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BANKRUPTCY WHEN BANKRUPTCY IS NOT THE BEST OPTION DETERMINING WHEN

Family and Foster Care

Inter-American Commission on Human Rights' Domestic-Violence Ruling

U Visa Protections for Immigrant Victims

State Revenue from Persons Accused or Convicted of Crimes

Independent-Contractor Misclassification

Relief from Student Loan Debt

Mobile Banking for the Unbanked

And Stories from Advocates:

Due Process Procedures for Authorizing Medicaid Services in North Carolina

Ending Ohio's Backlog in Processing Medicaid Applications

FEMA's Postdisaster Grant Recoupment in Louisiana



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IDENTIFYING MISCLASSIFIED WORKERS

Lessons Learned from Maryland's Workplace Fraud Act

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Joe is a construction worker at ABC Contracting Incorporated. ABC dictates Joe's work hours, supplies his materials, and gives him daily directions for how to complete his work. He is paid by check every week, but no deductions are taken out of his pay. One day a piece of drywall falls on Joe, and he falls awkwardly on his knee. He goes to the hospital and files a workers' compensation claim, which is denied. When he cannot go back to work, his boss at ABC tells him that he is laid off. Joe applies for unemployment insurance, but again his claim is denied. At the end of the year Joe receives a 1099 form from ABC.

Maria is a home health care worker earning \$10 an hour for a home health care staffing agency. The agency gives Maria daily instructions, including the names and addresses of her clients, her schedule, and the care each client requires. At the end of the week Maria is required to turn in detailed time sheets showing her work time. She is not compensated for her travel time between clients' homes. Maria is paid her \$10 an hour only for the time she is with clients, even when she works over forty hours a week. If Maria calculates her total work time, including the time she spends traveling between clients' homes, she is actually earning less than the minimum wage of \$7.25 an hour.

Joe and Maria are likely misclassified by their employers as independent contractors. As a result, they lose critical employee protections. Although many employment law practitioners are well aware of misclassification related to exemptions for administrative and executive employees under the Fair Labor Standards Act, independent-contractor misclassification is an equally serious problem with grave consequences for workers, state governments, and businesses. Moreover, the problem preys on the most vulnerable. It is particularly prevalent among low-wage workers, especially in the construction, landscaping, home health care, and courier/delivery industries.¹ As with other schemes that cheat the system, independent-contractor misclassification enables low-road employers to cut their costs illegally while employees lose workplace protections.

Here I explain independent-contractor misclassification through the prism of the Workplace Fraud Act, Maryland's independent-contractor misclassification law.² I discuss the scope of independent-contractor misclassification and explain how advocates can identify misclassified individuals. I explore potential claims on behalf of misclassified workers and discuss the Workplace Fraud Act. The strength of the opposition that the Act has faced—both before and after its passage—shows the potential power that this type of legislation bears against unscrupulous employers.

¹See, e.g., Stacy Canan et al., *How the Fair Labor Standards Act Fails Home Health Aides and Consumers*, 45 CLEARINGHOUSE REVIEW 308 (Nov.–Dec. 2011).

²Maryland Workplace Fraud Act, MD. CODE ANN., LAB. & EEMPL. §§ 3-901–3-920 (LexisNexis 2009) (amended 2012).

Independent-Contractor Misclassification Defined

Independent-contractor misclassification refers to the practice of improperly classifying employees as independent contractors. It is also referred to as “1099-ing” an employee because of the Internal Revenue Service 1099 form issued to independent contractors.³ However, some misclassified employees are never issued any tax forms and are paid only in cash, “off the books,” or “under the table.”

True independent contractors behave very differently from employees and are treated differently by employers. Independent contractors are in business for themselves; they have specialized skills and perform services that the employer does not provide. Independent contractors typically bring their own materials and tools to a job and are required to pay their own income taxes, social security taxes, and workers' compensation policies.⁴ An example of an independent contractor is a plumber hired by a doctor's office to fix a problem with the office sink. Because of the specialized nature of independent contractors' work and the focus on owning their own legitimate businesses, true independent contractors are far less common in the workplace than employer-employee relationships.

By contrast, employees are subject to an employer's control and are usually hired to perform the very services that the employer advertises. The employer has the right to control and direct an employee's work, as well as how and where the work is performed. The employer also supplies the equipment and tools needed to perform the work. Employee and employer are both required to pay their respective shares of social security and Medicare

taxes. However, the employer is required to provide certain employee benefits and protections, including paying the full premiums for workers' compensation and unemployment insurance.⁵ Employees are covered by protective labor laws, such as antidiscrimination laws, which do not apply to independent contractors.

