



Source: Construction Labor Report: News Archive > 2011 > 01/13/2011 > Lead Report > Independent Contractors: Panelists Say Data Shows Large Problem With Worker Misclassification/Underreporting

56 CLR 1361

## **Independent Contractors**

### **Panelists Say Data Shows Large Problem With Worker Misclassification/Underreporting**

DENVER—Government enforcement efforts are placing employers on notice that there has been an increase in the likelihood and costs associated with getting caught for misclassifying and underreporting workers in construction and other industries, speakers said Jan. 7 at a panel session of the Labor and Employment Relations Association annual meeting.

James A. Parrott, deputy director and chief economist for the Fiscal Policy Institute in New York, said that recent significant increases in New York's restaurant employment may have been driven by the state's enforcement sweeps that have targeted the industry.

"It was found that about 95 percent of restaurants in Brooklyn have some kind of misclassification," Parrott said. "Employers are now putting them on the books because of the enforcement action," resulting in a 10 percent increase in reported restaurant employment, he said.

Parrott was a member of a panel on state-level studies about misclassified and unreported workers, especially in the construction industry. Parrott and other panelists presented evidence that many employers are treating workers as independent contractors—or paying them cash "under the table" and not reporting them at all—when they are in fact employees. Employers do so to circumvent their liability for payroll taxes, Social Security insurance premiums, and workers' compensation premiums, the panelists said.

#### **Misclassification Also Creates Problems for Workers**

Meanwhile, employee misclassification creates problems for workers, panelists said. In addition to not being covered by workers' compensation, unemployment insurance, or state temporary disability insurance, misclassified and underreported workers lose overtime pay and access to health care coverage and other benefits, such as retirement benefits and paid time off, they said.

Misclassified workers are liable for the full Social Security and Medicare payroll taxes, and if they do not pay payroll taxes, the amount of Social Security benefits for which they are eligible may be reduced. They lose many other employment rights, such as the right to organize and form a union, in addition to protections from discrimination, members of the panel said.

Parrott said New York's enforcement data gathered from September 2007 through the end of March 2010 begins to demonstrate the extent of employee misclassification.

A New York Joint Enforcement Task Force on Employee Misclassification conducted some 67 sweeps across the state that identified nearly 35,000 cases of employee misclassification and discovered more than \$457 million in unreported taxes, more than \$13.2 million in unemployment insurance taxes due, and more than \$14 million in unpaid wages, he said.

#### **Data Suggests Misclassification Explosion**

Discrepancies in data between one set of employment measures and another "strongly suggests an explosion in the misclassification of workers," Parrott said.

According to data compiled by the Commerce Department's Census Bureau, which counts workers paid as independent contractors and who receive an Internal Revenue Service Form 1099, the nonemployer series of workers increased by 240,500 from 2000 through 2005, a growth rate of 20 percent, he said.

Across the same time frame, private payroll employment in New York increased by only 33,500, or 0.5 percent, he said. The private payroll employment figures count only workers who receive a W-2 form. The growth in the nonemployer series has been so much greater than the growth in payroll employment that it "likely reflects an increase in misclassification," Parrott said.

While independent contractor misclassification occurs in many industries, it is very prevalent in the construction sector, panelists said. That has fueled the idea that the misclassification problem is an immigrant problem, an idea most panelists dismissed.

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## **Not Just Problem for Illegal Workers**

"The characterizations of this as an illegal immigration problem are not true," said Matthew Capece, an attorney with the Carpenters and Joiners of America. "This has gotten to the point where it encompasses not only undocumented workers, but people who are documented citizens of the U.S."

And, he added, policy solutions to address alien workers will not resolve the misclassified employee problem. "If you are an employer, you're not going to I-9 or E-Verify an independent contractor or someone you pay off the books," he said.

Capece also dismissed the notion that misclassification merely is a technical violation or a paperwork error. "There is much more outright fraud and problems with nonreporting" than unintentional or negligent behavior, he said. "And this is not about ma and pa businesses renovating kitchens. It's about a problem that is widespread within the residential construction industry."

## **Misclassification Can Involve Criminal Violations**

Employee misclassification touches upon "money laundering, conspiracy, racketeering, grand theft—a whole cornucopia of criminal laws that are being violated," he added.

Some employers have argued that if enforcement were to increase further at construction job sites, there could be harmful economic impacts, Capece noted. They also have suggested a clearer definition of "independent contractor" is needed to distinguish it from "employee."

"With the class of people we are talking about, Moses himself could come down from heaven with a definition of employment chiseled on stone, and it wouldn't matter unless there was adequate enforcement to back it up," Capece said. "We are dealing with a class of people who don't care about the law at all. The law is just a traffic cone for them to avoid."

Although misclassification stretches across industries and is not just an immigration problem, there is a clear tie to immigration with many employers, said Randall Adams, associate professor of sociology at Alice Lloyd College in Pippa Passes, Ky. "If you look at this problem, you can't ignore the influence of immigration," he said, adding that alien workers "don't complain."

## **Alien Workers Intimidated**

Adams referred to a newspaper article Capece read to the panel quoting an employer that said companies "don't have to worry about paying worker's comp for Mexicans because they are afraid to go to the hospital."

"We have these people intimidated," Capece quoted the employer as saying.

Adams described a study he conducted on misclassification in Tennessee using "secondary data" from the Census Bureau, IRS, state workers' compensation figures, and unemployment insurance numbers. The study concluded that some 22,000 to 40,000 construction workers in Tennessee were misclassified, he said.

"You can use these secondary data to demonstrate a state has a problem with misclassified workers," Adams said.

## **Economic, Social Costs Discussed**

Similarly, Dale Belman, associate director and professor in the School of Labor and Industrial Relations at Michigan State University, detailed the findings of a study he helped conduct into the economic and social costs of misclassified workers in Michigan.

The state loses between \$19.5 million and \$32.5 million dollars in state tax revenue to underreporting and misclassification, Belman said. "In combination with forgone unemployment insurance revenues of \$16.8 million, Michigan annually forgoes between \$36.3 and \$49.3 million in revenues," he said.

The study found that construction employers were much more likely to engage in nonreporting fraud than to misclassify workers as independent contractors. About 26.4 percent of construction employers misclassified workers or paid them off the books, he said.

*By Tripp Baltz*

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ISSN 1523-5688

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