

**THE MISCLASSIFICATION OF WORKERS AS
INDEPENDENT CONTRACTORS: WHAT POLICIES
AND PRACTICES BEST PROTECT WORKERS?**

JOINT HEARING

BEFORE THE

SUBCOMMITTEE ON HEALTH,
EMPLOYMENT, LABOR AND PENSIONS

AND THE

SUBCOMMITTEE ON WORKFORCE PROTECTIONS

COMMITTEE ON

EDUCATION AND LABOR

U.S. HOUSE OF REPRESENTATIVES

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**THE MISCLASSIFICATION OF WORKERS
AS INDEPENDENT CONTRACTORS:
WHAT POLICIES AND PRACTICES
BEST PROTECT WORKERS?**

Tuesday, July 24, 2007

U.S. House of Representatives

Subcommittee on Health, Employment, Labor and Pensions

Subcommittee on Workforce Protections

Committee on Education and Labor

Washington, DC

The subcommittees met, pursuant to call, at 10:30 a.m., in Room 2175, Rayburn House Office Building, Hon. Robert Andrews [chairman of the Subcommittee on Health, Employment, Labor, and Pensions] presiding.

Present from Subcommittee on Health, Employment, Labor, and Pensions: Representatives Andrews, Kildee, Tierney, Wu, Holt, Loeb sack, Hare, Kline, McKeon, Boustany, and Walberg.

Present from Subcommittee on Workforce Protections: Woolsey, Payne, Bishop of New York, Shea-Porter, Hare, Wilson, and Kline.

Staff present: Aaron Albright, Press Secretary; Tylease Alli, Hearing Clerk; Jordan Barab, Health/Safety Professional; Jody Calemine, Labor Policy Deputy Director; Lynn Dondis, Policy Advisor for Subcommittee on Workforce Protection; Carlos Fenwick, Policy Advisor for Subcommittee on Health, Employment, Labor and Pensions; Michael Gaffin, Staff Assistant, Labor; Jeffrey Hancuff, Staff Assistant, Labor; Brian Kennedy, General Counsel; Joe Novotny, Chief Clerk; Megan O'Reilly, Labor Policy Advisor; Rachel Racusen, Deputy Communications Director; Michele Varnhagen, Labor Policy Director; Robert Borden, Minority General Counsel; Cameron Coursen, Minority Assistant Communications Director; Steve Forde, Minority Communications Director; Ed Gilroy, Minority Director of Workforce Policy; Rob Gregg, Minority Legislative Assistant; Jim Paretti, Minority Workforce Policy Counsel; Molly McLaughlin Salmi, Minority Deputy Director of Workforce Policy; Linda Stevens, Minority Chief Clerk/Assistant to the General Counsel; and Loren Sweatt, Minority Professional Staff Member.

Chairman ANDREWS [presiding]. Ladies and gentlemen, the subcommittee will come to order. I would ask everyone to please take their seats.

We welcome our witnesses and the members of the public for today's hearing.

In the last 6 years, over 2 million Americans have found themselves in a situation where the 40-hour work-week law that applies to virtually everyone else doesn't apply to them; where laws that govern pensions and health care, that apply to just about everyone else, do not apply to them; where laws that deal with the right to collectively bargain, the right to organize, the right to grieve, that apply to almost everyone else, does not apply to them.

In the last 5 or 6 years, we have had an increase of more than 2 million people who fall into the category in our workforce of independent contractors.

Now, in some cases, that status is quite right and quite appropriate. If someone is retained for a limited purpose, usually for a limited time, to do a specific job function for an employer, it is quite necessary and appropriate that that person not be treated as an employee for reasons of flexibility, for reasons of fair compensation, for reasons of the appropriate organization and carrying out of the employer's business.

But in cases where someone looks an awful lot like an employee—is told what to do and when he or she can do it, is given no discretion over how to conduct the affairs of the business, whose compensation is fixed and set by the employer—when that person looks an awful lot like an employee, we think the law should treat them as an employee, should provide that person with the protections and the rights that employees have under our federal laws.

The question before the committee today was initiated by Chairwoman Woolsey's efforts a few weeks ago. This is a joint hearing of the Workforce Protections Subcommittee and our HELP Subcommittee. And Chairwoman Woolsey did a great job with our colleagues in beginning to flesh out the issue as to how prevalent is the problem of misclassification of people. How prevalent is it that someone who truly is an employee is being treated as an independent contractor and, therefore, divested of the rights that I made reference to earlier?

As a result of the good work that Ms. Woolsey did at that hearing, she and I and some of our colleagues wrote a letter to the United States Department of Labor, asking that the department outline its efforts in identifying the scope of the problem and outline its efforts to deal with reducing and solving the problem.

The purpose of today's hearing is to get answers to those questions that were asked in our letter in May in our first panel. And then to proceed with the second panel, we will look at various perspectives on the scope of the problem, the nature of the problem, and some ideas to solve the problem.

Our first witness today, Mr. DeCamp, is the director of the Wage and Hour Division of the Department of Labor. We are very happy he is with us today. And we look forward to an exchange where we can hear more about the department's efforts to properly define the scope of this problem and to remediate its effects.

I will say this to you in closing my remarks. The image that is often conjured up of an independent contractor is a Web site designer, you know, someone who designs Web sites and Web pages for a multiplicity of clients and works out of his or her home, and

is very much on the fly, on the go; an independent entrepreneur with a laptop and a vision and a business card and a chance to make himself or herself a wealthy person. Long may that person be treated as an independent contractor, because they are.

But there are people who are mowing lawns and driving trucks and working in garment linen factories, working in all different places around this country, who sure do look like employees to me. And if they have the functional job of an employee—if they are told what to do, when to do it, how much money they are going to make, what the work rules are, what they can and cannot do—if they have that sort of work life as an employee, then I think the law should treat them as an employee. And they should get the benefits of the 40-hour work-week and the workers' safety laws and the pension and health-care laws and the other protections of this country.

Legislating is about drawing lines. And where we draw this line and how we deal with remediating problems that fall on the wrong side of the line is the legislative job of the committee. I look forward to a full and vigorous discussion of those issues here today.

At this point, I am going to turn to the ranking member of the HELP Subcommittee, my friend from Minnesota, Mr. Kline, for his opening statement.

[The statement of Mr. Andrews follows:]

Prepared Statement of Hon. Robert E. Andrews, Chairman, Subcommittee on Health, Employment, Labor and Pensions

Good morning and welcome to the Joint Health, Employment, Labor, and Pensions Subcommittee and Workforce Protections Subcommittee hearing on "The Misclassification of Workers as Independent Contractors: What Policies and Practices Best Protect Workers." I am delighted to share the gavel today with my colleague, Chairwoman Woolsey.

Today, we will examine the issue of worker misclassification. This joint venture is a follow-up to the Workforce Protections Subcommittee's previous hearing on the misclassification of workers as independent contractors. Today we will have the opportunity to hear the views from the Department of Labor regarding worker misclassification and what actions they have taken to address the problem.

Worker misclassification is a problem that adversely affects employees, employers, taxpayers, and states. Billions of dollars of tax revenue and unemployment insurance have been stolen by employers seeking to avoid the costs of payroll taxes, insurance premiums, and benefits. The witnesses' testimony today will further prove how worker misclassification 1) strips workers of employee benefits and protections; 2) puts good employers at a competitive disadvantage; and 3) cheats the taxpayer out of revenue. I thank the witnesses for their testimony today and look forward to the hearing.

Mr. KLINE. Thank you, Mr. Chairman.

Good morning to all, and welcome to our distinguished panels of witnesses.

As a member of the Workforce Protections Subcommittee and as the ranking member of the Health, Employment, Labor, and Pensions Subcommittee, I am particularly interested in this morning's joint hearing.

At a Workforce Protections Subcommittee hearing earlier this year, we heard from a number of witnesses as to policy issues surrounding the potential misclassification of workers as contractors rather than employees.

