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

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Introduction and Background

Employers increasingly misclassify their employees as independent contractors, denying them the protection of workplace laws, robbing unemployment insurance and workers' compensation funds of billions of much-needed dollars, and reducing federal, state and local tax withholding and revenues. State-level task forces, commissions, and research teams are using agency audits along with unemployment insurance and workers' compensation data to document the scope of independent contractor misclassification. Confirming the findings of earlier national studies, these state reports show that 10 to 30% of employers, or even more, misclassify their employees as "independent contractors," meaning that several million workers nationally may be misclassified. State and federal governments lose billions in revenues annually.

1. National studies and reports

Several government studies document the extent to which misclassification drains federal revenues. The data is limited, however, and should be updated to give a more accurate assessment of the current economic impact.

A 1994 study by Coopers and Lybrand estimated the federal government would lose $3.3 billion in revenues in 1996 due to independent contractor misclassification, and $34.7 billion in the period from 1996 to 2004.[1]

A 2000 study commissioned by the U.S. Department of Labor (DOL) – the "Planmatics" study – found that between 10% and 30% of audited employers misclassified workers.[2] Misclassification of this magnitude exacts an enormous toll: researchers found that misclassifying just one percent of workers as independent contractors would cost unemployment insurance (UI) trust funds $198 million annually. This report also shows that workers would benefit tremendously from increased scrutiny; up to 95% of workers who claimed they were misclassified as independent contractors were reclassified as employees following review.

A 2009 report by the Government Accountability Office (GAO) estimated independent contractor misclassification cost federal revenues $2.72 billion in 2006.[3] The GAO's estimate

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was derived from data reported by the IRS in 1984, finding that 15% of employers misclassified 3.4 million workers at a cost of $1.6 billion (in 1984 dollars). From 2000 to 2007, the number of misclassified workers identified by state audits increased from approximately 106,000 workers to over 150,000 workers. These counts likely undercount the overall number of misclassified employees because states generally audit less than 2% of employers each year.

A 2010 study by the Congressional Research Service estimated that a proposed modification to the IRS's "Safe harbor" rules, which currently allow employers significant leeway to treat workers as independent contractors for employment tax purposes, would yield $8.71 billion for FYs 2012-21. The proposal would permit the IRS to require prospective reclassification of workers who are currently misclassified and whose reclassification has been prohibited under current law.[4]

2. Findings from State Studies and 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 over 20 state-level studies. The studies rely on a range of data. Most studies rely on data from unemployment insurance and workers' compensation audits; 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

The 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.

Annual Losses Due to Independent Contractor Misclassification:
Summary of Leading State Studies[5]

* Indicates figures for the construction industry only.

State	% Employers who misclassify	Loss to UI	Loss to Wkrs Comp	Unpaid state income taxes
CA[6]	29% of audited employers			$194 mil (collected)
CO[7]	33.9%			
CT[8]	42% of audited employers	$17 mil	$57 mil	$65 mil $611,600 (collected)
IL[9]	19.5% ('05)	$53.7 mil ('05) $8.9 mil*	$97.9 mil $23.2 mil*	$124.7 - $207.8 mil $14.8 mil*
IN[10]	16.8%	$36.7 mil	$24.1 mil	$147.5 mil
IA[11]		$2.5 mil recovered		
ME[12]	11% 14%*	$314,000*	6.5 million*	$2.6 – 4.3 mil*
MA[13]	12% 14% *	$35 mil $3.9 mil* $2.4 mil (collected 2011)	$91 mil $7 mil* $2. 2 (collected)	$91 -152 mil $6.9 mil* $1.6 mil (collected 2004)
MD[14]	20-30% DOL study: 30%	$22 mil $3.5 mil (collected)		
MI[15]	30%	$17 mil		$20-33 mil
MN[16]	14% 15% *			
NE[17]	10%			
NV[18]	31,000 misclassified employees	$8.2 mil		
NJ[19]	38-42% of audited cases	$15 mil (UI and disability)		$5 mil
NY[20]	10.3% 14.9%*	$198 mil annually $14.5 mil (collected by JETF in 2011) $13 mil (IDed by NY DOL audits)	$1.1mil (incl. penalties) $640,000 (collected 2011)	$170 mil
OH[21]		$12 - $100 mil	$60-510 mil	$21-$248 mil
PA[22]	9%	$200 mil	$81 mil	
TN[23]	17%*	$8.4 - $15 mil	$52 - 91.6 mil $3 mil*	
Austin, TX[24]				$8,618,869 (state and federal combined)
VT[25]	10-14%			
VA[26]	27% of audited cases 30%*			$28
WA[27]	62% of audited cases[28]	$2.51 mil (collected)	$25.4 mil	$29.7 mil (collected)
WI[29]	44% of audited employers			

- **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 who are reclassified as employees following review. For example, targeted audits conducted by the Ohio 1099 Task Force resulted in the reclassification of almost 47% of the workers interviewed.[30] At just one company it audited, the Maryland Division of Labor & Industry's Division of UI Fraud found 537 misclassified workers and a total of $2,257,596 in taxable unreported wages.[31] From 2005-2008, California's Employment Development Department identified 49,738 workers who had been misclassified, including 13,202 in 2008 alone. According to its latest Taskforce report, the Connecticut DOL identified close to 6,500 misclassified workers.[32] The New York Task Force reported that it identified 18,500 misclassified workers in 2010, a total of 50,000 since the task force's start in September 2007, and that the NY DOL identified nearly 218,000 misclassified workers through UI audits.[33] Studies that extrapolate from audit data put the actual numbers of misclassified workers at much higher levels: an estimated 368,685 workers in Illinois;[34] 4,792 in Maine;[35] between 125,725 and 248,206 in Massachusetts;[36] 704,785 in New York;[37] between 54,000 and 459,000 in Ohio;[38] 580,000 in Pennsylvania;[39] and 214,000 in Virginia.[40]

- **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.[41] 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% from 2001 to 2005. A recent report by the Ohio Attorney General reported a 53.5% increase in the number of workers reclassified from 2008 to 2009.[42] 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.

