

TASK FORCE ON MISCLASSIFICATION AND PAYROLL FRAUD AGENDA

Wednesday, August 28, 2019
10:00 a.m. – 2:00 p.m.
Department of Workforce Development
201 E. Washington Avenue, Madison, Wisconsin
GEF-1, Room D203

Welcome Governor Tony Evers DWD Secretary Caleb Frostman, Task Force Chair	10 Minutes
Task Force Overview – DWD <ul style="list-style-type: none">• Purpose and Charge Under Executive Order• Operational Processes/Roles and Responsibilities	5 Minutes
Member Introduction <ul style="list-style-type: none">• Who you are• What your role is• Why you are part of the task force	60 minutes
Break and Lunch – (Box lunch provided)	20 Minutes
Overview of 2009 Reports and Current State of Classification Issues at DWD Presentations by: Unemployment Insurance Division Workers Compensation Division Equal Rights Division	60 Minutes
Break	10 Minutes
Task Force Member Discussion - <ul style="list-style-type: none">• Goal Setting• Topics for future meetings and desired information• Tentative Meeting Dates through February 2020<ul style="list-style-type: none">○ September 25○ October 23.○ November 20○ December 18○ January 15○ February 12• Locations/ length of meetings<ul style="list-style-type: none">○ Statewide (Eau Claire, Milwaukee, Fox Valley)○ Three hours	75 Minutes
Adjournment	

*For press inquiries including interview requests, please contact the DWD Communications Office:

Media Line – 608-266-2722 or E-Mail – DWDSOCcommunicationsOffice@dwd.wisconsin.gov



EXECUTIVE ORDER #20

Relating to the Creation of the Joint Enforcement Task Force on Payroll Fraud and Worker Misclassification

WHEREAS, a significant number of employers in Wisconsin and elsewhere are improperly classifying individuals they hire as "independent contractors" even when those workers should be classified as employees;

WHEREAS, in 2009 the Wisconsin Department of Workforce Development, Unemployment Insurance Division found that 44% of the workers investigated during employer audits had been misclassified as independent contractors;

WHEREAS, from January 2016 to April 2019, the Worker Misclassification Section of the Department of Workforce Development conducted 1,963 investigations, with 422 resulting in audits. The 422 audits found 5,841 workers misclassified, found under-reported gross wages of almost \$70 million, and assessed approximately \$1.8 million in unemployment insurance taxes, interest, and penalties;

WHEREAS, worker misclassification denies vulnerable workers legal protections and benefits;

WHEREAS, this fraudulent practice also results in millions of dollars of losses to state government and taxpayers due to underpayments of wages, unemployment insurance contributions, worker's compensation insurance, and payroll taxes;

WHEREAS, employers that misclassify workers as independent contractors gain an unlawful competitive advantage that allows them to under-bid and out-compete law-abiding employers;

WHEREAS, enforcement activities in this area have historically been divided among different agencies, which can reduce the efficiency and effectiveness of enforcement without intentional collaboration;

WHEREAS, research and experience in other states suggest that enforcement efforts to address the problem of misclassification can be enhanced and made more efficient through interagency cooperation, information-sharing, and joint enforcement efforts against serious violators; and

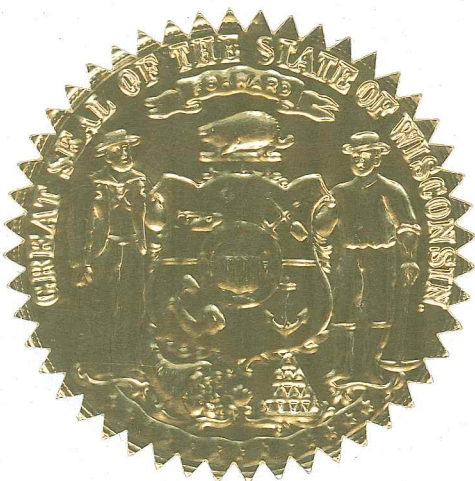
WHEREAS, research and experience in other states suggest that the creation of a joint task force has proven to be an effective mechanism for coordinating, enhancing, and streamlining enforcement in this area.

NOW, THEREFORE, I, TONY EVERS, Governor of the State of Wisconsin, by the authority vested in me by the Constitution and the Laws of the State, including Section 14.019 of the Wisconsin Statutes, do hereby create the Joint Enforcement Task Force on Worker Misclassification ("Task Force") and order the following:

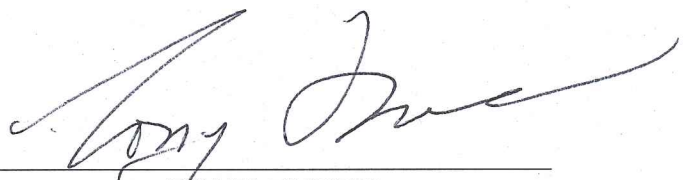
1. The Task Force shall be staffed by the Department of Workforce Development with technical assistance provided by staff of other agencies as needed. The Task Force shall consist of:
 - a. The Secretary of Workforce Development or a designee, who shall serve as the chair;
 - b. The Attorney General or a designee;
 - c. The Secretary of the Department of Revenue or a designee;
 - d. The Commissioner of Insurance or a designee;
 - e. The Administrator of the Worker's Compensation Division of the Department of Workforce Development;
 - f. The Administrator of the Unemployment Insurance Division of the Department of Workforce Development;
 - g. The Administrator of the Equal Rights Division of the Department of Workforce Development;
 - h. Other individuals appointed by the Governor to serve at the pleasure of the Governor, including at least one individual representing workers and at least one individual from the business community in an industry affected by misclassification, such as construction.

2. The Task Force shall facilitate coordination of investigation and enforcement of worker misclassification matters by the Department of Workforce Development, Department of Revenue, Commissioner of Insurance, Department of Justice, and other relevant agencies. This includes, but is not limited to:
 - a. Reviewing the work of the Worker Misclassification Task Force established by the Department of Workforce Development in October 2008, including its final report of June 2009, and the recommendations contained therein;
 - b. Examining and evaluating existing misclassification enforcement by agencies and reviewing the subsequent work on this issue by the Department of Workforce Development Misclassification Section;
 - c. Facilitating the sharing among the Task Force members of information relating to suspected worker misclassification violations, in a timely manner and to the maximum extent permitted by law;
 - d. Developing recommendations for pooling, focusing, and targeting investigative and enforcement resources;
 - e. Assessing existing methods, both within Wisconsin and in other jurisdictions, of preventing, investigating, and taking enforcement action against worker misclassification violations, and to develop best practices for participating agencies to improve their prevention and enforcement efforts;
 - f. Facilitating the filing of complaints and identification of potential violators;
 - g. Facilitating cooperation and participation of local district attorneys and other relevant state and federal agencies;
 - h. Working cooperatively with business, labor, and community groups interested in reducing worker misclassification, including but not limited to:
 - i. Seeking ways to prevent worker misclassifications, such as through the further dissemination of educational materials regarding the legal differences between independent contractors and employees; and
 - ii. Enhancing mechanisms for identifying and reporting worker misclassification where it does occur;
 - i. Increasing public awareness of the illegal nature of and harms inflicted by worker misclassification;
 - j. Working cooperatively with federal, state, and local social services agencies to aid vulnerable populations that have been exploited by

- worker misclassification, including but not limited to immigrant workers; and
- k. Reviewing statutes and regulations related to worker misclassification and recommending any appropriate changes to relevant legislation or administrative rules.
3. The Task Force shall issue a report to the Governor on or before March of each year, which shall:
- a. Describe the accomplishments and recommendations of the Task Force;
 - b. Include the amounts of wages, premiums, taxes, and other payments or penalties collected with coordinated agency activities, as well as the number of employers cited for legal violations related to misclassification and the approximate number of workers affected;
 - c. Identify any administrative or legal barriers impeding the more effective agency coordination, including any barriers to information sharing or joint action;
 - d. Propose, after consultation with representatives of business and organized labor, members of the legislature and other agencies, appropriate administrative, legislative, or regulatory changes to:
 - i. Reduce or eliminate any barriers to coordinated agency investigations;
 - ii. Prevent worker misclassification from occurring;
 - iii. Investigate potential violations of the laws governing worker misclassification; and
 - iv. Improve enforcement where such violations are found to have occurred; and
 - e. Identify successful mechanisms for preventing worker misclassification, and thereby reducing the need for greater enforcement.
4. Every agency, department, office, division, or public authority of the State of Wisconsin shall cooperate with the Task Force and furnish such information and assistance as the Task Force determines is reasonably necessary to accomplish its purposes.



IN TESTIMONY WHEREOF, I have hereunto set my hand and caused the Great seal of the State of Wisconsin to be affixed. Done in the City of Madison this fifteenth Day of April in the year of two thousand nineteen.

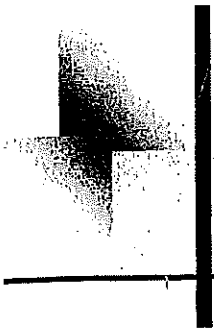


TONY EVERS
Governor

By the Governor:



DOUGLAS LA FOLLETTE
Secretary of State



Report of the Worker Misclassification Task Force

Submitted to
Secretary Roberta Gassman
Department of Workforce Development

June, 2009

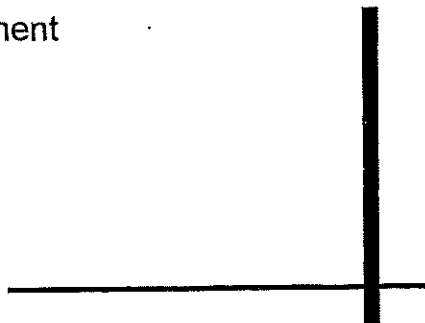


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Background

The Worker Misclassification Task Force was established by Department of Workforce Development Secretary Roberta Gassman in October 2008. The Task Force was chaired by Hal Bergan, administrator of the Division of Unemployment Insurance.

The Task Force was charged with examining the problems relating to misclassifying workers and recommending administrative and legislative steps to address those problems. The Task Force included the following members:

Lyle Balistreri, President
Milwaukee Building and Construction Trades Council

Jeffrey J. Beiriger, Attorney
Cook and Franke

Hal Bergan (Chair), Administrator, Division of Unemployment Insurance
Department of Workforce Development

Amy Bomkamp, Section Chief
Audit Technical Services
Department of Revenue

Don Garner-Gerhardt, Government Affairs Director
Teamsters Joint Council 39

Frances Huntley-Cooper, Administrator, Workers Compensation Division
Department of Workforce Development

Greg Jones, Administrator
Safety and Buildings Division
Department of Commerce

Paul Lovinus, Secretary-Treasurer
Teamsters Local 344

James Macejkovic, Executive Vice-President
Building Service, Inc.

Mark Reihl, Executive Director
Wisconsin State Council of Carpenters

James. M. Steele, President
Steele Construction Corporation

The Task Force met 10 times from October 2008 through March of 2009. The deliberations drew heavily on the experience of the individual members in describing misclassification and its consequences. The Task Force heard testimony from contractors, labor union members and building inspectors within Wisconsin, and enforcement personnel and legal experts from other states. Matthew F. Capece, Representative of the General President of the United Brotherhood of Carpenters and Joiners of America, provided a national perspective on the misclassification issue. Throughout the meetings of the Task Force, there was attention to the laws and enforcement models used elsewhere. There was an active search for the best practices that would permit Wisconsin to draw the maximum benefit from the experience of other states.

Representatives of Wisconsin's construction industry observed the work of the Task Force and were active participants in many of the discussions. They included: Jim Boullion and Scott Tyre of Associated General Contractors; Brad Boycks, Cindi Gruebling and Pat Stevens of Wisconsin Builders Association; and John Mielke and Andrew J. Engle of Associated Builders & Contractors.

Daniel LaRocque, Chief of the Unemployment Insurance (UI) Division's Bureau of Legal Affairs, and Tracey Schwalbe, the Division's Research Attorney, provided legal support and important contributions in clarifying legal issues. Ed Pyykonen, the Chief of UI's Audit Section, and Brian Krueger, Bureau Chief of the Worker's Compensation Insurance Bureau, were available as resources to the Task Force and made key contributions to its final recommendations.

The Task Force discussion focused on the problems of misclassification in the construction industry. The Task Force paid some attention to the transportation industry as well, but the recommendations in the report are aimed primarily at practices in the construction business.

What Is Worker Misclassification and Why Is It A Problem?

Worker misclassification is the practice of employers wrongfully identifying workers who should be treated as employees as "independent contractors." These workers are denied the protection of workers compensation and unemployment insurance. Companies that misclassify workers avoid paying unemployment and withholding taxes and purchasing worker's compensation insurance. Misclassification by employers puts them at an unlawful competitive advantage over employers who "play by the rules" and pay these costs as the law requires. The cost differential can be devastating to a law-abiding employer bidding for construction contracts and is generally destabilizing to the business climate.

Related to the problem of misclassification is the practice by some employers in the construction industry of operating in the underground economy. In the underground economy, employers do not report all or even a significant portion of their employees. They pay their workers in cash and their enterprises have a "here today and gone tomorrow" character that keeps them one step ahead of most enforcement efforts. A typical arrangement might have a construction company showing a few people on its official payroll and several construction subcontractors. These subcontractors, in turn, often call their workers independent contractors or simply pay them in cash. Their names never appear on a check stub, an unemployment insurance wage record, or as potential recipients of worker's compensation.

This practice is particularly common with companies that employ illegal workers who, because of their status, are unlikely to seek assistance if they are injured on the job or laid off. The challenge faced by agencies seeking to enforce proper classification of workers is compounded by unreported workers and wages paid in cash or otherwise off the employers' books.

Matthew Capece of the United Brotherhood of the Carpenters and Joiners of America described the situation like this: "In the construction industry, misclassification fraud gives irresponsible employers a 30 percent or more advantage in labor costs. And in a competitive industry like construction, that means responsible employers who play by the rules (and their employees) lose work. Misclassification in construction is more common than in other industries because of competitiveness, mobility of employers and the workforce, the temporary nature of the work and the multiple layers of contractors and subcontractors."

Studies of misclassification in several states estimate the number of improperly classified workers as about 14% or 15% of the workforce in construction. A Massachusetts study pegged the percentage as "up to 24%." No similar study exists for Wisconsin, but anecdotal evidence and existing state enforcement outcomes suggest that misclassification is no less problematic here. Members of the Task Force were outspoken in describing their own experience with misclassification. For workers, it means less work and no labor protections. For employers, it means losing business to competitors who unfairly avoid costs through classification fraud. The problem of misclassification is not a new phenomenon, but it is becoming more widespread in Wisconsin and across the country. There is some early evidence that misclassification is becoming more common in commercial as well as residential construction.

The practice of engaging a "subcontractor" whose sole obligation is to employ and pay individuals on a construction project highlights the nature and extent of the misclassification problem, particularly as it relates to larger projects. Here is how it can work. A general contractor wins an award for a large commercial building. That general contractor has obtained bids for drywall installation from

drywall subcontractors. Often, those subcontractors have a very small roster of employees and a much larger roster of individuals described as independent contractors or subcontractors. In reality, the independent contractors are employees according to the laws governing employment taxes, wages and worker's compensation. These employees are misclassified as independent contractors. There can be many such workers on a large construction site.

It is not unusual for earnings to be paid in cash without wage records and without withholding for Social Security, Medicare and income taxes. In many instances, the labor contractor neglects even the most basic steps to identify the workers, making investigation and proof of violation all the more difficult. Injuries and layoffs are not compensated by worker's compensation and unemployment insurance, and employer obligations to fund these benefits are shifted to other employers or the taxpayer. The benefits and savings from these unlawful practices are not limited to the subcontractors; they flow upward to the general contractor and project owners as well.

The multiple layers of relationships tend to slow and discourage agency enforcement. By the time all layers are penetrated by audit or investigation, the labor subcontractor has disbanded, discharged the employees, and set up shop under a new name.

Wisconsin State Agency Enforcement Efforts

DWD: Unemployment Insurance

The Unemployment Insurance (UI) Division has a Field Audit Section whose goal is to achieve a balanced tax program that will ensure that the unemployment tax provisions are enforced and that taxes are paid on an equitable basis by all employers. Having a strong auditing presence has a deterrent effect so that employers will report all of their employees and pay their fair share of UI taxes.

UI field audit investigations demonstrate that the issue of misclassification of workers has been increasingly problematic in all types of businesses, but especially in the construction industry. The staff of 20 auditors spends much of its time investigating whether workers who are performing services for pay are valid contractors or should be treated as employees.

The audit selection process involves two types of audit investigations: request and verification audits. Request audits involve referrals of known issues from within the agency, issues which most often arise from a benefit claim. Request audits also originate from other governmental agencies, like the IRS and Worker's Compensation, as well as tips from other employers, workers, and the general public. These audits represent about 45 percent of all audits.

Verification audits are selected from a pool of audit candidates that are generated weekly by the tax system from a number of different variables and parameters. One of these selection components targets certain kinds of employers using a weighted value based on industry classification, whether their UI account is overdrawn or not, number of 1099's that they issue, how long they have been in business and the results of any previous audit. Using these parameters, employers in the construction industry have a substantially greater chance to be selected for an audit than a retail business.

The small staff of 20 auditors is only able to audit about 2% of the employers each year. In 2008, there were 2,199 audit investigations completed of which 30% were in the construction industry. In all categories, a total of 16,561 workers were investigated during these audits. Of these, 7,283 or 44% of workers examined were reclassified as employees. Misclassification of employees is by far the most important of the issues identified and corrected in the audit process.

DWD: Worker's Compensation

Throughout the years, the Worker's Compensation Division (WCD) has routinely received complaints and questions from employers expressing concern that employers and competitors are not complying with the Worker's Compensation (WC) law by treating actual employees as alleged independent contractors, resulting in an unfair competitive advantage.

While the complaints encompass a wide variety of businesses, the complaints are more prevalent in the areas of construction, roofing, trucking and logging. Insurance non-compliance in these high-risk occupations is more common due to the higher cost of insurance.

The WCD makes every effort to educate employers regarding their worker's compensation insurance obligations under the Wisconsin Worker's Compensation Act. The WCD also diligently enforces the insurance requirements of the Act and strives to maintain a level playing field for all Wisconsin employers by ensuring employers who are required to carry worker's compensation insurance have a policy in force. The WCD detects and addresses misclassification of employees as independent contractors by investigating complaints and also forwards the complaints to the Unemployment Insurance Division for review.

Under the Wisconsin Worker's Compensation Act, the nine point test under s. 102.07(8), Wis. Stats., used to determine whether a worker is an independent contractor or an employee is complex, time consuming and somewhat subjective.

