

# Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries

*A Survey of Research*

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*Fact Sheet*  
*August 2014*

**NELP**  
**National Employment  
Law Project**

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misclassified and whose reclassification has been prohibited under current law.<sup>5</sup>

New data on the scope of misclassification may be on its way soon: the Department of Labor has engaged a nation-wide field survey of workers and employers.<sup>6</sup>

## ***2. Findings from State Studies & Reports***

**A** growing number of states have been calling attention to independent contractor abuses by creating inter-agency task forces and committees to study the magnitude of the problem and passing new legislation to combat misclassification. Along with academic studies and other policy research, the reports document the prevalence of the problem and the attendant losses of millions of dollars to state workers' compensation, unemployment insurance, and income tax revenues.

The following chart summarizes the findings from more than 20 state-level studies. The studies rely on a range of data and methods. Most studies rely on data from unemployment insurance and workers' compensation audits, targeted or random; some draw on the records of multi-level government agencies; and a few used interviews with workers. Some studies examine the workforce as a whole, while others focus on industries where misclassification is rampant, such as construction.

## ***3. Trends in the Findings from State Studies***

**T**he findings from these state studies demonstrate the staggering scope of misclassification, the difficulties in reaching precise counts of workers affected and funds lost, and the potential for enforcement initiatives to return much-needed funds to state coffers.

- **A STAGGERING NUMBER OF WORKERS ARE MISCLASSIFIED.** Audits generally uncover numerous cases of misclassification at an individual workplace or employer, resulting in large numbers of workers being reclassified as employees following review. For example, targeted audits conducted by the Ohio 1099 Task Force resulted in the reclassification of almost 47 percent of the workers interviewed.<sup>35</sup> At just one company it audited, the Maryland Department of Labor, Licensing and Regulation's Division of Unemployment Insurance found 537 misclassified workers and a total of \$2,257,596 in taxable unreported wages.<sup>36</sup> In 2012, California's Employment Development Department identified 89,063 workers who had not previously been reported.<sup>37</sup> According to its latest task force report, the Connecticut DOL identified close to 6,500 misclassified workers.<sup>38</sup> The New York Task Force reported that it identified 20,200 misclassified workers in 2012, a total of 88,700 since the task force's start in September 2007, and that the New York DOL identified nearly 218,000 misclassified workers through UI audits.<sup>39</sup> Studies that extrapolate from audit data put the actual numbers of misclassified workers at much higher levels: an estimated 368,685 workers in Illinois;<sup>40</sup> 4,792 in Maine;<sup>41</sup> between 125,725 and 248,206 in Massachusetts;<sup>42</sup> 704,785 in New York;<sup>43</sup> between 54,000 and 459,000 in Ohio;<sup>44</sup> 580,000 in Pennsylvania;<sup>45</sup> and 214,000 in Virginia.<sup>46</sup>
- **STUDIES MOST LIKELY UNDERESTIMATE THE TRUE SCOPE OF MISCLASSIFICATION.** Many of the studies are based on unemployment insurance tax audits of employers registered with the state's UI program. The audits seek to identify employers who misclassify workers, workers who are misclassified, and the resulting shortfall to

misclassified and whose reclassification has been prohibited under current law.<sup>5</sup>

New data on the scope of misclassification may be on its way soon: the Department of Labor has engaged a nation-wide field survey of workers and employers.<sup>6</sup>

## ***2. Findings from State Studies & Reports***

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## ***3. Trends in the Findings from State Studies***

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- **STUDIES MOST LIKELY UNDERESTIMATE THE TRUE SCOPE OF MISCLASSIFICATION.** Many of the studies are based on unemployment insurance tax audits of employers registered with the state's UI program. The audits seek to identify employers who misclassify workers, workers who are misclassified, and the resulting shortfall to

the UI program. Researchers extrapolate from UI audit data to estimate the incidence of misclassification in the workforce and its impact on other social insurance programs and taxes. These UI audits miss a large portion of the misclassified workforce, however, because they rarely identify employers who fail to report any worker payments to state authorities or workers paid completely off the books—the “underground economy”—where misclassification is generally understood to be even more prevalent.

- **BILLIONS OF DOLLARS OF PAYROLL ARE NEVER REPORTED TO STATE GOVERNMENTS.** As explained above, many employers underreport their payroll, or pay workers off the books and do not report any wages. In California and New York alone, employers fail to report billions of dollars to state agencies each year.<sup>47</sup> Reliance on random audits as the sole investigatory strategy may result in an undercount of violations and unpaid taxes.
- **MISCLASSIFICATION ALSO RESULTS IN LOST INCOME TAX REVENUE TO LOCAL GOVERNMENTS.** Municipal governments supported by payroll taxes are also hit hard by misclassification. This includes some of the nation’s largest and most important economic centers.
- **INDEPENDENT CONTRACTOR MISCLASSIFICATION RATES ARE RISING.** In Illinois, the rate of misclassification by violating employers increased by 21 percent from 2001 to 2005. A recent report by the Ohio attorney general reported a 53.5 percent increase in the number of workers reclassified from 2008 to 2009.<sup>48</sup> And a study of misclassification in Massachusetts’s construction industry from 2001 to 2003 noted that both the prevalence of misclassification and the severity of its impact have worsened over the years. According to

the U.S. Department of Labor’s Employment and Training Administration, the average number of misclassified workers identified per audit more than doubled between 2002 and 2011.<sup>49</sup>

