

**ANNUAL REPORT OF THE JOINT ENFORCEMENT
TASK FORCE ON EMPLOYEE MISCLASSIFICATION**

To
Honorable Andrew M. Cuomo
Governor State of New York

February 1, 2013

TASK FORCE MEMBERS

NEW YORK STATE DEPARTMENT OF TAXATION AND FINANCE
NEW YORK STATE WORKERS' COMPENSATION BOARD
NEW YORK STATE WORKERS' COMPENSATION BOARD FRAUD
INSPECTOR GENERAL
NEW YORK STATE ATTORNEY GENERAL
COMPTROLLER OF THE CITY OF NEW YORK

Submitted by:
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Chair, Joint Enforcement Task Force



Executive Summary

Governor Andrew M. Cuomo's Executive Order No. 2 continued the Joint Enforcement Task Force on Employee Misclassification (JETF), originally established in 2007 by Executive Order No. 17. Noting that employee misclassification has a significant adverse impact on the residents, businesses and economy in New York State, the Order charged the JETF with:

- investigating the practice of worker misclassification;
- coordinating state agencies to ensure enforcement of the laws violated when employers misclassify workers; and
- developing legislative proposals and other tools to combat the problem.

The Executive Order also requires the JETF to issue a report to the Governor on February 1 of each year describing its record and accomplishments, and proposing and identifying mechanisms for improved enforcement by the JETF.

Misclassification occurs when an employee is incorrectly labeled an independent contractor, or is not reported by the employer in any capacity (i.e. "off the books"). This practice hurts the government which is deprived of substantial revenues due to nonpayment of taxes and decreased legitimate business activity; hurts law abiding businesses which must compete with employers who engage in this illegal cost-cutting practice; and hurts employees by denying them the protection of various employment and labor laws by reducing compliance with employment and job safety standards.

In 2012, the Joint Enforcement Task Force on Employee Misclassification continued its efforts to address the serious problem of employee misclassification. The JETF carried out its mission by:

- engaging in joint enforcement sweeps;
- coordinating assignments among agency partners;
- making systematic referrals to appropriate law enforcement agencies; and
- implementing the sharing of data between agencies.

Additionally, with the passage of the Construction Industry Fair Play Act, which was signed into law in August 2010 and went into effect on October 26, 2010, the JETF focused considerable effort on ensuring awareness of this new law, assisting employers with compliance of the notice requirements, and ensuring enforcement of the law via investigations and tax payer protection operations. In 2012, the JETF:

- identified over 20,200 instances of employee misclassification;
- discovered over \$282.5 million in unreported wages; and
- assessed over \$9.7 million in unemployment insurance contributions.

Coordinated Enforcement Cases

In addition to the JETF investigations conducted in 2012, the Department of Labor completed 2,200 fraud investigations discovering over \$214.9 million in unreported wages and over \$7.9 million in unemployment insurance contributions due.

I. Background and Purpose of the Task Force

A. Employee Misclassification Defined

Employers with employees are subject to wage and hour laws, must register with the State, must pay unemployment and social security taxes, must withhold state and federal income taxes, and must obtain workers' compensation insurance. Employee misclassification occurs when a worker is improperly denied the benefits and protections provided to "employees" as that term is defined by state and federal law. Workers who are classified as employees receive a wide range of legal protections including eligibility for unemployment insurance if they are laid off, eligibility for workers compensation if they are injured on the job and, where applicable, the right to be paid the minimum wage and overtime pay.¹

Workers who are properly classified as independent contractors should be provided with a Form 1099 for tax reporting purposes, but the employer is not responsible for employment taxes and employee benefits.

There are two primary forms of worker misclassification:

Misclassification as an Independent Contractor

This occurs when a worker who meets the legal standards for classification as an employee is instead misclassified as an independent contractor. In New York State, whether a worker should be classified as an employee or as an independent contractor is dependent on what is called the "common law test." The essential elements of the common law test involve determining whether the worker is subject to the control and supervision of the employer in performing the job, whether the work that is performed is part of the usual work of the employer's business, and whether the worker has an independently established business offering services to the public, similar to the service they are performing for the employer. The implementation of the Construction Industry Fair Play Act results in a different test applicable to those working in the construction industry, known as the "ABC test." For additional information regarding this law, see page 8. Ultimately, the question is, who is responsible for this worker's taxes and bills, if he or she is injured on the job?

