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# Confronting Misclassification and Payroll Fraud:

## A Survey of State Labor Standards Enforcement Agencies

By Mark Erlich and Terri Gerstein – June 2019



**HARVARD LAW SCHOOL**  
Labor and Worklife Program

# TABLE OF CONTENTS

EXECUTIVE SUMMARY.....	3
INTRODUCTION.....	7
LEGAL CONTEXT.....	8
ENFORCEMENT PRACTICES.....	11
TASK FORCES.....	14
ADMINISTRATIVE ISSUES.....	18
OUTREACH AND USE OF THE MEDIA.....	20
MEASURING RESULTS AND ENSURING FUTURE COMPLIANCE.....	23
GIG ECONOMY.....	27
CONCLUSION.....	29
NOTES.....	28

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617MediaGroup for layout and design of this report

# EXECUTIVE SUMMARY

## THE IDEA FOR THIS REPORT

stemmed from an annual meeting of the Interstate Labor Standards Association (ILSA), an organization of state labor departments and other agencies that enforce labor standards. The idea was to question labor standards agencies about their approach to misclassification and understand more broadly what has been done in this area. The report details the results of a written survey of agencies in twenty-seven states and follow-up interviews with representatives from nine states. The purpose is to help state labor standards agencies learn what is being done in other states; to establish some baseline practices that states should adopt, based on respondents' assessments; and to share innovative approaches that should be considered more broadly.

The report summarizes officials' reflections on various aspects of payroll fraud and misclassification enforcement, including most notably the legal framework and enforcement practices.

## Legal context:

- A number of states have adopted the streamlined "ABC test" for one or more laws in determining employee status, while the majority use a variety of tests for the relevant laws (wage and hour, workers' compensation, unemployment insurance). Survey respondents and interviewees identified the varied tests as a source of confusion, while states with the ABC test reported that it was workable and effective.
- In addition, some states have laws specifically treating misclassification as a stand-alone violation of the law, which they found useful; other states lack such provisions.
- Many states have sought ways to enforce the law not only in situations where workers are treated as independent contractors, but also in the increasingly more common situations where workers are paid cash wages "off the books."

## Enforcement practices:

- Most survey respondents reported that they use a combination of proactive and complaint-based (or reactive) enforcement approaches, and interviewees noted the value and impact of a more proactive and strategic approach, including on-site investigations (as opposed to only "desk audits") and use of stop work orders where available.
- A number of states have established task forces to monitor and address misclassification and payroll fraud. They reported that these allow them to address the problem in a more effective and comprehensive manner; however, the extent of operational integration of the various divisions and agencies varies by state.
- Finally, states that collaborated extensively with stakeholders, including unions, community-based organizations, high-road employer associations, and worker centers reported that these collaborations enabled them to be more effective.

The report also notes some areas where further work is needed, including the development of metrics and methods for measuring impact and effectiveness of enforcement efforts. Finally, the report contains recommendations for states wishing to improve their enforcement in this area, including more workable (while still protective) legal standards, establishment of active and ongoing multi-agency task forces, adopting a proactive and strategic approach to enforcement, and creating an effective metric for assessing impact.

# INTRODUCTION

**IN RECENT DECADES,** there has been a sharp increase in employers misclassifying workers as independent contractors when they should be treated as employees.<sup>1</sup> Misclassification is often an effort to reduce labor costs and evade workplace laws, virtually all of which only cover employees. In addition, many employers, particularly in industries like construction, pay workers cash wages “off the books.” This, too, is a method of avoiding employers’ legal obligations, including minimum wage, overtime, prevailing wage, workers’ compensation premiums, unemployment insurance contributions, and employer FICA taxes.

Misclassification and payroll fraud harm workers, depriving them of rights and protections to which they are legally entitled. Law-abiding businesses also suffer, as they struggle to compete with companies that unlawfully lower their costs. And public coffers suffer when employers fail to obtain workers’ compensation insurance, pay unemployment insurance contributions, or pay their share of payroll taxes.<sup>2</sup>

Because of the significant harm resulting from such practices, government agencies have made targeted and sustained efforts to address misclassification and payroll fraud. During the Obama administration, the Wage and Hour Division (WHD) of the United States Department of Labor (USDOL) escalated enforcement programs at the federal level and ultimately signed Memoranda of Understanding with twenty-seven states in order to collaborate in combating misclassification.<sup>3</sup>

In the past two years, however, the USDOL has been rolling back worker protections in a variety of ways, initially withdrawing a WHD Administrative Interpretation on misclassification, and piloting an amnesty program for wage and hour violators, called the PAID program.<sup>4</sup> As a result of this retreat at the federal level, state enforcement has become more critical than ever.

The gulf between federal and state policies continues to widen. On April 16, 2019, the general counsel of the National Labor Relations Board drafted a memorandum determining that Uber drivers were independent contractors rather than employees.<sup>5</sup> Two weeks later, in response to a request from an unidentified virtual marketplace company, the US Department of Labor issued an opinion letter on April 29, 2019 concluding that the workforce of a firm that operates in the ‘on-demand’ or ‘sharing’ economy should be considered independent contractors, not employees.<sup>6</sup> Yet in the same month, three states launched new initiatives to crack down on misclassification as Michigan’s Attorney General Dana Nessel established a new Payroll Fraud Enforcement Unit,<sup>7</sup> Wisconsin’s Governor Tony Evers signed an executive order to form a Joint Enforcement Task Force on Employee Misclassification,<sup>8</sup> and Montana’s Governor Steve Bullock issued an executive order to create a Task Force on Integrity in Wage Reporting and Employee Classification.<sup>9</sup>

***“Misclassification and payroll fraud harm workers, depriving them of rights and protections to which they are legally entitled. Law-abiding businesses also suffer, as they struggle to compete with companies that unlawfully lower their costs”***

In fact, states have been involved in combatting misclassification and payroll fraud for many years. The first statewide inter-agency task force on misclassification was created in New York in 2007.<sup>10</sup> Indeed, some of the worst consequences of misclassification – failure to pay unemployment insurance contributions and to procure workers’ compensation insurance – have the greatest impact on the state level, where those programs are administered. Over the past two decades, many states have taken considerable measures to root out and stop misclassification and payroll fraud.

In an effort to understand the variety of approaches, as well as states’ own assessments of what has been most effective, we conducted the research contained in this report in two stages: (1) a written survey of agencies from 27 states, generally labor standards enforcement agencies; and (2) in-depth follow-up interviews with agencies in 9 states. The vast majority of input came from state departments of labor, and not from agencies administering unemployment insurance benefits or enforcing workers’ compensation laws; given the nature of misclassification and payroll fraud, those agencies would likely have additional and perhaps distinctive insight.

This report contains the findings resulting from our survey and interviews. Our goal in sharing this information is threefold: (1) to help state labor standards officials gain awareness of what has been done by their counterparts elsewhere; (2) to establish some baseline practices that all states should be doing, based on officials’ assessment of their impact; and (3) to share innovative approaches that should be considered more broadly. We also identify several unanswered questions and missing pieces that are areas in need of further discussion and development.

## LEGAL CONTEXT

Enforcing the laws related to misclassification and payroll fraud involves a variety of legal issues. A full discussion of all the legal considerations is beyond the scope of this report. However, it is useful to have an overview of some of the key aspects of the misclassification laws, as well as the perspectives of agency officials as to what aspects of their state laws and powers are particularly useful or challenging.

### Definition of employee

Virtually all workplace laws cover “employees” and exclude “independent contractors.” As a result, a precondition of investigating and enforcing workplace laws includes the determination of employee status. Many of the states interviewed have statutory schemes that incorporate different tests for the various laws involved, including the wage and hour, unemployment insurance, workers’ compensation, and tax laws, for example. These tests tend to examine similar and overlapping factors, such as the extent of control exerted by the putative employer, the duration of the relationship, and whether the worker has investment in the business and the opportunity for profit and loss. On the federal level, the Internal Revenue Service, for example, examines 20 factors<sup>11</sup> and the Fair Labor Standards Act has a number of factors.<sup>12</sup> The tests under various state laws also examine a multitude of factors, and while they sound somewhat alike—and may well be difficult for a layperson to tell apart — they are not exactly the same. Several states reported that this multitude of tests presents a challenge: it makes it harder to enforce the law; creates inefficiencies in that one state agency cannot take action based upon the employee status determination of another; and makes it more difficult for companies to understand their compliance obligations and for workers to understand their rights.

Gerhard Taebel (OR) noted that even after making a determination, his agency refers cases to other agencies “to see whether they would want to take up a case based on their definitions.” Rhonda Gerharz (AK) observed that employers are “responsible for trying to sort out each and every aspect between federal, state and local government compliance requirements, which makes it hard for the ones who really want to do it right as opposed to those who deliberately misclassify to save money and underbid competitors.” Maura McCann (NY) argued that “a simpler test, or single test, could help the regulated community understand a bit better” and that a bright line rule would be helpful: “What’s easier to enforce?...theoretically, the simpler it is, the easier to enforce.” Brent DeBeaumont (WA) similarly noted that the variety of tests is “confusing for employers and employees alike.”

A number of states have adopted the more streamlined and clear “ABC test” either broadly or in a limited fashion. Under this test, the default assumption is that workers are employees unless certain conditions are satisfied. Specifically, an employer who wants to treat someone as an independent contractor rather than an employee has to show that the work:

- is done without the direction and control of the employer; and
- is performed outside the usual course of the employer’s business; and
- is done by someone who has their own, independent business or trade doing that kind of work.

Massachusetts adopted this test by statute in 2004, and New Jersey’s Supreme Court adopted the test for wage and hour laws in 2015; it was already codified in the unemployment insurance statute.<sup>13</sup> In 2018, California’s Supreme Court mandated use of the ABC test in *Dynamex Operations W v. Superior Court*. Dynamex, a package and document delivery company, was sued by two drivers on the grounds that the company had misclassified them

as independent contractors.<sup>14</sup> Prior to 2004, the company had treated drivers as employees and the subsequent nature of the work was unchanged. Business groups, particularly from the gig economy, are currently engaging in extensive lobbying attempts to unravel the Dynamex decision legislatively. However, on May 29, 2019, the California State Assembly passed AB5, a bill that would codify the ABC test and the Dynamex decision in the state's statutes. The bill awaits action by the Senate and the Governor. Other states have partially adopted the ABC test; for example, New York has largely incorporated the ABC test for two industries: construction and the commercial goods transportation industry.<sup>15</sup>

The terrain is constantly changing. In 2017, the Alaska legislature approved a transportation network company carve-out bill, one of many that have been introduced and passed in state legislatures around the country. The statute exempted Uber drivers from state employment laws, thereby resolving a 2015 dispute between Uber and the Alaska Department of Labor and Workforce Development in Uber's favor. For example, in 2018 the Alaska legislature passed HB79, a bill that clarified the definition of an independent contractor for the purposes of workers compensation insurance with a stringent seven factor test and mandated that corporate officers and limited liability company members needed to have a minimum of a 10% ownership interest in order not to be considered an employee.<sup>16</sup>

## Designation of misclassification as a stand-alone violation of the law

In many states, there is no express prohibition on misclassification, but the issue arises through the enforcement and case law development under wage and hour, unemployment, and other laws. In these jurisdictions, for example, misclassifying workers and failing to pay unemployment insurance contributions as a result would constitute a violation of only the unemployment insurance laws.

