

Special Joint Commission to Study the  
Underground Economy and Employee  
Misclassification

**Findings and Recommendations**

Report Submitted to the

Rhode Island General Assembly

June 2009

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## **Special Joint Commission to Study the Underground Economy and Employee Misclassification**

### **Members:**

Senator Christopher Maselli, **Co-Chair**  
Representative Arthur Corvese , House Committee on Labor Chairman, **Co-Chair**  
Senator David Bates  
Representative Douglas W. Gablinske  
Representative Brian Newberry  
Judge George Healy, Rhode Island Workers' Compensation Court  
David Sullivan, Tax Administrator, Rhode Island Division of Taxation  
Matt Carey, Rhode Island Department of Labor and Training  
Paula Pallozzi, Rhode Island Department of Business Regulation  
David Burnham, Rhode Island Independent Contractor's Association  
Steven LaBrie, Teamsters Local Union 251  
Michael D. Lynch, Beacon Mutual Insurance  
Terrance S. Martiesian, Martiesian & Associates  
George H. Nee, Rhode Island AFL-CIO  
David Palmisciano, Carpenters' Union Local 94

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**Senator Christopher Maselli and Representative Arthur Corvese**  
Co-Chairs of the Special Joint Commission to Study the Underground Economy and Employee  
Misclassification

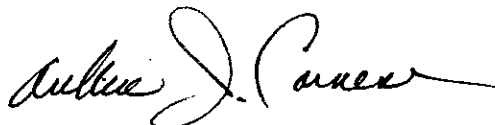
We are pleased to present these findings and recommendations on the issue of employee misclassification and the underground economy in the state of Rhode Island. This report represents the best thinking of a distinguished and dedicated Commission whose membership consisted of elected officials, the Rhode Island court system, departments within state government, labor groups, representatives of independent contractors, representatives of the construction industry, insurance professionals, and business owners from throughout the state. Over the course of several hearings, Commission members heard informed testimony, examined the impact that employee misclassification can have on employees, employers, and the state, reviewed best practices in addressing the issue of employee misclassification, and considered the most reasonable and effective means to prevent the misclassification of employees and improve compliance enforcement in the state of Rhode Island.

Misclassifying employees as independent contractors, or paying them on an 'under the table' cash basis wrongly deprives employees of the protection of workers' compensation, unemployment insurance, and wage and labor laws; deprives the state of millions in uncollected tax revenues and insurance premiums; and unfairly puts honest, rule-abiding, employers at significant competitive disadvantage versus employers who cheat the system.

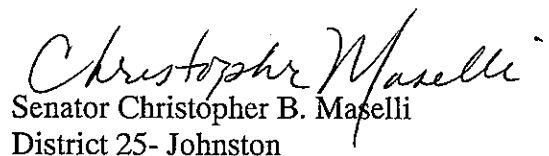
We offer these findings and recommendations with confidence that we can decrease the incidence of employee misclassification, increase the level of collaboration and communication amongst state agencies, and improve the enforcement of wage and labor law in the state of Rhode Island. If implemented correctly, the Commission's recommendations will enable state departments to quickly and effectively communicate with one another on issues of compliance, improve the state's ability to collect the revenues and insurance premiums it has been empowered to collect, and level the playing field for compliant businesses who play by the rules and properly classify their employees.

We are grateful to every member of the Commission for their willingness to take part in these discussions and further express our gratitude to the numerous members of the public who took time to appear before the Commission and contribute to our understanding of the challenges and impacts that the underground economy can have on workers and businesses.

Sincerely,



Representative Arthur J. Corvese  
District 55 - North Providence



Senator Christopher B. Maselli  
District 25- Johnston

## **TIMELINE OF THE SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION**

- July 8, 2008 – Senate Resolution 3099, sponsored by Senator Daniel P. Connors, becomes effective, creating the Special Joint Commission to Study the Underground Economy and Employee Misclassification
- February 25, 2009, Room 310, State House – First Commission hearing- organizational meeting. Representative Arthur Corvese and Senator Christopher Masselli are elected Commission co-chairs. The Commission reviews and discusses their legislative charge and schedules future hearing dates.
- March 11, 2009, Senate Lounge, State House – Second Commission hearing. State agencies provide an overview of current oversight of the underground economy and employee misclassification. Testimony as to the impact of employee misclassification on the state is given by the Division of Taxation, the Department of Labor and Training, Unemployment Insurance Auditing Department, Workers Compensation Fraud and Compliance Unit, and the Attorney General's Medicare Fraud Unit.
- March 25, 2009, Senate Lounge, State House – Third Commission hearing. Presentation by Commission legal counsel is given on possible legislative recommendations. Commission staff provide an introduction and review of the Commission Mission Statement. *Public Testimony: The Impact of the Underground Economy and Employee Misclassification on Employers, Employees, and Independent Contractors.*
- April 8, 2009, Senate Lounge, State House – Fourth Commission hearing. Testimony and presentation is provided by Thomas M. Jones, Esq., Deputy Director for the Massachusetts Department of Labor, and Linnea Walsh, Director of the Massachusetts Underground Economy Task Force, regarding the Commonwealth's experience with the issue of employee misclassification and the steps it has taken to reduce it.
- April 22, 2009, Senate Lounge, State House – Fifth Commission hearing. *Public testimony* is provided by employees and from Dan Reilly, State Legislative Coordinator, International Brotherhood of Teamsters. A review of possible draft legislation is provided by Commission legal staff.
- May 6, 2009, Senate Lounge, State House – Sixth Commission hearing. *Public testimony* is provided along with testimony from Matthew Capece, Representative of the General President, United Brotherhood of Carpenters and Joiners of America. A review of possible draft legislation continues.
- May 20, 2009, Senate Lounge, State House – Seventh Commission hearing. An outline of proposed principles for legislation is presented and discussed.
- June 10, 2009, Senate Lounge, State House- Eight Commission hearing. An outline of proposed principles for legislation is presented and discussed. Members are provided a draft copy of Commission report for review.
- June 24, 2009, Senate Lounge, State House- Ninth Commission hearing. Draft legislation is reviewed and endorsed by the Commission. Draft commission report is reviewed and accepted by the Commission.

## EXECUTIVE SUMMARY

On July 8, 2008, Senate Bill 2008 – S 3099, introduced by Senate Majority Leader Daniel P. Connors, created the Special Joint Commission to Study the Underground Economy and Employee Misclassification. The Commission, co-chaired by Senator Christopher Maselli (District-25, Johnston) and Representative Arthur Corvese (District 55 – North Providence) was authorized to study the underground economy and employee misclassification as it relates to workers' compensation, taxation and unemployment, and explore possible solutions to this developing problem thereby lessening the impact on government and law abiding businesses and workers.

Senate Bill 2009- S 0279 extended the expiration date of the Commission to August 30, 2009. The Commission was charged to present its findings and recommendations to the General Assembly on or before June 30, 2009. This document represents the final report of the Special Legislative Commission.

Each member of the Commission, along with others who provided testimony, presentations, opinions, and assistance to the Commission, have been instrumental in preparing this document through a series of hearings and commission meetings.

When implemented, the proposals and recommendations contained herein would create a single, unified statutory definition of 'employee' and 'independent contractor' for enforcement agencies and departments. Doing so will help eliminate the confusion, ambiguity, and inconsistency among enforcement bodies as it pertains to these definitions, providing clarity and uniformity for employees, employers, state agencies, and the court system. Furthermore, these recommendations provide a financial disincentive for misclassifying employees and would help facilitate enhanced coordination and communication among state departments and agencies that had previously taken a siloed approach to inspection and enforcement.

The Commission considers enactment of the recommendations described herein as the most immediate step toward improving state enforcement, and reducing instances of employee misclassification and the prevalence of the underground economy.

## **FINDINGS**

### **❑ Employee Misclassification is an Issue in the state of Rhode Island that Harms Employees, Businesses, and the State**

Through public testimony, the Commission learned that employee misclassification is a serious issue in the state of Rhode Island that leaves employees vulnerable, denies the state significant funds that it is entitled to collect, and harms legitimate business owners who are playing by the rules. Over the course of several hearings, workers and business owners (see Addendum: Notes and Minutes of Commission Hearings) described how the misclassification of employees has negatively impacted their businesses and placed them at a competitive disadvantage. In one instance, a business owner described (see Addendum- Minutes of March 25, 2009) how his construction company was underbid for a building contract by over 10% - while the owner conceded that a some cost variation was certainly possible due to other business factors, the owner was convinced that his company, which had played by the rules, paid the required premiums and fees to the state, and classified its employees properly, was undercut by a company that was violating employment laws and misclassifying its workers as independent contractors to avoid paying items such as workers compensation or unemployment insurance.

In their annual report to the Governor and General Assembly, the state Department of Labor and Training reported that of the 500 employers and 7,121 workers it had audited in FY 2008; 6% of employers had misclassified at least 1 person as an Independent Contractor, and 4.33% of employees had been misclassified as an Independent Contractor<sup>1</sup>. While these figures are alarming on their own, it is important to recognize that due to staff reductions and other enforcement limitations, the Department is unable to determine whether these percentages represent the full picture of misclassification in Rhode Island. Furthermore, these percentages reflect only those companies audited in the select sample; increased oversight and enforcement is likely to result in an even higher percentage of employment fraud.

The Commission was provided with statistical analysis conducted by Workers Compensation Court staff which indicated that, even at a very conservative estimate of 1% employee misclassification (Significantly lower than the Department of Labor and Trainings own aforementioned audit findings), the state of Rhode Island stood to lose \$12,007,346 in FY 2008 (See pg. 16, Addendum: Notes and Minutes of Commission Hearings) due to employee misclassification. A weighted average of ten states that have calculated their percentage of misclassified employees, including our neighboring states of Massachusetts and Connecticut, further indicated that potentially 6.1% of Rhode Island employees were misclassified in FY 2008, which would have cost the state a total of \$49,852,317 in uncollected income tax, unemployment insurance, temporary disability insurance, and workers compensation premiums. While these figures are not based on empirical data, but rather reasonable and informed estimates; they nevertheless indicate the significant cost that employee misclassification represents to Rhode Island and all states.

Just as states are deprived of significant funds when employees are misclassified, the federal government also loses revenue from uncollected income tax, and other items such as Social

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<sup>1</sup> Rhode Island Department of Labor and Training Annual Report. Fiscal Year 2008. Released 2009

Security. The most recent “complete misclassification estimation”, conducted by the Internal Revenue Service, “estimated that 15 percent of employers misclassified 3.4 million workers as independent contractors, resulting in an estimated tax loss of \$1.6 billion (or \$2.72 billion in inflation- adjusted 2006 dollars) in social security tax, unemployment tax, and income tax”<sup>2</sup>. While these figures are alarming, they do not describe the full impact of employee misclassification, as they fail to take into consideration the secondary social costs of such exploitation. Misclassified workers, for example, likely will not qualify for certain guaranteed protections such as those offered under the Americans with Disabilities Act, family leave, or overtime pay, in addition to unemployment and workers’ compensation insurance. Instead, misclassified workers who are injured at work or laid off often burden taxpayer-supported programs, such as public healthcare and unemployment insurance. These costs divert tax revenue from other needs, such as education, local community aid, property tax relief, or other social and public safety programs. Additionally, employee misclassification helps increase overall workers’ compensation costs due to higher care costs, as well as improper premium collection from employers who shuffle employees between low-cost, low-risk and independent contractor job classifications to high-cost, high-risk occupations after a serious work related injury. Honest tax abiding employers are placed at a serious competitive disadvantage versus employers who cheat the system.