Worker's compensation misclassification issues include:

- Alleged independent contractor does not meet the 9-point test.
- The employer has a worker's compensation policy with little if any payroll, because the employer maintains all workers are independent contractors.
- The employer does not have a worker's compensation policy and indicates all workers are independent contractors.
- The employer is reporting employees to UI but maintains they are independent contractors for worker's compensation purposes.

The WCD has six compliance investigators tracking approximately 120,000 employers.

- Employers are notified by the WCD and encouraged to maintain coverage 60 days prior to the expiration of their policy so that a lapse in coverage will not occur.
- The WCD works with the Department of Revenue, DWD's Division of Unemployment Insurance, the Wisconsin Compensation Rating Bureau, the Department of Natural Resources and the Department of Commerce to identify employers who are operating in violation of the law.
- All new UI employer accounts and DOR tax withholding accounts are crossmatched by FEIN against the WC insurance policy database to determine if the employer has the required WC insurance. If no policy is found, an investigation is begun. If the employer has a worker's compensation policy, but it appears inadequate for the likely number of employees, the issue may be referred to the insurance company to audit.
- DNR submits a monthly report to WCD of all contractors awarded contracts on timber sales of county forests and DNR owned lands in the prior month. WCD verifies the loggers' WC compliance with the worker's compensation coverage requirements. WCD reports inconsistencies to DNR for further review and action and investigates non-compliant employers.
- The WCD reports job classification inconsistencies to the insurance carrier and the Wisconsin Compensation Rating Bureau (WCRB).
- The WCD provides information to employers in various forums such as labor law clinics and group requests.

DWD: Equal Rights Division

The Equal Rights Division (ERD) encounters similar worker misclassification issues when it investigates wage complaints. The ERD uses definitions of employee that differ from the definitions used by UI, WC and the Department of Revenue. Laws enforced by ERD include the requirement that employers provide employees with the number of hours worked, the rate of pay, and the amount of and reason for each deduction from wages due or earned by the employee. This information must be stated on the paycheck, pay envelope or other paper accompanying the payment. The penalty for violating this requirement is \$10 to \$100 per violation. In addition, employers are required to maintain records and hours, pay overtime, and otherwise comply with the Fair Labor Standards and counterparts in state laws.

Department of Revenue

Employee misclassification is one of several tax avoidance strategies utilized by employers. Employee misclassification enforcement activities performed by the Department of Revenue include:

- Informant emails and letters are reviewed and may be assigned for field or office audit depending on reliability of misclassification information available.
- Taxpayer information is reviewed for possible audit assignment, which will include withholding tax issues if identified.
- If a worker misclassification issue arises while conducting an audit of another tax type, the audit may be expanded to include withholding tax.
- When the Department discovers a misclassified worker, the auditors seek to get the employer properly registered and initiate withholding. A penalty can be imposed. The employee's expenses, other than the allowable employee business expenses that are reportable on Form 2106, can be disallowed and a penalty imposed.

Department of Commerce

The Department of Commerce recently passed an emergency rule requiring the registration of building contractors. The registration requirements apply to building contractors not already credentialed by the Department. (For example, dwelling contractors, electrical contractors, and other specialty contractors are already credentialed.) The fee for registering is \$100 and the term of the registration is four years. The primary purpose of the registration is to identify contractors so that the Department can provide information about development of and changes to the statewide building codes, changes in policies and

procedures, product recalls, obligations to other state agencies and the federal government. The Department anticipates that approximately 80% of the estimated 30,000 contractors will register pursuant to the rule.

The roster of registered contractors will be of significant assistance to the Departments of Workforce Development and Revenue in their pursuit of worker misclassification violations. Building Contractor Registration (BCR) identifies what building contractor businesses are operating in Wisconsin. It helps local and state agencies ensure that the businesses are following the same rules in terms of employees, taxes, permits, worker's compensation and unemployment insurance. In fulfilling those roles, BCR works against unfair competition. Providing more information on codes, code changes, employer regulations, education, and business responsibilities helps contractors provide better service and helps consumers get better results.

Activities in Other States

Worker misclassification is a nationwide problem and Wisconsin is far from the first state to address it. Over the last few years, other states have employed a variety of strategies to curb misclassification and provide a level playing field for businesses that meet their legal obligations to the people who work for them. The vast majority of construction businesses across the country "do the right thing" by paying into their state's unemployment insurance reserve fund and providing worker's compensation coverage for their workers. The growing number of construction companies that flaunt the law are problematic in many ways and states have devised a range of strategies to deal with them. The Task Force was diligent in examining those strategies in an effort to identify which were most effective and the best fit for Wisconsin's situation. The basic strategies are identified below.

Contractor Registration

Minnesota law requires the certification of individuals performing public or private sector commercial or residential building construction or improvement services. Persons operating in the construction industry without an independent contractor certificate are considered employees of the contractor. Corporations and LLCs are exempt from the certification requirements. An independent contractor must meet a nine-point test to be certified. The test is almost identical to the test applied in Wisconsin's unemployment insurance and worker's compensation programs.

The application fee for an independent contractor certificate is \$150 and the certificate must be renewed every two years. Individuals and contractors who fail to comply with the law are subject to a penalty of up to \$5,000. The program began operation in late 2008. To date, approximately 2,000 certificates have been issued, a smaller number than expected. At the same time, the number of

LLCs is up significantly, indicating that there may be an active effort to avoid coverage under the law.

Stop Work Orders

Several states employ stop work orders as an important component in worker classification enforcement. Though the specifics differ, the focus in most states is on ensuring that workers have the protection offered by worker's compensation. Other state laws make specific reference to the proper classification of workers. States with stop work orders related to worker misclassification include California, Connecticut, Florida, Massachusetts, New Jersey, and New York. Wisconsin currently utilizes stop work orders in enforcement of the statewide building code when health and safety are threatened.

Definition of employee and/or independent contractor

New Hampshire, New Jersey, Minnesota and Washington have tried to provide a consistent definition of employment across several state programs. Iowa provides one definition for WC, UI, wage, state and federal income taxes. In general, this uniformity provides consistency between a state's worker's compensation and unemployment compensation programs.

Massachusetts has focused on defining an independent contractor according to the kind of work the person does. According to this approach, an individual must "provide service outside the usual course of the employer's business" in order to qualify as an independent contractor. This is a "bright line" test that would simplify enforcement, but may not add much to Wisconsin's already stringent standard for classification as an independent contractor.

Recommendations

The Task Force weighed a wide range of options to address the issue of worker misclassification and the underground economy. The general principles that guided the Task Force decisions included:

- Focus primary attention on the worst offenders.
- Limit the impact on contractors who play by the rules.
- Design an enforcement system that emphasizes quick action and prompt resolution of issues.
- Improve data sharing among state agencies committed to reducing misclassification.
- Educate the public and the contractor community about misclassification issues, enforcement, and penalties.
- Take enforcement actions that are strong and visible in order to deter those who would engage in misclassification.
- Stay flexible in addressing misclassification; be prepared to make adjustments as we learn what works and what does not.

The recommendations do not seek to solve every problem that results from misclassification. Rather, the Task Force concentrated on developing an approach that draws on the strengths of our existing laws and agency expertise, while overcoming the lack of speed and flexibility in our existing enforcement processes. There was particularly strong consensus behind the idea that the recommendations should create an interagency effort that has misclassification issues as its primary focus.

Recommendation 1: Create an Office Of Worker Misclassification; empower the Office to issue stop work orders.

This small office (six staff) would focus exclusively on employee misclassification. It would include investigators and enforcement personnel who would visit job sites and ensure that workers on the site were properly credentialed as employees or independent contractors. Contractors on the job site would be required to provide the following:

- Proof of workers compensation insurance.
- Unemployment Insurance account number.
- Department of Revenue withholding tax number.
- Proof of Department of Commerce registration for all independent contractors.
- Payroll records, including appropriate payroll deductions, for all employees.
- Names, addresses, and Social Security Numbers for all workers on site.

This is information that should be readily available for a contractor working within the law. If supervisors are unable to provide this information at the work site, enforcement personnel are authorized to issue a stop work order for all elements of the work under the control of a non-complying contractor or subcontractor. The contractor would be able to appeal the stop work order "on the spot" and resume work, but would be required to provide proof of compliance within a specific time period. If compliance is not accomplished within the deadline, the stop work order would be reinstated.

This system is designed to encourage compliance with the law. It provides timely enforcement with appropriate safeguards for contractors that fulfill the requirements of the law. It serves as an incentive for major contractors to ensure that their subcontractors are legitimate businesses meeting their legal obligations to their workers and state enforcement agencies. A stop work order is a serious matter and most contractors would take the steps necessary to avoid such an action.

Recommendation 2: Increase information sharing among state agencies.

There is currently good cooperation among state agencies with enforcement responsibilities regarding misclassification, but improved consultation and information sharing processes can strengthen the misclassification enforcement process. There will be an in-depth review of interagency information sharing agreements with an eye towards strengthening existing efforts. The new Department of Commerce contractor registration program will provide important information to the Department of Workforce Development (DWD) and the Department of Revenue. The activities of the Office of Worker Misclassification will provide information useful to DWD, Revenue and Commerce. The close coordination of these activities will strengthen enforcement overall and send a clear message to those contractors seeking to operate outside the law.

Recommendation 3: Support the operations of the Department of Commerce Builder Contractor Registration (BCR) program.

This initiative requires building contractors to register with the Department of Commerce. It provides contractors that register with a four-year credential for a fee of \$100. The registration program supplies communication, education, and oversight to building contractors. BCR will permit the Department to improve participation by contractors in the process of developing rules and procedures. Moreover, it will provide an important channel of communication concerning contractor obligations relating to workers and state and federal agencies.

Recommendation 4: Establish a "hotline" to facilitate reports from workers, contractors, and the general public about misclassification abuses.

Timely information about construction projects operating outside the law is crucial to an effective enforcement effort. This information often comes to workers, local building inspectors, and other participants in the construction industry. A hotline would provide a way to share this information with the Office of Worker Misclassification and provide the basis for timely intervention when appropriate.

Recommendation 5: Undertake an aggressive campaign to educate contractors and the general public about misclassification issues.

In some instances, contractors engage in misclassification because they fail to understand the law. An active education campaign is necessary to address this problem. Raising public awareness will also serve as a warning to contractors who knowingly and willfully misclassify workers that they can expect a strong enforcement effort and significant penalties for violating the law.

Recommendation 6: Withhold 2% on form 1099 from payments made by contractors to subcontractors, including individuals operating as independent contractors.

This change would provide additional enforcement tools for Department of Revenue efforts to deal with misclassified workers and the underground economy. The withholding requirement will permit DOR to monitor payments to firms and individuals who are seeking to operate in violation of Wisconsin's requirements on the proper classification of workers. It can provide the basis for audit activity at the Department of Revenue as it seeks to curtail the practice of non-filing and underreporting on the part of building contractors.

Recommendation 7: Provide significant penalties for contractors actively seeking to subvert and avoid proper classification of workers.

Most enforcement activity envisioned in these recommendations is aimed at producing compliance on the part of contractors, subcontractors, and individuals engaged in construction. In most instances, compliance will be accomplished through investigation and more effective administrative processes. On-site inspections and stop work orders will provide a more proactive enforcement effort when it is required. Even in those cases, sanctions will not be severe so long as compliance is achieved.

Some contractors will actively take steps to avoid compliance. There are contractors who use misclassification as part of their routine business practices. Their purpose is to avoid the payment of taxes and insurance charges that are necessary to protect workers and their families. These rogue contractors actively seek a competitive advantage over contractors who play by the rules. For them, more serious penalties are needed. Their actions not only disadvantage legitimate contractors, they shift costs to taxpayers and others for uncovered medical expenses, uncollected taxes, and social services to workers not covered

by unemployment insurance. The Task Force recommends significant penalties for "willful misclassification." These penalties should be sufficient to deter even the worst offenders from pursuing this business strategy.

Recommendation 8: Conduct additional study of other policy options designed to combat worker misclassification.

The Task Force identified other policy alternatives that might strengthen enforcement of Wisconsin's laws concerning worker classification. These alternatives are worthy of further study. They include:

- A uniform definition of "independent contractor" by Workers Compensation, Unemployment Insurance, Equal Rights, and the Department of Revenue.
- Massachusetts "bright line" independent contractor definition. An individual must "provide service outside the usual course of the employer's business" in order to qualify as an independent contractor. In other words, an individual working as a roofer for a roofing contractor must be treated as an employee.
- Create a private "cause of action" for contractors disadvantaged by misclassification of workers on the part of their competitors.

Appendix 1

Relevant Statutory Definitions of Employee/Independent Contractors

Relevant Statutory Definitions of Employee/Independent Contractor in Wisconsin

Wisconsin Department of Revenue

(Income Tax Withholding) Wis. Stat. §71.63 (2) "Employee" means a resident individual who performs or performed services for an employer anywhere or a nonresident individual who performs or performed such services within this state, and includes an officer, employee or elected official of the United States, a state, territory, or any political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of these entities. The term includes an officer of a corporation, an entertainer and an entertainment corporation, but does not include a qualified real estate agent or a direct seller who is not treated as an employee under section 3508 of the Internal Revenue Code.

WDOR uses the federal common law definition. See 26 CFR 31.3121(d)-1. See also, Revenue Ruling 87-41 discussing the applicable common law standard definitions for employee. See also, IRS publication 15-A, Employer's Supplemental Tax Guide 2009

DWD – Equal Rights Division (various)

(Employment Regulations) Wis. Stat. §103.001 (5) "Employee" means any person who may be required or directed by any employer, in consideration of direct or indirect gain or profit, to engage in any employment, or to go or work or be at any time in any place of employment.

(Family or Medical Leave) Wis. Stat. §103.10 (1)(b) "Employee" means an individual employed in this state by an employer, except the employer's parent, spouse or child.

(Minimum Wage Law) Wis. Stat. §104.01 (2) (a) "Employee" means every individual who is in receipt of or is entitled to any compensation for labor performed for any employer.

(b) "Employee" does not mean:

1. Any individual engaged in the house to house delivery of newspapers to the consumer or engaged in direct retail sale to the consumer.
2. Any individual engaged in performing services for a person as a real estate agent or as a real estate salesperson, if all of those services are performed for remuneration solely by commission.
3. Any individual engaged in performing services for an employer described in sub. (3) (b) if that individual is not considered under 29 USC 203 (e) (4), as amended to April 15, 1986, to be an employee for the purposes of the fair labor standards act, 29 USC 201 to 219, or if that individual is exempt under 29 USC

213, as amended to April 1, 1990, from being paid at least the federal minimum hourly wage under 29 USC 206 (a) (1).

4. Any individual engaged in performing services for an employer described in sub. (3) (b) if that individual is not subject to the civil service laws of the employer and if that individual is an elective officer; is on the personal staff of an elective officer, other than a member of the legislature; is appointed by an elective officer to serve on a policymaking level; or is an immediate adviser to an elective officer with respect to the constitutional or legal powers of the elective officer's office.

(Wage Payments, Claims and Collections) Wis. Stat. §109.01 (1r)

"Employee" means any person employed by an employer, except that "employee" does not include an officer or director of a corporation, a member or manager of a limited liability company, a partner of a partnership or a joint venture, the owner of a sole proprietorship, an independent contractor, or a person employed in a managerial, executive, or commissioned sales capacity or in a capacity in which the person is privy to confidential matters involving the employer-employee relationship.

DWD – Worker's Compensation Division

Wis. Stat. §102.07 Employee defined. "Employee" as used in this chapter means:

(1) (a) Every person, including all officials, in the service of the state, or of any municipality therein whether elected or under any appointment, or contract of hire, express or implied, and whether a resident or employed or injured within or without the state. The state and any municipality may require a bond from a contractor to protect the state or municipality against compensation to employees of such contractor or employees of a subcontractor under the contractor. This paragraph does not apply beginning on the first day of the first July beginning after the day that the secretary files the certificate under s. 102.80 (3) (a), except that if the secretary files the certificate under s. 102.80 (3) (ag) this paragraph does apply to claims for compensation filed on or after the date specified in that certificate.

(b) Every person, including all officials, in the service of the state, or of any municipality therein whether elected or under any appointment, or contract of hire, express or implied, and whether a resident or employed or injured within or without the state. This paragraph first applies on the first day of the first July beginning after the day that the secretary files the certificate under s. 102.80 (3) (a), except that if the secretary files the certificate under s. 102.80 (3) (ag) this paragraph does apply to claims for compensation filed on or after the date specified in that certificate.

* * *

(4) (a) Every person in the service of another under any contract of hire, express or implied, all helpers and assistants of employees, whether paid by the employer or employee, if employed with the knowledge, actual or constructive, of the employer, including minors, who shall have the same power of contracting as adult employees, but not including the following:

1. Domestic servants.
2. Any person whose employment is not in the course of a trade, business, profession or occupation of the employer, unless as to any of said classes, the employer has elected to include them.

(b) Par. (a) 2. shall not operate to exclude an employee whose employment is in the course of any trade, business, profession or occupation of the employer, however casual, unusual, desultory or isolated the employer's trade, business, profession or occupation may be.

* * *

(8) (a) Except as provided in par. (b), every independent contractor is, for the purpose of this chapter, an employee of any employer under this chapter for whom he or she is performing service in the course of the trade, business, profession or occupation of such employer at the time of the injury.

(b) An independent contractor is not an employee of an employer for whom the independent contractor performs work or services if the independent contractor meets all of the following conditions:

1. Maintains a separate business with his or her own office, equipment, materials and other facilities.
2. Holds or has applied for a federal employer identification number with the federal internal revenue service or has filed business or self-employment income tax returns with the federal internal revenue service based on that work or service in the previous year.
3. Operates under contracts to perform specific services or work for specific amounts of money and under which the independent contractor controls the means of performing the services or work.
4. Incurs the main expenses related to the service or work that he or she performs under contract.
5. Is responsible for the satisfactory completion of work or services that he or she contracts to perform and is liable for a failure to complete the work or service.
6. Receives compensation for work or service performed under a contract on a commission or per job or competitive bid basis and not on any other basis.
7. May realize a profit or suffer a loss under contracts to perform work or service.
8. Has continuing or recurring business liabilities or obligations.
9. The success or failure of the independent contractor's business depends on the relationship of business receipts to expenditures.

(c) The department may not admit in evidence state or federal laws, regulations, documents granting operating authority or licenses when determining whether an independent contractor meets the conditions specified in par. (b) 1. or 3.

DWD – Unemployment Insurance Division

Wis. Stat. §108.02 (12) EMPLOYEE. (a) "Employee" means any individual who is or has been performing services for pay for an employing unit, whether or not the individual is paid directly by the employing unit, except as provided in par. (b), (bm), (c), (d), (dm) or (dn).