I would highlight one point that I think all of our witnesses and, indeed, many of our members agreed upon. This point was put particularly well by Mr. Richard Shavell, who had testified on behalf of the Associated Builders and Contractors.

He testified, "It is critical to distinguish between wrongful classification and misclassification. In construction, wrongful classification by a competitor can result in a competitive disadvantage to other contractors. Contrast this with misclassification, which can easily occur because current law and rules are extremely complex. Those companies not paying employee taxes or worker compensation by wrongful classification can undercut the competition by offering lower bids.

"ABC in no way condones intentional misclassification by businesses that shirk their duties to society and their workers. We endorse a level playing field for all businesses and workers. For those workers who are faced with improper misclassification, we believe they should be accorded every opportunity to have their financial situation corrected."

I think that all of us here this morning share that view: that the wrongful classification of workers should not be tolerated. Where we may differ is in whether and how the law currently allows, if not outright condones, confusion by subjecting employers to a multitude of different tests under a multitude of different statutes.

Perhaps that is a good question for today's hearing and one that I certainly hope that we are going to get to.

I would also point out that a number of witnesses at our hearing back in March, both Democrats and Republicans, made plain their view that our focus should not be on amending the underlying substantive laws, but rather, focusing on enforcement and, in particular, targeted enforcement.

One witness, Ms. Catherine Ruckelshaus, the director of the National Law Employment Project, put it very succinctly when she testified, "The laws are sufficiently broad and sufficiently define 'employee' to cover most of the people I have been talking about," said she, "and most of the people that my co-presenters have been discussing. It is really not a question of changing the law, as much as enforcing the laws that are on the books and doing it more strategically to plug up these loopholes."

And in that light, I am particularly pleased to welcome our first witness, Paul DeCamp, the administrator of the Department of Labor's Wage and Hour Division. I know the chairman will reintroduce him.

The Wage and Hour Division is the lead agency tasked with administering our nation's wage and hour laws and one of a number of federal agencies charged with ensuring workers are correctly classified. I am particularly interested in hearing how the department has been strategically addressing the issue of worker classification in a targeted way.

I look forward to Mr. DeCamp presenting to us the challenges the department faces in doing so and offering any suggestions as to how we may better assist the department in its enforcement efforts.

Again, I welcome all our witnesses, and I yield back.
[The statement of Mr. Kline follows:]

**Prepared Statement of Hon. John Kline, Ranking Republican Member,
Subcommittee on Health, Employment, Labor, and Pensions**

Good morning, and welcome to our distinguished panel of witnesses.

As a member of the Workforce Protections Subcommittee, and as Ranking Member of the Health, Employment, Labor, and Pensions Subcommittee, I am particularly interested in this morning's hearing.

At a Workforce Protections Subcommittee hearing earlier this year, we heard from a number of witnesses as to policy issues surrounding the potential misclassification of workers as "contractors" rather than "employees." I would highlight one point that I think all of our witnesses—and indeed, many of our Members—agreed upon. This point was put particularly well by Mr. Richard Shavell, who testified on behalf of the Associated Builders and Contractors. As Mr. Shavell testified, it is critical to distinguish between wrongful classification and mis-classification. In construction, wrongful classification by a competitor can result in a competitive disadvantage to other contractors. Contrast this with misclassification, which can easily occur because current law and rules are extremely complex. Those companies not paying employee taxes or worker' compensation by wrongful classification can undercut the competition by offering lower bids. ABC in no way condones intentional misclassification by businesses that shirk their duties to society and their workers. We endorse a level playing field for all businesses and workers. For those workers who are faced with improper misclassification we believe they should be accorded every opportunity to have their financial situation corrected.

I think that all of us here this morning share that view—that the wrongful classification of workers should not be tolerated. Where we may differ is in whether and how the law currently allows, if not outright condones, confusion by subjecting employers to a multitude of different tests under a multitude of different statutes. Perhaps that is a good question for today's hearing, one that I hope our witnesses will address.

I would also point out that a number of witnesses at our hearing back in March,—both Democrat and Republican—made plain their view that our focus should not be on amending the underlying, substantive laws, but rather focusing on enforcement, and in particular, targeted enforcement. One witness, Ms. Catherine Ruckelshaus, the Director of the National Law Employment Project, put it very succinctly when she testified:

The laws are sufficiently broad and sufficiently define employee to cover most of the people I have been talking about and most of the people that my co-presenters have been discussing. It is really not a question of changing the law as much as enforcing the laws that are on the books and doing it more strategically, to plug up these loopholes.

In that light, I am particularly pleased to welcome our first witness, Paul DeCamp, the Administrator of the Department of Labor's Wage and Hour Division. The Wage and Hour Division is the lead agency tasked with administering our nation's wage and hour laws and one of a number of federal agencies charged with ensuring workers are correctly classified. I am particularly interested in hearing how the Department has been strategically addressing the issue of worker classification in a targeted way. I look forward to Mr. DeCamp presenting to us the challenges the Department faces in doing so and offering any suggestions as to how we may better assist the Department in its enforcement efforts.

I welcome each of our witnesses this morning, and yield back my time.

Chairman ANDREWS. Thank you, Mr. Kline.

When she assumed the chairmanship of the Workforce Protections Subcommittee, Chairwoman Woolsey launched a vigorous effort to regenerate oversight and legislative review of the laws that protect people in the workplace. She has done some outstanding work already on public-sector employee safety. She has helped to guide through some important legislation already in that area. And I am honored to share this joint hearing with her today.

The gentlewoman from California.

Ms. WOOLSEY. Thank you, Mr. Chairman.

And welcome to all of our witnesses.

This is going to be a very useful, productive joint hearing this morning.

As you know, and as the chairman said, the Workforce Protections Subcommittee held a hearing on this very important issue of misclassification of workers as independent contractors in March.

It seems like just yesterday, right, Mr. Chairman?

And we are really pleased to be here with this joint committee because we are going to continue to look at the issue. It became more important, not less important, after our first hearing.

Today, we will have the opportunity to hear from the administration. And we will hear from others, also, about this serious problem. And it is a problem that hurts our workers, but not only our workers, but also honest contractors and all of society as states and federal governments lose billions of dollars in lost revenues by this misclassification.

After the last hearing, Mr. Andrews and I wrote a letter to Department of Labor asking for information about the misclassification. We got the department's response. It was just a little over a week ago, in time for this hearing. Thank you.

And I am pleased that Mr. DeCamp is here to present answers to the questions that we asked.

But I have some very serious reservations about whether the department is really dealing with this problem in an adequate manner. And what we need to find out today is: if the department can't deal with it, what does the Congress need to do to make it possible for the overreaching agency to do the right thing?

And, at the outset, I would like to say that there are true independent contractors and that this is not about them. Nobody questions that. This is about the countless workers who are really employees but have been deliberately misclassified by employers because those employers want to avoid the costs associated with an employee, such as workers' compensation insurance, payment into Social Security and Medicare systems.

The number-one reason that employers deliberately misclassify is to avoid paying workers' compensation and otherwise avoid workplace injury and disability disputes. So if a worker gets seriously injured—and make no mistake, this practice usually affects mostly low-income workers—there is no income that he or she can go to when they can't work. And there is likely no health insurance to help with the medical expenses. But the employer lowers its costs.

In fact Mr. Wade Horn, a contractor who testified at the hearing in March, said that when companies misclassify their employees, they expect to reduce their labor costs between 15 and 20 percent.

In March, our witnesses were principally from the building trades. They told us how widespread miscalculation is in that industry. But we know for certain misclassification occurs across a wide range of industries.

For example, Representative Stupak, chair of the Subcommittee on Oversight and Investigations on the Energy and Commerce Committee, has been investigating the widespread misclassification of jockeys as independent contractors.

I am very glad that Mr. Williams is here today to testify about his experiences with FedEx. My own state of California is waging a battle against FedEx's practice of misclassifying its couriers as independent contractors. And in the year 2004, the California Employment Development Department issued a payroll tax assess-

ment of \$7.8 million against the company. And they did that because it failed to pay payroll taxes for appropriate employees.

