

STATE REPRESENTATIVE
CHRISTINE SINICKI

1. In 2019 Gov. Evers appointed a bipartisan Task Force to examine the problem of some Wisconsin employers gaining unfair economic advantages by misclassifying their legal employees as independent contractors.
2. I and other legislators, including our Chairman here today, served on that three-year task force, along with, employers from the construction industry and other effected workforce sectors, representatives from unions and state agencies impacted by these practices.
3. The problem of misclassification is not unique to Wisconsin – employers across the country in certain industries commonly misclassify workers as "independent contractors," even when under the laws like Wisconsin's, those workers should be classified as employees.
4. This practice is illegal for a number of reasons, including:

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- Worker Misclassification denies vulnerable workers numerous legal protections and benefits such as unemployment insurance, worker's compensation, and many labor protections.
 - It can be involved in worker trafficking, and
 - Often targets vulnerable workers such as those who are undocumented.
5. The Governor's Task Force in the end recommended legislation that was condensed into four bills. They were introduced last legislative session and in the current one.
6. I will not go into more detail on AB 472, since we have experts here to talk about it, contractors who abide by Wisconsin's misclassification laws already.
7. The other three bills that will not get a hearing, again, this session, include:
- **Assembly Bill 473, which has to do with staffing of investigations of worker misclassification**

- **Assembly Bill 474**, **requiring** various methods of educating everyone about employee misclassification, and
- **Assembly Bill 475**, relating to Workers Compensation and misclassification.

###



Testimony in Support of Assembly Bill 472
Assembly Committee on Housing and Real Estate

February 14, 2023

Chairman Brooks, Vice Chair Penterman, and members of the committee, thank you for holding a hearing on Assembly Bill 472, legislation that aims to crack down on the issue of worker misclassification.

This legislation comes directly from the 2022 Joint Enforcement Task Force on Payroll Fraud and Worker Misclassification Report. Our bill requires construction contractors to be registered with the Department of Safety and Professional Services and provides additional mechanisms for the department to ensure that construction contractors are following Wisconsin's worker classification laws.

One of the first recommendations of the Task Force on Payroll Fraud and Worker Misclassification was to create an enhanced Contractor Registration Program that requires all individuals representing themselves as contractors in Wisconsin to register with DSPS before performing services. Requiring contractor registration will ensure transparency and corresponding accountability when it comes to properly classifying workers.

This is important for several reasons, as it is a first step in ensuring that everyone is following the law and is on an equal playing field when it comes to cracking down on misclassification. If we take this first step, I am hopeful the Legislature can go further to protect our workforce from employers acting in bad faith, ensure that employers following Wisconsin's worker classification laws aren't being put at a competitive disadvantage, and prevent employers from underreporting wages, which costs taxpayers and the state government millions of dollars in income and payroll taxes each year.

At a time when Wisconsin is experiencing a severe workforce shortage in so many critical sectors of our economy, it's crucial that we do everything in our power as state legislators to support workers and employers who follow the law. This is a commonsense bill that deserves bipartisan support, and I really do want to recognize and thank the committee chairman for holding this hearing. Having said that, I am happy to answer any questions the committee may have.



TASK FORCE ON
**PAYROLL FRAUD AND
WORKER MISCLASSIFICATION
REPORT**

2020

STATE OF WISCONSIN



Department of Workforce Development

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INTRODUCTION AND BACKGROUND SUMMARY

On April 15, 2019, Governor Tony Evers signed Executive Order # 20 (attached as Appendix 1), creating the Joint Enforcement Task Force on Payroll Fraud and Worker Misclassification. Governor Evers recognized that worker misclassification not only denies vulnerable workers various labor protections, worker's compensation, and unemployment benefits, but results in millions of dollars in losses to state government and taxpayers due to the underpayment of wages, unemployment insurance contributions, worker's compensation insurance, and payroll taxes. For example, the estimated amount of UI tax underreported statewide for workers misclassified as independent contractors in 2019 is over \$56 million and the average of worker's compensation benefits paid to workers injured while working for illegally uninsured employers over the past 10 years is \$2.6 million annually. In addition, the Department of Revenue estimates that potentially \$91.2 million in personal income tax revenue was forgone in 2019 due to worker misclassification as well as approximately \$50.7 million lost in business taxes from the construction industry on an annual basis. Moreover, employers that misclassify workers as independent contractors gain an unlawful competitive advantage that allows them to under-bid and out-compete law-abiding employers. Executive Order # 20 created the Task Force and charged the members with evaluating existing laws and practices to determine ways to enhance enforcement mechanisms currently used to combat worker misclassification; facilitate information sharing and investigative resources between agencies; and work cooperatively with business, labor, and community groups to raise public awareness and prevent worker misclassification through the further dissemination of educational materials and other resources.