However, in a number of jurisdictions, misclassification itself is mentioned by name in statutes and is prohibited, with penalties or other consequences. For example, the workers' compensation law in Alaska creates both civil and criminal liability for misclassifying a worker.<sup>17</sup> The California labor code also explicitly prohibits willful misclassification,<sup>18</sup> and Maine law imposes penalties of between \$2,000 and \$10,000 for intentionally or knowingly misclassifying a worker as an independent contractor regardless of whether there are attendant minimum wage or other labor standards violations.<sup>19</sup>

***A representative from the Massachusetts Attorney General's office noted that under the Massachusetts ABC test workers are presumed to be employees and the putative employer has the burden of proving all three ABC factors are met... This is critically important because most workplace protections, including minimum wage, overtime, worker's compensation and anti-discrimination laws, are based on employee status.***

Seventeen of the states surveyed reported that their states had laws specifically addressing and/or establishing penalties for misclassification.

## Criminal enforcement

Only a handful of states reported that there had been criminal prosecution of the various violations resulting from misclassification. Criminal prosecutions that occur are typically handled either by state attorneys general or the local prosecutor (county or district attorney). California Labor Secretary Julie Su reported a district attorney prosecution of a case "in which the misclassification was egregious and rampant."

A number of survey respondents did not have information needed to report whether criminal prosecutions had occurred in their jurisdiction. One state official (Charles Ziegert of WA) reported that talks were ongoing in his agency regarding establishing a method for referring cases for criminal prosecution.

## **Misclassified independent contractors versus “off the books” workers in the cash economy**

Bringing criminal charges based solely on misclassification as independent contractors may be difficult in some cases, depending on the facts, given the high burden of proof in criminal cases (beyond a reasonable doubt) as well as the difficulty of proving the requisite intent.

However, when employers compensate their workers off the books entirely, this situation can give rise to a host of criminal charges, including violations related to the nonpayment of wages (depending on the jurisdiction, these may include wage theft, theft by swindle, larceny, scheme to defraud, theft of services, or other charges) as well as charges related to false documents created when workers are compensated off the books (filing a false document, maintaining false business records) and charges related to workers' compensation or unemployment insurance obligations specifically.

## **Joint employment and individual liability**

Imposing liability “up the chain” is particularly important for effectively addressing misclassification. Brent DeBeaumont (WA), an unemployment insurance official, noted that his agency cites both employers where there are more than one. A New Jersey wage and hour official noted that the state’s prevailing wage law creates joint liability for upper level and lower-tier subcontractors, and said that this would be helpful as well in the private sector: “We would like to be able to work our way up to the general contractor, the person who is responsible for actually hiring these subs.”

Several jurisdictions have laws that create liability for higher-level entities when their subcontractors commit violations, including California’s client employer law<sup>20</sup> (which has already been used to hold a national restaurant chain jointly liable for wage violations with a janitorial contractor)<sup>21</sup> and statutes in the District of Columbia.<sup>22</sup> If adopted more broadly, this type of statute could play a significant role in reducing misclassification and other workplace violations.

Various states allow a finding of individual, and not just corporate, liability provided that requisite facts are present. An official from a southern state observed that individual liability was his biggest stick, especially when an employer could evade corporate liability by declaring bankruptcy and reincorporating the next day.

## **Availability of private right of action**

Most states allow private litigants to bring wage and hour cases directly in court. However, typically there are not methods for a private litigant to file a lawsuit against a company for failure to comply with workers' compensation or unemployment insurance laws.

# ENFORCEMENT PRACTICES

## ENFORCEMENT PRACTICES

In the conventional practice of labor standards enforcement in recent years, worker complaints have typically served as the primary trigger for federal and state agency activity. Over time, the treatment of wage violations has been affected by the larger political dynamics of the systematic reduction of resources in the public sector.<sup>23</sup>

Over the past several decades, the conventional practice in federal and state labor standard enforcement agencies has generally been complaint-based enforcement: a worker complains, and the agency investigates that individual's employer, either from the office or through a field inspection. This complaint-based approach was largely, but not wholly, fueled by resource constraints. However, over the last decade, a discussion among leaders in government, unions, worker advocacy organizations, and academic researchers has challenged long-held assumptions about whether that complaint-based approach is the most effective vehicle to address the chronic and growing problem of labor law violations in US workplaces. Studies have demonstrated an imperfect overlap between sectors that are the sources of most complaints and sectors with the highest incidence of non-compliance with labor laws. The most problematic industries in terms of compliance are often found in low-wage industries with a large immigrant workforce that may be reluctant to use reporting tools requiring interactions with regulatory authorities.

David Weil, WHD administrator in the latter years of the Obama administration and currently Dean of the Heller School of Social Policy and Management at Brandeis University, developed a complaint/compliance matrix that suggests the limitations of relying on complaints as the driver of agency priorities. Weil has recommended shifting the focus from Quadrants 1 and 3 – the highest source of complaints – to Quadrants 1 and 2 – the greatest loci of violations. This re-imagined orientation has been termed a strategic enforcement model.<sup>24</sup>

***“Adopting a strategic enforcement prototype requires targeting industries where evidence shows workers are most likely to be mistakenly or deliberately cheated out of their wages, and making particular efforts to reach those sectors where workers are least likely to report such violations”***

	High Noncompliance	Low Noncompliance
High CR	<b>QUADRANT 1</b> Complaint response: High threshold for conciliations; Integration with directed initiatives <u>Directed initiatives: Focused on special industry initiatives only (e.g., garment, eating &amp; drinking)</u>	<b>QUADRANT 3</b> Complaint response: Conciliate* <u>Directed initiatives: Few</u>
Low CR	<b>QUADRANT 2</b> Complaint response: High threshold for conciliations; Integration with directed initiatives <u>Directed initiatives: Focus on these</u>	<b>QUADRANT 4</b> Complaint response: Conciliate* <u>Directed initiatives: Few**</u>

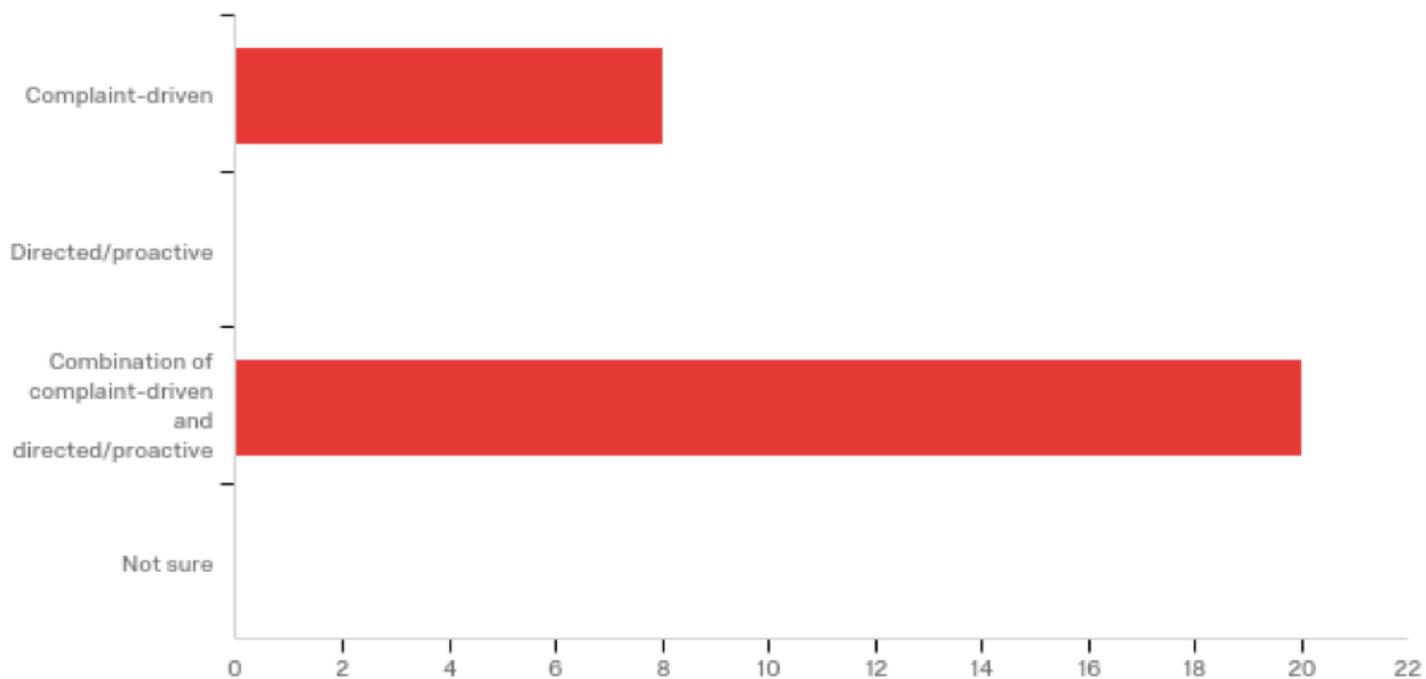
# ENFORCEMENT PRACTICES

Adopting a strategic enforcement prototype requires targeting industries where evidence shows workers are most likely to be mistakenly or deliberately cheated out of their wages, and making particular efforts to reach those sectors where workers are least likely to report such violations. Recognizing that public agencies operate with limited resources, strategic enforcement involves prioritizing which industries to focus on, which workplaces to target within selected industries, and determining which regulatory tools are most effective.