(b) During the period beginning on January 1, 1996, and ending on December 31, 1999, with respect to contribution requirements, and during the period beginning on January 1, 1996, and ending on April 1, 2000, with respect to benefit eligibility, par. (a) does not apply to an individual performing services for an employing unit other than a government unit or nonprofit organization in a capacity other than as a logger or trucker, if the employing unit satisfies the department that:

1. The individual:

a. Holds or has applied for an employer identification number with the federal internal revenue service; or

b. Has filed business or self-employment income tax returns with the federal internal revenue service based on such services in the previous year; and

2. The individual meets 6 or more of the following conditions:

a. The individual maintains a separate business with his or her own office, equipment, materials and other facilities.

b. The individual operates under contracts to perform specific services for specific amounts of money and under which the individual controls the means and method of performing the services.

c. The individual incurs the main expenses related to the services that he or she performs under contract.

d. The individual is responsible for the satisfactory completion of the services that he or she contracts to perform and is liable for a failure to satisfactorily complete the services.

e. The individual receives compensation for services performed under a contract on a commission or per-job or competitive-bid basis and not on any other basis.

f. The individual may realize a profit or suffer a loss under contracts to perform services.

g. The individual has recurring business liabilities or obligations.

h. The success or failure of the individual's business depends on the relationship of business receipts to expenditures.

(bm) During the period beginning on January 1, 2000, with respect to contribution requirements, and during the period beginning on April 2, 2000, with respect to benefit eligibility, par. (a) does not apply to an individual performing services for an employing unit other than a government unit or nonprofit organization in a capacity other than as a logger or trucker, if the employing unit satisfies the department that the individual meets

7 or more of the following conditions by contract and in fact:

1. The individual holds or has applied for an identification number with the federal internal revenue service.

2. The individual has filed business or self-employment income tax returns with the federal internal revenue service based on such services in the previous year or, in the case of a new business, in the year in which such services were first performed.

3. The individual maintains a separate business with his or her own office, equipment, materials and other facilities.

4. The individual operates under contracts to perform specific services for specific amounts of money and under which the individual controls the means and methods of performing such services.

5. The individual incurs the main expenses related to the services that he or she performs under contract.

6. The individual is responsible for the satisfactory completion of the services that he or she contracts to perform and is liable for a failure to satisfactorily complete the services.

7. The individual receives compensation for services performed under a contract on a commission or per-job or competitive-bid basis and not on any other basis.

8. The individual may realize a profit or suffer a loss under contracts to perform such services.

9. The individual has recurring business liabilities or obligations.

10. The success or failure of the individual's business depends on the relationship of business receipts to expenditures.

(c) Paragraph (a) does not apply to an individual performing services for a government unit or nonprofit organization, or for any other employing unit in a capacity as a logger or trucker if the employing unit satisfies the department:

1. That such individual has been and will continue to be free from the employing unit's control or direction over the performance of his or her services both under his or her contract and in fact; and

2. That such services have been performed in an independently established trade, business or profession in which the individual is customarily engaged.

(d) Paragraph (a) does not apply to a contractor who, in fulfillment of a contract with an employing unit, employs any individual in employment for which the contractor is subject to the contribution or reimbursement provisions of this chapter.

(dm) Paragraph (a) does not apply to an individual who owns a business that operates as a sole proprietorship with respect to services the individual performs for that business.

(dn) Paragraph (a) does not apply to a partner in a business that operates as a partnership with respect to services the partner performs for that business.

(e) This subsection shall be used in determining an employing unit's liability under the contribution provisions of this chapter, and shall likewise be used in determining the status of claimants under the benefit provisions of this chapter.

(f) The department may promulgate rules to ensure the consistent application of this subsection.

See also Wis. Admin. Code DWD 105 Relationship of Carriers and Contract Operators

See also Wis. Admin. Code DWD 107 Employment Relationships in the Logging Industry

Department of Commerce

(Regulation of Industry, Buildings & Safety) Wis. Stat. §101.01 (3)

"Employee" means any person who may be required or directed by any employer, in consideration of direct or indirect gain or profit, to engage in any employment, or to go or work or be at any time in any place of employment.

Appendix 2

State Legislation and Executive Orders Regarding Misclassification Fraud
(Capece, 2008)

**State Legislation and Executive Orders
Regarding Misclassification Fraud**

Updated October 7, 2008

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State Legislation or Executive Order	Year Became Law	Description
<p>California <u>Unemp Ins. Code Sec. 329</u></p>	<p>1995</p>	<p>(1) Statute creates a joint enforcement task force on the underground economy. It includes representatives from employment development, department of consumer affairs, industrial relations, insurance and criminal justice. (2) The duties of the task force include facilitating sharing of information and coordination of activist to combat the underground economy.</p>
<p>Colorado <u>SB 869 An Act Relating to Enforcing the Requirement to Carry Workers' Compensation</u></p>	<p>2007</p>	<p>(1) Compares companies registered with unemployment and workers compensation records to identify employers without compensation coverage. (2) Labor commissioner to investigate employers identified through the program. (3) Penalties reinvested to administration and enforcement. (4) Requires annual reporting on results and posting on the labor department's web site.</p>
<p>Colorado <u>HB 1366 An Act Concerning Workers' Compensation Coverage for Workers in the Construction Industry</u></p>	<p>2007</p>	<p>(1) Requires all construction workers, including independent contractors, to have compensation coverage, unless the independent contractor is incorporated or an LLC. Also, doesn't apply to residential work performed by owner occupants. (2) Persons performing construction work must have compensation. If they are subcontracting work, they must have proof of coverage from their subcontractors. (3) Violations result in a civil penalty. Penalty revenues are used for enforcement.</p>
<p>Connecticut <u>Sec. 52-57e Action for Damages From Violations of Workers Compensation or Unemployment Compensation Laws</u></p>	<p>1990</p>	<p>The law provides a cause of action for companies that lose a bid due to their competitor violating knowingly workers compensation or unemployment compensation laws. Employment status is determined by the Internal Revenue Code.</p>
<p>Connecticut <u>PA 7-89 An Act Concerning Penalties for Concealing Employment or Other Information Related to Workers' Compensation Premiums</u></p>	<p>2007</p>	<p>(1) Establishes stop work orders against employers for workers' compensation premium fraud due to misclassification or for not having compensation insurance. (2) Makes not having compensation a felony. (Premium fraud had already been a felony.)</p>

State Legislation or Executive Order	Year Became Law	Description
<p>Connecticut cont. <u>PA 8-156 An Act Establishing a Joint Enforcement Commission on Employee Misclassification</u></p>	2008	<p>(1) A task force is established that includes the labor commissioner, chair of the workers compensation commission, attorney general and the chief state's attorney. (2) Purpose is to: (a) coordinate civil and criminal investigations and prosecutions, (b) consult with representatives of business and labor to make recommendations for improving state enforcement and to reduce misclassification and (c) cooperate with state and other social service organizations to assist employees exploited by misclassification. (3) Also creates an advisory board of employee and employer representatives.</p>
<p>Delaware <u>SS 1 for SB 68 An Act to Amend Workers' Compensation Code</u></p>	2007	<p>The law provides that independent contractors cannot be exempt from workers' compensation coverage.</p>
<p>Florida <u>Sec. 440-140 Competitive Bidders Civil Actions</u></p>	1993	<p>The statute provides that if a bidder on a construction project loses due to its competitor violating workers compensation laws, then the bidder can bring suit for liquidated damages and attorney fees. To prevail, the defendant must have known or should have known that the law was being violated.</p>
<p><u>S. 50A Workers' Compensation Reform and Additional Penalties</u></p>	2003	<p>The law contained numerous revisions to workers compensation including (1) Limiting exemptions to workers compensation coverage and extending coverage to independent contractors in the construction industry. (2) Increasing criminal penalties for employers committing premium fraud and who violate stop work orders. Also, civil penalties for violating stop work order are increased. (3) An employer's second violation is a "knowing violation." (4) Employers are fined \$5,000 for each employee misclassified as an independent contractor. (5) Stop work orders provided for premium fraud as well as failure to secure coverage.</p>
<p><u>HIB 561, Section 10 Forfeiture</u></p>	2006	<p>Forfeiture assets to be deposited into a fund for the operations of the Insurance Fraud Division.</p>
<p><u>S. 2158 An Act Tightening Regulation of Check Cashing Businesses</u></p>	2008	<p>The bill contains numerous provisions designed to crack down on use of check cashing stores in money laundering schemes. Check cashing stores have proven to play a central role in hiding unreported cash transactions to escape employment tax and workers compensation coverage laws. Some of the new record keeping requirements includes keeping</p>

State Legislation or Executive Order	Year Became Law	Description
Florida cont.		copies of the photo identification of presenters of checks over \$1,000 and in some instances thumb prints. Includes criminal penalties for violating record keeping requirements and other unlawful practices.
Iowa <u>Exec. Order 8 Independent Contractor Reform Task Force</u>	2008	(1) This is a study task force made of representatives from the governor's office, workforce development, revenue, economic development and the labor commissioner. (2) The purpose is to study misclassification and make recommendations on education and any needed changes for enforcement, regulations and legislation. (3) A report is due to the governor by December 17, 2008
Illinois <u>PA 95-0026 Employee Classification Act</u>	2007	(1) For the purposes of the Act, creates a presumption of employment in the construction industry. (2) Makes the failure to properly classify a worker as an employee a violation of law. Includes standards for independent contractor status. (3) Exempts contractors from liability for the violations of their subcontractors. (4) Requirements of Act posted in labor department offices and its web site in multiple languages. (5) Provides for agency and private enforcement. The department gets investigatory subpoena power. Violations can result in (a) collection of any wages or compensation denied or lost, (b) criminal penalties, (c) civil penalties, (d) debarment and (e) extra penalties for willful violations. (Willfulness is proven by a preponderance of the evidence.) (6) All moneys collected go into an enforcement fund. (7) There is whistleblower protection. (8) Private suits can be brought by anyone interested in compliance with the Act and damages include (a) wages or compensation lost or denied, (b) liquidated damages of \$500 per violation, (c) attorney's fees and costs. (8) The Act requires state agencies to cooperate in enforcement actions and if misclassification is found to check if there are violations of the laws under their jurisdiction—workers' compensation, unemployment, etc.
Kansas <u>Sec. 44-766 Employer Misclassification of Employees</u>	2006	Prohibits employers from intentionally misclassifying employees as independent contractors in order to avoid requirements under state income tax and unemployment tax laws.
Louisiana <u>HB 554 An Act Relative to Discontinuance of Business Operations and Penalties for Failure to Carry Workers Compensation Insurance</u>	2008	Amends current law by providing that a court must order a non-compliant employer to secure workers compensation insurance and pay a fine up to \$10,000 within ninety days. If the employer fails to do either, the court will issue an order to the employer to cease business operations until the employer has insurance and has paid fines in full.

State Legislation or Executive Order	Year Became Law	Description
<p>Massachusetts <u>GL 149 Sec. 148B Fair Competition for Bidders on Construction</u></p>	<p>2004</p>	<p>(1) Prohibits the failure to properly classify an individual as an employee in the construction industry. That failure must also accompany a violation of minimum wage, overtime, prevailing rate, child labor, safety, state income tax withholding or other workplace standards law. (2) Creates a presumption of employment and includes standards for independent contractor status. (3) Penalties include civil, criminal and debarment.</p>
<p><u>S 1059 An Act to Clarify the Law Protecting Employee Compensation</u></p>	<p>2008</p>	<p>The law provides for private and class action suits regarding prevailing rate, overtime and minimum wage violations. Recovery includes treble damages, costs and attorney fees.</p>
<p><u>Exec. Order 499 Establishing a Joint Enforcement Task Force on the Underground Economy and Employee Misclassification</u></p>	<p>2008</p>	<p>(1) Task force to include representatives from the labor department, revenue, industrial accidents, attorney general, occupational safety, public safety, licensing, apprenticeship and unemployment tax. (2) Purpose of the task force is to foster compliance with the law by education, conducting joint investigations, protect health and safety and restore a level playing field for law-abiding businesses. Task force members are required to share information, identify and investigate non-compliant industries, seek cooperation and advice from labor and business representatives, work with social service agencies to assist exploited workers and identify changes in the law that are needed. (3) An annual report to the governor is required.</p>
<p>Michigan <u>Exec. Order 2008-1 Interagency Task Force on Employee Misclassification</u></p>	<p>2008</p>	<p>(1) A task force is made of representatives of the director of the department of labor, workers compensation, unemployment, tax enforcement and business services. (2) The purpose of the task force is to improve interagency cooperation and information sharing. Also, to develop law enforcement strategies, solicit case referrals, work with the labor and business communities, cooperate with local and federal agencies and make recommendations for legislation. (3) The task force can hold hearings and report to the governor.</p>
<p>Minnesota <u>Sec. 181.722 Misrepresentation of Employment Relationship Prohibited</u></p>	<p>2005</p>	<p>(1) Prohibits employers from misrepresenting an employment relationship or from failing to report individuals as employees. (2) Agreements to misclassify an employee as an independent contractor are prohibited. (3) Employment is determined by unemployment and workers' compensation laws. (4) A construction worker can bring a suit for damages against an employer who violates the law. Employee representatives may also bring suit. Damages can include attorney's fees and costs. (5) A court finding a violation of the law must report it to the labor commissioner. The labor commissioner shall report to other state and federal agencies.</p>

State Legislation or Executive Order	Year Became Law	Description
Minnesota (cont.) <u>Chapt. 135, HF 172, Sec. 15 Defining Independent Contractor Status and Requiring Certification</u>	2007	(1) Creates a presumption of employment for workers compensation, unemployment and other labor laws in the construction industry if services are in the course of a client's trade or business. Sets standards for independent contractor status. (2) To be considered an independent contractor a worker must hold a certificate from the department of labor. The law establishes an application process and qualifications for independent contractor certification. (3) Certificates last for 2 years. Certificates can be cancelled by the individual or revoked by the state if the individual no longer meets the criteria. (4) Persons can't work as an independent contractor without having a certificate. (5) Prohibits misrepresentation on applications and forcing person to apply for certification. (6) "Knowingly" defined as knew or could have known. (7) \$5,000 fine per violation. (8) Provides for investigatory subpoena power. (9) Revenue to be notified of violations.
<u>Chapter 154 HF 3201 Article 3 Income Taxes, Sec. 8 and 9</u>	2008	(1) Law requires a 2 percent withholding of state income taxes from compensation paid to independent contractors in the construction industry. (2) It also requires sample auditing of those withholdings and a report to the legislature.
Missouri <u>HB 1549T Addressing Immigration and Misclassification</u>	2008	Misclassification provisions were added to this immigration bill. (1) The act requires every employer in the state with 5 or more employees to file 1099 forms with the state for its independent contractors. Failure to repeatedly file the forms results in misdemeanor charges and fines. (2) Employment is defined by the IRS twenty factor test. (3) A violation occurs if an employer knowingly or has reason to know that a worker is an employee but fails to claim the worker as an employee. (4) Attorney general investigates violations. (5) Violations can result in (a) injunction against prohibited acts, (b) \$50 penalty for knowing misclassification includes per worker per day fines up to total of \$50,000.
Montana <u>Secs. 39-71-415 to 419 Independent Contractor Certification for Workers Compensation</u>	2005	(1) To be free of the requirement to cover with workers compensation, a person must fall into an exempt category or be a certified independent contractor. (2) Certifications can be revoked if the degree of direction and control creates employment status or if there was a misrepresentation in the application. (3) An employer cannot coerce a person or by fraudulent means require an employee to adopt independent contractor status. (4) Violations, including working as an independent contractor without having been certified, result in a \$1,000 fine per violation on top of any other penalties provided by law.

State Legislation or Executive Order	Year Became Law	Description
<p>Montana cont. <u>HB 65 § 1 An Act Generally Revising Workers' Compensation Law</u></p>	2007	<p>Section 1 of the Act gives workers compensation investigators access to construction sites to investigate compliance with coverage requirements.</p>
<p><u>New Hampshire</u> <u>SB 92 An Act Relative to the Definition of Employee and Clarifying the Criteria for Exempting Workers from Employee Status</u></p>	2007	<p>(1)The law creates a uniform definition of employment for (a) workers compensation, (b) workplace protections, (c) whistleblower and (d) minimum wage. (2) For workers compensation a presumption of independent contractor status can be created by contract, but civil penalties are imposed if the contract is intended to misrepresent the employment relationship. Penalties are deposited into a dedicated enforcement fund.</p>
<p><u>HB 336 An Act Requiring Notice of the Classification of Employee and Independent Contractor</u></p>	2007	<p>Requires employers to post information about criteria for classifying workers as employees and independent contractors.</p>
<p><u>HB 337 An Act Relative to Penalties for Failure to Have Workers' Compensation and Continually Appropriating a Special Fund</u></p>	2007	<p>(1)Increases civil penalties for failure to secure compensation coverage. (2) Persons with responsibility to disburse funds or salaries are held personally liable. (3) Insurers fined if they don't supply the state with notice of coverage within a reasonable time. (4) The penalties are deposited into a designated enforcement fund.</p>
<p><u>HB 426 An Act relative to workers' compensation and resolution of disputes involving employment status</u></p>	2007	<p>The insurance commissioner can investigate and hold hearings to resolve disputes between employers and their workers' compensation carriers about whether workers are employees or independent contractors.</p>
<p><u>HB 471 An Act Relative to Workers' Compensation Compliance in the Construction Sector and Continually Appropriating a Special Fund</u></p>	2007	<p>(1)Officers, directors or LLC members of a construction company who do on-site construction work cannot be excluded from compensation coverage. (2) Requires all contractors, subcontractors and independent contractors on state projects to provide proof of workers' compensation coverage. The number of employees or independent contractors and their compensation classification codes on such projects also must be disclosed. Violations can result in civil penalties and debarment. Civil penalties go to a workers' compensation enforcement fund.</p>
<p><u>HB 692 An Act Relative to Workers Compensation</u></p>	2008	<p>The legislation amends HB 471 passed in 2007. HB 692 re-establishes exemptions from workers compensation coverage for up to three executive officers of a corporation or members of a limited liability company.</p>