Task Force Membership

The Task Force consists of the following members:

- ▶ Caleb Frostman (Task Force Chair), Secretary, Department of Workforce Development (DWD)
- ▶ Michael Morris, Assistant Attorney General, Department of Justice
- ▶ Maria Guerra Lapacek, Assistant Deputy Secretary, Department of Revenue
- ▶ Nathan Houdek, Deputy Commissioner of Insurance, Office of the Commissioner of Insurance
- ▶ Steve Peters, Administrator, DWD's Worker's Compensation Division
- ▶ Mark Reihl, Administrator, Unemployment Insurance Division
- ▶ Jesús Villa, Administrator, Equal Rights Division
- ▶ Rep. Rob Brooks, State Representative for Assembly District 60, Wisconsin State Assembly
- ▶ Senator Dave Hansen, Senator for Senate District 30, Wisconsin State Senate
- ▶ Senator Dale Kooyenga, Senator for Senate District 5, Wisconsin State Senate
- ▶ Rep. Christine Sinicki, State Representative for Assembly District 20, Wisconsin State Assembly
- ▶ Pete Braun, President and CEO, Wall-Tech
- ▶ Cynthia Buchko, General Counsel, Construction Business Group
- ▶ Andy Buck, Government Affairs Director, Painters and Allied Trades District Council 7
- ▶ Tim DeMinter, Business Manager, Financial Secretary/Treasurer, Ironworkers Local 383
- ▶ Gary Rockweiler, Vice President and CEO, Rockweiler Insulation Inc.
- ▶ Jerry Shea, President, Market and Johnson
- ▶ Steuart Wilson, Business Representative, Sheet Metal, Air, Rail, and Transit

The Executive Order also directed the Task Force to review the work of the Worker Misclassification Task Force established by the Department of Workforce Development (DWD) in 2008 and review the recommendations contained in the June 2009 report.

Efforts in Response to the Recommendations in the 2009 Task Force

The DWD Secretary created the Worker Misclassification Task Force in October 2008 to examine problems relating to worker misclassification and recommend administrative and legislative approaches to address those problems. The 2008-2009 Task Force was composed of individuals representing the interests of workers and business communities in industries affected by misclassification, as well as representatives from DWD's Unemployment Insurance and Workers Compensation Divisions, the Department of Revenue and the Department of Commerce.

The 2008-2009 Task Force heard from stakeholders impacted by worker misclassification, enforcement personnel, and experts from other states to determine the best practices to address the problems of misclassification. The 2008-2009 Task Force weighed a wide range of options to develop recommendations that would be the most effective strategies for Wisconsin. The 2008-2009 Task Force made the following eight recommendations:

- ▶ **Recommendation 1:** Create an Office of Worker Misclassification; empower the Office to issue stop work orders.
- ▶ **Recommendation 2:** Increase information sharing among state agencies.
- ▶ **Recommendation 3:** Support the operations of the Department of Commerce Builder Contractor Registration (BCR) program.
- ▶ **Recommendation 4:** Establish a "hotline" to facilitate reports from workers, contractors, and the general public about misclassification abuses.
- ▶ **Recommendation 5:** Undertake an aggressive campaign to educate contractors and the general public about misclassification issues.
- ▶ **Recommendation 6:** Withhold 2% on form 1099 payments made by contractors to subcontractors, including individuals operating as independent contractors.
- ▶ **Recommendation 7:** Provide significant penalties for contractors actively seeking to subvert and avoid proper classification of workers.
- ▶ **Recommendation 8:** Conduct additional study of other policy options designed to combat worker misclassification.

Seven out of the eight recommendations contained in the June 2009 final report were implemented in Wisconsin. The only recommendation that was not implemented was the recommendation to withhold 2% on form 1099 payments made by contractors to subcontractors, including individuals operating as independent contractors. Despite the recommendation of the Task Force, the Department of Commerce BCR program was eliminated in July 2013.

The complete 2009 Report of the Worker Misclassification Task Force is available here: dwd.wisconsin.gov/misclassification/pdf/2009-task-force-report.pdf

ACTIVITIES OF THE 2019 JOINT ENFORCEMENT TASK FORCE ON PAYROLL FRAUD AND WORKER MISCLASSIFICATION

The Task Force held six meetings at locations throughout Wisconsin from August 2019 through February 2020. Due to the number of agencies that have potential jurisdiction over the issue of misclassification, and the vast reach of its consequences impacting both workers and business across agencies and programs, the Task Force focused its initial efforts on ensuring Task Force members had a clear understanding of the current state of worker classification in Wisconsin and current efforts to address the issue of worker misclassification.

Governor Evers kicked off the first meeting of the Task Force on August 28, 2019. At that meeting, Task Force members received an overview of the 2009 report and heard presentations from DWD's Unemployment Insurance, Worker's Compensation, and Equal Rights Divisions on the current state of worker misclassification. Members discussed areas where additional information/-data was necessary to gain a better understanding of specific issues and to develop potential solutions.

The Task Force held its second meeting on September 25, 2019 in Wisconsin Rapids where members learned about the tests and standards used to determine whether a worker is an independent contractor or an employee and heard perspectives from key program experts on the advantages and limitations when applying the different tests.

At the following meetings held in Madison, Milwaukee, and La Crosse, the Task Force enlisted outside experts from the National Employment Law Project (NELP), National Legal Advocacy Network, and UMOS to educate Task Force members on other adverse consequences resulting from worker misclassification such as human trafficking and to highlight the different strategies and best practices utilized by other states, such as the New York State Joint Enforcement Task Force.

The Task Force also examined existing investigation and enforcement policies, and the procedures utilized by Wisconsin state agencies and associated entities to identify and combat worker misclassification. See Appendix 4 for all meeting materials.

THE EXTENT AND COSTS OF MISCLASSIFICATION AND RECOVERY EFFORTS

In addition to learning about the investigation and enforcement processes, the Task Force evaluated the amounts of taxes, penalties, and collections resulting from those activities. Misclassification not only negatively affects workers and employers who comply with the law, it also has a negative impact on state government. To quantify the adverse consequences of worker misclassification and demonstrate the effect worker misclassification has on state resources, the Task Force was provided data and statistics on the results of investigation and enforcement efforts from: DWD's Unemployment Insurance Division – Field Audit and Worker Classification Sections; DWD's Worker's Compensation Division; DWD's Equal Rights Division; the Wisconsin Compensation Rating Bureau; the U.S. Department of Labor – Wage and Hour Division; and the Wisconsin Department of Revenue.