Employers have many incentives to misclassify their employees as independent contractors. There is the obvious economic incentive: employers can save up to 30 percent of their payroll costs by failing to withhold employer-side taxes and not contributing to unemployment insurance and workers' compensation.⁶ Lower payroll costs mean that misclassifying employers can underbid competitors for jobs and obtain additional business. Employers who misclassify their employees may also believe that they are avoiding liability under federal and state wage and antidiscrimination statutes, which only apply to employees.

A 2000 study commissioned by the U.S. Department of Labor noted that a significant number of independent contractors were reported in the construction, home health care, landscaping, and food preparation and processing industries notwithstanding that many workers in those industries are not their own bosses, do not own their own businesses, and do not use their own work equipment.⁷ Recent immigrants—both documented and undocumented—are especially prevalent among workers misclassified as independent contractors because many immigrants are unaware of their legal rights.⁸

Immigrant workers are not the only victims of misclassification, however; up to 30 percent of American businesses misclassify their employees as indepen-

³Internal Revenue Service, U.S. Department of the Treasury, Form 1099-MISC (2012), <http://1.usa.gov/K3XLmD>.

⁴LALITH DE SILVA ET AL., PLANMATIC, INDEPENDENT CONTRACTORS: PREVALENCE AND IMPLICATIONS FOR UNEMPLOYMENT INSURANCE PROGRAMS 2 (Feb. 2000), <http://bit.ly/JwUJ71> (prepared for Employment and Training Administration, U.S. Department of Labor).

⁵*Id.*

⁶*Leveling the Playing Field: Protecting Workers and Businesses Affected by Misclassification: Hearing Before the S. Comm. on Health, Education, Labor & Pensions*, 111th Cong. 22 (2010) (testimony of Catherine K. Ruckelshaus, Legal Codirector, National Employment Law Project), <http://bit.ly/KDjfWg>.

⁷DE SILVA ET AL., *supra* note 4, at 35.

⁸*Id.*

dent contractors.⁹ This number is likely even higher in the underground economy, where low-wage and immigrant workers are often paid off the books. In the mid-1990s a national study of independent-contractor misclassification estimated that about 80,000 workers were misclassified. The researchers predicted that “an increase in the unemployment rate could precipitate an avalanche of [independent-contractor] related issues.”¹⁰ The unemployment rate at the time of the study was 4 percent, the lowest unemployment rate in three decades.¹¹ The current unemployment rate is 8.1 percent.¹² Advocates widely confirm that the researchers’ prediction has become a reality. The increased prevalence of independent-contractor misclassification has left hundreds of thousands of workers without necessary workplace protections.

The Maryland Department of Labor, Licensing and Regulation conducts annual, random audits of 2 percent of the state’s employers. These audits consistently show that about 20 percent of Maryland employers misclassify employees as independent contractors. However, the percentage in certain industries such as construction, where misclassification is most prevalent, is likely much higher.¹³

Effects of the Problem

Misclassification costs states revenue in the form of unpaid and uncollectable income taxes, payroll taxes, and unem-

ployment insurance and workers’ compensation premiums. Nationwide misclassification of just 1 percent of workers as independent contractors is estimated to cost over \$198 million to unemployment insurance trust funds alone.¹⁴

Based on the Maryland Department of Labor, Licensing, and Regulation’s audits in Maryland, the state’s unemployment insurance trust fund is estimated to lose between \$15 million and \$25 million each year due to misclassification.¹⁵ Because Maryland’s audits are random, do not target industries with a higher prevalence of misclassification, and cover only employers who report at least some wages and pay at least some unemployment insurance tax, the total cost of misclassification is much higher. Employers that do not pay any unemployment insurance—for example, those who pay their workers off the books—would never be subject to these audits.¹⁶ That estimate does not include payroll and income taxes or workers’ compensation premiums that the state has not collected from misclassifying employers.

As the examples of Joe and Maria demonstrate, workers who are misclassified as independent contractors lose coverage under unemployment insurance and workers’ compensation, as well as their right to earn minimum wage and overtime pay.¹⁷ They also lose protection from federal and state discrimination laws, the right to bargain collectively, and the right to join a union.¹⁸ They may also be denied

⁹*Id.* at i–iv.

¹⁰*Id.* at iv, 69.

¹¹*Id.* at 4.

