NATIONAL EMPLOYMENT LAW PROJECT

TESTIMONY

Testimony of M. Patricia Smith

National Employment Law Project

New Jersey Misclassification Task Force
Public Forum
Newark, NJ
December 5, 2018

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Thank you for the opportunity to participate in this public forum on independent contractor misclassification of workers in New Jersey. My name is M. Patricia Smith and I am Senior Counsel at the National Employment Law Project (NELP). NELP is a national legal, research and policy organization that for nearly 50 years has focused on the ways in which various work structures – such as classifying workers as "independent contractors" –drive labor standards erosion, rising income and wealth inequality, enduring and evolving structural racism and occupational segregation, and the shifting of power away from workers and toward corporations.

I have been involved in the problem of misclassification of workers, and developing strategies on how government can best attack the problem, for at least twenty years. First, at the Attorney General's office in New York, where I was chief of the Labor Bureau for eight years. Then, as Commissioner of Labor in New York State, I directed the nation's first Joint Task Force on Employee Misclassification ("New York Task Force"). Finally as Solicitor of the U. S. Department of Labor ("USDOL") for seven years, I spearheaded that Department's efforts to combat misclassification. I would like to talk a little about the scope of the problem and then recommend some enforcement best practices.

In the United States, over 10 million workers—about 7 percent of the workforce—are classified as independent contractors.[1] Notably, this number excludes the many workers who have a traditional main job but engage in an independent contractor work arrangement on the side, which appears to be increasingly common.[2] For example, according to recent reports, 1 in 6 teachers are working part time on the side—such as driving for Uber or Lyft—to supplement their meager teaching salaries.[3]

For decades, corporations have characterized workers as "self-employed" or "independent contractors," as a tactic to shift risk downwards onto workers, while shifting wealth towards investors and CEOs. Corporations can save as much as 30 percent on their payroll costs by labeling their workers as independent contractors rather than employees.[4] These arrangements – often presented to workers as take it or leave it propositions – strip them of all labor rights, from core labor standards like minimum wage and anti-discrimination laws, to social insurance and employer benefit programs, like unemployment benefits and health insurance.

Misclassification harms not only workers, but also law-abiding employers that cannot compete, and the integrity of our tax coffers and safety nets systems.

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[1] Bureau of Labor Statistics, Contingent and Alternative Employment Arrangements News Release (June 7, 2018), https://www.bls.gov/news.release/archives/conemp_06072018.htm.

[2] Bureau of Labor Statistics, Labor Force Statistics about the Current Population Survey, Frequently Asked Questions about Data on Contingent and Alternative Work Arrangements, https://www.bls.gov/cps/contingent-and-alternative-arrangements-faqs.htm#collected.

[3] Alexia Fernandez Campbell, *"I Feel Mentally Numb": More Teachers are Working Part-Time Jobs to Pay their Bills,* VOX, Apr. 4, 2018, https://www.vox.com/policy-and-politics/2018/4/4/17164718/teachers-work-part-time-jobs.

[4] National Employment Law Project, *Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries*, Sept. 2017, https://s27147.pcdn.co/wp-content/uploads/NELP-independent-contractors-cost-2017.pdf.

Independent contractor misclassification can take several forms. In some cases, even though the employer controls most aspects of the job, including how the work is performed, what the worker is paid, and relationships with clients, employers call workers "independent contractors". In other cases, the employer will require its workers to form a limited liability corporation or franchise company-of-one as a condition of getting a job. These workers are sometimes required to sign boilerplate contracts attesting to independent contractor status, even where the functional relationships do not reflect true independence and the workers are not running their own business under any definition. Finally, some employers do not even go through the process of formally misclassifying their employees, and do not provide 1099 or W2 forms. They pay their employees "off the books," and structure their financial records to hide these workers and the payments to them. If caught by a government agency, they use the "independent contractor" classification as a defense to their actions.