In California, misclassification is an enormous problem. But we are an enormous state. The California insurance commissioner has reported that 30 percent of employers in the state do not carry workers' compensation insurance, and that is one of the sure signs that those employers' workers are being treated as independent contractors.

This problem has so concerned my state that there is a bill in the assembly, State Assembly Bill 622, which, if passed, will make willful misclassification illegal. And it will assess penalties of up to \$15,000 per violation and up to \$25,000 for those employers who have engaged in a pattern of practice of misclassification. Our very own attorney general has started a program to protect vulnerable workers from unscrupulous employers throughout this process.

But, unfortunately, other states are having problems with misclassification, as well. And it is a national problem. It has far-reaching consequences.

And I have great confidence that we are working to find out why we can't do something about it. But first we have to find out what we need to do about it.

Thank you very much, Mr. Chairman.

[The statement of Ms. Woolsey follows:]

Prepared Statement of Hon. Lynn C. Woolsey, Chairwoman, Subcommittee on Workforce Protections

Thank you Chairman Andrews and welcome to all of the witnesses for joining us here today.

As you know, my Workforce Protections Subcommittee held a hearing on this very important issue of misclassification of workers as independent contractors in March.

And I am very glad that—through this Joint Subcommittee hearing—we are continuing to look at this issue.

Today we will have an opportunity to hear from the Administration and others about this serious problem, which hurts not only our workers, but also honest contractors and all of society as state and federal governments lose billions of dollars in lost revenues.

After the last hearing, Mr. Andrews and I wrote a letter to DOL asking for information about misclassification.

We got the Department's response a little over a week ago. It was a late reply but in time for this hearing.

I am very pleased that Mr. DeCamp from DOL is present to answer questions about DOL's response because I have serious reservations about whether the Department is dealing with this problem in an adequate manner.

At the outset let me say that there are true independent contractors out there—this is not about them.

This is about the countless other workers who are really employees but have been deliberately misclassified by employers because those employers want to avoid the costs associated with an employee, such as workers compensation insurance and payment into the Social Security and Medicare systems.

So if a worker gets seriously injured—and make no mistake, this practice affects mostly low-income workers—there is no income when he can't work and likely no health insurance to help with medical expenses.

But the employer lowers its costs.

In fact, Mr. Wade Horn, a contractor who testified at the hearing in March said that when companies misclassify their employees, they expect to reduce their labor costs between 15 and 20 percent.

In March, our witnesses were principally from the building trades and they told us how widespread misclassification is in that industry.

But misclassification occurs across a wide range of industries.

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I am very glad that Mr. Williams is here to testify about his experiences with Fed-Ex.

My own state of California is waging a battle against Fed Ex's practice of misclassifying its couriers as independent contractors.

And in 2004, the California Employment Development Department issued a payroll tax assessment of \$7.8 million against the Company because it failed to pay payroll taxes on employees that they had misclassified as independent contractors.

In California, misclassification is an enormous problem. The Insurance Commissioner has reported that 30% of employers in the State do not carry worker's compensation insurance—one of the sure signs that those employers' workers are being treated as independent contractors.

This problem has so concerned my State that there is a bill in the State Assembly, S.B. 622, which if passed will make willful misclassification illegal and assesses civil penalties of up to \$15,000 per violation and up to \$25,000 per violation for those employers have engaged in a pattern or practice of misclassification.

And our Attorney General has started a program to protect vulnerable workers from unscrupulous employers.

I am confident that this hearing will bring us closer to solutions to it.

Chairman ANDREWS. Thank you, Madam Chairman. I appreciate it.

I will now turn to the ranking member of the Workforce Protections Subcommittee, our friend from South Carolina, Mr. Wilson?

Mr. WILSON. Thank you, Mr. Chairman, and thank you, Madam Chairman, for conducting this hearing today.

Good morning. In the interest of moving on to hear directly from our distinguished panel of witnesses this morning, I will keep my remarks brief.

I look forward to hearing from our distinguished witnesses and, in particular, welcome a discussion of the current state of law as it relates to the classification of workers as employees or independent contractors.

As I said at our subcommittee's last hearing on this topic, a point borne out by the testimony of witnesses at that hearing, I expect that there may be many areas in which we agree and areas in which we disagree. I was particularly interested to note at our last hearing that there was significant agreement among the witnesses, Democrat and Republican, as to a number of points.

First, that the law relating to the classification of a worker as a contractor or employee is complicated, often confusing and, in many instances, not at all clear as to the proper outcome.

Second, that no one defends the practice of an employer purposefully or intentionally misclassifying workers.

Third, many agree that the laws, as written, are adequate to address these concerns. And many agree that our focus should be not on changing the laws or statutes we have on the books.

And finally, there was general agreement that the issue here may be one of enforcement, particularly targeted enforcement.

In that light, I especially welcome Wage and Hour Administrator Paul DeCamp. And I look forward to him telling us what his agency, which is but one of many charged with administrating the laws relating to contractor status, is doing to ensure that the law is being followed and administrated properly.

So with that in mind, I look forward to today's hearing and the testimony of our two panels of witnesses. And I yield back my time.

[The statement of Mr. Wilson follows:]

**Prepared Statement of Hon. Joe Wilson, Ranking Republican Member,
Subcommittee on Workforce Protections**

Good morning. In the interests of moving on to hear directly from our distinguished panel of witnesses this morning, I will keep my remarks brief.

I look forward to hearing from our distinguished witnesses, and in particular welcome a discussion of the current state of the law as relates to the classification of workers as employees or independent contractors.

As I said at our Subcommittee's last hearing on this topic—a point borne out by the testimony of witnesses at that hearing—I expect that there may be areas in which we agree, and areas in which we disagree. I was particularly interested to note at our last hearing that there was significant agreement among witnesses, Democrat and Republican, as to a number of points:

First, that the law relating to the classification of a worker as a contractor or employee is complicated, often confusing, and in many instances not at all clear as to the proper outcome;

Second, that no one defends the practice of an employer purposefully or intentionally misclassifying workers;

Third, that the laws, as written, are adequate to address these concerns, and our focus should not be on changing the laws or trying to “create” a failure in the statutes we have on the books;

And finally, there was agreement that the issue here may be one of enforcement, particularly targeted enforcement. In that light, I especially welcome Wage and Hour Administrator DeCamp, and look forward to him telling us what his agency—which is but one of many charged with administering the laws relating to contractor status—is doing to ensure that the law is being followed and administered properly.

So with that said, I look forward to today's hearing and the testimony of our two panels of witnesses and yield back my time.

Chairman ANDREWS. I thank Mr. Wilson.

And we welcome Mr. DeCamp to the subcommittees.

Mr. DeCamp, your written statement is accepted into the record, without objection, in its entirety. We would ask if you could summarize your written remarks in about 5 minutes.

I think you have testified here before and know the light system. When the yellow light goes on, you have about a minute left, and when the red light goes on, we would ask you to summarize.

Paul DeCamp is the administrator of the Wage and Hour Division of the United States Department of Labor, a post he has held since 2006. Prior to his appointment to this position by President Bush, Mr. DeCamp was a senior policy advisor to the assistant secretary of labor for employment standards.

He also practiced law with the firm of Gibson, Dunn and Crutcher in Los Angeles and here in Washington, where he focused on employment matters. Mr. DeCamp received his B.A. from Harvard and his J.D. from Columbia University. But he overcame these liabilities—

[Laughter.]

He clerked for the Honorable Alan E. Norris for the Sixth Circuit Court of Appeals.

Mr. DeCamp, we are delighted to have you with us this morning. Welcome to the subcommittees.

**STATEMENT OF PAUL DECAMP, ADMINISTRATOR OF THE
WAGE AND HOUR DIVISION, U.S. DEPARTMENT OF LABOR**

Mr. DECAMP. Thank you.

Chairman Andrews, Chairwoman Woolsey, Ranking Members Wilson and Kline, and distinguished members of the subcommit-

tees, thank you for the opportunity to appear before you today to discuss the misclassification of workers as independent contractors.

