

Stevens & Lee

M E M O

TO: Kate McDonnell
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FROM: Steven R. Rowland

RE: Statutory Exemption from UCL Taxation from the ABC Test for Trucking

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By way of background, the trucking industry was substantially deregulated during the Carter and Reagan administrations, and, as a result, the Interstate Commerce Commission was eliminated and federal regulation of rates and routes was ended. Similarly, States were broadly prohibited from regulating rates and routes. See 49 U.S.C. § 14501(c)(1) (“[A] State ... may not enact a law, regulation, or other provision having the force and effect of law related to a price, route, or service of any motor carrier ... with respect to the transportation of property.”). The trucking industry changed from a model where the motor carrier owned its equipment to one where carriers “lease” trucks provided by owner-operators who, in turn, are paid by the owner each time they move cargo pursuant to leases subject to the federal Truth-in-Leasing Regulations set forth at 49 C.F.R. §§ 376.1-376.26.¹ As a result, the industry was transformed by new entries, and the rate structure was no longer distorted by a closed system that benefited only the incumbent carriers and their drivers.

In connection with that deregulation, during the Kean administration, the trucking industry obtained a statutory exemption from the ABC Test of employment with respect to taxation under the state Unemployment Compensation Law (“UCL”), N.J.S.A. 43:21-1 et seq. The exemption reads as follows:

Services performed by the operators of motor vehicles weighing
18,000 pounds or more, licensed for commercial use and used for

¹ “There are hundreds of thousands of owner-operators in the United States, many of whom contract with federally regulated motor carriers.” Owner-Operator Ind. Driver Ass’n v. Swift Transportation Co., Inc., 367 F.3d. 1108, 1110 (9th Cir. 2004).

highway movement of motor freight, who own their equipment or who lease or finance the purchase of their equipment through an entity which is not owned or controlled directly or indirectly by the entity for which the services were performed and who were compensated by receiving a percentage of the gross revenue generated by the transportation move or by a schedule of payment based on the distance and weight of the transportation move [N.J.S.A. 43:21-19(i)(7)(X)].

Moreover, as a result of the many exemptions to the ABC Test, N.J.S.A. 43:21-19(i)(7)(A-Z) and elsewhere, the test of employment and taxation for UCL purposes often will be whether the work relationship is subject to taxation under the Federal Unemployment Tax Act (“FUTA”).

In particular, the introductory clause of N.J.S.A. 43:21-19(i)(7) states that there is no UCL taxation owed if there is either a categorical exemption from FUTA or where FUTA “contributions are not required to be paid into a state unemployment fund as a condition for a tax offset credit against the tax imposed by the Federal Unemployment Tax Act, as amended,” i.e., where UCL taxation need not be collected for the state plan to be federal compliant thereby preserving the offset credit. Similarly, under NJDOL’s regulation, the State statutory exemption from the ABC Test depends on whether “there is a corresponding exemption under the Federal Unemployment Tax Act (“FUTA”) or the services are otherwise not subject to tax or coverage under FUTA.” N.J.A.C. 12:16-23.1(b). Under the plain language of both N.J.S.A. 43:21-19(i)(7) and the corresponding regulation, N.J.A.C. 12:16-23.1(b), if no FUTA tax is due at owing, neither is UCL taxation.

For most large truck motor carriers, the current pathway to showing that they are not subject to FUTA does not involve an IRS classification determination, but rather through what is effectively a categorical exemption from FUTA pursuant to Section 530 of the Revenue Act of 1978. Under Section 530, a putative employer alleged to have misclassified a worker as an independent contractor is nonetheless not subject to FUTA if “the taxpayer did not treat an individual as an employee” ... “unless the taxpayer had no reasonable basis for not treating such individual as an employee.” Thus, Congress has directed that FUTA can only be imposed if and only if “the taxpayer had no reasonable basis for not treating such individuals as an employee.” Revenue Act of 1978, Pub. L. No. 95-600, 92 Stat. 2763 (as amended by Act of Dec. 29, 1979, Pub. L. No. 96-167, 93 Stat. 1275); Act of Dec. 17, 1980, Pub. L. No. 96-541, 94 Stat. 3204; Tax

Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324; Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2085; Small Business Protection Act of 1996, Pub. L. No. 104-188, 110 Stat. 1755. Further, under the 1996 Amendment to Section 530, Congress directed IRS to use Section 530 -- where potentially applicable -- as the primary test of whether FUTA taxation is owed. For that reason, when IRS audits a motor carrier, it has been directed by Congress to apply Section 530 as the primary test of whether federal employment tax can be assessed. Thus, IRS will have no reason to make a classification² determination in an audit of a motor carrier, but rather the carrier will be deemed to be not subject to FUTA taxation pursuant to Section 530.³

² The common law test of employment that the IRS previously used incorporates 20 factors and was set forth in IRS Revenue Ruling 87-41. The test focuses on the putative employer's "right to control" and most importantly, for present purposes, does not consider whether the owner-operator is economically dependent on the carrier. Currently, when IRS is required to make a classification determination, it uses a restatement of the 20-factors known as the three-category test focusing on behavioral control, financial control, and the relationship of the parties. Similarly, the three-category test does not consider whether the worker is economically dependent on the putative employer.

Notably, the United States Supreme Court has determined that owner-operators are independent contractors under the Social Security Act -- which incorporates a common law test of employment -- regardless of whether the owner-driver drove for a single business or multiple businesses. See United States v. Silk, 331 U.S. 704, 719 (1947) ("In one instance they haul for a single business, in the other for any customer. The distinction, though important, is not controlling. It is the total situation, including the risk undertaken, the control exercised, the opportunity for profit from sound management, that marks these driver-owners as independent contractors.").

Most significantly for present purposes, given the multi-factorial nature of all of the IRS's tests of common law employment -- a situation that predated IRS Revenue Ruling 87-41 -- IRS audits were unpredictable. This unpredictability resulted in Congressional action, namely, Section 530.

³ Under N.J.A.C. 12:16-23.2(a)(2), NJDOL accepts as proof of FUTA exemption an employment tax audit conducted by IRS "which determined that there was to be no assessment of employment taxes for the services in question; however, the determination must not have been the result of the application of Section 530 of the Revenue Act of 1978" The regulatory history, 26 N.J.R. 4730(a) (Dec. 5, 1994), may provide a clue for the rationale of NJDOL's refusal to accept a Section 530 determination as it bafflingly alludes to "a conformity issue which may result in noncertification of FUTA credit for employers." Of course, when a putative employer does not have to pay FUTA because of Section 530, that does not create a plan conformity issue if the State does not require UCL taxation unless federal law affirmatively requires a state plan to cover a class

Section 530 provides three essential methods by which a taxpayer may show it had a “reasonable basis” for the classification of its workers as independent contractors thereby preventing both retrospective and prospective reclassification. The provision states:

For the purpose of paragraph (1), a taxpayer shall in any case be treated as having a reasonable basis for not treating an individual as an employee for a period if the taxpayer’s treatment of such individual for such period was in reasonable reliance on any of the following:

- (A) judicial precedent, published rules, technical advice with respect to the taxpayer, or a letter ruling the taxpayer;
- (B) a past Internal Revenue Service audit of the taxpayer in which there was no assessment attributable to the treatment [for employment tax purposes] of the individuals holding positions substantially similar to the position held by this individual; or
- (C) long standing recognized practice of a significant segment of the industry in which such individual was engaged.

Given the industry’s reliance on owner-operators, a carrier that is audited will, for federal employment tax purposes, be deemed by IRS not to be subject to FUTA due to the “long standing recognized practice of a significant segment of the industry in which such individual was engaged.” The carrier will obtain a determination made pursuant to Section 530 which NJDOL’s regulations inexplicably reject as proof the putative employer is not subject to FUTA taxation. See N.J.A.C. 12:16-23.2(a)(2).

As Counsel is aware, approximately 80% of the “moves” at Port Newark are done by owner-operators as opposed to trucks owned by the motor carrier. See e.g., Karen Kerrigan, “NJ Independent Contractor Rule Threatens to Hamstring Business, Job Growth,” Bergen Record (Aug. 8, 2025). For purposes of Section 530, a “significant segment” requires only 25% of the industry following the practice. Thus, Section 530 will be the test applied to IRS audits of motor carriers. As a result, even if the carrier is audited by the IRS, since Section 530 will be applied, the carrier is unlikely to obtain a determination that NJDOL will accept.

of workers that are not subject to FUTA -- such as State employees. There is no such state coverage requirement for motor carriers.