¹²John M. Galvin, Bureau of Labor Statistics, U.S. Department of Labor, Statement (June 1, 2012), <http://1.usa.gov/MAETPu>.

¹³Hearing on H.B. 1590 Before the H. Economic Matters Comm., 2008 Leg., 425th Sess. (Md. 2008) (testimony of Thomas E. Perez, Secretary, Department of Labor, Licensing and Regulation), <http://bit.ly/KFXbhU>.

¹⁴DE SILVA ET AL., *supra* note 4, at 69.

¹⁵Hearing on H.B. 1590, *supra* note 13.

¹⁶*Id.*

¹⁷See, e.g., MD. CODE, LAB. & EMPL. § 8-201 (2012) (defining “covered employment” for purposes of unemployment insurance and differentiating employees from independent contractors), § 9-202 (2012) (requiring employers’ workers’ compensation policies to cover employees unless they can establish independent contractor relationship); Fair Labor Standards Act, 29 U.S.C. §§ 206–207 (providing minimum wage and overtime protections to “employees”).

¹⁸Title VII, 42 U.S.C. § 2000e-2; National Labor Relations Act, 29 U.S.C.A. § 157 (“Employees shall have the right to self-organization, to form, join, or assist labor organizations, to bargain collectively through representatives of their own choosing, and to engage in other concerted activities for the purpose of collective bargaining or other mutual aid or protection[.]”).

other employee benefits, such as any paid sick leave, vacation, health benefits, or pensions provided by their employer to employees. Misclassified employees do not benefit from having social security and Medicaid payments credited to their accounts either.

How to Identify Misclassified Workers

In many respects, misclassification is a silent problem. Workers often do not realize that misclassification is a problem until they are laid off and denied unemployment, or until they are injured on job sites and denied workers' compensation. Advocates can identify misclassification claims when workers come forward with typical wage-theft claims, particularly overtime claims.¹⁹ Workers' paycheck stubs may reveal one of the following scenarios suggesting possible misclassification:

- More than forty hours of work in a workweek, all paid at a regular hourly rate.
- Flat rate of daily or weekly pay, without regard to hours worked.
- Multiple paychecks for the same pay period showing hourly work paid at the worker's regular rate.
- Combination of hourly and piece rates or other pay, such as "bonus pay."
- A total amount paid with no deductions or indications of hourly pay; sometimes with the notation "contract labor" or "1099."

Evidence of misclassification can be found elsewhere. Sometimes workers report filling out a new application for employment or signing new tax forms months or years after beginning their jobs even though the terms and conditions of their employment have not changed. Employment contracts are another sign of misclassification. Many misclassifying employers require employees to sign contracts as part of their job applications—and as a condition of employment—stating that the applicants

understand that they are independent contractors and agree to make all federal- and state-required contributions. Most of these contracts are in English, regardless of the language or literacy capabilities of the job applicant, and the terms are not explained. In industries that use a largely low-wage, immigrant workforce, workers in order to secure work are more likely to agree to a range of terms of employment that they may not understand. This is especially true in industries—such as the construction industry—that have been hard-hit by the recession. Employers view these contracts as a way to avoid potential wage and misclassification claims. Workers may also be deterred from enforcing their rights once they have signed a contract agreeing to be treated as an independent contractor, regardless of the economic reality of their working relationship. However, such agreements are not effective to convert an employee to a lawful independent contractor. The employees' rights and protections referred to above generally cannot be waived by contract.

Misclassification cases can also be identified by reviewing unemployment and workers' compensation denials. State unemployment insurance and workers' compensation agencies are already trained to spot misclassification cases. Meeting with key people in those agencies to discuss methods of partnering to identify cases and share information can be a way to identify misclassification cases in your area.

Both in Maryland and across the country, workers' advocates still have a lot of work to do to protect misclassified workers. Both advocates and state departments of labor need continued training to help them identify misclassified workers seeking assistance on wage problems. When seeking legal assistance or a state benefit, misclassified workers may report receiving a 1099, produce a signed independent-contractor agreement, or even self-identify as an independent contractor or as self-employed. Without specialized training, state agencies and

¹⁹For state-specific discussions of wage theft, see Alvar Ayala, *Amending the Illinois Wage Payment and Collection Act: An Organizing Victory Against Wage Theft*, 45 CLEARINGHOUSE REVIEW 369 (Nov.–Dec. 2011); Deborah Axt, et al., *The Campaign to Pass New York's Wage Theft Prevention Act*, 45 CLEARINGHOUSE REVIEW 154 (July–August 2011).