- **MISCLASSIFICATION RATES ARE DISPROPORTIONATELY HIGH IN CERTAIN INDUSTRIES, SUCH AS CONSTRUCTION, REAL ESTATE, HOME CARE, TRUCKING, JANITORIAL AND HIGH-TECH JOBS.** Many misclassification studies focus on the construction because the industry has been so plagued by independent contractor abuses. The Maine, Massachusetts, Minnesota and New York studies found rates of misclassification up to several points higher in construction as compared with the workforce as a whole. Delivery drivers and truckers have also experienced widespread abuse.<sup>50</sup> Sixteen states have negotiated with FedEx to end the delivery company’s practice of misclassifying its drivers as independent contractors.<sup>51</sup> And an estimated two-thirds of port truck drivers are misclassified.<sup>52</sup> Reports indicate that employers in several other key sectors routinely misclassify workers.
- **MISCLASSIFIED WORKERS MAKE SIGNIFICANTLY LESS THAN WORKERS PAID AS EMPLOYEES.** One government expert calculated that a construction worker earning \$31,200 a year before taxes would be left with an annual net compensation of \$10,660.80 if paid as an independent contractor, compared to \$21,885.20 if paid properly as an employee.<sup>53</sup> And a study on port truck drivers found that annual median net earnings before taxes were \$28,783 for drivers paid as contractors as compared with \$35,000 for employees.<sup>54</sup>
- **TARGETED AUDITS ARE COST-EFFECTIVE AND HAVE THE POTENTIAL OF RETURNING HUNDREDS OF MILLIONS OF DOLLARS**

TO STATE COFFERS. Audits conducted by California's Employment Development Department between 2005 and 2008, for example, recovered roughly \$173 million in payroll tax assessments, over \$28 million in labor code citations, and more than \$64 million in assessments on employment tax fraud cases. Since it was formed in September 2007, the New York Joint Enforcement Task Force has assessed over \$21.5 million unemployment taxes and over \$1.85 million in unemployment insurance fraud penalties, and over \$2.3 million in workers' compensation fines and penalties. The Washington State Labor and Industry Fraud Prevention and Compliance Program (focused on workers' compensation) reported that it brought in over \$7 for every dollar invested in enforcement efforts.<sup>55</sup> Utah conducted 913 targeted audits between 2008 and 2012, uncovering \$138 million in unreported wages.<sup>56</sup> These numbers do not take into account fraud that is deterred before a violation even takes place, when employers take note of aggressive enforcement activities and voluntarily come into compliance.

Misclassification of employees as independent contractors exacts an enormous toll on workers and our economy. Accurate information on the prevalence of the problem, and on patterns of violations, can help state officials to direct their efforts at the worst violators and most problematic industries. The growing body of research summarized here has been vital to recent efforts in the states to combat misclassification; new research will further facilitate enforcement.

## **About NELP**

*The National Employment Law Project is a non-partisan, not-for-profit organization that conducts research and advocates on issues affecting low-wage and unemployed workers. In partnership with grassroots and national allies, NELP promotes policies to create good jobs, enforce hard-won workplace rights, and help unemployed workers regain their economic footing. For more about NELP, please visit [www.nelp.org](http://www.nelp.org).*

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## **End Notes**

- 1 Coopers & Lybrand, *Projection of the Loss in Federal Tax Revenues Due to Misclassification of Workers*, Prepared for the Coalition for Fair Worker Classification (1994).
- 2 Lalith De Silva, et al., *Independent Contractors: Prevalence and Implications for Unemployment Insurance Programs*, Planmatics, Inc., Prepared for the US Department of Labor Employment and Training Administration (2000), available at <http://wdr.doleta.gov/owsdrr/00-5/00-5.pdf>.
- 3 U.S. General Accounting Office, *Employee Misclassification: Improved Coordination, Outreach, and Targeting Could Better Ensure Detection and Prevention* (August 2009), available at <http://www.gao.gov/products/GAO-09-717>. See also, Treasury Inspector General for Tax Administration, *While Actions Have Been Taken to Address Worker Misclassification, and Agency-Wide Employment Tax program and Better Data are Needed* (February 4, 2009), available at <http://www.treas.gov/tigta/auditreports/2009reports/200930035fr.pdf> (explaining that "Preliminary analysis of Fiscal-Year 2006 operational and program data found that underreporting

attributable to misclassified workers is likely to be markedly higher than the \$1.6 billion estimate from 1984.”)

- 4 Tim Crowley, UI Tax Chief, U.S. Department of Labor, *Worker Misclassification – An Update from Constitution Ave.* (Oct. 24, 2012) [http://www.naswa.org/assets/utilities/serve.cfm?gid=86824dbe-575c-4edb-9e93-444cef85c837&dsp\\_meta=0](http://www.naswa.org/assets/utilities/serve.cfm?gid=86824dbe-575c-4edb-9e93-444cef85c837&dsp_meta=0).
- 5 A 2010 study by the Congressional Research Service built on earlier national studies to compare the costs and benefits of improved classification if President Obama’s proposed modification of Section 530 of the Revenue Act of 1978 were passed. The modification would permit the IRS to prospectively reclassify workers who are misclassified. The US Treasury estimated that the proposal would yield \$8.71 billion for the period of FY 2012 through 2021. The CRS study acknowledged, however, that the work needed to reduce misclassification “would impose significant costs.” James M. Bickley, *Tax Gap: Misclassification of Employees as Independent Contractors*, Congressional Research Service (March 10, 2011), available at [http://op.bna.com/dlrcases.nsf/id/vros-8euvqa/\\$File/taxgap.pdf](http://op.bna.com/dlrcases.nsf/id/vros-8euvqa/$File/taxgap.pdf).
- 6 DOL’s study will gather information about workers’ employment classification and pay arrangements and will measure workers’ knowledge about their current job classification, and their knowledge about the rights and benefits associated with their job status. Proposed Information Collection Request (ICR) for the Worker Classification Survey; Comment Request, Fed. Reg. 78, 2247 (Jan 11, 2013) <http://www.gpo.gov/fdsys/pkg/FR2013-01-11/pdf/2013-00389.pdf>
- 7 Some states have created task forces but have not conducted a quantitative study, demonstrating the difficulty in compiling data on misclassification. For example, New Hampshire established the Joint Agency Task Force on Employee Misclassification Enforcement in September of 2010 and published its first report in September of 2011, but the report did not contain state-specific data on the incidence or cost of independent contractor misclassification. Joint Agency Task Force on Employee Misclassification

Enforcement, *First Report of the Joint Agency Task Force on Employee Misclassification Enforcement* (September 1, 2011), available at <http://www.nh.gov/nhworkers/documents/1stReportofthejaeme.pdf>.