The Commission learned that 19 states have recognized that employee misclassification is a serious issue and have begun the process of examining the issue more in depth. Within the past year, Rhode Island’s neighbors of Connecticut, Massachusetts, New Hampshire and Vermont have all formed commissions to study the matter. During such difficult economic times, when state revenues are dropping significantly, employee misclassification is denying states of urgently needed funds, and puts honest, law-abiding workers and employers at a significant economic and competitive disadvantage.

### **❑ Rhode Island Lacks a Single Uniform Statutory Definition of ‘Employee’ and ‘Independent Contractor’**

Through testimony from state departments, as well as research conducted by legal staff, the Commission learned that there are several different statutory definitions of what an employee is versus an independent contractor, complicating cross-agency cooperation and communication. Workers compensation law (R.I.G.L. § 28-29-2), for example, defines an independent contractor as a person who has designated themselves an independent contractor, or who is found to be an independent contractor by the workers compensation court. Unemployment insurance (R.I.G.L. § 28-42-7), on the other hand, has a different definition for employee and defers to “those factors used by the Internal Revenue Service in its code and regulations” in determining an independent contractor. Lastly, the Rhode Island Division of Taxation relies on a 20-point IRS test to differentiate between an employee and independent contractor. These definitions have changed and evolved over years and can confuse and complicate joint enforcement efforts as one agency may overlook clear noncompliance with the statutes of another because their own statutory definitions are satisfied.

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<sup>2</sup> Nilsen, Sigurd R. Improved Outreach Could Help Ensure Proper Worker Classification. United States Government Accountability Office.



## **❑ Monitoring and Enforcement of Noncompliance and the Underground Economy By Departments Has Been Isolated**

As previously mentioned, at least 19 other states have begun to study the issue of employee misclassification. Many of these states, including Rhode Island's neighboring states of Massachusetts<sup>3</sup> and Connecticut<sup>4</sup>, have found that the monitoring and enforcement of various labor and wages laws are disconnected and 'siloed' among state agencies and departments. While the Commission found that several of Rhode Island departments were sharing information to a degree, and had increased the level of cooperation since the Commission formed, there is still a lack of widespread interdepartmental coordination and communication. For example, the Commission learned through department testimony that there is no uniformity and little cross-referencing among individual departments' documents and forms. The Commission then discussed the effectiveness, and simplicity, of connecting compliance across agencies by requiring that applicants prove compliance with one entity to obtain compliance with another. Also, the Commission learned from testimony provided by Thomas M. Jones, Esq., Deputy Director for the Massachusetts Department of Labor, that most departments that deal with wage and employment matters are viewing and investigating the same information, but through different perspectives. By enabling joint enforcement, these departments can more easily share data and information, and become more aware of the procedural 'red flags' that they should be looking for when monitoring for another agency's noncompliance. Lastly, by creating a joint enforcement and information sharing effort, the state can streamline and promote better efficiency in government, which can help simplify processes for business owners, employees, and enforcement agents.

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<sup>3</sup> Executive Order No. 499. [http://www.mass.gov/?pageID=elwdterminal&L=4&L0=Home&L1=Government&L2=Departments+and+Divisions+\(EOLWD\)&L3=Joint+Task+Force+on+the+Underground+Economy+and+Employee+Misclassification&sid=Elwd&b=terminalcontent&f=Executive+Orders\\_executive\\_order\\_499&csid=Agov3](http://www.mass.gov/?pageID=elwdterminal&L=4&L0=Home&L1=Government&L2=Departments+and+Divisions+(EOLWD)&L3=Joint+Task+Force+on+the+Underground+Economy+and+Employee+Misclassification&sid=Elwd&b=terminalcontent&f=Executive+Orders_executive_order_499&csid=Agov3)

<sup>4</sup> An Act Concerning Employee Misclassification. <http://www.cga.ct.gov/2008/ACT/PA/2008PA-00156-R00SB-00454-PA.htm>

## **RECOMMENDATIONS**

Modeled after similar principles that have been introduced in several other states, the following policy recommendations endorsed by a majority of the Commission would help reduce the incidence of employee misclassification by greatly improving enforcement measures, closing statutory loopholes that are often taken advantage of, and increasing governmental outreach and public awareness of new and current employment laws for businesses.

While full compliance with any law can never be guaranteed, these recommendations would tighten up enforcement, increase public education, and improve the current Independent Contractor system. Importantly, improved and coordinated enforcement efforts will help increase revenues for the state through the enhanced collection of those funds it has been empowered to collect, while reducing the costs to the state resultant from workers compensation noncompliance, undocumented or improper employment practices, tax and unemployment insurance premium avoidance, and other wage or labor law violations.

### **❑ Develop a Unified Statutory Definition of the Terms ‘Employee’ and ‘Independent Contractor’**

As mentioned previously on page 8, Rhode Island state departments currently lack a single clear and concise definition of what an ‘independent contractor’ is, as compared to an ‘employee’. While there are thousands of individuals working in the state of Rhode Island who clearly function in an independent capacity; evidence and experiences in other states suggest that many workers who classify themselves as independent contractors are, in fact, employees, but have chosen to, or have been persuaded to, register as independent contractors.

The Commission recommends replacing current statutory definitions of independent contractor with respect to Workers Compensation and Unemployment Insurance with a comprehensive three-part, dual test definition. Under such a definition, a person would be presumed to be an employee unless:

- (1) the person is free from control and direction in connection with the performance of their service, both under his or her contract for the performance of service and in fact; *and either:*
- (2) the service is performed either outside the usual course of the business for which the service is performed or outside of all the places of business of the enterprise for which the service is performed, *or;*
- (3) the person is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in the service performed.

This clear definition of 'independent contractor' would eliminate any ambiguity about proper classification and would close a significant loophole that is often used to misclassify workers. Additionally, state agencies would find it easier to share information and coordinate enforcement if their definitions are alike and they are operating on the 'same page' as it pertains to noncompliance.

### **❑ Modify Filing Procedures for Independent Contractor Status**

The Commission further proposes replacing the filing procedure for designation as an independent contractor. Currently, there is no established criterion or financial commitment involved when filing as an independent contractor. Thus, individuals who clearly meet the standard of an employee are able to incorrectly file as an independent contractor with few regulatory, and no financial, commitments. Employers are thereby able to use this filing, whether entered into correctly or incorrectly, voluntarily or unwillingly, as defense when suspected of improperly classifying employees. While this does not preclude a court from determining independent contractor status, it does complicate the enforcement process and provides the channel through which many incidences of employee misclassification occur.

The Commission recommends requiring an annual registration fee for filing as an independent contractor and for entities hiring independent contractors. While independent contractors can be hired by several entities over the course of a year, they would be required to pay this fee only once annually. Likewise, business entities hiring independent contractors would be required to pay the contractor fee once annually, but would be able to continue to hire independent contractors as needed without paying an additional fee for each. This provision would be limited only to companies and businesses, thus preventing a homeowner hiring an independent contractor for a single job from being subject to the fee.

Establishing this registration fee would, for the first time, require a financial commitment on the part of an independent contractor and the hiring entity that would discourage filing incorrectly and provide a disincentive to misclassify employees, while raising revenue for the state. Funds from this registration could help assist education and outreach efforts to improve compliance and prevent misclassification in the first place

**□ Extend the Special Joint Commission to Study the Underground Economy and Employee Misclassification**

To monitor the effectiveness and implementation of the legislative recommendations, recommend further action if necessary, and to ensure that proper enforcement against employee misclassification continues, the members recommend extending the life of the Special Joint Commission to Study the Underground Economy and Employee Misclassification further. The Commission would continue to rely on industry and departmental expertise, and promote coordinated enforcement and information sharing across departmental lines. As it continues to monitor incidences of employee misclassification, the Commission would further recommend any additional statutory or regulatory changes necessary to improve cross-agency cooperation and prevent misclassification.

By ensuring that those businesses which should be paying into items such as workers compensation or unemployment insurance are doing so, other states have been able to lower premiums for all payers due to the increased number of participants contributing to the system.<sup>5</sup> While such a result cannot be guaranteed for the state of Rhode Island, consistent and coordinated enforcement can ensure that the obligation to fund those items designed to protect all employers and employees in the state is being shared by all appropriate participants.

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<sup>5</sup> Ibid.

2008 -- S 3099

**STATE OF RHODE ISLAND**

**IN GENERAL ASSEMBLY**

**JANUARY SESSION, A.D. 2008**

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**JOINT RESOLUTION**

**CREATING A SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND  
ECONOMY AND EMPLOYEE MISCLASSIFICATION**

**Introduced By:** Senator Daniel P. Connors

**Date Introduced:** June 12, 2008

**Referred To:** Senate Constitutional & Regulatory Issues

RESOLVED, That a special joint commission be and the same is hereby created consisting of fifteen (15) members: three (3) of whom shall be members of the Senate, not more than two (2) from the same political party, to be appointed by the President of the Senate; three (3) of whom shall be members of the House of Representatives, not more than two (2) from the same political party, to be appointed by the Speaker of the House; one of whom shall be the Director of the Department of Labor and Training, or designee; one of whom shall be a member of the Worker's Compensation Court, to be appointed by the Chief Judge; one of whom shall be the Director of the Department of Business Regulation, or designee; one of whom shall be a representative of the Division of Taxation, to be appointed by the Director of the Department of Revenue; three (3) of whom shall be representatives of the Workers' Compensation Advisory Council, to be appointed by its Chairman, one of whom shall be representative of labor, one of

whom shall be representative of business and one of whom shall be representative of insurance; and two (2) of whom shall be public members, one of whom shall be representative of small Business, and one of whom shall be representative of labor, to be appointed by the President of the Senate and Speaker of the House.

In lieu of any appointment of a member of the legislature to a permanent advisory commission, a legislative study commission, or any commission created by a General Assembly resolution, the appointing authority may appoint a member of the general public to serve in lieu of a legislator, provided that the majority leader or the minority leader of the political party which is entitled to the appointment consent to the member of the general public.

The purpose of said commission shall be to study the underground economy and employee misclassifications as it relates to workers' compensation, taxation and unemployment, and possible solutions to a developing problem thereby lessening the impact on government and law abiding business and workers.

