Internal Revenue Service
United States Department of the Treasury

Government Workers: Employees or Independent Contractors?

The question of whether someone who works for you is an employee or an independent contractor has important tax consequences. If you have employees, you have liability to pay and withhold Federal income tax, social security and Medicare taxes, and Federal unemployment tax, report wages and issue statements to employees. For independent contractors, generally no withholding is required.

For most workers, whether in the private or public sector, the same common-law tests are applied to determine whether someone is an employee or an independent contractor. However, there are special rules that apply to determine whether certain groups of government workers are employees, and additional rules that create exceptions to general rules for income tax, social security and Medicare tax withholding.

In general, someone who performs services for you is your employee if you can control what will be done and how it will be done. To make this determination requires an analysis of all the relevant facts. The courts have considered many facts in deciding whether a worker is an independent contractor or an employee. These facts fall into three main categories:

- Behavioral control,
- Financial control, and
- Type of relationship

These facts and relevant examples are discussed in detail in Publication 15-A, and at the Independent Contractor or Employee? page. There are specific laws, however, that apply to certain categories of government workers. Some government workers may be deemed to be employees by law, and others may be considered employees but are subject to special legal provisions for withholding income, social security and Medicare taxes. Some of the important special rules are discussed below.

Workers Covered by a Section 218 Agreement: Some state and local government employees are covered by a voluntary agreement between their state and the Social Security Administration (SSA) to provide social security coverage for workers. If a position is covered by the Section 218 Agreement, any worker who holds that position is an employee and subject to social security and Medicare tax under the terms of the agreement.

The following are some types of workers that are covered by special rules:

Public Officials: Internal Revenue Code section 3401(c) indicates that an “officer, employee, or elected official” of government is an employee for income tax withholding purposes. If this is the case, generally these workers will also be employees for social security and Medicare tax purposes; however, in some special cases the law or a Section 218 Agreement may specify otherwise.

Elected Officials: Elected officials are employees for income tax purposes under the section 3401(c) provision that applies to public officials. They are subject to a degree of control that typically makes them employees under the common law, and are subject to social security and Medicare taxes. Very few elected officials could be considered independent contractors.

Fee-Basis Officials: A fee-basis public official receives and retains remuneration directly from the public. This work is considered self-employment under IRC 1402(c)(2)(E) and these individuals are not employees with respect to this work. An official who receives salary, even if it is called “fees,” is a common-law employee and is subject to social security and Medicare withholding. Fee-basis individuals are subject to self-employment tax.

A Position compensated by salary and fees is considered a fee-basis position if the fees are the principal

source of compensation, unless a state law provides that a position for which any salary is paid is not a fee-basis position. A Section 218 Agreement may provide an exclusion from social security tax for individuals.

Emergency Workers: Individuals hired on a temporary basis in case of fire, storm, snow, earthquake, flood, or other emergency are excluded from social security and Medicare under IRC 3121(b)(7)(F)(iii). This does not include permanent employees who work regularly in response to emergencies; these individuals are subject to social security and Medicare if they are common-law employees.

Election Workers: Election workers are common-law employees; however, under IRC 3121b)(7)(F)(iv) an exception from FICA is provided for election officials and workers who earn less than a specified amount for a calendar year ($1,500 for 2011). This provision applies to employing entities that do not have a Section 218 Agreement. If the employing entity has a Section 218 Agreement, the Agreement determines the treatment of election worker wages for social security tax. It may exclude election workers altogether from social security; it may specify a lower threshold at which social security tax is withheld; or it may provide no exclusion for election workers, in which case social security and Medicare taxes apply from the first dollar paid.

Medical Residents: Medical residents generally meet the tests to be common-law employees and are therefore employees of the hospital where they work. However, under IRC 3121(b)(10), enrolled students who work less than full-time and for whom education, not employment, is the primary purpose of the relationship, may be excepted from FICA. See Revenue Procedure 2005-11.

Section 218 Agreements and all of the above classes of workers are discussed in detail in Publication 963, Federal State Reference Guide.