This type of misclassification can lead to a number of harms. Misclassified workers may find themselves without access to employers' benefits plans and without the protection of workers' compensation or unemployment insurance.

Businesses that comply with the law may be at a significant disadvantage with respect to competitors who elect to lower their operating costs by calling their employees independent contractors.

And the federal and state governments potentially lose out on tax revenues, at least to the extent that the misdesignated workers do not pay the taxes that their employers should have withheld.

One important point to understand at the outset is that misdesignation of employees as independent contractors is not, in and of itself, a violation of any of the approximately 70 laws that the Wage and Hour Division enforces.

If, for example, an individual works 40 or fewer hours in a workweek and receives compensation at least equal to the minimum wage, there is no violation of the Fair Labor Standards Act—the law that accounts for more than 80 percent of the agency's cases—even if the worker is misdesignated.

Therefore, the Wage and Hour Division historically has not focused resources on the independent contractor issue, per se. Instead, we look for the violations of our laws, such as failure to pay the required minimum wage or overtime, or the improper denial of family or medical leave, or the unauthorized transportation of migrant farm workers.

Approximately 60 percent of the Wage and Hour Division's enforcement centers on low-wage industries, where violations of the laws we enforce tend to be the most prevalent. The agency devotes more than one-third of its enforcement resources to nine of those industries, including such sectors as janitorial services, construction and landscaping. The agency's experience has been that many of these same low-wage industries tend to have a high incidence of misdesignation of employees as independent contractors.

In short, the Wage and Hour Division vigorously protects workers whose rights may be jeopardized by misdesignation as independent contractors. We do so, however, by focusing on their rights under the federal wage and hour laws.

The Wage and Hour Division's enforcement work represents a combination of investigating worker complaints and conducting investigations on the agency's own initiative in the absence of a complaint.

The agency recognizes that low-wage workers, among others, are often unlikely to report wage and hour violations for a variety of reasons. Therefore, we supplement our complaint-based investigations with strategically targeted cases directed at those industries and employers where we have reason to believe violations are going unreported.

Every year, the agency devotes extensive management resources to our annual strategic planning process, which is how we determine the types of issues and industries to focus on in the coming year. Those directed cases constitute around 20 percent of our caseload.

We also make available to workers and employers a significant amount of information regarding the issue of employee versus independent contractor. On our Web site, we have fact sheets that explain the applicable rules. Much of this information is available in Spanish, Chinese, Thai, and Vietnamese.

We also have an interactive advisor on our Web site that allows a user to answer some questions and then receive guidance regarding how a worker should be classified. Our Web site also includes a chapter from our field operations handbook regarding, among other things, the employment relationship.

In addition, the agency conducts approximately 2,000 training and outreach events each year. When we address workers or businesses in industries where misdesignation as independent contractors is a significant concern, we provide information on that issue.

One final point that I would like to discuss involves communication with other government entities. The Wage and Hour Division is very reluctant to provide information to other agencies where doing so might jeopardize our enforcement mission.

In order to be able to protect the wage and hour rights of all workers, we need information from workers regarding violations. If workers are hesitant to report violations to us, it becomes much more difficult to maintain the integrity of the labor standards set forth in our statutes.

Many of the employers we investigate are in low-wage industries that employ ever-increasing numbers of undocumented workers. We, therefore, need to be very careful to avoid taking steps that would have the unintended consequence of deterring those workers from seeking our assistance.

If workers believe that they may be worse off for having contacted the Wage and Hour Division, we will not hear from them. And then workers lose, as a result. It is important to our agency that we avoid that outcome.

Thank you. And I will be happy to answer any questions that the subcommittees may have.

[The statement of Mr. DeCamp follows:]

Prepared Statement of Paul DeCamp, Administrator of the Wage and Hour Division, U.S. Department of Labor

Chairwoman Woolsey, Chairman Andrews, Ranking Members Wilson and Kline, and distinguished members of the Subcommittees: Thank you for the opportunity to discuss the efforts of the Department of Labor's Wage and Hour Division (WHD) to promote compliance with the Nation's labor standards laws. WHD has a strong record of enforcement on behalf of workers in this country, including employees who have been misclassified as independent contractors.

WHD employs a number of strategies for ensuring that employees are paid in accordance with the laws WHD enforces. Many of these strategies address worker classification issues. Before discussing these strategies, however, it is important to understand the backdrop against which these strategies are implemented. The misclassification of an employee as an independent contractor is not itself a violation of the Fair Labor Standards Act (FLSA) or the many other laws that WHD enforces. The Government Accountability Office (GAO) acknowledged this fact in its 2006 audit, *Employment Relationships: Improved Outreach Could Help Ensure Proper Worker Classification* (GAO-06-656). In that report, GAO also accurately noted that, despite the fact that such misclassification is not a violation of the FLSA, WHD nevertheless detects and addresses the issue of employees who have been misclassified as independent contractors in its investigations of employer compliance with the FLSA. It is critical to understanding WHD's approach to enforcing the provisions

of the various statutes for which it is responsible that one also understand that the act of misclassification is not a violation of the FLSA.

Determining An Employment Relationship Under The Federal Wage And Hour Laws

Under most labor standards laws, an employer-employee relationship must be established in order for the law's provisions to apply. The FLSA, which establishes minimum wage, overtime, and child labor protections, defines "employee" more broadly than virtually any other federal statute. In cases such as *Rutherford Food Corp. v. McComb*, 331 U.S. 722 (1947), *United States v. Silk*, 331 U.S. 704 (1947), and *Bartels v. Birmingham*, 332 U.S. 126 (1947), the U.S. Supreme Court provided guidance for determining whether a worker is an employee under the FLSA, and those rulings continue to inform how WHD and the courts analyze the issue today. The Court provided that an employee, as distinguished from a person who is engaged in a business of his or her own (i.e., an independent contractor), is one who, as a matter of economic reality, is dependent on the business that he or she serves.

The Court further indicated that there is no single rule or test for determining whether an individual is an independent contractor or an employee for purposes of the FLSA. Instead, the determination must be based on the totality of the circumstances and not on a single criterion. The relevant factors include the following:

- The extent to which the services rendered are an integral part of the principal's business;
- The permanency of the relationship;
- The amount of the alleged contractor's investment in facilities and equipment;
- The nature and degree of control by the principal;
- The alleged contractor's opportunities for profit and loss;
- The amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor; and
- The degree of independent business organization and operation.

See, e.g., *Silk*, 331 U.S. at 716; *Brock v. Mr. W Fireworks*, 814 F.2d 1042 (5th Cir. 1987); *Donovan v. DialAmerica Mktg.*, 757 F.2d 1376 (3d Cir. 1985).

I mention these specific factors for two reasons. First, all WHD investigators must use these criteria to establish an employment relationship to pursue remedies on behalf of workers under most of the statutes the agency enforces, including the FLSA and the Family and Medical Leave Act (FMLA). As a consequence, investigators will, at various stages throughout the investigation, examine how an employer classifies its workers. For example, investigators will ask for information during the initial conference with an employer to establish the employer's classification practices. Investigators will review records including without limitation payroll records, cash disbursements journals, check registers, and 1099s to ensure that all workers are identified and that any worker not listed on the payroll is properly compensated. As a normal part of investigations, WHD investigators will tour an employer's establishment and question workers about their pay, their duties, and their working conditions, as well as those of their co-workers, looking for, among other things, potentially misclassified employees. As GAO noted in its audit, when WHD investigators suspect that employers are not properly classifying workers as employees, the investigator will pursue several avenues of investigation to ascertain whether a violation of a wage and hour statute has occurred.

The second reason for highlighting the FLSA employment relationship factors is to distinguish these criteria from the test used by the Internal Revenue Service (IRS) in applying the common law "right to control" test often used by the courts and from the definitions and standards set forth in other statutes. WHD acknowledges that the issue of employee misclassification raises a number of concerns wholly outside the responsibility or authority of WHD. The misclassification of workers may affect some state programs such as worker compensation and unemployment insurance programs, in addition to other federal and state worker protection statutes. Finally, misclassification issues may involve the IRS and the Social Security Administration.