Forthwith upon passage of this resolution, the members of the commission shall meet at the call of the President of the Senate and the Speaker of the House and organize and shall select, from among the legislators, a chairperson. Vacancies in said commission shall be filled in like Manner as the original appointment.

The membership of said commission shall receive no compensation for their services.

All departments and agencies of the state shall furnish such advice and information, documentary and otherwise, to said commission and its agents as is deemed necessary or desirable by the commission to facilitate the purposes of this resolution.

The Joint Committee on Legislative Services is hereby authorized and directed to provide Suitable quarters for said commission; and be it further

RESOLVED, That the commission shall report its findings and recommendations to the General Assembly no later than January 27, 2009 and said commission shall expire on June 27,

2009.

## **Addendum: Notes, Minutes, and Distributable of Commission Hearings**

### **SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION**

**Honorable Christopher B. Maselli  
Honorable Arthur J. Corvese  
Co-Chairs**

**February 25, 2009**

#### **Attendance**

**Members Present:** (14) Senator Christopher Maselli, Senator David Bates, Representative Arthur Corvese, Representative Douglas Gablinske, Mike Lynch, George Nee, David Burnham, Terry Martiesian, David Palmisciano, Judge Morin (on behalf of Chief Judge Healy), Paula Pallozzi, David Sullivan, Matt Carey, Steven LaBrie

**Member Absent:** (1) Representative Brian Newberry

#### **Summary:**

- 1) Upon motion by George Nee, seconded by Mike Lynch, Senator Maselli and Representative Corvese are unanimously elected Co-Chairmen of the Commission.
- 2) Senate Policy Staff hands out informational packets about employees / independent contractors.
- 3) George Mason, Chief of Staff to the Senate Majority Leader addressed the members and described that the three proposed action steps for the Commission – improved legislative definition of ‘employee’ and ‘independent contractor’; increased coordination and communication between departments; and better community awareness and outreach; were taken from best practices from other states across the nation that have dealt with the issue of misclassification.
- 4) Senate Majority Leader Daniel P. Connors addresses the Commission.
- 5) Representative Corvese – “I would like our legal counsel to review all definitions of independent contractor and employee and be able to brief us at our next Commission Meeting.”
- 6) Commission members decide to have the next meeting on March 11<sup>th</sup> at 1:00 in the Senate Lounge. The next agenda will have testimony from state agencies affected.

## MEETING MINUTES

### **SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION**

WEDNESDAY, MARCH 11, 2009  
1:00 P.M. – SENATE LOUNGE – STATE HOUSE

**PRESENT:** Hon. C. Maselli, Hon. A. Corvese, Hon. D. Gablinske, Hon. D. Bates,  
Chief Judge. G. Healy, S. Labrie, P. Pallozzi, M. Carey, D. Birmingham, M. Lynch,  
D. Sullivan, G. Nee, T. Martesian

**ABSENT:** Hon. B. Newberry

Co-Chairs Maselli and Corvese convened the meeting at 1:10 p.m. They both welcomed those in attendance. They reported to those present that they both met with legal counsel to discuss what was discussed at the previous meeting, obtaining the definitions of the various statutes regarding employee and independent contractor.

Mr. Igliazzi reported that he met with Fred Marzilli, legal counsel for the House, and Robert Kotkowski and Stephen Iannazzi from the Senate Policy Office. Mr. Marzilli was unable to attend today's meeting; Sen. Igliazzi supplied the Commission with a report in his absence. At least four different definitions were used for the statutes in Rhode Island – one used by the Department of Revenue for tax purposes; one by the Worker's Compensation Courts; one by the Unemployment Department and the Common Law definition. It is the Commission's mission to come up with unified definitions of the statutes as they would affect the various departments. Twenty-seven states have already done this.

Mr. Sullivan of the Department of Revenue pointed out there is presently a list (20 questions/test), which is utilized by his department, and he would be happy to provide it at the next meeting. He noted that Mr. Marzilli cautioned him that this would be a complex area and would take a cooperative effort of all departments to make it work. Representative Corvese noted that the two major reasons that this joint commission was created was to address 1) loopholes and abuse; and 2) the fact that there is a lack of communication and there were different statute definitions being used among the various departments. Both he and Senator Maselli, on behalf of the members of the Commission, thanked the offices of Legal Counsel and Policy Staff for the excellent job they did to prepare for this as well as the initial meeting.

It was noted that the State of Massachusetts is one of the latest states to come up with the most comprehensive definition. Representative Corvese requested, with the permission of Senator Maselli and the rest of the members, to see Massachusetts's definition. He also believed the New York has now developed a good definition for its state. The Senate Policy office was requested to research and obtain the statute definitions from the states of Massachusetts, Connecticut and New York and extend invitations to these states to testify at the March 25<sup>th</sup> meeting. The definitions from the remainder of the 27 states would also be requested for perusal by the members of the commission.



Agencies Testimony

David Sullivan of the Unemployment Insurance Auditing Department of the Department of Taxation, reported (see attached) that his department's responsibility is to administer the taxes that are instituted by the General Assembly in the most efficient manner (i.e. corporate income tax, personal income tax, sales tax and a variety of other taxes.) His department became, in 1996, the main revenue collector enforcement division for Unemployment Insurance (i.e. TDI-temporary disability insurance, and training fund.) The department also does the revenue collection and enforcement for unemployment insurance. (See attached.)

The Unemployment Insurance Board defines the statute the same way that the Internal Revenue Code defines it. In the Rhode Island statute it is refers to as the Internal Revenue Service classifies and employee that, for unemployment insurance, does the same.

At present, employee tax statutes are not combined. This is due to the fact the Rhode Island's personal income tax piggyback off the Federal tax. If you are classified as an employee at the Federal level, then you are the same at the State level. If you are an independent contractor or self-employed individual at the State level, you are the same at the Federal level. He noted that the IRS code does not have a complete definition of and employee vs. an independent contractor. Over the last 40/50 years they have had different cases (i.e. behavior control, is employee training provided, is training provided the employee regarding financial control, is the individual subject to their own boss, is there a contract or an investment, are employees reimburses expenses incurred, and employee benefits. He referred to the "20 step test", which includes questions such as are you provided training, whose equipment do you use – your own, is it supplied by the employer, etc. Are work tasks specifically defined? (See distributed two-sided pamphlet attached.) He also noted that the "20 step test" is not included as part of the Federal code. Mostly, definition of an "employee" is determined on an individual appealed court case.

The question was raised as to whether the Rhode Island Internal Revenue Service does random searches? Answer – yes. Question was also raised as to whether is would be easier to drop from 20 points to 3 thereby making it easier to administrate? Rep. Corvese noted that this may create a problem, but was surprised that the 20 point test are not part of the code, and that nothing was derived from those previous court cases. The IRS found many businesses had a problem defining an "employee", and thus came up with the 20-point questionnaire to come to a determination. Question was posed as to whether his department receives a copy of that determination. However, after the determination is made, the employer will either issue a W-2 if an employee, or a 1099 for an independent contractor, his department does get an electronic copy of the W-2's and 1099's. If the IRS does an audit, and changes some of the employees to independent contractors or a business and does an assessment, they receive copies of the audit reports. In addition, any Federal information his department receives they must keep confidential according to IRS guidelines. His department is audited once every two years by the IRS to make sure that the information (which is shared with the Unemployment Insurance Special Joint Commission Department for insurance purposes.)

Question was raised if the Department of Labor and Training receives this same information from the IRS. Once the information is changed on the state level, it then becomes state information.

Judge Healy questioned whether the IRS, once having performed an audit, if they can then reverse the original decision? Mr. Sullivan responded no. A question was raised if the decision is made public and would an employer be able to make inquiries of the Department of Internal Revenue as to the status of employees working for him? That is done by the Federal IRS and through a public ruling and a "private letter ruling" is done.

Mr. Sullivan also noted that, under Federal law, his department is required to perform an audit on 2% of the employers (sometimes a little more) a year for unemployment insurance. In addition, his department also has data matching – the General Assembly appropriated a fund for the Division of Taxation to create a data warehouse a year and a half ago. They are in the process of continuing to load different forms of data – at this time there are Federal, State and other states' data, and continue to add. A question was raised if his department received all W-2s and 1099s? He reported that they received both W-2s and 1099s for all residents of the state and for any resident employer making payments for any individual. Question was then raised of how many 1099s are issued in the State of Rhode Island? Mr. Sullivan said he would obtain that information for the Commission by the next meeting.

Mr. Lynch inquired if any data is coming out of the data warehouse? Mr. Sullivan reported that, yes, they have been running compliance programs over the last six months. Upon first running a match of federal vs. state taxes submitted (in 2004), there were approximately 15,000 who did not file a state return, but did file a federal one. Some people were audited, and in 2005, some 4 million people did not file, who owed about \$2 million in state taxes.

He continued that his department performed approximately 650 employer tax audits per year. Of that, 25-30% of them for that calendar year contained a reclassification of an independent contractor to employer; which comes to 600 individuals that were found, upon auditing those companies, that they were misclassified as an independent contractor. Representative Corvese asked at what tax implication? Mr. Sullivan noted that it consisted of unemployment insurance, TDI, and his office is presently looking for an assessment, which he would supply to the Commission. He said in performing the audit, they use the 20-point test to determine independent contractor vs. employee. Should an individual disagree with the determination of his office, they can go through the appeal process and, ultimately, the court if they wish.

A question was raised that, when Mr. Sullivan's department auditors the employers, are individual returns looked at also? Mr. Sullivan said, yes, his department follows up on that as well. Regarding "inner agency" involvement/discussion, the question was raised as to whether Mr. Sullivan's department has gone to Department of Labor and Training and asked for a list of independent contractors who are registered and pick 2% of those to see if they are living within

the rules? Mr. Sullivan said it is absolutely possible – prior to obtaining info through the data warehouse, they would have only been able to obtain 6,000 people, now electronic file can be retrieved. After the Commission's last meeting of March 11<sup>th</sup>, his department was in contact with the Department of Labor and Training and was able to obtain the independent contractors list, which contains social security numbers, etc., thereby being able to build a profile of that individual.

Mr. Lynch inquired if the 650 employer audits and the 20-30% are done every year? Mr. Sullivan replied yes. The question was raised as to whether, with the 650 employer audits done every year, were there certain industries that seem to be out of compliance? The department has not delved down that far as yet into statistics for this, but can using the NRCS code, which is a new code, to attempt to find out what industry the employers are in. Mr. Sullivan said that many times there is confusion within the construction industry as to employer vs. independent contractor. He said it is as much their fault as the individuals, the State does educate the taxpayer as much as is necessary to explain to them upfront explaining what they need to do to comply. Most times, these individuals follow what other's in the industry are advising them to do and do not receive proper advice. He noted that, for the most part, there are more legitimate independent contractors than there are those abusing the system.

