

Independent Contractor Misclassification

**What it is,
why it matters,
& solutions.**

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What is independent contractor misclassification ?

Employers label employees independent contractors (“1099-ing”), subcontract to other individuals, or pay workers off-the-books, to save upwards of 30% of payroll and related taxes for employees.

The Impact

- ❑ Federal & State Governments lose \$ billions in revenues - state & fed payroll taxes, UI and WC payments
 - ❑ Workers lose out on benefits & protections (right to minimum wage & overtime, organizing rights, etc.)
 - ❑ Law-abiding businesses can't compete – skews market, increases premiums
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Misclassification adds to nation's tax gap

- ❑ GAO estimate - \$4.7 billion loss in federal income tax
 - ❑ '94 study – proper classification could increase tax receipts by \$34.7 billion from '96-04
 - ❑ Misclassifying just 1% of workers as ICs costs UI trust funds \$198 million/year.
 - ❑ \$200M in lost UI tax revenue/year through '90s – estimated losses around \$343 M/yr for 2005
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Extent of misclassification – *staggering*

Results of 2000 DOL study:

- Up to 30% of firms misclassify

Percentage of firms that misclassify ranges from 9% in NJ to 42% in CT, according to state-level studies

Percentage of workers misclassified several points higher in problem industries, like construction.

Losses to States

- **CT** – state income taxes reduced by \$65M/year, \$57 million loss to workers comp, \$17 million loss to UI
 - **IL** – as much as \$207.8 million loss in state income taxes, and \$39.2 million loss to UI
 - **NY** – \$175.6 million loss to UI, \$170 million loss to WC
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Other consequences

- ❑ **Enforcement of workplace rights more difficult:** workers think they don't have rights, fewer records of employers' misdeeds
 - ❑ **Rigged bids:** firms that misclassify workers underbid; law-abiding contractors can't compete
 - ❑ **Growing underground economy:** Erosion of standards in industries where problem is prevalent, like construction, truck-driving
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Where we see the problem



What can
states do?

State agency taskforces

Inter-agency taskforces and committees can

- ❑ pool resources to
 - ❑ study the magnitude of the problem and patterns of abuse in their states,
 - ❑ coordinate and strengthen enforcement mechanisms.
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Recent AG and DOL efforts return much-needed funds to states

- **NY** Jt. Enf. Task Force recovered (since 9/07) over \$11M in UI taxes, over \$1.3M in UI fraud penalties, over \$14.5M in unpaid wages, and over \$1.5M in workers comp fines + penalties
 - **IL** AG reached agreement with 5 Chicago construction firms – deal included fines of \$80k and debarment for 4yrs
 - **MA** AG – indictment against temp labor co. that failed to report \$11M in payroll; recent settlement with FedEx returns \$3M to Commonwealth & payments to drivers
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Enforcement pays off!

- CA DOL recovered \$112M in payroll tax assessments, \$18.5M in labor code citations and \$40.3M in assessments in employment tax fraud cases
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State Legislation Addressing IC Misclassification

- “The Simple Fix”:** Laws that create presumptive “employers” or “employees” for those performing or receiving labor or services for a fee
- ❑ Presumption of employee status for all labor & employment laws, or
 - ❑ By individual law (workers comp – MA IC law), or
 - ❑ Presumption of employer status
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State Legislation, cont.

Sector-Specific laws targeted at worst abuses in industries with rampant misclassification problems.

Example:

- **DE Workplace Fraud Act** – presumption of employment relationship in the construction industry when individual performs work for remuneration
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ABC TEST

[A]n individual performing any service... shall be considered to be an employee under those chapters unless:—

- (1) the individual is free from control and direction in connection with the performance of the service, both under his contract for the performance of service and in fact; and
- (2) the service is performed outside the usual course of the business of the employer; and,
- (3) the individual is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in the service performed.

MASS, FAIR COMPETITION FOR BIDDERS ON CONSTRUCTION,
ETC., OF PUBLIC WORKS

What to aim for:

- ❑ The “Simple Fix” – presumption of employee status with objective test
ABC Test best
 - ❑ Private right of action
 - ❑ Strong anti-retaliation protections
 - ❑ Monetary damages **per** worker
 - ❑ Debarment remedies for violators who are local & county public contractors
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Please get in touch with us!

NELP loves to help, we have helped many groups on independent contractor misclassification issues, and we want to gather studies and model language.

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