DWD Unemployment Insurance Division – Field Audit Section

To calculate the estimated cost of misclassification on the UI program, the UI Division provided Task Force members metrics from its Field Audit and Worker Classification Sections.

Based on UI audit data, the estimated amount of underreported taxes statewide for workers misclassified as independent contractors increased from \$16,609,705 (3.8% of total UI taxes collected statewide) in 2000 to \$56,950,205 (10.2% of total UI taxes collected statewide) in 2019. See Appendix 2 for additional details.

UI also provided information on industries with the highest percentage of misclassified workers. Based on UI audit assignments from January 1, 2013 to November 1, 2019, the industries with the highest percent of misclassified workers found include:

- ▶ Educational Services, having misclassified workers found at 47.58% of audits;
- ▶ Agriculture, Forestry, Fishing and Hunting having misclassified workers found at 47.2% of audits; and
- ▶ Real Estate and Rental and Leasing having misclassified workers found at 45.53% of audits.

Over 40% of UI audits of employers in the construction industry discovered misclassified workers and that industry included the highest total number of individual workers being misclassified. See Appendix 2 for additional details.

DWD Unemployment Insurance Division – Worker Classification Section

The UI Worker Classification Section conducts proactive field investigations at construction worksites and a variety of other businesses. Approximately 61% of the Section's investigations are at construction sites. From the time the UI Worker Classification program was initiated in May 2013 through January 2020, misclassification investigators conducted 2,740 worker classification investigations, resulting in 622 audits and the identification of 8,274 misclassified workers. This resulted in the assessment of more than \$2.7 million in UI taxes and interest. As of January 2020, \$66,000 in administrative penalties have been issued in 13 cases for intentional misclassification. The UI Tax Field Audit Section identified an additional 43,174 misclassified workers since 2013 resulting in tax assessments and interest of \$12.6 million.

The tax field auditors and worker classification investigators perform follow-up activities for continued noncompliance by employers through daily operations and special follow-up by the UI Division's Worker Classification Section on referred employers.

DWD Worker's Compensation Division

Worker misclassification can lead to a loss of premiums for the insurance industry and higher premiums passed onto insured businesses. The Worker's Compensation Division is unable to estimate the total costs to the worker's compensation program resulting from worker misclassification but identified the amount of insurance premiums generated by new employers brought into compliance, much (but not all) of which is related to misclassification. From 2009 to 2018 over \$13.7 million in additional insurance premiums were generated from employers brought into compliance. See Table 1 & Chart 1 in Appendix 3 for additional details.

The Worker's Compensation Division has a team of seven consumer protection investigators who conduct investigations to help ensure that employers subject to the Worker's Compensation Act have proper worker's compensation insurance coverage. These investigators conduct approximately 22,000 investigations annually and issue about 200 penalties per month. The average penalty resulting from an investigation is \$2,567 and the Worker's Compensation Division assesses around \$5.5 million in penalties annually.

The Uninsured Employers Fund (UEF) pays worker's compensation benefits on claims filed by employees injured while working for illegally uninsured employers. Payments vary substantially from year-to-year, depending on the severity of claims accepted. The annual average for the last 10 full years is \$2.6 million. The Worker's Compensation Division investigates and issues penalties against illegally uninsured employers to recover funds for UEF. There were approximately 226 injuries in UEF claims from 2009-2019, of which 134 (or 59%) were covered by nine industries. The industries with the highest number of UEF injuries from 2009 – 2019 (those with four or more injuries during the 10-year period) include:

- ▶ Construction
- ▶ Trucking
- ▶ Automotive
- ▶ Bus Co.
- ▶ Tree Pruning, Spraying and Repairing
- ▶ Restaurant
- ▶ Healthcare
- ▶ Landscape, Gardening & Drivers
- ▶ Farm Products

See Chart 2 in Appendix 3 for additional details.

There were approximately 15,539 UEF penalties issued against employers during 2009-2019. The top 10 industries (those with over 500 penalties, which together account for 11,078 or 71% of the total penalties) include:

1. Clerical Office Employees (not otherwise classified)
2. Restaurants
3. Salesperson or Collectors, Outside
4. Construction
5. Child Day Care Center
6. Bar/Nightclub
7. Store Retail (not otherwise classified)
8. Healthcare
9. Barber Shop/Beauty Parlor/Hair Styling Salon
10. Trucking

See Chart 3 in Appendix 3 for additional details.

The Worker's Compensation Division is able to identify repeat offenders when it discovers any employer with multiple penalty accounts (vs. injury reimbursement accounts). There were approximately 2,475 multiple penalty accounts for employers from 2009-2019. Eleven industries account for 56% of all employers that were assigned multiple penalty accounts during that time period. *See Chart 4 in Appendix 3 for additional details.*

DWD Equal Rights Division

The Equal Rights Division (ERD) enforces over 40 state laws covering labor standards and civil rights in employment, housing, and public accommodations. The ERD also provides research and technical assistance to employers on how to comply with those laws. ERD staff investigate complaints, identify law violations, work to resolve disputes among parties, and make determinations of liability. The ERD is only able to address worker misclassification to the extent it relates to other labor standards issues, such as wage theft and minimum wage violations. As a result, the ERD cannot actively seek out worker misclassification cases and, while it does not maintain statistics on the matter, anecdotally the ERD receives approximately 15 complaints a month on wage and hour matters where worker classification is an issue. Last year, the Equal Rights Division processed over 4,000 complaints and recovered over \$1.1 million in wages owed to Wisconsin workers.