State Legislation or Executive Order	Year Became Law	Description
<p>New Hampshire (cont.) <u>SB 500 An Act Relative to Certain Insurance Fraud and Establishing a Task Force on Employee Misclassification</u></p>	2008	<p>(1) Increases penalty for the failure to carry workers' compensation to a class B felony. (2) Requires insurers to have written or electronic signatures on insurance, including workers' compensation, applications. (3) A person convicted of insurance fraud will be debarred from public works projects for 1 to 3 years and will be ordered to pay restitution to the insurance carrier. The third offense will result in permanent debarment. (4) A misclassification task force is established. (a) Task force includes representatives of: state senate, state house of representatives, labor commissioner, commissioner of unemployment, commissioner of insurance, commissioner of revenue, attorney general, labor unions, construction contractors, other business owners and insurance carriers. (b) The purpose of the task force is to study misclassification and issue a report and recommendations for legislation.</p>
<p>New Jersey <u>S 468 Withholding Taxes From Payments to Unincorporated Contractors</u></p>	2006	<p>(1) Payments made to unincorporated contractor for improvements made to real property are subject to a 7 percent withholding. (2) Liability for withholding from lower tiered subcontractors can extend to owners and lessors if they gave work to an unincorporated contractor who subcontracted to other unincorporated contractors and failed to withhold. (3) Does not apply to a governmental entity, homeowner, tenant, or if a person receives from its unincorporated contractor proof of its registration with the division of revenue. (4) Persons making deductions must furnish statements.</p>
<p>A 4009 An Act Concerning the Classification of Construction Employees for Certain Purposes and Supplementing Title 34 of the Revised Statutes</p>	2007	<p>(1) Establishes the failure to properly classify a worker as an employee a separate violation of law. (2) For construction work it creates a universal presumption of employment and a uniform definition under state law—with the exception of the workers compensation. (3) Knowing violations result in criminal penalties. Other penalties include debarment, restitution, suspension of contractor registration, stop-work orders and fines. Fines go an enforcement and administrative fund. (4) Provides for private-causes of action for workers. Class action suits are possible, and actions can be brought on behalf of a worker or class by worker representatives. Damages include attorney's fees and costs. (5) The Act also provides whistleblower protection.</p>
<p>Exec. Order No 96 Governors Advisory Commission on Construction Industry Independent Contractor Reform</p>	2008	<p>(1) The order establishes an advisory commission of representatives from labor & workforce development, the attorney general, treasurer and eight public representatives from labor unions, developers and contractors. (2) Purpose of the commission is to create public awareness and make recommendations to enhance law enforcement and cooperation between state and federal agencies. (3) The commission can hold hearings and must report to the governor.</p>

State Legislation or Executive Order	Year Became Law	Description
<p>New Mexico <u>SB 657 Employer, Employee Relationship in the Construction Industry and Independent Contractors</u></p>	2005	<p>(1)The law creates a presumption of employment in the construction industry and standards for independent contractor status. (2)An employer violates the law if it intentionally treats or lists an employee as an independent contractor when the employee does not meet the independent contractor definition. (3)Employers who violate the law face criminal penalties, suspension or revocation of licenses.</p>
<p>New York <u>Exec. Order 17 Misclassification Task Force</u> <u>A 6163 An Act to Amend the Workers' Compensation Law. §§52D, 141A</u></p>	2007 2007	<p>(1)Forms a task force of representatives from the labor department, attorney general, taxation and finance, workers compensation board, workers compensation fraud and New York City comptroller. (2) Purpose is to coordinate investigations, share information, pool resources and to consult business, labor representative and other representatives. (3) Reporting to the governor is required. Establishes stop work orders, debarment and criminal penalties for employers who don't have workers' compensation or who commit premium fraud.</p>
<p>South Carolina <u>SB 332 An Act Reforming Workers Compensation, Sections 3, 4, 5</u></p>	2007	<p>(1) Clarifies that a false statement or misrepresentation to gain a lower insurance premium includes misclassification of employees. (2) Penalties for workers compensation fraud increase with amount of money involved. (3) Gives the attorney general authority to hire a forensic accountant.</p>
<p>Tennessee <u>SB 1784 An Act Regarding Contractor Licensing</u> <u>HB 1645 An Act Relative to Requiring Workers Compensation Coverage for Sole Proprietors</u></p>	2007 2008	<p>Any applicant for a license or renewal of a license must supply an affidavit that the applicant maintains general liability and workers' compensation insurance coverage. (1)The law requires workers' compensation coverage in the construction industry for sole proprietors and independent contractors. Contractors using independent subcontractors would have to cover them with workers compensation insurance. 2)Some exemptions exist for work done for home owners: the sole proprietor wouldn't need coverage but any workers for the sole proprietor would have to be covered.</p>
<p>Utah <u>SB 189 Independent Contractor Database Act</u></p>	2008	<p>(1) Law creates an independent contractor enforcement council. Council made of representatives from departments/agencies of commerce, labor, workforce services and technology services. 2) Purpose is to create a database that will track independent contractors and</p>

State Legislation or Executive Order	Year Became Law	Description
Utah cont.	2008	compare information between agencies. Also, to study cost of misclassification, and reduce instances of intentional misclassification. Council is also to coordinate enforcement efforts. They are assisted by office of public safety and commissioner of taxation. 3) Annual report to be issued on extent of efforts and degree of misclassification.
Vermont S 196 An Act Relating to Failure to Insure for Workers' Compensation Coverage by Employers and Contractors	2007	(1) Creates a new requirement for a contractor (other than residential), upon request of the state, to submit a "compliance statement" with the number of employees, number of hours on which compensation was paid, classification codes and the name of the insurance carrier and agent. Failure to comply or filing false information results in fines and other penalties. The compliance statement is a public document. (2) State will study (a) establishing a proof-of-coverage website (b) extent of misclassification and cost to workers compensation and (c) effectiveness of state laws to counter misclassification.
S 345 An Act Related to Lowering the Cost of Workers' Compensation Insurance	2008	The law contains provisions about safety and other issues to lower workers compensation premiums. Also: 1) Adds workers compensation fraud into the insurance fraud chapter. 2) Creates a joint enforcement task force that expires in 2010.
Washington HB 2010 An Act Relating to Bidder Responsibility	2007	(1) Bidders and bidders' subcontractors on public works contracts must comply with registration, tax and workers compensation laws. (2) Municipalities given the power to adopt other criteria to judge responsibility. (3) State agencies and municipalities can create "small works rosters" of responsible contractors.
SB 5373 An act relating to unemployment coverage and obligations	2007	(1) Sec. 4 defines who a bona fide officer is for exemption from unemployment. (2) Sec. 8, et. seq. settles co-employment coverage for professional employer organizations and client employers and establishes reporting and registration requirements. (3) Sec. 14, 15 defines temporary staffing agencies and unemployment coverage obligations.
SB 5926 An Act Relating to Creating a Joint Legislative Task Force to Review the Underground Economy in the Construction Industry	2007	Establishes a task force to study the underground economy in construction and to formulate a state policy. Members include legislators, contractor and employee representatives and representatives from the department of labor and industries.
HB 3122 An Act Relating to Consolidating, Aligning, and Clarifying Exception Tests for Determination of Independent Contractor Status	2008	This law applies a uniform definition of independent contractor in the unemployment and workers compensation codes. It also applies other recommendations of the underground economy task force.

Index

Certification required to be an independent contractor
Minnesota Chapt. 135 § 15 (2007), Montana for workers compensation §39-71-419 (2005).

Databases to be used to identify violators
All of the taskforces are studying or requiring information sharing by agencies. Some, though, get technical and specifically require use or creation of databases. See Utah SB 189 (2008). Also, see California SB 869 (2007) which requires comparing companies registered with unemployment tax to those with workers' compensation coverage.

Failure to classify as an employee punished
Illinois PA 95-0026 (2007), Massachusetts GL 149-§148(b) (2004), New Jersey A.4009 (2007).

Misclassification as an independent contractor punished
Connecticut PA 7-89 (2007), Florida S 50A (2003), Kansas §44-766 (2006), Minnesota Sec. 181.722 (2005), Missouri HB1549T (2008), New Mexico SB 657 (2005).

Penalty revenue to enforcement
Again, there are many states that allow for penalty money to fund enforcement. This is a list of newer actions: Colorado HB 1366 (2007), Connecticut PA 7-89 (2007), Florida HB 561 §10 (2006), Illinois PA95-0026 (2007), New Hampshire SB 92 (2007), New Jersey A 4009 (2007).

Penalties, in general
There are a variety of penalties, including criminal, civil, administrative, debarment, suspension or revocation of licenses and stop work orders.

Presumptions of employment
Many states have presumptions of employment, especially in their un-

employment codes, like Louisiana, Tennessee and others. This is a list where the presumptions were either established or re-affirmed: Illinois PA 95-0026 (2007), Minnesota Chapt. 135 § 15 (2007), Montana for workers compensation if no independent contractor certification §39-71-419 (2005), New Jersey A 4009 (2007), Massachusetts GL 149-§148B (2004).

Private cause of action allowed for effects of misclassification or non-reporting

Here are samples of laws that allow employers to bring suit for unfair competition: Connecticut §52-570e (1990), Florida §440-140 (1993). Here are statutes that allow employees to bring suit: Illinois PA 95-0026 (2007), Minnesota SF 69 (2005), New Jersey A 4009 (2007).

Responsible bidder/contractor
Washington HB 2010 (2007).

Stop work orders
Connecticut PA 7-89 (2007), New Jersey A 4009 (2007), New York A 6163 (2007). (Since 1987 Massachusetts has provided for stop work order for employers that fail to secure compensation coverage. Mass. GL 152- §25C(1)-(4). Also, see Florida §440-107 for their stop work order law.)

Task forces
California Unemp. Ins. Code §329 (1995), Connecticut PA 8-156 (2008), Iowa (study only) EO 8 (2008), New Hampshire (study only) HB 500, New Jersey EO 96 (2008), New York EO 17 (2007), Massachusetts EO 499 (2008), Michigan EO 2008-1 (2008), Utah SB 189 (2008), Vermont S 345 (2008), and Washington (study only) SB 5926 (2007).

Tax withholding from independent contractors in the construction industry
Minnesota Chapt. 154 HF 3201 (2008), New Jersey S 468 (2006).

"Universal" definitions of employment
New Hampshire SB 92 (2007), New Jersey A 4009 (2007), Minnesota
Chapt.135 § 15 (2007), Washington HB 3122 (2008).

Workers compensation coverage required, with some exceptions, for
independent contractors

There are numerous states that require employers to have workers com-
pensation insurance for independent contractors/sole proprietors, but
then apply exemptions. Listed here are more recently created laws:
Colorado HB 1366 (2007), Delaware SSI (2007), Florida S 50A
(2003), Montana (if not a certified independent contractor) §39-71-419,
(2005), New Hampshire (on public construction work) HB 471 (2007),
Tennessee HB 1645 (2008).

Workers' compensation premium fraud

Again, many states punish workers-compensation premium fraud spe-
cifically or as an insurance fraud. These are newer state laws address-
ing the problem: Louisiana HB 554 (2008), New Hampshire SB 500
(2008), South Carolina SB 332 (2007), Vermont S 345 (2008).

Appendix 3

Federal and State Actions to Counter Misclassification Fraud
(Capece, 2008)

Federal and State Actions to Counter Misclassification Fraud

November 7, 2008

By: Matthew F. Capece, JD

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For Wisconsin Misclassification Task Force

The failure of construction industry employers to properly classify workers as employees is a priority concern of the United Brotherhood of Carpenters. We welcome the state of Wisconsin's focus on the problem. My comments will focus on how we see the practice being carried out and to survey the solutions sought so far by federal and state authorities. I will not take much space describing the degree and effects of fraud, because that road has already been well traveled.¹ The paper will conclude with recommendations.

Construction is a very competitive business with contracts frequently awarded to low bidders. Unscrupulous employers that fail to pay employment taxes, workers compensation premiums and overtime can save 30 percent or more on labor costs; allowing them to underbid their law-abiding competition. The impact of illegitimate operators can be dramatic. For instance, the Fiscal Policy Institute released a study in December 2007 on illegal employment practices in the New York City construction market.² They found that 50,000 of 200,000 construction employees were either misclassified or paid off the books, resulting in an estimated cost of \$557 million in lost federal, state and local income taxes, employment taxes, workers compensation premiums and health care cost shifting for injured workers.³

Fraud in the construction industry-How it's done

The misclassification fraud we see in the construction industry comes in two forms. First, there are the employers who intentionally misclassify employees as independent contractors and report their payments to the Internal Revenue Service and the workers with 1099 misc. forms. Second are the employers who pay their workers by check or cash and do not report their payments as the law requires to insurers, state and federal authorities. This latter method can be the response to increased enforcement of 1099 misclassification or other labor, tax and immigration laws. It is also the method that is the most challenging to law enforcement because transactions are hidden.

¹ See, *Size and Cost of Misclassification Fraud and Unreported Pay: Survey of National and State Studies*, by Matthew F. Capece, United Brotherhood of Carpenters (August 10, 2008) and Misclassification Web Site, United Brotherhood of Carpenters at www.carpenters.org/misclassification.

² *Building Up New York, Tearing Down Job Quality: Taxpayer Impact of Worsening Employment Practices in New York City's Construction Industry*, Fiscal Policy Institute (New York City Construction) (December 2007).

³ *Ibid.*, pp. 1, 20.

Typically on the state level we see enforcement come from audits by unemployment tax and workers compensation compliance investigators of employers that pay into the system. That becomes complicated when employers chose not to participate at all, employee contact information is not kept, purported construction companies use fake addresses and primary contractors use subcontractor agreements to shield themselves from liability. When this occurs, the effect can be devastating. Take, for instance, the following information from Florida. Note that Florida has very strong state law on workers-compensation premium fraud, racketeering and money laundering.

In three years one billion dollars of cash was funneled by just ten construction companies through check cashing businesses into the Florida construction industry.⁴ The largest loss was workers compensation premiums-about \$200 million.⁵ That is according to a 2007 presentation by the Florida Department of Financial Services Division of Insurance Fraud and the Eighteenth Statewide Grand Jury report on money laundering by check cashers released in March of 2008.⁶ The net result was a loss of \$409 million in workers compensation premiums and state and federal employment taxes.⁷

The Eighteen Statewide Grand Jury and reports by the Division of Insurance Fraud describe a sophisticated workers compensation premium fraud scheme.⁸ We have taken those descriptions as well as those of recent prosecutions and indictments by the US Attorney's Office in South Florida along with press reports and information from our interviews of carpenters and contractors to construct the following summary.⁹

⁴ *Eighteenth Statewide Grand Jury, Second Interim Report of the Statewide Grand Jury, Check Cashers: A Call for Enforcement*, Case No SC 07-1128, p. 13 (West Palm Beach, FL, March 2008)(hereinafter Grand Jury Report)

⁵ Presentation by the Florida Department of Financial Services Division of Insurance Fraud to the Florida Workers' Compensation Fraud Task Force, slides 31 and 32 (January 10, 2007). The presentation can be found at <http://www.fldfs.com/fraud/presentations/WorkersCompTaskForce.htm> (hereinafter Task Force Presentation).

⁶ Grand Jury Report, p. 13 and Task Force Presentation, slides 31 and 32.

⁷ Task Force Presentation, slides 31 and 32.

⁸ Grand Jury Report, pp. 10-14 and *Joint Report to the President of the Florida Senate and the Speaker of the Florida House of Representatives*, The Florida Department of Financial Services (January 1, 2007 and January 1, 2008), p. 1.

⁹ See, *South Florida Men Sentenced in \$15 Million Check Cashing Fraud: Criminal Charges Include Racketeering, Grand Theft, Workers Compensation Fraud, Money Laundering*, Press Release, Attorney General Bill McCollum (October 30, 2008), *CFO Sink Uncovers Fraudulent Check-Cashing Scheme; Delivers \$325,000 in Restitution*, Press Release, Florida Department of Financial Services (September 3, 2008), *Construction Company Owner Pleads Guilty to Federal Payroll Tax Evasion Conspiracy*, Press Release, US Attorney's Office, Southern District of Florida (August 22, 2008), *Construction Company Owner Sentenced to 10 years for Payroll Tax Evasion*, Press Release, US Attorney's Office, Southern District of Florida (February 25, 2008), *Broward County Tax Preparer Sentenced for Tax Fraud Related to Workers' Compensation Insurance Scheme*, Press Release, US Attorney's Office, Southern District of Florida (February 7, 2008), *Florida Framing Contractors Sentenced to Probation in Scheme to Avoid Payroll Tax*, *Bureau of National Affairs, Construction Labor Report*, vol 53, no. 2640, p. 1003 (October 3, 2007), *Undocumented Workers Paying Tab for S Florida Fraud*, *WorkCompCentral* (September 29, 2006)

A primary interior systems contractor supplements its workforce with a labor subcontractor. The labor subcontractor provides labor only, and may be an individual with a crew of workers. (Typically, these subcontractors are not licensed employment leasing services.) To protect itself from liability, the primary contractor needs a corporate identity and a workers compensation policy for the labor subcontractor.

A person we will call a "facilitator" provides a shell company identity and an insurance policy. The shell company exists in the records of the secretary of state, but the address for the company may be bogus or the purported officers have no involvement in the daily activities of running a construction business. The facilitator "rents" the construction company to the labor subcontractor. (The shell company may even be used by many subcontractors who do not know one another on different projects in the state.)

Workers compensation premiums are based upon the amount of payroll, the type of work performed and the claims experience of the employer. The facilitator secures the workers compensation policy from an insurance agent that only covers a fraction of the true payroll. The larger, true, payroll is not revealed to the insurance carrier. The labor subcontractor gets an insurance certificate. Insurance certificates for workers compensation do not reveal work classification codes, nor do they reveal payroll information. (Those are on the information page of the insurance policy which is not required to be disclosed to the primary contractor.)

The labor subcontractor can now provide the primary contractor with an insurance certificate showing workers compensation coverage and a corporate identity. The labor subcontractor receives checks in the name of the shell company. The checks are brought to a designated check cashing store. (Transactions over \$10,000 are required to be described in currency transaction reports (CTRs) to the US Treasury Department. They are shared with state authorities.) The CTRs are not filed or they are falsified by the check cashing business. A percentage of the check, larger than what the law provides, is shared by the check cashing store and the facilitator. The labor subcontractor is given cash and the cash is given to the workforce. (Sometimes, the labor subcontractor deducts from the workers' pay a portion of the percentage taken by the facilitator and check cashing store.)

The Internal Revenue Service does not know how much money was given by the primary contractor to the labor subcontractor. Nothing in federal law requires reporting to the IRS by a corporation of the amount of money paid to another corporation.¹⁰ The amount paid to the subcontractor is lumped into the primary contractor's business deductions. That leaves the facilitator's accountant free to underreport on the quarterly employment-tax reports and yearly returns for the shell company. In our example, let's say, in the course of a year the primary contractor pays the labor subcontractor \$1 million. The accountant only reports \$150,000 paid for the services performed by three employees. The rest, \$850,000, is left to be paid in unreported cash.

¹⁰ See, *General Explanations of the Administration's Fiscal Year 2009 Revenue Proposals*, Department of the Treasury (February 2008), p. 63, *General Explanations of the Administration's Fiscal Year 2008 Revenue Proposals*, Department of the Treasury (February 2007), p. 63.