A recent study based on audits of New York employment records found that up to 10% of the employees covered by the audits may have been misclassified. Researchers found that misclassifying just 1% of workers as Independent Contractors would cost the Unemployment Insurance Trust Fund \$198 million annually, and that 95% of workers who claimed they were misclassified as Independent Contractors were reclassified as employees following review. Employers who misclassify employees as independent contractors may do so because they believe that the employees meet the standard for classification as an independent contractor or they may deliberately misclassify their employees in order to evade the regulations and taxes protecting employees.

Since August 2007 enforcement and data sharing activities have identified over 88,700 instances of employee misclassification and discovered over \$1.4 billion in

1. Workers who are classified as employees are also protected by a number of Federal laws including the National Labor Relations Act.

unreported wages.

Unreported Employment or “Off-the-Books” Work

This form of misclassification involves employees who are paid “off-the-books” and are not reported at all for tax and other financial purposes. Some of these employees may work for businesses that do not register with State and Federal taxation agencies or do not have workers’ compensation insurance. Others work for businesses that register with state and federal authorities but underreport the number of workers employed by the business.

In 2006 and 2007, several studies were released describing the extent of worker misclassification in New York State. The Cornell University School of Industrial and Labor Relations issued a report in February 2007 estimating that approximately 10.3% of New York State’s private sector workforce is misclassified each year.² The report also estimated that approximately 14.9% of the construction industry workforce is misclassified in a given year.

B. Executive Order Establishing the Joint Enforcement Task Force

On September 5, 2007, Governor Eliot Spitzer signed Executive Order #17 establishing the Joint Enforcement Task Force. Governor David Paterson continued the Task Force with Executive Order # 9 on June 18, 2008. Governor Andrew Cuomo continued the Task Force with Executive Order # 2 on January 3, 2011. The six JETF partners are:

- The New York State Department of Labor including the Unemployment Insurance Division, the Division of Labor Standards, the Division of Safety and Health, the Office of Special Investigations and the Bureau of Public Work;
- The New York State Workers’ Compensation Board;
- The New York State Workers’ Compensation Fraud Inspector General;
- The New York State Department of Taxation and Finance;
- The New York State Attorney General’s Office; and
- The Comptroller of the City of New York.

The Commissioner of Labor is designated as Task Force Chair and the New York State Department of Labor Office of Special Investigations is the lead agency coordinating Task Force efforts.

The Executive Order establishing the Task Force stressed the multiple ways in which misclassification harmed New Yorkers. The practice:

- gives employers who misclassify their employees an improper competitive advantage over law-abiding businesses;
- deprives vulnerable workers of important protections and benefits; and
- deprives the State of substantial revenues.

² Linda H. Donahue, James Ryan Lamare, Fred B. Kotler, J.D., “The Cost of Worker Misclassification in New York State” (Cornell University, ILR School, February 2007).

The Executive Order charges the JETF with:

- Sharing information about suspected employee misclassification violations and pooling and targeting investigative and enforcement resources to address them;
- Developing strategies for systematically investigating employee misclassification within industries in which misclassification is most common;
- Identifying significant cases of employee misclassification which should be investigated jointly, and forming joint investigative teams to utilize the collective investigative and enforcement capabilities of the JETF members;
- Establishing protocols through which individual JETF agencies investigating employee misclassification matters under their own statutory or administrative schemes will refer a matter to other participating agencies for assessment of liability under their statutory or administrative schemes;
- Soliciting the cooperation and participation of local district attorneys and other relevant agencies, and establishing procedures for referring cases to prosecuting authorities as appropriate;
- Facilitating identification of potential violators and the filing of complaints, including soliciting referrals and other relevant information from the public through an advertised telephone hotline;
- Working cooperatively with business, labor, and community groups in identifying and preventing misclassification, educating employers and the public about misclassification, and enhancing mechanisms for identifying and reporting employee misclassification;
- Proposing appropriate administrative, legislative and regulatory changes to eliminate barriers to the Task Force's operations, prevent employee misclassification from occurring and improve enforcement where such violations are found to have occurred;
- Assessing existing methods of preventing and investigating employee misclassification, and subsequent enforcement actions, and recommending that participating agencies adopt appropriate measures to improve prevention and enforcement efforts;
- Increasing public awareness of the harms inflicted by employee misclassification;
- Working cooperatively with federal, state and local social services agencies to provide assistance to vulnerable populations exploited by worker misclassification; and
- Consulting with representatives of business, organized labor, members of the legislature, and other agencies regarding the activities of the Task Force and ways of improving its operations.