## Complaint-Based vs. Pro-Active Enforcement

Many state agencies are constrained from entirely abandoning a complaint-driven approach in favor of a pro-active enforcement strategy, for various reasons, including statutory mandates, political expectations, and historical tradition. Nonetheless, we asked our respondents to assess where they stood on this spectrum.\*

Respondents reported a wide range of sources of complaints, including not only complaints directly from individual workers themselves, but also referrals from unions, community organizations, worker centers, employer groups,



federal agencies, other state agencies, anonymous tips, and the general public. Most agencies surveyed (61%) have a telephone tip line, and even more (86%) indicated that they have a method to report violations through the internet.

Among the agencies in our survey, 29% reported that their priorities were driven solely by complaints while 71% said their investigations were based on a combination of responses to complaints as well as agency choices of directed or proactive investigations.

Brent DeBeaumont (WA) described his agency’s approach as “primarily complaint-driven. The reason for that is the department has a mandate under the Wage Payment Act to investigate every complaint that we receive from workers.” Representatives of the Massachusetts Attorney General’s Office suggested that there is a roughly 80-20

\*Although we surveyed a total of 27 states, in some cases we had more than one response per state. As a result, in this and other charts, the numbers may add up to a total higher than 27.

# ENFORCEMENT PRACTICES

split between acting on complaints compared to launching pro-active investigations but noted that they “try to make the biggest impact given limited resources. So even when we are opening complaint driven investigations, we focus on industries and geographic areas that fit into our priorities. We also try to help workers who wouldn’t otherwise have access to legal help.”

In many states, limited resources drive priorities. Lindsay Moore (AR) indicated that staffing cutbacks determined his agency’s choices. “We were being pro-active in areas where we knew problems exist,” he reported, “but I’ve had to scale back and go back to a complaint driven system right now.” Other states in similar situations have tried to adopt directed programs. Former Oregon Wage and Hour Administrator Gerhard Taeubel (OR) acknowledged that while his agency had been very complaint-driven in the past, the Oregon legislature recently subsidized several positions for pro-active enforcement by drawing on funds from the state’s Wage Security Fund -- a 1980s-era state program ensuring workers’ ability to receive final wages when companies went out of business.

In a parallel development, state agencies responsible for administering unemployment insurance have shifted auditing strategies as a means of improving efficiency in tracking down misclassification violations, moving from a system of exclusively random to a higher percentage of targeted audits. As an example, Ricky Masarracchia (LA) described the transition in 2011 from a focus on randomly chosen employers to a “risk-based system [that] searched for industries that we thought were ripe for misclassification.” As a result, the numbers of discoveries of misclassification increased from “very few” to a peak of 20,000 in 2015. “We are particularly proud of our selection process,” reported Masarracchia. “Very rarely do we do an audit now and not discover a misclassified worker.”

The survey respondents identified a litany of industries that are particularly problematic in terms of misclassification and other wage violations. While the single most egregious violators may vary slightly from state to state, the overall list is relatively consistent – construction, restaurants and hospitality, trucking and transportation, janitorial services, nail salons, car wash firms, home health care and medical staffing companies. Localized mini-booms in certain industries, such as the shale plain in northern Arkansas, were also cited as dependent on the use of misclassified workers.

Rhonda Gerharz (AK) urged agencies to be pro-active, to monitor various forms of media in order to track new businesses and trending industries. “Don’t wait for a claim to come in,” she suggested. “If your law allows it, don’t be so reactive. When you see a problem, be the first to contact them. Tell them about labor laws and encourage voluntary compliance.”

## **Sweeps / Stop Work Orders**

As part of the evolution of enforcement practices, a number of agencies have created opportunities for investigators to spend more time in the field, returning to an earlier method of policing worksites. “We definitely recommend the value of having an enforcement presence in the community,” said representatives from the Massachusetts Attorney General’s office. According to the AG’s Office, it is now part of the agency’s standard operating procedure. “But there’s a balance,” they pointed out. “For all the time that investigators are out in the field, they’re not at their desks doing audits and much of our work is paper-driven.” Similarly, John Monahan (NJ) reported that periodic ‘sweeps’ are part of his agency’s mission. A team of investigators sets out on a pre-planned series of site visits, as varied as

# ENFORCEMENT PRACTICES

searching for misclassification on construction projects to locating child labor issues among migrant workers on New Jersey's farms.

For the past decade, Connecticut has had an aggressive system of sweeps used in conjunction with the state's stop work order legislation passed on October 1, 2007.<sup>25</sup> Stop work orders allow enforcement agencies to halt a business' activities immediately if a violation has occurred. "We do targeted sweeps," said Resa Spaziani (CT), but "we are not going to issue a stop work order because of a complaint on a business. We are doing it much more industry-based." Spaziani described a statewide sweep on the nail salon industry in which four teams of two inspectors shut down 26 salons in one day for a series of violations, including failure to pay minimum wage, off-the-books compensation, and failure to procure workers' compensation insurance policies.

***"We do targeted sweeps," said Spaziani, but "we are not going to issue a stop work order because of a complaint on a business. We are doing it much more industry-based."***

Spaziani has applied similar tactics to the construction industry. Her team obtains building permits in a defined geographical part of the state to determine where construction is occurring, and subsequently visits area sites. One inspector enters the job-site trailer to speak with a representative of the general contractor, other inspectors fan out on the site to interview workers, and another works a computer from the car to see if the various contractors on the project are registered with the state, contribute to the unemployment system, and are up to date in their workers' compensation payments. Spaziani described the system as fast-paced and relatively effective

because businesses that receive a stop work order are motivated to settle in order to reopen or resume operations.

Spaziani claimed that the authority to issue stop work orders has expedited what had been a long and clumsy process. "If I went into a business and the workers told me they were getting paid cash, I would ask the employer for all the records. He wouldn't send them to me and I would subpoena him. The turnaround on a basic wage and hour case was probably 3-6 months. Now they get me their records by the end of that day or the next business day."

According to Spaziani, employer pushback to the expedited system "is not what people think. By the time I've left that site, my phone is already ringing by the owner of the company, by their attorney, by their accountant, by their insurance carrier...It's not that you're chasing the people, but they're chasing you." Depending on the violations involved, the cure can be as simple as getting a current workers' compensation policy, providing proof of payroll payment, or bonding with the departments of revenue or unemployment for out-of-state employers. "Our average turnaround on a stop work order –and somebody did this study – was a day and a half," she continued.

## Cash Compensation

As federal and state agencies increased their focus on the problem of employers misclassifying employees as independent contractors, some employers shifted to a simpler system of cash or off-the-books compensation as a different method to achieve the same labor cost saving goals. Paying workers in cash eliminated the complexities of

# ENFORCEMENT PRACTICES

filing 1099 tax forms and coincided with the growth of an immigrant workforce that many employers believed would be less likely to challenge employers' compensation practices.<sup>26</sup> The descent into an underground economy where worker payments are unrecorded and unreported has provided additional challenges for enforcement agencies.

The shift in employer tactics has forced agencies to reconsider their enforcement approach. As misclassification gives way to under-the-table payments without the issuance of 1099s, new enforcement challenges have emerged. Since cash payments are typically not, in and of themselves, wage and hour violations, the ability to crack down on employers that pay in cash as a means of avoiding tax and insurance obligations will vary from state to state depending on the jurisdictional responsibilities of each state's departments and the level of inter-agency cooperation. Typically labor standards agencies will be able to act only if there are also wage and hour violations in addition to the violations resulting from off-the-books compensation, which is often, but not always, the case. Maura McCann (NY) noted that "off-the-books situations that don't necessarily involve wage theft" are "really tax theft." In the case of an investigation into a cash payment employer, Gerhard Taeubel (OR) indicated that his agency might review underlying minimum wage or overtime violations if relevant, but "if we got a complaint of that nature, we would be looking to refer to the Department of Revenue if they're not reporting or the Employment Department if unemployment taxes aren't being paid."

***"Maura McCann (NY) noted that  
"off-the-books situations that don't  
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"really tax theft."***

Agencies that have multiple jurisdictions under one roof are well positioned to use a variety of tools to respond to the cash economy. Rhonda Gerharz (AK) said her agency looks to see if there is a failure to provide workers compensation insurance. According to Mark Ryan (RI), his agency takes the position that "wages paid in cash that have been documented by the employee and employer on a ledger sheet are treated as wages for the purpose of determining if a misclassification violation has occurred." Similarly, Ivan Bayci (MI) suggested that if "a claimant submits a proof of payment [it will lead] to an investigation in which an unemployment claim can be established."

Some labor standards agencies have protocols to follow when workers report that they have been paid cash wages, that allow the agencies to enforce the laws vigorously despite the absence of records; they rely upon worker testimony, additional witness corroboration, and other sources of evidence. Still, the agencies' jurisdictions provide them with the authority to pursue minimum wage or failure-to-pay violations, but the inherent nature of a system that purposely has little or no documentation is sometimes a barrier to thorough investigations for agencies with limited resources and more straightforward cases to handle. Furthermore, the enforcement of the larger and more consequential violation, i.e., tax avoidance, is typically in the hands of a separate state division, not the labor standards enforcement agency. "The state departments of revenue, unemployment and workers' compensation all need to be at the vanguard of enforcement in this new cash wage business model," concluded representatives from the Massachusetts Attorney General's Office.