That is how, in a large construction market like Florida's, just ten contractors can generate \$1 billion dollars of unreported cash in a short amount of time. There are variations to the scheme with various degrees of culpability. The facilitator may be the primary contractor or the check cashing store. The labor subcontractor may operate under a "real" corporate identity, but use shell companies to pay its foremen's crews. Certainly, though, these transactions don't arise from legitimate entrepreneurship or confusion over the requirements of the law. This is organized crime.

And it happens on all types of construction projects-single-family residential, hospitals, schools and \$100 million condominium towers. The Eighteenth Statewide grand jury concluded its description of workers' compensation premium fraud with the following:

"In the short term, it may be prudent for the legislature to inquire of the [construction] industry, when considering this Grand Jury's recommendations, why they have apparently decided over the last few years to move increasingly to an all cash payroll."¹¹

Florida isn't the only state where this is happening. We have seen variations of the fraud scheme in Nevada, Massachusetts, Connecticut, New York, Louisiana, Georgia, Virginia, Maryland, Idaho, Washington and in other states. The violations of the law we see not only include employment and tax law, they also include money laundering, racketeering, grand theft, mail fraud, wire fraud and insurance fraud.

Attached are summaries of state, federal, university and other studies of misclassification fraud. Given the methodology of the studies and the anecdotal information we see in states like Florida, the estimates of the size and cost of the fraud in most of the studies are conservative. Taken together, what the studies do say is that fraud is a serious problem in the construction industry, it reduces government revenue, shifts tax and workers-compensation insurance costs to law-abiding employers,¹² lowers working conditions and steals jobs from legitimate employers and their employees.

Federal response

Misclassification fraud has caught the attention of the federal government. The IRS has initiated an information sharing and joint unemployment tax auditing program with a majority of states following recognition that misclassification is part of the \$345 billion

¹¹ Grand Jury Report, p. 14

¹²For a good discussion on cost shifting due to workers compensation premium fraud read: *Fraud in Workers' Compensation Payroll Reporting: How Much Employer Fraud Exists and How are Honest Employers Impacted*: Report for the Commission on Health and Safety and Workers' Compensation, by Frank Neuhauser and Colleen Donovan, University of California, Berkeley (August 2007), pp 1-3 and 7.

federal tax gap.¹³ In addition, misclassification in the construction industry has been identified as a 2008 enforcement priority by the US Department of Labor.¹⁴

There are four pieces of pending federal legislation:

S. 2044 Independent Contractor Proper Classification Act of 2007: This bill was introduced by Senator Obama (Ill.) in September 2007. The legislation amends the revenue code's safe harbor provisions which allow misclassification in certain instances. The bill reduces the number of safe harbors and further limits their application. It allows the IRS to issue regulations on employment status. A process for determining employment status is created that protects workers from retaliation. Treasury and Labor are required to share information and issue annual reports on their law enforcement work related to misclassification. Labor has to focus on industries where the practice is prevalent.

HR 5804 Taxpayer Responsibility, Accountability and Consistency Act: This bill was introduced in April of 2008 by Rep. McDermott (WA), Rep. Tierney (MA) and Representative Neal (MA). Reporting of corporate to corporate transactions to the IRS is required. (This is also an administration proposal.)¹⁵ The bill reduces the number of safe harbors and further limits their application. It allows the IRS to issue regulations on employment status. A process for determining employment status is created that protects workers from retaliation. Treasury is required to issue annual reports on their law enforcement work related to misclassification and to inform Labor about discoveries of misclassification.

HR 6111 Protecting Workers from Misclassification Act and S 3648 Employee Misclassification Prevention Act: The House bill was introduced by Rep. Andrews (NJ) and Rep. Woolsey (CA) in May 2008. Its companion in the Senate was introduced in October 2008 by Senators Kennedy (MA), Obama (MA) and Kerry (MA). The bills makes it a violation to fail to properly classify an individual as an employee. Employers of independent contractors would have to keep records of their use and notify them of their status. Labor is required to keep a web site that summarizes employee rights under federal law. State labor departments are required to establish auditing and investigative plans to identify employers that misclassify employees or pay unreported compensation. Reports from the states on their plans and enforcement efforts are to be made to Labor. Information on violators may be shared by Labor with IRS if appropriate. Labor's wage and hour division has to target audits in non-compliant industries.

¹³ This is the Questionable Employment Tax Practices program. See information at: <http://www.irs.gov/newsroom/article/0,,id=175457,00.html> and *IRS Entering Accord with States to Target Worker Misclassification for Examinations*, Daily Labor Report, Bureau of National Affairs, No. 94, p. A-4, Wednesday, May 16, 2007.

¹⁴ *Wage and How Collects a Record \$220 Million in Back Wages for Over 341,000 Employees in Fiscal Year 2007*, US Department of Labor, p. 5, available at: <http://www.carpenters.org/misclassification/ALL%20DOCUMENTS/DOL%20WHD%202007%20Statistics%20Fact%20Sheet-misclassification%20as%20IC%20a%202008%20focus.pdf>.

¹⁵ See fn. 7

State Response

State legislators and executives have been taking action. Attached is a compilation of state initiatives including laws and executive orders that impact enforcement of state wage and employment tax laws.¹⁶ What I've done here is index the laws by subject matter. The index isn't exhaustive, but it hits the high points. Refer to the attached list if you want to see them indexed by state.

Certification required to be an independent contractor

Minnesota Chapt.135 § 15 (2007), Montana for workers compensation §39-71-419.

Conspirators, other than direct employer, specifically punished:

Florida §440.105

A flaw of the Illinois bill is that it specifically says that contractors will not be liable for the actions of their subcontractors. PA95-0026 §10(f) (Ill. 2007) It may only mean that there isn't strict liability, so existing conspiracy laws will apply. It will take a judge to figure that one out.

Databases to be used to identify violators

All of the task forces are studying or requiring information sharing by agencies. Some, though, get technical and specifically require use or creation of databases. See Utah SB 189 (2008). Also, see California SB 869 (2007) which requires comparing companies registered with unemployment tax to those with workers' compensation coverage.

Failure to classify as an employee punished

Illinois PA95-0026 (2007), Massachusetts GL 149-§148B, New Jersey A4009 (2007).

Misclassification as an independent contractor punished

Connecticut PA 7-89 (2007), Florida §440.107(7)(f), Kansas §44-766 (2006), Minnesota Sec. 181.722 (2005), Missouri HB1549T (2008), New Mexico SB657 (2005).

Penalty revenue to enforcement

Again, there are many states that allow for penalty money to fund enforcement. This is a list of newer actions: Colorado HB 1366 (2007), Connecticut §31-69a (1994) also in PA 7-89 (2007), Florida HB 561 §10 (2006), Illinois PA95-0026 (2007), New Hampshire SB 92 (2007), New Jersey A4009 (2007).

Penalties, in general

There are a variety of penalties, including criminal, civil, administrative, debarment, loss of licenses and stop work orders.

Presumptions of employment

Many states have presumptions of employment, especially in their unemployment codes, like Louisiana, Tennessee, Maryland and others. This is a list where the presumptions

¹⁶ Prevailing rate laws, though, are not included. They have not been included, because they have been the subject of legislation for many years, so they are numerous. The point of this research is to track efforts effecting the more basic laws affected by misclassification fraud. Those actions have been in an upswing.

were either established or re-affirmed: Illinois PA95-0026 (2007), Minnesota Chapt. 135 §15 (2007), Montana for workers compensation if no independent contractor certification §39-71-419 (2005), New Jersey A4009 (2007), Massachusetts §149-148B.

Private cause of action allowed for effects of misclassification or non-reporting

There are many states that, for instance, allow employees to bring private suits to collect unpaid wages. Below are statutes that apply more directly to the effects of misclassification fraud. Here are samples of laws that allow employers to bring suit for unfair competition: Connecticut §52-570e (1990), Florida §440-140 (1993). Here are statutes that allow employees to bring suit: Illinois PA95-0026 (2007), Minnesota §181.722 (2005), New Jersey A4009 (2007).

Responsible bidder/contractor laws for permitting/registration and public construction

There are numerous state and local laws with criteria for bidders on public work. What is less common are laws that address the contractor's labor and employment tax law performance. In New England states there are numerous local ordinances that do that and, especially in Ohio, require registration and compliance with workers compensation and local income tax laws. There have been some arguments that state laws do not allow municipalities or other public entities to take those items into consideration for bidders on public contracts. Here are two examples of state actions that enable consideration of labor and employment tax issues for bidders: Ohio Res. 07-98 School Facilities Commission (2007) and Washington HB 2010 (2007).

Stop work orders

Connecticut PA 7-89 (2007), Florida §440-107, Massachusetts GL 152§25C, New Jersey A4009 (2007), New York A 6163 (2007).

Task Forces

California Unemp Ins Code §329 (1995), Connecticut PA 8-156 (2008), Iowa (study) EO 8 (2008), New Hampshire (study) SB 500, New Jersey EO 96 (2008), New York EO 17 (2007), Massachusetts EO 499 (2008), Michigan EO 2008-1 (2008), Utah SB 189 (2008), Vermont S 345 (2008), West Virginia (by internal collaboration), Washington (study) SB. 5926 (2007) and Wisconsin (study, done my internal collaboration).

Tax withholding from independent contractors in the construction industry

Minnesota Chapt. 154 HF 3201 (2008), New Jersey S 468 (2006).

"Universal"¹⁷ definitions of employment

New Hampshire SB 92 (2007), New Jersey A4009 (2007), Minnesota Chapt.135 § 15 (2007), Washington HB 3122 (2008).

Workers compensation coverage required, with some exceptions, for independent contractors

¹⁷ To fit into this category, the law had to apply to more than one code-workers compensation and unemployment, for instance.

There are numerous states that require employers to have workers compensation insurance for independent contractors/sole proprietors, but then apply exemptions. Listed here are more recently created laws: Colorado HB 1366 (2007), Delaware SS1 (2007), Florida §440-02(15)(c)(3) or S 50A (2003), Montana (if not a certified independent contractor) §39-71-419, New Hampshire (on public construction work) HB 471 (2007), Tennessee HB 1645 (2008).

Workers' compensation premium fraud

Again, many states punish workers-compensation premium fraud specifically or as an insurance fraud. These are newer state laws addressing the problem: Louisiana HB 554 (2008), New Hampshire SB 500 (2008), South Carolina SB 332 (2007), Vermont S 345 (2008).

Enforcement actions

We have not seen an abundance of enforcement activity coming from these laws and initiatives, because they are new. But, there have been impressive results in, for instance, in Connecticut,¹⁸ Massachusetts¹⁹ and New York.²⁰ In general, we are seeing increased interest and the number of enforcement actions growing under new and existing laws, including private actions in, for example, Washington.²¹

Much of the Florida law on workers compensation premium fraud and stop work orders has been in existence for many years and there are many well documented cases.²² We are seeing in Florida an increased number thorough investigations by state and federal authorities that have impacted co-conspirator insurance brokers, accountants, check cashing stores, subcontractors and contractors. Those actions can serve as a model in other states. Despite the enormous magnitude of the problem there, increased enforcement has contributed to lowering of workers' compensation costs in the construction industry.²³

See the United Brotherhood of Carpenters web site at www.carpenters.org/misclassification for news and other reports of enforcement actions.

¹⁸ "Stop Work" Legislation Puts Brakes on Employers Trying to Avoid State Laws, Connecticut Department of Labor News Release (August 13, 2008).

¹⁹ *Construction Company Pleads Guilty to Premium Evasion, Payroll Fraud*, WorkCompCentral (March 24, 2008) and *[Massachusetts] AG Issues Advisory to State Employers on Complying with Worker Classification*, Bureau of National Affairs Construction Labor Report, vol. 54, no. 2670, p. 1988 (May 7, 2008).

²⁰ See fn 10 and *Workers' Comp Board Issues 1,000th Stop Work Order: Businesses That Refuse to Carry Comp Face Closure*, Workers Comp. Board Press Release (NY September 2, 2008).

²¹ See, e.g., the examples on the United Brotherhood of Carpenters Misclassification Fraud web site at www.carpenters.org/misclassification and *King County Court Approves Settlement of \$635,000 in Drywallers' Class Action*, Bureau of National Affairs Construction Labor Report, vol. 53, no. 2637, p. 910 (September 12, 2007).

²² See, e.g., *Florida Busts 25 Job Sites in Panhandle*, WorkCompCentral (August 8, 2007) and *Joint Report to the President of the Florida Senate and the Speaker of the Florida House of Representatives*, The Florida Department of Financial Services (January 1, 2007 and January 1, 2008).

²³ *2007 Workers' Compensation Annual Report*, Florida Office of Insurance Regulation, p. 25 (January 1, 2008).

Recommendations

There has been growing activity over the past few years on the federal and state levels. While new legislation is welcome for strengthening laws and creating more enforcement tools, that legislation and existing laws are of no use without adequate support and coordination of the law enforcement personnel needed to get the job done.

With that in mind, here are our recommendations for Wisconsin:

Stop Work Orders

The majority of states that have stop work orders use them for employers who violate workers' compensation coverage requirements. For instance, if an employer has no workers compensation insurance or is committing premium fraud (paying premiums on only a portion of their employees) a state investigator can issue an order immediately stopping that employer from continuing to do business until they come into compliance and pay their fine. The employer is entitled to a hearing to challenge the order. The states that do this now are Florida, New York, Connecticut and Massachusetts. (The Massachusetts law, though, doesn't apply to premium fraud.) New Jersey enacted stop work orders as part of a larger anti-fraud bill in 2007, and their stop work orders apply to the failure to properly classify an individual as an employee. The constitutionality of the Florida law has been challenged, and the law was upheld.²⁴

Florida credits its law enforcement, which includes stop work orders, for playing a large role in decreasing workers' compensation rates.²⁵ The Connecticut law is new, but it is having a positive impact and the support of construction industry employers.²⁶ Stop work orders are a powerful law enforcement tool.

In Wisconsin, stop work orders can be applied to workers compensation requirements, unemployment tax or state withholding tax laws. Current field auditors for those divisions can use it without adding additional personnel. It will increase compliance with workers' compensation laws and increase unemployment and income tax revenue.

Law Enforcement Task Force

Law enforcement task forces to fight labor and employment tax fraud have been established in California, Connecticut, New Jersey, New York, Massachusetts, Michigan, Utah and Vermont. The task forces are charged with sharing information, coordinating enforcement, educating the public and recommending any needed changes to existing law. The task forces have been either put into place by executive order or legislation. Included in the task forces are representatives from the following departments/agencies: labor, revenue, attorney general, licensing, workers compensation, employment security and state police.

²⁴ *Riopelle v. Dept. of Financial Services, Div. of Workers' Compensation*, 30 FlaWeekly D 1601, 907 So.2d 1220, 2005 Fla.App.LEXIS 100001 (Fla. 1st Dist. Ct. App. 2005).

²⁵ See fn. 25.

²⁶ *New Law Shuts Down Dozens of Work Sites*, Connecticut Law Tribune (September 29, 2008).

In just four months the New York misclassification task force found \$19.4 million in unreported wages, 2,078 misclassified workers, and assessed \$1.4 million in unemployment taxes, penalties and interest. If possible, it gets more shocking. They found 646 employees owed \$3 million in wages.²⁷

The same can certainly be done in Wisconsin using existing resources and dedicated prosecutors. We would recommend establishing a task force with legislation and add to the group representatives from insurance regulation, banking regulation and a district attorney representative.

Additional Authority for Building Inspectors

The government representatives who have the most contact with construction contractors and sites are building inspectors. Give them the authority to request to see workers compensation certificates and quarterly unemployment tax reports. Suspected problems can then be reported by the inspectors to the appropriate law enforcement agencies.

Require Independent Contractor Certification

Minnesota has a good model for an independent contractor certification law.²⁸ A construction worker must be treated as an employee unless the worker holds a state independent contractor certificate. There are protections in the statute that revoke certificates if applications are falsified or if the holder truly doesn't fit the statutory definition of an independent contractor. Regulations have been issued and it is coming into effect January 1, 2009. Application fees and increased revenue are expected to cover the cost of administration.

Conclusion

We are seeing unscrupulous employers supersede legislatures by using market-place competition to unilaterally repeal over a hundred years of labor and employment tax laws. To accomplish that, they rely on weaknesses in the law and a patch-work quilt of law enforcement.

Given the harm misclassification fraud has done to the construction industry, the lost revenues and associated criminal activity, the issue is important enough for legislators, enforcement agencies, state attorney generals and local prosecutors to make it a priority. It is certain that there is a significant amount of uncollected income taxes, unemployment taxes and workers compensation premiums in the construction industry. We can expect enforcement to increase as federal and state governments struggle more with their bottom line during the current economic downturn.

It is important to note that efforts to bring order to the construction industry are not only welcomed by employee organizations, they are also supported by employers.²⁹ We are

²⁷ *Report of the Joint Enforcement Task Force on Employee Misclassification to Eliot Spitzer, Governor State of New York* (February 1, 2008), pp. 3-4, and 11-13

²⁸ Minn.Stat. §181 723 (2008).

²⁹ See, e.g., *Testimony of Scott Morrissey, Owner Red Line Wall Systems, Inc., Commercial Drywall and Metal Stud Installation Company* before the US Senate Committee on Small Business & Entrepreneurship

not seeking new employment benefits-only better enforcement of what the law already requires, fair competition and more vigilance by the construction industry.

Appendix 4

Department of Commerce Emergency Rule Materials

DEPARTMENT OF COMMERCE
EMERGENCY RULE RELATING TO
BUILDING CONTRACTORS

Finding of Emergency

The Department of Commerce finds that an emergency exists within the state of Wisconsin and that adoption of an emergency rule is necessary for the immediate preservation of the public health, safety and welfare. A statement of the facts constituting the emergency is as follows:

1. Under Chapter 560 of the Statutes, the department of commerce is charged with facilitating the establishment and retention of business enterprises in Wisconsin, and with seeking closer cooperation and coordination between units of state government, so that the economy of the state may continue to develop fully and meet citizen and community needs.
2. Under Chapters 101 and 145 of the statutes, the department of commerce has oversight over the design, construction, alteration and maintenance of public buildings and places of employment, one- and two- family dwellings, public swimming pools and public water attractions in order to protect public safety, health and welfare and the waters of the state.
3. The department has proposed an administrative rule that would require the registration of various types of building contractors not already credentialed by the department under existing administrative rules. Under the proposed rules contractors must be registered with the department by January 1, 2010. A public hearing on that proposal was held on January 21, 2009.
4. The proposed rule has three main benefits to Wisconsin: first, it will enhance the department's ability to communicate with and educate building contractors throughout the state about their obligations to limit safety and health risks for the citizens of Wisconsin; second, it will enhance the ability of the department to cooperate and coordinate with the Department of Workforce Development relative to their administration of unemployment insurance and workers compensation insurance programs; and third, it will enhance the ability of the department to cooperate and coordinate with the Department of Revenue relative to their administration of the state income tax program.
5. Due to the current economic circumstances, the department has determined that the implementation for building contractor registration should be July 1, 2009 in order for the benefits to be in effect for the 2009 building construction season.