The Task Force also received overviews from the Department of Revenue, Office of the Commissioner of Insurance, Wisconsin Compensation Rating Bureau and U.S. DOL on their procedures for investigating and identifying worker misclassification and metrics on the effectiveness of their enforcement efforts.

Department of Revenue

The Department of Revenue estimates that potentially \$91.2 million in personal income tax (PIT) revenue was forgone in 2019 due to worker misclassification. This amount was calculated using DWD's estimated total of taxable wages underreported statewide based on UI audit data of \$1.85 billion and an effective tax rate of 4.93% (the average rate for all workers) for calendar year 2019. Total underreported wages could be higher than \$1.85 billion to the extent that total wages paid exceed the \$14,000 per employee per employer limit for wages subject to UI tax. This could result in the upper limit of foregone PIT being greater than \$91.2 million.

However, the actual amount of foregone revenue is likely to be less than \$91.2 million for two reasons:

- ▶ First, for state personal income tax purposes, a worker who is misclassified as an independent contractor may still pay tax on their income by reporting a 1099-MISC instead of a W-2. Consequently, unreported income for PIT is likely to be significantly less than unreported wages for UI. PIT revenue will be foregone to the extent that earnings are altogether unreported, not just improperly reported for a misclassified worker.
- ▶ Second, some workers who are paid in cash may have a total income low enough that they would not have a filing requirement for personal income tax (for tax year 2019, a tax return is not required for a gross income level below \$11,560 for filing single, or \$21,510 if married filing jointly). It's also possible that a worker's income could be low enough to qualify for the refundable earned income tax credit, in which case not only would they not have a net tax liability but they could receive a payment from the state, an additional cost to the state from worker misclassification.

In addition to the potential \$91.2 million in forgone income taxes on unreported wages, the Department of Revenue estimates that there is roughly a \$50.7 million loss in business taxes from the construction industry on an annual basis.

DOR used IRS tax gap data and some assumptions to determine the amount of forgone business tax revenue for the construction industry. DOR focused on the construction industry due to the high potential of worker misclassification and the prevalence of misclassified workers found in that industry.

Based on information in the IRS 2019 Tax Gap report, the tax gap related to business income for individuals is equivalent to approximately 10.6% of net collections. A similar measure for small corporations suggests an underreporting tax gap of 4.2% among corporate tax filers. Construction businesses make up approximately 1.5% of net tax collections for corporations in Wisconsin, while construction companies make up 4.6% of state GDP. The Department of Revenue does not have information on the industrial mix of business income reported by individuals. Assuming 5.0% of business income is attributable to construction businesses, DOR estimates that forgone taxes on business income from the construction industry is about \$50.7 million on an annual basis.

Barriers to Interagency Enforcement, Coordination, and Data Sharing

To get a first-hand perspective on the challenges faced when combating worker misclassification, the Task Force enlisted the expertise of agency staff to discuss pain points they experience relating to worker misclassification prevention and enforcement, and what obstacles prevent them from addressing those issues as effectively as possible. Agency staff informed the Task Force members of the coordinated activities and data sharing that occurs between agencies but explained that there are areas where additional information is needed to improve investigation and enforcement.

Some of the most common barriers to the efficient exchange of information between agencies are the confidentiality restrictions imposed on certain types of data and information. Unemployment insurance records are generally confidential under federal and state law and cannot be disclosed unless specific exceptions apply. Confidential UI records may be shared with most governmental entities at the local, state, and federal levels only if certain legal requirements are met.

Similarly, Wisconsin worker's compensation law provides that any record maintained by DWD that reveals the identity of an employee who claims worker's compensation benefits, other injury or medical information relating to a worker's compensation claim, and any financial information provided to DWD by an employer regarding self-insurance are generally confidential and not open to public inspection. Additionally, no information from the Wisconsin Compensation Ratings Bureau (WCRB) about worker's compensation insurance coverage, including the names of insured employers, employer addresses, business status, type, dates of coverage, manual premium code, policy numbers, cancellations, terminations, endorsement and reinstatement dates, obtained by DWD may be made public by the department except as authorized by the WCRB.

Utilizing Existing Successful Mechanisms to Prevent Worker Misclassification

There are several practices currently in place to encourage compliance. DWD has developed a multi-faceted program to ensure that workers in Wisconsin are properly classified. The program consists of these elements: worksite investigations and employer audits; active collaboration with other government agencies on worker classification issues; a website that provides guidance to workers and employers on worker classification; and public outreach and educational activities. The Task Force recommends continuing to use the strategies that have proven effective through the years but also looking for opportunities to build on the success of those efforts.

Recommendations

Worker misclassification is a nation-wide problem and each state's approach to solving it may be different based on what methods are best suited for that state. The Task Force heard recommendations from outside experts on best practices employed by other states and took those into consideration when developing recommendations for this report.

Recommendation 1: Create an enhanced Contractor Registration Program that requires all individuals representing themselves as contractors in Wisconsin to register with the Department of Safety and Professional Services (DSPS) before performing services.

Require that all individuals performing construction or improvement services register with the Department of Safety and Professional Services before performing services in Wisconsin.

- ▶ Require the following basic information for registration: 1) name, contact information, and physical address for the business principal, 2) a business registration with the Department of Financial Institutions (DFI), 3) a valid UI account, and 4) proof of a worker's compensation policy.
- ▶ Require a minimal fee that would cover the cost of administering the program.
- ▶ Include in the registration process a form that requires acknowledgment of worker classification laws and penalties to ensure registered contractors are aware of their obligations under the law.