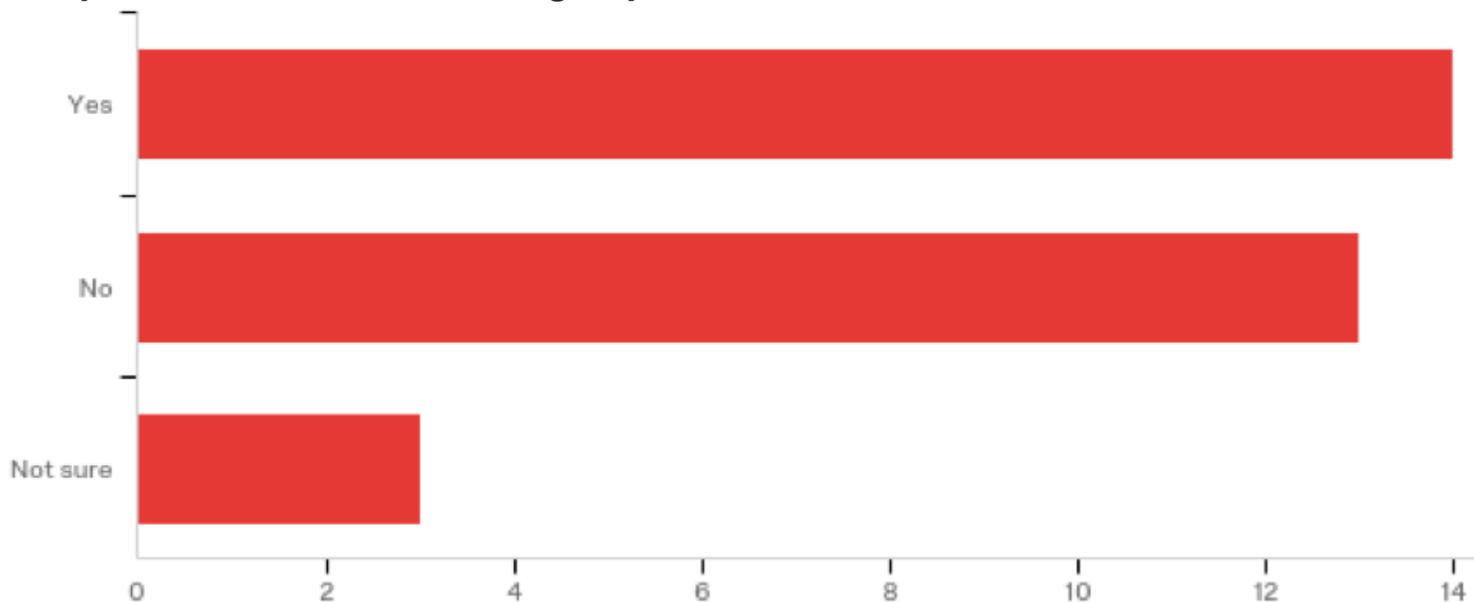
A number of states have formed joint state task forces to monitor and address misclassification and payroll

# TASK FORCES

fraud. Assembling staff from multiple agencies that are charged with regulating the assorted forms of wage theft -- wage and hour violations, income and unemployment tax avoidance, insurance fraud -- allows for a larger pool of inspectors to work collectively on investigations of common targets. A 2016 National Employment Law Project (NELP) policy brief suggested that at least nineteen states had established an inter-agency task force or a study commission, although it should be noted that not all of these involved ongoing, indefinite working collaborations.<sup>26</sup> Our survey showed that just under one half of the respondents reported having some form of a combined agency structure.

Given the number of agencies that have potential jurisdiction over the issue of misclassification, some of these task forces may include up to a dozen different agencies. In New York state, the original body was established in 2007. "The agencies involved include the Department of Labor (Unemployment Insurance and Labor Standards), the Workers Compensation Board Fraud Inspector General, the state Attorney General, the Comptroller, and Tax and Finance," reported Milan Bhatt (NY). In 2016, it was expanded to other agencies, including, for example, the State Liquor Authority, which may seem like an unlikely bedfellow, but which possesses the ability to impose licensing consequences for violations in the restaurant and other industries.<sup>27</sup> "It's sharing information, exchanging tips, turning things into misclassification joint investigations that ordinarily would've just stayed in their separate arenas," concurred Maura McCann (NY). The ability to aggregate resources allows for increased strategic planning as well as field operations. "We get very involved in strategy, how to catch an employer who might be doing something widespread," said McCann. "We'll do joint sweeps in all industries." The relevant agencies in New York meet on a regular basis, cross-train their investigators, and conduct joint sweeps. For instance, New York set up a Nail Salon Task Force that flagged cases for multi-agency collective action.

## Does your state have a combined agency structure?



In smaller states with fewer staff, a task force can prove the old adage that the whole is greater than the sum of its parts. Collaboration can lead to increased efficiencies in government operations and help avoid the inefficiencies that occur when a government agency intervenes in a workplace but addresses only one of many existing and related violations. Michele Small described the operation in New Hampshire. “The task force met with the different agencies and developed an on-line form for complaints. [The Department of] Labor manages the site and triages the complaints...[then] other agencies will pursue the company as well. All information is shared via the web site and by sharing the actual inspection reports.”

Like any other facet of public policy, however, inter-agency task forces can be impacted by political transitions. For example, the Massachusetts Task Force on the Underground Economy established in 2008 was highly effective, but has become less active as a result of a change in gubernatorial administrations. For this reason, it is critical that task forces involve collaboration among civil service career staff, not just political appointees, and that changes, such as routine methods for inter-agency referrals, are integrated into ongoing agency operations.

## **Community Partnerships**

In an era of limited public resources, many state enforcement agencies have developed cooperative working relationships with non-governmental organizations that have an interest in addressing issues of payroll fraud and misclassification. Many unions, particularly in the building trades, have appealed to lawmakers and agency leaders to help clean up construction and other sectors that are facing a growing problem of unscrupulous employer behavior. Worker centers around the country have sought assistance as they advocate for fair treatment of low wage and immigrant workers. Legally compliant employers, concerned about their ability to compete with firms that avoid tax and insurance obligations, welcome heightened enforcement activity as a means of establishing a level playing field. These outside groups are often the best sources of reliable information about serious violations and can assist investigations by serving as a bridge between the government agency and workers on the ground, as well as by helping to gather initial information and documents related to potential violations. In addition, unions, workers centers, and employers know their industries’ internal structures and dynamics; that familiarity can provide valuable context for investigators or agencies attempting to develop a comprehensive strategy to change employer practices or simply resolve an individual or group complaint.

“Our partnerships with advocacy organizations are a fundamental dimension of the Task Force’s efforts,” commented Milan Bhatt (NY). Ricky Masarrachia (LA) reported that “contractors, the business community, and unions supply us with all the tips and leads we can handle,” and his colleague Renita Williams (LA) concurred, citing “the anonymous tips that we received not only from employers but by union officials who saw their members being affected by taxes not being properly withheld.” According to Robert Asaro-Angelo (NJ), the construction unions “do a great job of letting all of our elected officials know what a problem it is because

# TASK FORCES

they're seeing it every day. Every business representative, every organizer sees that it's taking jobs away from their members."

The Massachusetts AG Office's Fair Labor Division has two sets of regular meetings with worker stakeholders: with the Fair Wage Campaign (immigrant worker centers and legal services offices) and with their Labor Advisory Council (comprised primarily of labor leaders). At these meetings, they discuss cases, trends, challenges, new approaches, priorities, etc. Representatives from the Massachusetts Attorney General's Office also emphasized the value of working closely with the business community: "We have a standing meeting with a group of non-union construction industry folks to hear from them and for us to talk about our enforcement. These are the most responsible employers who are frustrated because they can't compete. Often the feedback is for us to take enforcement action against irresponsible contractors so they can compete on a level playing field. We're committed to working with responsible businesses."

The Massachusetts Attorney General's Office is just one of the many agencies around the country that has conducted routine and ongoing outreach to immigrant communities, but reaching those workers has been made more difficult as a result of increased and aggressive federal immigration enforcement and the resulting apprehension in immigrant communities about cooperation with any public authorities. This challenge has existed even when agencies have been clear that they do not collaborate with Immigration and Customs Enforcement (ICE). Resa Spaziani (CT) described the ups and downs of her agency's ability to assist immigrant workers: "When we first started, workers would think we were Immigration and run from us. Once they learned we were actually there to help them get their wages we had a huge turnaround where the undocumented worker was not afraid to come to us." But in the current environment, she continued, "all of a sudden we're not getting those complaints." It is crucial that labor enforcement agencies take steps to ensure that the rights of all workers, including immigrant workers, are enforced and respected.

While a number of task forces started during the time period from 2009-2011, there has been renewed interest in this approach. At least six states started new task forces since the beginning of 2018 (Colorado, Michigan, Montana, New Jersey, Virginia, and Wisconsin).

Based on the information provided in the surveys and follow-up conversations, an effective task force should go beyond simply meeting, issuing legislative recommendation or conducting studies. Rather, it should ensure routine and ongoing integration of operational activities among the agencies involved. Patricia Smith, former Solicitor of the United States Department of Labor and

former Commissioner of Labor in New York State, recently testified regarding best practices for multi-agency task forces.<sup>28</sup>

Her recommendations were consistent with our respondents' input:

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

Smith also recommended reviewing the first Report of the Joint Enforcement Task Force on Employee Misclassification in New York<sup>29</sup> to understand the actions taken to get New York's task force, the first in the country, under way.

## ADMINISTRATIVE ISSUES

### Job Titles / Staffing Levels

Most agencies use primarily investigators to combat misclassification; 83% reported that the most common job titles for staff engaged in this work was investigators. Attorneys and auditors were also frequently-used job titles. As noted in the previous section, agencies often work within severe resource constraints. Although some large states, like California and New York, have enforcement staff numbering well into the hundreds, a 2018 report in Politico found that seven states had no investigators whose responsibilities included minimum wage and overtime, and most states had fewer than 10 on staff.<sup>30</sup> Arkansas is one of those states. Lindsay Moore (AR) stated, as of 2014, his agency had ten staffers and two attorneys. Those numbers have since been reduced to five and one. As a result, “we used to do 400-450 wage and hour cases. It’s now running around 250. Collections are about half of what I was finding, and there’s a case backlog of about six months.”

### Training

Most agencies reported that they have staff training on enforcement related to misclassification (83%), with a mix of on-the-job and more formal training programs. For example, the Massachusetts Attorney General’s Office, Fair Labor Division, offers a “robust program for our investigators, support staff and new attorneys.” The training includes provision of written materials and use of PowerPoint presentations, and covers the range of laws enforced by the division, including wage and hour laws, earned sick time, child labor, prevailing wage, and other laws.

Alaska (for workers’ compensation fraud) and New Jersey (for wage and hour) both have more of an on-the-job training approach, although New Jersey is in the process of further development. According to Ron Marino (NJ), “we have a field manual for new staff when they are hired. We’re in the process of coordinating right now with Employer Accounts to get training on the ABC test so all our people will be schooled in that. And we’re also in the process, as far as misclassification is concerned, of putting together a manual for them specifically as to how they can do job site inspections and what they look for record inspections and things of that nature.”

In Oregon, there is training for every new staffer that comes on board, on all of the regulations the department enforces, as well as continual exchanges of information between staff and managers.

Lindsay Moore (AR) reported that his agency has trained investigators in better interviewing techniques. “When I came in, 60% of cases went to legal division for hearing, because the staff was so ill prepared that they would lose.” Cases were not sufficiently developed to hold up through the legal process. Now, “we’ve been successful. 98% of cases don’t get forwarded to legal anymore – we settle them within the division.”