Question was raised as to how many people from his department would be assigned to this type of audit? The employer tax section has approximately eight auditors to 650 audits per year. There about 30-35 auditors who do most of the sales tax/corporate income tax. Mr. Sullivan noted that for every additional full-time auditor hired, generates anywhere from \$600,000 to \$750,000 in additional revenue per year. Each additional auditor is paid approximately \$50,000 including benefits; a fully trained auditor returns anywhere from 10-1 on their investment. The 650 audits that are done per year represents approximately a little over 3% of the employers, which is considered high. The department is required to perform 2% worth of audits, but try to do as many as possible. There are approximately 28,000-30,000 employers currently in the state.

The question of realtors as independent contractors was raised. If the realtor works for one person in that person's office, are they considered an independent contractor? A realtor is explicitly not an employee under the Workman's Compensation Act. Many years ago, they were using the IRS definitions at the time to suggest that they were not considered employees under the IRS; therefore they would not be considered employees under the Workman's Compensation Act. Mr. Sullivan explained that although a realtor has his/her own desk at an agency, they usually have their own computer and are responsible for their running their own advertisements, setting their own hours and soliciting their own business. Just because one works for one person, does not necessarily mean you are an employee; they can work for one person and still be considered an independent contractor.

Regarding the 650 employer tax audits, the question was raised as to whether they are mostly Rhode Island based, and whether outside companies that may work in Rhode Island are audited

also? Mr. Sullivan replied that as for the employer tax, his department audits Rhode Island companies who are subject to the unemployment insurance tax. They do at least the 2% of the employers, as well as having staff auditors who travel all over the company who audit those companies who do work in the State of Rhode Island. He also noted that, in addition to these audits, his auditors perform approximately 2,400 audits per year; these are not employer tax audits, but they are also sales, corporate ones.

Judge Healy asked if there are a certain criteria that determines who are to be audited or are they randomly selected? Mr. Sullivan said that the audits are done at random, as the taxpayer cannot know when they will be audited because it takes the guesswork out of whether they should "push the envelope" or not. The department also does a lot of data matching where IRS information is obtained from returns what are filed with the state; as well as the corporate returns (where the wages may say are paid at \$7 million dollars – but the Rhode Island company only pays the state a withholding of \$100, which shows that there is something really wrong.)

Judge Healy then asked if the 25-30% post-audit reversals would not necessarily be indicative of the entire appeal? Mr. Sullivan noted that a lot of their audits are r-audits; his department will audit someone in 2004, the company may change employees, they will wait 3 years and go back and re-audit them make any corrections 2007, and schedule them for a re-audit again in 2011. He noted that most times the companies will wait for his department to come and do the audit, as they don't want to do the bookkeeping or paperwork required and wait to be audited and have the work done for them. He also noted that many of their high audits are re-audits.

Representative Corvese asked for an example of an outside company that may be audited, i.e. a franchise? Mr. Sullivan said that it could be a franchise and may also be a multi-state business, or a state that may have a small contract in Rhode Island, in order to make certain that that company is reporting all their sales and use taxes as well as all of their withholdings, or a large contractor. The department does not discriminate – they try to cover as much of the industries as they can, to try to keep people honest. The question was raised if these outside company audits are 2-3% or less? Mr. Sullivan reported that that is the percentage, more or less, as they use more auditors for the sales and use tax audits, which generate the highest revenues.

Mr. Lynch questioned whether, in relation to tracking information there was a parallel effort of information exchange by the state and the federal IRS going on at the same time with other states, and if so, does UI Auditing benefit from it? Mr. Sullivan said that most of the states are taking advantage of the data exchange and matching. The New England states have done some work in a collaborative effort to try to deal with non-residents employee working in the state and taking credit for working in the state. He noted that on a federal level, it is a constant area of confusion and misuse. Mr. Lynch asked if UI shares in the results from their audits with these other states, too? Mr. Sullivan said yes; however, the federal government is more technologically advanced than his department is. The federal audits are dated and done electronically, where many of his department's audits reports are still done in Word and not

actually saved electronically. His department gets the federal information quicker than his department can get its information to them.

Mr. Nee posed a question in regards to the \$750,000 additional revenue each additional auditor generates for the state. He asked if there was a point a point of diminishing returns with that? Mr. Sullivan answered no, the tools that his department has now, they have more work than they can get to (i.e. discrepancies with audit leads.) There have been a few revenue agents added back for auditing to his department's budget this year and 2010.

The questions was also asked if the 3% if the Rhode Island employers that are audited every year was the norm, and is there a norm nationwide? Mr. Sullivan replied that the federal government requires for unemployment that his department audits at least 2% of the state's employers to comply with code. **He noted that every year the state does a tax performance systems report to the IRS, Department of Labor within the federal government, so that they have that in place.** Chairman Corvese asked the Senate Policy staff to research this.

Question was asked if Mr. Sullivan was familiar with the "Questionable Employment Tax and Practice Initiative" with the IRS, a program designed to improve compliance with employment. He replied yes, he was familiar with it, that Rhode Island's has unemployment insurance and the wage withholding, and it is not that these are not any less important, but at the federal level they have Social Security and Medicare making it a lot more revenue that is at stake. He also noted that the IRS has done a study of a "tax cap" two or three years ago on the non-compliance of self-employed individuals; a lot of times these people are misclassified as they claim to be independent contractors when they are, in fact, employees. When one is an independent contractor who is self-employed, they can write off certain expenses that you can't as an employee, resulting in more benefit. When this person is re-classified as an employee, those deductions go away and their income becomes higher.

Chair Maselli asked Mr. Sullivan if his department presently has any specific recommendations for coordinating enforcement across the departments? Mr. Sullivan said that his department is working with the other state departments to breakdown some of the barriers in communication (i.e. in following up with the Division of Taxation, they follow strict guidelines of disclosure – they are unable to openly share information with certain people. However, with regard to certain statutes, it can be done.) He noted that they need to continue to see what and who it would be beneficial to his department to share information in order to include it into the present statutes. He also stated that he cannot share federal information when it comes to federal statutes. Chairman Corvese asked if the sharing can be done once the federal information becomes state information, can it be shared between state departments? Mr. Sullivan said, yes, once the information is converted to the state level.

Mr. Nee noted that he thought it would be extremely beneficial to having one, centralized area where tax/audit information was shared between departments and that would be disseminated out

to different tax agencies (i.e. Department of Health, etc.) – very beneficial to both businesses and the state.

Matthew Carey

Department of Labor and Training/Worker's Compensation and Self Insurance

Mr. Carey reported that statute legislation was implemented in 2001. The question was raised if the legislation addressed employers or independent contractor statute. Both employers and independent contractors are required to file a form with the Department of Labor and Training and it is recorded and listed on the web. Final decision rests with the court. He noted that 7,000 pre-filing fines were filed annually since 2001. One contractor can file numerous independent contractor forms. The form includes a number of warnings (see attached.) Chairman Maselli questioned if there was a filing fee, and are name, social security number, etc. required when filing. Mr. Carey noted that the form was created after the statutes passed in 2001.

It was also noted that the three most filed were from Brown, a local dance club in Rhode Island and the cities and towns (i.e. snow plow drivers.) The question was raised as to how the independent contractors are informed? Mr. Carey reported that there is an educational effort put forth to all employers. In the event of an employee injury, it goes to the courts – the court will seek a completed form should one not be on file. He noted that the hiring entity does not sign the form, only the independent contractor. Chairman Corvese questioned if the form is signed under oath? Mr. Carey said no, but with each form filed, a casement form is filed as well. Question was also raised as to the employee Worker's Compensation forms are signed under penalty of perjury? Mr. Carey said that the certification shows that they signed their form.

It was noted that of the 12,000 independent contractor registrations filed, most from the construction field are not registered. Mr. Carey noted that the main concern is if an employer has Worker's Compensation coverage – that will satisfy all employees on the job site and there is no need to list all – they are covered. Should any of the independent contractors end up in court, Judge Healey would determine the outcome of their filing.

Mr. Lynch questioned whether or not those who are not presently classified but those who are paying out or not, thereby avoiding the issue of filing? It was noted that since 2001 the Worker's Compensation law/sanctions have been given toughened penalties. It was questioned whether there was a penalty for falsification of a form, the answer – yes.

Chairman Corvese went back to the issue of the 7,000 filed per year (12,000 with the Independent Contractor's Board registered – the auditors can obtain from them.) Mr. Carey reported that a form was created in 2001 by consensus – a list of the parties involved – to see if they were represented in the same way in this joint committee. The ultimate goal would be to be

able to share information from the form with the unemployment insurance auditors, which would be very helpful.

Mr. Martiesian inquired if those who are exempt (i.e. fisherman, electricians, etc.) are required to file under the Department of Labor and Training? Mr. Carey answered yes, they were.

Mr. Nee asked if Mr. Carey had any idea how many of the 7,000 forms filed multiple times (i.e. if the person is working three separate jobs, six months later three more, are they required to file a new form for each new job with Worker's Compensation? Mr. Carey replied, yes, they are required to do so.

**Julie Tamuleviz, Esq. – Worker's Compensation Fraud and Compliance Unit**

Ms. Tamuleviz reported that she also works in conjunction with Mr. Carey's departments. Her responsibilities are to investigate any worker's compensation fraud. She noted that someone who is working for one or more employer, needs to file both a worker's compensation and independent contractor forms, with the Department of Labor and Training, where the records are recorded and kept. She noted that her department keeps track of over 5,000 filings and they share these with the auditors, such as when Unemployment Insurance needs withholdings of foreign companies who may be working in Rhode Island.

Mr. Nee inquired if out of state independent contractors are responsible for \_\_\_\_\_ not sure \_\_\_\_\_ withholdings but not unemployment insurance? For example, if someone were from Connecticut and working a job in Rhode Island and obtaining his earnings, would Connecticut be responsible for paying the worker's compensation insurance?

Chairman Corvese questioned where out of state workers would go to get the proper papers to file? (Example: Rhode Island obtains the papers from the Secretary of State's office.) Is there a problem trying to match those who are registered with Secretary of State's office since there is no employer identification number on the form? Chairman Maselli noted that out of state workers should be registered with the Secretary of State's office. Mr. Lynch gave an example of in the state of Massachusetts, a charge is applied for a building permit, and they must show proof that a worker's compensation form has been filed. Chairman Maselli also noted in order for someone to be listed as "incorporated", they must file as "incorporated" with the Secretary of State's office.

It was also noted that clarification is needed when an independent contractor is working with a sub-contractor, with withholdings of 3%-6% at the end, they need to get a letter of good standing beforehand.

SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND  
ECONOMY AND EMPLOYEE MISCLASSIFICATION

A Meeting of the "Special Joint Commission To Study the Underground Economy and Employment Misclassification" was held on Wednesday, March 25, 2009 at 1:00 PM in the Senate Lounge.

In attendance were the following members:

Senator Christopher Maselli  
Representative Arthur Corvese  
Representative Douglas Gablinske  
Senator David Bates  
Honorary George Healey  
Representative Brian Newberry  
George Nee  
Michael Lynch  
Matt Carey  
David Sullivan  
Paula Pellozzi  
David Palmisciano  
David Burnham  
Steven Labrie  
Terry Martisian.