Background: The 2008-2009 Task Force recommended supporting the operations of the Department of Commerce Builder Contractor Registration program. Despite the 2008-2009 Task Force's recommendation, that program was eliminated in July 2013.

Worker misclassification investigators, field auditors, and other key program experts indicated a public database that lists the status of all contractors (registered/suspended) in the state would be of great assistance identifying employers and workers during misclassification investigations. Task Force members also expressed the benefit to members of the public who wish to select and support law-abiding contractors.

NOTE: Additional information regarding the Construction Contractor Registration program is included under the "Penalties" section in Recommendation 4.

Recommendation 2: Create an Interagency Coordinated Enforcement Team, consisting of the Departments of Workforce Development, Revenue, Justice, and Financial Institutions and the Office of the Commissioner of Insurance, to address interagency coordination and data sharing improvements to the extent permitted by law.

- ▶ Require Team to meet regularly to address confidentiality restrictions and improve the sharing of data necessary for coordinated investigation and enforcement actions by reviewing and updating memorandums of understanding between appropriate agencies and developing recommendations and systems to address data-sharing needs.
- ▶ Direct Team to develop recommendations targeting insurance fraud, including a data sharing agreement between the Worker's Compensation Division and worker's compensation insurance providers to allow the results of insurance company audits to be reported to DWD.
- ▶ Require Team to report to the Task Force at least annually on its activities and recommendations.

Background: Facilitating and engaging in the systematic exchange of data relating to worker misclassification between appropriate agencies was a charge for the Task Force included in Governor Evers' Executive Order, a recommendation of the 2008-2009 Task Force, and a best practice recommended by outside

experts. While state agencies involved in the Task Force can and do share data to the extent permitted by law, the Task Force identified areas where the coordinated exchange of information could be improved to better facilitate worker misclassification investigations and enforcement efforts.

Recommendation 3: Increase the capacity of the Department of Workforce Development to investigate and enforce the laws regarding worker classification.

- ✦ Authorize new positions to hire more UI field auditors.
- ✦ Require DWD's UI Division, with the assistance of Department of Administration's Division of Personnel Management, to review all recruitment and on-boarding processes to ensure that auditor positions are properly classified and are keeping pace with comparable positions and the associated compensation in the labor market.
- ✦ Direct DWD to review the current resources available to investigators and auditors to evaluate additional strategies and improvements that could be implemented with increased resources, such as the following:
 - Cross training of agency investigators (worker's compensation investigators, UI worker classification investigators, field auditors, etc.);
 - More bilingual staff; and
 - IT improvements that will allow the more efficient exchange of information.

Background: Hiring additional UI field auditors would increase the number of audits completed, provide a greater presence in the employer community, and improve the turnaround time of these audits. Audit visibility is a crucial aspect of compliance and creating a "fair playing field" for all employers. Because audits that identify misclassification are typically more time consuming, additional staff would increase the likelihood of identifying worker misclassification while assisting the field audit section in meeting the Effective Audit Measure (EAM) required by the U.S. Department of Labor. UI field auditors' salaries have not kept pace with other state agencies with staff performing similar audit functions, which has made recruitment and retention of field auditors difficult.

Recommendation 4: Develop Penalty Structure for Worker Classification Violations that Deter Repeat Violations

- ✦ Create escalating penalties for repeat violators of non-compliance with worker's compensation law and to "scale" the penalties by the size of the business (i.e., number of workers).
- ✦ Expand the intentional misclassification penalty for violations of the unemployment insurance program to other industries and eliminate monetary caps on the current intentional misclassification penalty.
- ✦ Create an escalating administrative penalty for repeat offenders (e.g., penalties double for second violation with no monetary cap and continued referral for criminal prosecution for second and subsequent violations).
- ✦ Utilize the reconstituted Construction Contractor Registration program to ensure construction contractors are complying with the law.

DSPS would assess a penalty for contractors performing services in the state without being registered. In addition, DSPS would establish penalties for contractors that hire an unregistered or suspended contractor under the Construction Contractor Registration program to include escalating penalties for continued violations up to suspension or revocation of a contractor's own registration and/or disqualification from being eligible to bid on any public project (state, municipal, school district) or certain tax credits.

NOTE: local municipalities' building inspectors could be a resource to verify a contractor is registered to assist with enforcement efforts.

Allow for waiver of part or all of the penalty for first-time violations if the contractor comes into compliance within a specified amount of time.

Background: Wisconsin's worker's compensation law provides an employer that does not obtain and maintain a worker's compensation insurance policy as required may be subject to a penalty of double the insurance premiums they should have been paying during the uninsured period, or \$750, whichever is greater. The penalty has been in effect since January 1990 and the majority of employers penalized for failure to carry worker's compensation insurance are never penalized again; however, there are employers in the state with multiple penalties (some exceeding 10). This suggests that the current penalty for failure to carry worker's compensation insurance is sufficient in most cases to deter non-compliance but there are employers who accept the risk of being penalized as the "cost of doing business."

The intentional misclassification penalties for unemployment insurance have been in effect since October 2016. The penalties for construction employers who knowingly and intentionally provide false information to DWD for the purpose of misclassifying or attempting to misclassify an employee, are \$500 for each employee who is misclassified, not to exceed \$7,500 per incident. In addition, the criminal penalty for intentional misclassification by construction employers is a fine of \$1,000 for each employee misclassified up to a maximum fine of \$25,000 for each violation. There is also a separate administrative penalty for construction employers who coerce individuals to adopt non-employee status.