Investigators and others enforcing unemployment insurance laws often receive more uniform training than those enforcing wage and hour laws. Federal requirements regarding training related to unemployment insurance enforcement ensure more formalized and robust trainings for investigators and auditors probing misclassification in this context. In New Jersey, new auditors go through a comprehensive training program, with a three-inch thick manual of procedures dictated by the U.S. Department of Labor. In addition, Mindy Gensler (NJ) reported that: “In the audit side, we have a monthly training for our auditors by their immediate supervisors. We have a yearly workshop...and we just started a voluntary training session every second Thursday of the month with our auditors dealing with any changes, any court cases that came up, any difficulties that they’re having in some of their cases

# ADMINISTRATIVE ISSUES

that come in to try and get help. So they're constantly getting trained.... USDOL gives us instructions. They give us what is called a TPS review. We have to meet these 9 tests that the USDOL requires us to do. So it is mandatory for every auditor to learn these tests to be able to pass our audits that USDOL conducts."

## Language abilities

Given the composition of the low-wage workforce, it is critical for agencies to have the ability to communicate with workers from a wide range of national origins. Some agencies emphasized the importance of having staff with language abilities in order to be able to do their jobs effectively. Two thirds of the agencies reported having at least one Spanish-speaker, and a variety of other languages were listed as well, including Portuguese, Vietnamese, Korean, Haitian Creole, Mandarin, and Cantonese. Some agencies conduct language access training for staff, to ensure that they know about the various resources, such as telephonic translation services, that may be available.

## Tip lines

Most agencies surveyed have a telephonic tip line and/or can receive complaints via the internet; however, only nine of them could report with certainty that they routinely collected data regarding incoming complaints through these sources.

## Technology

Twenty-two of the agencies have not developed specialized technology or data analysis tools to detect or target their misclassification efforts, beyond the general case management systems used for all of their case work.. Of the agencies that did use such tools, two reported using particular software programs (called Discovery and AWARE); one conducts a review of tax-related documents, one is comparing 1099-misc data with current or new independent contractor exemption certificate applicants, and another sorts complaints and enforcement on Excel spreadsheet. Several agencies reported that they are actively in the process of addressing this gap. Ricky Masarrachia (LA) reports that his agency is developing "new software that will have built-in analytics that will minimize the physical and manual processes that a tax agent has to go through" which should "allow more time to be able to address more businesses and be able to do more audits." Lindsay Moore (AR) also indicated that his agency is implementing a new complaint system which would process information before case assignment, and which would allow wage and hour complaints to be filled out online, which has improved their "ability to get better information and take action."

## OUTREACH AND USE OF THE MEDIA

In their role as members of the executive branch of state government, labor standards enforcement agency leaders have the opportunity to use the authority and credibility of their offices to reach out to a variety of constituencies impacted by the issue of misclassification. Many agencies regularly conduct public education about legal requirements, to employer associations, worker organizations, and others. A more limited number proactively publicize results of their enforcement.

Most of the agencies we surveyed make significant efforts to educate and inform. Our respondents all reported a regular regimen of public speaking to business associations, unions, community organizations, immigrant advocacy groups, workers centers, lawyers, accountants, human resource professionals, religious groups, police departments, and the general public. When she was California Labor Commissioner, Julie Su (who is currently the Secretary of the California Labor and Workforce Development Agency) launched a "Wage Theft is a Crime" campaign in 2014 that included a new website in English and Spanish, posters on bus sides and bus shelters, and multilingual radio ads about wage theft and the right to report cases to the Labor Commissioner.<sup>31</sup>

"Our focus has been on pro-active education to prevent unsafe practices as well as uninsured injuries," reported Rhonda Gerharz (AK). "Just letting people know that they don't get to deem someone an independent contractor at will goes a long way. It is a common misconception here that you can make someone an independent contractor simply by issuing a 1099. My favorite thing to do is give presentations to business associations. For instance, we had a huge problem with master guides and assistant guides in our hunting and fishing industries where assistant guides were often treated as independent contractors even though their own laws say they're employees. We saw a reduction in that practice after given a presentation to the professional hunting guides association."

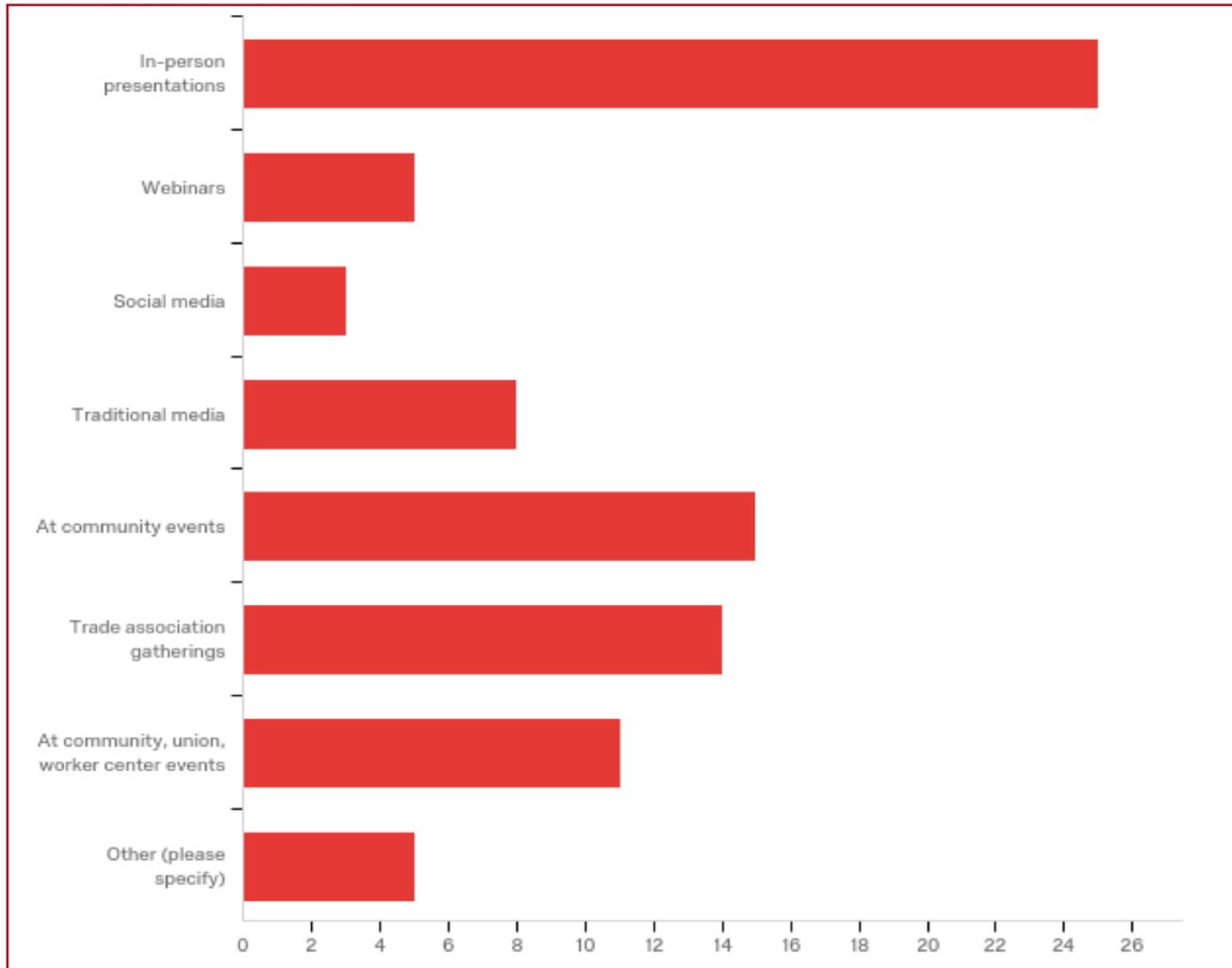
***We're never going to catch every bad employer by just knocking on every door... They need to have a fear of breaking the law by seeing somebody else doing what they're doing, and going to jail or getting severe fines or penalties***

Renita Williams (LA) said that her agency had "spoken at virtually every human resource society chapter, both public and private" in Louisiana. The outreach has presumably been effective. "In the past," confirmed Ricky Masarrachia (LA), "you really had to argue with accountants and CPAs because they thought the use of independent contractors was a good business model and that's the advice they gave their clients." Masarracchia suggested that the efforts of continuing education along with a system of regular audits had paid off: "Our relationship has had almost a 180 degree turn. Now we actually host the Louisiana CPA Society annual meeting at our administrative offices."

Outreach also provides the opportunity for enforcement agencies to explain their understanding of the definitions of independent contractor versus employee, and how they intend to enforce the law. Such efforts can provide helpful clarification, particularly in light of the debate in the business, legal, and political communities over these definitions.

Commissioner Rob Asaro-Angelo (NJ) noted the need for outreach to help businesses, especially smaller businesses, understand the applicable legal standards, adding, “I feel some empathy for those who misclassify because that’s the way everybody else does it in that industry.”

## Forms of Outreach



Some agencies augment their speaking programs with a high-profile media posture – using the bully pulpit to drive compliance through press releases, publications, and the use of social media. The Massachusetts Attorney General’s Office strongly recommended the value of regular announcements of convictions, settlements, and other significant agency activity. “We’ve spent a lot of time building up our press distribution list, including second-language ethnic media that we know are interested. But then we also resend releases to our community partners and unions, and encourage them to retweet or reshare the information.” Shari Purves-Reiter (WA) reported that her agency has rewritten its website to educate both employees and employers and makes extensive use of social media. States that have joint task forces frequently issue annual reports, summarizing their actions as well as calculating lost wages and revenues collected. Zack Fields (AK) reported that his state’s Labor Commissioner uses the agency’s monthly economic research magazine to discuss labor rights enforcement and policy issues.

# OUTREACH

For all of the attempts to be pro-active and use education as a vehicle to forestall misclassification, our respondents recognized that deterrence requires both carrots and sticks. “We’re never going to catch every bad employer by just knocking on every door,” insisted Commissioner Angelo (NJ). “They need to have a fear of breaking the law by seeing somebody else doing what they’re doing, and going to jail or getting severe fines or penalties.” The logic of deterrence rests on an understanding of the law breakers’ business model. In many cases, it is a straightforward financial decision based on calculating whether the benefits of violating the law outweigh the chances of being caught and suffering potential penalties. In other cases, additional considerations come into play.

