRC 6020(b) Returns for FUTA*.

## 4.23.8.7.1 (03-19-2021) **FUTA State Credit Reduction**

- (1) Title XII of the Social Security Act provides for advances to states which are in need of supplementary funds for the payment of unemployment compensation benefits. If the advances are not repaid in full within the specified period, employers in affected states will have their credit against the FUTA tax reduced as provided by IRC 3302(c)(2). The amount collected because of the reduced credit is applied against the outstanding balances of the respective state(s).

**Note:** See IRC 4.19.5.4.7.8, *Credit Reduction States*, for more information.

**Note:** For a listing of FUTA credit reductions, see the Department of Labor website: [https://oui.doleta.gov/unemploy/futa\\_credit.asp](https://oui.doleta.gov/unemploy/futa_credit.asp)

- (2) The IRS certifies actual collection data to the Financial Management Service (FMS) and the Department of Labor (DOL). The FUTA state credit reduction amount is derived from information on Form 940.
- (3) After the close of each taxable year, the IRS receives certifications made by the Secretary of Labor to the Secretary of the Treasury relating to the approval of state unemployment compensation laws and with respect to additional credit allowance, in accordance with IRC 3303(b)(1) and IRC 3304(c). Announcement of such certifications is published annually in the Internal Revenue Bulletin.
- (4) For the purpose of the additional credit allowance and in accordance with Treas. Reg. 31.3302(b)-2, the IRS receives, at the close of each taxable year, a letter of certification from each state disclosing the highest rate of contributions applied under the state law in the calendar year. Unless the IRS advises to the contrary, area offices will assume that the highest rate of contributions applied in a calendar year under the law of any state was not lower than 5.4 percent. If, in the case of any state, notification is received that the highest rate applied under the state law was lower than 5.4 percent, the amount of the additional credit computed with respect to such state will be reduced accordingly.

4.23.8.7.2  
(02-01-2003)  
**Allowing FUTA Credit in  
Cases Involving  
Insolvent Taxpayers**

- (1) In the case of an insolvent taxpayer or where the estate of any deceased debtor, in the hands of executors or administrators, is insufficient to pay all the debts due from the deceased, the taxpayer's right to pay the state and take credit against the federal tax has been discontinued. Accordingly, once priority attaches under 31 USC 3713, payments of the assets in the custody of the fiduciary into a state unemployment fund cannot serve to reduce FUTA tax liability.
- (2) If doubt exists in any case regarding the allowance of credit under the FUTA credit provisions, the advice of the TEGEDC area counsel attorneys should be requested.

4.23.8.7.3  
(08-11-2009)  
**Special Rules Relating  
to FUTA and RUIA Taxes**

- (1) Railroads are not covered under the FUTA. Instead they have their own unemployment compensation system referred to as the RUIA. Although the IRS is responsible for FUTA, FICA and RRTA, it is not responsible for RUIA. RUIA filings, taxes, collections, and benefits are controlled solely by the U.S. RRB. A railroad employer is always subject to RUIA and never to FUTA for railroad employees.

**Note:** However, the same entity may be both a railroad employer for railroad employees and non-railroad employer with respect to other employees.

- (2) If an employer erroneously paid FUTA tax with respect to the remuneration of employees for services which are covered under the RUIA, the examiner will notify the employer that they are entitled to a refund of FUTA and recommend the over-assessment of the FUTA tax. As the IRS does not have jurisdiction over RUIA taxes, FUTA payments cannot be transferred to RUIA. The employer needs to work with the RRB to pay RUIA separately.

4.23.8.7.4  
(04-17-2024)  
**FUTA Tax Overpayments**

- (1) If during an examination it is determined an overpayment of FUTA tax was reported, prepare an examination report showing the over-assessment.
- (2) If a refund of FUTA tax is based on credit allowable for contributions paid under the unemployment compensation laws of a state, no interest is allowable on the refund. In those cases, indicate on Form 3198 or RCCMS 3198-A. (Refer to IRC 6413(d)).

4.23.8.7.5  
(04-17-2024)  
**Federal Unemployment Tax Return Processing Procedures**

- (1) In order to correctly process cases with an adjusted Form 940 examiners must provide the appropriate Case Processing Support unit with the following information:
  - a. Total tax adjustment and the state code being adjusted,
  - b. Wage adjustment and the state code being adjusted,
  - c. Total corrected Form 940 wages, and
  - d. Credit reduction wages, credit reduction amount and the state code(s) for the state(s) subject to credit reduction (if applicable).

**Note:** For TE/GE Exempt Organization (EO), provide to the appropriate EO closing function.

- (2) When a FUTA examination results in a change of wages (increase or decrease), report the change in Item 15 of Form 5344 (or the Individual/Bus (1 of 3) tab of the closing record in RCCMS for TE/GE) by inserting a three character reference code and the rounded dollar amount of the change in wages. (This will equal Line 2 of Form 4667, Examination Changes – Federal Unemployment Tax Examination Closing Record). The reference code will be a “W” followed by the state abbreviation sanctioned by the United States Postal Service, (for example, “WCA” for California or “WIN” for Indiana). If adjustments are made to more than one state, the wage adjustment amount(s) attributed to each state will be entered.
- (3) When a FUTA examination results in a change in tax (increase or decrease), report in Item 15 of Form 5344 (or the Individual/Bus (1 of 3) tab of the closing record in RCCMS for TE/GE) by inserting a three character reference code and the rounded dollar amount of the tax change. (This will equal Line 8 of Form 4667). The reference code will be a “T” followed by the state abbreviation as described in (2) above, for example, “TUT” for Utah. If adjustments are made to more than one state, the tax adjustment amount(s) attributed to each state will be entered.
- (4) Use the top two lines for wage and tax increases. Enter the code on the left and the dollar amounts on the right of Item 15. Enter decreases on the bottom two lines in the same manner.

4.23.8.8  
(02-01-2003)  
**Computing Income Tax Withholding**

- (1) IRC 3402 requires employers to deduct and withhold income tax from payments of wages. When income tax withholding is involved and IRC 3509 is not applicable, use the supplemental wage withholding rates. See IRM 4.23.8.4, *IRC 3402(d) - Relief for Employer When Employees Have Paid Income Tax on Wages*.
- (2) Where the employer can establish the employee’s allowable number of exemptions from the Form W-4, Employee’s Withholding Allowance Certificate, on file for the employees during the audit years, the computation can be made based on the laws and regulations in existence during those years.

- (3) Treas. Reg. 31.3403-1 states that every employer required to deduct and withhold the tax under IRC 3402 from the wages of an employee is liable for the payment of such tax, whether or not it is collected from the employee by the employer.
- (4) Under IRC 3402(d), the employer may request relief from payment of FITW. Form 4669 and Form 4670 are used for this purpose. See IRM 4.23.8.4.3, *Procedures for Relief Under IRC 3402(d) and/or IRC 3102(f)(3) in Examination*.

4.23.8.8.1  
(08-11-2009)  
**Income Tax Withholding  
Overpayments - Current  
Year**

- (1) If, during any return period, an employer collects from an employee more than the correct amount of FITW and repays the amount of the over-collection to the employee and obtains a written receipt showing the date and the amount of the repayment before the return for such period is filed with the IRS and before the end of the calendar year in which the over collection was made, the employer will not report on any return or pay to the IRS the amount of the over-collection.
- (2) If, in any return period in a calendar year, an employer collects from any employee more than the correct amount of FITW under IRC 3402 and the employer pays the over-collection to the IRS, and if the employer discovers the error within the calendar year in which the wages were paid, the employer may correct the error. The employer must repay or reimburse its employees in the amount of the over-collection prior to the end of the calendar year in which the wages were paid. See Treas. Reg. 31.6413(a)-1(b)(2). The employer may correct the overpayment through an interest-free adjustment by filing an adjusted return (for example, Form 941-X). See Treas. Reg. 31.6413(a)-2(c)(2). Form W-2 or Form W-2c, *Corrected Wage and Tax Statement*, will be prepared so as to adequately reflect the adjustments.

4.23.8.8.2  
(05-17-2018)  
**Income Tax Withholding  
Overpayments  
Discovered in an  
Examination**

- (1) Any overpayment of income tax withholding paid to the United States Treasury during the return periods of one calendar year is not adjustable if the error is discovered in a subsequent year, or if the employer does not repay or reimburse its employees in the amount of the over-collection before the end of the calendar year in which the wages were paid, unless it is attributable to an administrative error. An administrative error is any error that does not change the amount of income tax that was actually deducted and withheld. Only transposition or basic math errors, such as addition, subtraction, and multiplication computations, in which the amount reported does not agree with the amount actually deducted and withheld from an employee's wages, are administrative errors. In addition, the employer may not claim a refund or credit of the overpayment on a Form 941-X unless the amount of such overpayment was not withheld from an employee's wages.

