



**State of Utah**  
GARY R HERBERT  
*Governor*

SPENCER J. COX  
*Lieutenant Governor*

**Labor Commission**  
SHERRIE HAYASHI  
*Commissioner*

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*Deputy Commissioner and  
General Counsel*

August 30, 2016

Governor Gary R. Herbert  
Senator Curtis S. Bramble  
Representative Val L. Peterson

To Governor Herbert, Senator Bramble, Representative Peterson, and the members of the Business and Labor Interim Committee.

This is the sixth annual report from the Worker Classification Enforcement Council ("Council"), submitted pursuant to U.C.A. § 34-47-202. In the year since the Council's October 2015 report, the Council has continued to meet on a quarterly basis. Agenda and Minutes for all Council meetings are available on Utah's Public Notice Website.

### **The Nature and Extent of Misclassification in Utah**

Misclassification of employees remains an important issue in Utah. Common problems the Council continues to see are employers treating employees as independent contractors and, over the last few years, companies inappropriately using the owner-worker model to misclassify employees. Industries where misclassification is a particular concern are professional services, construction, and transportation. Through misclassification, employees are denied the wages they have earned and are denied the protections afforded by workers compensation and unemployment insurance. Law-abiding employers are disadvantaged by dishonest employers who, by skirting the law, create an uneven playing field. And, Utah citizens suffer lost tax revenue as a result of employers not complying with the law.

As detailed in this report, over the last year the Council has continued its efforts to cooperatively investigate and address worker classification issues. The efficiency of information sharing and referrals continues to improve between Council member agencies. Investigations, enforcement actions, collection of penalties and fines, and obtaining agreements from offending employers to comply with the law have all been successfully pursued. Also, litigation regarding improper uses of the owner-worker model has been successfully concluded. Each member agency and the Attorney General continue to view the Enforcement Council as an effective body in addressing misclassification of workers in Utah.

## **Results of Regulatory and Law Enforcement Efforts, and the Status of Sharing Information by Member Agencies**

### **The Labor Commission**

Since 2012 the Labor Commission has maintained a web page explaining worker misclassification issues in the State of Utah. The web page defines employee misclassification, describes the negative impacts it can have across all facets of society, and educates the public on how to file a complaint of misclassification with the Commission. The Commission has also monitored a misclassification hotline since 2012 and has received a number of misclassification complaints through the hotline.

The Commission is responsible for ensuring each employee in the State of Utah is covered by workers' compensation coverage. When the Commission receives a misclassification complaint, either directly or as a referral through one of the Council's member agencies, the Commission's Industrial Accidents Division investigates the complaint to ensure the employer carries appropriate workers' compensation coverage for its employees. The Division also conducts internal investigations on hundreds of employers each year to ensure compliance with workers' compensation requirements. The Commission has assessed and collected thousands of dollars in penalties against noncompliant employers based on misclassification complaints and referrals, as well as these internal investigations.

The Commission reviewed 90 specific complaints of misclassification for workers' compensation compliance during fiscal year 2016. These complaints were received primarily through the hotline, or were referred from the Department of Workforce Services and other agencies. Some of the complaints were received from the Commission's Wage Claim Unit or from the Commission's Occupational Safety and Health Division and arose during investigations performed by these divisions. After investigation, the Industrial Accidents Division found the employer to be noncompliant with workers' compensation requirements in 57 of these cases. The Commission assessed penalties in the total amount of \$2,474,363. Most of these parties appealed the determination or otherwise entered into a negotiated settlement with the Industrial Accidents Division. After appeal or settlement, the final penalties assessed in these 57 cases amounted to \$741,135.

Of the 90 cases reviewed by the Industrial Accidents Division, 32% involved employers engaged in the professional services industry, which includes employers providing health services in either a home or an office setting. Ten percent (10%) of these cases involved employers engaged in the construction industry. Employers engaged in the transportation industry comprised another 8% of these cases.

The Commission, like the Council's other member agencies, shares the misclassification complaints it receives, the results of subsequent investigations, and the results of its internal investigations with the other member agencies of the Council. This ability to share information between member agencies has been and continues to be

critically important to the Council's work in addressing employee misclassification in Utah. The Commission feels the Council remains an effective tool in addressing employee misclassification in Utah.

### **The Department of Commerce**

The methods of worker misclassification that the Department of Commerce continues to encounter include the following:

- (1) Companies inappropriately classifying employees as "owners";
- (2) Contractors inappropriately paying workers as independent contractors rather than as employees;
- (3) Contractors accepting cash payments to avoid payroll taxes and to avoid reporting to governmental agencies, either as employees or as independent contractors.

The five lawsuits mentioned in the 2015 report have now all been dismissed by agreement of the parties. The United States Department of Labor prevailed on its claim that the owner-workers used by the company in question must be treated as W-2 employees. Accordingly, the company agreed to fines and restitution for employee overtime that was not paid and agreed to pay workers in the future as W-2 employees. The company then discontinued trying to use the owner-worker model and agreed to dismiss all of its lawsuits against the Department of Commerce and the Division of Occupational and Professional Licensing (DOPL).

In August 2014 the division hired a full-time auditor to perform financial audits of contractor licensees and to investigate the payment practices and labor misclassification within the construction industry in the State of Utah. This was a newly created position aimed at addressing misclassification.

Thus far this auditor's efforts have resulted in the following:

- 421 opened cases;
- 339 closed cases;
- 188 cases closed with administrative sanctions including fines, probation, and/or revocation of licensure;
- \$119,300 in fines paid as a result of signed stipulations and orders;
- 11 cases with outstanding stipulation offers; and
- 58 licensees on probation being monitored.