Consequently, in establishing an employment relationship under the FLSA, there may be instances where WHD investigators identify potential misclassification issues of other programs or statutes. WHD has no authority or expertise, however, to interpret or to enforce provisions outside its jurisdiction. In many instances, the misclassification of a worker under the FLSA will not, given the broad interpretation of the FLSA, result in a violation of another statute or program.

WHD Strategies For Enforcing Labor Standards Provisions Relating To Independent Contractor Issues

The labor standards that WHD enforces provide basic protections for all workers in this country. Although they differ in scope, all of the statutes enforced by WHD

are intended to protect the welfare of the Nation's workforce and to ensure fair compensation for work performed. Minimum wage, overtime, and child labor cases constitute the majority of WHD's enforcement responsibilities. FLSA cases represent approximately 84 percent of all WHD cases, and FMLA investigations an additional one percent. The Migrant and Seasonal Agricultural Worker Protection Act (MSPA), the Davis-Bacon Act (DBA), and the McNamara-O'Hara Service Contract Act (SCA) are other key statutes enforced by WHD.

Misclassified workers may be identified during the course of investigations that cover many provisions and statutes enforced by WHD. For example, WHD investigators must establish an employment relationship under the FMLA and most of the MSPA provisions. Investigations into compliance with these program areas necessarily contain an element of inquiry into the status of workers as employees.

Under DBA and SCA, however, WHD does not need to establish such an employment relationship. According to the statutory language of the DBA, laborers and mechanics are entitled to prevailing wage rates "regardless of the contractual relationship that is alleged to exist between a contractor or subcontractor and such persons." Similar language applies to service employees performing on Federal service contracts. Under these two statutes, the individuals performing work are entitled to prevailing wage and fringe benefit compensation even if they are classified as independent contractors.

Because erroneous classification of an employee as an independent contractor is not itself a violation of the federal wage and hour laws, WHD does not maintain data regarding how many cases present that issue. Thus, WHD cannot provide statistics regarding the prevalence of misclassification. However, there have been instances in which a misclassification resulted in a minimum wage or overtime violation. These cases clearly demonstrate WHD's attention to potential violations that may result from the improper designation of workers. The following are some recent examples:

- In November 2006, WHD collected nearly \$75,000 in back wages for 76 employees of an Ohio construction contractor that had misclassified its workers as independent contractors.
- In October 2006, a Houston construction company paid nearly \$130,900 in back wages to 81 employees who had been misclassified.
- The Department sued a Houston drywall company in August 2006, to recover over \$500,000 in back wages on behalf of misclassified employees who were working to rebuild the Mississippi Gulf Coast casinos following Hurricane Katrina.
- In a similar case involving the employees working to rebuild the Gulf Coast region, WHD collected over \$362,000 in back wages from three construction firms that had misclassified employees as independent contractors.
- In March 2006, the Department sued a Glendale, California, janitorial company for \$900,000 in back wages that resulted from the company's improper practice of classifying the workers as independent contractors.

WHD has, for a number of years, prioritized its statutory enforcement responsibilities to maximize protections for workers, including the most vulnerable in the workforce: low-wage, immigrant, and young workers. WHD receives approximately 30,000 complaints during a fiscal year and utilizes approximately 70% to 78% of the program's enforcement resources to resolve complaints. In addition to its responsibilities to respond to allegations of noncompliance, WHD has devoted between 22% and 30% of its enforcement resources to targeted investigations (i.e., investigation initiated without a complaint), the focus of which is in low-wage industries that employ large numbers of vulnerable, low-skilled workers.

These industries, such as construction, janitorial, restaurants, landscaping, agriculture, garment manufacturing, and health care, are often characterized by the employment of immigrant workers who are particularly vulnerable to exploitation, as well as young workers who are not fully versed in FLSA protections. Investigations in these industries tend to disclose high rates of FLSA minimum wage and overtime violations. Moreover, it is the experience of WHD that undocumented workers, many of whom may have been misclassified as independent contractors or have been engaged in contingent employment relationships, account for an increasing percentage of employees in these industries.

WHD initially focused its low-wage program on the three nationally targeted industries of garment manufacturing, agriculture, and health care. While compliance efforts continue in those identified industries, in FY 2004 WHD began expanding its low-wage program to include a broader group of identified low-wage industries. Working with external evaluators, WHD identified approximately 33 low-wage industries in which workers were most likely to be the subject of a minimum wage or overtime violation. This research enabled the agency's local and regional offices

to identify and to target in their geographic areas industries with the most serious compliance issues.

In FY 2006, WHD collected nearly \$50.6 million in back wages for approximately 86,700 workers in nine of the larger group of low-wage industries, an increase in back wages collected in the same low-wage industries of over 10% as compared to the previous fiscal year. Over a third of WHD enforcement resources are attributed to investigations in nine low-wage industries, which include day care, restaurants, janitorial services, landscaping, and temporary help. This fiscal year, WHD is conducting over 100 initiatives in low-wage industries. These compliance initiatives are concentrated in restaurants, retail, construction, janitorial, hotels and motels, and health care. WHD offices in garment manufacturing centers are continuing their enforcement efforts to increase compliance in that industry. WHD offices also have enforcement and compliance assistance activities in agriculture and reforestation. Again, these industries share common characteristics with the industries in which employees are most likely to be misclassified as independent contractors.

As a complement to its enforcement activities, WHD has an active compliance assistance program that takes advantage of opportunities to educate employers and employees about the laws that it enforces. WHD outreach to the employer and employee community is a critical component of its overall compliance program because it aims to ensure that employers have information on the statutory and regulatory requirements in a clear and concise manner and that employees are versed in their rights and the remedies available to them. In its 2006 audit, GAO acknowledged WHD's outreach to workers and to employers on employment relationship concepts and the agency's procedures for its field staff in identifying and reporting potential misclassification issues to other Federal agencies.

Among the examples of compliance assistance information noted by GAO is Fact Sheet 13: Employment Relationship Under the Fair Labor Standards Act (FLSA), which describes the factors involved in determining whether an individual is an employee under the FLSA and where to find additional information or help in making such a determination. This fact sheet is available in Chinese, Korean, Spanish, Thai, and Vietnamese, as well as English. The Employment Relationship fact sheet and others like it, including various industry specific fact sheets, are available on WHD's web site. The Employment Laws Assistance for Workers and Small Businesses (elaws) FLSA Advisor, also on the web site, is another tool that provides an interactive mechanism for employers and workers to determine whether a worker is an employee under the FLSA.

In addition to these electronic and printed materials, WHD field personnel participate in a variety of outreach activities such as seminars, training programs, and community-based activities, including Spanish-language radio and television programs. WHD distributes worker rights cards to day laborers, health care workers, garment workers, and farmworkers, among others, in order to inform workers of their rights and to prevent misclassification from happening in the first place.

Justice and Equality in the Workplace Program

To further increase awareness of relevant labor laws, to encourage greater employer compliance with those laws, and to assist vulnerable workers in achieving the protections to which they are entitled, WHD has also developed strategic partnerships and collaborations with businesses and trade associations; labor unions; federal, state and local government agencies; faith- and community-based organizations; and foreign agencies. Just one example is the established in Houston, Texas, to educate low-wage immigrant and non-immigrant workers about their rights under federal law and to bring the employers of these workers into compliance through education and enforcement.

In summary, WHD balances three complementary strategies—compliance assistance, partnerships and collaborations, and strong complaint-based and targeted enforcement—to promote and achieve compliance on behalf of all employees, including those who have been misclassified as independent contractors.

WHD Response To GAO Recommendations To Improve Outreach To Facilitate Proper Worker Classification

As mentioned previously, GAO examined WHD's role in identifying and addressing instances in which workers were misclassified as independent contractors. While recognizing WHD's efforts in addressing instances of worker misclassification under the FLSA, GAO had two recommendations for WHD. Both have been addressed by WHD.