Pursuant to section 227.24, Stats., this rule is adopted as an emergency rule to take effect upon publication in the official state newspaper, except for ss. Comm 5.30 (1) and Comm 61.295 (2) which shall take effect on July 1, 2009.

Dated at Madison this _____
day of _____, 2009,
by the Department of Commerce.

Richard J. Leinenkugel, Secretary

The Wisconsin Department of Commerce adopts an order to create Comm 5.01 (4) (h), Comm 5.02 Table 5.02 line 8m., Comm 5.02 Table 5.02 footnote a, Comm 5.06 Table 5.06 line 8m., Comm 5.30 and Comm 61.295 relating to building contractors and affecting small business.

Analysis of Rule

1. Statutes Interpreted

Statutes Interpreted: ss. 101.02 (1), 101.02 (4), 101.02 (13) (b), 101.02 (15) (a), (b), (f), (h), (k) and (L), 101.12 (3) (h), 101.19 (1) (f), 101.63 (1), 145.02 (2) and (3), 560.01 (1) and (2), and 560.02 (4), Stats.

2. Statutory Authority

Statutory Authority: ss. 101.02 (1), 101.02 (4), 101.02 (13) (b), 101.02 (15) (a), (b), (f), (h), (k) and (L), 101.12 (3) (h), 101.63 (1), 145.02 (2) and (3), 560.01 (1) and (2), and 560.02 (4), Stats.

3. Related Statute or Rule

Statutes: 101.148, 101.178, 101.654, 101.862, 101.94, 101.95, 101.951, 101.96, 101.985 (1), and 895.07 (13)
Administrative Rules: Comm 5.31, 5.32, 5.323, 5.327, 5.41, 5.42, 5.70 and 5.9905

4. Explanation of Agency Authority

Under chapter 560 of the Wisconsin Statutes, the Department of Commerce is charged with facilitating the establishment and retention of business enterprises in Wisconsin, and seeking closer cooperation and coordination between units of state government, so that the economy of the state may continue to develop fully and meet citizen and community needs.

Under chapters 101 and 145 of the Wisconsin Statutes, the Department of Commerce also protects public health, safety, and welfare by promulgating comprehensive requirements for design, construction, use and maintenance of public buildings and places of employment, public swimming pools and water attractions and adopts rules that establish uniform, statewide standards for the construction of one- and 2-family dwellings. Various construction trades are involved in building or modifying these types of structures. Together with building owners and designers, construction trades share a responsibility to ensure that the buildings, relative to the respective trade's work, do not pose risk to public health and safety.

The registration would enhance the department's communication, education and oversight efforts for those businesses that contribute in various ways and aspects to the creation or alteration of buildings that limit the safety and health risks for the citizens of Wisconsin. Utilizing the registry of building contractors the department will more efficiently and effectively inform contractors about safety regulations and consumer protection regulations, such as the consumer notice required under s. 101.148 (2), Stats., pertaining to procedures for addressing construction defects.

The department recognizes that by registering Wisconsin building contractors and subcontractors, information pertaining to such registrants can be posted on the internet and made available to the Wisconsin Departments of Workforce Development and Revenue for use in their administration of unemployment insurance, workers compensation insurance and income tax programs, respectively. The registry of building contractors can be used by the aforementioned agencies to reinforce their efforts to minimize the misclassification of employees and to maximize proper participation in unemployment insurance and workers compensation insurance programs and proper payment of income taxes.

5. Summary of Proposed Rules

The proposed rules require a registration credential for various building contractors who are involved in the construction or modification of public buildings and places of employment and one- and 2-family dwellings, unless the contractor already holds another type of contractor credential issued by the department. The registration credential is for a contracting business and is not required for each partner or employee who is involved with physically constructing or modifying the structures.

6. Summary of, and Comparison with, Existing or Proposed Federal Regulations

An internet-based search of the code of federal regulations and the federal register did not identify any federal requirements relating to contractor registrations.

7. Comparison with Rules in Adjacent States

An Internet-based search for the states of Illinois, Iowa, Michigan and Minnesota found the following:

Illinois:

The state of Illinois does not have any regulations regarding the licensure of building contractors, except roofers

Iowa:

The state of Iowa requires all individual contractors and businesses performing construction work in Iowa to be registered. The fee is \$25 for a two year registration. The prerequisites for registration include the demonstration of compliance with worker's compensation insurance requirements and compliance with unemployment tax requirements.

Michigan:

The state of Michigan requires licenses for persons and businesses that contract with property owners to build new homes or remodel homes. The license types are: Residential Builder, and Maintenance and Alteration Contractor. The Maintenance and Alteration Contractor is restricted to perform only specific trades and services for which they are licensed. The fee is \$225 for a three year license. Applicants for the license must complete 60 hours of approved education and pass an examination. Michigan does not have a licensing law regulating builders of commercial buildings.

Minnesota:

The state of Minnesota requires certifications for persons and businesses that contract with property owners to construct or improve dwellings for habitation by one to four families and where the person or business is involved with two or more special building skills. The Residential Contractor license and Remodeler license are annual licenses. The fees, which are based upon gross receipts, are \$260 to \$360. The application for the license must include a qualifying person who must take the required examination and fulfill the continuing education requirements for the licensee.

Also under the Minnesota Independent Contractor Certification Law, as of January 1, 2009, a certification is required for building contractors where contractors must establish that they are independent contractors versus employees utilizing the "9 Items" test related to Worker's Compensation. The fee for a two year certification is \$250.

8. Summary of Factual Data and Analytical Methodologies

The registration provisions of the proposed rules were developed by analyzing and comparing the current administrative rules under chapter Comm 5 for other types of building contractors currently licensed, certified or registered by the department. The concept of the contractor registration was developed in light of proposed Wisconsin legislation under 2007 SB 228 and AB466, and with consideration of legislation in the states adjacent to Wisconsin.

9. Analysis and Supporting Documents used to Determine Effect on Small Business or in Preparation of Economic Impact Report

The proposed rules require the registration of individuals and entities that act as building contractors or subcontractors who are involved in the construction or modification of public buildings, places of employment and one- and 2- family dwellings and who are not already credentialed by the department. The department currently credentials several contracting trades, including dwelling contractors, HVAC contractors, electrical contractors and elevator contractors. The rules would apply to those persons and entities engaged in the business of commercial general construction, drywall, plastering, electrical wiring, finish carpentry, flooring, framing carpentry, glass and glazing, insulation, masonry and stone work, plumbing, concrete work, roofing, siding, building site preparation and/or stabilization, structural steel, tile and terrazzo, wall coverings, and other building or equipment specialties.

The department estimates that the number of contractors to be registered under the rules would be 30,000. A contractor registration would cost \$100 for a 4-year term if applied for electronically and \$115 if applied for via paper. The department does not believe that this registration and fee would pose a significant impact on businesses.

An economic impact report has not been required to be prepared.

10. Agency Contact.

Robert DuPont, Bureau Director, robert.dupont@wisconsin.gov, (608) 266-8984

11. Public Hearing Comments.

The hearing record on this emergency rule will remain open until April 10, 2009. Written comments on the proposed may be submitted to James Quast, at the Department of Commerce, P.O. Box 2689, Madison, WI 53701-2689, or Email at jim.quast@wisconsin.gov.

SECTION 1. Comm 5.01 (4) (h) is created to read:

Comm 5.01 (4) (h) Building contractor.

SECTION 2. Comm 5.02 Table 5.02 line 8m. is created to read:

Partial Table 5.02

Table 5.02
FEES

	License, Certification or Registration Category	Type	Application Fee	Examination Fee	License, Certification or Registration Fee
	Subchapter III				
8m.	Building Contractor	Registration	\$15 ^a	NA	\$100

SECTION 3. Comm 5.02 Table 5.02 footnote a is created to read:

^a No fee if application is submitted electronically; \$15 application fee for a late renewal per s. Comm 5.07 (2) (b)
1. a.

SECTION 4. Comm 5.06 Table 5.06 line 8m is created to read:

Partial Table 5.06

Table 5.06
TERMS

	License, Certification or Registration Category	Term	Expiration Date	Continuing Education Cycle
	Subchapter III			
8m.	Building Contractor	4 years	Date of Issuance	NA

SECTION 5. Comm 5.30 is created to read:

Comm 5.30 Building contractor. (1) GENERAL. (a) Except as provided in par. (b), no person or entity may engage in a construction business or offer to engage in a construction business that affects public buildings, places of employment, one- and 2- family dwellings, public swimming pools and water attractions, unless the person or entity holds a registration issued by the department as a registered building contractor.

(b) Paragraph (a) does not apply to any of the following:

1. A person or entity that holds any of the following credentials issued by the department:

a. A dwelling contractor certification.

b. A dwelling contractor – restricted certification.

- c. A manufactured home manufacturer license.
 - d. A manufactured home dealer license.
 - e. A manufactured home installer license.
 - f. An electrical contractor certification.
 - g. An electrical contractor – restricted certification.
 - h. An HVAC contractor registration.
 - i. An elevator contractor license.
2. A person or entity that works only on real estate or property they own or lease.

(c) Under this section:

1. "Construction business" means a trade that installs, alters or repairs any building element, component, material or device that is regulated under the commercial building code, chs. Comm 60 to 66, the uniform dwelling code, chs. Comm 20 to 25, the electrical code, ch. Comm 16, the plumbing code, chs. Comm 81 to 87, or the public swimming pools and water attractions code, ch. Comm 90. The term does not include the delivery of building supplies or materials, or the manufacture of a building product not on the building site.

Note: Examples of construction businesses that are to register:

Building site preparation/stabilization	Masonry and stone work
Drywall and plastering	Plumbing
Electric Wiring	Poured concrete foundations and structures
Finish carpentry	Precast concrete
Fire protection	Public swimming pools and water attractions
Flooring	Roofing
Framing carpentry	Siding
General building construction	Structural steel
Glass and glazing	Tile and terrazzo
Insulation	Wall coverings
	Other building or equipment specialties

2. "Dwelling unit" means a structure or that part of a structure which is used or intended to be used as a home, residence or sleeping place by one person or by 2 or more persons maintaining a common household, to the exclusion of all others.

3. "One- and 2- family dwelling" means any building that contains one or 2 dwelling units that construction of which commenced on or after December 1, 1978.

(2) APPLICATION FOR BUILDING CONTRACTOR REGISTRATION. A person applying for a building contractor registration shall submit all of the following:

- (a) An application in accordance with s. Comm 5.01.
- (b) An application fee and a registration fee in accordance with s. Comm 5.02, Table 5.02.

(c) The social security number or federal employer identification number for the business.

(d) A statement certifying compliance with worker's compensation requirements under ch. 102, Stats., and unemployment compensation requirements under ch. 108, Stats.

(3) QUALIFICATIONS FOR REGISTRATION. The person applying for a building contractor registration shall be the owner of the construction business, a partner in the construction business applying on behalf of a partnership, or the chairman of the board or chief executive officer applying on behalf of the construction corporation.

(4) RESPONSIBILITIES. A person or entity that holds a building contractor registration shall do all of the following:

(a) Include their registration number on all construction bids and contracts.

(b) Not contract with another person or entity to engage in construction business activities unless the person or entity holds a credential under sub. (1) (a) or (b) 1.

(c) Not commence a construction business activity until a permit is issued for the construction for any project that requires a uniform building permit under s. Comm 20.08.

(d) Not commence a construction business activity until a permit is issued for the construction for any project that requires a municipal building permit involving a public building, a place of employment or a one- or 2- family dwelling.

(e) Not commence a construction business activity until plan approval has been obtained as required under ss. Comm 61.30, 82.20, 83.22, or 90.04.

(5) RENEWAL. (a) A person may renew a building contractor registration.

(b) A building contractor registration shall be renewed in accordance with s. Comm 5.07.

SECTION 6. Comm 61.295 is created to read:

Comm 61.295 Administrative coordination. (1) Pursuant to ss. 101.02 (13) (b) and 101.12 (3) (h), Stats., if plans are required to be submitted to the department for review under s. Comm 61.30, a municipality may not issue a building permit to commence construction or use of the building until the plans have been approved by the department or its agent.

(2) Pursuant to s. 101.02 (13) (b) Stats., a municipality may not issue a building permit to commence a construction business activity to a person or entity unless the person or entity holds a registration issued by the department under s. Comm 5.30 as a building contractor or holds one of the credentials listed under s. Comm 5.30 (1) (b) 1., except as provided in s. Comm 5.30 (1) (b) 2.

END

EFFECTIVE DATE

Pursuant to s. 227.24, Stats., this rule shall take effect as an emergency rule upon publication in the official state newspaper, except ss. Comm 5.30 (1) and Comm 61.295 (2) which shall take effect on July 1, 2009.

(Note: Publication Date, March 2, 2009)

Credential Fee (nonrefundable): \$115.00 class code 7644

Make checks payable to: Department of Commerce The fee consists of a \$15 application fee and a registration fee of \$100. The credential will be effective for 4 years from the date of issuance.

You also have the option of registering online by visiting:

<https://apps.commerce.wi.gov/credential-online-application>

If you choose to register online, the application fee of \$15 will be waived and you will only be paying the registration fee of \$100.

* Notice Information collected may be used for participation surveys, eligibility for approvals, law enforcement (including child support and tax delinquency enforcement) purposes and other secondary purposes The Department may also provide this information to requesters pursuant to Wisconsin's open records law, ss. 19.31-19.39, Stats. Social security numbers are required when applying for a license according to Wisconsin Stats But they may not be disclosed to anyone except other State of Wisconsin governmental agencies.

Reason for Registration: No person or entity may engage in a construction business or offer to engage in a construction business that affects public buildings, places of employment and one- and two- family dwellings, public swimming pools and water attractions, unless the person or entity holds a registration issued by the department as a registered Building Contractor

You do not need this registration if you currently hold any of the following credentials issued by the department:

Dwelling Contractor Certification	Electrical Contractor Certification
Dwelling Contractor - Restricted Certification	Electrical Contractor - Restricted Certification
Manufactured Home Dealer License	HVAC Contractor Registration
Manufactured Home Installer License	Elevator Contractor License
Manufactured Home Manufacturer License	

Or you are a person or entity that works only on real estate or property you own or lease.

Examples of Construction Businesses that are to be registered with the Department of Commerce:

Building site preparation/ stabilization	Plumbing
Drywall and plastering	Poured concrete foundations and structures
Electric Wiring	Precast concrete
Finish carpentry	Public swimming pools and water attractions
Fire protection	Roofing
Flooring	Siding
Framing carpentry	Structural steel
General building construction	Tile and terrazzo
Glass and glazing	Wall coverings
Insulation	Other building or equipment specialties
Masonry and stone work	

**** Additional information can be viewed at <http://commerce.wi.gov/SB/SB-BuildingContractorProgram.html>****

Responsibilities of Registrant: A person or entity that holds a building contractor registration shall do all of the following:

Include their registration number on all construction bids and contracts.

Not contract with another person or entity to engage in construction business activities unless the person or entity holds a business license, certification or registration issued by the Department of Commerce.

Not commence a construction business activity until a permit is issued for the construction for any project that requires a uniform building permit under s Comm 20.08, Wisconsin Administrative Code.

Not commence a construction business activity until a permit is issued for the construction for any project that requires a municipal building permit involving a public building, a place of employment or a one- or two- family dwelling.

Not commence a construction business activity until plan approval has been obtained as required under ss Comm 61.30, 82.20, 83.22, or 90.04.

Please visit <http://commerce.wi.gov/SB/SB-DivEmailSignup.html> to sign up for Safety and Buildings email lists for programs you work in or are interested in. You will receive information from Safety and Buildings regarding code changes, product information, forms, etc

"Misclassification of Workers" - Not identifying an employee's status correctly for the purposes of safety protections, workers' benefits, and taxes is termed "Misclassification of Workers" in current high-profile national and state efforts to manage the problem. This practice is recognized by businesses, labor, and government as especially damaging in the construction industry.

Misclassification usually involves employers wrongly identifying employees as independent contractors or independent contractors collecting pay without accurately accounting for taxes or government service fees. While sometimes this is inadvertent, usually it is done knowingly to gain a financial advantage

The problem has multiple edges:

- Employees may not be rightly covered by standard safety regulations and may not be enrolled in unemployment and worker's compensation programs that they should be eligible for
- Identifying workers as independent contractors instead of employees can significantly reduce an organization's labor costs, creating unfair business advantage compared to honest employers.
- Huge amounts of money due government agencies to support services fraudulently are not paid. Not only is it illegal, it is unfair to all other taxpayers (for example, businesses supporting the unemployment system).

The Safety and Buildings Division of the Wisconsin Department of Commerce does not classify employees and businesses for purposes of other agencies, but it does make information available to those agencies about who does or does not hold a Building Contractor Registration.

The Minnesota Office of Legislative Audit did a study in 2007 that found misclassification of employees as independent contractors is major a problem in Minnesota. The study said an estimated 14 percent of Minnesota employers subject to unemployment insurance taxes - or 1 in 7 - misclassified at least one worker in 2005 See report, <http://www.auditor.leg.state.mn.us/PED/2007/miscclass.htm>.

According to a study conducted by the University of Missouri-Kansas City, from 2001 to 2005, the state of Illinois lost an estimated \$124.7 million in income tax annually - \$8.9 million of it in the construction sector.¹

A 2007 Cornell University study, which focused on the misclassification of workers in New York state, found that approximately 10 percent of the state's workers were misclassified.²

On February 11, 2008, the New York Department of Labor announced that in four months through December 2007, staff conducted 15 audits focusing on the restaurant and construction industries and found more than \$19 million in unreported wages, approximately \$3 million in minimum and overtime wages owed to workers, and the agency assessed more than \$1.2 million in taxes and penalties to noncompliant employers.

The U.S. federal Internal Revenue Service provides [this Web site](#) about employee classification.

¹ The Economic Cost of Employee Misclassification in the State of Illinois, *Michael P. Kelsay, et al*, University of Missouri-Kansas City, December 2006.

² The Cost of Worker Misclassification in New York State, *Linda H. Donahue, et al*, Cornell University, February 2007.

Appendix 5

Massachusetts Attorney General Opinion
On Three-Prong Employee Definition Test
(2008)

**An Advisory from the Attorney General's Fair Labor Division on
M.G.L. c. 149, s. 148B
2008/1¹**

The Office of the Attorney General (AGO) issues the following Advisory regarding M.G.L. c. 149, s. 148B, the Massachusetts Independent Contractor Law or the Massachusetts Misclassification Law (the "Law"). This Advisory provides guidance with respect to the Attorney General's understanding of and enforcement of the Law. This Advisory is not a formal opinion. Opinions of the Attorney General are formal documents rendered pursuant to specific statutory authority. M.G.L. c. 12, s. 3, 6, and 9. The Advisory is intended to provide guidance only and does not create any rights or remedies.