Consequently, because of Section 530, IRS has, with respect to motor carriers, no federal tax reason to make a classification assessment under the common law test of employment. Yet NJDOL insists that motor carriers obtain such an IRS ruling in order to assert in the Section 19(i)(7)(X) exemption from the ABC Test.

Further, there is no legal process by which a motor carrier can compel IRS to render a classification determination as now required by NJDOL regulation. See N.J.A.C. 12:16-23.2(a)(1,3). The SS-8 instructions specifically state that: “Firms and workers file Form SS-8 to request a determination of the status of a worker for federal employment taxes and income tax withholding.” (emphasis added). Similarly, the IRS explains: “A Form SS-8 determination may be requested only in order to resolve federal tax matters.” (emphasis added). IRS also makes clear that it has no obligation to issue an SS-8 determination and it can use that discretion to refuse to decide for “reasons not in the best interest of tax administration.” Similarly, with respect to IRS private letter rulings from the IRS Office of Chief Counsel in Washington, D.C., not only are such rulings potentially costly to the taxpayer both in terms of user fees and professional costs, but IRS also has no obligation to issue them. See Internal Revenue Bulletin: 2025-1 (Dec. 30, 2024). Again, as with the SS-8 process, IRS will not issue a private letter ruling if it is not in the best interest of tax administration and the ruling itself will concern only a federal tax issue.

These concerns are not theoretical but rather have resulted in UCL assessments where an exemption to the ABC Test was intended. Specifically, in State Shorthand v. N.J. Department of Labor, 2024 WL 536446, *7 (App. Div. Feb. 12, 2024), the putative employer, a court reporting service statutorily exempt from the ABC Test under N.J.S.A. 43:21-19(i)(7)(G), was not permitted to assert that exemption because the IRS did not issue it an SS-8 determination:

Regarding the proceedings against SSRS, the matter was assigned to an ALJ, who ordered the matter be placed on the inactive list pending the processing of an Internal Revenue Service (“IRS”) Form SS-8. On July 14, 2016, the IRS issued an “information letter” to SSRS, which stated “based solely on the information you provided ... we conclude that an employer/employee relationship does not exist in the situation you described.” However, the letter also stated it “isn’t a determination letter and isn’t binding.”

More recently, in Farruggio’s Bristol and Philadelphia Auto Express, Inc. v. N.J. Department of Labor, 2025 WL 1788899 (OAL April 23, 2025), the Commissioner refused to apply the Section 19(i)(7)(X) ABC Test to the ABC Test notwithstanding that the motor carrier had obtained an IRS SS-8 determination that its owner-operators were independent contractors. Further, in the Farruggio Express SS-8 determination, the IRS expressly found that the carrier compensated the owner-operators on a percentage basis.

Under NJDOL's current regulations and practice, notwithstanding the Section 19(i)(7)(X) statutory exemption, it may be impossible for a motor carrier to assert that exemption. In an audit, IRS will apply Section 530 -- which NJDOL does not accept under N.J.A.C. 12:16-23.2(a)(2). In an IRS audit, the agency will rely on Section 530 -- as directed by Congress, but NJDOL will not accept that under N.J.A.C. 12:16-23.2(a)(2). In addition, with the repeal of N.J.A.C. 12:6-23.2(a)(4), effective September 17, 2018, NJDOL now mandates that anyone invoking an exemption from the ABC Test have an IRS determination in hand to invoke the exemption to the ABC Test. As shown, the putative employer cannot compel the IRS to issue either an SS-8 determination or render a private letter ruling. And if the carrier, like Farruggio's Express, is fortunate enough to obtain an SS-8 determination, the Commissioner will not in any event abide by it. At the end of the day, NJDOL essentially has created a Catch-22: to invoke the Section 19(i)(7)(X) exemption, the motor carrier must have an IRS determination that the carrier has no right to obtain. As a result, the statutory large truck exemption effectively has been overruled by regulation and administrative practice.