The Executive Order requires the JETF to issue a report to the Governor on February 1 of each year describing its record and accomplishments and proposing and identifying mechanisms for improved enforcement. This is JETF's sixth annual report. Previous reports described in detail the procedures used to carry out the joint enforcement efforts including how tips and cases are generated, how the sweeps are conducted, and how audits and results are coordinated. Previous reports also described the type of misclassification seen by the JETF and also discussed the extensive cross-training conducted by the JETF in 2009-2010.³

II. Enforcement and Data-Sharing Efforts

In 2012, the JETF continued its joint enforcement and data-sharing efforts. Through joint enforcement sweeps, coordinated investigations, referrals, audit results, and data-sharing, the JETF seeks to ensure an efficient and comprehensive approach to enforcement of misclassification cases ensuring that an employer that is found to be engaging in the misclassification of employees is financially and legally liable for all of the resulting violations. By sharing investigation resources and tips, and by each agency learning to identify violations in other areas, the agencies involved in the JETF are able to do more work with fewer resources.

A. Joint Enforcement Sweeps

In 2012, the JETF conducted 36 sweeps bringing the total number of sweeps conducted since the JETF began to 142. Joint enforcement sweeps involve a coordinated visit and inspection of a worksite by JETF members. On nearly every sweep, the sweep teams have included investigators from the Department of Labor Unemployment Insurance and Labor Standards Divisions, the Department of Labor's Office of Special Investigations, the Workers' Compensation Board Bureau of Compliance, and the Workers' Compensation Board Office of the Fraud Inspector General. On sweeps involving public work construction projects and some private construction jobs, the Department of Labor, Bureau of Public Work was also included. All completed sweep cases in which misclassification is found continue to be referred to the New York State Department of Taxation and Finance for assessment of state income tax owed. Completed unemployment audits are also sent to the United States Internal Revenue Service.

This year, the JETF wants to facilitate closer coordination of agency efforts, including a reworking of the Executive order to expand its mission and number of agency participants.

(1) Results

The 2012 sweeps were conducted at construction sites, restaurants, car washes, automotive tire and repair centers, wholesale food distributors, adult entertainment clubs,

³ Annual reports from 2008, 2009, 2010 and 2011 are available at <http://www.labor.ny.gov/ui/employerinfo/employer-misclassification-of-workers.shtml>

retail establishments and entertainment venues. In 2012, completed audits and investigations of businesses found through the JETF sweeps:

- uncovered nearly \$67.6 million in unreported wages;
- resulted in the assessment of over \$1.8 million in additional unemployment insurance contributions; and
- uncovered over **\$640,000** in unpaid employee compensation; and
- revealed over 6,400 misclassified workers.