I. INTRODUCTION

A. The Need for Enforcement

The need for proper classification of individuals in the workplace is of paramount importance to the Commonwealth.² Entities that misclassify individuals are in many cases committing insurance fraud and deprive individuals of the many protections and benefits, both public and private, that employees enjoy. Misclassified individuals are often left without unemployment insurance and workers' compensation benefits. In addition, misclassified individuals do not have access to employer-provided health care and may be paid reduced wages or cash as wage payments.

Similarly, entities that misclassify individuals deprive the Commonwealth of tax revenue that the state would otherwise receive from payroll taxes. In addition, as a result of misclassification, the Commonwealth often incurs additional costs, such as providing health care coverage for uninsured workers. Other potential costs for the Commonwealth include providing workers' compensation benefits paid by the Workers' Compensation Trust Fund, and unemployment assistance without employer contribution into the Division of Unemployment Assistance fund, among other indirect costs.

Finally, businesses that properly classify employees and follow all of the relevant statutes regarding employment are likely to be at a distinct competitive disadvantage when vying for the same work, customers or contracts as those businesses that do not play by the rules. Further, by paying the proper taxes and insurance premiums, businesses following the Law are, in effect, subsidizing those businesses that do not. Misclassification undermines fair market competition and negatively impacts the business environment in the Commonwealth. The AGO expects businesses to contract only with businesses that properly classify their workers.

¹ This Advisory supersedes the Attorney General's prior Advisories regarding M.G.L. c. 149, s. 148B, including "An Advisory from the Attorney General, Amendments to Massachusetts Independent Contractor Law," Advisory 2004/2; and an "Advisory from the Attorney General's Fair Labor and Business Practices Division on the Issue of Employee Versus Independent Contractor," Advisory 94/3.

² The Commissioner of Revenue is charged with administering the Massachusetts wage withholding laws under M.G.L. c. 62B, which provides a different definition of employee than M.G.L. c. 149, s. 148B, for purposes of Massachusetts income tax withholding. See Department of Revenue TIR 05-11: Effect of New Employee Classification under M.G.L. c. 149, s. 148B on Withholding of Tax on Wages under M.G.L. c. 62B. In addition, a definition similar but not identical to M.G.L. c. 149, s. 148B, exists for unemployment insurance purposes. M.G.L. c. 151A, s. 2. The Massachusetts Workers' Compensation Law also provides a different definition of employee. M.G.L. c. 152, s. 1(4).

B. The History of the Law

The proper classification of employees has long been an issue of great concern in the Commonwealth. Under common law, a number of factors determined the existence of an employer/employee relationship based on the totality of the relationship. See, e.g., *Commonwealth v. Savage*, 31 Mass. App. Ct. 714 (1991). Those factors included the degree of control, the opportunity for profit and risk of loss, the employee's investment in the business facility, the permanency of the relationship, the skill required and the degree to which the employee's services were integral to the business.

In 1990, Massachusetts enacted the first version of the Law. By enacting the Law, the Legislature established that notwithstanding that a working relationship could be considered to be one of independent contractor under common law, the worker may still be deemed in employment for the purposes of the Law. *Boston Bicycle Couriers v. Deputy Director of the Division of Employment and Training*, 56 Mass. App. Ct. 473, 477 (2002)

Subsequent to its enactment in 1990, the Law has undergone several amendments including: Section 214 of Chapter 286 of the Acts of 1992; Section 165 of Chapter 110 of the Acts of 1993; Section 12 of Chapter 236 of the Acts of 1998; and Section 26 of Chapter 193 of the Acts of 2004. The 2004 amendment was part of legislation making broad changes to the laws governing the public construction industry. However, the Law, including the 2004 amendment, applies more broadly to a wide range of industries. The 2004 amendment kept intact, in large part, the standard for determining whether an individual is an employee, but made several changes from the earlier version of the statute. The amendment deleted the element "or is performed outside of all places of the business of the enterprise" as an alternative factor in prong two. In addition, the first element of prong two of the Law had read: "such service is performed . . . outside the usual course of business *for which the service is performed* . . ." After the 2004 amendment, the element reads: "the service is performed outside the usual course of business *of the employer*." Finally, the amendment added "trade" to the list of activities eligible for independent contractor status in prong three

II. THE LAW

M.G.L. c. 149, s. 148B, provides a three-part test which requires that all three elements (commonly referred to as prongs one, two and three or the A, B, C test) must exist in order for an individual to be classified other than as an employee. The burden of proof is on the employer, and the inability of an employer to prove any one of the prongs is sufficient to conclude that the individual in question is an employee. M.G.L. c. 149, s. 148B (using the term "unless"). See also *Scalli v. Citizens Financial Group*, 2006 WL 1581625, *14 (D. Mass. 2006); *Rainbow Development, LLC v. Com., Dept. of Industrial Accidents*, 2005 WL 3543770, *2 (Mass. Sup. Ct. 2005).

Courts have had a limited opportunity to interpret M.G.L. c. 149, s. 148B. In *College News Service v. Department of Industrial Accidents*, 21 Mass.L. Rptr. 464, 2006 WL 2830971, the Superior Court noted that M.G.L. c. 149, s. 148B is almost identical to M.G.L. c. 151A, s. 2, the statute used by the Division of Unemployment Assistance, and therefore relied on the case law analyzing M.G.L. c. 151A, s. 2, to interpret M.G.L. c. 149, s. 148B. See *4 ("If the Legislature uses the same language in several provisions concerning the same subject matter [e.g., the definition of an employee in distinction from an independent contractor], the courts will presume it to have given the language the same meaning in each provision.").

See also *Commonwealth v. Germano*, 379 Mass. 268, 275-76 (1979). Because prongs one and three of M.G.L. c. 149, s. 148B and M.G.L. c. 151A, s. 2 are nearly identical and because prong two of M.G.L. c. 149, s. 148B contains one of the two steps of prong two in M.G.L. c. 151A, s. 2, Massachusetts case law interpreting M.G.L. c. 151A, s. 2 provides a useful guide to interpreting M.G.L. c. 149, s. 148B.

A. The Three Prong Test

Prong One: Freedom from Control

The first prong of M.G.L. c. 149, s. 148B provides that the individual must be “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” in order for the individual to be an independent contractor. In *Commissioner of the Division of Unemployment Assistance v. Town Taxi of Cape Cod*, 68 Mass. App. Ct. 426, 434 (2007), the Court noted in interpreting the nearly identical language of prong one of M.G.L. c. 151A, s. 2 that:

The first part of the test examines the degree of control and direction retained by the employing entity over the services performed. The burden is upon the employer to demonstrate that the services at issue are performed free from its control or direction. The test is not so narrow as to require that a worker be entirely free from direction and control from outside forces.

Id. (citations omitted)

The first prong of the test includes a determination of the employer’s actual control and direction of the individual. See M.G.L. c. 149, s. 148B (using the phrase “in fact”). An employment contract or job description indicating that an individual is free from supervisory direction or control is insufficient by itself to classify an individual as an independent contractor under the Law. To be free from an employer’s direction and control, a worker’s activities and duties should actually be carried out with minimal instruction. For example, an independent contractor completes the job using his or her own approach with little direction and dictates the hours that he or she will work on the job.

Prong Two: Service Outside the Usual Course of the Employer’s Business

Prong two of M.G.L. c. 149, s. 148B(a)(2) provides that the service the individual performs must be “outside the usual course of business of the employer” in order for the individual to not be classified as an employee. Prior to the 2004 amendment, the employer could alternatively demonstrate that the work was performed “outside of all places of the business of the enterprise.” The Law does not define “usual course of business” and Massachusetts courts have had limited opportunities to do so. In *Athol Daily News v. Division of Employment and Training*, 439 Mass. 171, 179 (2003), the Court found that newspaper carriers were performing the “usual course of business” of the newspaper relying on the employer’s own definition of its business. In *American Zurich v. Dept. of Industrial Accidents*, 2006 WL 2205085, *4 (Mass. Super. 2006), Judge Paul Troy noted that “a worker whose services form a regular and continuing part of the employer’s business” and “whose method of operation is not such an independent business” through which workers’ compensation costs can be channeled, “should be found to be an employee.” *Id.* Yet, “if the worker is performing services that are part of an independent, separate, and distinct business from that of the employer,” prong two is not implicated. *Id.*

Prong Three: Independent Trade, Occupation, Profession or Business

Prong three provides that 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" in order for the individual to be classified other than as an employee M.G.L. c. 149, s. 148B(a)(3). "Under the third prong, the court is to consider whether the service in question could be viewed as an independent trade or business because the worker is capable of performing the service to anyone wishing to avail themselves of the service or, conversely, whether the nature of the business compels the worker to depend on a single employer for the continuation of the services" *Coverall v Division of Unemployment Assistance*, 447 Mass. 852, 857-58 (2006) (interpreting prong three of M.G.L. c. 151A, s. 2). The court went on to note in *Coverall*:

Although the court can consider whether a worker is capable of performing the service to anyone wishing to avail themselves of the services, the court may also consider whether the nature of the business compels the worker to depend on a single employer for the continuation of the services [citation omitted]. In this regard, we determine whether the worker is wearing the hat of the employee of the employing company, or is wearing the hat of his own independent enterprise.

Id

B. Issues Deemed Irrelevant

An employer's failure to withhold taxes, contribute to unemployment compensation, or provide worker's compensation is not considered when analyzing whether an employee has been appropriately classified as an employee. M.G.L. c. 149, s. 148B(b). Hence, an employer's belief that a worker should be an independent contractor has no relevance in determining whether there has been violation of the Law. Similarly, the Law deems irrelevant the status of a worker as a "sole proprietor or partnership," for the purpose of obtaining worker's compensation insurance. M.G.L. c. 149, s. 148B(c)

C. Violation of the Law

M.G.L. c. 149, s. 148B(d) provides that an employer violates the statute when two acts occur. First, the employer classifies or treats the individual other than as an employee although the worker does not meet each of the criteria in the three prong test. Second, in receiving services from the individual, the employer violates one or more of the following laws enumerated in the Law:

- The wage and hour laws set forth in M.G.L. c. 149.
- The minimum wage law set out in M.G.L. c. 151, s. 1A, 1B, and 19; 455 CMR 2.01, et seq.
- The overtime law set forth in M.G.L. c. 151, s. 1, 1A, 1B, and 19.
- The law requiring employers to keep true and accurate employee payroll records, and to furnish the records to the Attorney General upon request as required by M.G.L. c. 151, s. 15.
- Provisions requiring employers to take and pay over withholding taxes on employee wages M.G.L. c. 62B.³
- The worker's compensation provisions punishing knowing misclassification of an employee. M.G.L. c. 152, s. 14.

³ As noted in footnote 2, for purposes of income tax withholding, M.G.L. c. 62B provides a definition of employee that differs from the three prong test in M.G.L. c. 149, s. 148B

The statute authorizes the Attorney General to impose substantial civil and criminal penalties, and in certain circumstances, to debar violators from public works contracts. M.G.L. c. 149, s. 27C(a)(3). The penalties and length of debarment depend upon the nature and number of violations. M.G.L. c. 149, s. 148B(d) also creates liability for both business entities and individuals, including corporate officers, and those with management authority over affected workers.

III. ENFORCEMENT GUIDELINES

A. General Enforcement Guidelines

The AGO recognizes that enforcement guidelines are useful to employers, entities and individuals who must determine whether a particular situation or individual has employee status. When enforcing the Law, the AGO attempts to protect workers, legitimate businesses and the Commonwealth, consistent with the goals of the Law outlined in the Introduction.

The Law is focused on the misclassification of individuals. In the event that all individuals performing a service are classified and legitimately treated as employees of an entity (paid W-2 income, received W-2 tax forms, subject to withholdings for federal and state taxes, covered by workers' compensation insurance, eligible for unemployment compensation benefits, etc.) and are performing the service as an employee, then there is no misclassification of those workers. Accordingly, in determining whether the Law has been violated, the initial question is whether an individual or individuals are classified other than an employee. For example, if painting company X cannot finish a painting job and hires painting company Y as a subcontractor to finish the painting job, provided that all of the individuals performing the painting are employees of company Y, then the Law does not apply. However, if painting company X hires individuals as independent contractors to finish the painting job, then this would be a violation of prong two and a misclassification under the Law.

The AGO is cognizant that there are legitimate independent contractors and business-to-business relationships in the Commonwealth. These business relationships are important to the economic wellbeing of the Commonwealth and, provided that they are legitimate and fulfill their legal requirements, they will not be adversely impacted by enforcement of the Law. The difficulty arises when businesses are created and maintained in order to avoid the Law. The AGO will enforce the Law against entities that allow, request or contract with corporate entities such as LLCs or S corporations that exist for the purpose of avoiding the Law. In these situations, the AGO will consider, among other factors, whether: the services of the alleged independent contractor are not actually available to entities beyond the contracting entity, even if they purport to be so; whether the business of the contracting entity is no different than the services performed by the alleged independent contractor; or the alleged independent contractor is only a business requested or required to be so by the contracting entity.

In reviewing situations for misclassification, the AGO considers certain factors to be strong indications of misclassification that warrant further investigation and may result in enforcement. These include:

- Individuals providing services for an employer that are not reflected on the employer's business records;
- Individuals providing services who are paid "off the books", "under the table", in cash or provided no documents reflecting payment;
- Insufficient or no workers' compensation coverage exists;
- Individuals providing services are not provided 1099s or W-2s by any entity;

- The contracting entity provides equipment, tools and supplies to individuals or requires the purchase of such materials directly from the contracting entity; and
- Alleged independent contractors do not pay income taxes or employer contributions to the Division of Unemployment Assistance.

Since it is not feasible to address in this Advisory every situation that could occur and since each case involves its own set of facts, it should be recognized that each potential enforcement action shall be reviewed by the AGO on a case-by-case basis, consistent with the Law.

B. Prong Two Guidelines

Due to the nature of prong two and the lack of judicial precedent, the AGO recognizes the complexity that prong two presents and the concerns regarding legitimate independent contractors, particularly among certain segments of the workforce

As discussed above, the AGO emphasizes that the initial question in determining whether the Law has been violated is whether an individual or individuals are classified other than as an employee. Only when an individual or individuals are classified other than as an employee will there be a determination of whether any of the prongs – including the complex prong two – are violated.

In *Athol Daily News*, the Court advised that no prong should be read so broadly as to render the other factors of the test superfluous. 439 Mass. at 180. Thus, prong two should not be construed to include all aspects of a business such that prongs one and three become unnecessary.

In its enforcement actions, the AGO will consider whether the service the individual is performing is necessary to the business of the employing unit or merely incidental in determining whether the individual may be properly classified as other than an employee under prong two.

Some examples of how the Attorney General will apply prong two⁴:

- A drywall company classifies an individual who is installing drywall as an independent contractor. This would be a violation of prong two because the individual installing the drywall is performing an essential part of the employer's business.
- A company in the business of providing motor vehicle appraisals classifies an individual appraiser as an independent contractor. This would be a violation of prong two because the appraiser is performing an essential part of the appraisal company's business.
- An accounting firm hires an individual to move office furniture. Prong two is not applicable (although prongs one and three may be) because the moving of furniture is incidental and not necessary to the accounting firm's business.

⁴ In interpreting the Illinois independent contractor law, the Supreme Court of Illinois noted in *Carpetland USA, Inc v IL Dept. of Employment Security*, 201 Ill.2d 351, 386-88 (2002):

The washing of windows or mowing of grass for a business is incidental. But when one is in the business of selling a product, sales calls made by sales representatives are in the usual course of business because sales calls are necessary. When one is in the business of dispatching limousines, the services of chauffeurs are provided in the usual course of business because the act of driving is necessary to the business.

Although the Illinois statute is not the same as the Massachusetts statute, the court's analysis is useful for guidance on how the Attorney General will undertake prong two enforcement

IV. CONCLUSION

As this Advisory reflects, the AGO will carry out its enforcement responsibilities to serve the goals of the Law as articulated in the Introduction. The Law has been passed and amended over time to address serious abuses by various entities, and the AGO's goal is to prevent and remedy those practices without disrupting legitimate business activity.

Appendix 6

Massachusetts Three-Prong Employee Definition Test and Questions &
Answers Regarding Massachusetts Law

Massachusetts Chapter 149: Section 148B. Persons performing service not authorized under this chapter deemed employees; exception

Section 148B. (a) For the purpose of this chapter and chapter 151, an individual performing any service, except as authorized under this chapter, 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.

(b) The failure to withhold federal or state income taxes or to pay unemployment compensation contributions or workers' compensation premiums with respect to an individual's wages shall not be considered in making a determination under this section.

(c) An individual's exercise of the option to secure workers' compensation insurance with a carrier as a sole proprietor or partnership pursuant to subsection (4) of section 1 of chapter 152 shall not be considered in making a determination under this section.

(d) Whoever fails to properly classify an individual as an employee according to this section and in so doing fails to comply, in any respect, with chapter 149, or section 1, 1A, 1B, 2B, 15 or 19 of chapter 151, or chapter 62B, shall be punished and shall be subject to all of the criminal and civil remedies, including debarment, as provided in section 27C of this chapter. Whoever fails to properly classify an individual as an employee according to this section and in so doing violates chapter 152 shall be punished as provided in section 14 of said chapter 152 and shall be subject to all of the civil remedies, including debarment, provided in section 27C of this chapter. Any entity and the president and treasurer of a corporation and any officer or agent having the management of the corporation or entity shall be liable for violations of this section.

(e) Nothing in this section shall limit the availability of other remedies at law or in equity.

State of Massachusetts IC Law Questions and Answers

There is no case law at this time.

1. A general contractor that is building a house hires in a plumber to do the plumbing for the house. The plumber has no employees. The plumber only works by himself and does not carry worker's compensation insurance. How does the IC law treat the plumber? Is the plumber "outside the usual course of business of the general contractor"?

Answer: The plumber is a sole-proprietor and if he has no employees he is not an employee of the general contractor. If the plumber has employees he is not a sole-proprietor, he is an employer, then the plumber needs WC insurance.

2. Are any of the following occupations considered outside the usual course of business of a general contractor builder?

- ✓ Carpenter
- ✓ Drywaller
- ✓ Roofer
- ✓ Mason
- ✓ Electrician
- ✓ Plasterer
- ✓ Tile Setter
- ✓ Glazier
- ✓ Landscaper

Answer: They are outside the usual course of business of a general contractor builder if general contractor brings them in separately.

If the general contractor is a drywaller himself and hires drywallers, the drywallers are employees. They are considered the general contractor's employees and WC insurance is required.