advocates may not investigate further. However, those documents and agreements are not dispositive of whether a worker is truly an independent contractor. In fact, they may be meaningless. State misclassification laws, where they exist, largely recognize what Fair Labor Standards Act litigation has already established: the worker's classification depends on the reality of the relationship with the employer or contractor.²⁰

Legal Claims for Misclassified Individuals Under Federal and State Law

Where workers can show that they were employees under the Fair Labor Standards Act as a matter of economic reality, they can recover any owed minimum wages or overtime pay, plus liquidated damages, attorney fees, and costs.²¹ In analyzing the question of whether a worker is an employee or an independent contractor under the Fair Labor Standards Act, courts use a factor-by-factor test known as the economic realities test to determine whether the worker is financially dependent on an employer.²² The factors include (1) the degree of control that the employer has over the manner in which work is performed; (2) worker's opportunity for profit or loss dependent on worker's managerial skill; (3) worker's investment in equipment or material, or

worker's employment of other workers; (4) degree of skill required for the work; (5) permanence of the working relationship; and (6) the degree to which the services rendered are an integral part of the employer's business.²³ No single factor is dispositive.²⁴ Instead courts "look[] at the totality of the circumstances to capture the economic realities of the relationship between the worker and putative employer."²⁵ Because the Act's protections are to be interpreted broadly so as to effectuate its remedial goals, the economic realities test is considered to have the most expansive employee classification.²⁶

Once misclassified workers establish that they were, in fact, employees under the economic realities test, if they earned a daily, weekly, or piece rate as independent contractors they may be able to prove minimum-wage violations. They simply need to calculate their hourly rate by dividing total compensation by hours worked.²⁷ Similarly, if they worked over forty hours in any workweek, even while paid at an hourly rate, they are owed an extra 50 percent of their hourly rate for all hours over forty in a workweek.²⁸ State minimum wage and overtime laws may provide similar relief to a misclassified worker.²⁹

Misclassified workers likely have—in addition to statutory claims—common-law claims such as breach of contract, unjust enrichment, and *quantum meruit*. These

²⁰See, e.g., MD. CODE ANN., LAB. & EMPL. § 3-903(c) (LexisNexis 2012).

²¹Fair Labor Standards Act, 29 U.S.C. § 216(b). An expansive body of Fair Labor Standards Act case law has developed around the distinction between an employee and an independent contractor (see, e.g., *United States v. Silk*, 331 U.S. 704, 716 (1947); *Brock v. Superior Care Incorporated*, 840 F.2d 1054, 1058 (2d Cir. 1988); *Shultz v. Capital International Security Incorporated*, 466 F.3d 298, 307–9 (4th Cir. 2006); *Brock v. Mr. W Fireworks Incorporated*, 814 F.2d 1042, 1043 (5th Cir. 1987); *Weisel v. Singapore Joint Venture Incorporated*, 602 F.2d 1185, 1189–90 (11th Cir. 1979).

²²Under the Fair Labor Standards Act, an employee is broadly defined as "any individual employed by an employer." An "employer" means "any person acting directly or indirectly in the interest of an employer in relation to an employee." "Employ," in turn, is defined expansively as "to suffer or permit to work" (29 U.S.C. §§ 203(e)(1), (d), (g)).

²³*Silk*, 331 U.S. at 716; *Heath v. Perdue Farms Incorporated*, 87 F. Supp. 2d 452, 457 (D. Md. 2000); *Shultz v. Capital International Security Incorporated*, 466 F.3d 298, 304 (4th Cir. 2006).

²⁴*Quinteros v. Sparkle Cleaning Incorporated*, 532 F. Supp. 2d 762, 769 (D. Md. 2008).

²⁵*Id.*

²⁶*Nationwide Mutual Insurance Company v. Darden*, 503 U.S. 318, 326 (noting "striking breadth" of definition of "employ," which broadens "the meaning of employee to cover some parties who might not qualify as such under a strict application of traditional agency law principles").

²⁷29 C.F.R. § 778.109 (2012).

²⁸This is provided he was paid straight time for all hours worked (see *id.* § 778.110).

²⁹See, e.g., MD. CODE ANN., LAB. & EMPL. § 3-427 (LexisNexis 2012).

claims are based on the theory that the worker conferred a benefit on the employer, and the employer therefore has a contractual and equitable obligation to compensate the worker with legally required regular time and overtime wages. To have received the benefits of the worker's labor without paying for its value is inequitable for the employer.³⁰ In the case of a misclassified employee, a common-law claim could allow the worker to recover any unpaid regular and overtime wages where the worker was not properly compensated. However, a common-law claim would likely fall short of remedying an improper denial of unemployment insurance or workers' compensation.

