

**INTERNAL REVENUE SERVICE**  
**NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM**

September 30, 2003

Number: **200407014**  
Release Date: 2/13/04  
Index (UIL) No.: 3121.04-01  
CASE-MIS No.: TAM-110334-03, CC:TEGE:EOEG:ET1

Director, Field Operations, SBSE

Taxpayer's Name:  
Taxpayer's Address:  
Taxpayer's Identification No  
Years Involved:  
Date of Conference:

**LEGEND:**

Firm =  
Worker =  
Agency A =  
Agency B =

**ISSUE(S):**

Whether the worker under the circumstances described below, is an employee of the firm for Federal employment tax purposes.

**CONCLUSION(S):**

The worker is an employee of the Firm for Federal employment tax purposes.

**FACTS:**

The Firm submitted a Form SS-8, Determination of Workers Status for Purposes of Federal Employment Taxes and Income Tax Withholding, requesting a determination from the Service that the Worker is not an employee for services performed from the middle of 2001 to the present. The Worker also submitted a Form SS-8 with information consistent with the information provided in the Firm's Form SS-8. Prior to this time, the Worker was treated as an employee for four years. As an employee, the Worker was paid an hourly wage and subject to the Firm's control regarding hours worked and trips

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made. According to the Firm, the Worker became the sole employee of the Firm operating under an independent licensee agreement. The Firm plans to engage other employees under the same agreement if it receives a favorable ruling.

The Firm provides transportation to wheelchair passengers. Most of the wheelchair passengers transported by the Firm, travel pursuant to contracts between the Firm and two governmental agencies, Agency A and Agency B. The Firm and the agencies agree on the fares to be charged for trips. The Worker is required to adhere to these prices for trips dispatched through the Firm. Under these contracts, both agencies pay for transportation of wheelchair individuals certified as eligible by the agencies. Trips that are paid by an agency must be submitted to the Firm to verify eligibility. Passenger request for transportation made directly to the Worker are not subject to approval by the Firm. According to the Firm, the Firm and/or its independent contractor driver, the Worker, are the exclusive providers of such transportation.

These agencies imposed several requirements on the Firm, including that drivers providing services are trained in cardiopulmonary resuscitation, first-aid and sensitivity in helping people using wheelchairs. Agency B also requires that 50 percent of the drivers who transport wheelchair passengers traveling pursuant to its contract with the Firm be employees of the Firm. The Firm ordinarily provides this training to drivers when they are hired as employees, but if a driver can demonstrate that the driver has already been trained elsewhere, no training is required.

The Firm also trains the drivers to safely operate specialty equipment, such as a wheelchair lift (used to lift a wheelchair person into a van), and to safely secure the wheelchair in the van to prevent the wheelchair from moving while the van is in motion. Both the training required by Agency A and the additional training by the Firm are conducted once, before the driver begins transporting wheelchair passengers.

Under the independent licensee agreement, the Firm leases a van equipped to transport wheelchair passengers to the Worker. The Worker is the driver of the van. The Worker pays a fixed daily or weekly fee to the Firm, in exchange for which the Worker acquires the use of the van, painted with the Firm's colors, trademark, and logo, and equipped with a two-way radio or computer dispatch equipment; the right to use the van as a taxi (under the Firm's operating authority); and access to the Firm's scheduling, dispatch, cashiering, and collection services. As the owner of the vehicle, the Firm purchases insurance and pays for all routine maintenance and repairs. The Worker is entitled to keep all fares and tips received from the wheelchair passengers, whether paid directly by the passenger, or collected by the Firm from the agencies and credited or paid (if in excess of the Worker's lease fee) to the Worker. The Worker pays for the operating expenses of the vehicle, including gasoline, tolls, tickets, and other incidental expenses, and for up to \$2,500 for repairs required due to the

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Worker's own negligence. The Worker also is responsible for purchasing (and replacing as needed) maps, belts to secure the passenger in the wheelchair, business cards (if desired), and uniforms (also voluntary).

The Firm prepares "routes" for the Worker. Each route is a series of trips prescheduled by wheelchair passengers, and "packaged" by the Firm to minimize the amount of time and distance during which the passenger is not being transported. This benefits the Worker by maximizing the time and distance the Worker is transporting passengers, and thus earning fares and tips and minimizing the Worker's "dead" time and distance. The Worker may select a route (on a "first-come, first-served" basis), begin work when necessary in order to pick up the first passenger and end work when the last passenger is delivered to his or her designation. When there are sufficient time/distance gaps between trips, perhaps because a schedule passenger cancels, or before the packaged route begins or after it ends, the Worker may (but it is not required to) supplement the route, either with a passenger who has contacted the Worker directly, or with another trip dispatched through the Firm. The Worker is not required to supplement gaps in the packaged route schedule, and any supplemental trip may not adversely affect the next prescheduled trip on the route. The Worker keeps fares and tips from the supplemental trips as well as from the trips packaged by the Firm. Alternatively, the Worker may reject any or all routes, and simply request the opportunity to accept individual trips from the Firm's dispatch service. The Worker may also arrange his own trips without using the Firm's dispatch service. In this case the Worker may accept cash, bill a passenger directly, or arrange for the Firm to bill a passenger. The Worker is free to advertise and to obtain supplemental business from passengers who contact him directly.