3. If a drywaller needs additional help to finish a job and sub-contracts with another drywaller and the sub-contractor does not have a worker's compensation policy, how does the IC law treat the sub-contracted drywaller?

Answer: The sub-contracted drywaller is an employee of the drywaller.

4. If a drywaller need additional help to finish a job and sub-contracts with another drywaller and the sub-contractor has a worker's compensation policy, how does the IC law treat the sub-contracted drywaller?

Answer: If all have WC insurance, all is okay, there is no violation.

5. If both the contractor and a sub-contracted have worker's compensation policies does the IC test still come into play at all?

Answer: For WC law, it does not.

6. Assume that an individual who is referred to as a "freelance" writer enters into a contract to provide an article of a designated number of column inches to a specific publication and that the writer is to be compensated in a set amount for his/her work. The writer performs the services using a computer in his/her home and all communications regarding the work are via e-mail. If it is assumed for the sake of argument that prongs A and C of the "ABC" test are satisfied, will the writer be considered an employee of the publication if it is determined that the services of the writer were not "outside the usual course of the business" of the publication?

Answer: The writer is an employee of the publication.

7. What do you look for to determine the legitimacy of a business-to-business relationship.

Answer: All Massachusetts businesses must obtain a business certificate to operate. Look for Corporation filing with Secretary of State or business certification filed with local clerk. If not legally registered as a business, they are employees.

If business is certified then parts 1 & 2 of test are looked at. Must meet all 3.

8. Have you developed interpretation guidelines for investigators outlining how the law is to be applied? If yes, can you provide a copy?

Answer: Guideline is the attorney general opinion. Decisions can be appealed to a department hearing office.

9. Has the 3 prong IC test eased or complicated the investigation process? How?

Answer; Eased it dramatically. 20 point test is gone. Burden is on the employer to demonstrate that there is a true IC situation. And eliminates 1099 questions.

10. What are the major issues that have arisen during the implementation of the 3 prong IC test? (complaints, questions, interpretation, misunderstanding, litigation, education etc.)

Answer: Education and publicity is key.

SWO process raised concerns and awareness. If no WC, SWO is issued until they are in compliance. \$100 per day for fine. Employer can appeal on the site and the order is put in abeyance, and they may continue to work. Hearing is held within 14 days. If they lose at appeal, the penalty is \$250 per day and is retroactive going back to the original date.

The employer can withdraw their appeal ^{if they come into compliance} and receive the \$100 per day penalty.

11. Regarding stop work orders. If there are 5 contractors working on a job site and you find 4 have worker's compensation insurance and 1 does not and is found in violation of the law, is the entire worksite shut down or is only the non-complaint contractor ordered to stop working?

Answer; Only the person in violation. All other compliant businesses continue working.

12. What has been Massachusetts's experience with the provision allowing a private cause of action for any person or firm that loses a competitive bid for a contract?

Answer: Allowed under statute, if it has occurred they are not aware of it. See Massachusetts law 152.25c.

13. What kinds of numbers have you seen for Stop-work-orders? For appeals? Court cases?

Answer: Issued 355 last month (12 investigators), estimated 90% are appealed. 3 or 4 hearings last month. 0 to circuit court. Majority appeal to continue working and then come into compliance and withdraw the appeal.

14. How do you follow up on the employees getting paid for 10 days? Any enforcement for this?

Answer: When SWO is issued the employer is told they must continue to pay employees, if they appeal, they can continue to work. Employee's are told on the work site that wages must continue for 10 days. There have not been any none payment of wage issues raised by employees. If wages are not paid, case is sent to AG for handling.

15. When does an employer required to have WC coverage in Massachusetts?

Answer: If an employer has one employee, the employer is required to have insurance.

16. Do you share data with the MA Unemployment Division and the MA Department of Revenue?

Answer: No direct data exchange with UI or DOR, but they share information on cases.

MA has a Joint Taskforce on the Underground Economy, 18 agencies meet weekly, have a referral line for any labor law violation.

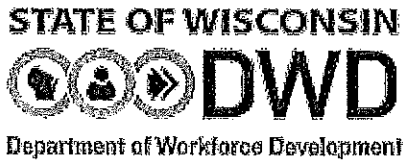
All referrals are entered into a tracking system. All 18 agencies have access to the tracking system, all agencies enter information whether the case is an issue or not an issue for their agency.

Every Wednesday the agencies meet to go over major cases.

Joint action strike team, target a company or industry and bring 7 or 8 agency's staff in at once and review all aspects of regulatory compliance.

If SWO is issued, the employer is placed on the State debarment list for 3 years, and can not enter into contract with State of Massachusetts or any Massachusetts municipality.

Finally, they indicated the publicity is needed to get the word out. A lot of voluntary compliance can be obtained through publicizing strike team results.



Worker Classification

Welcome! This site was designed to provide employers with a clear and understandable process to assist them in determining if their workers are employees or independent contractors.

The questions in the evaluation process are derived directly from Wisconsin statutes that govern the classification of workers. We hope this site is helpful both to employers and others involved in worker classification.

Is a Worker an "Employee" or an "Independent Contractor"?

Employers are required by law to correctly classify each worker as either an "employee" or "independent contractor."

Legal Obligations

It is important for employers to correctly classify their workers. Worker classification determines whether or not the employer has legal obligations under the law for unemployment insurance, worker's compensation, wage payments, work hours, record keeping and civil rights protections. There are consequences for misclassifying or attempting to misclassify a worker as an independent contractor.

Steps to Classify a Worker

This website will guide you through Wisconsin's worker classification laws. Select the appropriate law(s) to begin the process to evaluate how to correctly classify a worker as either an employee or independent contractor:

[Unemployment Insurance](#)

[Worker's Compensation](#)

[Labor Standards](#)

[Civil Rights](#)

[Disclaimer](#)

Employee or Independent Contractor

Why it Matters

Worker classification is important to employers because the correct classification determines whether the employer has legal obligations for:

- Unemployment Insurance
- Workers Compensation
- Wage Payments
- Work Hours
- Record Keeping
- Civil Rights Protections

When employers intentionally misclassify workers as independent contractors, they avoid:

- Unemployment Insurance Taxes
- Workers Compensation Coverage
- Withholding State and Federal Income Taxes
- Paying Social Security and Medicare Taxes

Employers who misclassify workers as independent contractors gain an unfair competitive advantage

Legal Consequences

Under the law, workers are presumed to be employees and subject to tax unless determined by law to be independent contractors. An employer found to be utilizing misclassified workers may be liable for additional tax, interest and penalties. Employers engaged in the construction trades may also be subject to a stop work order. In addition, employers engaged in the painting or drywall finishing of buildings or other structures who willfully provide false information to DWD for the purpose of misclassifying or attempting to misclassify a worker as an independent contractor can be fined \$25,000 for each violation.

Steps to Classify a Worker

DWD has developed a website to help employers correctly classify their workers:

http://dwd.wisconsin.gov/worker_classification

This online test takes employers through each factor in the law that is used to determine whether a worker is an independent contractor. The website also provides employers with real life case examples and case law to help them evaluate whether their workers are independent contractors.

If a worker does not meet the independent contractor criteria, report the worker as an employee and file wage and tax reports at <http://dwd.wisconsin.gov/uitax>.

The decision of an employer to classify a worker as an independent contractor is subject to review and determination by the department.

Report Suspected Misclassified Workers

If you suspect an employer is utilizing misclassified workers, please contact us:

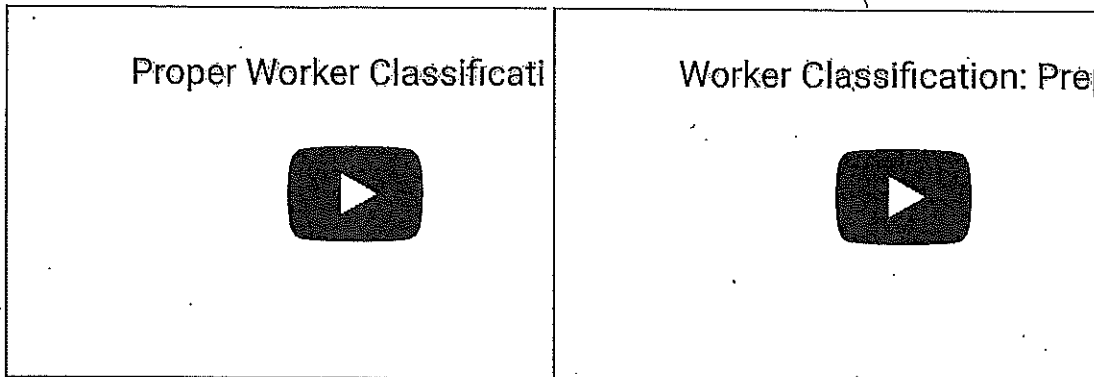
- E-mail: workermisclass@dwd.wisconsin.gov
- Call: (608) 261-5835





Unemployment Insurance - Worker Classification

Is a Worker an "Employee" or an "Independent Contractor"?



Wisconsin employers (referred to as "employing units" in the unemployment insurance law until unemployment insurance coverage or an employee/employer relationship is established) have an obligation under the unemployment insurance law to classify workers correctly as either "employees" or "independent contractors". Employees are covered by the unemployment insurance law; independent contractors are not covered.

If a worker is or has been "performing services for pay" for an employing unit, there is a presumption in the law that the worker is an "employee," not an independent contractor. That presumption can only be overcome by evidence under the applicable unemployment insurance law that the worker is an independent contractor.

NOTE: The department has utilized the term "employer" in this website with the recognition that not all "employing units" are covered under the unemployment insurance law or have employee/employer relationships with their workers. Nevertheless, for ease of discussion in the context of deciding whether a worker is an independent contractor or an employee, the term "employer" is frequently used, rather than "employing unit."

Compliance and Penalties

The department works to ensure that workers are properly classified as employees or independent contractors through compliance programs. If an employer is found to be improperly classifying workers as independent contractors, penalties may result.

Steps to Classify a Worker

Choose Category of Employer

The first step in the process of determining an employer's obligation under the unemployment insurance law is to determine which of the following categories describes the employer:

- **General Private Employers** (services performed for any other person or entity)
- **State and local government employers** (service performed for a unit of state or local government)
- **Nonprofit employers** (services performed for an organization that is described in §501(c)(3) and exempt from federal income tax under §501(a) of the Internal Revenue Code)
- **Trucking employers** (services performed as a truck driver for a licensed motor carrier that leases a vehicle from the contract operator)
- **Logging employers** (services performed as a piece cutter or skidding operator for a forest products manufacturer or logging contractor)
- **Indian tribal government employers** (services performed for an Indian tribe that is federally recognized under 25 USC 450B(e))

Select the appropriate employer category to continue to worker classification tests:

General Private Employers

State and Local Government

Nonprofit Employers

Trucking Employers

Logging Employers

Indian Tribal Government

Compliance

The department works to ensure that workers are properly classified as employees or independent contractors through the field audit process and worksite compliance investigations.

Department field auditors conduct routine periodic examinations of employer records. The specific audit objectives include investigating alleged independent contractor issues, determining compliance with unemployment insurance reporting requirements, and investigating suspected unemployment insurance benefit fraud.

The department is authorized by Wis. Stat. § 103.06, to conduct compliance investigations at construction worksites as defined in Wis. Stat. § 108.18 (2)(c) to determine if workers are being properly classified as employees or independent contractors.

Penalties

If an employer is found to be utilizing misclassified workers, the employer may be liable for additional tax, interest and penalties. If as a result of an investigation an employer is found to be utilizing misclassified workers, additional tax, interest and civil penalties, including the issuance of stop work orders, may result. In addition, an employer may be subject to criminal penalties for intentional misclassification.

Administrative Penalty for Intentional Misclassification:

Wis. Stat. § 108.221(1) provides that employers engaged in construction as described in Wis. Stat. § 108.18 (2)(c), or who are engaged in the painting or drywall finishing of buildings or other structures, who knowingly and intentionally provide false information to the department for the purpose of misclassifying or attempting to misclassify an employee, shall for each incident, be assessed a penalty by the department in the amount of \$500 for each employee who is misclassified, not to exceed \$7,500 per incident.

The department shall consider the following factors in determining whether an employer knowingly and intentionally provided false information to the department: (1) whether the employer was previously found to have misclassified an employee in the same or substantially similar position; and (2) whether the employer was the subject of litigation or a government investigation relating to worker misclassification and the employer, as a result of that litigation or investigation, received an opinion or decision from a federal or state court or agency that the subject position or a substantially similar position should be classified as an employee. The statute provides those factors are non-exclusive; therefore, the department may also consider other factors.

Criminal Penalty for Intentional Misclassification:

Under Wis. Stat. § 108.24 (2m), any employer engaged in construction as described in § 108.18 (2) (c) or engaged in the painting or drywall finishing of buildings or other structures who, after having previously been assessed an administrative penalty by the department under § 108.221 (1), knowingly and intentionally provides false information to the department for the purpose of misclassifying or attempting to misclassify an individual as a nonemployee shall be fined \$1,000 for each employee who is misclassified, subject to a maximum fine of \$25,000 for each violation.

The department may refer violations of this subsection for prosecution by the department of justice or the district attorney for the county in which the violation occurred.

Administrative Penalty for Coercion:

Under Wis. Stat. § 108.221 (2) (c), any employer described in § 108.18 (2) (c) or engaged in the painting or drywall finishing of buildings or other structures who, through coercion, requires an individual to adopt the status of a nonemployee shall be assessed a penalty by the department in the amount of \$1,000 for each individual so coerced, but not to exceed \$10,000 per calendar year.

Employers described in Wis. Stat. § 108.18 (2)(c), include those engaged in the construction of roads, bridges, highways, sewers, water mains, utilities, public buildings, factories, housing, or similar construction projects.



Worker's Compensation - Worker Classification

Is a Worker an "Employee" or an "Independent Contractor"?

Employers are required by law to correctly classify each worker as either an "employee" or "independent contractor" for purposes of the employer's obligations under the law for worker's compensation insurance.

The worker's compensation insurance law uses a definition of "employee" (with exceptions) to separate those individuals (workers) whose employer is obligated to provide worker's compensation benefits (employees) from those whose employer is not obligated to provide worker's compensation benefits (independent contractors).

The Wisconsin Worker's Compensation Act (Act) defines an employee as "every person in the service of another under any contract of hire, express or implied, all helpers and assistants of employees, whether paid by the employer or employee, if employed with the knowledge, actual or constructive, of the employer, including minors, who shall have the same power of contracting as adult employees" but not including (1) domestic servants, (2) any person whose employment is not in the trade, business, profession or occupation of the employer unless the employer elects to cover them."

It is important that you carefully read the definition of "employee" and the exceptions in the worker's compensation law: Wis. Stats. 102.07(4)(a) and 102.07(8).

Steps to Classify a Worker

If you are an employer or a worker and want to determine how to properly classify a worker as either an employee or an independent contractor for worker's compensation insurance, continue to the worker classification test to begin the process:

Begin the Process

Definitions

Any Contract of Hire

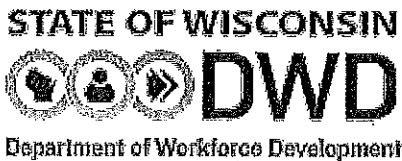
A contract of hire means that the person performs services for which he or she is compensated. Compensation is something of value and may be cash or in-kind.

Domestic Servant

Although neither the statutes nor case law provide a definition of "domestic servant" as it is used in s. 102.07(4) of the Act, the department has consistently ruled that persons hired in a private home to perform general household services such as nanny, baby-sitting, cooking, cleaning, laundering, gardening, yard and maintenance work and other duties commonly associated with the meaning of domestic servant, meet the definition of domestic servant intended by the Act.

Trade, business, profession or occupation of the employer

Cornelius v. Industrial Commission, 242 Wis. 183, 185 (1943) defines a trade or business as an occupation or employment habitually engaged in for livelihood or gain. If a person's employment is in the trade, business, profession or occupation of the employer, he or she is an employee, no matter how casual or isolated the employer's trade, business, profession or occupation may be. For example, typically a home-owner who hires someone to mow his or her lawn is not an employer subject to the Act because being a home-owner is not associated with a trade, business, profession or occupation.



Labor Standards

Is a Worker an "Employee" or an "Independent Contractor"?

Employers are required to correctly classify each worker as either an "employee" or an "independent contractor" for the purposes of the employer's obligations under the wage and hour laws.

The wage and hour laws contain definitions of "employee" to separate those individuals (employees) who have protections under the wage and hour laws from those individuals (independent contractors) who do not. These definitions of "employee" do not determine which individuals should or should not be paid under prevailing wage laws, Secs. 66.0903 and 103.49, Wis. Stats.

The statutes enforced by the Labor Standards Bureau contain **three definitions of employee**:

- Section 103.001 (5) of the Wisconsin employment regulations law defines an employee as any person who may be required or directed by any employer in consideration of direct or indirect gain or profit, to engage in any employment, or to go or work or be at any time in any place of employment.
- Section 104.01 (2) (a) of the Wisconsin minimum wage law defines an employee as every individual who is in receipt of or is entitled to any compensation for labor performed for any employer.
- Section 109.01 (1r) of the Wisconsin wage payments, claims and collections law defines an employee as any person employed by an employer, except that "employee" does not include an officer or director of a corporation, a member or manager of a limited liability company, a partner of a partnership or a joint venture, the owner of a sole proprietorship, an independent contractor, or a person employed in a managerial, executive, or commissioned sales capacity or in a capacity in which the person is privy to confidential matters involving the employer-employee relationship.

The Labor Standards Bureau presumes that a worker is an employee unless the worker meets one of the exceptions listed in sections 104.01 (2) (b) and 109.01 (1r) of the Wisconsin Statutes.

Note: The Labor Standards Bureau also follows interpretations of the U.S. Department of Labor's Wage and Hour Division in this regard.

See U.S. Department of Labor Guidance - Wage and Hour Division.

Steps to Classify a Worker

If you are an employer or a worker and want to determine how to properly classify a worker as either an employee or an independent contractor for wage and hour laws continue to the worker classification tests to begin the process:

Begin the Process

STATE OF WISCONSIN



Department of Workforce Development

Civil Rights - Worker Classification

Is a Worker an "Employee" or a "Non Employee"?

The statutory definition of "employee" is found in Section 111.32 (5) of the Wisconsin Fair Employment Act. Section 111.32(5) of the act states that an "employee" does not include any individual employed by his or her parents, spouse or child. The definition of employer is found in Section 111.32 (6) of the act. These definitions are limited, so in Wisconsin the definitions of employee, non employee and employer are primarily developed in case law interpreting the Wisconsin Fair Employment Act.

Steps to Classify a Worker

If you are employer or a worker and want to determine how to properly classify a worker as either an employee or a non employee under the Wisconsin Fair Employment Act, continue to the worker classification tests to begin the process:

Begin the Process