The importance of publicizing cases in which employers have paid a steep price for labor standard violations is critical in impacting future behavior by those employers and their colleagues. In a recent study, Duke University researcher Matthew Johnson analyzed the effect of the Occupational Safety and Health Administration’s (OSHA) practice since 2009 of issuing press releases about facilities found to be in violation of safety and health regulations. Johnson determined that the attendant publicity prompted other similar facilities to substantially improve their compliance.<sup>32</sup>

This approach is likely equally relevant in the world of labor standards enforcement. Publicity makes employers aware of their obligations and potential consequences for noncompliance; it has a reputational impact that can drive deterrence by similarly situated firms and helps alert workers to potential violations. In addition, even when joint employment is difficult to establish, higher level companies may want to avoid association with contractors or subcontractors with a known history of violations, and at times, negative publicity can serve as motivation for interventions by the parent company to prompt resolution of violations by the lower-tier firms.

***“Our focus has been on pro-active education to prevent unsafe practices as well as uninsured injuries,” suggested Rhonda Gerharz (AK). “Just letting people know that they don’t get to deem someone an independent contractor at will goes a long way.”***

# MEASURING RESULTS

## MEASURING RESULTS AND ENSURING FUTURE COMPLIANCE

Agencies use varied methods to measure the results of their enforcement activities. The metric most commonly used by labor standards agencies is the amount of money recovered for workers. Twenty-three of the agencies surveyed measure back wages collected, while a significant number also measured the unemployment taxes and workers' compensation penalties collected. "Collections are really how we measure our results," said Resa Spaziani (CT).

Other states also measure office activities, procedures, and efficiency. Rhonda Gerharz (AK) said, "We have an interactive statistics log where we track everything in all of our active cases. Did they settle? Did they go to hearing? What was the penalty amount? We have a separate tracking system for uninsured injuries, public inquiries, compliance checks, tips from the public, on-site visits, etc." She also reported that since her agency became more proactive, she had observed a decrease in uninsured injury reporting. States with multi-agency task forces may have annual reports that provide an opportunity for yearly reporting on key issues. For example, the Washington annual report to the legislature on the underground economy includes "the number of unregistered employers that have been found, the amount of assessments that have been made...And we also do our own performance measures within each division to identify assessments, penalties assessed, unregistered employers, all those things as well." Steve Beaty (WA).

New York tracks "the total number of sweeps, the total number of cases, misclassification cases and how many workers were impacted by those cases. The extent that we were able to recover revenue and bring it back to the state." said Milan Bhatt (NY).

Oregon tracks case handling: "We want to make sure we're doing everything as efficiently as we can," said Gerhard Tauebel (OR), adding, "Of course we also want to see that what we're doing has some kind of effect. But I think gauging the effectiveness is probably much harder than just kind of knowing how we're doing things and how well our processes are working."

This observation identifies a critical missing element in labor standards enforcement: the development of appropriate ways to measure effectiveness in driving compliance and deterring violations, either specific deterrence (of the particular employer investigated) or general deterrence (of similarly-situated employers or of the overall employer community).

***"New York tracks "the total number of sweeps, the total number of cases, misclassification cases and how many workers were impacted by those cases. The extent that we were able to recover revenue and bring it back to the state." Milan Bhatt (NY).***

# MEASURING RESULTS

One way to assess specific deterrence is to conduct ongoing monitoring, an on-site revisit/follow-up inspection, or at least in-office reviews or audits of employer payroll and other documents subsequent to resolution of an investigation. Employer compliance suggests effective enforcement, while employer noncompliance suggests that changes are needed. Ongoing monitoring, revisits, or reviews can relatively definitively answer the question: has the agency's intervention led to lasting change in that specific employer's practices?

Ten agencies reported that they conduct revisits or reviews either routinely or on occasion. However, agencies do not seem to use the results of such revisits more broadly as a way to assess agency effectiveness generally. Rather, they use them primarily to confirm ongoing compliance by that particular employer.

New York officials noted certain readily identifiable measures of compliance as well. For example, a recent state initiative focused on improving labor standards at nail salons requires salons to obtain a bond to cover wage underpayments or similar liabilities, and Milan Bhatt (NY) reported "pretty universal" compliance with the bond requirements since they came into effect. His colleague Maura McCann also noted that the state's Construction Industry Fair Play Act required employers to post notices of workers' rights under the law; incidents of failure to post has dropped dramatically over time.

Many officials interviewed recounted anecdotal and informal ways they assessed the impact of agency action. "We keep track of our public inquiries and there's lots of gratitude expressed for explaining the high liability risk, not only for personally not having insurance and for potentially misclassifying employee labor, but for also contracting with anybody who does not have Workers' Comp," said Rhonda Gerharz (AK). Steve Beaty (WA) noted that there was a greater impact when there was outreach to the media.

## **Ensuring Future Compliance**

As noted above, some agencies use revisits, reviews, or ongoing monitoring as a method of ensuring future compliance by employers who have been found to have violated the law. For example, Arkansas and New Jersey both have relatively informal processes for conducting revisits to ensure compliance.

Resa Spaziani (CT) said that her agency does not currently have any automatic method of triggering inquiries about employer compliance after a stop work order is lifted, but she noted this as a goal after an upcoming computer system upgrade. Ultimately, though, she said deterring violations and ensuring future compliance would be difficult: "We've had some very big cases and some very big wins, but they just find another way to cheat."

Some states use terms of settlement agreements to drive future compliance. For example, Oregon uses suspended penalties and ongoing monitoring:

# MEASURING RESULTS

“In some of these settlements that we’re talking about, we may say, ‘Well, the penalties for this would be X amount of dollars. We agree to waive half of those or a percentage of those on condition that you remain compliant the next three years and we’ll monitor you during that period of time.’ That seems a pretty strong incentive, I guess, for an employer to at least for a period of time get into the practice of actually making sure that they are complying with the wage and hour regulations. And hopefully during that period of time they will see that it’s not that difficult to do to accomplish that, and even after that agreement expires they will continue in those practices,” said Gerhard Taubel (OR).

In Louisiana, settlements require the employer to admit that it has misclassified the worker, enabling stiffer penalties in the event of future misclassification. The agency then conducts a “desk audit” a year later. “We’re looking at the companies that we audited, we’re making sure that their payroll has increased, the number of workers has increased as per the original audit.” If expected changes have not occurred, “then we follow up with that other audit. And that’s when we’re able to assess those monetary penalties,” says Ricky Masarrachia (LA). One state includes compliance measures in settlement agreements; for example, requiring the employer to agree not to use independent contractors except in limited circumstances, and another state provides notice that future violations will result in escalated enforcement, including more severe penalties and, for public contractors, debarment. Some state laws allow for increased penalties for repeat violations. Some agencies also share violation information with other relevant sister agencies within the state, to ensure more thorough future compliance. One state monitors monthly lists of cancelled or expired workers’ compensation policies as a way to flag potential violations.

## Metrics

In the survey and interviews, agency officials identified several key areas for development, such as legislative reforms. In addition, several missing pieces, or areas for improvement, emerged based on an overview of the information gathered.

One major gap in labor standards and misclassification enforcement is the shortfall in meaningful measurements of success. The commonly used metric of wages collected has the virtue of being readily available and easily comprehensible, and it unquestionably indicates something: generally, agencies that are ineffective at enforcement do not collect significant money for workers. However, this number is limited in that it does not indicate the deterrent impact of enforcement, either on the specific employer or on other employers in that industry. The goal of enforcement is ultimately to create a culture of compliance and to deter violations, and counting the dollars collected does not indicate whether this goal has been met. Consistently high annual collections from within the same industry may indicate, for example, that violations persist and that firms in the industry consider payment of restitution a cost of doing business.

# MEASURING RESULTS

Some research exists suggesting other ways to measure impact: for example, David Weil analyzed the impacts of prior investigations in a geographic area on the behavior of workplaces subsequently investigated in that same area. He examined, for example, whether a fast food outlet behaves differently if many other nearby fast food restaurants were investigated than if that were not the case, and found that prior investigations do have a significant deterrent impact.<sup>32</sup> (See, <https://www.dol.gov/whd/resources/strategicenforcement.pdf>. Pp. 49-57.)

With regard to misclassification in particular (as opposed to enforcement generally), agencies could use information from unemployment tax filings to assess effectiveness: for example, if there is a sweep or concerted effort to enforce within a given industry and/or geographical region, does that result in a noticeable increase in the number of employees reported on tax reporting forms for unemployment insurance? Or any increase in the number of employees or amount of remuneration reported to workers' compensation carriers? Figuring out effective methods of measuring impact is critical to enforcement and fighting misclassification; therefore, focused attention on metrics would be appropriate.

## Information sharing among states

Another area for development is in information sharing and collaboration among states. Several agency officials noted this gap, which is especially problematic in relation to neighboring states: "if an individual employer is misclassifying workers in Pennsylvania and they also come across the border, we really should be aware of that so we can evaluate to see whether or not that individual is also misclassifying employees in the state of New

Jersey." said Ron Marino (NJ). John Monahan (NJ) added, "a lot of companies come from outside of the state of New Jersey and if we go on a site and we do get to interview them, we don't see them the next day or the next week. They're gone. They've gone back to wherever they come from. So that makes it a

***"We've had some very big cases and some very big wins, but they just find another way to cheat." – Resa Spaziani (CT)***

little difficult on us as far as enforcing the statutes concerned for out-of-state contractors."

## Additional areas for development

Some states have powers in the statutes that they have not routinely been utilizing to improve collections or compliance. For example, New Jersey has a law allowing the Labor Commissioner to do a repeat audit a year after an initial violation, and order a license suspension or revocation if the conduct persists; the agency is

# MEASURING RESULTS

currently exploring making use of this statute. Other states may have licensing consequences that could be imposed upon violators, representing more untapped potential.

In addition, many states do not seem to be utilizing the full potential of settlement agreements to ensure future compliance. Few states reported using ongoing monitoring or injunctive/remedial measures (aside from payment of back wages) as part of their routine resolution of investigations.

Finally, collecting money owed is an ongoing challenge for many agencies.<sup>33</sup> Often there are more robust remedies available—such as tax liens—in relation to unemployment insurance liability than for back wages. One state noted that tax liens are subject to varied and progressive collection efforts up to wage garnishment, tax intercept, and bank account levies. Wisconsin has a law allowing workers to place a lien on an employer's property in order to enforce wage law protections and other states, such as New York, have pending bills proposing similar remedies.<sup>34</sup>

Agencies reported a range of methods for trying to collect money owed: referring the debt to the state attorney general's office, docketing a judgment (and seizing any assets that can be found), withholding of progress payments (for public contractors). One state has a full-time loan/collections officer to collect workers' compensation penalties. Another state contracts with a collection agency when they cannot collect the money themselves. Two states noted the importance of individual liability in enabling effective collections. Identifying new ways to swiftly collect money owed would be valuable for increasing agencies' impact.