Co-Chairs Maselli and Corvese opened the meeting at 1:05PM. They both welcomed those in attendance. Representative Corvese explained that as previously discussed, this meeting would have public testimony by Employees, Independent Contractors, Employee Organization and Employers. At this time the testimony would begin.

Thomas Savoie from the RI Carpenters Local 94

Testified that various companies pick their own sub-contractors and hire their own employees. Employees interviewed on these jobs explained that they work 7 days per week with no overtime, receive no benefits and were paid cash. These inconsistencies were reported to various State and Federal agencies and after this investigation was completed nothing was resolved and jobs were completed.



Tim Byrne from the Plumbers and Pipefitters

Testified regarding prevailing wage laws and the enforcement of them. A report from the Massachusetts Attorney General Office stated that businesses that properly classified their employees and follow all related statutes are at a competitive disadvantage applying for work. Reviewed prevailing wage laws that are part of every contract. Also gave examples of inconsistency in payroll and payments of employees.

Felix Carlone from RI Contractors Registration and Licensing Board

Stated Contractors Registration Board position is a claims board for the homeowner's, and see the problems with prevailing wage on a much smaller scale. The Board hears a small fraction of violation of misclassification of workers. Investigators found a mix-bag of what was going out on in terms of levels of administration, wages and payroll. Contractors are using the registration process to prevent hiring employees so they are paying no payroll taxes, worker's comp insurance and no unemployment taxes. This process has been a problem since day one and getting worse by the day due because of the economy, lay offs; rising unemployment and more people are working under the table.

Ed Ladouceur from RI Builder's Association

Stated that Contractor's Registration Board generates over one million dollars a year, they are a self-sustaining enterprise. The Contractor's Registration Board has the resources to fund enforcement & staffing but does not have the approval. Monies are in the budget although difficulties have arose in getting approval to buy the necessary equipment to document these illegal activities on the jobsites. Also stated, he serves as a member of the OSHA 10 Safety & Enforcement Board, where there is a vacant investigator's position.

George Wayland - Contractor's Registration and Licensing Board

Testifies there are unfunded mandates currently in effect. Contractor's Registration Board registers all contractors residential & commercial, law was changed in 2001. Unfortunately there is not enough staff to complete this process. Major concern is enforcement, priority concerns are the homeowners. Following other states like Florida and Arizona "sting operation" technique to enforce violations.

Michael Sabitoni- Build RI, Laborers' Local Union 271

Testified of first hand knowledge of the fraud presently affecting the public and private construction industry. Part of the problem is lack of enforcement due to lack of staffing at various RI state agencies. On public projects, employers misclassify higher skilled workers as laborers, enabling them to reduce hourly costs. Employers consistently pay these workers less than prevailing wage by falsifying payroll records. These contractors knowingly get away with these acts and can calculate these illegal costs cutting measures into their bids creating

an unfair advantage over law-abiding firms. Also contractors have falsely labeled workers as helpers as to reduce payroll records. Underground economy includes unreported practices as employers paying their workers in cash and forcing work to be complete off the clock. In private construction there is zero oversight in paying workers cash, contractor misclassification is even more prevalent. These firms that misclassify, don't provide health insurance and don't employed RI residents. (See written testimony)

Bob Baldwin- RI Builders Association,

Testified on a few major issues.

(1) Those residential home additions are one area where substantially lower bids come in and provide competition to union members who in turn lose the jobs. Example: after inquires of which company won the bid it was revealed that the jobs were being done on weekends by police officers and firefighters who are under the radar. No taxes are paid, no worker's comp is paid... **Cash is King.**

(2) Out of state contractor particularly how they relate to big box chains. They are supposed to have licensed contractors, but they have sub contractors from out of state. Examples Home Depot, Lowes.

(3) Statewide Building Code gives homeowners the authority to do their own electrical, plumbing, and carpentry work outside the jurisdiction of everyone. This takes job away from union members. Building inspectors can only assess the job to see if it meets the building code standards.

(4) Penalties and responsibilities to the recipients' of cash.

Armand Lusi- A.F. Lusi Construction

Signatory contractors with Laborers' Union. Contractors are suspicious when they are under bid by fellow contractors by 10%. There are certain costs every contractor has, labor wages can not change from contractor to contractor because the rates are set by prevailing wage laws. The only ways to under bid by 10% or more is by paying cash to employees or misclassify a worker into a lower paying position.

Monica Staff- RI Association of Realtors, Inc.

RI Association of Realtors believes that the existing system works well for consumers and real estate licensees and urges to recognize the limited exemptions for real estate licensees who are compensated mainly by commissions. (Please note written testimony)

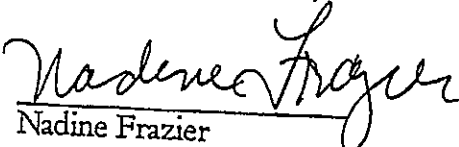
At this point, Chairman Corvese thanked all those who testified. After further discussion Chairman Corvese asked the Senate Staff to contact other New England States to testify on how they deal with the underground economy and misclassification of workers.

The next scheduled meeting has been set for April 8, 2009 at 1:00 PM in the Senate Lounge.

Seeing there was no further business to come before this meeting it was unanimously voted to adjourn.

Adjourned: 3:40PM

Respectfully submitted,

  
Nadine Frazier

## MEETING MINUTES

### **SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION**

**WEDNESDAY, APRIL 8, 2009  
1:00 P.M. – SENATE LOUNGE – STATE HOUSE**

**PRESENT:** Hon. C. Maselli, Hon. A. Corvese, Hon. D. Gablinske, Hon. D. Bates,  
Hon. B. Newberry, Hon. G. Healey, M. Cary, P. Pallozzi, G. Nee, M. Lynch,  
T. Martiesian, D. Palmisciano, S. LaBrie, D. Burnham

**ABSENT:** D. Sullivan

Co-Chairs Maselli and Corvese convened the meeting at 1:15 p.m. They welcomed guests, Thomas M. Jones, Esq., Deputy Director for the Massachusetts Department of Labor, and Linnea Walsh, Director of Communications for the Massachusetts Department of Labor.

Mr. Jones distributed informational packets, which included a copy of the Executive Order that created their state's commission, which was signed by Governor Patrick on March 12, 2008. He outlined some of the main issues that came up in dealing with organized labor were the misclassification of employees and the failure of employers to properly pay withholdings, i.e. workman's compensation, unemployment, minimum wage, etc. All of the appropriate social charges when doing business were not occurring, thereby representing a significant problem for business from a competitive point of view. This resulted in Governor Patrick formulating a task force to look at and question the proper classification of employees, wages, etc., resulting in hundreds of millions of dollars that were not being recovered.

Their task force, beginning in 2007, began looking at the various agencies, i.e. Unemployment, Workman's Compensation, Department of Revenue and Attorney General's office, finding that these departments were not sharing information. This task force originally consisted of nine (9) agencies, and has now increased to 17. Investigators then began to check and coordinate enforcement by all agencies, i.e. complaints, cases presently being worked on, action being taken and share this information between the various agencies. (See informational packet regarding compliance and fines charged.)

Mr. Jones noted that a provision was included for those employers who cannot provide insurance to their employees, and then they must pay approximately \$2.95 per employee. They found that most bars and restaurants don't offer health insurance or the necessary requirements under the law, and also don't pay the assessment. This has resulted in the Alcohol and Beverage Control Provision, now saying that the state will now hold up their license if the required assessment is not paid. This also applies to Professional Licensure and Apprenticeship – if the proper certification is not possessed for inclusion in an apprentice program, then the license will be pulled, thereby not able to bid on state work.

In addition, a "tip" line has been implanted (a 1-888 #), allowing employers an opportunity to anonymously call in and relay reports, i.e. "underbidding of work." Approximately 531 of these calls have been made since the May, 2008. Town hall meetings have also been implemented, 6-8 across the state, inviting those from the various communities to come forth and testify regarding problems with compliance of state business requirements.

Mr. Jones noted that the State of Massachusetts has three definitions of independent contractors, i.e. one for Department of Revenue, an "ABC" test for Unemployment, which is different from the wage and hourly ABC test. The ABC Law is worker's compensation, unemployment insurance and wage and hour, relying mostly on wage and hour. This was put into place in 2004. The Massachusetts Attorney General and the Executive Branch finds these are the most clean and effective definitions that they can work with. He also noted that there has been no objection by employers to these definitions. The Massachusetts Legislature is very supportive. Before the present budget deficit, the legislature was prepared to offer the department \$3 million to bolster their efforts in this regard.

The penalties that are in place are the existing penalties, however, there is now greater access to the information. Mr. Jones noted that two bills have been drafted to allow for a statutory change in order for the various agencies to open up information. These bills would allow for all agencies to share information between each other. (See attached bills.) As for Worker's Compensation, the present Massachusetts law states either an employer has Comp or they don't. There is presently a bill in now that would expand the authority of the investigators to go on the property to begin to remove records to see if documentation on file is supported (proper wage and hour, etc.)

There are presently 17 Worker's Compensation investigators, most of who are on the road 3-4 days per week. Their W.C. is funded by Assessment Unemployers - out of \$100 premium, the employers pay approximately \$4.50-\$5.00, which funds the agency, the trust fund for uninsured employees (any workers who are injured and are employed by employers who do not supply insurance), a COLA trust fund, a second injury trust fund, and various other trust funds. These trust funds raise approximately \$80 million dollars per year to fund the whole operation. The agency itself receives approximately \$21 million dollars in the "red", and is presently being investigated. (Please see the Massachusetts legislature website for "House 17".)

Mr. Jones also reported that they have a proposal, "Proof of Coverage", will be available online, where information can be shared. Presently, there is an issue as to whether that information is in compliance or not (payroll record sharing, etc.) The fact whether there is actual coverage or not will be shared. In addition, Massachusetts also has a direct link to the "Worker's Compensation Rating Bureau." There were previously approximately 25-30 "stop work" orders (violations) a month; now it is approximately 250-300 per month; this is all as a result of the task force sharing information and identifying new targets, and getting out around the state and investigating the various landscaping and construction sites across the state who may not be in compliance.

Of the 17 agencies in enforcement, some have more unique authority than others. For example, Unemployment will come onsite, but will not shut an operation down until a full audit has been done to determine whether or not there has been a violation on the payroll side, which may take up to a year; Worker's Compensation can shut down immediately, if they believe there is no insurance offered; Occupational Safety and Overseas Temporarily Help agencies can stop work due to license renewal (compliance, etc.) The Department of Occupational Safety oversees temporarily help agencies that can stop work for non-license renewals. Massachusetts does not have a state OCEA. Of the approximately 250 stop work orders, many do obtain insurance; however, some, with small staff – 2-3 people – try to get away with no insurance. Those the agency usually has a problem with are nail salons, auto body shops, pizzerias and landscapers, which are on a seasonal basis.