In many states, misclassified workers are not limited to common-law claims. Pennsylvania, Delaware, Maine, Massachusetts, and Maryland have all enacted legislation to combat the misclassification of employees as independent contractors.³¹ Many other states have introduced similar bills in the last several years.³² State misclassification laws may target specific industries and give state agencies varying powers, such as civil penalties, stop-work orders, and withholding of funds for public contracts, or even debarment.³³ Some also provide private rights of action, recovery of lost wages, and damages, including damages for loss of unemploy-

ment insurance or workers' compensation benefits.³⁴

Maryland's Workplace Fraud Act

Enacted in 2009, Maryland's Workplace Fraud Act prohibits the misclassification of construction and landscaping employees as independent contractors. The Act contains a presumption of employee status and adopts the ABC test to determine whether a worker is an independent contractor or an employee.³⁵ The ABC test focuses on the putative employer's right to control and direct the work, and whether the work is part of the usual course of the employer's business.³⁶ Contract terms indicating an independent contractor relationship are irrelevant to a determination under the ABC test.

The Workplace Fraud Act allows for both administrative and private enforcement. Further, misclassified workers can sue for recovery of lost wages and benefits, plus treble damages and attorney fees.³⁷ In terms of administrative enforcement, where a citation for a knowing violation is issued by the Department of Labor, Licensing and Regulation to an employer in a public works contract, payment to the employer is withheld in sufficient amount to pay wages due as well as any benefits, taxes, or other contributions required by law to be paid on the employee's behalf.³⁸ Public

³⁰See, e.g., Complaint at 28–29, *Bouthner v. Cleveland Construction Incorporated*, Case No. 1:11-cv-00244-RDB (D. Md. Jan. 28, 2011).

³¹Pennsylvania Construction Workplace Misclassification Act, 43 PA. STAT. ANN. §§ 933.1 *et seq.* (2010); Delaware Workplace Fraud Act, DEL. CODE ANN. tit. 19 §§ 3501 *et seq.* (2009); Maine Workers' Compensation Act of 1992, ME. REV. STAT. ANN. tit. 39-A, § 114 (2011) (independent contractor status for truckers and couriers); MASS. GEN. LAWS ANN. ch. 149 § 148B (LexisNexis 2004) (labor and industries, payment of wages; commissions; exemptions; check-cashing facilities; procedure for change from weekly to biweekly payments; penalty for violation); Maryland Workplace Fraud Act, MD. CODE ANN., LAB. & EMP. §§ 3-901–3-920 (LexisNexis 2012).

³²Catherine K. Ruckelshaus & Sarah Leberstein, National Employment Law Project, NELP Summary of Independent Contractor Reforms: New State and Federal Activity (Nov. 2011), <http://bit.ly/K8mE0J>.

³³*Id.*

³⁴See, e.g., MD. CODE ANN., LAB. & EMP. § 3-911 (LexisNexis 2012) (providing private right of action to recover economic damages, plus treble damages for knowing violations, as well as attorney fees and costs).

³⁵*Id.* § 3-903(c).

³⁶*Id.* § 3-903(c)(ii). An employer-employee relationship is presumed unless the employer can demonstrate that (1) the worker is free from the direction and control over the performance of her work both in fact and by contract; (2) the worker is customarily engaged in an independent business of the same nature as the work that the worker is performing; and (3) the work is either outside the usual course of business for the putative employer or is performed outside the putative employer's place of business. All three factors must be met in order to overcome the presumption of employee status.

³⁷*Id.* § 3-911.

³⁸*Id.* § 3-913, amended by S. 272, 2012 Leg., 430th Sess. (Md. 2012) (allowing withholding of public funds only for citations of knowing violations), <http://bit.ly/JVjxqd>.

enforcement of the Act is funded through the workers' compensation fund.³⁹

The Act also provides for civil penalties in some circumstances.⁴⁰ After receiving notification of a violation, the employer is given an opportunity to come into compliance without any penalty.⁴¹ A citation of up to \$1,000 is issued only after an employer refuses or is unable to remedy the violation.⁴² Where a knowing violation is found, the employer may be fined up to \$5,000.⁴³ Repeat violations are subject to additional penalties.⁴⁴