Issues for Firefighters

Firefighters

This discussion addresses some of the common questions we receive from firefighters and their employing organizations.

Compensation

Generally, tax laws apply to firefighters in the same manner as for other types of workers. It does not matter whether firefighters are termed “volunteers”, are considered employees, or are identified by any other name, if the work they do is subject to the will and control of the payer, under the common-law rules, they are employees for Federal tax purposes. The determination as to whether workers are common-law employees or independent contractors is made applying the same standards used for other workers. See IRS Publication 15, Employer’s Tax Guide, for more information on determining whether a worker is a common-law employee.

Similarly, it does not matter whether they are paid on a “call” basis, monthly, hourly, etc.; or whether the worker is full-time or part-time. These payments are wages that should be reported on Form W-2, subject to withholding for Federal income tax, social security, and Medicare purposes. Employers are responsible for withholding on these wages and filing Form 941.

If a worker is a common-law employee, any amounts received that are not exempt under a special

provision, are reported on Form W-2 as wages. It does not matter what the payments are called.

Income Tax

Generally, all amounts employees received are taxable for Federal income tax purposes. Some fringe benefits are excluded by specific provisions of law. Some common benefits that may qualify to be excluded from include:

- Certain de minimis (minimal) fringe benefits
- Meals provided for the convenience of the employer
- Employee discounts
- Achievement awards
- Health insurance
- Educational benefits

For more information, see IRS Publication 15-B, Employer's Tax Guide to Fringe Benefits.

Reimbursements for expenses may be excludable from wages if they meet the accountable plan rules, discussed below.

Social Security Tax

After July 1, 1991, state and local government employees are generally subject to mandatory social security tax for wages paid unless they either (1) participate in a qualifying public retirement system, or (2) are covered by a voluntary ("Section 218") agreement between their state and the Social Security Administration. The requirements for a qualifying public retirement system are discussed in IRS Publication 963, Federal-State Reference Guide.

Your State Social Security Administrator can tell you whether a Section 218 agreement is in effect for a specific group of workers. See www.ncsssa.org for a list of State Social Security Administrators.

Medicare Tax

With few exceptions, employees (including firefighters) hired after March 31, 1986, are covered by the Medicare tax. Employees hired before that date may be exempt if they have remained in continuous employment since then.

For more information on social security and Medicare coverage rules for government employees, see IRS Publication 963, Federal-State Reference Guide.

Emergency Workers

The Internal Revenue Code provides an exception under IRC 3121(b)(6)(C) from social security and Medicare tax for a worker "serving on a temporary basis in case of fire, storm, snow, earthquake, flood, or other similar emergency." This exception applies only for temporary workers hired in response to an unforeseen emergency. It does not apply to firefighters who work on a recurring, routine or regular basis, even if their work involves situations that may be considered emergencies, including responding to fires.

Internal Revenue Service
United States Department of the Treasury

Expenses and Reimbursements

Firefighters may receive amounts that are designated as expenses for transportation, equipment, clothing, etc. In general, these are treated as taxable wages. However, if the amounts are paid under an ***accountable plan***, they may be excluded from wages and no tax reporting is required. For payments to be considered made under an accountable plan, the employees must:

1. Incur the expenses in the performance of work;
2. Adequately account for the expenses within a reasonable period of time; and
3. Return any amounts in excess of expenses within a reasonable period of time.

Ordinary and necessary expenses firefighters incur in the course of performing their jobs are excludable from income if paid under an accountable plan. A fixed cash amount which does not require documentation of expenses, regardless of its purpose, is treated as ordinary wages. It is subject to income tax, social security and Medicare tax withholding.

For a detailed explanation of the accountable plan rules, see section 5 of Publication 15.

State or Local Tax Benefits

In some cases, volunteer firefighters receive benefits in the form of state or local tax credits or rebates. If these benefits are offered in return for services performed, their value represents income to the worker for Federal tax purposes and should be included in taxable wages.

For More Information

The FSLG website has more information on all these topics. Our FSLG Newsletter includes a directory of local FSLG Specialists throughout the country who can assist you with questions involving the tax responsibilities of government entities.