Currently, the penalties for intentional misclassification for unemployment insurance only apply to the construction industry; however, data shows misclassification is occurring in other industries as well. In many cases, the penalties are being treated by construction employers as a cost of doing business.

Recommendation 5: Educate Workers and Employers on the Rules, Requirements, and Penalties Associated with Worker Misclassification

- ▶ Require the Department of Financial Institutions to include informational materials and resources on worker misclassification with new business registrations.
- ▶ Require DWD to design work site posters that employers must display with information on worker classification laws, requirements, and penalties for non-compliance.
- ▶ Expand DWD's worker classification website to an all-state agency website that explains the common elements of all employee classification tests and lists information on who to contact with questions.
- ▶ Direct agencies to provide more targeted multilingual educational outreach to employers, workers, and allied organizations that serve vulnerable populations. Emphasize in the communications who to contact and the protection of anonymity to help overcome fear of retaliation.
- ▶ Direct OCI to educate insurance professionals on misclassification issues so they can identify potential violations and report them to the appropriate agency.
- ▶ Develop a communication plan that coordinates activities around Labor Day, such as PSAs, conferences, etc. to call attention to the issues of worker misclassification.

Background: DWD and other agencies currently have robust education and outreach efforts to inform employers and workers on worker misclassification issues, but the Task Force saw opportunities to build on those effort to further prevent worker misclassification through improved education and outreach.

Topics for Further Discussion and Study by the Governor's Task Force

The Task Force has identified several topics of interest that it intends to further examine during future meetings that may inform future recommendations.

1. Increased education, outreach, and enforcement of labor trafficking issues.
2. Options of making public repeat violators of UI, WC, and tax violations while addressing due process concerns and federal confidentiality requirements.
3. Deterrence of worker's compensation insurance premium fraud.
4. Evaluations of other states' worker classification tests and the outcomes from implementing a new test. In addition, re-examine the experiences with Wisconsin's worker classification tests after the other recommendations of the Task Force have been implemented to assess whether a revised test would be beneficial.
5. Greater partnerships and outreach opportunities with community groups.
6. Allowing DWD's Equal Rights Division to investigate third-party violations of labor standards and civil rights laws without the need for an individual who has been wronged to bring forward the complaint.
7. Explore education and resources that can assist businesses with bringing themselves into compliance.
8. Explore strict liability as a means of enforcement.
9. Examine existing DFI registration requirements for the purposes of enforcing worker misclassification laws.

The Task Force plans to engage the Unemployment Insurance Advisory Council (UIAC), Worker's Compensation Advisory Council (WCAC), and stakeholder groups to gather their views and input on implementing the proposed recommendations and solutions.

Conclusion

Over the past year, the Task Force evaluated the current efforts by Wisconsin state agencies to combat worker misclassification, studied the best practices implemented in other states to identify areas for improvement and determined which strategies would be effective in Wisconsin. During their evaluation, the Task Force identified key issues that needed to be addressed to increase compliance with worker classification laws, which are: the need for improved access to information and more efficient sharing of data and communication between relevant entities; greater interagency coordination; increased penalties to hold repeat violators accountable; and the need for expanded outreach and education with specific attention on vulnerable populations.

The recommendations presented in this report were the items the Task Force members agreed should be the primary focus for addressing those key issues but encourage continued study of additional measures that could be taken to combat worker misclassification. Going forward, the Task Force will focus on worker's compensation insurance premium fraud, the feasibility of establishing single employee status tests across all agencies and programs, combating labor trafficking in connection with worker misclassification, and additional ways to foster interagency collaboration and enforcement efforts.

The Task Force looks forward to working with the Governor's Office, the Legislature, other agencies, UIAC and WCAC, and stakeholders to implement these recommendations and develop solutions to further combat worker misclassification.

APPENDIX

Appendix 1 – Executive Order



EXECUTIVE ORDER #20

**Relating to the Creation of the Joint Enforcement Task Force on Payroll
Fraud and Worker Misclassification**

WHEREAS, a significant number of employers in Wisconsin and elsewhere are improperly classifying individuals they hire as "independent contractors" even when those workers should be classified as employees;

WHEREAS, in 2009 the Wisconsin Department of Workforce Development, Unemployment Insurance Division found that 44% of the workers investigated during employer audits had been misclassified as independent contractors;

WHEREAS, from January 2016 to April 2019, the Worker Misclassification Section of the Department of Workforce Development conducted 1,963 investigations, with 422 resulting in audits. The 422 audits found 5,841 workers misclassified, found under-reported gross wages of almost \$70 million, and assessed approximately \$1.8 million in unemployment insurance taxes, interest, and penalties;

WHEREAS, worker misclassification denies vulnerable workers legal protections and benefits;

WHEREAS, this fraudulent practice also results in millions of dollars of losses to state government and taxpayers due to underpayments of wages, unemployment insurance contributions, worker's compensation insurance, and payroll taxes;

WHEREAS, employers that misclassify workers as independent contractors gain an unlawful competitive advantage that allows them to under-bid and out-compete law-abiding employers;

WHEREAS, enforcement activities in this area have historically been divided among different agencies, which can reduce the efficiency and effectiveness of enforcement without intentional collaboration;

WHEREAS, research and experience in other states suggest that enforcement efforts to address the problem of misclassification can be enhanced and made more efficient through interagency cooperation, information-sharing, and joint enforcement efforts against serious violators; and

WHEREAS, research and experience in other states suggest that the creation of a joint task force has proven to be an effective mechanism for coordinating, enhancing, and streamlining enforcement in this area.