The Governor of North Carolina recently issued an executive order creating the Governor’s Task Force on Employee Misclassification but the Task Force has not yet issued a report. See “EO 125: Establishing the Governor’s Task Force on Employee Misclassification” (August 2012), available at <http://www.governor.state.nc.us/NewsItems/ExecutiveOrderDetail.aspx?newsItemID=2555>.

- 8 Tax audits conducted by California’s Employment Development Department (EDD) from 2005 to 2008 identified 49,738 previously unreported employees. The number of unreported employees increased 54% from 2005 to 2007, reaching 15,751 workers in 2007. The number then dipped to 13,202 in 2008. During the 4-year period from 2005 to 2008, the EDD recovered a total of \$173,516,334 in payroll tax assessments, \$28,950,656 in labor code citations, and \$ 64,229,829 in assessments on employment tax fraud cases. The Tax Audit Program as a whole in 2008 conducted 6,356 audits and investigations resulting in assessments totaling \$193,781,599 and identifying 64,539 previously unreported employees. California Employment Development Department, Annual Report: Fraud Deterrence and Detection Activities, report to the California Legislature (June 2009), available at [http://www.edd.ca.gov/pdf\\_pub\\_ctr/report2009.pdf](http://www.edd.ca.gov/pdf_pub_ctr/report2009.pdf).

In 2012 California’s Employment Development Department’s (EDD) Tax Branch conducted 4,290 audits and investigations, resulting in assessments totaling \$230.6 million, and identified 89,063 unreported employees.

The Compliance Development Operations within the EDD Tax Branch, which includes several programs that concentrate on the underground economy, conducted 2,600 joint inspections, identified 13,226 previously unreported employees, assessed \$36 million in payroll tax assessments and assessed over \$9 million on fraud cases in 2012. California

Employment Development Department, *Annual Report: Fraud Deterrence and Detection Activities*, report to the California Legislature (June 2013), available at [http://www.edd.ca.gov/about\\_edd/pdf/Fraud\\_Deterrence\\_and\\_Detection\\_Report13.pdf](http://www.edd.ca.gov/about_edd/pdf/Fraud_Deterrence_and_Detection_Report13.pdf)

- 9 The US DOL reported that 33.9% of audited employers in Colorado misclassified employees as independent contractors; 41,915 employers in the state had misclassified new workers as independent contractors; 8.5% of workers at audited employers were found to have been misclassified; 172,609 workers statewide misclassified; total taxable wages underreported statewide for new workers misclassified as independent contractors: \$36,291,042; tax underreported statewide for new workers misclassified as ICs: \$6,429,685; average UI tax rate: 17.7%; percent of state UI taxes underreported due to workers misclassified as ICs: 3.6%. See Planmatics report, note 2, supra.
- 10 A 1992 study estimated that the state and the federal governments were losing \$500 million annually as a result of worker misclassification. Each year, state income tax receipts were reduced by \$65 million; the workers' compensation system lost \$57 million in unpaid premiums; and the unemployment insurance fund lost \$17 million. William T. Alpert, *Estimated 1992 Costs in Connecticut of the Misclassification of Employees*, Department of Economics, University of Connecticut (1992). The 2011 annual report from the Joint Enforcement Commission on Worker Classification reported that from March 1, 2010 through February 28, 2011 the Tax Division's Field Audit Unit completed approximately 1,600 audits and another 9,000 individual wage complaint investigations. Those investigations resulted in the reclassification of approximately 6,500 workers and the discovery of roughly \$50 million in previously unreported or underreported payroll. During the same period, the Department of Revenue Services conducted audits that resulted in the assessment of \$611,568 in additional taxes, penalties and interest. The Department of Revenue Services assessed an additional almost \$611,600 in unpaid

taxes, penalties and interest. *State of Connecticut Joint Enforcement Commission on Worker Misclassification, Annual Report, Prepared for the Honorable Dannel Malloy, Governor and the Labor and Public, Employees Committee of the General Assembly* (December 2011), available at <http://www.ctdol.state.ct.us/wgwkstnd/JEC/JEC.pdf>. Figures on incidence of misclassification among audited workers from Planmatics report, note 2, supra.