At present, 2-3 thousand workers are now covered by Worker's Compensation. Through the efforts of the data sharing process, weekly investigators meetings (which are chaired by the Worker's Compensation office), \$1.5 million dollars has been generated in the last year. In addition, through the Fair Share contribution (the medical money) and the employers who fail to pay the Unemployment Insurance, close to \$1 million of the \$1.5 million, which does not go back into the state general fund, but goes back into the UI trust fund to help pay benefits. Each agency conducts their own investigation; there is no "coat-tailing" by other departments.

It is difficult to monitor those businesses who pay their employees on a cash basis. Some employees are afraid to report their employers. The town hall meetings conducted across the state is helping to rectify that and giving those employees the information as to how they can report anonymously. At present, Massachusetts is trying to organize a regional conference of the New England states, on this issue. This may take place either June or September of this year. Every state is different as to whether they will be able to participate in this conference. By sharing information state to state, it gives those employers who do not follow state statutes fewer places to "hide."

Through the investigator group and in conjunction with the Attorney General's office, those who are not properly documenting employees (back wages, etc.) would be penalized. The A.G.'s office, Occupational Safety, Worker's Compensation (everyone but the Department of Revenue which uses the 20 point test) would use the ABC test, which is a stricter law. Massachusetts' Attorney General is the first A.G. to be actively engaged in the independent contractor workplace fraud. Those who attend the weekly investigators' meeting, also have additional full-time positions within their individual department. There is not, at this time, due to the state budget deficit, to create new positions. However, in the next 1-2 years, the plan is to possibly hire attorneys to conduct the investigations and prosecute these cases; right now, attorneys are being utilized through the Attorney General's office and the various "share" agencies.

At present, there is a Worker's Compensation form that is signed by the independent contractors, which is subject to judicial interpretation should there be a questions regarding an employee.

Lianna Walsh, Director of Communications for the Massachusetts Department of Labor, discussed the co-sharing through sub-teams (there are 5), who are presently looking at ways to streamline informational sharing, through technology, legal, data retention. There is a referral line and website, where town hall-style meetings are publicized as a public service, with announcements, website, telephone. The PSA, through the Department of Revenue, is also extremely helpful. Director Powell noted that the I.T. section of her department is presently trying to write programs to facilitate sharing between the Workman's Compensation and the Unemployment Insurance systems.

The U.S. Department of Labor representative for the State of Massachusetts, George is quite interested in taking part in the regional conference. The U.S. Department of Labor is also planning on hiring an additional 250 investigators over the next couple of years to assist the states in this endeavor.

As for the statutory tests (ABC vs. 20 point), it would be nice to have one, standard test for employers to adhere to. In the case of Federal Express, who presently has many suits against them, the IRS definitions are utilized as a defense. Fed Ex considers themselves a "terminal service delivery" service.

Massachusetts Division of Revenue has put together a "Voluntary Disclosure" Program (as opposed to an "Amnesty Program"), which runs until the end of April. However, this program will not protect the employer from the IRS, and any information that is shared with Unemployment Insurance.

As for a "workable" definition of an independent contractor, the State of New York has one that works well. Massachusetts' definition is useful and is manageable. Those employers who would be defined in Massachusetts as "independent contractors" are realtors, plumbers, electricians, carpenters, anyone who come onto a job site and does the work. As for attorneys who work under another attorney, they would be determined as employees. Those attorneys, who do title work for another firm, would be considered an employee of that firm. They are considered an employee, unless they can prove to the contrary. This may also be determined by the nature of the agreement between the two parties working together, and the work to be performed.

Co-Chairs Maselli and Corvese thanked those who took time out of their busy schedules to testify today. The members review the Commission's "Mission Statement", and suggestions for revisions were offered.

**Special Joint Commission**  
**Underground Economy/Employee Misclassification**

**April 8, 2009**  
**Page 5**

With no further business to discuss, Chairman Corvese adjourned the meeting at 2:45 p.m. The next meeting of the Commission will be held on Wednesday, April 22, 2009, at 1:00 p.m., in the Senate Lounge.

Respectfully submitted,

Mary J. Black  
Commission Secretary

4/21/09  
Attachments



SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND  
ECONOMY AND EMPLOYEE MISCLASSIFICATION

Wednesday April 22, 2009

State House

Senate Lounge

In attendance were the following members:

Senator Christopher Maselli  
Senator David Bates  
Honorable George Healey  
George Nee  
Michael Lynch  
Matt Carey  
Paula Pellozzi  
David Palmisciano  
David Burnham  
Steven Labrie  
Terry Martisian

Absent were:

Representative Arthur Corvese  
Representative Douglas Gablinske  
Representative Brian Newberry  
David Sullivan

Chairman Maselli called the meeting to order at 1:10 PM. and welcomed the members and invited guests. Also in attendance was Dan Reilly, State Legislative Coordinator, from the International Brotherhood of Teamsters. Senator Maselli explained that at the previous meeting it was agreed by all to hear public testimony from the invited guests.

Public Testimony

Dan Reilly, International Brotherhood of Teamsters

Mr. Reilly gave an in depth presentation on clarification of misclassification of workers relating to illegal (and hidden) tax on our communities and presented several examples. He also provided examples of companies who are tied to misclassification and the action taken against these companies.

He explained and gave examples of what a misclassified employee loses. Stated that many states are reviewing the problems associated with misclassification and what states are doing throughout the country to address misclassification of workers. task force are being put in place, executive orders, and audits. Discusses QTEP a program designed by the IRS, the purpose of this program is to exchange information on employers and ensure compliance with tax codes.

This program has been instrumental in identifying (bad actors) companies that misclassify employees. In addition to these methods, investigations by Attorney General offices has taken place in several states i.e., California, Massachusetts and Ohio. Many states have introduced legislation on misclassification in 2009 and task forces have been implemented (see attached testimony).

**David White, Independent Insurance Agents of RI**

He testified that Workers Compensation Insurance rates in Rhode Island are double that of Massachusetts. (more information to follow)

**Cap Willey, RI Association of Certified Public Accountants**

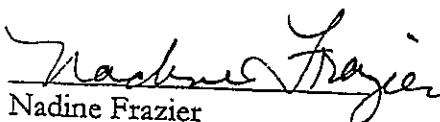
He testified that enforcement is a major issue with the misclassification of employees. (more information to follow)

In conclusion of this meeting, it was decided by all the members that at the next scheduled meeting there would be discussion of possible legislative recommendations to address the concerns of underground economy and employee misclassification. Senator Maselli thanks those who came before the committee to testify today.

Seeing there was no further business to come before this committee it was unanimously voted to adjourn at 2:27PM.

The next scheduled meeting has been set for May 6, 2009 at 1:00PM in the Senate Lounge.

Respectfully submitted,

  
Nadine Frazier

## MEETING MINUTES

### SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION

WEDNESDAY, MAY 6, 2009  
1:00 P.M. – SENATE LOUNGE – STATE HOUSE

PRESENT: Hon. A. Corvese, Hon. C. Maselli, Hon. D. Gablinske, Hon. D. Bates, T. Martiesian,  
M. Lynch, G. Nee, S. LaBrie

ABSENT: Hon. G. Healey, P. Pallozzi

Senator Maselli called the meeting to order at 1:15 p.m.

The minutes of the April 22<sup>nd</sup> meeting were accepted as written.

Matthew Capece, Representative of the General President of the United Brotherhood of Carpenters and Joiners of America, gave testimony. Mr. Capece has worked for over 20 years as a payroll fraud investigator, as well as in the policy arena, and is presently working on numerous pieces of state and federal legislation in employee misclassification and employee/employer fraud. (Please see the enclosed handout outlining the various states' legislations and/or executive orders regarding misclassification fraud.) Outlined in his handout/slide show were suggestions on how to counter misclassification/payroll fraud, cash/pay issues within the construction industry, labor subcontractors ("shell companies" – subcontractor entities which the primary contractors write their checks to and also may receive falsified workman's compensation certificates from.)

Mr. Capece also reported check cashing by the above "shell companies" who falsify (not file) monies "laundered", who then pay the workers in cash (see attached.) From personal observation (interviews/enforcement) insurance brokers who work the "fraud scheme" investigated the "personal injury" to find out who else is involved. He also discussed the lack of communication among state agencies and violators. The United States Treasury Office of the Inspector General issued a report and has brought the IRS to task in order to stop operating separately and to encourage them to work together and better coordinate their efforts. Mr. Capece also noted that in order to have proper prosecution and enforcement, more jail time for these conspiracies needs to be given. This type of fraud goes all the way up the contract chain; more severe jail time would result in better enforcement of the law.

Mr. Capece covered stop work orders/no WC insurance provided to employees and premium fraud (finding this prevalent in CT, FL, MA, NY and WA.) The State of Florida has the best legislative language and prevents fraud through intense investigation. An employer can appeal a "stop work" order. Also discussed were problems with undocumented workers.

He also noted that the "definition" or "ABC test" is recommended for adoption in Rhode Island. Approximately 25 other states have adopted this test for the past 50 years. The three-point test refers to whether one is assumed to be an employee, independent trade or business, or not performing same services that are performed by a client. If one passes all three of these factors, then they are classified as an independent contractor.

Mr. Capece also noted that, similar to Rhode Island's "piggyback system" of state and federal taxes, many of the 25 other states, such as Connecticut, still use the ABC test to define employee status, whereas the 20 factor test is usually used to define the independent contractor status. Of the 25 states that are using the ABC test and the UI statutes, the ABC test would only apply to determine if one is an employee or an independent contractor; there would be a separate definition for Workman's Compensation and/or the wage per hour issue. It is hard to coordinate an enforcement campaign to restrict contractor criminal fraud. Mostly all the states have similar ABC and 20 point testing; there are rare occasions where there is one definition for contractor, one for employee. There are also instances where independent contractors are required to have workman's compensation insurance – some states want to get away from the argument of who is an independent contractor and who is an employee – i.e. some in the construction industry do not have to have WC insurance (FL, CO, DE, TN.) There are some differences within the 25 states regarding the 3-way ABC testing, but most states are the same.

The failure to properly classify an employee or ways that others find ways to violate the law has been happening in the New England area (i.e. IL, CT, NJ, and MA.) The states of Maryland and Colorado presently have legislation on their Governors' desks to be signed into law on May 7<sup>th</sup>. Mr. Capece noted that misclassifying an employee or not classifying as an independent contractor are not violations of the law; however, not paying taxes or Workman's Compensation Insurance are violations.

Mr. Capece offered the members a recommendation regarding enforcement of insurance laws. In the state of Florida if there is a violation of insurance laws (i.e. worker's compensation premium fraud), if there is a criminal action, there is forfeiture/penalty, which is placed into a dedicated fund. This fund assists the agencies in enforcement costs.