(2) Criminal Cases Resulting from Sweeps

In 2012, the Task Force continued to evaluate all sweep cases for potential criminal violations. The Department of Labor's Office of Special Investigations leads this process. Cases that show evidence of criminal violations are referred to either the Attorney General's Office or District Attorney's offices for prosecution. Examples of two such cases are:

The JETF conducted sweeps at two commonly owned meat markets on January 31, 2012 pursuant to a tip/information sharing with a task force partner, the Workers Compensation Board. The task force team interviewed 40 employees in total. The vast majority of these employees were being paid off the books and were not reported by the employer. The employees were paid in cash, were not paid overtime, and were not provided wage statements. Most of the employees were paid a set amount per week regardless of the actual hours worked, resulting in wages below the required minimum wage. The employers did not maintain records of the hours worked by its employees, nor did they maintain payroll records. The employers filed fraudulent documents with the State and Federal governments. The completed audits reveal that one entity owes \$191,853.16 in unpaid wages and \$36,531.73 in unpaid UI contributions while the other owes \$238,896.36 in unpaid wages and \$20,105.19 in unpaid UI contributions. The OSI referred this case to the Kings County District Attorney's office in August 2012. The case is ongoing.

The JETF conducted a tax payer enforcement operation at a restaurant that is commonly owned with two other restaurants in the Capital Region. The enforcement operation, and subsequent audit, revealed that all three locations severely underreported payroll and filed fraudulent documents with the State and Federal governments resulting in underpayments to the UI fund. Additionally, the employer failed to pay minimum wage, failed to pay overtime and failed to keep required records. The employer paid most employees in cash, paying \$30.00 per day for employees working nine hour days, or paying \$3.00 per hour. The employer operated a fourth location, for approximately two years, that they never reported to the NYS DOL, thereby failing to remit any of their required contributions to the UI fund. The employer owes back wages in the amount of \$161,197.43, and has underpaid the UI fund approximately \$68,000.00. This case was referred to the Albany County District Attorney's office and is ongoing.

This year, the JETF wants to establish a Retaliation Unit that focuses on the deprivation of workers' civil rights that rise to the level of criminality.

B. Coordinated Assignments

Some of the most significant results of the JETF's work have been in the area of Unemployment Insurance (UI) fraud. The state's UI Trust Fund currently has a \$3.68 billion deficit that has been exacerbated by high unemployment. The JETF's efforts to secure proper employer payments into the UI Trust Fund help to restore solvency to the UI system.

- In 2012, there were over 2,200 completed unemployment insurance audits and investigations that came from tips and referrals.
- The audits and investigations found nearly \$7.9 million in additional unemployment insurance contributions due.

The JETF's public efforts include a fraud hotline where many individuals, businesses, labor unions and community groups call and provide tips about misclassification. The Department of Labor receives and reviews the tips that come in by telephone, e-mail and letter. Referrals that come in through the data-sharing processes set up with other government agencies are also reviewed.

In addition, the JETF coordinates the investigation and resolution of cases that do not rise to the level of a sweep. The JETF works to coordinate each member agency's approach to bad actors and to mediate disputes between employers and employees in cases that do not rise to the level of criminality. In 2012, the number of coordinated misclassification assignments continued to grow significantly. This year the JETF would like to coordinate education efforts for businesses as well.

Internally, the JETF continued to hold bi-weekly meetings with representatives of the Unemployment Insurance Division and the Labor Standards Division to ensure that the tips that come in to the hotline are properly screened for possible labor standards and workers' compensation issues, as well as possible underpayment of unemployment insurance contributions, and that cases containing potential violations in multiple areas are handled in a coordinated fashion. At these meetings, the group also considers cases that come in from local Labor Standards, Unemployment Insurance and Workers' Compensation offices.

Examples of cases handled include:

- A referral from Department of Taxation and Finance indicated an ambulette service was issuing payroll checks to individuals without deducting withholding or other taxes, and misclassifying the workers as independent contractors. A review of Unemployment Insurance records indicated the employer submitted a quarterly report for the third quarter of 2009 showing wages paid, but then indicated it had permanently ceased paying wages after that quarter. The Unemployment Insurance Employer Services Representative found that the employer had operated continuously,

had misclassified drivers as independent contractors and had not reported compensation paid to corporate officers. Additional contributions due totaled \$13,953.37, and a 50% fraud penalty was assessed.