- 11 A 2006 study estimated that independent contractor misclassification resulted in a loss of \$39.2 million in unemployment insurance taxes, and between \$124.7 million and \$207.8 million in state income taxes each year from 2001 to 2005. Close to 18% of audited employers, about 56,650, misclassified employees as independent contractors. The study estimated that an average 368,685 employees were misclassified each year. The rate of misclassification by violating employers increased 21% from 2001 to 2005. Michael P. Kelsay, *et al.*, *The Economic Costs of Employee Misclassification in the State of Illinois*, Department of Economics, University of Missouri-Kansas City (2006), available at <http://www.carpenters.org/EmployerPayrollFraud/studies/reports.aspx>. Other reports for which there no url is listed can be found on the United Brotherhood of Carpenters website.
- 12 According to a 2010 report, 47.5% of Indiana employers audited by the state in 2007-2008 – approximately 73,629 employers – were found to have misclassified workers as independent contractors; 8,200 of these employers were in the construction industry. The number of Indiana employees affected by improper misclassification is estimated to have averaged 418,086 annually for the period 2007-2008, about 16.8% of employees overall. In each year from 2007-2008, the state lost \$147.5 million in state income tax revenue and \$24.1 million in unpaid workers' compensation premiums, while the unemployment insurance system lost an average of \$36.7 million. Michael P. Kelsay and James I. Sturgeon, *The Economic Costs of Employee Misclassification in the State of*

Indiana, Department of Economics, University of Missouri-Kansas City (2010) available at <https://www.carpenters.org/misclassification/all%20documents/Misclassification%20in%20Indiana%20Summary%20Report%209-10.pdf>.

- 13 The Iowa Misclassification Task Force's 2<sup>nd</sup> Report noted that 230 employers were found to have flouted the law by misclassifying workers, creating a competitive advantage over some 72,000 law-abiding employers. Through audits and missing wage investigations completed by Unemployment Insurance Tax Bureau field auditors from July 1, 2009 through December 30, 2010, 134 employers were found to have misclassified a total of 544 workers. These employers failed to report \$5,692,181 in employee wages to IWD for unemployment insurance tax purposes and owed a total of \$130,511 in unpaid unemployment insurance taxes, penalty and interest. *Iowa Misclassification Task Force 2<sup>nd</sup> Report*, Iowa Workforce Development (December 30, 2010), available at <http://www.iowaworkforce.org/misclassification/MisClass2010Report.pdf>.
- 14 From 1999 to 2002, 11% of all Maine employers and 14% of construction employers misclassified their workers, totaling 4,792 misclassified workers across all industries. Misclassification of construction workers resulted in an annual average loss of \$314,000 in unemployment compensation taxes, \$6.5 million in workers compensation premiums, between \$2.6 million and \$4.3 million in state income taxes, and \$10.3 million in FICA taxes. Françoise Carré and Randall Wilson, *The Social and Economic Costs of Employee Misclassification in the Maine Construction Industry*, Construction Policy Research Center, Labor and Worklife Program, Harvard Law School and Harvard School of Public Health (2005), available at <http://www.law.harvard.edu/programs/lwp/Maine%20Misclassification%20Maine.pdf>.
- 15 A study of misclassification in the state's construction industry from 2001-2003 found that at least 14% of Massachusetts construction employers and 13% of all Massachusetts employers

misclassified workers. Less conservative methods suggest that construction misclassification could run higher and range up to one in four (24%) of Massachusetts construction employers. An estimated 7,478 to 15,790 of construction employees were misclassified. In the workforce as a whole, an estimated 125,725 to 248,206 workers were misclassified. The state lost an estimated \$91 million to \$152 million in income tax revenue and up to \$91 million of worker compensation premiums. The study noted that both the prevalence of misclassification and the severity of the impact have worsened over the years. Françoise Carré and Randall Wilson, *The Social and Economic Costs of Employee Misclassification in the Construction Industry*, Construction Policy Research Center, Labor and Worklife Program, Harvard Law School and Harvard School of Public Health (2004), available at <http://www.law.harvard.edu/programs/lwp/Misclassification%20Report%20Mass.pdf>. In 2012, Massachusetts' Joint Task Force on the Underground Economy and Employee Misclassification recovered over \$15.4 million through its enforcement efforts: the Department of Unemployment Assistance recovered \$13 million in unpaid employer contributions to the UI Trust Fund and Fair Share Contribution; the Department of Revenue recovered \$328,000 in unpaid taxes; and the Attorney General's Office brought in \$593,400 in restitution, penalties, and fines related to violations of the state's wage and hour and independent contractor laws. The Department of Industrial Accidents (DIA) issued 15 stop work orders for lack of workers' compensation coverage, brought 81 workers under coverage, and recovered \$10,500 in fines from employers. In its complementary enforcement process, the DIA brought coverage to 7,016 workers, issued 2,707 stop work orders and assessed \$1.4 million in fines from employers. Massachusetts Department of Labor, *Joint Task Force on the Underground Economy and Employee Misclassification 2012 Annual Report* (August 2013), available at <http://www.mass.gov/lwd/eolwd/jtff/>

[annual-report-2012.pdf](#)

16 Audits conducted by Maryland's Unemployment Insurance Division found an average of 20% of employers misclassify workers. The Division's report estimated that misclassification accounts for an annual loss of between \$15 million and \$25 million to the Unemployment Trust Fund. The Secretary of the Department of Labor noted that the estimate is likely conservative because audits are random, do not target industries where misclassification is most prevalent, and do not capture the underground economy. Testimony of Thomas E. Perez, Secretary of the Department of Labor, Licensing and Regulation, on HB 1590, before the House Economic Matters Committee (March 20, 2008), available at <http://www.dllr.state.md.us/whatsnews/testimonymisclass.shtml>. In 2009 Maryland passed the Workplace Fraud Act of 2009 and created the Joint Enforcement Task Force on Workplace Fraud. The Task Force established work-groups on enforcement and education and began coordinating unemployment insurance tax investigations, identifying 8,474 misclassified workers and approximately \$50.9 million in unreported wages paid to employees. David W. Stevens, *An Estimate of Maryland's Annual Net Unemployment Compensation Tax Loss from Misclassification of Covered Employees*, Baltimore, MD (February 1, 2009). In its 2011 report, the Task Force noted that misclassification costs the Unemployment Insurance Trust Fund up to \$22 million every year. In 2011, the Department of Labor & Industry opened 660 investigations and issued citations to 12 companies; the Division of Unemployment Insurance completed 76 UI Workplace Fraud Audits and identified 3,178 misclassified workers and over \$17 million in unreported wages paid to employees, while UI Workplace Fraud Audits resulted in \$618,752 paid into the UI trust fund; and the Comptroller completed 7 joint audits with the Task Force, which resulted in \$364,400 assessed for withholding taxes. Department of Labor, Licensing and Regulation, *Annual Report of the Joint Enforcement*

*Task Force on Workplace Fraud* (December 2011), available at <http://www.msa.md.gov/megafile/msa/speccol/sc5300/sc5339/000113/014000/014584/unrestricted/20120420e.pdf>.