**Note:** For examples of administrative errors, see IRM 21.7.2.4.6.3.1, *Administrative Errors*.

- (2) If an examiner discovers an overpayment in a prior calendar year and no adjustment was made and no claim filed, the examiner will allow the overpayment for refund only to the extent the overpayment was an administrative error and not deducted or withheld from an employee's wages.
- (3) If an adjustment was made on a return for a period in one calendar year to correct an overpayment on a return for a period in another calendar year, where the overpayment was not actually withheld the examiner will:

- a. Adjust the return on which the adjustment was made by increasing the FITW reported by the amount of the adjustment, and
- b. Include the overpayment on the examiner's report for the period in which the overpayment was made.

## 4.23.8.9 (04-17-2024) **Gross Up of Employment Taxes**

- (1) For the year in which the employment tax liability is paid, if the employer deducts the employee FICA tax from other remuneration paid to the employee or otherwise collects the amount from the employee in accord with the regulations under IRC 6205, the payment of employee FICA tax by the employer is not additional compensation to the employee in the year paid. However, if the employer does not seek repayment of the employee FICA tax from the employee, the employer's payment of employee FICA tax in the year paid without collecting the amount from the employee is additional wages to the employee when paid and is subject to employment taxes.
- (2) The employer may either withhold the employee's FICA tax and income tax on such additional wages in the year paid from other wages or via payment by the employee or may calculate the applicable employment taxes on such additional wages in the year paid by grossing up the employee FICA tax and income tax withholding under the procedures of Rev. Proc. 81-48, 1981-2 C.B. 623 and Rev. Rul. 86-14, 1986-1 C.B. 304.

**Note:** For further discussion of grossing up the employee FICA tax and income tax withholding during an examination refer to PMTA 2018-15 dated June 25, 2018 ([https://www.irs.gov/pub/irsoa/pmta\\_2018\\_15.pdf](https://www.irs.gov/pub/irsoa/pmta_2018_15.pdf)).

- (3) The IRS's position regarding a request for a refund of taxes on a Form 941-X that resulted from a gross up of wages due to a pre-arranged agreement is discussed in IRM 4.23.13-3, *FAQs on Form 941-X Claims*, question 8.
- (4) An employer's payment of taxes that should have been withheld in a prior year does not create additional wages to the employee for the prior year.

## 4.23.8.10 (06-07-2011) **Period of Limitation on Credit or Refund**

- (1) General Rule:
  - a. As with other claims for refund, under IRC 6511(a), claims for credit or refund of any overpayment of FICA, FITW, FUTA, or RRTA taxes must be filed within three years from the date the return was filed or two years from the time the tax was paid, whichever is later. If no return was filed by the taxpayer, a claim for credit or refund must be filed within two years from the time the tax was paid.
  - b. If the claim for refund is filed within the three-year period, the amount of the credit or refund is limited to the portion of tax paid during the three years immediately preceding the filing of the claim (plus the period of any extension of time for filing the return). If the claim was not filed within the three-year period, the amount of the credit or refund will not exceed the portion of the tax paid during the two years immediately preceding the filing of the claim.
- (2) In computing the period of limitations, IRC 6513(c) provides that employment tax returns reporting FICA tax or FITW for any period ending with or within a calendar year filed before April 15th of the succeeding calendar year are deemed filed on April 15th of such succeeding calendar year. Likewise, IRC 6513(c) provides that FICA tax or FITW paid during any period ending with or

within a calendar year before April 15th of the succeeding calendar year is deemed paid on April 15th of the succeeding calendar year.

- (3) The statutory period of limitations also applies to the allowance of credits taken on FICA and RRTA returns. Credit for overpayment of taxes claimed on a return are considered to be claimed on the date the return is filed with the IRS. Under IRC 6513(c), FICA returns filed before April 15th of the succeeding calendar year are deemed filed on April 15th of the succeeding calendar year, but this does not apply to RRTA returns.

4.23.8.10.1  
(05-17-2018)  
**Mitigation of Statutes of  
Limitations in Case of  
FICA and SECA Taxes  
(IRC 6521)**

- (1) In certain circumstances, IRC 6521 can mitigate the effects of an expired period of limitations in the case of FICA and SECA taxes. IRC 6521 does not provide a mechanism to assess FICA or SECA taxes but instead provides limited mitigation of the expiration of the assessment statute of limitations for FICA or SECA taxes when a taxpayer's employment status has been corrected and either self-employment income is incorrectly treated as wages and FICA taxes are paid, or wages are incorrectly treated as self-employment income and SECA taxes are paid. IRC 6521 mitigates these types of errors by providing a reduction or offset of the amount erroneously paid by the amount due, or of the amount actually due by the amount erroneously paid, despite the expiration of the limitations period as to one of the taxes. Refer to Rev. Rul. 78-127, 1978-1 C.B. 436, when dealing with mitigation issues under IRC 6521.

**Note:** IRC 6521 does not apply if neither SECA nor FICA tax was paid. IRC 6521 also does not apply if the assessment statute of limitations on both the employer's employment tax returns and the employee's income tax return are currently open.

- (2) Examiners are advised to take a conservative approach and protect the FICA tax statute rather than rely on mitigation rules. See IRM 25.6.22.6.10.1, *Employment Taxes – Employee Share of FICA*.

**Note:** See IRM 4.23.8.5.2, *Application of IRC 3509*, and CCA 200825043. If IRC 3509 applies, IRC 6521 does not apply.

4.23.8.11  
(04-17-2024)  
**Delinquent Forms  
W-2/W-2c**

- (1) The employer reports wage information to the SSA on Form W-2, *Wage and Tax Statement*, or Form W-2c, *Corrected Wage and Tax Statement*. Delinquent Forms W-2 or Forms W-2c discovered during an examination should be secured by the examiner.
- (2) Paper forms should be sent to SSA's Wilkes-Barre Data Operations Center (WBDOC) at the addresses listed on Form W-3 or Form W-3c. These addresses should be used for both worker classification and non-classification cases. Select the appropriate mailing address depending on the carrier chosen (U.S. Postal Service or a private delivery service such as FedEx or UPS).
- (3) For electronic submissions, refer the employer to the SSA's webpage (<https://www.ssa.gov/employer/>), *Employer W-2 Filing Instructions & Information*, for services offered to businesses online and Form W-2 filing assistance.

**Note:** Prior to January 1, 2024, if the employer is expected to file 250 or more Forms W-2 or Forms W-2c during a calendar year, they are required to be file them electronically.

**Note:** Form W-2 and W-2c, required to be filed **on or after January 1, 2024**, the final regulations reduce the electronic filing threshold from 250 W-2s to 10 informational returns. If an employer is required to file 10 or more informational returns (such as Forms W-2 or 1099), they must file electronically unless the IRS grants a waiver or exemption.

- (4) If the adjustment is for RRTA, Centralized Case Processing (CCP) will forward a copy of Form 4668 to the RRB.
- (5) Prepare Form 5346, *Examination Information Report*, for recipients of Form W-2/W-2c that appear to have high income tax potential for possible income tax under-reporting. Email the Form 5346 with Form 3210 to ET-WSD at **\*SBSE ET WSD Referrals** (sbse.et.wsd.referral@irs.gov).

## 4.23.8.11.1 (04-17-2024) **Delinquent Forms W-2/W-2c Secured By Examiner Due to Examination Adjustments**

- (1) Employers will be advised to prepare Form W-2 or Form W-2c, whichever is applicable, to report the amount of wage adjustments for each individual who was affected by the employment tax examination. Since no income taxes were withheld from the employee's wages as a result of the examination, no income taxes should be reported on delinquent Form W-2 or Form W-2c statements in Box 2.

**Note:** If the names of the workers are unknown, the examiner should not solicit Forms W-2 from the taxpayer. The examiner should advise the taxpayer that they may receive a notice from the SSA in the future due to the tax assessed not matching the Forms W-2 filed and they should respond with a copy of their audit report.

**Note:** TE/GE employees should refer to IRM 4.70.13.9.5.8, *Delinquent Forms W-2/W-2c Secured by Examiner During Examination*, for their procedures.