First, GAO recommended that because WHD's enforcement program was primarily complaint-based, the FLSA poster should be modified to provide additional contact information. This revision was intended to facilitate the reporting of possible

misclassification complaints that also alleged minimum wage or overtime violations. WHD agreed with the recommendation, and the new FLSA poster prominently displays the agency's toll-free number and web site address. Calls to the toll-free number are answered by call center staff who refer complainants to the appropriate WHD local office. The call center has Spanish-speaking customer service representatives and an interpreter service that supports 150 languages.

Second, GAO recommended that WHD evaluate the extent to which misclassification cases identified through FLSA investigations are referred to the appropriate federal or state agency potentially affected by employee misclassification, and take action to make improvements as necessary. GAO also suggested that WHD build upon efforts by its district offices currently engaged in such referrals. Finally, GAO indicated that any referral of cases should include notifying the employer that the misclassification case has been forwarded to the appropriate agency.

WHD agreed with GAO that there is value in sharing potential employee misclassification with appropriate federal and state programs. As a result, WHD reviewed its internal processes for referral of potential employee misclassification to other agencies with all first-line field managers during a national managers training conference in May 2007. To ensure that all WHD district offices refer employee misclassifications that could lead to potential violations of laws enforced by other agencies, the first-line managers were reminded to follow the agency's longstanding Field Operations Handbook instructions and to refer such violations using the established form WH-124.

We believe that an explicit policy of automatic referrals to all other agencies, however, could have an adverse impact on WHD's mission and ultimately harm those workers whom the agency is tasked with protecting. If it becomes common knowledge that WHD routinely refers potential violations to some agencies it would hinder the agency's ability to persuade employees to report violations of the wage and hour laws or otherwise voluntarily provide workplace information. Moreover, employers would be less likely to produce copies of written documents or records if they believed such documents were going to other law enforcement authorities for reasons unrelated to the labor standards investigation. As a result, WHD would be required to compel the release of information through the courts, a timely and costly means of enforcing federal labor standards. In addition, because the definition of "employee" under the FLSA is more inclusive than the definition used in many other statutes, a determination of misdesignation of an employee as an independent contractor by WHD may not be applicable for other purposes. Accordingly, WHD disagrees with GAO that referral is appropriate in all instances and believes that determinations as to whether to refer a matter to another agency must be made after considering the particular circumstances. In terms of the worker protections that WHD is trying to ensure, there are tradeoffs in reporting to other agencies, and whether or not reports are made represents the outcome of a balancing of benefits and costs for the workers the agency is trying to help.

WHD also does not agree with GAO's recommendation that employers be notified when WHD refers potential misclassification cases involving laws not enforced by the WHD to another agency. As WHD explained, this type of process would place WHD staff in the untenable position of explaining or defending a referral based upon interpretations of laws concerning which WHD has neither expertise nor interpretive or enforcement authority.

Future WHD Compliance Activities

Over the last several years, WHD has planned a number of compliance initiatives in low-wage industries to address the more common violations, such as off-the-clock violations and misclassification of executive, administrative, and professional employees as exempt personnel. In support of its compliance priorities in low-wage industries, WHD's FY 2008 performance plan focuses on addressing the violations that may arise from employment relationships not designated as such, especially those involving contingent workforces, misclassified employees, and subcontracting structures. Each of the agency's regional and local district offices' low-wage initiatives will include compliance activities in at least one of the low-wage industries in which independent contractor misclassifications are common. WHD is committed to promoting compliance in low-wage industries and to ensuring that the designation of workers as independent contractors does not result in violations of the labor standards laws that we enforce.

Madam Chairwoman, Mister Chairman, this concludes my prepared remarks. I will be happy to answer any questions that you or the Members of the Subcommittee may have.

Chairman ANDREWS. Thank you very much, Mr. DeCamp. We appreciate it.

On page four of your testimony, you indicate that the division receives about 30,000 complaints a year. And then the resolution of those complaints absorbs between 70 and 78 percent of your enforcement resources. Between 22 and 30 percent of your enforcement resources are to targeted investigations.

How many targeted investigations do you do in a year?

Mr. DECAMP. I think it varies, depending on the year, depending on the resources available, but somewhere in the neighborhood, I believe, of 7,000 to 10,000 a year.

Chairman ANDREWS. Of the 7,000 to 10,000 a year, how many are for violations of the Fair Labor Standards Act?

Mr. DECAMP. That is about 80 percent of our caseload, 5,000 to 6,000 probably.

Chairman ANDREWS. Okay. So it would be 80 percent of that?

Mr. DECAMP. Or more.

Chairman ANDREWS. And a precondition to pursuing an FLSA claim is that there be an employer-employee relationship, correct?

Mr. DECAMP. Correct.

Chairman ANDREWS. So of those FLSA investigations that you have conducted, how many of them yield the result that there is a misclassification of an employee who should be under FLSA but isn't?

Mr. DECAMP. We don't really track the cases that way because independent contractor versus employee is a coverage issue, rather than a violation issue. So we haven't historically kept records of how the violations came about.

Chairman ANDREWS. I would think if you did some data-mining you would be able to figure that out, right, because if you follow up on an FLSA violation claim, by definition, the person is an employee, right? You wouldn't be pursuing the claim if you conclude the person is not an employee.

Mr. DECAMP. If we get to the end of the investigation and have concluded that, yes, the person is an employee, then, yes, we would have found that person is covered.

Chairman ANDREWS. So some subset of those investigations that you get to the end, you have made a prior determination that the person is an employee or there has been some dispute about that, right?

Mr. DECAMP. Yes, except that information isn't necessarily reflected in the case file or in the records.

Chairman ANDREWS. So if one of your inspectors goes into an employer and says, "These 12 people are not being paid overtime," the employer says, "Well, they are not employees; they are independent contractors," there is nothing in your case file that would say that that defense was raised?

Mr. DECAMP. There might or there might not be. And it is not in the computer records, which is the basis from which we would really pull data together.

Chairman ANDREWS. Would you favor a statutory change that would require you to keep that kind of record?

Mr. DECAMP. I take no position on that.

Chairman ANDREWS. You think it would be a good idea?

Mr. DECAMP. I don't know that it would help our enforcement mission in terms of protecting the workers.

Chairman ANDREWS. Well, let us look at this for a moment.

In New Jersey, in 2006, 871 audits of the construction industry were conducted. And in 41 percent of those cases, the finding was that there was a misclassification of workers.

Do you have any basis to either agree or disagree with—if one were to put forth the proposition that that is typical of across the country, are you in a position to agree or disagree with that statement?

Mr. DECAMP. I don't know in terms of the specific numbers whether the New Jersey results would generalize nationwide. But I would agree, certainly, that in construction, that is a low-wage industry with a high incidence of misdesignation.

Chairman ANDREWS. So you think it would be fairly probable there would be a high incidence of misclassification?

Mr. DECAMP. Yes.

Chairman ANDREWS. Okay.

Another thing that you say in your testimony repeatedly is that misclassification of an employee as an independent contractor is not, in and of itself, a violation of the FLSA, correct?

Mr. DECAMP. Correct.

Chairman ANDREWS. Should we make it a violation of the FLSA?

Mr. DECAMP. Well, it depends on what the policies of the FLSA are. Currently, the FLSA is about making sure that people are getting minimum wage and overtime, among other things.

Chairman ANDREWS. Well, which people?

Mr. DECAMP. Covered employees.

Chairman ANDREWS. Okay. So if there is a dispute about systematic misclassification of covered employees, wouldn't it be logical—if the public policy behind that statute is to say that people who are in an employer-employee relationship should get overtime, should get minimum wage, should get the other protections, wouldn't it be logical to make it one of the enforcement duties to make that determination?

Mr. DECAMP. Again, it is an issue of whether the workers have been harmed. If—

Chairman ANDREWS. Well, they have been harmed, haven't they? If someone has been misclassified and not being treated as an employee, and they don't get overtime for their 41st hour, they have been harmed, right?

Mr. DECAMP. Well, sure. And in that case, we would assert an overtime violation under the FLSA.

