

## **EASTMAN & SMITH LTD. MEMORANDUM**

**TO:** The Ohio Association of Boards of Health

**FROM:** Joseph R. Durham; Eastman & Smith Ltd.

**DATE:** October 29, 2010

**RE:** Analysis of employment status of members of boards of health and Ohio Attorney General Opinion 2010-023

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### **Introduction**

Recently, the Ohio Attorney General issued Opinion 2010-023 discussing the Internal Revenue Service (IRS) audit of Guernsey County, which concluded that for federal tax purposes, members of boards of health are “employees” for whom income tax withholding and FICA taxes should be withheld, as opposed to independent contractors. We have reviewed the opinion of the Ohio Attorney General; an “Explanation of Items” (Form 886-A) from the Internal Revenue Service addressing whether appointed Board of Health members are employees for federal tax purposes; and other items provided by the Ohio Association of Boards of Health (OABH). A review of these materials establishes that: (1) the IRS has taken the position that for federal tax purposes, board of health members are employees under federal law, and so proper federal tax withholdings should be made for payments to board of health members; and (2) the Ohio Attorney General has opined that even though the IRS has concluded that board of health members are employees for federal tax purposes, this does *not* mean they are public employees for purposes of Ohio law, such as participation in the Ohio Public Employees Retirement System (OPERS). Such seemingly opposite conclusions have raised questions by OABH members. Before addressing the questions of OABH members, it is important to understand the options for health districts in responding to the conclusion of the IRS.

To begin, it is important to keep in mind that every health district has a legal advisor by statute. For example, the prosecuting attorney of the county comprising all or a major part of the district is the statutory legal advisor for general health districts. R.C. 3709.33.<sup>1</sup> This memorandum is not intended to provide advice to any particular health district, and individual OABH members are advised to rely on the particular advice of their statutory legal counsel. For instance, we are aware of at least one legal opinion issued by a Prosecuting Attorney’s Office which concluded that “the IRS determination is valid and legally enforceable,” and advised that particular health district to conform to the IRS proscriptions.

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<sup>1</sup> For a City Health District, the City Attorney is the legal advisor; for a Combined Health District, the counsel would depend on the manner in which the Combined Health District was formed. See, e.g., Ohio Attorney General Opinion 1997-029.

Further, we agree that the conclusion reached by the IRS in the generic “Explanation of Items” appears to be consistent with the Internal Revenue Code; however, the conclusion of an “Explanation of Items” is not definitive, and there are still several options for health districts.<sup>2</sup> As noted by the Ohio Attorney General, a county need not accept the IRS administrative determination that board of health members are employees for federal tax purposes. A general health district, the county auditor, or other appropriate authority (any person or party that is considered to be a taxpayer) could request a private letter ruling from the IRS seeking a definitive answer, which would apply to only the requestor. See Regulation section 601.201; Revenue Procedure 88-1; Internal Revenue Bulletin 1988-1, 7. A health district could continue to compensate board members as independent contractors until the IRS takes some adverse action by issuing findings or enforcement against the district or the county auditor making the payments, and then challenge or appeal the IRS action. Or, as set forth below, the health district could accept the IRS determination and treat board members as employees for federal tax withholding purposes, while still recognizing that the board members are not eligible for OPERS.

This memorandum will address several of the specific questions surrounding this issue raised by OABH members, including: (1) whether or not a board member of a general health district, if paid as an employee, is a member of OPERS; (2) whether or not a board member of a general health district, if paid as an employee, is a member of a union if other employees are union members; (3) whether or not federal tax withholdings are to be deducted from the board members’ compensation as set forth in Ohio Revised Code section 3709.02(B); and (4) whether or not the IRS conclusion relating to board members of a general health district applies to a combined local health district.

### Ohio Law

According to the Ohio Revised Code Section 3709.02(B), “each member of the board shall be paid a sum not to exceed eighty dollars a day for the member’s attendance at each meeting of the board. No member shall receive compensation for attendance at more than eighteen meetings in any year.” This caps a board member’s payment in exchange for attending board meetings at \$1,440.00 per year. Members of the board may also additionally receive reimbursement for travel expenses. R.C. §3709.02(C).

General health districts are independent political subdivisions, and are not part of any county, township, or municipal government. See OAG Opinion No. 2010-023; OAG Opinion No. 2008-017; OAG Opinion No. 1991-016; and OAG Opinion No. 1980-087. The State of Ohio has determined that members of boards of health are public officers who exercise a portion of the sovereignty of the State of Ohio. See OAG Opinion No. 1999-036.

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<sup>2</sup> It should be noted that the “Explanation of Items” cites U.S. Department of the Treasury Regulations, Public Revenue Rulings issued by the IRS, and previously decided court cases to support the position of the IRS that board of health members are employees for federal tax purposes. Revenue Rulings represent the administrative position of the IRS on questions of federal tax law, but are not binding on courts if a taxpayer challenges such position.