- (2) When the employee FICA is paid by the employer, the employee receives credit for the employee FICA tax and the employer is instructed under regulations under IRC 6205 how to collect the employee FICA tax from the employee. Corrections should be made by the employer to the corrected wages on Form W-2 and/or Form W-2c in box 1, *Wages, tips other compensation*, box 3, *Social security wages*, and box 5, *Medicare wages and tips*. Additional employee FICA tax paid by the employer should be reported in box 4, *Social security tax withheld*, and box 6, *Medicare tax withheld*, as applicable.
- (3) Examiners will solicit Form W-2 or Form W-2c, and Form W-3 or Form W-3c, from the employer at the completion of an agreed employment tax examination. The employer should be given a reasonable time to prepare the wage statements. Penalties for Failure to File and Failure to Furnish must be considered even if the documents are secured. The case workpapers must be noted if reasonable cause penalty relief exists. See IRM 4.23.9.13.2, *Wage and Tax Statements*, for penalty information. See (8) below if employer is to submit the forms after the examination.

**Note:** If an examiner does not solicit Form W-2 or Form W-2c, and Form W-3 or Form W-3c, from the employer at the completion of an agreed employment tax examination the examiner needs to document the case file as why they did not.

**Reminder:** Forms W-2/W-3 are not secured for Classification Settlement Program (CSP) cases. See IRM 4.23.6, *Classification Settlement Program (CSP)*, for more information.

- (4) If there are no reasons for a waiver of the penalties, the penalties must be proposed and processed at the same time as the employment tax examination. See IRM 4.23.8.12, *Information Return Penalty Case File*, for instructions.
- (5) If the taxpayer does not provide the examiner with Form W-2 or Form W-2c and Form W-3 or Form W-3c at the conclusion of an agreed case, the examiner must include on Form 4668 the number of employees who should receive wage statements, the date to file and furnish the wage statements, and the address of where to send the wage statements.

**For SB/SE, include the following in the information section of Form 4668:**

Furnish Form W-2 (Wage and Tax Statement) or Form W-2c (Corrected Wage and Tax Statement) on or before January 31, [Insert Year], to each of the [Insert number] employees whose wages are adjusted by this report.

File Forms W-2 with Form W-3 (Transmittal of Wage and Tax Statements) or Forms W-2c with Form W-3c (Transmittal of Corrected Wage and Tax Statements) on or before January 31, [Insert year], with the Social Security Administration (SSA).

IRC 6721 and IRC 6722 provide penalties for failure to file and failure to furnish information returns. You must file the information returns electronically if you are required to file 250 or more returns. To obtain specifications for e-filing your returns, visit the SSA's website at [www.socialsecurity.gov/employer](http://www.socialsecurity.gov/employer). If filing paper returns, file with the SSA at the appropriate address in the General Instructions for Forms W-2 and W-3, (Including Forms W-2AS, W-2CM, W-2GU, W-2VI, W-3SS, W-2c, and W-3c).

**Note:** For TE/GE functions: All returns should be sent to SSA directly.

- (6) When Forms W-2/W-2c are secured:
  - a. Reconcile the FICA wages on Form W-3/W-3c to the FICA wages on Form 4668.
  - b. Resolve any discrepancies with the employer.
  - c. Annotate "Wage Statements Secured By Examiner" in the Form 4668 block regarding the filing of Forms W-2/W-2c and in the other instructions section of Form 3198 or RCCMS 3198-A.
  - d. Annotate in red "Delinquent Returns - Secured by Examination — Penalty Considered" across the bottom of Form W-3/W-3c. This will alert the SSA that the area office has taken appropriate action concerning the assertion of penalties under IRC 6721 and IRC 6722.
  - e. A copy of the Form W-3/W-3c and Forms W-2/W-2c must be uploaded to IMS and named using standard naming conventions. See IRM 4.23.4.5.5, *File Naming Convention*.

- f. If the employer has not already done so, send the original paper Forms W-2/W-3 and W-2c/W-3c sent to SSA's Wilkes-Barre Data Operations Center (WBDOC) at the addresses listed on Form W-3 or Form W-3c with a Form 3210.
- g. An employer filing Forms W-2/W-3 or W-2c/W-3c electronically must provide confirmation that SSA has received the electronic submission. The confirmation receipt should be included in the workpapers as sufficient filing substantiation.

**Reminder:** Prior to January 1, 2024, if the employer is expected to file 250 or more Forms W-2 or Forms W-2c during a calendar year they are required to file them electronically. On or after January 1, 2024, the electronic filing threshold was reduced from 250 Forms W-2 to 10 informational returns. See IRM 4.23.8.11, *Delinquent Forms W-2/W-2c*, for additional information.

- (7) Secured Forms W-2 due to conversion of independent contractor to employee:
  - a. Annotate "Reclassification - Employee Status" on Form 3198 or RCCMS 3198-A and on top of Form 4668. This will assist CCP in identifying for SSA any Forms W-2 that are subsequently filed by the employer.
  - b. Advise the employer to take prompt action in notifying their employees so that the workers will have the opportunity to file a claim for refund if they did pay self-employment tax on the same wages.
  - c. Provide the employer with an example of a letter they would issue which explains to the workers why they are receiving the wage statement and Notice 989. See IRM 4.23.10.8.1, *Non-CSP Procedures*. See IRM 4.23.10-10, *Filing Instructions for Reclassified Workers*, for an example of a letter that the employer could issue to employees.
- (8) In some circumstances, the examiner may permit the employer to delay the submission of the forms. For example, where it is determined that reasonable cause exists, the examiner may allow the employer an extension of time to prepare the Form W-2 or Form W-2c. However, the employer must file Form W-2c by the last day of January following the calendar year in which the employer agrees to the employment tax assessment. For example, for an agreed examination completed in September 2024, the Form W-2c is to be filed by the last day of January, 2025. The employer will be instructed to file Forms W-2 or Forms W-2c directly with SSA. The instructions included with Form 4668 (see IRM 4.23.8.11, *Delinquent Forms W-2/W-2c*) will provide the taxpayer with how and when to properly submit the forms. The employer must furnish the forms to employees by the last day of January of the calendar year following the assessment. Other Business Operating Divisions (BODs) should consult their respective procedures.

4.23.8.11.2  
(04-17-2024)  
**Delinquent Forms  
W-2/W-2c Not Secured  
by Examiner**

- (1) When Form(s) W-2/W-2c are not obtained from the employer at the conclusion of an agreed case, the examiner must provide instructions on Form 4668 to the taxpayer on where and when to send the completed forms. See IRM 4.23.8.11.1 (5) and (8).
- (2) The examiner must prepare a "tickler file." This file will be a single Adobe (.pdf) file and will include:
  - Full audit report for all applicable tax periods (Forms 2504, 4668, etc.),

- Form(s) 886-A, Explanation of Items, and
- List of employees whose wages are to be reported on the Forms W-2/W-2c. If an Excel file is available, the Excel file should be emailed to ET-WSD.

**Note:** TE/GE employees should refer to IRM 4.70.13.9.5.8.1.1, *Delinquent Forms W-2/W-2c Not Secured*, for their procedures.

- (3) The examiner will email this file to ET-WSD at **\*SBSE ET WSD Case Closing Packages** (sbse.et.wsd.case.closing.packages@irs.gov) for monitoring with the subject **Tickler File – Tax Periods 20XX03-20XX12**. The examiner should review the tickler file prior to emailing to ET-WSD to confirm that all scanned documents are complete and legible. A copy of the file must be uploaded as a workpaper in IMS to the relevant issue SAIN.
- (4) If an employer fails to file Forms W-2/W-2c by January 31 of the subsequent year, ET-WSD will determine if the case warrants penalty development by an examiner. If so, ET-WSD will control the case as a penalty case file and assign to the appropriate group.
- (5) Efforts will be made to secure the Forms W-2/W-3 and Form W-2c/W-3 c even if penalties are asserted. If the Failure to File Penalty and the Failure to Furnish Penalty have already been assessed and the taxpayer still refuses to file the forms, the Willful Failure to File Penalty under IRC 7203 should be considered. The taxpayer's appeal rights are post-assessment.