17 A 2008 study of Michigan's unemployment insurance system found that an average of 30% of employers misclassify employees or underreport employee payroll, and that 8% of the state's construction workers are misclassified or receive income that is not reported by their employer. Each year, about \$1.5 billion in payroll is not reported to the UI Agency. Misclassification costs the state's unemployment insurance trust fund \$17 million each year, and results in an estimated loss of \$20 to 33 million in state income taxes. Dale Belman and Richard Block, *Informing the Debate: The Social and Economic Costs of Employee Misclassification in Michigan*, Michigan State University (2009), available at <http://www.ippsr.msu.edu/Publications/BEBelman.pdf>. Michigan established its Underground Economy Task Force in June 2008. The Task Force found that more than 8% of Michigan employees are misclassified, \$16.8 million in UI payments went uncollected, and \$30 million in wages were not reported. Michigan Supreme Court, *Underground Economy* (June 2010), available at: <http://courts.michigan.gov/scao/resources/publications/reports/UETF-2010.pdf>.

18 The Minnesota Office of the Legislative Auditor used UI audit data to estimate that 14% of employers misclassified workers in 2005 – about 17,500 employers. Misclassification rates in the construction industry were higher: 15% of construction employers and 31% of drywall employers misclassify their employees. The estimates are conservative because they exclude employers that operate in the “cash” economy or fail to register in the unemployment program. James Noble, *Misclassification of Employees as Independent Contractors*, Program Evaluation Division, Minnesota Office of the Legislative Auditor (2007), available at <http://www.auditor.leg.state.mn.us/ped/pedrep/missclass.pdf>.

- 19 Mo. Dep't of Labor and Indus. Relations, *Are you Off the Books?* (2013), available at <http://labor.mo.gov/offthebooks>
- 20 From July 1, 2010 - June 30, 2011, Nebraska UI Tax field representatives conducted 938 audits and investigations; 669 of these audits targeted high violation industries. Of these 669 audits, 1,039 misclassified workers and additional tax collections of \$42,559 were uncovered. *Nebraska Employee Misclassification Act, Annual Report 2010-11*. Nebraska Department of Labor (2011), available at <http://dol.nebraska.gov/employers/safety/EmpClassAct/2011%20Employee%20Classification%20Act%20Annual%20Report.pdf>.  
From July 1, 2011 – June 30, 2012, UI Tax field representatives completed 766 audits and missing wage investigations. Of those, 727 field audits targeted high violation industries resulted in 947 misclassified workers and additional tax collections of \$44,826.08. <http://dol.nebraska.gov/employers/safety/EmpClassAct/2012EmployeeClassificationActReport.pdf>
- 21 Nevada Employment Security Division records indicate that 12.4 percent of benefit claims investigations involved a claim of independent contractor misclassification and 2.7 percent of audited employment was misclassified. This led to a conservative estimate of approximately 31,000 employees in the state that may be misclassified. The estimated annual revenue lost to the Unemployment Trust Fund is \$8.2 million. *Employee Misclassification- Bulletin No. 11-07*. Nevada Legislative Counsel Bureau (January 2011), available at <http://leg.state.nv.us/Division/Research/Publications/InterimReports/2011/Bulletin11-07.pdf>.
- 22 New Jersey Department of Labor and Workforce Development (Nov. 8, 2007).  
23 A 2007 study issued by the Cornell University School of Industrial and Labor Relations, based on audits by the New York DOL UI Division of select industries from 2002-05, estimated annual misclassification rates of about 10.3% in the state's private sector and approximately 14.9% in the construction industry. Each year, an estimated 39,587 employers within those audited industries misclassified workers. Approximately 704,785 workers were misclassified. Average UI taxable wages underreported due to misclassification each year was \$4,238,663, and UI tax underreported was \$175,674,161. Linda H. Donahue, James Ryan Lamare, Fred B. Kotler, *The Cost of Worker Misclassification in New York State*, Cornell University School of Industrial Labor Relations (February 2007), available at <http://digitalcommons.ilr.cornell.edu/reports/9/>. According to the February 2014 report by the Joint Enforcement Task Force on Employee Misclassification, since its inception in 2007, the Task Force has identified over 114,000 instances of employee misclassification and discovered over \$1.8 billion in unreported wages; . The 2013 sweeps were conducted at construction sites, bars/restaurants, adult entertainment venues, automotive tire and repair centers, grocery stores, and retail establishments. In 2013, completed audits and investigations of businesses found through the JETF sweeps: uncovered nearly \$62.2 million in unreported wages; resulted in the assessment of over \$2.2 million in additional unemployment insurance contributions; and revealed over 4,700 misclassified workers. <http://www.labor.ny.gov/agencyinfo/PDFs/Misclassification-Task-Force-Report-2-1-2014.pdf>  
A 2007 study estimated that between \$25 billion and \$50 billion in payroll – 20% of total payroll – was unreported for workers' compensation. The estimate may be conservative, because it was calculated by comparing payroll reported to the state for UI with payroll reported to the WC system, and did not account for payroll that was not reported to either

system. Fiscal Policy Institute, *Building up New York, Tearing Down Job Quality: Taxpayer Impact of Worsening Employment Practices in New York City's Construction Industry* (December 2007), available at [http://www.fiscalpolicy.org/publications2007/FPI\\_BuildingUpNY\\_TearingDownJobQuality.pdf](http://www.fiscalpolicy.org/publications2007/FPI_BuildingUpNY_TearingDownJobQuality.pdf).