Chairman ANDREWS. So would you favor making a violation of the FLSA the misclassification of employees? Is that a good idea?

Mr. DECAMP. I don't think it is because we already protect the workers by enforcing their rights to minimum wage and to overtime.

Chairman ANDREWS. But how do you protect the workers if they have been misclassified? Because you just told us that you don't keep records of that. So if someone had been misclassified and the investigation was not properly handled, you wouldn't know, would you?

Mr. DECAMP. If the worker has been misclassified, then we would assert an employment relationship, and then we would look to see whether their rights to minimum wage or overtime had been violated.

Chairman ANDREWS. But you don't know in how many cases you have done that because you don't keep track of it. You assume that your field people have done that, but you don't know, do you?

Mr. DECAMP. I don't know whether people have kept track of the independent contractor issue. It is not part of the computer database.

Chairman ANDREWS. No. But if an employer has raised a defense that someone is an independent contractor, not an employee, your database doesn't let you keep track of how you have resolved that defense, does it?

Mr. DECAMP. I don't believe that it does.

Chairman ANDREWS. Okay. Thank you.

I see my time is up. Mr. Kline is recognized for 5 minutes.

Mr. KLINE. Thank you, Mr. Chairman.

And thank you, Mr. DeCamp.

We are in these continuing discussions of lawyers and lawyers here, so I will admit, once again, that I am not one, so I need to cut down to some sort of basics here.

We heard in the previous hearing, I think one of our colleagues said that the issue of whether an individual worker is a contractor or an employee isn't that complex. Would you agree with that?

Mr. DECAMP. I think it really depends on the situation. I think there are many employment relationships where it is perfectly clear who is an employee and who wouldn't be. I think there are certain industries where it becomes difficult to draw the lines. I think construction and some of the industries that we have talked about present some of the more challenging gray areas.

Mr. KLINE. So in some cases it may be, in fact, quite complex, and others it might be pretty straightforward. I think Mr. Andrews indicated some cases where it might be pretty straightforward and others where it is not clear at all. He talked about people mowing lawns. Well, sometimes that may be clear that they are an employee, and sometimes it is clear that they are an independent contractor. So just what industry you are in and what job you are doing may not be the best indication of that.

Now, let us get to a couple of things here, because I am going to run out of time.

In its examination of misclassification cases, the GAO made a number of recommendations to the Wage and Hour Division. Can you explain in more detail what these recommendations were and how the division has responded to GAO's recommendations?

Mr. DECAMP. There were really two recommendations the GAO made in the report.

One of the recommendations was to include contact information on our workplace poster that would explain to workers how to contact the Wage and Hour Division in order to pursue issues, to present a complaint. We have addressed that by including the toll-free number for the Wage and Hour Division on our poster.

The second recommendation was that we regularize, I guess would be the best way to put it, our processes for communicating

information about potential violations to other agencies. That is an issue where we continue to examine how best to approach that issue, because there are pros and cons to dealing with other agencies, such as IRS or other agencies, as well.

We need to balance the need to enforce and protect those other laws that are outside our agency's jurisdiction with the need to maintain the integrity of our enforcement mission.

Mr. KLINE. Okay. Thank you.

Now, I want to go back, because I am still thinking about this, how your division works. Let us take a for-instance case, a hypothetical. You have someone working for a company, Company A, and they are working as an independent contractor. But, in your judgement, they have been misclassified.

Mr. DECAMP. Okay.

Mr. KLINE. You are not concerned with that as a matter of a violation of law. But if that person who has been misclassified is making less than minimum wage, for example, what would you do? What would your department do?

Mr. DECAMP. We would assert a minimum-wage violation and pursue back wages or any other remedies that were appropriate.

Mr. KLINE. Okay. So even though they are an independent contractor, and neither the worker nor their employer is breaking a law because of that—or not being held accountable because of your department—nevertheless, because they were getting less than minimum wage, your department would take action. Is that correct?

Mr. DECAMP. Well, we would say that they are being held accountable for the substantive violation of the Fair Labor Standards Act, the minimum-wage violation.

Mr. KLINE. Right. But the misclassification itself is not an issue with you, and so, because of that, you are not recording that. It is not in your computer database.

Mr. DECAMP. Right—

Mr. KLINE. But the fact that there was a violation that they were not paid the minimum wage or perhaps weren't paid overtime, those the employer is held accountable for. Is that correct?

Mr. DECAMP. Right. Technically, the Fair Labor Standards Act does not require that employees be classified one way or another. It requires that employees who are genuinely employees under the law receive overtime and receive minimum wage as required by the law.

Mr. KLINE. Okay. I see my yellow light is coming on.

Let me just explore something else with you. You have cases where people are reluctant to come forward and make a complaint. You probably also have cases where you have workers who prefer that status to the employee status and wouldn't come forward either. Is that correct?

Mr. DECAMP. That is probably fair to assume.

Mr. KLINE. Okay. I yield back.

Chairman ANDREWS. Thank you very much.

I recognize the gentlewoman, the chairperson of the Labor Standards Subcommittee, Ms. Woolsey, for 5 minutes.

Ms. WOOLSEY. I feel like we are going backwards, Mr. Chairman. We get to a point where we know we have a problem. And we ask

the agency, the department who we think should be responsible for protecting all workers, and all we hear is that it ain't their responsibility.

So let me ask you who, then, if not the Department of Labor, is responsible for protecting all employees? And whose mission is it to investigate? And if we, the Congress, and if our laws are making it impossible for you to do your job, what is it we need to change?

Because these answers are not acceptable. The answers to our questions in the letter were the same kind of gray mushy mush. It is probably not your fault; maybe you can't be any clearer than this.

We have to get clear. We know we have workers that are called one thing and are another. And they are not getting their full benefit from being a working American.

So give us some guidance. What can we do?

Mr. DECAMP. Well, again, I think the agencies that enforce the particular statutes are the ones who protect the workers.

For example, the wage and hour rights: The Wage and Hour Division very aggressively pursues cases in low-wage industries where misdesignation of independent contractors is common. We protect those rights to minimum wage, to overtime.

Ms. WOOLSEY. But you don't know who they are.

Mr. DECAMP. We do.

Ms. WOOLSEY. You don't keep track of them.

Mr. DECAMP. We do know who they are because we are very active in the workplaces where these people are working, where these issues arise. We are active in the industries. So we go to the work-sites. And we don't care how an employer wants to designate a worker, as an independent contractor or an employee.

Ms. WOOLSEY. Well, then let me ask it another way. Why are there so many of them still? What is wrong with the way you are doing your jobs?

Mr. DECAMP. I wouldn't say there is anything wrong with the way we are doing the job. I think it is partly a resource issue, frankly. I would love to see the agency able to do more investigations, to have more investigators, to be more active. And that is mainly a resource constraint.

And, frankly, you know, the administration has asked for additional resources. And I hope that we will receive additional resources so that we can do more of these investigations.

Ms. WOOLSEY. Well, get back to us about that. That is what we are trying to find out. What do we need to do?

Mr. DECAMP. Again, I think it is about getting more investigators on board so that we can do more targeted investigations. I think targeted investigations in low-wage industries are the most important tool that we have to try to protect these workers, because many low-wage workers don't come to us. They have concerns about immigration status or other concerns where they don't come to us.

Ms. WOOLSEY. Well, what does an inspector do? Do they need to be called into the place of employment? Do they need to interview the workers? Do they need to interview the employer?

Mr. DECAMP. Right, well, investigations can come about in a couple of different ways. One is that we may receive a complaint from

a worker or from another interested party, in which case that might spur an investigation.

Another way is that we may, as part of our strategic planning process, decide we need to target this industry this year. And so, without a complaint, we might go into several workplaces and conduct an investigation, which would involve examining records, interviewing workers, interviewing all sorts of personnel to try to figure out what is going on in the workplace.

Ms. WOOLSEY. And, well, how long have you been in this position, Mr. DeCamp?

Mr. DECAMP. Since August of last year.