Available evidence suggests that misclassification is widespread. Federal studies and state-level agency audits, along with unemployment insurance and workers' compensation data, indicate that between 10 and 30 percent of employers misclassify at least one employee as an independent contractor, meaning that several million workers nationally may be misclassified.[5]

Misclassification is especially prevalent in construction, janitorial, home care, trucking and delivery services, and other labor-intensive low-wage sectors, where employers can gain a competitive advantage by driving down payroll costs.[6] This means that the employers that correctly classify workers as W-2 employees are often unable to compete with lower-bidding companies that reap the benefits of artificially low labor costs. This also means that people of color—who are overrepresented in many of these sectors—toil in jobs that are insecure, underpaid and have no workplace protections or benefits, which exacerbates income inequality and economic insecurity for black and brown communities.

A 2009 study of port truckers in New Jersey showed how drivers classified as independent contractors operated with little autonomy.[7] The trucking companies prohibited their drivers from making deliveries for other companies, thereby controlling the drivers' access to work. Many drivers also leased their trucks from and obtained their insurance through their trucking company, which meant that the companies took possession of the leases and deducted insurance from the drivers' pay. At the same time, the drivers were excluded from workplace protections and benefits, like health insurance and workers' compensation, which are critically important in high-risk sectors like truck driving. These drivers bore all of the risks and costs of being in business for themselves with virtually none of the benefits.[8]

More recently, well-capitalized online platform companies have joined the trend of labelling their workers as independent contractors while maintaining control of the work performed. Technology has enabled platform companies to surveil every second of work. Uber's

[5] *Id*. at 2.
[6] *Id*. at 2, 7
[7] Francoise Carre, *(In)dependent Contractor* Misclassification, Economic Policy Institute, June 8, 2015, at 11, https://www.epi.org/publication/independent-contractor-misclassification/
[8] *Id.; see also* David Benson, *Port Trucking Down the Low Road: A Sad Story of Deregulation,* Demos, 2009, https://www.demos.org/sites/default/files/publications/Port%20Trucking%20Down%20the%20Low%20Road.pdf.

technology, for example, allows it to track drivers in granular detail, including the speed at which the car is driven and the route taken for each ride.[9] The technology also matches drivers with customers and determines the rate for each ride and the payment to each driver. According to recent reports, Uber regularly makes unilateral changes to driver's pay and work conditions, often with the effect of squeezing more out of drivers.[10]

Notably, New Jersey has joined other states and adopted a broad test for who is an employee, under its Wage & Hour and Unemployment Insurance laws, which means that independent contractor misclassification should be easy to identify. New Jersey uses the "ABC test" for employment classification, which presumes that a worker is an employee unless the employer can demonstrate three factors:

(A) Such individual has been and will continue to be free from control or direction over the performance of such service, both under the contract of service and in fact;
(B) Such service is either outside the usual course of business for which such service is performed, or is performed outside of all the places of business of the enterprise for which such service is performed; and
(C) Such individual is engaged in an independently established trade, occupation, profession or business.[11]

The "ABC test" means that companies cannot outsource core aspects of their enterprise to so-called independent contractors while maintaining control of the performance of the work. It also means that broad swaths of the New Jersey workforce may be misclassified.

. An employer who is illegally misclassifying workers is likely breaking not one state law, but multiple laws. Several laws are implicated, including Wage and Hour, Unemployment Insurance, Workers Compensation, and Tax laws. Misclassification exacts a huge toll on state treasuries: researchers found that misclassifying just one percent of workers as independent contractors would cost unemployment insurance (UI) trust funds $198 million annually.[12] According to Governor Murphy, audits indicate that misclassification has deprived New Jersey of over $500 million in tax revenue every year.[13] The issue, then, is enforcement

New York and Federal Independent Contractor Taskforces

In order to fight misclassification, in 2007 New York State established the nation's first Joint Enforcement Task Force on Employee Misclassification. The New York Task Force created a