- 24 A 2009 report by the Ohio Attorney General – extrapolating from UI audit data, and using findings from other state studies – estimated that between 54,000 and 459,000 workers were misclassified each year, and found that the state lost between \$12 million and \$100 million in unemployment compensation payments, between \$60 million and \$510 million in workers compensation premiums and between \$21 million and \$248 million in forgone state incomes tax revenues. Report of the Ohio Attorney General on the Economic Impact of Misclassified Workers for State and Local Governments in Ohio (Feb. 18, 2009), available at <http://www.ohioattorneygeneral.gov/getattachment/f2b2aa5b-de26-45a2-9631-2e0fd21cf9b5/Misclassification-Report.aspx>.
- 25 A 2008 study found that 9% of Pennsylvania's workforce, or 580,000 workers, are misclassified as independent contractors each year. Misclassification resulted in a loss of over \$200 million to the unemployment compensation trust fund and \$81 million to the workers compensation system. Testimony of Patrick I. Beaty, Deputy Secretary for Unemployment Compensation Programs, Pennsylvania Department of Labor and Industry, before the House of Representatives Commonwealth of Pennsylvania, Labor Relations Committee on HB 2400, The Employee Misclassification Prevention Act (April 23, 2008), available at [http://www.legis.state.pa.us/cfdocs/legis/TR/transcripts/2008\\_0091\\_0001\\_TSTMNY.pdf](http://www.legis.state.pa.us/cfdocs/legis/TR/transcripts/2008_0091_0001_TSTMNY.pdf).
- The office of Unemployment Compensation Services is conducting audits of registered and unregistered employers in industries, where historically workers have been misclassified. During 2012, OUCTS discovered 8,971 misclassified workers and \$2,453,944.37 in underreported contributions. This effort will continue in 2013.

[file:///C:/Users/kfreund/Downloads/Actuarial\\_Evaluation.pdf](file:///C:/Users/kfreund/Downloads/Actuarial_Evaluation.pdf)

- 26 Audits by Traveler's Insurance Company over a 12 month period beginning in October 2011 revealed that only about 63% of employers classified workers as employees for both workers' compensation and unemployment purposes that have been insured by Travelers. If a business has workers and has obtained a workers' compensation insurance policy to provide coverage to those workers, the same workers should be eligible for unemployment insurance, and the business should pay unemployment taxes in addition to workers' compensation insurance premiums. It should be noted that the majority of businesses misclassifying workers are smaller businesses. It is at this "grass roots" level that the misclassification begins and finds its way to the other business sectors such as commercial construction. Only 50% of trucking businesses and 12% of residential construction businesses consistently classified workers as employees for both workers compensation and unemployment insurance. Tennessee's Employee Misclassification Advisory Task Force recommends sharing information among existing agencies and appointing additional investigators to identify noncompliant employers, but small scale investigations support the assertion that employee misclassification is prevalent in some industries. Investigations of 32 companies in the drywall, painting, framing, general construction, and roofing industry identified 1,035 misclassified workers and half a million in money owed to the state. Investigations of 23 drywall employers identified 884 misclassified workers and \$374,652 in money owed to the state.
- EMPLOYEE MISCLASSIFICATION TASK FORCE, 2013 ANNUAL REPORT 20 (2013), available at [http://www.tn.gov/labor-wfd/EMEEF/AnnualReports/2013\\_EMATF\\_AnnualReport.pdf](http://www.tn.gov/labor-wfd/EMEEF/AnnualReports/2013_EMATF_AnnualReport.pdf)
- The Employee Misclassification Advisory Task Force's first annual report in 2012 highlights findings contained in Dr. William Canak and Dr. Randall Adams' 2010 study. The study estimates that between

21,990 and 38,680 construction workers were either misclassified or unreported in 2006 - approximately 17% of all construction workers. The study also estimated losses of between \$8.4 million and almost \$15 million to the state's unemployment insurance program, between \$52 million and \$91.6 million to the state's workers compensation program, between \$15.2 million and \$73.4 million in federal income taxes, and between \$7.8 million and \$42 million in Social-Security and Medicare taxes. William Canak & Randall Adams, *Misclassified Construction Employees in Tennessee* (January 15, 2010); Employee Misclassification Advisory Task Force, *2012 Annual Report* (January 30, 2010), available at [http://www.tn.gov/labor-wfd/EMEEF/2012\\_EMATF\\_AnnualReport.pdf](http://www.tn.gov/labor-wfd/EMEEF/2012_EMATF_AnnualReport.pdf).