4.23.8.11.3  
(04-17-2024)

**Special Procedures For  
Failure to File Form W-2  
— Unagreed Case**

- (1) When the examiner recommends assessment of penalties for failure to file and failure to furnish Form W-2 on an employment tax case involving reclassification of workers to employee status and the case is unagreed, the appropriate Information Return Penalty Package will be prepared. When neither Forms 1099-MISC (for periods prior to 1/1/2020), or Forms 1099-NEC (for periods after 12/31/2019) nor Forms W-2 were filed, the following special procedures must be followed:
  - a. Prepare two forms Form 8278, *Assessment and Abatement of Miscellaneous Civil Penalties*, and two forms Form 3645, *Computation of Penalty for Failure to File Information Returns or Furnish Statements*. The first set of documents should reflect Form W-2 penalty assessments and the second should reflect the Form 1099 penalty assessments (a copy of Form 3645 should not be provided to the taxpayer).
  - b. Both sets of documents must be uploaded to the appropriate issue SAIN in IMS and named using standard naming conventions found in IRM 4.23.4.5.5, *File Naming Convention*. The first set (Form W-2 penalty) is named with a descriptive phrase beginning "PRIMARY POSITION." The second set (Form 1099 penalty) is named with a descriptive phrase beginning "ALTERNATE POSITION."

**Note:** For paper case file assembly, staple the first set (Form W-2 penalty) to the inside front cover and the second set (Form 1099 penalty) to the inside back cover. On the first set, attach a slip of paper indicating "PRIMARY EXAMINER POSITION;" on the second set, attach a slip of paper indicating "ALTERNATE EXAMINER POSITION."

- c. On Form 4318-ET or penalty lead sheet, prepare two explanations; title the first explanation "PRIMARY EXAMINER POSITION" and the second

“ALTERNATE EXAMINER POSITION.” The Form 4318-ET or penalty lead sheet must be uploaded to the appropriate technical issue SAIN in IMS and named using standard naming conventions.

**Note:** For paper case file assembly, prepare and attach Form 3210, *Document Transmittal*, to the front of Form 4318-ET or the penalty lead sheet.

- d. Enter in the Special Instructions section of Form 3198 or in the “other” section of RCCMS 3198-A “Suspend assessment of information return penalties until the taxpayer’s request for appeal period has expired.”

**Note:** If an Appeals conference is not requested, the civil penalty recommendation shown in the penalty package as the “PRIMARY EXAMINER POSITION” will be processed. If an Appeals Conference is requested, the civil penalty package with the examination case file will be closed to Appeals by Technical Services, where a final penalty determination will be made

- e. Associate the penalty file with the examination case file. In IMS, the penalty case can be added as an additional return within the same IMS case as the Form 941 returns.

4.23.8.11.4  
(04-17-2024)

## Delinquent Forms 1099 Secured by Examiner

- (1) The examiner should secure any delinquent Forms 1099 that were required to be filed during the audit years.

**Reminder:** TE/GE employees should refer to IRM 4.70.13.9.5.6, *Processing Delinquent Information Returns (Other than Form 5500 Series Returns)*, for further information.

- (2) Date stamp correspondence, envelope, transmittals, and any attached return(s) received. An acceptable “IRS Received Date” stamp must only be stamped on the face of the document in an area that does not cover taxpayer entries. Refer to IRM 3.10.72.6, *IRS Received Date*, for procedures on IRS received date stamping and postmark date stamping.
- (3) Prepare Form 1096, *Annual Summary and Transmittal of U.S. Information Returns*, if it is not furnished with the Forms 1099. Write “Delinquent Returns - Secured by Examination - Penalty Considered” in red ink in the space at the bottom of the Form 1096. Enter “E” (Exam) in the first box under “For Official Use Only.” This will alert the Campus that the area office has taken the appropriate action concerning assertion of penalties under IRC 6721 and IRC 6722.

**Note:** Do not make any markings in the top margin of Form 1096. This will interfere with the processing of these documents.

- (4) If there is more than one type of information return, prepare a separate transmittal Form 1096 for each type of information return.
- (5) Send Form 1096 and Forms 1099 to the appropriate Campus as indicated in IRM 20.1.7.5.1, *Field Examination Delinquent Information Return Procedures*, via Form 3210. A copy of the Form 1096 and Forms 1099 must be uploaded to IMS and named using standard naming conventions. See IRM 4.23.4.5.5, *File Naming Convention*.
- (6) For paper case file assembly, attach copies of the forms, including transmittals, to the workpapers.

**Note:** Retain original correspondence (including envelope) along with copies of the transmittal document and information returns in the penalty case file. Refer to IRM 4.23.8.12, *Information Return Penalty Case File*, for further information.

- (7) Evaluate and address whether backup withholding applies when Forms 1099 were required but not filed or furnished and the taxpayer did not have the payee's TIN at the time of making a reportable payment.
- (8) Prepare Form 5346 for recipients of Form 1099 that appear to have high income tax potential for possible income tax under-reporting. Email the Form 5346 with Form 3210 to ET-WSD at **\*SBSE ET WSD Referrals** (sbse.et.wsd.referral@irs.gov).

4.23.8.12  
(04-17-2024)  
**Information Return  
Penalty Case File**

- (1) When a determination is made that penalties for failure to file and failure to furnish Form W-2, Form W-2c, or Form 1099 apply to the examination, the examiner must prepare an Information Return Penalty case file. However, if an extension to file Form W-2c is granted by the examiner, the Form W-2c penalties do not become assessable under IRC 6721 and IRC 6722 until February 1st of the year following the examination.

**Note:** For further information see IRM 4.23.8.11.2, *Delinquent Forms W-2/W-2c Not Secured by Examiner*, IRM 4.23.9.13, *Penalties for Failure to File Certain Information Returns or Furnish Certain Statements*, and IRM 20.1.7, *Penalty Handbook - Information Return Penalties*.

**Note:** The OSP SharePoint (<https://irsgov.sharepoint.com/sites/ETD-KMT-KB015>) provides information to assist examiners with properly processing secured delinquent information returns and working and closing information return penalties cases, including Document 13267, *Field Procedures for Securing and Processing Information Return Penalties*.

**Note:** The Employment Tax Small Business Knowledge Base site (<https://irsgov.sharepoint.com/sites/ETD-KMT-KB014>) under the Tools chapter of the "Contacts Tools and Training" book there is the "Information Return Penalty Application." This is a tool that can be used to create, calculate and prepare the forms required for an information return penalty case.

**Reminder:** TE/GE employee should refer to IRM 4.70.13.9.5.6.2.1, *EO Information Return Penalties*, for further information.

- (2) Use Form 5345-D to request controls of the penalty case file on Examination Returns Control System (ERCS). Complete as normal with the following exceptions:
  - **Form Type:** Identify if the case is "Form 1099 Penalty", "Form 1099 NEC Penalty", or "Form W-2 Penalty".
  - **MFT Code:** For IMF, "P9/55", for BMF "P9/13".
  - **Activity Code:** 506.
  - **Statute date:** Non-filed information returns may either be "01/EE/YYYY" or "02/EE/YYYY". See IRM 4.23.9.13.1, *Information Returns Regarding*

*Payment of Remuneration for Services, IRM 4.23.9.13.6, Information Return Penalty Statute of Limitations, and IRM 20.1.7-3, Forms, for guidance.*

**Note:** EO follows local procedures to establish Information Return Penalty case file in RCCMS. Refer to IRM 4.70.13.9.5.6, *Processing Delinquent Information Returns (Other than Form 5500 Series Returns)*.

**Note:** Submit Form 5348 to update the penalty Assessment Statute Expiration Date (ASED) on ERCS to 3 years from the date that the delinquent returns were secured.

- (3) The workbook automates the preparation of Form 8278 the assessment document which is required for the completion of an Information Return Penalty case file. It also automates preparation of Form 3645 for each tax year. Refer to IRM 4.23.9-1, *Instructions for Determining Civil Penalty Statute of Limitations*, for instructions on determining the civil penalty statute of limitations.

**Note:** Do not provide a copy of Form 8278 or Form 3645 to the taxpayer.

- (4) Letter 5005, *Information Return Penalty Notice (Form W-2)*, or Letter 5005-P, *Information Return Penalty Notice (Form 1099)*, should be furnished to the taxpayer upon completion of the penalty calculations.

**Note:** The "Information Return Penalty Application" will generate Letter 5005 and 5005-P and Form 886-A, *Explanation of Items*.

- (5) Record on Form 886-A all pertinent information including the issues, facts, law, taxpayer's position, and conclusion. This will be part of the Information Return Penalty case file.
- (6) If the taxpayer agrees with the penalty, request payment. Prepare Form 3244-A, *Payment Posting Voucher - Examination*, to post payments received.