- **Misclassification rates are disproportionately high in certain industries, such as construction, real estate, home care, trucking, janitorial and hi-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.[43] Sixteen states have negotiated with FedEx to end the delivery company's practice of misclassifying its drivers as independent contractors.[44] Reports indicate that employers in several other key sectors routinely misclassify workers.

- **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 & Industry Fraud Prevention and Compliance Program (focused on workers' compensation) reported that it brought in over $7 for every dollar invested in enforcement efforts.[45] 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.

[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] 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.

[5] 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 no Employee Misclassification" (August 2012), available at http://www.governor.state.nc.us/NewsItems/ExecutiveOrderDetail.aspx?newsItemID=2555.

[6] 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.

[7] 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.

[8] 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.

[9]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 incomes 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.

[10] 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.

[11] The Iowa Misclassification Task Force's 2nd 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 2nd Report, Iowa Workforce Development (December 30, 2010), available at http://www.iowaworkforce.org/misclassification/MisClass2010Report.pdf.

[12] 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.

[13] 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 2011, Massachusetts' Joint Task Force on the Underground Economy and Employee Misclassification recovered roughly $10.9 million through its enforcement efforts: the Department of Unemployment Assistance recovered $2.4 million in new unemployment insurance taxes; the Department of Revenue recovered $3.4 million in unpaid taxes; and the Attorney General's Office brought in $3 million in restitution, penalties, and fines related to violations of the state's wage and hour and independent contractor laws. The Department of Industrial Accidents brought under coverage 7,568 workers who had previously been without coverage, issued 3,058 stop work orders and assessed $2.1 million from employers for WC violations. Massachusetts Department of Labor, *Joint Task Force on the Underground Economy and Employee Misclassification 2011 Annual Report* (April 2012), available at http://www.mass.gov/lwd/docs/dia/task-force/jtfannualreport2011-fs.pdf .

[14] 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.

[15] 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.

[16] 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.

[17] 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.

[18] 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.

[19] New Jersey Department of Labor and Workforce audits found that between 38% and 42% of employers either misclassified workers or paid in cash "off-the-books," and between 25,000 and 28,286 workers were misclassified. *New Jersey State Agency Will Share Employment Tax Examination Results with the IRS*, State of New Jersey Department of Labor and Workforce Development (Nov. 8, 2007).

[20] 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 2012 report by the Joint Enforcement Task Force on Employee Misclassification, since its inception in 2007, the Task Force has identified over 68,100 instances of employee misclassification and discovered over $1.1 billion in unreported wages; it has conducted 106 joint sweeps. In 2011, the JETF identified over 19,600 cases of employee misclassification; discovered over $412 million in unreported wages; and assessed over $14.5 million in unemployment insurance taxes. The JETF conducted 27 sweeps in 2011, uncovering over $84.6 million in unreported wages, resulting in the assessment of nearly $1.5 million in additional unemployment insurance taxes, and uncovering over $640,000 in unpaid employee compensation. In addition to the JETF investigations conducted in 2011, the Department of Labor completed 14,800 audits and investigations finding nearly 131,700 misclassified workers and unpaid taxes of $48.5 million. *Annual Report of the Joint Enforcement Task Force on Employee Misclassification*, (February 1, 2012), available at http://www.labor.ny.gov/agencyinfo/PDFs/Misclassification-Task-Force-Report-2-3-2012.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.

[21] 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/Missclasification-Report.aspx.

[22] 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 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), available at http://www.legis.state.pa.us/cfdocs/legis/TR/transcripts/2008_0091_0001_TSTMNY.pdf.

[23] 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 incomes 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.

[24] 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%20_Austn_Report.pdf

[25] 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.

[26] 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/.

[27] 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 in workers compensation premiums. In-state construction employers failed to pay $13.1 million in taxes: $1 million in state income tax, $3.4 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. 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.

[28] 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.

[29] 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).

[30] Richard Cordray, Ohio Attorney General, *Misclassification of Employees as Independent Contractors* (May 11, 2010).

[31] 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.

[32] See *State of Connecticut Joint Enforcement Commission on Worker Misclassification, Annual Report* (December 2011), note 8, supra.

[33] See *Annual Report of the Joint Enforcement Task Force on Employee Misclassification*, note 20, supra.

[34] See *The Economic Costs of Employee Misclassification in the State of Illinois,* note 9, supra.

[35] *The Social and Economic Costs of Employee Misclassification in the Maine Construction Industry*, note 12, supra.

[36] *The Social and Economic Costs of Employee Misclassification in the Construction Industry*, note 13, supra.

[37] *The Cost of Worker Misclassification in New York State*, note 20, supra.

[38] Report of the Ohio Attorney General on the Economic Impact of Misclassified Workers for State and Local Governments in Ohio, note 21, supra.

[39] 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.

[40] *Review of Employee Misclassification in Virginia*, Report to the Governor and the General Assembly of Virginia (June 11, 2012), note 26, supra.

[41] 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.

[42] See Cordray, *Misclassification of Employees as Independent Contractors*, note 30, supra.

[43] 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.

[44] 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&news_id=301.

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