NOW, THEREFORE, I, TONY EVERS, Governor of the State of Wisconsin, by the authority vested in me by the Constitution and the Laws of the State, including Section 14.019 of the Wisconsin Statutes, do hereby create the Joint Enforcement Task Force on Worker Misclassification ("Task Force") and order the following:

Testimony of Mr. Greg Wolf in Favor of AB 472

My name is Greg Wolf, and I am the owner and President of Schmelzer Paint Company, Inc. Schmelzer Paint is a commercial/ industrial painting contractor located in Madison, Wisconsin who just celebrated 75 years in business. I am also the President and co-founder of the Wisconsin Finishing Contractors Association, which represents the interests of commercial finishing contractors, their employees and the finishing industry.

The construction industry is under attack. There are literally hundreds of what I call Labor Brokers—because these people are not legitimate contractors—that are operating in this state without regard for the law. Out of state contractors are also having a field day with our lack of regulations and registration.

Labor Brokers engage in payroll fraud. Payroll fraud starts with the misclassification of workers. I personally do not like the word misclassification. It implies a mistake between reporting someone as an employee versus an independent contractor. Let me be clear, there is no mistake. Labor Brokers do not report their workers as employees or independent contractors. They pay them cash under the table, which allows them to evade their income, payroll and unemployment tax obligations. They also have no workers compensation insurance, which means that when the people working for them get injured, the rest of us cover the cost of their health care services.

According to a report issued by the State of Wisconsin, payroll fraud results in over \$200 million annually—let me repeat that, \$200 million annually—in unpaid tax that is unjustly kept by bad actors not paying their fair share. In the construction world, Labor Brokers undercut law-abiding contractors, like myself. Their prices are easily a third lower than mine because they are breaking the law. Companies like mine will either be out of business before too long or decide to cheat like the competition. Neither option is good for Wisconsin.

Recently, the IRS convicted a Wisconsin Labor Broker. He tried to halt IRS collection for years by operating his businesses through nominee entities, meaning companies that legally existed but were not legitimate. He also avoided IRS liens and levies by operating in large amounts of cash that he received from cashing checks at different establishments. This Labor Broker owes the IRS over a half million dollars in unpaid tax. What is so frustrating for a business owner like me is that the same Labor Broker owes the State of Wisconsin over **\$2 million** in unpaid income tax and unemployment tax. I have attached a listing of the public CCAP listings proving what this Labor Broker owes Wisconsin.

I have personally interviewed several of these labor brokers(not knowing that's what they were) in an attempt to hire more staff. They had no interest in anything legitimate and they had no legal documentation to work here. The last one I interviewed three weeks ago had access to 20+ workers for the next day if needed. He also claimed to have worked for our competitors. The problem is growing exponentially and all our legitimate contractors have experienced the same issues.

Other states are cracking down on payroll fraud. It is time Wisconsin did too. The contractor registry in AB 472 will not solve the entire problem, but it is a small step in the right direction. It will make it harder for Labor Brokers to operate and provide the enforcement teeth necessary to curtail bad actors. I urge you to support AB 472 to protect honest business owners, the construction industry and all Wisconsin taxpayers.

Thank you for your time today.

Sincerely,
Greg Wolf

A handwritten signature in cursive script that reads "Greg Wolf".

Schmelzer Paint Co., Inc
President

Date	Agency	Case No.	Amount	Notes
7/29/2015	DWD Unemployment Division	2015UC0677 (Dane County)	\$ 8,395.97	Against Mr. Reyes Personally; paid 2/23/2016
12/9/2015	DWD Unemployment Division	2015UC1059 (Dane County)	\$ 4,048.75	Against Mr. Reyes Personally; paid 1/23/2017
6/1/2018	DWD Unemployment Division	2018UC260 (Dane County)	\$ 163,957.72	Against Elite Drywall; remains unpaid
11/5/2018	DWD Unemployment Division	2018UC0690 (Dane County)	\$ 171,658.92	Against Mr. Reyes Personally; remains unpaid
6/12/2020	DOR	2020TW862 (Dane County)	\$ 2,069.24	Against Mr. Reyes Personally; paid 9/26/2022
6/12/2020	DOR	2020TW860 (Dane County)	\$ 35,945.00	Against Mr. Reyes personally; remains unpaid
6/12/2020	DOR	2020TW857 (Dane County)	\$ 42,767.43	Against Mr. Reyes personally; remains unpaid
6/16/2020	DOR	2020TW1819 (Dane County)	\$ 8,042.60	Against Mr. Reyes personally; remains unpaid
6/16/2020	DOR	2020TW1814 (Dane County)	\$ 316,074.48	Against Mr. Reyes personally; remains unpaid
11/30/2020	DOR	2020TW1798 (Dane County)	\$ 7,132.51	Against Mr. Reyes personally; remains unpaid
8/31/2021	DOR	2021TW1227 (Dane County)	\$ 6,900.01	Against Mr. Reyes personally; remains unpaid
12/10/2021	DWD Unemployment Division	2021UC1007 (Dane County)	\$ 486,194.17	Against Elite Drywall; remains unpaid
1/5/2022	DWD Unemployment Division	2022UC8 (Dane County)	\$ 488,912.03	Against Mr. Reyes personally; remains unpaid
1/11/2022	DWD Unemployment Division	2022UC54 (Dane County)	\$ 36,674.22	Against Royal LLC; remains unpaid
4/21/2022	DWD Unemployment Division	2022590 (Dane County)	\$ 2,430.57	Against Royal LLC; paid 6/6/2022
11/21/2022	DWD Unemployment Division	2022UC2215 (Dane County)	\$ 2,466.71	Against Royal LLC; remains unpaid
3/10/2023	DWD Unemployment Division	2023UC369 (Dane County)	\$ 2,462.85	Against Royal LLC; remains unpaid
4/17/2023	DWD Unemployment Division	2023UC535 (Dane County)	\$ 2,481.85	Against Royal LLC; remains unpaid
6/6/2023	DWD Unemployment Division	2023UC747 (Dane County)	\$ 456,367.35	Against Elite Drywall; remains unpaid
6/27/2023	DWD Unemployment Division	2023UC838 (Dane County)	\$ 24,488.83	S & L Insolation Drywall LLC (not named in the federal indictment but owned/controlled by Mr. Reyes); remains unpaid
			\$ 2,269,471.21	