[9] Alex Rosenblat, *When Your Boss is an Algorithm,* NEW YORK TIMES, Oct. 12, 2018, https://www.nytimes.com/2018/10/12/opinion/sunday/uber-driver-life.html?smid=tw-nytopinion&smtyp=cur.
[10] Alex Rosenblat, *Uber May Have Imposed 12-Hour Driving Limits, but It's Still Pushing Drivers in Other Troubling Ways,* SLATE, MARCH 2, 2018, https://slate.com/technology/2018/03/uber-may-have-imposed-12-hour-driving-limits-but-its-still-pushing-drivers-in-other-troubling-ways.html.
[11] NJ courts have stated that Part C requires that the individual maintain an enterprise that can exist independently of and an apart from the particular service arrangement.
[12] NELP, *supra* note 4, at 2.
[13] New Jersey Exec. Order No. 25, May 3, 2018, https://nj.gov/infobank/eo/056murphy/pdf/EO-25.pdf.

partnership consisting of representatives of five New York State agencies, each of which had its own interest in preventing worker misclassification.[14] The goal of the New York Task Force was to combine agency resources to conduct statewide industry enforcement sweeps, to improve interagency date sharing and to develop policy solutions. Within four months of its establishment, the New York Task Force was required to issue the first of its yearly reports. In that short period, it had conducted 117 sweeps of business, uncovered 2,078 misclassified employees and identified $19 million in unreported wages. It found unpaid back wages owed of $3 million.[15] A year later, the New York Task Force reported that it had identified 12,300 cases of misclassified employees, $157 million in unreported wages and $12 million in unpaid wages owed.[16] In 2015, the last year it operated independently,[17] the New York Task Force reported that since 2007 it had identified nearly 140,000 instances of employee misclassification and discovered nearly $2.1 billion in unreported wages.[18]

More than half of the states have established independent contractor task forces or entered into Memoranda of Understanding with the USDOL.

The US Department of Labor during the Obama administration also began a misclassification initiative. The Wage Hour Division, along with the Solicitor's Office, worked with the Internal Revenue Service and 34 states to share information and coordinate enforcement to ensure that all were using their resources most strategically and effectively to combat the misclassification problem. From September 2011 to January 2013, the Wage and Hour Division collected more than $9.5 million in back wages, which resulted from more than 11,400 workers being misclassified as independent contractors or otherwise not properly treated as employees. This represented an 80% increase in back pay and 50% increase in the number of workers receiving back pay since DOL began to implement these agreements with the States.[19]

Recommendations

Based upon my experience with these efforts, I recommend you consider recommending adopting the following best practices.

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[14] The Labor Department enforces wage hour laws, including the prevailing wage law on state projects and the unemployment compensation law. The Worker's Compensation Board enforces the worker's compensation laws. The Department of Taxation and Finance enforces state tax laws and 1099 fraud. The Comptroller of the City of New York enforces the prevailing wage law on City projects. The New York Attorney General has criminal enforcement powers upon referral of cases from the agencies.

[15] Report of the Joint Enforcement Task Force on Employee Misclassification, February 1, 2008, available at https://www.labor.ny.gov/pdf/Report%20of%20the%20Joint%20Enforcement%20Task%20Force%20on%20Employee%20Misclassification%20to%20Governor%20Spitzer.pdf.

[16] Report of the Joint Enforcement Task Force on Employee Misclassification to David A. Paterson, Governor, State of New York, Feb. 1, 2009, https://www.labor.ny.gov/ui/PDFs/2009_02_02_12_38_52.pdf.

[17] In 2016, the Governor issued a new executive and created the Joint Task Force on Worker Exploitation and Worker Misclassification. See https://www.ny.gov/end-worker-exploitation/task-force-combat-worker-exploitation.

[18] Annual Report of the Joint Enforcement Task Force on Employee Misclassification to Hon. Andrew Cuomo, Governor State of New York, Feb. 1, 2015, https://www.labor.ny.gov/agencyinfo/PDFs/Misclassification-Task-Force-Report-2-1-2015.pdf

[19] Staci Ketay Rotman, *DOL's Misclassification Initiative Continues*, Wage & Hour Insights, Jan. 13, 2013, https://www.wagehourinsights.com/2013/01/dols-misclassification-initiative-continues/.