- A telephone call to the Misclassified Worker Hotline from a former employee led to an investigation of a moving company that paid employees in cash without reporting these wages for Unemployment Insurance purposes. The employer only reported wages for three employees, but the Unemployment Insurance Employer Services Representative found that the employer could not operate with this small of a workforce. Based on available information from the employer’s website, wages for seven additional employees were estimated. Additional contributions were determined due of \$5,124.15 and a 50% fraud penalty was also assessed.
- Information received from the New York County District Attorney’s office indicated that it was investigating several massage parlors suspected of human trafficking. A review of Unemployment Insurance records, and observations by Unemployment Insurance Employer Services Representatives, showed that seven of these employers were either underreporting wages paid to employees or were not reporting wages at all. Additional contributions due for each employer ranged from approximately \$2500 to \$8500. Fraud penalties were assessed in each case.
- An anonymous telephone call to the Misclassified Worker Hotline indicated that a night club/bar was not paying its employees an hourly wage, and that the employees were only being paid in tips. A review of available Unemployment Insurance records revealed that the employer had not reported any wages paid to employees in its first quarter of operation. An Unemployment Insurance Employer Services Representative found that the employer did not report sufficient wages based on its hours of operation. A review of the employer’s records found numerous cash transactions for which no explanation was provided. Additional contributions of \$2,101.83 were estimated to be due. A 50% fraud penalty was also assessed.

C. Construction Industry: Enforcement and Legislative Efforts

Based on research and statistics, the construction industry has some of the highest incidents of employee misclassification. Therefore, the JETF has, and will continue to, focus attention on this industry. The inception of the Construction Industry Fair Play Act in August 2010 has assisted in refining the investigative process by creating a presumption of employment in the construction industry unless an employer can meet the ABC test.⁴

Additionally, the Fair Play Act contains a twelve part test to determine when a sole proprietor, partnership, corporation or other entity will be considered a “separate business entity” from the contractor for whom it provides a service. The Construction

⁴ Under the ABC Test, an individual is considered an employee unless he or she is free from direction and control in performing the job, AND the work that is performed is not part of the usual work done by the business that hired the individual, AND the individual has an independently established business.

Industry Fair Play Act has, and will continue to, make investigation and enforcement of employee misclassification in the construction industry a more precise and uniform process.

- The JETF conducted 6 sweeps of construction sites in New York State in 2012.
- 2 were conducted in the NYC Metropolitan area which resulted in the initiation of 14 investigations.
- 4 were conducted in upstate NY resulting in 4 investigations.

The sweeps resulted in the discovery of nearly \$15.8 million in unreported wages, over \$644,500 in unemployment insurance contributions due, the imposition of fraud penalties and the identification of over 1,700 misclassified workers.

D. Ongoing Department of Labor Unemployment Insurance Efforts

In 2012, the Department of Labor completed nearly 14,000 audits and investigations, finding nearly 113,500 misclassified workers and unpaid taxes of \$43.3 million. The job categories showing the highest incidence of worker misclassification included:

- Professional, Scientific and Technical Services;
- Administrative and Support Services;
- Performing Arts, Spectator Sports, and Related Industries;
- Ambulatory Health Care Services;
- Food/Drink Services;
- Construction of Buildings;
- Educational Services;
- Specialty Trade Contractors;
- Personal and Laundry Services;
- Motion Picture and Sound Recording Industries.

III. Data Sharing

Representatives of the JETF agencies together with representatives of two additional state agencies, the New York State Department of Insurance and the Department of Motor Vehicles meet regularly in a “Forms Team” to discuss the sharing and coordination of forms and information to aid in fraud detection efforts. The Forms team implements provision 141-C of the Workers’ Compensation Law⁵ that allows for the sharing and coordination of forms to aid in fraud detection efforts. The team has implemented a number of procedures that give agencies access to information contained in each other’s files and to automatically

⁵ Section 141-c of the Workers’ Compensation Law: Coordination of forms. The board, the commissioner of labor, the commissioner of taxation and finance, the commissioner of motor vehicles, and the superintendent of insurance shall consult on an ongoing basis to coordinate the amendment of forms used to gather data helpful in identifying fraud, so as to promote effective use and sharing of such information for identifying fraud in the area of workers' compensation. Through such consultations and other means, these agencies shall study the implementation of appropriate practicable technology to verify the authenticity of forms, including certificates of coverage.

notify partners of fraud found during investigations.