- 27 Based on estimates using 2006 data, Tennessee lost between \$2.1 million and \$3.7 million in uncollected workers' compensation premium taxes Tennessee's estimated losses from unpaid unemployment insurance premiums range from \$8.4 million to \$14.9 million. Workers' compensation insurers lost an estimated \$52.1 million to \$91.6 million in unpaid workers' compensation premiums. Actual TDLWD Unemployment Insurance audit figures related to misclassification for the last two years revealed that in 2013, 1,537 audits were conducted where 1,930 misclassified workers were discovered with net total wages of \$36,442,784. In 2012, 1,421 audits revealed 2,510 misclassified workers with total wages of \$25,456,799. <https://www3.workcompcentral.com/fileupload/uploads/2014-07-17-030728EMEEF%202014%20Annual%20Report%20to%20Leg.pdf>
- 28 A 2009 study found that 38% of the construction workers in the Austin area were misclassified. In "vertical construction" alone, this misclassification resulted in an estimated loss of at least \$8,618,869 in federal taxes and state unemployment taxes. *Building Austin, Building Injustice: Working Conditions in Austin's Construction Industry*, Workers Defense Project in collaboration with the Division of Diversity and Community Engagement at the

University of Texas at Austin (June 2009), available at <http://www.buildaustin.org/Building%20AustinReport.pdf>

- For a 2012 study, researchers from the same organizations surveyed 1,194 construction workers, conducted in-depth interviews with workers and employers, and analyzed government data, finding that at least 41% of Texas construction workers are misclassified as independent contractors or paid off-the-books in cash or by check. The researchers extrapolated from this 41% figure to estimate that approximately 308,793 construction workers in the state are misclassified as independent contractors, costing the Texas UI Fund \$54.5 million annually. The researchers also found that 7.6% of construction workers experienced wage theft within the past year, costing the state an estimated \$8.8 million in lost sales tax. *Build a Better Texas: Construction Working Conditions in the Lone Star State*, Workers Defense Project in collaboration with the Division of Diversity and Community Engagement at the University of Texas at Austin (January 2013), available at [http://www.workersdefense.org/Build%20a%20Better%20Texas\\_FINAL.pdf](http://www.workersdefense.org/Build%20a%20Better%20Texas_FINAL.pdf).
- 29 The Unemployment Insurance Division of the Department of Workforce Services completes both "random" and "targeted" audits of Utah employers. In the four and one-half year period between January 1, 2008 and June 30, 2012, the division completed 5233 "random" audits, covering \$1.4 billion in total reported wages. The random audits identified \$42 million in total unreported wages to 6949 workers who were misclassified as "independent contractors." The random audits revealed a variance of 2.9% (.029). During the same time period the division completed 913 "targeted" audits of Utah employers, covering \$970 million in total reported wages. Targeted audits, which primarily use IRS form 1099 information to identify potential unreported workers, yield different results. The targeted audits identified \$138 million in total unreported wages to 18,114 workers who were misclassified as "independent contractors."

The targeted audits revealed a variance of almost 14% (.14)” Jody McMillan, Chief of Contributions, Utah Department of Workforce Services, *Effective Methods to Detect and Deter Worker Misclassification* (Oct. 24, 2012).

- 30 The Vermont Workers’ Compensation Task Force issued a report in April 2009. It found that 10-14% of Vermont employers misclassify their workers. *Vermont Workers’ Compensation Task Force 2008-2009 Progress Report*, available at [http://www.nh.gov/nhworkers/documents/vt\\_08-09\\_rpt.pdf](http://www.nh.gov/nhworkers/documents/vt_08-09_rpt.pdf).
- 31 The Virginia Joint Legislative Audit and Review Commission (JLARC) relied on data compiled by the Virginia Employment Commission (VEC) in 2010, finding that of the 1% of employers audited by the VEC, 27% of them had misclassified at least 1 employee. The study acknowledged that the targeted nature of the audits may have resulted in an inflated estimate of the proportion of employees misclassified in all sectors. JLARC’s study also found that roughly \$28 million was lost in unpaid state income taxes. Joint Legislative Audit and Review Commission, *Review of Employee Misclassification in Virginia*, Report to the Governor and the General Assembly of Virginia (June 11, 2012), available at [http://www2.timesdispatch.com/mgmedia/file/768/20120612\\_jlarc/](http://www2.timesdispatch.com/mgmedia/file/768/20120612_jlarc/).
- 32 The 2010 Washington State Underground Economy Benchmark Report reported that, in FY 2010, the three departments uncovered a combined 1,677 unregistered businesses that were assessed nearly \$39 million in unpaid taxes, premiums, penalties, and interest. The department of Labor & Industries conducted 5,846 audits with an associated \$26.4 million in assessments from worker misclassification and unregistered businesses; the Employment Security Division conducted 4,006 audits with an associated \$2.51 million in assessments from worker misclassification, unreported wages and unregistered businesses; and the Department of Revenue assessed a total of \$29,718,684 in unpaid taxes, penalties and interest from previously unregistered businesses that were involuntarily registered. *Underground*

*Economy Benchmark Report: 2010 Report to the Legislature*, Joint Report of the Washington State Department of Labor and Industries, Washington State Department of Revenue, and the Washington State Employment Security Division (November 2010), available at <http://www.lni.wa.gov/Main/docs/UWBenchmarkFY2010.pdf>. An earlier report by the Washington Department of Revenue studied discrepancies in the number of businesses that had registered with the IRS but not with the State, finding that in-state and out-of-state businesses registered with the IRS in 2004 failed to pay \$274 million in state taxes: \$225 million in state income taxes, \$14.8 million in unemployment insurance taxes, and \$34.5 million in workers compensation premiums. In-state construction employers failed to pay \$13.1 million in taxes: \$1 million in state income tax, \$3.4 million in unemployment insurance taxes, and \$8.7 million in workers compensation. In 2001, the state lost \$183 million in taxes from employers registered with neither the IRS nor the state. Washington State Dept. of Labor and Industries and the Washington State Employment Security Dept., *Unregistered Business Study: Joint Report of the Washington State Dept. of Revenue* (November 2007), available at [http://dor.wa.gov/docs/reports/Unregistered\\_Business\\_Study\\_finalfinal.pdf](http://dor.wa.gov/docs/reports/Unregistered_Business_Study_finalfinal.pdf). The Joint Legislative Task Force on the Underground Economy in the Construction Industry also found that over \$100 million state income taxes were not being paid in that industry. Available at [http://www.leg.wa.gov/JointCommittees/UECI/Documents/FinalReport\\_1-20-2009.pdf](http://www.leg.wa.gov/JointCommittees/UECI/Documents/FinalReport_1-20-2009.pdf).