1. To the extent legally possible, engage in interagency coordinated enforcement.
2. Whether or not interagency coordinated enforcement is adopted, engage in data sharing and systematic referrals to appropriate agencies.
3. Establish a public outreach infrastructure including a dedicated hotline, website, and e-mail address. A robust press strategy is an important component to public outreach.
4. Provide interagency cross training and joint education and require frequent meetings between partner agencies that assures information about possible misclassification is appropriately shared.
5. Make criminal referrals in appropriate cases.
6. Require reports to the legislature or the governor for transparency and accountability.

I cannot emphasize enough that these best practices take planning and real work on the part of the partner agencies, and of course, additional resources will enhance the efforts and results. However, they can be implemented, as happened in New York, without additional resources. Planning, especially at the beginning, is crucial. I recommend the first report of the New York Task Force, which set forth in detail the extent of initial planning that occurred.[20] Coordinated interagency enforcement effort involves research, both to develop leads and to address any legal issues that arise. They need to be carefully planned and then just as carefully carried out. The sharing of information obtained and follow-up audits also need planning. Communications strategies must be developed, both to keep the public informed and to assist the public in contacting the Task Force members with tips and complaints.

Coordinated Enforcement

Coordinated interagency enforcement can involve a number of strategies.[21] It can involve participants from multiple agencies conducting on-the- ground investigations of possible misclassification. It generally involves more than looking at books and records, because misclassification often cannot be identified only by looking at books and records. When employers violate the law, payroll records are often inaccurate regarding the number of employees, wages paid, and employee job duties. Employee interviews are critical for assessing the accuracy of company records. In addition, understanding if a worker is properly classified involves gaining an understanding of a company's business practices. This most often involves talking to workers about what services they perform, the extent to which they are running a separate business, and the amount of control the company has over the provision of those services.

I recognize that not all agency partners are necessarily skilled in this type of fact intensive investigation. In New York, we addressed this issue by joint training and delegation of investigation responsibilities. For example, when talking to workers during sweeps, the Wage & Hour investigators, who had years of experience talking to workers, took the lead while the Unemployment Insurance investigators took the lead in looking at the company's books and records. This type of joint investigation takes planning but much of it is no different than

[20] See Report of the Joint Enforcement Task Force on Employee Misclassification, Footnote 15 at 9.
[21] In New York, these investigations took two forms. Sometimes a particular industry, usually construction, was the subject of interagency "sweeps". Other times a "main street" approach was taken when investigators would go door to door to all businesses in a shopping district. Each strategy successfully uncovered illegal misclassification.

planning a single agency investigation. Development of employer and employee interview sheets; scripts explaining to employers each agency's authority and their need to comply with information requests; handouts, in various languages explaining to workers what the purpose of the investigation is and their right to talk to investigators without retaliation; all of these will make investigations easier. The first New York Task Force Report details the steps taken before conducting coordinated interagency enforcement sweeps.[22]

Of course, these coordinated enforcement actions do not end with the on the ground investigation. An analysis of the facts gathered in the investigation must be performed; applying each agency's governing law to determine if there are violations. When violations are found, appropriate audits must be conducted to determine back wages owed, unemployment contributions owed, workers compensation premiums owed, and taxes owed. However, when multiple agencies participated in the fact gathering aspect of the investigation, that one investigation can often be used to support violations of multiple state laws with appropriate remedies and penalties. This saves state resources since one and not several investigations took place. I also recognize there may be legal limits on the ability of the partner agencies to engage in coordinated interagency enforcement. For example, tax investigations may have strict confidentiality requirements. However, to the extent legally possible, coordinated interagency enforcement is the best "best practice" because it allows the agency partners to best leverage their resources in achieving compliance with little or no additional resources.

Data Sharing

Data sharing is critical, whether or not coordinated interagency enforcement is in place. Not all investigations merit a coordinated enforcement action. Moreover, as mentioned above, there may be legal limits on the ability of certain agency partners to engage in coordinated enforcement actions. For example, in New York, the Department of Taxation and Finance was statutorily limited in its ability to participate in sweeps. However, it was able to receive and act upon information received during a sweep and to use that information to begin and conduct its own investigation into possible tax fraud.