**Note:** Do not secure an agreement on Form 2504 or Form 4549. The information return penalty case file is separate from an employment, income tax, or other case file.

- (7) When asserting the penalty and the penalty relief provisions were considered, the following must be noted on Form 8278.

Form 8278 Penalty Relief
a. When penalty relief is denied:
1. Assert the penalty,
2. Note on Form 8278 that the relief provisions were considered, and
3. Identify the relief requested using the penalty reason codes in Exhibit 20.1.1-2, <i>Penalty Reasons Code Chart</i> , of the Penalty Handbook (IRM 20.1.1).
b. When penalty relief is granted:

<b>Form 8278 Penalty Relief</b>
1. The penalty should not be assessed, and
2. A notation should be made on Form 8278 that the relief provision was granted.
c. After determining whether to grant or deny the relief provisions, identify the relief request using the penalty reason codes in IRM 20.1.1-2, <i>Penalty Reason Code Chart</i> , of the Penalty Handbook (IRM 20.1.1). Compliance functions use penalty reference codes in the 600 series for assessing these penalties.

- (8) In a case involving delinquent Forms 1099, examiners should consider the applicability of backup withholding under IRC 3406. See IRM 4.23.8.14, *IRC 3406 — Backup Withholding*.
- (9) The preparation of the penalty case file will follow the procedures outlined in IRM 20.1.7, *Penalty Handbook - Information Return Penalties*.
- (10) Close the penalty case concurrently with the related employment, if possible. The penalty case (agreed or unagreed, paid or unpaid) should be closed using Disposal Code (DC) “12” and updated to Status Code “51”. Form 3198 or RCCMS 3198-A should reflect DC “12”.
- (11) **Miscellaneous Penalty Time:** The time spent reviewing books and records to determine if taxpayers are in compliance with various filing requirements should be charged to the key case. Once it is determined that miscellaneous penalties should be applied, the time spent from that time forward should be applied to the activity code for miscellaneous penalties.

4.23.8.12.1  
(04-17-2024)  
**Information Return  
Penalty — Case File  
Assembly**

- (1) The examiner must complete the following actions:
  - a. Check the “Other” block and add “Assess Civil Penalty as Indicated on Form 8278 & Form 3645” on Form 3198 and RCCMS 3198-A.
  - b. Ensure all forms, letters, documents, supporting workpapers, or other transmittals are uploaded to the appropriate issue SAIN in IMS and named using standard naming conventions. See IRM 4.23.4.5.5, *File Naming Convention*.
- (2) The examiner must confirm that Form 4318-ET or the penalty lead sheet:
  - Documents the actions completed.
  - Includes an explanation of why the taxpayer did not file the forms in a timely manner. Any defense by the taxpayer should be in writing and signed under penalties of perjury.
  - Explains whether the failure was due to reasonable cause.
- (3) For secured paper Forms 1096/1099, Forms W-2/W-3 or Forms W-2c/W-3c the examiner will:
  - a. Upload copies of the forms including the transmittals to the appropriate issue SAIN in IMS and name the documents using standard naming conventions.

- b. Send the original paper Form 1096 and Forms 1099 to the appropriate campus (as indicated in IRM 20.1.7.5.1, *Field Examination Delinquent Information Return Procedures*) and original paper Forms W-2/W-3 and Forms W-2c/W-3c to the SSA according to IRM 4.23.8.11, *Delinquent Form W-2/W-2c*.
- c. Include transcripts or a copy of the tax return(s) under audit for the year(s) of the delinquent information returns in the case file. Generally, these will be Form 941.
- d. Prepare Form 5346 for recipients of Form W-2/W- 2c and/or Form 1099 that appear to have high income tax potential for possible income tax under-reporting. Email the Form 5346 with Form 3210 to ET-WSD at **\*SBSE ET WSD Referrals** (sbse.et.wsd.referral@irs.gov). A copy of Form 5346 will be retained with the workpapers in the penalty case file.

4.23.8.12.2  
(04-17-2024)  
**Information Return  
Penalty — Paper Case  
File Assembly**

- (1) In addition to the instructions found in IRM 4.23.8.12.1, *Information Return Penalty Case File Assembly*, and IRM 20.1.7, *Penalty Handbook – Information Return Penalties*, the following actions must be completed for paper case files.
- (2) The examiner will staple Form 3198 or RCCMS 3198-A to the front of the folder.
- (3) The examiner will include the following in the inside of the folder:
  - Form 8278 (for internal use only)
  - Form 3645
  - Form 4318–ET or penalty lead sheet and supporting workpapers

4.23.8.13  
(04-17-2024)  
**Reporting and  
Withholding Tax on  
Certain Gambling  
Winnings**

- (1) The payor of gambling winnings from such activities must report winnings of \$600 or more to the IRS by filing Form W-2G, *Certain Gambling Winnings*. The payor of winnings from a bingo or slot machine win must report winnings of \$1,200 or more. For keno, the reportable amount is \$1,500 or more.  
  
**Note:** See “General Instructions for Certain Information Returns” for information on filing Forms W-2G.
- (2) Payors of certain types of gambling winnings must withhold income tax on proceeds that are over \$5,000. IRC 3402(q) was amended to reduce the regular gambling withholding rates to equal the third lowest rate of tax applicable to single filers as defined in IRC 1(c).
- (3) Winnings from the following types of activities are subject to withholding:
  - a. State-conducted lotteries when the proceeds are over \$5,000,
  - b. Sweepstakes, wagering pool, or lottery other than “a” above, when the proceeds are more than \$5,000,
  - c. Poker tournament winnings of more than \$5,000. See Rev. Proc. 2007-57, 2007-2 C.B. 547, and
  - d. Other wagering transactions, such as pari-mutuel pool for horse races, dog races, and jai alai when the proceeds exceed \$5,000 and are at least 300 times the amount wagered.

**Note:** No income tax withholding is required on winnings from bingo, keno, or slot machines. However, backup withholding may apply.

- (4) Back-up withholding is required if the winner of reportable amounts does not furnish a Taxpayer Identification Number (TIN) to the payor. This includes reportable amounts of winnings from bingo, keno, or slot machines.
- (5) When examining the income tax return of a taxpayer engaged in the business of gambling, the retained copies of the employment tax returns should be requested (including retained copies of Form W-2G) and inspected. Based on this inspection and all other available information, a decision must be made whether the employment tax returns (including the withholding on gambling winnings requirement) warrant an examination.
- (6) Where an employment tax examination is warranted, consideration should be given to using a computer assisted examination technique to screen the large volume of transactions for proper withholding and winner identification. The examiner should consider requesting the assistance of a Computer Audit Specialist.
- (7) All references to employment tax procedures for the withholding of income tax on wages will apply equally to the withholding of tax on certain gambling winnings.
- (8) The report writing instructions for examinations of income tax withholding for Form 945 are contained in IRM 4.23.10, *Report Writing Guide for Employment Tax Examinations*. Additional information can be found in the instructions for Form 1098, Form 5498, Form W-2G, and in Instructions for Forms 1099-MISC and 1099-NEC.

4.23.8.14  
(04-17-2024)  
**IRC 3406 — Backup  
Withholding**

- (1) IRC 3406 requires payors to withhold income tax on reportable payments of interest, dividends, and other payments under certain conditions. IRC 3406(a) also provides for backup withholding on certain reportable payments, if:
  - a. The payee fails to furnish a Taxpayer Identification Number (TIN) to the payor in the manner required (IRC 3406(a)(1)(A)),
  - b. The Secretary notifies the payor that the TIN furnished by the payee is incorrect (IRC 3406(a)(1)(B)),
  - c. There has been a notified payee under-reporting described in IRC 3406(c) (IRC 3406(a)(1)(C)), or
  - d. There has been a payee certification failure described in IRC 3406(d) (IRC 3406(a)(1)(D)).

**Note:** Generally, an employment tax examiner will encounter backup withholding issues when either (a) or (b) occurs.

**Note:** A reportable payment means any reportable interest or dividend payment and any other reportable payment (IRC 3406(b)(1)).

- (2) The withholding rate for backup withholding under IRC 3406(a)(1) effective January 1, 2018, is 24 percent.
- (3) Under IRC 3406(b)(1)(A), “reportable interest or dividend payment” means any payment which is required to be shown on a return required under:
  - IRC 6042(a) (dividend payments),
  - IRC 6044 (patronage dividend, but only to the extent such payment is in money), and
  - IRC 6049(a) (interest payments).