Certificates of insurance were discussed. The contractor provides notation of number of workers in order to be assured of paying the proper insurance premium; this is listed on the insurance premium page (similar to an auto or life insurance premium page) and should be disclosed to any investigative enforcers. Washing State has a workman's compensation website where employers can list the number of their employees, so that there is verification of coverage for each employee. Mr. Capece reported that, a study was conducted at the University of California-Berkeley, regarding Workman's Compensation fraud. They found over \$100 billion per year in monies lost to fraud – mostly by those within the following industries: landscaping and roofing.

Regarding the states that have passed taking away the extension for single employers in the construction industry, the question was raised as to whether there was any backup on how much additional money is funded back into the system? Within the construction industry in the State of Florida, they found that 30% of these single employers were not paying into the Workman's Compensation Insurance resulting in lower medical benefits, etc. The Florida study also revealed that there were more than 50% of the dollars that should have been going into the Workman's Compensation system than actually should have been for those who were employed. The insurers were fleeing the state.

A discussion ensued regarding the ABC test vs. the 20-point test, and that the goal should be to have all of the agencies utilize the identical test. The ABC test weighs more toward an employee; however, this test is not ideal for tax purposes. All agreed that a universal test is needed to stop the independent contractors from being misclassified. It was noted that the ABC test can be too strict and is an issue in the State of Massachusetts. It was also noted that there are currently barriers in trading between divisions (problem in taxation – see Chairman Stephen Costantino’s recent legislation.) There is a need for the DLT (Division of Labor and Training), the Division of Taxation and the Attorney General’s office to meet privately to discuss this. This meeting would not be open to the public, due to privacy reasons.

Also discussed was the need for uniformity in enforcement, publicity and training within the Workman’s Compensation Insurance. The Rhode Island General Assembly has recently passed strong laws pertaining to Workman’s Compensation fraud.

Representative Gablinske referred those in attendance to please peruse his handout pertaining to the Massachusetts Bid for Real Estate Appraisers from K&L Gates (see attached.)

Representative Corvese thanked those present for their testimony and asked the members of the Commission to peruse the information provided to them. He asked all members to come to the next meeting (in two weeks – May 20th) with their suggestions, and to be prepared to vote on a “statute definition”(in four weeks – June 3rd.)

With no further business to discuss, Representative Corvese adjourned the meeting at 2:25 p.m. The next meeting of the Commission will take place on Wednesday, May 20, 2009, at 1:00 p.m., in the Senate Lounge, at the State House.

Respectfully submitted,

Mary J. Black  
Commission Secretary

mjb  
5/19/09  
Attachments

SPECIAL JOINT COMMISSION TO STUDY THE  
UNDERGROUND ECONOMY AND EMPLOYEE  
MISCLASSIFICATION

A meeting of the "Special Joint Commission to Study the Underground Economy and Employment Misclassification" was held on Wednesday May 20, 2009 at 1:00 PM in the Room 310 at the State House.

In attendance were the following members:

Senator Christopher Maselli  
Representative Arthur Corvese  
Representative Douglas Gablinske  
Steven Labrie  
George Nee  
Michael Lynch  
David Sullivan  
Paula Pellozzi  
Terry Martisian  
David Palmisciano the

Absent were:

Senator David Bates  
Honorable George Healey  
Representative Brian Newberry  
Matt Carey  
David Burnham

Co-Chairs Maselli and Corvese opened the meeting at 1:15PM and welcomed those in attendance. Co-Chairman Corvese explained that the minutes of the previous meeting were in a "*rough draft stage*" and the "*final version*" would be forwarded to the members by mail.

Co-Chairs Maselli and Corvese presented the membership with a rough draft of the proposed legislation for review by the members. All members looked at the proposed legislation together with the Co-Chairs and Legal Council and answered any questions that were submitted to the committee.

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After reviewing the proposed legislation, it was suggested by Chairman Corvese that any committee member who would like to make a recommendation for the proposed legislation contact the Senate Policy Office on or before Friday May 26, 2009 by 5PM.

This would allow the legal counsel time to properly revise and prepare a new document for reviewing at the next meeting. All members present were in complete agreement.

Seeing there was no further business to come before this committee it was unanimously voted to

Adjourn: 1:55 P.M.

The next meeting is scheduled for Wednesday June 10, 2009 at 1:00PM in the Senate Lounge.

Respectfully submitted,

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Nadine Frazier  
Secretary

## MEETING MINUTES

### SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION

WEDNESDAY, JUNE 10, 2009  
2:00 P.M. – SENTATE LOUNGE – STATE HOUSE

PRESENT: Hon. A. Corvese, Hon. D. Bates, Hon. B. C. Newberry, Hon. D. Gablinske,  
Hon. B. Morin, S. LaBrie, D. Sullivan, M. Carey, M. Lynch, P. Pallozzi,  
D. Palmisciano, T. Martiesian, D. Burnham

ABSENT: Hon. C. Maselli, G. Nee

Chairman Corvese welcomed the members and began the meeting at 2:15 p.m. At this time, he asked the members to voice any comments or concerns regarding the draft of the employee misclassification final report.

Questions were raised regarding Section 42-161-51, within the draft legislation, Registration of Independent Contractors (see attached.) The draft reflects a change those who employ an independent contractor would now be required to register. Currently, if one is an independent contractor and is working for the "X, Y, Z Company", that person would be required to register three times for each company that they are working for. Under the language in the draft, if an employer is required to register three times, a concern was noted regarding the \$100 charge required for each registration, and what would be the appropriate way to deal with it. The comfort level with requirement of the employee entity to register was discussed. Clarification of this section and how the \$100 registration fee applies was questioned and discussed; could become very costly to the independent contractor.

In addition, the subject of an employer of an independent contractor withholding 20% of the net contract proceeds was questioned. This 20% net contract proceed does not define what "net contract proceeds" are; and this percentage seems slightly high. For example, if one was an individual, the highest marginal tax rate would be 9.9%; for a corporation, the highest tax rate would be 9%, and that is on the net income. Currently, there is a mechanism in place for non-resident construction contractors where the general contractor does not have to pay the person 3% of the entire contract, until that sub-contractor, independent contractor or non-resident contractor gets a certificate of clearance from the Taxation. The Department of Revenue presently has a problem with this set-up, and is willing to testify as such. The Department of Revenue would feel consistent with going with the 3%; however, in doing that, then the general contractor would be made responsible for the withholding.

In addition, the Department of Revenue would like to see this section of the proposed legislation expanded; if the correct amount is not withheld, regardless of the percentage, the person who is responsible for withholding the tax, then Revenue has the right to go after the entity that was supposed to withhold. Questions would then arise as to whether that person would be responsible and how would it apply? Would it be credited to him, who is withholding, or would it be credited to the individual at an estimated payment? If the general contractor has several sub-contractors, then it can become very confusing, and if he were making payment on behalf of all of them, this would pose a heavy administrative burden on that contractor. In the situation of larger companies who utilize 20 or 30 sub-contractors, then it would result in a tremendous burden on those general contractors to withhold those monies and remit them to the Division of Taxation. It would almost be easier to treat them (the sub-contractors) as employees. Clarification of intent of the legislation was also requested.



Chairman Corvese noted that the draft recently submitted would be subject to numerous changes, and is just the beginning of further discussion and interpretation. Much of the drafted legislation will be sifted through and tossed as deliberations go along.

The procedure for the issuance of local licenses issued to independent contractors (located on page 9 of the drafted legislation) was discussed. Currently the Department of Business Regulation does not enforce the Workman's Compensation statutes; they utilize a national database. The department does not require the state to provide proof of WC insurance before issuing licenses, but are subject to the discretion of the department director. Department of Labor and Training notifies Department of Business Regulation. The two steps of licensure application was also discussed; step 1 – filing with the Department of Labor and Training as an independent contractor, step 2 – filing with the Division of Taxation for a Certificate of Registration, with the registration fee being paid at Taxation, not DLT, resulting in a dual-filing, with only one fee.

It was noted that over 100,000 licenses are issued on a yearly basis, and, as it stands now, should an independent contractor apply for a license having no WC coverage, then the application is deferred to the State Licensing Board for review (see Page 10 of the attached drafted legislation.)

Though most of the Commission's focus during these meetings pertained largely to the construction field, a concern was raised as to how this proposed legislation would affect other forms of (professional) businesses, i.e. architectural, engineering and design firms. Some of these firms may have their own internal policies and workman's compensation insurances, yet requiring these firms to withhold the 20% fee from them would be abhorrent. Most of these types of companies consider themselves as independent contractors, having their own insurance and employees. It was recommended to find a way to separate these entities from the contracting industry.

The need to educate and implement policies and procedures regarding insurance requirements was addressed (i.e. DBR, rate taking, premium determinations, etc.) The importance for a need for advance notice to those companies in question was stressed. In addition, the question was raised as to how soon did the Commission estimate an implementation date could take place? The redundancy of having to file with both the Department of Revenue and the Department of Labor was raised as a concern, also. The present shortfall of bodies in state government to accommodate the extra workload in processing these applications was also noted.

Questions were raised relating to Sub-Section C, Section 28-29-72.2, on page 6 of the first draft of the proposed legislation, regarding "anyone failing to treat a person as an employee, according to this chapter, shall be subject to sanctions and penalties, as provided in Section 20-33-17.2." It was noted that this law seemed too broad and ambiguous and needed to be fine-tune where it refers to "anyone." Chairman Corvese recommended that those who agreed with this observation were welcomed to propose language to Legal Counsel for inclusion in the new proposed legislation for the purpose of clarification. There was some agreement on the observation under registration of independent contractors in terms of both the "hiring" and the "entities hired" and the need for better clarification, which would help alleviate future litigation as to one who files a form and one who doesn't.

Department of Labor and Training noted that their department has a new computer system with database and imaging system up and running and ready to go and the department would have no problem in accepting the filings. It was the department's recommendation to narrow down the filing of insurance

applications to one filing, and noted that this would make it easier to share information with the Division of Taxation and other state agencies. The DLT also echoed DBR's previous observations. It was noted that the section in the proposed drafted legislation regarding the filing of insurance forms with the tax administrator, was in the section of the statute that falls under the Department of Labor of Training and the functions of the Director. Clarification or revision in this statute was recommended.

The Workman's Compensation Court had noted that there was nothing in the proposed legislation that would adversely impact on the Court's ability to operate as in the past. It was also recognized by the Court that there might be some disputes among the various state agencies as to who would bear the responsibility of accepting certain documentation as necessary. The WC COURT warranted no modifications of the proposed legislation at this time.