The Worker was interviewed by the Service and indicated that either he accept the lease arrangement offered by the Firm or lose his job. According to Worker, this lease arrangement was a way the Firm escaped having to pay his compensation and taxes. When asked what types of business decisions the Worker made with regard to the services he provided, the Worker answered none. The Worker also stated that schedules, routes and fees were not within his control. The Worker stated that he did not advertise because he was scheduled for 10 hours per day. The Worker never solicited customers and he had no business cards. While the van went home with the Worker at night and he could have used it during his off hours, he did not because he worked full days. The Worker did not provide a substitute driver because the driver had to be someone who had the same training the Worker had. When the Worker could not drive, the Firm would give the trips to another Firm driver. When asked what the differences were between lease arrangement and the employment arrangement, the Worker answered that nothing changes except how he was paid. There were set trips scheduled through the Firm every day and the Firm furnished everything. The Worker further stated that prospective customers had to call the Firm 24 hours in advance.

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When the Firm was interviewed, they indicated that the lease arrangement was prompted by the Firm wanting to shift the economic arrangement to the Worker who will collect fees and tips and pay a flat rate for the lease.

The Firm believes that the Worker is now an independent contractor because the details and means by which the Worker performs services for the Firm are not subject to the Firm's control or direction. According to the Firm, the Worker is an independent contractor because he pays a flat fee to the Firm to lease the van used in the Firm's dispatch service. The Firm believes that it has no significant incentive to control the details and means by which the Worker provides services. The Firm believes that the services of this Worker are governed by Situation Two in Rev. Rul. 71-572, 1971-2 C.B. 347.

#### LAW AND ANALYSIS:

Section 3121(d)(2) of the Internal Revenue Code (Code) defines "employee" as any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee.

The question of whether an individual is an employee under the common law rules or an independent contractor is one of fact to be determined upon consideration of the facts and the application of the law and regulations in a particular case. Guides for determining the existence of that status are found in three substantially similar sections of the Employment Tax Regulations, namely sections 31.3121(d)-1, 31.3306(i)-1, and 31.3401(c)-1, relating the FICA, the FUTA, and federal income tax withholding respectively.

Section 31.3121(d)-1(c)(2) of the regulations provides that generally, the relationship of employer and employee exists when the person for whom the services are performed has the right to control and direct the individual who performs the services not only as to the result to be accomplished by the work, but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but as to how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he or she has the right to do so. In general, if an individual is subject to the control or direction of another merely as to the result to be accomplished and not as to the means and methods for accomplishing the result, he or she is an independent contractor.

Section 31.3121(d)-1(a)(3) of the regulations provides that if the relationship of an employer and employee exists, the designation or description of the parties as anything other than that of employer and employee is immaterial. Thus, if an employer-employee

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relationship exists, the designation of the employee as partner, coadventurer, agent, or independent contractor must be disregarded.

In determining whether an individual is an employee or an independent contractor under the common law, all evidence of both control and lack of control or autonomy must be considered. In doing so, one must examine the relationship of the worker and the business. Relevant facts generally fall into three categories: behavioral controls, financial controls, and the relationship of the parties.

Behavioral controls are evidenced by facts which illustrate whether the service recipient has a right to direct or control how the worker performs the specific tasks for which he or she is hired. Facts which illustrate whether there is a right to control how a worker performs a task include the provision of training or instruction.

Financial controls are evidenced by facts which illustrate whether the service recipient has a right to direct or control the financial aspects of the worker's activities. These include significant investment, unreimbursed expenses, making services available to the relevant market, the method of payment, and the opportunity for profit or loss.

The relationship of the parties is generally evidenced by examining the parties' agreements and actions with respect to each other, paying close attention to those facts which show not only how they perceive their own relationship but also how they represent their relationship to others. Facts which illustrate how the parties perceive their relationship include the intent of the parties, as expressed in written contracts; the provision of, or lack of employee benefits; the right of the parties to terminate the relationship; the permanency of the relationship; and whether the services performed are part of the service recipient's regular business activities.

As is the case in almost all worker classification cases, some facts point to an employment relationship while other facts indicate independent contractor status. The determination of the worker's status, therefore, rests on the weight given to the factors under the common law, keeping in mind that no one factor is determinative of a worker's status.

Courts often look at the intent of the parties. This is most often embodied in their contractual relationship. Thus, a written agreement describing the worker as an independent contractor is viewed as evidence of the parties' intent that a worker is an independent contractor. A contractual designation, in and of itself, is not sufficient evidence for determining worker status. The facts and circumstances under which a worker performs services are determinative of the worker's status. Treas. Reg. section 31.3121(d)-1(a)(3) provides that the designation or description of the parties is

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immaterial. This means that the substance of the relationship, not the label, governs the worker's status.

It is the substance rather than the form of the transaction that governs tax treatment. O'hare v. Commissioner, 641 F.2d 83 (2d Cir. 1981); Garlock Inc. v Commissioner, 58 T.C. 423, 434 (1972), aff'd, 489 F.2d 197 (2d Cir. 1973), cert. denied, 417 U.S. 911 (1974); Commissioner v. Court Holding Co., 324 U.S. 331, 334 (1945); Gregory v. Helvering, 293 U.S. 465 (1935). If the form of the transaction is at variance from the substance of the transaction and lacks economic reality, the form will be disregarded and effect will be given to the substance. Commissioner v. Court Holding Co., 324 U.S. 311, 1945 C.B. 58; Frank Lyon Co. v. United States, 435 U.S. 561, 573 (1978).

We have carefully considered the information submitted in this case and the facts discussed above, and conclude that in substance, the Worker is an employee of the Firm and the services of this Worker is not governed by Situation Two in Rev. Rul. 71-572, 1971-2 C.B. 347.

CAVEAT(S):

A copy of this technical advice memorandum is to be given to the taxpayer(s). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.