



# LEGAL ALERT

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February 2009

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## The IRS has taken the “Disregarded” out of “Disregarded Entity” for Employment Tax Purposes

Single member limited liability companies and qualified subchapter S subsidiaries (“Q-Subs”) are generally treated as “disregarded entities” for federal tax purposes. Effective on and after January 1, 2009, an owner of a disregarded entity is required to obtain an Employer Identification Number (EIN) for the entity and pay and report Federal employment taxes and wage payments under the entity’s name and EIN. Prior to January 1, 2009, disregarded entities were permitted to pay and report employment taxes and wage payments using either the entity’s name and EIN or the owner’s name and EIN. This means that if you currently operate through a disregarded entity which does not have its own EIN, you must apply for one and report Federal employment taxes and wage payments under the entity’s name and EIN.

Please note, however, that even though employment taxes must now be reported by the entity, the entity’s owner continues to be responsible for properly withholding and paying Federal employee side employment taxes and also for correctly classifying workers as employees or independent contractors. A failure to correctly withhold, pay, or classify workers may result in liability for the entity, and personal liability for the owner and certain other officers and employees of the entity. The Treasury Inspector General for Tax Administration (TIGTA) recently issued an audit report that estimated a tax gap well exceeding \$1.6 billion resulting from the misclassification of workers as independent contractors versus employees. TIGTA’s audit report has brought renewed



attention to the issue of worker classification and the IRS plans to coordinate a study in fiscal year 2009 on worker classification and other employment tax issues. As a result, you should expect increased audit activity in the future relating to worker classification.

A disregarded entity continues to be disregarded for other Federal tax purposes.

Additionally, the individual owner of a disregarded entity treated as a sole proprietorship continues to be treated as self-employed for purposes of Self-

Employment Contributions Act (SECA) taxes, and not as an employee of the disregarded entity for employment tax purposes.

An EIN can be obtained online at <https://sa1.www4.irs.gov/modiein/individual/index.jsp>

If you need assistance in applying for an EIN or have additional inquiries regarding your withholding and worker classification obligations, you should consult with a legal professional.



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Bahar's practice specializes in tax planning for joint ventures and real estate transactions, including 1031 exchanges, drafting LLC and partnership agreements, designing service provider equity compensation for LLCs and partnerships, and representing taxpayers before the Internal Revenue Service and Arizona Department of Revenue.



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Carlene Miller's practice is concentrated in general federal tax including partnership, limited liability company, corporate and tax-exempt formation and planning, as well as employment tax, debt relief, state and local tax, and collections representation.