Division of Taxation agreed with points made by the Department of Business Regulation as to any license holding or renewal. There was no objection by this department with regards to having the registrations be kept in the Department of Labor and Training, rather than Taxation. Taxation also agreed that clarification was needed as to the number of times needed to file once, annually, or for every single job or independent contractor one hires, is definitely is an issue and needs clarification. The \$100 fee also needs clarification. In addition, Taxation questioned the 20% holding – finding it too high – as well as the “net” contract proceeds not being clearly defined, needs to be looked at again. It was noted that if it was the “gross” contract, it puts the burden on the company that hires the independent contractor, and the professional services was also an issue. This would drag in every independent contractor and not just in the construction industry. As for the implementation of the proposed legislation, Taxation recommends a starting date of January 1<sup>st</sup>. Most members were in agreement of an implementation date of January 1, 2011. This would keep an independent contractor from having to be switched mid-year and listed as an employee, which would make it complicated for both the businesses and the individuals involved.

A concern was raised as to the need for the Commission to focus on the penalties and enforcement – who will be responsible for “going after” those who are not following statute.

The IRS definition on Page 6, Section 29-29-17.2, it was noted that there is a history with the IRS as to the rule of who is an independent contractor and who is not. There was an issue with the phrasing (i.e. “services performed, either outside the usual course of the business for the which the services are performed, etc.”), and could drag everyone in as an “employee.” In addition, on Page 12, line 21 the phrase stating, “any employer or an independent contractor” was questioned. The proper term should be “hiring entity” or a “hire”, which would better define an employer/employee relationship. It was recommended to use the word “retained” rather than “hire”, or rather than “employer.” “Contract services” was also recommended as wording used instead of “employer.”

An additional concern was raised as to clarification of the definition of “hiring entity”, as some independent contractors also hire specialty trade workers – and the confusion on interpretation, which can be derived from that. It was explained by legal counsel that the draft lists the definition of “a person hired as an independent contractor” performs the same skills for other people that the general contractor is hiring him for. For example, if one hires someone to build a computer network, and that person performs the same work for other companies as well, then they are performing a service that you are hiring them for as a trade of business to other people. This strengthens the one “hired” as an “independent contractor” by saying that they do this work for the general contractor, but that they also do the same work for the “X, Y, Z companies, as well.

**Special Joint Commission to Study the  
Underground Economy and Employee Misclassification**

**June 10, 2009  
Page 4**

All of the commission members present thanked the Policy Office for their excellent work on the report presented. Chairman Corvese thanked everyone for their attendance, and asked for those who had concerns regarding the draft legislation to please submit their concerns in writing to the Senate Policy Office prior to the next meeting.

With no further business to discuss, Chairman Corvese adjourned the meeting at 3:30 p.m. Next meeting will take place on Wednesday, June 24, 2009, at 1:00 p.m., in the Senate Lounge.

Respectfully submitted,

Mary J. Black  
Commission Secretary

mjb  
6/22/09

**SPECIAL JOINT COMMISSION TO STUDY THE UNDERGROUND  
ECONOMY AND EMPLOYEE MISCLASSIFICATION**

*A meeting of the "Special Joint Commission to Study the Underground Economy and Employment Misclassification" was held on Wednesday June 24, 2009 at 9:00 AM in the Senate Lounge.*

*The following members were in attendance:*

*Senator Christopher Maselli  
Senator David Bates  
Representative Arthur Corvese  
Representative Brian Newberry  
Representative Douglas Gablinske  
Steven Labrie  
George Nee  
Michael Lynch  
Terry Martisian  
David Burnham  
David Sullivan  
Director Marquese, DBR*

*Absent were:*

*Honorable George Healey  
David Palmisicano  
Matt Carey*

*Co-Chairs Maselli and Corvese opened the meeting at 9:15 AM and thanked all for attending. Members were all distributed a copy of the final report together with a copy of the proposed legislation for their review. A discussion then took place among the members and co-chairs. Some members proposed serious questions regarding the definition of the term "employee" on page 10, with ABC 3 tiered licensing test, and of a one hundred (\$100.00) dollar filing fee for an independent contractor - to be paid to Department on Labor & Training. After a lengthy discussion there was a compromise to amend the report, which addressed all those concerns. All members were in complete agreement of the proposed changes.*

*On a roll call vote upon motion by Co-Chair Corvese and seconded by Senator Maselli, it was unanimously voted for the adoption of the amended final report. Co-Chairman Corvese stated that all the changes proposed would now be reflected in the new proposed legislation.*

*Co-Chairs Maselli and Corvese stated that the report would extend this existing commission to become a permanent commission.*

*Co-Chairs Corvese and Maselli thanked all who participated in this commission and named each of the members.*

*Seeing there was no further business to come before this commission it was unanimously voted to adjourn.*

*Adjourned 10:45 AM.*

*Respectfully submitted,*

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*Nadine Frazier  
Secretary*

# Workers Compensation Court Staff Analysis on the Estimated Costs of Employee Misclassification (FY 2008 Wage and Employment Data)

## □ At 1% of total Employment

Private Employment	Employers	Employees	Wages	Avg. Wage
Total P.E	35,297	417,706	\$16,178,446,118	\$ 38,732
Construction	<u>4,335</u>	<u>22,803</u>	<u>\$ 1,064,172,845</u>	\$ 46,668
Total non-construction	30,962	394,903	15,114,273,273	\$ 38,273

### Total non-construction

Misclassification %	<u>1%</u>	<u>3,949</u>	<u>\$ 151,142,733</u>
	5%	19,745	\$ 755,713,664

### Construction

Misclassification %	<u>1%</u>	<u>228</u>	<u>\$ 10,641,728</u>
	5%	1,140	\$ 53,208,642

### Grand Totals

Misclassification %	<u>1%</u>	<u>4,177</u>	<u>\$ 161,784,461</u>
	5%	20,885	\$ 808,922,306

	<u>RI Income Tax</u> 3.75%	<u>UI</u> 2.57%	<u>TDI</u> 1.50%	<u>Comp</u> \$ 4.00	<u>RI Total</u>
<u>Non-construction:</u>	\$ 6,492,252	\$ 1,826,821	\$ 2,267,141	\$ 604,571	\$ 11,190,785
<u>Construction:</u>	<u>\$ 508,881</u>	<u>105,487</u>	<u>159,626</u>	<u>42,567</u>	<u>\$ 816,561</u>
	\$ 7,001,133	\$ 1,932,308	\$ 2,426,767	\$ 647,138	<u>\$ 12,007,346</u>

	<u>Social Security</u> 15%	<u>Fed Income Tax</u> 18%	<u>FED Total</u>
<u>Total non-construction:</u>	\$ 22,671,410	\$ 27,205,692	\$ 49,877,102
<u>Construction:</u>	<u>\$ 1,596,259</u>	<u>\$ 1,915,511</u>	<u>\$ 3,511,770</u>
	\$ 24,267,669	\$ 29,121,203	<u>\$ 53,388,872</u>

<u>Grand Total RI &amp; FED</u>	<u>\$ 65,396,218</u>		
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☐ At 6.1 % of total Employment (Based on Ten-State Average Rate)

Private Employment	Employers	Employees	Wages	Avg. Wage
Total P.E	35,297	417,706	\$ 16,178,446,118	\$ 38,732
Construction	4,335	22,803	\$ 1,064,172,845	\$ 46,668
Total non-construction	30,962	394,903	15,114,273,273	\$ 38,273

**Total non-construction**

Misclassification %	1%	3,949	\$ 151,142,733
	5%	19,745	\$ 755,713,664
	6.1%	24,089	\$ 921,970,670

**Construction**

Misclassification %	1%	228	\$ 10,641,728
	5%	1,140	\$ 53,208,642
	9%	2,107	\$ 98,329,571

**Grand Totals**

Misclassification %	1%	4,177	\$ 161,784,461
	6.3%	26,196	\$ 1,020,300,241

	<u>RI Income Tax</u> 3.75%	<u>UI</u> 2.57%	<u>TDI</u> 1.50%	<u>Comp</u> \$ 10.00	<u>RI Total</u>
<b>Total non-construction:</b>	\$ 39,602,735	\$ 1,420,861	\$ 2,267,141	\$1,511,427	\$ 44,802,164
<b>Construction:</b>	\$ 4,702,064	82,045	159,626	106,417	\$ 5,050,153
	\$ 44,304,799	\$ 1,502,906	\$ 2,426,767	\$1,617,845	\$ 49,852,317

	<u>Social Security</u> 15%	<u>Fed Income Tax</u> 18%	<u>FED Total</u>
<b>Total non-construction:</b>	\$ 138,295,600	\$ 165,954,721	\$304,250,321
<b>Construction:</b>	\$ 14,749,436	\$ 17,699,323	\$ 32,448,758
	\$ 153,045,036	\$ 183,654,043	\$336,699,079

<b>Grand Total RI &amp; FED</b>	\$386,551,396		
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## Percentage of Employee Misclassification (General)

General Rate			
State	Total Number of Employees	Number of Misclassified Employees	Percentage of Misclassified Employees
California <sup>1</sup>	16,672,244	1,983,997	11.9%
Colorado <sup>1</sup>	2,033,235	172,825	8.5%
Connecticut <sup>1</sup>	1,710,698	90,667	5.3%
Illinois <sup>2</sup>	4,915,800	368,685	7.5%
Maryland <sup>1</sup>	2,679,250	160,755	6.0%
Massachusetts <sup>3</sup>	2,793,889	125,725	4.5%
New Jersey <sup>1</sup>	3,629,865	323,058	8.9%
New York <sup>4</sup>	6,842,573	704,785	10.3%
Rhode Island <sup>5</sup>	417,000	4,177	1.0%
Washington <sup>1</sup>	2,460,188	78,726	3.2%
Wisconsin <sup>1</sup>	2,548,484	158,006	6.2%
<b>Weighted Average (excluding Rhode Island):</b>			<b>9.0%</b>

<sup>1</sup> "Planometrics Chart." Collected from State Employment, UI, and UI Tax Audit Data.

<sup>2</sup> Kelsay, Michael, James Sturgeon, and Kelly Pinkham. The Economic Costs of Employee Misclassification in the State of Illinois. Economics, University of Missouri- Kansas City. 6 Dec. 2006. 4 Aug. 2008 <[http://www.lecetchicagoarea.org/pdfs/illinois\\_misclassification\\_study.pdf](http://www.lecetchicagoarea.org/pdfs/illinois_misclassification_study.pdf)>. Report based on data averages from 2001-2005, provided by the Illinois Dept. of Employment Security.

<sup>3</sup> Bernard, Elaine, and Robert Herrick. The Social and Economic Costs of Employee Misclassification in Construction. Construction Policy Research Center, Harvard Law School and Harvard School of Public Health. MA, 2004. 1-28. 17 Dec. 2004. Harvard Law School. 4 Aug. 2008 <<http://www.law.harvard.edu/programs/lwp/misclassification%20report%20mass.pdf>>. The data for this report was collected from "Planometrics, 2000".

<sup>4</sup> 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).

<sup>5</sup> Employment Numbers are based on data from the "Statistical & Fiscal Digest 2007" (report by the Rhode Island Department of Labor & Training). 1% employee misclassification is not based on empirical data, but solely a conservative estimate for discussion basis.