Leadership and support from the Maryland Department of Labor, Licensing and Regulation and a good working relationship between the department and workers' advocates were vital to the Workplace Fraud Act's passage. Before the bill was introduced in January 2009, the department convened work groups—contractor associations, union representatives, worker and immigrant advocates (the Public Justice Center, CASA [Central American Solidarity Association] de Maryland, and Progressive Maryland), and small-business representatives—to discuss the proposed legislation and build consensus. Although not all conflicts were resolved, proponents' and opponents' concerns with the bill surfaced

at a very early stage. Workers' advocates were able to prepare their responses to the opposition before the legislative session began. While this helped advocates defend the bill from harmful amendments, compromises made early also helped ensure the bill's passage.⁴⁵

One of the most contentious challenges to the passage of the Workplace Fraud Act was the use of the ABC test. The bill's opponents attempted to replace the more employee-friendly ABC test with the IRS test. Based on the common-law concept of the master-servant relationship, the IRS test uses twenty factors divided into three categories to determine workers' degree of control over their own work: (1) behavioral control, (2) financial control, and (3) type of relationship.⁴⁶ Not all factors must be satisfied to show an independent-contractor relationship, but some factors weigh more heavily in favor of a finding than others. Similar to the other tests, a contract stating the nature of the relationship is not dispositive, although the IRS test does give such a contract some weight in its determination.⁴⁷ The various factors are guidelines rather than strict requirements as in the ABC test. Thus the IRS test allows for a more likely finding of independent-contractor status.

³⁹*Id.* §§ 3-919(b), 9-316.

⁴⁰*Id.* §§ 3-908, 909.

⁴¹*Id.* § 3-903(a).

⁴²*Id.* § 3-903(b).

⁴³*Id.* § 3-909(a).

⁴⁴*Id.* § 3-909(d) ("An employer in violation of § 3-904 of this subtitle may be assessed double the administrative penalties set forth in subsection (a) of this section if the employer has been found previously to have violated this subtitle by a final order of a court or an administrative unit."); § 3-909(e) ("An employer who has been found by a final order of a court or an administrative unit to have violated § 3-904 of this subtitle three or more times may be assessed an administrative penalty of up to \$20,000 for each employee.").

⁴⁵Telephone Interview with Scott Jensen, Deputy Secretary, Maryland Department of Labor, Licensing and Regulation (April 10, 2012).

⁴⁶INTERNAL REVENUE SERVICE, U.S. DEPARTMENT OF THE TREASURY, PUBLICATION 15-A, EMPLOYER'S SUPPLEMENTAL TAX GUIDE (SUPPLEMENT TO PUBLICATION 15 (CIRCULAR E), EMPLOYER'S TAX GUIDE) 7 (Jan. 31, 2012), <http://1.usa.gov/JUKhLU>; Internal Revenue Service U.S. Department of the Treasury, Independent Contractor (Self-Employed) or Employee? (May 1, 2012), <http://1.usa.gov/L8dx1E>. Behavioral control is demonstrated by the type and degree of instruction given, employee evaluation systems, and training conducted. Financial control is demonstrated where the business has the right to control the economic aspects of the worker's job, such as the rate of pay. Independent contractors are more likely to have made a significant investment in their work, have unreimbursed work expenses, have an opportunity for profit or loss, and make their services available to the market. The relationship category involves looking at how the employer and worker view their relationship to each other. This includes an examination of written contracts, employee benefits, the permanency of the relationship, and whether the services provided are a key activity of the employing business.

⁴⁷Internal Revenue Service, U.S. Department of the Treasury, Type of Relationship (May 30, 2012), <http://1.usa.gov/MYadRO>.

The Department of Labor, Licensing and Regulation and workers' advocates fought back any changes by arguing that Maryland's unemployment insurance laws have been using the ABC test for fifty years. Both the department and employers already were familiar with complying with and enforcing the ABC standard. Despite opponents' contentions, the ABC test was not new and did not add any requirements for compliance. The department was also clear that changes in the ABC test would not be considered.⁴⁸ The bill was passed with the ABC test intact as well as with an explicit presumption of an employer-employee relationship.⁴⁹

Concessions were also made in order to ensure that the bill passed. For example, the 2009 bill initially targeted three industries with high rates of misclassification in Maryland: construction, landscaping, and package delivery services (courier services). Opposition from the courier services industry pointed out that some categories of delivery services, such as groups of independent truck drivers, were exempted from the unemployment insurance law several years before. For the purposes of the Workplace Fraud Act, no compromise could be reached on how to distinguish classes of delivery services that were already exempted from unemployment insurance from those that were not.⁵⁰ Package delivery services were stricken from the bill.⁵¹ Once the Act was passed, the Department of Labor, Licensing and Regulation also sought input from key interest groups, among them the Public Justice

Center and other workers' advocates, in the drafting and revising of regulations under the Act.⁵²

Challenges to Enforcement

The struggle surrounding the Maryland Workplace Fraud Act did not end after it was passed. Enforcement has been a constant battle on several fronts.