- (4) IRC 3406(b)(3) defines “other reportable payments” as any payment of a kind, and to a payee, required to be shown on a return required under:
- IRC 6041(a) (relating to certain information at source payments),
  - IRC 6041A (payments for remuneration of services and direct sales),
  - IRC 6045 (returns of brokers),
  - IRC 6050A (payments to certain fishing boat operators),
  - IRC 6050N (royalty payments), and
  - IRC 6050W (relating to returns for payments made in settlement of payment card transactions).

**Note:** Backup withholding can apply to most kinds of payments that are reported on Forms 1099-MISC and 1099-NEC.

- (5) Backup withholding is reported by the taxpayer on the annual Form 945, *Annual Return of Withheld Federal Income Tax*. The examiner will compute backup withholding tax on an annual basis whether the payments are sporadic over the year or by a single lump sum.
- (6) Payors will be held liable for the payment of any backup withholding required to be deducted and withheld under IRC 3406 per IRC 3403.
- (7) Backup withholding adjustments are subject to IRC 6672.
- (8) Backup withholding is treated as withholding on wages per IRC 3406(h)(10).
- (9) Foreign payees are subject to backup withholding, not nonresident alien withholding, when their status as a foreign person or a U.S. person cannot be determined. The presumption rules under IRC Chapters 3 and 61 require the payer to treat the payee as a non-exempt U.S. person, or, when a participating Foreign Financial Institution (FFI) has made an election to withhold under IRC 3406 instead of withholding under Chapter 4 for certain payments to recalcitrant account holders. For further information refer to the Treas. Reg. 1.1471-4(b) and 1.1474-1(d)(4)(i)(B).

## 4.23.8.14.1 (04-17-2024) Overview of Backup Withholding Notices

- (1) When taxpayers file Forms 1099, the IRS reviews them for:
- Missing TINs
  - Obviously incorrect TINs
  - Mismatched names and TINs
  - Unassigned TINs
- (2) If there are errors, the IRS will notify the payor of these errors by sending notification CP2100. See Rev. Proc. 93-37, 1993-2 C.B. 477. The CP2100 notifies a payor that they may be responsible for backup withholding, and is accompanied by a listing of missing, incorrect, and/or not currently issued payee TINs.
- Small filer: Paper CP2100A Notice, less than 50 error documents
  - Mid-size filer: Paper CP2100 Notice, 50 to 249 error documents
  - Large filer: CD or DVD data file CP2100, over 250 error documents

**Reminder:** Under IRC 3406(a)(1)(A), the payor must backup withhold during the period during which the TIN has not been furnished in the manner required, regardless of whether the payor receives and complies with a CP2100 or CP2100A notice. For more information refer to PMTA 2023-03 (<https://www.irs.gov/pub/iranoa/pmta-2023-03.pdf>).

- (3) The CP2100 includes instructions to the payor to provide a “B” Notice to each payee whose Name/TIN combination and account number in the payor’s records matches the combination that IRS identified as incorrect.

**Note:** If an account does not match, this could be the result of a recent update to SSA records, an error in the information the payor submitted, or an IRS processing error. If this type of error occurred, the payor should correct or update its records, if necessary. No “B” Notice is required.

- (4) The “B” Notice informs the payee that the Name/TIN combination furnished to the payor does not match IRS or SSA records and describes the steps the payee must take to stop or prevent backup withholding. If this is the only notification of a Name/TIN mismatch received by the payor with respect to the account during the past three years, the “B” Notice, referred to as a “first B Notice,” instructs the payee to provide a signed Form W-9, *Request for Taxpayer Identification Number and Certification*, (or acceptable substitution) to the payor to stop or prevent backup withholding.
- (5) The payee should return the Form W-9 (or acceptable substitution) within 15 business days, or within 30 business days of the date of the CP2100 Notice. Once the Form W-9 (or acceptable substitution) is received, the payor should compare and update his records, if necessary, and backup withholding is not required.
- (6) If the payee does not provide the Form W-9 (or acceptable substitution) within 30 business days, the payor must begin backup withholding by the 30th business day after the date of the CP2100 Notice.

**Note:** The examiner’s backup withholding adjustment will begin on the 30th business day after the date of the CP2100 Notice.

- (7) If the payor receives a second notice with respect to an account within three years from the date of the first CP2100 Notice with respect to that account, Treas. Reg. 31.3406(d)-5(g) requires the payor to send the payee another “B” Notice, referred to as a “second B Notice.” In response to a “second B Notice,” a copy of a social security card will serve as validation from the SSA of a name and SSN combination. Letter 147-C, *EIN Previously Assigned*, issued by the IRS, serves as validation for a Business Master File (BMF) taxpayer as validation of the name and TIN. Under Treas. Reg. 31.3406(d)-5(g)(1)(i), a TIN certified on a Form W-9 is not sufficient to stop or prevent backup withholding for a second notice.
- (8) Payors may rely upon a social security card as being correct if:
- The name and SSN combination appearing on the card differ from the name and SSN combination appearing on the “second B Notice,” or
  - The social security card is dated no earlier than six months prior to the date of the “second B Notice.”
- (9) If a payee does not have a social security card, a new or replacement card must be obtained from the SSA. See Rev. Proc. 2014-43, 2014-32 I.R.B. 273.
- (10) For additional information on notice procedures, see:

- Pub 1281, *Backup Withholding on Missing and Incorrect Name/TINs (including Instructions for Reading Tape cartridges and CD/DVD Formats)*, and
- Pub 1586, *Reasonable Cause Regulations and Requirements for Missing and Incorrect Name/TINs (including instructions for reading CD/DVDs and Magnetic Media)*.

4.23.8.14.2  
(04-17-2024)

#### Procedures for Backup Withholding Examinations

- (1) A backup withholding examination consists of the determination of a taxpayer's compliance with the CP2100 process and an analysis of whether information returns were properly filed and completed. Although the failure to file Forms 1099 does not trigger backup withholding, a payor who did not file required Forms 1099 often did not secure the payees' TINs. Failure to secure payees' TINs subject the payor to backup withholding.
- (2) Backup withholding examinations require an in-depth review of a taxpayer's accounts payable and vendor master files to determine whether the payor solicited the payees TIN and, if so, the date(s) that the payor first solicited and received the payee's TIN. These dates determine the beginning date when backup withholding is required.
- (3) In addition to the analysis of accounts and disbursements to uncover substantial payments made to individuals and entities for which no Forms 1099 were issued, additional potential issues exist where the TIN is either incorrect, (that is blank or less than nine digits) or the TIN does not match the name of the payee. This may be identified through the backup withholding notice process. See IRM 4.23.8.14.1, *Overview of Backup Withholding Notices*.
- (4) The examiner should request a payer master file transcript (CC PMFOL) for a summary of the payor's information returns by year, type, and dollar amount. A PMFOLB shows the number of Forms 1099 filed with missing, unassigned, and mismatched TINs as well as the years that payor received a CP2100 Notice.
- (5) Before determining whether a payor is subject to backup withholding, examiners must first consider whether a potential worker classification issue exists with regard to the payees. If the payees are determined to be employees, backup withholding is not applicable even if the payor would have been subject to backup withholding based on failing to secure the payees' TINs. Failure to consider the worker classification issue first may provide the payor with a prior audit safe haven under section 530 for subsequent year.

**Reminder:** The non-filing or late filing of information returns eliminates the section 530 safe haven for that year. See IRM 4.23.5.3.3, *Establishing Section 530 Relief*.

**Reminder:** If a worker is later determined to not be an employee (for example, in an Appeals determination), backup withholding should be considered as an alternate position in a worker classification examination.

- (6) After the examiner has determined the payor has received a CP2100 Notice based on review of the PMFOLB transcript, the examiner may request a recreate of the CP2100 Notice. For more information on requesting a recreate of the CP 2100 Notice see IRM 4.23.8.14.2.1, *Examiners Requesting Recreates of CP2100 and CP2100A*.