During 2012, the Forms Team:

- Continued to refine and troubleshoot existing agency data-sharing processes to allow for the sharing of the most relevant and beneficial information;
- Continued development of data-sharing agreements between the Department of Labor and the State Liquor Authority;
- Finalized a data sharing agreement Memo Of Understanding with the Department of Motor Vehicles;
- Finalized an updated Memo Of Understanding with the Department of Tax and Finance;
- Developed compliance reviews between partner agencies to develop routine due diligence processes; and
- Continued form and process development to support implementation of the multi-agency Construction Industry Fair Play Act of 2010.

Additionally, an enforcement team comprised of Department of Labor's Public Work, Labor Standards and UI continue to meet regularly to review referral cases from within the DOL to determine penalties for notice and misclassification violations as well as cases referred from Department of Taxation and Finance and the Workers' Compensation Board.

In 2012, DOL UI issued 47 employee determinations utilizing the employment tests under the Fair Play Act. The DOL enforcement team identified 165 violations of the posting provisions for failing to conspicuously display Fair Play Act posters at job sites. To date, 472 poster violations have been issued resulting in the assessment of \$58,400 in fines, \$44,000 of which has been paid.

IV. Labor Law Legislation

The Wage Theft Prevention Act became effective in April 2011. The Act requires employers to provide notice to employees regarding rates of pay, designated payday, the employers' intent to claim allowances, and the basis of wage payment. The Act clarifies and expands the Department of Labor's authority to enforce the Labor Law and expands an employee's ability to bring complaints and private actions for violations. All private sector employers are covered by the Act. The Wage Theft Prevention Act will assist the JETF in conducting its investigations into employers' practices, and potentially highlight employers that may be violating the law through worker misclassification.

V. Outreach and National Activities

In 2012 the JETF continued to provide presentations/trainings to various unions, business groups and trade associations across the State regarding the work of the Task Force. At these presentations the attendees are encouraged to contact the Task Force with any leads and/or information regarding worker misclassification. Additionally, at these presentations the Construction Industry Fair Play Act is discussed in an effort to educate attendees on the

change in the law, to enhance compliance, and to encourage them to be on watch for worker misclassification in the construction industry.

VI. Goals for 2012

The JETF continues to work to decrease the incidence of misclassification through increased enforcement, data-sharing and outreach. **In the year ahead, the JETF will:**

- **Work to establish a Retaliation Task Force;**
- Improve and expand its focus on UI fraud and its prevention;
- Attempt to focus on the issue of employee misclassification that occurs in conjunction with labor trafficking; and
- **Consider expanding the Task Force to include additional members.**

Enforcement

- Continue strategic and coordinated enforcement sweeps in the construction industry, as well as other industries noted in this report, showing the highest incidents of employee misclassification;
- Identify industry-specific proactive investigations in industries with a high incidence of misclassification;
- Continue to work on effective and coordinated enforcement of the Fair Play Act;
- Continue to pursue criminal prosecutions with local District Attorneys and the Attorney General's Office in cases of serious employer fraud; and
- Work with other states to pursue employers that operate in multiple jurisdictions.
- Identify whether additional programmatic, legislative, or regulatory fixes are needed to combat employee misclassification.

Outreach

- Continue to conduct outreach to business, labor and community groups to ensure awareness of the Task Force and encourage communication therewith; and to ensure awareness of the recently passed Construction Industry Fair Play Act and compliance therewith.
- Increase outreach to the business community, including small businesses, to raise awareness of the problems of employee misclassification; and prepare additional educational materials for distribution to the public and to employers.

Coordination Between Agencies

- Improve processes for sharing enforcement information and moving cases through the enforcement process; and

- Continue to work on identifying data-sharing processes.

VII. Conclusion

During 2012, the JETF has actively enforced employment laws involving worker misclassification in order to protect workers and law-abiding businesses and to collect contributions due. Through coordinated enforcement and data-sharing between the JETF agencies, we are able to share resources and make all of our work more efficient. The JETF looks forward to continuing its work on these critical issues in 2013.