Data sharing makes targeted enforcement a real possibility. Reliance upon random audits as a sole investigatory strategy results in undercounts of violations and unpaid taxes. For example, between 2008 and 2012, the state of Utah conducted both random and targeted unemployment insurance audits of employers. The 5233 random audits identified $42 million in unreported wages to 6949 workers misclassified as independent contractors. By contrast, 913 targeted audits identified $138 million in unreported wages and 18,114 misclassified employees. While the random audits identified violations in 2.9% of cases, the targeted audits found violations in 14% of the cases.[23] A quick glance at the reports of the New York Task Force from 2008 to 2015 demonstrates the impressive results of targeted enforcement in New York.

Data sharing was the principle mechanism that the USDOL used to coordinate with the states and the IRS on misclassification. As I earlier mentioned, the USDOL entered into memoranda of

[22] Report of the Joint Enforcement Task Force on Employee Misclassification, Footnote 15 at 9.
[23] Jody McMillian, Chief of Contributions, Utah Department of Workforce Services, *Effective Methods to Detect and Deter Worker Misclassification*, Oct. 21, 2012)

understanding with 34 states. Each memorandum was a little different depending on the states' interest and their legal ability to share date with other agencies. I understand that last summer New Jersey's Department of Labor entered into such an agreement with USDOL. I cannot speak to how the states use the data that USDOL shares with them, but I can say that some of the largest and most impactful misclassification cases brought by USDOL were initiated based upon information received from the states. For example, based upon information received from the State of Utah, the USDOL forced 17 businesses in Arizona and Utah to reclassify over 1,000 of their workers as employees and pay over $1.3 million in back wages and penalties, as well as paying all federal, state and local taxes owed.[24]

Data sharing abilities must be carefully researched . Each agency is likely to have confidentially requirements that must be observed. I recommend that Memoranda of Understanding be entered into by all agencies that will participate in data sharing so that responsibilities and any limitations are clearly understood by all parties. Another concern, which I do not think should be a problem amongst New Jersey partner agencies, was the interaction with federal confidentially requirements and state sunshine laws. State laws that required public disclosure of information that could not be disclosed under federal law limited the ability of USDOL to share some detailed information with some states.

Data sharing can take many forms. Shared data can be the basis of coordinated interagency investigations. Shared information can trigger separate investigations by separate agencies. Agencies can share completed audits with other agencies, allowing them to spend fewer resources on their own investigations. Each of these forms of data sharing contribute to the success of interagency cooperation.

Public Outreach

Educating the public about the activities of the New Jersey Task Force and giving them an opportunity to provide information is crucial to success. I recommend that you establish an employment fraud hotline, website and email address. In just the first 4 months of the New York Task Force, these types of portals resulted in 200 new unemployment insurance tax audits. A robust press strategy is also important in keeping the public, including workers and employers, aware of your activities and encouraging participation in the information portals.

Cross Training

In order to make coordinated enforcement and data sharing effective, cross training of agency partners is critical. It is the foundation of successful interagency coordination. At a minimum, agency investigators need to be able to understand the laws their sister agencies enforce. With training, in investigations that do not involve sister agencies, potential violations of other laws can be identified and referred to the appropriate agencies.. In New York, cross training resulted in agencies being better prepared to participate in coordinated interagency enforcement. It also resulted in agencies sometimes inviting sister agencies to participate in their own investigations

[24] U.S. Dep't of Labor, Investigation in Utah and Arizona Secures Wages and Benefits for More Than 1,000 Construction Workers Who Were Wrongly Classified, Apr. 23, 2015, https://www.dol.gov/newsroom/releases/whd/whd20150518.

when possible violations of the sister agencies' laws were identified. However, one or two training is insufficient. Agency partners must meet frequently to assess the information coming into the Task Force and to decide upon the appropriate response to that information.

Criminal Referrals

In appropriate cases, criminal referrals should be considered. In New York, the Attorney General's Office was the lead agency on criminal prosecutions that resulted from the Task Force operations.

Reports

Transparency is important especially when the government begins new initiatives. Both the public and the state must be able to assess the success of new initiatives. In addition, transparency allows for critical review of actions taken and possible corrections or new actions if the results are not as expected. The Task Force should recommend to the governor that some sort of transparency, in the form of an annual report, be required.