# GIG ECONOMY

## GIG ECONOMY

The laws that state agencies are mandated to enforce were, for the most part, written and enacted in the last century. The past few decades have seen a tumultuous transformation of the world of work that has prompted some to question the continued relevance of existing labor laws for the realities of the contemporary workforce. These changes in the workplace create challenges for enforcement agencies. The Massachusetts Attorney General's Office noted that the "current enforcement statutes are, to some extent, built on an outdated employment model that contemplates direct employment relationships. This can sometimes result in problems identifying who is statutorily responsible when enforcing the laws."

A significant majority of American workers still work as full-time employees subject to all the rules and regulations governing that employment status. But there has been an evolution into "alternative work arrangements," a broadly defined category that includes independent contractors, freelancers, temp agency workers, on-call workers, contract workers, and other contingent forms of work. Studies assessing the size of these shifting work categories vary widely. The Bureau of Labor Statistics (BLS) estimated that in 2017, 3.8 percent of U.S. workers held contingent (or temporary) jobs, and also estimated that 6.9 percent of the workforce that year was in "alternative work arrangements," including independent contractors, on-call workers, temporary help agency workers, and similar arrangements. Economists Larry Katz and Alan Krueger estimated that the percentage of workers in alternative work arrangements rose from 10.7 % in 2005 to 15.8 % in 2015, although they subsequently walked back their initial estimates. When part-time employees are included in these calculations, the U.S. Government Accounting Office concluded that alternative work arrangements increased from 35.3 to 40.4 % of employment from 2006 to 2010. And when very broadly defined forays into contingent work are factored in, a recent Federal Reserve Bank report indicated that 31% of adults engaged in gig work in 2017 (defined as informal paid work activity either as a complement to, or as a substitute for, more traditional and formal work arrangements).<sup>35</sup>

Regardless of the reliability and consistency of the data, there is little doubt that the gig economy is a looming presence and even less doubt that it poses particular problems for enforcement agencies. The central question remains: what constitutes an independent contractor versus an employee in the on-demand economy. "It's still all up in the air and there's nowhere we can look to say that something is wrong," said Maura McCann (NY). "We could wait for complaints to come in and go down that road, but then the courts might not agree and the legislatures aren't really taking a stand."

The company in the innovation economy that has drawn the most scrutiny from public agencies has been Uber, the ride sharing firm that insists all its drivers are independent contractors and, as a result, free from most regulatory constraints. Uber has exerted considerable political influence in efforts to exempt itself from laws generally applicable to employers.<sup>36</sup> However, a few states have taken measures, either proactively or in response to complaints, in the

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time period since Uber and Lyft began their dramatic growth in cities around the country. In October 2014, the Alaska State Department of Labor and Workforce Development initiated an investigation after Uber established a beachhead in Anchorage. The Department determined Uber drivers were employees but the company did not go to a hearing, according to Rhonda Gerharz (AK). “They just left instead.” Uber settled for a penalty of \$78,000 for unpaid workers compensation insurance but admitted no wrongdoing. In March 2015, Uber simply eliminated its service in Alaska. Two years later, however, said Zack Fields (AK), “Uber and Lyft lobbied the state legislature and got them to pass a law stating that the drivers were independent contractors.” As in many other states around the country, Uber relied on its political resources and growing popularity to define “transportation network drivers” as exempt from employee status coverage.<sup>37</sup>

Other states have also found Uber drivers to be employees in response to claims filed against the company. In June 2015, the California Labor Commissioner found that an Uber driver was an employee of the company, and ordered Uber to reimburse her for business expenses incurred.<sup>38</sup> The same year, the Florida Department of Revenue concluded that an Uber driver was an employee for the purpose of collecting unemployment benefits, although that decision was subsequently overturned in 2017.<sup>39</sup> In October of 2015, Oregon Labor Commissioner Brad Avakian issued an advisory opinion that Uber and Lyft drivers should be considered employees in advance of the submission of any complaints or wage claims.<sup>40</sup> “That was meant to bring attention to this issue,” commented Gerhard Tauebel (OR), “and spur further conversation here in Oregon about the tech companies and these new forms of work and how we would apply the laws.” Most recently, an unemployment insurance case regarding driver status was pending before an appellate court in New York; the company decided not to continue with the appeal.<sup>41</sup>

Similar classification issues have also arisen in the food delivery business. Renita Williams (LA) described a company that came to her agency’s attention that offered the drivers a choice of terms of employment, i.e., to be hired as an independent contractor or as an employee. “It’s the nature of work that determines it,” noted Williams, “it’s not what the worker chooses. But we made a call to settle that one rather than risk losing in court.”

Enforcement agencies recognize that Uber and its allies have demonstrated significant political power in all those states where transportation network drivers have been deemed by legislatures and courts to be exempt from employment regulations. There is also the mystique of the information economy as the harbinger of the future, which causes hesitation regarding strong enforcement approaches. Some of the agencies we surveyed expressed concern about aggressive enforcement strategies fueling the perception of quashing innovation.

Despite these obstacles to action, many of our respondents see the expansion of independent contractors in these new occupations as a violation of existing labor laws. Commissioner Angelo (NJ) summarized a common perspective: “The gig economy can be a euphemism for exploiting workers. If folks are legitimate 1099 workers or independent contractors or freelancers, I’m happy to support them. But basically, it’s a way for employers to free themselves of their responsibilities to workers.”

# CONCLUSION

## CONCLUSION

This report is a survey of current policies and approaches of state labor standards enforcement agencies. Our goal has been to summarize best practices and lessons learned as outlined by respondents and also to complement their comments with our own views and recommendations.

As an overall perspective, we believe that adopting a strategic enforcement orientation will best serve the needs of working people in communities across the country. We recognize that, in some states, there may be statutory and/or institutional barriers that prevent a full adoption of strategic enforcement, but we believe agencies should prioritize which industries to focus on based on a comprehensive analysis of a given jurisdiction, which workplaces to target within selected industries, and which regulatory tools are most effective. Responding exclusively to complaints as they come in the door is less likely to produce broadly effective enforcement / deterrence results.

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The following recommendations constitute a check list of action steps that can help drive a strategic enforcement approach:

- **Collaborate with relevant governmental agencies** Establish an inter-agency task force or other method for routine, ongoing collaboration. States that have adopted ongoing inter-agency task forces have generally found that the sum of the parts is greater than the whole.
- **Break down silos** In many states, individual agencies often operate in silos, each with its own internal culture and methods of carrying out its mission. Because most misclassification and payroll fraud violations consist of multiple infractions – wage and hour, unemployment, tax and insurance fraud – enforcement will be that much more effective if the appropriate agencies share information and strategies.
- **Create cross-referral systems** Even without the establishment of a formalized task force, at the very least, there should be regular meetings among the relevant agencies, as well as a process for cross-referrals among agencies when they find instances of misclassification. It is inefficient for an agency to intervene in a given workplace, find violations, and take no steps to alert sister agencies about likely related violations.
- **Jointly select targets** A more effective approach toward misclassification would involve even greater collaboration, including joint strategic selection of targets, joint field investigations, and collective identification of trends and of needed legislation.
- **Coordinate cross-agency sweeps** One advantage of inter-agency cooperation is the ability to draw on broader resources. In those states that conduct sweeps of targeted industries, the capacity to cover more work sites is enhanced by incorporating staff from several agencies with multiple fields of expertise. In addition, in states that

allow the issuance of stop work orders, assembling a team of enforcement agents armed with the power to shut down irresponsible businesses can have a timely deterrent effect.

- **Engage with stakeholders** Engage in extensive external engagement: with stakeholders (including worker and employer organizations) and also the media.
- **Collaborate with non-governmental organizations.** In order to reach vulnerable workers and address egregious violations, agencies should collaborate extensively with non-governmental organizations, such as unions, advocacy groups, worker centers, and high-road employer groups. These groups are committed to supporting and aiding agency accomplishments, and agencies benefit from accepting outside organizations as partners in the mission to protect workers' right. While it is important to negotiate an appropriate relationship, partners can play a crucial role as sources of information unavailable to agency staff and as conduits to workers, among other things.
- **Use the office for educational outreach** and as a bully pulpit. When agency leaders regularly meet with employer and trade associations, unions, worker centers, community organizations, and other stakeholders, they can articulate the agency agenda, present the rationale for enforcement priorities, and outline their interpretation of their state's labor laws. For example, unambiguous and pro-active public explanations of the relevant definitions of what constitutes an employee vs. an independent contractor can clarify guidelines for those employers who want to "play by the rules" and serve as a warning for others who may seek to skirt the law. Outreach is also critical in educating workers about their rights.
- **Publicize policies and outcomes in the media** The educational outreach of the bully pulpit should be accompanied by a consistent media strategy that publicizes agency policies and the results of agency investigations. The impact of an agency action against a violator is amplified when the results are made public and can serve as a deterrent for the broader employer community. Again, publicity also helps inform workers about their rights and about resources available to them.

## **Adjust internal operations to meet the challenge of misclassification.**

- **Train staff on misclassification** Ensure adequate formal and ongoing training of agency staff on statutory authority, industry analysis, and enforcement techniques.
- **Develop an agency language access plan and make every effort to hire multi-lingual staff** Many of the most egregious violations take place in low-wage industries with a largely immigrant workforce. Agencies must expand language capacity to serve these communities. This will require development of a language access plan, and the hiring of staff who speak commonly-used languages.
- **Develop a strategy for addressing violations in the cash economy** As many violating employers have shifted from misclassifying workers as independent contractors to a system of under-the-table cash payments, it is critical that agencies develop a strategy to address this form of compensation. Having inter-agency cooperation is helpful in certain of these cases, where there is no wage and hour violation but tax and insurance violations exist.
- **Adapt strategies for the gig economy** Similarly, the emergence of the gig economy demands a comprehensive and consistent enforcement approach. This is a new challenge in that agencies will have to navigate the constantly shifting and uncertain political and judicial shoals of what constitutes legal employment in on-demand jobs.

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- Evaluate outcomes Agencies should measure results and find ways to track ongoing compliance and deterrence.
- Measure results Every agency should have a meaningful and consistent method of measuring results, ideally not limited only to the metric of lost wages recovered. An effective agency should find ways to determine if its work is serving to deter violators and ensure lawful working conditions.
- Track compliance Agencies need systems of tracking future compliance of past violators. Revisit or monitoring programs for former violators would help ensure future compliance as well as help assess the effectiveness of past enforcement.
- Update relevant laws Statewide adoption of the ABC test for determining employee status would lead to greater compliance, and benefit workers, employers, and enforcers alike. The test would provide a more clear and comprehensible method for all parties to determine status, in contrast to the plethora of overlapping yet distinct tests that exist in many states. Other helpful legislative measures identified by respondents include laws creating joint employment in a fissured workplace, laws imposing individual liability, statutes enabling the issuance of stop work orders, and laws allowing for criminal prosecution of egregious violators.