Testimony of Matt Marcellis

Executive Director of the Allied Construction Employers' Association

in Favor of 2023 AB 472

February 14, 2024

My name is Matt Marcellis. I am the Executive Director of the Allied Construction Employers Association (ACEA), an organization that represents the interests of hundreds of Wisconsin construction contractors employing thousands of Wisconsin construction workers. ACEA affiliated contractors employ a wide range of construction trades, including brick and cement masons, carpenters, iron workers, laborers, operating engineers, and painters, among others. In 2023, ACEA contractors reported over 5 and a half million hours worked, representing billions of dollars in wages paid. ACEA contractors help build Wisconsin and drive its economy. I appreciate the opportunity to speak before you today.

The construction industry in Wisconsin faces many serious challenges. Today, you are in the unique position of being able to help Wisconsin confront one of these challenges. AB 472 is a step in the right direction, and as an Air Force veteran, defender of free and fair markets, and, most importantly, a staunch believer in the rule of law, I urge you to support the bill.

Payroll fraud—which consists of income tax evasion, unemployment insurance fraud, workers' compensation fraud, and failure to pay overtime rates—has infiltrated the construction industry over the last decade. Illegally operating entities steal \$200 million annually from Wisconsin by failing to pay taxes that law-abiding businesses do. Much of this theft is occurring in the construction industry.

However, it is not just the State of Wisconsin and taxpayers that are victims of payroll fraud. A 2021 peer-reviewed study concluded that payroll fraud in the construction industry is costing the insurance industry \$26 million annually in unpaid worker's compensation insurance premiums. When a worker is not properly classified as a full-time employee and instead is paid in cash, the employer is likely not reporting that worker for insurance purposes. This is insurance premium fraud, which is illegal. For the largest member contractors in ACEA, these insurance costs can easily run to over \$1 million per year. In addition to placing workers at greater risk, insurance premium fraud represents a massive

economic loss to the State's worker's compensation and unemployment insurance systems.

Then there is the issue that companies engaging in payroll fraud also often disregard paid overtime laws. During busy times, ACEA members will have overtime on around 20-25% of their projects, paying a minimum of time and a half for those hours, which represents a massive economic investment in their workers and additional tax revenue for Wisconsin. Bad actors ignore this requirement.

These types of payroll fraud give at least a 33% competitive advantage over law-abiding businesses. And as ACEA's members universally offer strong middle-class wages, sponsor registered apprenticeship programs, and offer excellent retirement and health benefits, that competitive advantage is very likely even higher. And make no mistake, payroll fraud is not about making tough calls and applying complicated laws to ambiguous facts. Rather, it is a deliberate choice to ignore the law to gain an advantage over law-abiding competitors, increase profits, and avoid the financial risks honest entrepreneurs must accept. This unfair advantage has caused some larger ACEA members to avoid certain sectors of the construction industry, such as residential and light commercial, altogether. For other members, this results in being unable to compete financially in certain sectors unless it is to come in to fix mistakes after a poorly qualified, often out of state, contractor has left. Finally, and worst of all, numerous small, family-owned construction firms have been forced entirely out of business by this problem. These are locally owned Wisconsin businesses. Businesses whose owners live here, spend their money here, and employ people from here, the exact type of "little guy" our laws are supposed to protect the most. Businesses who cannot compete because bad actors, often coming from out of state, are willing to ignore Wisconsin's laws.

Why is payroll fraud so prevalent in the construction industry? I believe one reason is because it is easy for these bad actors to hide. For a large, commercial construction project, you will have a general contractor, a handful of first-tier subcontractors and then dozens of second, third, or even fourth-tier subcontractors. The employees who are paid cash off-the-books do the most labor-intensive work like drywall hanging and finishing, painting, and floor covering. These are the workers most in need of the protections offered by our state's workers' compensation and unemployment requirements and our overtime laws. They are often also the workers that are most easily taken advantage of.

AB 472 would help level this unfair playing field and protect Wisconsin workers by making it more difficult for those seeking to skirt the law to operate in Wisconsin. Project owners and general contractors would be able to ensure that they are only hiring legitimate subcontractors. And the State would have the enforcement right to keep bad actors from being registered so that only those firms willing to meet their legal and ethical financial obligations could work in Wisconsin.

Residential construction contractors have to be registered in Wisconsin to protect homeowners from unscrupulous business practices. That is good public policy and should be extended. AB 472 offers this same protection in the commercial construction space where ACEA's members operate. It helps protect the construction industry and all taxpayers from payroll fraud.

Thank you again for the opportunity to be here today.