The Department of Commerce continues to benefit from information that has been exchanged through the Worker Classification Coordination Enforcement Council. This exchange of information with other agencies has assisted the Department of Commerce to take action against contractor licensees that are not complying with financial responsibility requirements. The Department of Commerce's actions against

these contractors have assisted the Department of Workforce Services in its collection efforts for the Unemployment Insurance Fund.

### **The Department of Workforce Services**

The Department of Workforce Services Unemployment Insurance Division (DWS/UI) completes both “random” and “targeted” audits on Utah employers. In the last six and one-half year period ending June 30, 2016, DWS/UI completed 6,985 “random” audits, covering \$1.89 billion in total reported wages. The random audits identified \$54.5 million in total unreported wages paid to 7,955 workers who were misclassified as independent contractors, averaging \$6,851 in unreported earnings and 1.1 misclassified workers per random audit completed.

*During fiscal year 2016 alone, a total of 854 random audits were completed. Findings for the year include a total of \$7.5 million in unreported wages and 961 misclassified workers (average of 1.1 misclassified workers per audit).*

During the six and one-half year period ending June 30, 2016, DWS/UI completed 2,327 “targeted” audits of Utah employers, covering \$3.8 billion in total reported wages. These audits primarily use information from the IRS Form 1099 to identify potential unreported workers. The targeted audits identified over \$172.3 million in total unreported wages paid to 27,493 workers who were misclassified as independent contractors, averaging \$74,045 in unreported earnings and 11.8 misclassified workers per targeted audit completed.

*During fiscal year 2016 alone, a total of 379 targeted audits were completed. Findings for the year include a total of \$47.3 million in unreported wages and 5,912 misclassified workers (average of 15.6 misclassified workers per audit).*

The random and targeted audit results demonstrate that the vast majority of registered Utah employers are reporting workers properly, with less than half of all audits resulting in a change to the original wage reports. However, there continues to be an issue with worker misclassification. In recent years, DWS/UI has focused more of its audit resources on targeted audits to increase employer compliance.

The U.S. Department of Labor (DOL) has issued repeated guidance to all state UI agencies that worker misclassification detection and enforcement is a priority. Since 2011, DOL has calculated an Effective Audit Measure Score for each state. The DOL measure is comprised of four factors: 1) Percent of employers audited annually; 2) Percent of total wage change from audit; 3) Percent of total wages audited; and 4) Average number of misclassifications detected per audit. DWS/UI achieved an effective audit score of 14.7 for the year ending March 31, 2016, surpassing both the minimal acceptable score of 7 and national aggregate of 11.9.

Based on the effective audit measure score and other determining factors, Utah was awarded a “high performance bonus” grant by the U.S. Department of Labor in

2014. The bonus was provided for achieving superior performance in the area of worker misclassification detection and enforcement by the UI Contributions Field Audit team. Only four states qualified for this; Utah achieved the second highest score nationally. This money was invested into programming that increases the capability of DWS/UI to collect benefit overpayments and audit larger employers.

Since October 2014, DWS/UI has piloted three senior auditor positions which focus primarily on implementing an employer outreach program and conducting 1099 non-match status investigations. These investigations involve employers with a large number of 1099's issued that may or may not be known to the UI system. While these types of investigations often take twice as much time to complete, with an average of 21.6 hours, they often result in a significantly higher amount of misclassified workers per audit. DWS/UI plans to continue this through fiscal year 2017 as an additional tool in combating worker misclassification.

DWS/UI continues to work with the Council partners in addressing this issue. Commerce coordinates investigations with DWS/UI when contractors are violating unemployment insurance laws. As a direct result of this partnership, DWS/UI collected \$363,994 in past-due contributions from 97 Utah employers in calendar year 2015. Labor Commission refers investigations from their hotline number and Worker's Compensation investigations. As a direct result, DWS/UI assessed \$165,637 in past-due contributions from 72 Utah employers in calendar year 2015. Tax Commission also identified and referred numerous instances where employers issued Internal Revenue Service W-2 forms to employees that were not properly reported to DWS/UI.

DWS/UI employees also referred just over 100 unemployment insurance audits to Commerce, Labor Commission, and Tax Commission, identifying about 3,862 workers who were determined to be employees, not independent contractors.

The collaboration facilitated through this Worker Classification Enforcement Council continues to support DWS/UI goal of detecting worker misclassification and enforcing state laws that ensure qualified workers receive unemployment insurance coverage.

### **The Tax Commission**

The Tax Commission continues to benefit from the Enforcement Counsel with the many referrals received from Council member agencies on misclassified workers. These referrals are investigated by the Compliance staff in the Auditing Division. When it appears that there is criminal activity involved, the case may be referred to the Tax Commission's Criminal investigation staff or to the IRS Criminal Investigation Division. When this occurs, the Tax Commission's investigators are put in contact with the investigators from workman's comp and/or the Labor commission to work jointly on a case. The Tax Commission's goal is to bring employers into compliance with the employment laws of the State of Utah and create a level playing field for all employers.

## Recommended Legislative Changes

The Council appreciates the attention the Legislature has given to worker classification issues. The Council has no specific recommendations for the 2017 legislative session.

We look forward to continuing to report annual progress, and are glad to provide any other requested information or answer any questions.

Sincerely,



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ENFORCEMENT COUNCIL,  
ACTING COMMISSIONER, UTAH  
LABOR COMMISSION



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cc: Senator Karen Mayne