State Agencies. In 2010 Gov. Martin O'Malley created a Joint Enforcement Task Force on Workplace Fraud—comprising unemployment insurance, labor and industry, the comptroller, the attorney general's office, insurance administration, and the workers' compensation commission—to facilitate information sharing and outreach among the divisions of the Department of Labor, Licensing and Regulation.⁵³ The task force has the power to conduct random audits of employers and review payroll records to look for irregularities in pay.⁵⁴ In 2010 and 2011 the task force conducted outreach to more than twenty groups and held events to educate employers and workers about compliance with the Workplace Fraud Act.⁵⁵ The Department of Labor, Licensing and Regulation also initiated over seven hundred investigations into workplace fraud and issued twelve citations.⁵⁶ No penalties were assessed, but the audits resulted in over \$600,000 to be paid into the unemployment insurance trust fund, and almost \$400,000 of withholding taxes was assessed by the comptroller's office.⁵⁷

⁴⁸*Id.*

⁴⁹Md. CODE ANN., LAB. & EMPL. § 3-903(c)(1) (LexisNexis 2012).

⁵⁰Jensen, *supra* note 45.

⁵¹H.B. 819, 2009 Leg., 430th Sess. § 3-902(3) (Md. 2009), <http://bit.ly/Ksonj9>.

⁵²See generally Md. CODE REGS. 09.12.40.00 *et seq.* (2010).

⁵³Press Release, Maryland Department of Labor, Licensing and Regulation, Governor O'Malley Creates Task Force to Crack Down on Workplace Fraud (July 14, 2009), <http://bit.ly/KggIDP>.

⁵⁴Maryland Department of Labor, Licensing and Regulation, Annual Report of the Joint Enforcement Task Force on Workplace Fraud 3 (Dec. 2010), <http://1.usa.gov/KNTbYR>.

⁵⁵*Id.* at 9–10; Maryland Department of Labor, Licensing and Regulation, Annual Report of the Joint Enforcement Task Force on Workplace Fraud 11–12 (Dec. 2011), <http://bit.ly/MbTWg5>.

⁵⁶Maryland Department of Labor, Licensing and Regulation, *supra* note 55, at 3–4.

⁵⁷*Id.* at 3–5.

Anecdotal evidence suggests that there are several barriers to enforcement on the part of unscrupulous employers. Some create a second set of paycheck stubs to produce in response to audits or give workers fake stubs to show investigators during site visits. The fabricated stubs show proper payment of overtime and appropriate deductions. Fear of immigration enforcement has further fueled the underground economy, where workers are paid off the books and are off the radar of state enforcement agencies. Even with the audits it has conducted, the Workplace Fraud Unit is strapped for resources. The unit has six investigators covering all of the landscaping and construction employers in Maryland.⁵⁸

Public Interest Organizations and the Private Bar. One of the greatest challenges to private enforcement of independent-contractor misclassification laws is that private enforcement is in large part reliant on self-reporting. With the economic downturn and increased scrutiny of the immigrant workforce, potential claimants, fearing retaliation and loss of employment, are often afraid to speak out against their employers. The Public Justice Center's Workplace Justice Project has been to workers' centers, community centers, churches, and labor organizing events to educate workers about their rights, such as their protections from retaliation, under the Workplace Fraud Act. Even so, likely due at least in part to workers' fear of retaliation, few cases have been brought under the Act since its passage in 2009.⁵⁹

Employer Backlash in the 2012 Legislative Session. During Maryland's 2012 legislative session, the Workplace Fraud Act was subject to scrutiny, and the Department of Labor, Licensing and Regulation's alleged overreaching enforcement was the target of several local newspaper articles.⁶⁰ The department faced severe opposition from the flooring industry in particular, after several flooring companies were subject to Workplace Fraud Unit audits. Employers complained that the auditors in the unit did not understand the Act and enforced it inconsistently. Employers also complained that costly, time-consuming investigations went on for months with no discernible conclusion.