- 33 The *2010 Annual Fraud Report to the Legislature: Targeting Fraud and Abuse*, Washington State Department of Labor & Industries, reported on the Fraud and Compliance program examining workers’ compensation fraud in Washington State. The program identified unpaid premiums for 62% of employers that were targeted for audits, based on a screening process, and they assessed \$26.4 million through employer audits. The Report also noted that the program brought in over \$7 for every dollar

- invested, when the program's operating costs were compared to the money recovered, collected and avoided during the fiscal year. For FY 2010, nearly 250 FTEs were employed in the program.
- 34 The Wisconsin Unemployment Insurance Division found that 44% of the workers investigated in the course of employer audits had been misclassified. *Report of the Worker Misclassification Task Force*, Submitted to Secretary Roberta Gassman, Wisconsin Department of Workforce Development (June 2009).
- 35 Richard Cordray, Ohio Attorney General, *Misclassification of Employees as Independent Contractors* (May 11, 2010).
- 36 Maryland Department of Labor, Licensing and Regulation, *Annual Report of the Joint Enforcement Task Force on Workplace Fraud* (December 2011), available at <http://dllr.state.md.us/workplacefraudtaskforce/2010workplacefraudrpt.pdf>
- 37 See *Annual Report: Fraud Deterrence and Detection Activities* (June 2013), supra note 6.
- 38 See *State of Connecticut Joint Enforcement Commission on Worker Misclassification, Annual Report* (December 2011), note 8, supra.
- 39 See *Annual Report of the Joint Enforcement Task Force on Employee Misclassification*, (February 1, 2013), note 13, supra.
- 40 See *The Economic Costs of Employee Misclassification in the State of Illinois*, note 9, supra.
- 41 *The Social and Economic Costs of Employee Misclassification in the Maine Construction Industry*, supra note 12.
- 42 *The Social and Economic Costs of Employee Misclassification in the Construction Industry*, supra note 13.
- 43 *The Cost of Worker Misclassification in New York State*, note 20, supra.
- 44 Report of the Ohio Attorney General on the Economic Impact of Misclassified Workers for State and Local Governments in Ohio, note 21, supra.
- 45 Testimony of Patrick T. Beaty, Deputy Secretary for Unemployment Compensation Programs, Pennsylvania Department of Labor and Industry, before the House of Representatives Commonwealth of Pennsylvania, Labor Relations Committee on HB 2400, The Employee Misclassification Prevention Act (April 23, 2008), note 22, supra.
- 46 *Review of Employee Misclassification in Virginia*, Report to the Governor and the General Assembly of Virginia (June 11, 2012), note 26, supra.
- 47 See California Employment Development Department, *Annual Report*, note 6, supra, and New York DOL *Annual Report of the Joint Enforcement Task Force on Employee Misclassification*, note 20, supra.
- 48 See Cordray, *Misclassification of Employees as Independent Contractors*, note 30, supra.
- 49 US DOL Employment and Training Administration found that the average number of misclassified workers identified per audit rose from 1.1 in 2002 to 2.5 in 2011. Crowley, supra note 4.
- 50 See, for example, Erin Johansson, *Fed Up with FedEx: How FedEx Ground Tramples Workers' Rights and Civil Rights* (American Rights at Work, October 2007), available at <http://www.americanrightsatwork.org/dmdocuments/ARAWReports/fedupwithfedex.pdf>; and Rebecca Smith, David Bensman, and Paul Alexander Marvy, *The Big Rig: Poverty, Pollution, and the Misclassification of Truck Drivers at America's Ports*, (National Employment Law Project and Change to Win, 2010), available at <http://www.nelp.org/page/-/Justice/PovertyPollutionandMisclassification.pdf?nocdn=1>.
- 51 See, for example, *AG Coakley's Office Recovers over \$3 Million in Taxpayer Funds Back to Commonwealth in Settlement with FedEx Ground*, (July 15, 2010), available at <http://www.mass.gov/ago/news-and-updates/press-releases/2010/ago-recovers-over-3-million-in-taxpayer-funds.html>; *McDaniel Joins Inquiry into FedEx Worker Misclassification*, (March 18, 2010), available at <http://ag.arkansas.gov/newsroom/index.php?do:newsDetail=1&newsid=301>.
- 52 According to a recently updated study on misclassification in the port trucking industry, approximately 49,000 of the nation's 75,000 port

truck drivers are misclassified as independent contractors. Rebecca Smith, Paul Alexander Marvy and Jon Zerolnick, *The Big Rig Overhaul: Restoring Middle-Class Jobs at America's Ports through Labor Law Enforcement* (February 2014), available at <http://www.nelp.org/page/-/Justice/2014/Big-Rig-Overhaul-Misclassification-Port-Truck-Drivers-Labor-Law-Enforcement.pdf?nocdn=1>.

53 Crowley, *supra* note 4.

54 *The Big Rig Overhaul*, *supra* note 54, at 12

55 See website for the Washington Department of Labor and Industries, at <http://lni.wa.gov/ClaimsIns/FraudComp/WCFraud/About/Reports/default.asp>.

56 McMillan, *supra* note 29.