- (7) All references to employment tax procedures for the withholding of income tax on wages, except for special rules related to IRC 3509 rates or CSP, apply to backup withholding. Consequently, payors are liable for the payment of any backup withholding required to be deducted and withheld under IRC 3406.
- (8) The report writing instructions for examinations of backup withholding are contained in IRM 4.23.10.10.9.1, *Form 4668-B* and IRM 4.23.10-4, *Form 4668-B, Report of Examination of Withheld Federal Income Tax*:
  - a. Use Form 4668-B
  - b. The applicable tax rate is 24 percent effective 2018.
  - c. If the examination involves other employment taxes in addition to backup withholding, a Form 4668 will be prepared to reflect the other results of the examination.
- (9) If notices or billings are generated from the campus regarding backup withholding compliance measures, campus' review of any records regarding these actions does not constitute the examination of any federal tax return.
- (10) The backup withholding assessment under IRC 3406 is subject to the abatement provisions of IRC 3402(d). Examiners are authorized to accept and consider any Form 4669 submitted before the case is closed from the group. A separate form must be obtained from each payee for each year and is signed under the penalties of perjury. These completed forms must have every line item completed (Part 1 by the payor and Part 2 by the payee), and be accompanied by Form 4670 prepared by the payor. If any information is omitted from a Form 4669, it must be returned to the payor for correction, as it is the responsibility of the payor to obtain properly completed forms from payees. Follow IRM 4.23.8.4.3, *Procedures for Relief Under IRC 3402(d) and/or IRC 3102(f)(3) in Examination*.
- (11) If the examination is closed but the tax has not been paid, advise the taxpayer to submit the completed Forms 4669 and Form 4670 to the campus where the Form 945 is filed, along with a copy of the Form 4668-B from the examination, for consideration of the IRC 3402(d) abatement.
- (12) If the examination is closed and the tax paid, advise the taxpayer to submit a Form 945-X, *Adjusted ANNUAL Return of Withheld Federal Income Tax or Claim for Refund*, attaching the completed Forms 4669 and Form 4670, along with a copy of the Form 4668-B from the examination, for consideration of the claim under IRC 3402(d).
- (13) Additional information on backup withholding is found in:
  - Treas. Reg. 31.3406
  - Training Course 34103-002, *Technical Basic Employment Tax Training*
  - ITM course 53472, *SBE-SP-ET Backup Withholding*

4.23.8.14.2.1  
(04-17-2024)  
**Examiners Requesting  
Recreates of CP2100  
and CP2100A**

- (1) After the examiner has determined the payor has received a CP2100 Notice based on review of the PMFOLB transcript, the examiner may request a copy of the CP2100 Notice issued from Electronic Products and Services Support, Technical Services Operation (EPSS-TSO) by sending a facsimile transmission (fax) to (877) 477-0572 or email the request to **\*WI TSO Request** (wi.tso.request@irs.gov). Prepare the fax cover sheet for transmittal or the email request:

- “Recreate Notice” in the Subject Line
- “Cc” to the examiner’s group manager using the manager’s e-fax number or email address.

**Note:** Do not include Personal Identifiable Information (PII) in the fax cover sheet or the subject line of the encrypted email.

(2) Attached forms to the fax or within the email will include:

- Taxpayer’s name
- Taxpayer’s TIN
- Tax year(s)
- Examiner’s office mailing address (the response will be mailed to the examiner)
- Copy of Integrated Data Retrieval System (IDRS) command code PMFOLB transcript

**Note:** Examiners should allow four to six weeks to receive a response depending on volume a response may be sent earlier or later. Examiners who order CP2100 notice with 250 or more payees may experience unusually long delays in receiving a response. Examiners should submit their CP2100 requests as early in their examinations as possible.

(3) In any case where a taxpayer received a CP2100 notice with more than 249 payees, EPSS-TSO will provide images of recreated notice to the examiner on an encrypted CD. If the encryption code is not provided in a separate email from EPSS-TSO, Examiners should send an email to **\*WI TSO Request** to request the encryption key. For more information refer to IRM 3.42.9.14.4(6), Request to Recreate Notices CP2100, CP2100A, and 972CG.

**Note:** The encrypted CD that is sent to examiners is labeled with instructions to call 1-866-455-7438 to obtain the encryption key. This telephone number is for **taxpayer use only**. Examiners will not be able to obtain the encryption key by calling the telephone number.

(4) If a TSO employee declines to provide the encryption key after contacting **\*WI TSO Request**, send the request to **\*SBSE E BWH POLICY MB** (sbse.e.bwh.policy.mb@irs.gov). SB/SE Employment Tax Policy will contact the EPSS-TSO Information Technology Support analysts to resolve your problem.

**Note:** Examiners should not forward their request to **\*SBSE E BWH POLICY MB** unless they have requested the encryption key from **\*WI TSO Request**, and that request has been denied.

## 4.23.8.15 (04-17-2024) Form 944 Examinations and Filing Requirements

- (1) Form 944, *Employer’s ANNUAL Federal Tax Return*, is designed so the smallest employers (those whose annual liability for FICA and FITW is \$1,000 or less) will file and pay these taxes only once a year instead of every quarter.
- (2) For tax years 2006 through 2009, the IRS systemically identified and notified taxpayers who met Form 944 criteria of their new filing requirement change. This change is based upon an expected annual liability of \$1,000 or less. Taxpayers were given an opportunity to “opt out” of the filing requirement change, but those that did not were automatically changed over. Taxpayers must file Form 944 only if they have been notified by the IRS of the filing re-

quirement change. For the tax year 2010 and beyond, the Form 944 program was made voluntary. However, unless taxpayers pro-actively opt out or become ineligible (more than a \$1,000 liability), they will remain in the program until notified by the IRS of a new Form 941 filing requirement.

- (3) Once a Form 944 filing requirement has been assigned, one of the following actions must be taken for a taxpayer to be changed to a Form 941 filer for **subsequent** periods:
- File a timely Form 944 reporting wages that exceed the threshold for Form 944 filers,
  - Opt out of filing Form 944 between January 1 and March 31 of the current year by contacting the IRS with a written request or by phone; or
  - As part of an examination of Form 944, be determined to have wages that exceed the threshold for Form 944 filers.

**Note:** Any one of the above actions will change the taxpayer's filing status for subsequent periods upon proper notification to the taxpayer.

**Caution:** In no situation will an examiner retroactively change the filing requirements.

- (4) When an examiner is assigned a case, they must verify the controls are on the appropriate module. In some situations, taxpayers who have not filed may have been assigned a Form 944 filing requirement because their liability, based on the non-filing, was less than the threshold.
- (5) Examiners must use the appropriate filing requirement for each year when determining what module should be (or has been) controlled. If the examination(s) is incorrectly opened on the ERCS for Form 941 when the actual filing requirement is Form 944, or vice versa, controls must be reopened under the correct filing requirement for the specific tax period. The incorrect controls may be closed using the non-examined Disposal Code "36", No Return Filed. During the examination process, additional tax may be determined which exceeds the threshold criteria for Form 944, however, the assessment must be made under the Form 944 tax period if that is the filing requirement assigned for that year. A filing requirement cannot be changed retroactively for a calendar year at any time.
- (6) When an examiner receives a non-filer case or is expanding audit controls for prior and subsequent tax periods as part of an audit, they **must** verify the filing requirement to ensure controls are requested on the appropriate module. These filing requirements are determined each year and can be different between years. To make the proper determination on the appropriate filing requirement, the examiner will review the cache information on page 2 of the BMFOLE. The filing requirement will be separately determined for each year under examination using the cache indicator. Form 944 filing requirements:

Cache Indicator	Form	MFT
Blank	941	01
1	944	14
2	944	14

**Note:** The “2” indicates that the filing requirement will change to a Form 941 for the following year. A filing requirement cannot be changed retroactively. The examiner must establish controls using the information on the cache.

- (7) The examiner must also take steps to ensure the appropriate statute of limitations date is used for all cases controlled when there is a Form 941 vs. Form 944 filing requirement question. The statute of limitations will begin when a taxpayer files enough information to allow for an assessment to be made. In cases involving a Form 941 vs. Form 944 controversy, the filing of a Form 941 at any time could result in a “deemed” live statute for the Form 944 module (or vice versa). To correctly determine and protect the statute of limitations, the examiner must:
  - a. Research TRDBV command code to determine if the taxpayer attempted to file a return contrary to their filing requirement for the specific year in question. If a return was filed on the wrong form it will be reflected as an un-posted return under this command code.
  - b. Review the un-posted return. If the taxpayer filed a Form 941 when they had a Form 944 filing requirement the examiner will look at the image of the return to determine if it meets the criteria under *Beard v. Commissioner*, 82 T.C. 766, 777 (1984), aff’d per curiam, 793 F.2d 139 (6th Cir. 1986). If all criteria are met, the return is considered a valid return for purposes of the period of limitations on assessment even if the taxpayer filed the return on the incorrect form.
  - c. Review the “Stat-Hist” section on the TRDBV to determine when the return was processed and for which tax period.
  - d. Use the TRDBV “Rec’d Date” to determine when the return was filed.
  - e. Use the earliest TRDBV “Rec’d Date” as the deemed statute on the “non-filed” period.