Each general health district has a district health fund, which is meant to finance all of the operating expenses of the district. Payments to members of the board of health for attendance at meetings and for travel expenses are expenses of the general health district, which should be paid out of the health district's district health fund. R.C. §3709.28.

By statute, the county treasurer of the county constituting all or a major portion of a general health district is the "custodian" of the health district's health fund. See R.C. §3709.31; OAG Opinion No. 1210 (1946). Also by statute, the county auditor of the county constituting all or a major portion of a general health district is charged with issuing "warrants" to pay the expenses of the board of health, upon receipt of "vouchers" approved by the board of health. R.C. §3709.31. The health commissioner may sign expense vouchers, but they must be approved by the board of health. See OAG Opinion No. 82-019 (1982). In simplified terms, the county treasurer holds the health district's money and cashes its checks, like a bank. The auditor holds the board of health's check book and issues its checks, but only upon proper authorization from the board of health. An explanation of this system of checks and balances of payment under Ohio law is relevant because the IRS may hold the county auditor responsible for the proper withholding of federal taxes from board of health payments.

However, under state law, board members of a general health district are not employees of the county, as general health districts are not performing county functions, nor are they county agencies. OAG Opinion No. 1997-029. General health districts are separate and independent political subdivisions for which counties are in no way responsible, despite the fact that county officers provide some non-discretionary services to health districts by statute, as explained above. OAG Opinion No. 2010-023.

Furthermore, the Ohio Attorney General has opined on the nature of the payments to board of health members in several instances. In OAG Opinion No. 1994-054, the Attorney General determined that a general health district board member who receives payment under R.C. 3709.02 receives no "earnable salary" as that term is defined for purposes of membership in the Ohio Public Employees Retirement System (OPERS). In OAG Opinion No. 1997-005, the Attorney General also determined that "under R.C. 3709.02(B), the amounts paid to a member of a board of health for attending meetings of the board more nearly approximate compensation for services rendered rather than reimbursement for expenses incurred, and indeed the statute expressly designates these amounts as 'compensation'" (emphasis added). Finally, state statute specifically excludes board of health members from participation in OPERS. As the Ohio Revised Code states:

145.012 Public employee defined.

(A) "Public employee," as defined in division (A) of section 145.01 of the Revised Code, does not include any person:

(7) Who is a member of the board of health of a city or general health district, which pursuant to sections 3709.051 and 3709.07 of the Revised Code includes a combined health district, and whose compensation for attendance at meetings of

the board is set forth in division (B) of section 3709.02 or division (B) of section 3709.05 of the Revised Code, as appropriate;

R.C. §145.012(A)(7) (emphasis added).

### Federal Law

A question to be addressed by the Internal Revenue Code (IRC) is whether the payments made to board of health members pursuant to Ohio law are payments made to “employees” or payments made to “independent contractors.” If board of health members are independent contractors, then they can be issued an IRS 1099 Miscellaneous Income Form; if they are employees, they should be issued a W-2 form with the proper withholdings included. According to the IRS, employers should use a W-2 Form to:

- Report wages, tips and *other compensation paid to an employee*.
- To report the employee’s income tax and Social Security taxes withheld and any advanced earned income credit payments.
- To report wage information to the employee, and the Social Security Administration. The Social Security Administration shares the information with the Internal Revenue Service.

A Form 1099-MISC is:

- Generally, used to report payments made in the course of a trade or business *to a person who is not an employee* or to an unincorporated business.
- Required among other things, when payments of \$10 or more in gross royalties or \$600 or more in rents or compensation are paid.
- Provided by the payer to the IRS and the person or business that received the payment.

*IRS Frequently Asked Questions* (emphasis added).

The court case of *Pope v. Commissioner*, 138 F.2d 1006 (6<sup>th</sup> Cir. 1943), established the criteria for determining whether a position constitutes a “public office.” According to *Pope*, a public office: (1) must be created by the constitution or the legislature, or by a municipality or other body with authority conferred by the legislature; (2) must involve a delegation of a portion of the sovereign powers of government to be exercised for the benefit of the public; (3) the powers conferred and the duties to be discharged must be defined either directly or indirectly by the legislature or through legislative authority; (4) the duties must be performed independently and without control of a superior power other than the law; and (5) the office must have some permanency and continuity, and the officer must take an official oath. Under these criteria, members of a board of health fit the definition of public officers under Ohio law. This also means that they do not fit the definition of independent contractors.

Internal Revenue Code section 3401(c) indicates that an “officer, employee, or elected official” of government is an employee for federal income tax withholding purposes. If this is

the case, generally such public officers will also be employees for social security and Medicare tax purposes.

Government employees who are covered by a qualifying public retirement system are exempt from mandatory social security tax, even if they are common-law employees for income tax purposes. As stated above, however, members of boards of health are not covered by OPERS under Ohio law. Most government workers who are not members of a state public retirement system are subject to mandatory social security withholding instead. These employees generally fall under the same rules that apply to all other workers covered by social security (there are special considerations made for some specific classes of government employees, such as temporary election workers; however, no such federal exception appears to apply to members of boards of health). Because board of health members are public officers who are not exempt from federal tax withholdings by virtue of being covered by a state public employee pension system, and are not covered by any other exception to mandatory social security withholding, the position of the IRS is that W-2 Forms should be issued and the proper withholdings made.