Although a majority of employers' complaints had to do with the auditing rather than with the results, the frustration with the Act revived many 2009 legislative session battles, such as the use of the ABC test instead of the IRS test, thought to have been resolved.⁶¹ At least six bills were submitted during the 2012 General Assembly session on behalf of the flooring industry in response to concerns about enforcement.⁶² By contrast, advocates from the Public Justice Center and Maryland Legal Aid Bureau were interested in expanding the scope of the Act to eliminate any industry-specific restriction altogether.

Again, the Department of Labor, Licensing and Regulation convened a work group at the behest of a state senator. The group was tasked with hammering out an

⁵⁸Telephone Interview with Scott Jensen, Deputy Secretary, Maryland Department of Labor, Licensing and Regulation (April 23, 2012).

⁵⁹The Public Justice Center and the Employment Law Group filed in Maryland state court in 2011 a Workplace Fraud Act lawsuit alleging misclassification of construction workers by several construction contractors and subcontractors. That case was removed to federal court by one of the defendants under the Class Action Fairness Act (See *Bouthner v. Cleveland Construction Incorporated*, Case No. 1:11-cv-00244-RDB (D. Md. Jan. 28, 2011); Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4 (codified as amended in 28 U.S.C. §§ 1332(d), 1453, 1711–1715).

⁶⁰Terry Randall, *Maryland's Push to Find Misclassified Workers Further Burdens Businesses*, BALTIMORE BUSINESS JOURNAL, Jan. 6, 2012, <http://bit.ly/Kg49IA>; James Briggs, *Contractors Question Letter of Maryland Workplace Fraud Law*, BALTIMORE BUSINESS JOURNAL, Jan. 20, 2012, <http://bit.ly/K8rprl>; Kevin James Shay, *Employers Call Maryland's New Workplace Fraud Law Onerous*, GAZETTE.NET, Nov. 11, 2011, <http://bit.ly/LeflWd>; Bethany Rodgers, *Delegate: Redefine "Employee": State's Insistence on Adding Contractors Is Costly*, BUSINESS SAYS, FREDERICKNEWSPOST.COM, Feb. 21, 2012, <http://bit.ly/JhQ9vZ>.

⁶¹H.B. 309, 2012 Leg., 430th Sess. (Md. 2012); S. 272, 2012 Leg., 430th Sess. (Md. 2012) (replacing ABC test with the IRS test); S. 1005, 2012 Leg., 430th Sess. (Md. 2012) (providing defense to misclassification where employer produces independent contractor agreement).

⁶²S. 600, H.B. 734, H.B. 309, S. 1005, H.B. 1364, S. 272, 2012 Leg., 430th Sess. (Md. 2012).

agreement to meet industry concerns. Any attempts to expand the scope of the Act were set aside as the Act became in danger of being seriously weakened by the new bills. Despite protests from workers' advocates, a compromise bill was passed; the bill neutralized the presumption of an employer-employee relationship upon submission of a written independent-contractor contract (with several enumerated requirements), an affidavit signed by the putative independent contractor, a current certificate of status from the state, proof that the business holds all necessary licenses, and proof that the employer gave the independent contractor a required written notice.⁶³ The law was also amended to allow withholding of funds in public contracts only for knowing violations and changed deadlines for employers and the Department of Labor, Licensing and Regulation during Workplace Fraud Unit investigations.⁶⁴



The passage of the Workplace Fraud Act in Maryland offered an ideal opportunity for workers' advocates and the Maryland Department of Labor, Licensing and Regulation to curb the illegal misclassification of employees as independent contractors. Enforcement of the Act by advocates and the Department of Labor, Licensing and Regulation elicited a strong response from employers and industry advocates. Defendants' reactions—such as aggressive defenses mounted by nationally established employment law defense-side firms—to the few cases that have been filed under the Act suggest the potential power of private enforcement of the law. Similarly the business response to the Act in the state legislature speaks volumes about public enforcement's potential to eliminate unlawful misclassification.

⁶³S. 272, 2012 Leg., 430th Sess. (Md. 2012); MD. CODE ANN., LAB. & EMPL. § 3-903.1 (LexisNexis 2012).

⁶⁴MD. CODE ANN., LAB. & EMPL. § 3-913; § 3-905(e) (LexisNexis 2012) (giving employers thirty days to produce records); § 3-906(a) (requiring Maryland Department of Labor, Licensing and Regulation to issue citation or close an investigation within ninety days from date employer supplied requested records); § 3-906(f)(2) (stating that employer is entitled to hearing within ninety days of issuance of citation).



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