**Example:** 1) Taxpayer A had a Form 944 filing requirement for the 2023 tax year. The taxpayer failed to file Form 944 and the case was assigned as a CAWR case to make the assessment. A review of TRDBV reflects that four Forms 941 were filed for 2023 (one for each quarter), but because of the incorrect form, were un-posted. The examiner prints the Forms 941 and reconciles them to the BMFOLU wages. The examiner determines that these forms were timely filed throughout 2023 and before April 15, 2024. There is a deemed statute of April 15, 2027, that must be reflected on the 944 audit controls.

**Example:** 2) Same situation as Example 1, except only two Form 941 were filed by the taxpayer during 2023. Even though the wages reflected on the two Forms 941 are less than those reflected on the BMFOLU, there is still a deemed statute of April 15, 2027, because the taxpayer timely filed valid returns that must be used to determine the statute.

**Example:** 3) Taxpayer B had a Form 941 filing requirement for 2023 after having a Form 944 filing requirement from 2020 – 2022. The taxpayer incorrectly filed a Form 944 for 2023 rather than the required Forms 941. The Form 944 reflected on TRDBV shows the return to be timely filed. There is a deemed statute of April 15, 2027.

**Example:** 4) Taxpayer C had a Form 944 filing requirement for 2023. They submit a Form 941 for the first quarter of 2023, but there is no information on the return except for the name, address and TIN. This is clearly reflected on TRDBV. In this situation, the return submitted does not meet the “Beard” test and will not be accepted as a valid return for the purposes of the period of limitations on assessment. The valid statute will be 4/EE/27.

**Example:** 5) Taxpayer D had a Form 944 filing requirement for 2023. Research of TRDBV shows un-posted but valid Forms 941 filed for two of the quarters. However, these returns were not submitted until January 12, 2025. The deemed statute to be used for the audit controls on the Form 944 is January 12, 2028.

- (8) To establish proper statute controls the examiner must initially use a valid “EE” statute date when establishing the SFR controls because there is no evidence on the module of a return being filed (no TC150). Once established, the examiner will follow local procedures to update the statute to the appropriate “deemed” date.
- (9) Examiners will access the TRDBV returns and use them as a starting point to determine the correct wages.
- (10) If the wages reported on the TRDBV match the BMFOLU wages **and** it is determined that no other issues are present or will be developed due to limited scope, the examiner may run a report to match the amounts on the un-posted returns and close the case using DC “08” without issuing a report to the taxpayer. The reasons for processing the case in this manner must be fully documented in the case file.
- (11) If the wages on the TRDBV do not match the amounts reflected on the BMFOLU and there are other issues present, the examiner can assess the taxes reflected on the TRDBV return(s) using the partial assessment procedures before developing other issues. Examiners will follow normal audit procedures to fully develop all employment tax issues.
- (12) Examination assessments exceeding the threshold may not systemically change the taxpayer back to a Form 941 filer before the upcoming year. If it is expected the taxpayer’s liability will exceed the \$1,000 threshold for the current or future periods, the examiner should change the filing requirements for future filings and notify the taxpayer. A filing requirement change may be made for the current year if done prior to April 1st. Changes after April 1 will apply to the following year and the taxpayer should be instructed to file a Form 944 for the current year.
- (13) To process the filing requirement change for the current year, follow these steps:
  - a. Form 2363, *Master File Entity Change*, should be completed (check item 016, “Change misc. codes”). The appropriate filing requirement code from Document 6209 should be annotated under the correct tax return number, that is 944: MFT 14. In SB/SE, Form 2363 should be faxed to the CCP at the number provided at <https://irs.gov/sharepoint.com/sites/>

*ETD-KMT-KB051/SitePages/SBSECampusExamProcedures/  
ExamCentralizedCaseProcessing(CCP)/CCPExamEFaxNumbers.aspx.*

**Note:** All TE/GE Form 2363 requests shall be sent to the TE/GE FAST Team email at **tege.fast@irs.gov**.

- b. Once the filing requirement change has posted, identify tax deposits/credits already posted on the current tax module which should be transferred to the correct period(s). Form 3870, *Request for Adjustment*, should be prepared reflecting the tax deposits/credits to be transferred and faxed to CCP. (EO is to follow local procedures for processing Form 3870.)
- c. Hand-deliver or mail (certified) notification of filing requirement change, to be received by the taxpayer and/or POA prior to April 1st of the current year. Letter 3007, *Employment Return Filing Requirements/Instructions Form 941*, is used for this purpose.
- d. Document the case file with all actions taken.

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## Exhibit 4.23.8-1 (04-17-2024)

### Forms W-2, 1099-MISC, and 1099-NEC Due Dates and Statute Dates

Form	Title	Paper Transmittal	Due Date (Paper)	Due Date (E-File)	IRC 6721 Unfiled Statute	IRC 6722 Unfiled Statute
Form 1099-MISC (with NEC) (TY2016 thru TY2019)	Miscellaneous Income	Form 1096	Jan 31	Jan 31	1/EE/YYYY	1/EE/YYYY
Form 1099-MISC (without NEC)	Miscellaneous Information	Form 1096	Feb 28	Mar 31	2/EE/YYYY	3/EE/YYYY
Form 1099-NEC (starting TY2020)	Non-employee Compensation	Form 1096	Jan 31	Jan 31	1/EE/YYYY	1/EE/YYYY
Form W-2	Wage and Tax Statement	Form W-3	Jan 31 (starting TY2016)	Jan 31 (starting TY2016)	1/EE/YYYY	1/EE/YYYY

**Note:** If the due date falls on a Saturday, Sunday, or legal holiday, a return submitted on the next succeeding day which is not a Saturday, Sunday, or legal holiday will be considered timely filed. For more information refer to IRC 7503 and Treas. Reg. 301.7503-1.

**Note:** Forms 1099-MISC (only for amounts reported in box 8, Substitute Payments in Lieu of Dividends or Interest and box 10, Gross Proceeds to an Attorney) must be furnished on or before February 15th of the year following the year for which the information return is required.

**Note:** For the due dates for additional forms refer to IRM 20.1.7-3, *Forms*.

**Exhibit 4.23.8-2 (02-01-2003)****IRC Provisions Restricting and Prohibiting Interest — Employment Taxes**

<b>Employment Tax Code Sections</b>	<b>Subject</b>	<b>Restricted Interest IRC for Underpayments</b>	<b>Restricted Interest IRC for Overpayment</b>
IRC 3101, IRC 3111	FICA	IRC 6205(a)	IRC 6413(a)
IRC 3402	Income Tax Collected at Source	IRC 6205(a)	IRC 6413(a)
IRC 3121(l)	Foreign Subs Domestic Corp.	Blank	IRC 3121(l)(5)
IRC 3302(a), IRC 3302(b)	FUTA Tax Credit	Blank	IRC 6413(d)

**Exhibit 4.23.8-3 (04-17-2024)**
**Employment Tax Rate Chart under IRC 3509**
**IRC 3509(a) Rates**

Year	Social Security Rate	Social Security Wage Limit	Medicare Rate	AdMT Rate	FITW
2018	7.44%	\$128,400	1.74%	0.18%	1.5%
2019	7.44%	\$132,900	1.74%	0.18%	1.5%
2020	7.44%	\$137,700	1.74%	0.18%	1.5%
2021	7.44%	\$142,800	1.74%	0.18%	1.5%
2022	7.44%	\$147,000	1.74%	0.18%	1.5%
2023	7.44%	\$160,200	1.74%	0.18%	1.5%
2024	7.44%	\$168,600	1.74%	0.18%	1.5%

**IRC 3509(b) Rates**

Year	Social Security Rate	Social Security Wage Limit	Medicare Rate	AdMT Rate	FITW
2018	8.68%	\$128,400	2.03%	0.36%	3%
2019	8.68%	\$132,900	2.03%	0.36%	3%
2020	8.68%	\$137,700	2.03%	0.36%	3%
2021	8.68%	\$142,800	2.03%	0.36%	3%
2022	8.68%	\$147,000	2.03%	0.36%	3%
2023	8.68%	\$160,200	2.03%	0.36%	3%
2024	8.68%	\$168,600	2.03%	0.36%	3%

**Note:** Refer to Publication 15, *Circular E, Employer's Tax Guide*, for subsequent year rates and wage limitations.