Another issue is determining which entity is actually responsible for issuing the W-2 Forms and making the proper withholdings. According to federal law, the entity that has “control” of the payment is responsible entity. Under the Ohio Revised Code, there are possibly two entities that have “control” over payments to members of boards of health. First, the board of health itself is responsible for fixing the compensation for services rendered by board of health members, and for issuing vouchers indicating who should be properly paid and in what amounts. These factors arguably make a board of health itself the “common law employer” of board of health members for federal taxation purposes. However, the county auditor also arguably has “control” over payments to board of health members, because the auditor issues the warrants for payment upon receipt of valid vouchers. As the Ninth Circuit Court of Appeals held:

It is clear that under the scheme for the withholding of taxes the common law employer is normally the person who is liable to withhold and to pay over to the Internal Revenue Service both income and FICA taxes. However, under certain unusual circumstances if the common law employer does not have control of the payment of the wages for such services then the person who does have such control steps into his shoes for this purpose.

*Southwest Restaurant Systems Inc. v. IRS*, 607 F.2d 1237 (9th Cir. 1979).

On at least one occasion of which we are aware, the IRS has issued a directive regarding the necessity of issuing W-2 Forms to members of boards of health to a county auditor by way of an “Explanation of Items” attached to the county’s audit report. As previously explained, the “Explanation of Items” is the IRS’ proposal for adjusting a return, and it details the issue, facts, law, taxpayer’s position, government’s position, and a conclusion. However, the county would still have the opportunity to object to or challenge an “Explanation of Items.” Issuance of the “Explanation of Items” indicates that the IRS believes that the county auditor at least has some

measure of “control” over payments to board of health members, and might hold the county responsible for making proper withholdings. This does not mean, however, that a board of health might not also be responsible for ensuring proper withholdings as well.

Application to Local Boards of Health

1. If the Internal Revenue Service considers board members of a general health district as employees of the county for federal tax purposes, are they now eligible for the Ohio Public Employment Retirement System (OPERS)?

No. Ohio Revised Code section 145.012(A)(7), as set forth above, and Ohio Attorney General Opinions specifically exclude board members from the definition of “public employee” for the purposes of OPERS.

2. If the Internal Revenue Service considers board members of a general health district as employees of the county for federal tax purposes, are they eligible to join an existing union of county employees?

No. Members of a Board of Health for a general health district are the appointing authority for the general health district, and are not eligible to join a union whose members they employ.

3. If the board members of the general health district are paid the maximum \$80.00 per meeting pursuant to Ohio Revised Code section 3709.02(B) for no more than eighteen meetings, can payment of this compensation from the general health fund exceed eighty dollars to cover the cost of federal income tax withholdings?

No. The \$80.00 payment of compensation includes any necessary withholdings. For example, if a general health district reports that a board member attended eighteen meetings, the County Auditor could make one annual payment of \$1440.00 as Misc. Reimbursement to an employee, securing the appropriate employment and payroll tax withholdings (Medicare, Social Security, state income, etc.) after each board member completes an IRS Form W-4 (Employee’s Withholding Allowance Certificate) and Ohio Form IT-4 (Employee’s Withholding Exemption Certificate). The county auditor will not withhold any contribution for OPERS, because board of health members are not members of OPERS by statute.

4. Are board members of a combined general health district also subject to federal tax withholdings?

Yes. Ohio Revised Code section 3709.02 states, in part, that:

(A) In each general health district there shall be a board of health consisting of five members to be appointed as provided in section 3709.03 and 3709.41 of the Revised Code. The term of office of the members shall be five years from the date of appointment, except that of those first appointed one shall serve for five years,

one for four years, one for three years, one for two years, and one for one year, and thereafter one shall be appointed each year. **This paragraph does not apply to a combined board of health created under section 3709.07 of the Revised Code.**

(B) Each member of the board shall be paid a sum not to exceed eighty dollars a day for the member's attendance at each meeting of the board. No member shall receive compensation for attendance at more than eighteen meetings in any year.

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Ohio Revised Code section 3709.07 states, in part, that:

The combined district shall constitute a general health district, and the board of health or health department of the city, the board of health of the original general health district, or the combined board of health, as may be agreed in the contract, shall have, within the combined district, all the powers granted to, and perform all the duties required of, the board of health of a general health district.

The district advisory council of the combined general health district shall consist of the members of the district advisory council of the original general health district and the chief executive of each city constituting a city health district, each member having one vote.

If the contract provides that the administration of the combined district shall be taken over by a combined board of health, rather than the board of health of the original health district, the contract shall set forth the number of members of such board, their terms of office, and the manner of appointment or election of officers.

Additionally, board members of a combined general health district are not members of OPERS pursuant to R.C. 145.012(A)(7). Board members of a combined general health district would therefore be subject to federal tax withholdings in the same manner.