## NOTES

1. Some of the studies documenting trends in misclassification include:
  - “Employment Arrangements: Improved Outreach Could Help Ensure Proper Worker Classification.” U.S. Government Accountability Office, 2006. (<https://www.gao.gov/new.items/d06656.pdf>)
  - “Employee Misclassification: Improved Coordination, Outreach, and Targeting Could Better Ensure Detection and Prevention.” U.S. Government Accountability Office, 2009. (<https://www.gao.gov/assets/300/293679.pdf>)
  - “Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries.” ([http://www.faircontracting.org/wp-content/uploads/2012/09/icm\\_imposes-huge-costs1.pdf](http://www.faircontracting.org/wp-content/uploads/2012/09/icm_imposes-huge-costs1.pdf))
  - <https://blog.pgcgroup.com/the-rise-and-risks-of-ic-misclassification>
  - “Lots of Employees Get Misclassified as Contractors. Here’s Why It Matters.” (<https://hbr.org/2017/07/lots-of-employees-get-misclassified-as-contractors-heres-why-it-matters>)

- <https://www.epi.org/publication/independent-contractor-misclassification/>
- 2. There are a number of state-based reports estimating the social and economic costs of misclassification on revenues, including studies covering California, Colorado, Florida, Illinois, Maine, Massachusetts, Michigan, Minnesota, New Jersey, New York, Ohio, and Tennessee.
- 3. <https://www.dol.gov/whd/state/statecoordination.htm>
- 4. <https://www.dol.gov/whd/paid/>
- 5. <https://www.nytimes.com/2019/05/14/business/economy/nlr-uber-drivers-contractors.html>
- 6. [https://www.dol.gov/whd/opinion/FLSA/2019/2019\\_04\\_29\\_06\\_FLSA.pdf](https://www.dol.gov/whd/opinion/FLSA/2019/2019_04_29_06_FLSA.pdf)
- 7. <https://www.detroitnews.com/story/news/politics/2019/04/22/nessel-creates-unit-crack-down-payroll-fraud/3541002002/>
- 8. [https://dwd.wisconsin.gov/dwd/newsreleases/2019/190415\\_joint\\_taskforce\\_creation.htm](https://dwd.wisconsin.gov/dwd/newsreleases/2019/190415_joint_taskforce_creation.htm)
- 9. <http://cor.mt.gov/Publications/Article/on-tax-day-governor-bullock-creates-task-force-to-ensure-montanans-receive-fair-pay>
- 10. [https://govt.westlaw.com/nycrr/Document/4f087894cd1711dda432a117e6e0f345?viewType=FullText&originationContext=documenttoc&transitionType=CategoryPageItem&contextData=\(sc.Default\)](https://govt.westlaw.com/nycrr/Document/4f087894cd1711dda432a117e6e0f345?viewType=FullText&originationContext=documenttoc&transitionType=CategoryPageItem&contextData=(sc.Default))
- 11. [https://www.michigan.gov/documents/uia/IRSFactorTest\\_503194\\_7.pdf](https://www.michigan.gov/documents/uia/IRSFactorTest_503194_7.pdf)
- 12. <https://www.dol.gov/whd/regs/compliance/whdfs13.htm>;
- 13. <https://law.justia.com/codes/new-jersey/2009/title-43/43-21/43-21-19>
- 14. <https://law.justia.com/cases/california/supreme-court/2018/s222732.html>
- 15. New York State Construc on Industry Fair Play Act: N.Y. 2010 N.Y. ALS 418 ; New York State Commercial Goods Transporta on Industry Fair Play Act: N.Y. Lab. Law § 826–862e.
- 16. <https://law.justia.com/codes/alaska/2017/title-28/chapter-23/section-28.23.080/>; <http://www.akleg.gov/PDF/30/Bills/HB0079Z.PDF>
- 17. <https://codes.findlaw.com/ak/title-23-labor-and-workers-compensation/ak-st-sect-23-30-250.html>
- 18. <https://law.onecle.com/california/labor/226.8.html>
- 19. <http://legislature.maine.gov/statutes/26/title26sec591-A.html>
- 20. [https://leginfo.legislature.ca.gov/faces/codes\\_displaySection.xhtml?lawCode=LAB&sectionNum=2810.3](https://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?lawCode=LAB&sectionNum=2810.3).
- 21. <https://www.latimes.com/business/la-fi-cheesecake-factory-20180611-story.html>
- 22. <https://law.justia.com/codes/district-of-columbia/2015/division-v/title-32/chapter-13/subchapter-i/section-32-1303/>
- 23. Between 1978 and 2008, the number of US Labor Department Wage and Hour

Division (WHD) inspectors dropped from 1343 to 709 at the same time as the number of establishments covered by the Fair Labor Standards Act increased by 112%. Similar staffing cutbacks occurred in state agencies facing budget shortfalls. When resources had been adequate at federal and state agencies, there was a sufficient number of inspectors to

establish a street presence, regularly patrolling businesses on their watch. Employers in areas with ample regulatory staffing knew there might be periodic policing of their workplaces and that knowledge tended to discourage labor standards violations. As funding for inspectors dwindled, many agencies responded by pulling remaining staff off the streets and into their home offices. By 2004, 78% of all inspections by the WHD of the US Department of Labor were generated by complaints. In many cases, employers were freed from apprehensions about authorities routinely looking over their shoulders. In addition, the relocation of personnel off the street produced an internal cultural change that reinforced the complaint-based model

of enforcement. Investigators worked at their desks, developing a triage system to handle incoming reports about violations from workers in a random variety of workplaces.

Janice Fine and Jennifer Gordon. 2010. Strengthening Labor Standards through Partnerships with Workers' Organizations. *Politics and Society*. Vol 38, No. 4. David Weil and Amanda Pyles. 2005. Why Complain? Complaints, Compliance, and the Problem of Enforcement in the U.S. Workplace. *Comparative Labor Law & Policy Journal*. Vol. 27. No. 1

24. Weil and Pyles 2005; Fine and Gordon 2010.
25. <https://www.ctdol.state.ct.us/wgwkstnd/StopWork/Section31-76a.htm>
26. NELP Policy Brief from May 2016 by Sarah Leberstein and Catherine Ruckelshaus, "Independent Contractor vs. Employee: Why independent contractor misclassification matters and what we can do to stop it." Located at <https://www.nelp.org/wp-content/uploads/Policy-Brief-Independent-Contractor-vs-Employee.pdf>
27. [https://www.governor.ny.gov/sites/governor.ny.gov/files/atoms/files/EWTFReport\\_27.pdf](https://www.governor.ny.gov/sites/governor.ny.gov/files/atoms/files/EWTFReport_27.pdf)
28. <https://s27147.pcdn.co/wp-content/uploads/Testimony-NELP-M-Patricia-Smith-New-Jersey-Misclassification-Task-Force-December-2018.pdf>.
29. [https://iiifc.org/images/pdf/employee\\_classification/NY%20Task%20Force%20Feb.2008.pdf](https://iiifc.org/images/pdf/employee_classification/NY%20Task%20Force%20Feb.2008.pdf).
30. <https://www.politico.com/story/2018/02/18/minimum-wage-not-enforced-investigation-409644>
31. <https://wagetheftisacrime.com/>
32. Matthew Johnson, "Regulation by Shaming: Deterrence Effects of Publicizing Violations of Workplace Safety and Health Laws," Unpublished manuscript.
33. <https://www.nelp.org/wp-content/uploads/2015/03/Hollow-Victories-Unpaid-Wages-Report.pdf>
34. <https://www.nysenate.gov/legislation/bills/2019/s2844>
35. Lawrence Katz and Alan Krueger, The Rise and Nature of Alternative Work Arrangements in the United States, 1995-2015, September 2016; Lawrence Katz and Allan Krueger, The Rise and Nature of Alternative Work

Arrangements in the United States, 1995-2016, January 2019;

Federal Reserve Bank, Report on the Economic Well-Being of U.S. Households in 2017, May 22, 2018;

<https://www.epi.org/press/workers-were-more-likely-to-have-standard-work-arrangements-in-2017-than-in-2005/>

Robert Kuttner, John Schmitt, Heidi Shierholz, & David Weil, "The Future of Real Jobs: A Prospect Roundtable, " The American Prospect, May 14, 2019.

36. Resources about states that have passed legislation exempting Uber and Lyft from employment status:

- <http://www.forworkingfamilies.org/sites/pwf/files/publications/Uber%20State%20Interference%20Jan%202018.pdf>
- <https://onlabor.org/state-tnc-and-mc-legislation-preemption-and-employment-status-of-drivers/>

37. <https://nelp.org/publication/uber-state-interference/>

38. <https://www.scribd.com/doc/268911290/Uber-vs-Berwick>

39. <https://www.miamiherald.com/news/local/community/miami-dade/article130050824.html>

40. [https://www.oregon.gov/boli/SiteAssets/pages/press/10\\_14\\_15\\_BOLI%20issues%20Advisory%20Opinion%20on%20Employment%20Status%20of%20Uber%20Drivers.pdf](https://www.oregon.gov/boli/SiteAssets/pages/press/10_14_15_BOLI%20issues%20Advisory%20Opinion%20on%20Employment%20Status%20of%20Uber%20Drivers.pdf)

41. Link to Unemployment Insurance Appeal Board decision:

<https://www.documentcloud.org/documents/4613843-Uber-AB-Decision-Redacted.html>

Article about decision: <https://www.forbes.com/sites/janetwburns/2018/07/20/new-york-gives-uber-drivers-unemployment-rights-in-blow-to-non-employee-model/#199f28cf42c2>

Agency staff from the following states participated in the online survey: Alaska, Arizona, Arkansas, California, Connecticut, Georgia, Hawaii, Idaho, Maine, Maryland, Massachusetts, Michigan, Minnesota, Montana, New Hampshire, New Jersey, New York, North Carolina, Oklahoma, Oregon, Rhode Island, South Dakota, Tennessee, Virginia, Washington, Washington D.C., Wisconsin

Staff from the following states took part in phone interviews: Alaska, Arkansas, Connecticut, Louisiana, Massachusetts, New Jersey, New York, Oregon, Washington

Some of the respondents have since retired or taken other positions.