Ms. WOOLSEY. Okay. Give us some examples of a success story, where you made a difference for a misclassified group of employees.

Mr. DECAMP. Well, the department filed a lawsuit recently against Benitez Drywall Company, where the issue was misdesignation of employees as independent contractors. So we have pursued remedies for them in court.

I have outlined, actually, in the testimony on page four, a number of recoveries that we have had, or also litigations that we have commenced.

We have another case in Glendale, California, a janitorial company, where we sued them for \$900,000 in back wages.

Chairman ANDREWS. Will the gentlelady yield?

Ms. WOOLSEY. Yes, I will.

Chairman ANDREWS. Were those two cases initiated by the department, or were they a result of complaints by workers?

Mr. DECAMP. We actually don't disclose that information because of concerns about retaliation for the workers involved. I can tell you that on—

Chairman ANDREWS. Okay. But if they were initiated by the department, you wouldn't have that concern, would you?

Mr. DECAMP. I am sorry. I didn't understand.

Chairman ANDREWS. If the cases were initiated by the department, you know, that would not be an issue, would it? In other words, you respond to complaints, and then you initiate some audits.

Mr. DECAMP. Right.

Chairman ANDREWS. Were these initiated by audits, or were they complaints?

Mr. DECAMP. Well, this is what I am saying. If we identify only the cases that were initiated by the department, that also identifies which cases were initiated by complaints. [Laughter.]

Chairman ANDREWS. Okay.

Ms. WOOLSEY. Mr. Chairman, may I reclaim my time?

Is there follow-up? Do you know what that industry is doing now? Do you know what like industries are doing because of the initial complaint?

Mr. DECAMP. Well, whether or not it is a complaint, in those cases, they certainly received a lot of publicity. We are hoping that that has a spillover effect to increase compliance.

But we know we need to remain very active in janitorial work, in construction, and in these other low-wage industries. A continuing enforcement presence is going to be critical in those industries.

Ms. WOOLSEY. My time has expired.

Chairman ANDREWS. The chair recognizes the gentleman from South Carolina, Mr. Wilson, for 5 minutes.

Mr. WILSON. Thank you, Mr. Chairman.

And I want to join with my colleague from Minnesota, Colonel Kline, and express, as a fellow attorney, how happy I am to be in the presence of so many fine attorneys.

As we begin this morning, we have heard testimony about the IRS 20-factor test, as well as other tests used by other federal agencies and departments.

Can you tell us, are all of these tests consistent? What factors does IRS look at that Wage and Hour Division does not? And, perhaps most important, do each of these tests always produce the same result?

Mr. DECAMP. To take the last question first, my understanding is that the tests do not necessarily yield the same result in all cases.

As I mentioned before, there are many situations where the tests would all come out the same way regarding somebody who is clearly an employee as an employee.

But in the grayer areas—in construction, in some of these other types of industries that we are talking about where compliance is a particular concern—there may be differences in the outcomes under the tests.

The test that we use under the Fair Labor Standards Act is the economic realities test, which was set forth by the Supreme Court in a number of cases beginning in the 1940s. And what that is really looking at is: Is the worker functioning as an independent business, or is the worker functioning more as a traditional employee?

The IRS test—and I am not even certain that they still use the 20-factor test—is dealing with the common law right-to-control test, which has a different focus. I am not an expert in what factors the IRS uses. But I think that, given that they are looking at these statutes from more of a revenue than a wage perspective, I suspect that that is more of a focus of their inquiry. But I can't get into details of the IRS test. I am not an expert on that.

Mr. WILSON. You had indicated correctly that IRS is looking at the financial side of it. Is there anything that Wage and Hour specifically looks at that they wouldn't look at?

Mr. DECAMP. Again, I can talk about what Wage and Hour looks at, but I am truly not familiar with the way IRS goes about its task.

Mr. WILSON. Setting aside the issue of lost revenue, what sorts of damages will an employee who is misclassified be entitled to? In the absence of minimum-wage or overtime violations, are there other damages that misclassified workers suffer? Are these enforced by the Wage and Hour Division?

Mr. DECAMP. Again, with regard to the statutes that the Wage and Hour Division enforces, our focus is going to be on minimum wage and overtime primarily under the Fair Labor Standards Act. We also deal with other types of issues under the Family Medical Leave Act and the other 70 or so statutes that we enforce.

Generally, we are talking about back wages, and we may be talking about liquidated damages. We may be talking about other remedies that would be available for violations.

But I wasn't sure whether the premise of your question was that there was no overtime or minimum-wage violation.

Mr. WILSON. Right.

Mr. DECAMP. There may also be other issues that are outside the scope of Wage and Hour's jurisdiction, such as contributions to benefits plans, tax payments, you know, employment insurance payments, unemployment insurance payments, workers' comp. These may be harms that a worker would suffer if the worker is misdesignated under those statutes, under the IRS statutes or under state or other insurance programs.

Mr. WILSON. And it is so important that persons know their rights. Practically, how does this work? Is there a poster that is placed at workplaces? How do people know?

Mr. DECAMP. Well, we have a number of pamphlets and brochures and information on our Web site that helps to clarify this issue. We have fact sheets on our Web site that explain the difference between an employee and independent contractor, focusing on the tests that the Supreme Court has articulated for our statute.

We have a chapter from our field operations handbook that explains the employment relationship. We also have a lot of informational programs that we put on where we will talk to workers, we will talk to employers, and we will explain these tests and we will take questions to try to clarify.

We also have, as I mentioned in my opening statement, an advisor on our Web site, where, by responding to a few questions, the Web site will give guidance to a worker or to an employer or anyone else about the proper designation status.

Mr. WILSON. And there are training schools for technical students that I think would come right into this. Are the rights explained to students as they are taking courses in technical schools?

Mr. DECAMP. I don't know about technical schools.

Mr. WILSON. I just think that would be a way to reach really bright young people who are learning skills.

I yield the balance of my time.

Chairman ANDREWS. I thank the gentleman for yielding. I think that is an interesting idea about some training course, perhaps something we could pursue together in the Higher Education Bill.

Mr. WILSON. Yes.

Chairman ANDREWS. That is a good idea.

The chair recognizes the gentleman from Michigan, Mr. Kildee, for 5 minutes.

Mr. KILDEE. Thank you, Mr. Chairman.

Mr. DeCamp, you talked about a lack of resources to respond to complaints. Is that a lack of depth of response or just a lack of any response at all to the complaints?

Mr. DECAMP. I think the more resources that we have, the more investigations we can do and the more thorough we can be in the investigations that we do.

Mr. KILDEE. Are some not investigated at all because of a lack of resources, or is it a question of the depth of the response?

Mr. DECAMP. We investigate the complaints we receive. And then with the resources that are available over and above responding to the complaints, that is how we do our targeted investigations.

So the more resources we have over and above those that are necessary to respond to the complaints we receive, the more targeted investigations we can do.

Mr. KILDEE. Were your budgetary requests this year higher than what you had received previous years?

Mr. DECAMP. Yes, by about 10 percent.

Mr. KILDEE. And did the budget sent to the Congress reflect that difference?

Mr. DECAMP. Yes, sir.

Mr. KILDEE. I thank you very much.

Chairman ANDREWS. I thank the gentleman for his time.

I recognize the gentleman from Louisiana, Dr. Boustany, for 5 minutes.

Dr. BOUSTANY. Thank you, sir.

I guess we have to admit that the workforce or the workplace is a very complex and diverse area with regard to relations among workers and those who deal with the transactions of, you know, paying out for work and so forth. And I am struck by the fact that the tests that were talked about did not always yield the same results.

And so there are a number of variables out here that really complicate this. And God bless you for trying to figure it all out. It seems very complicated to me. I am just a heart surgeon. [Laughter.]

I would also think that workforce shortages which we are seeing, particularly in the construction area, certainly in my state of Louisiana and I think nationwide, would also create a different type of variable in this that would have some impact on whether somebody is misclassified versus wrongfully classified.

Because if you have a workforce shortage with plumbers or carpenters or some group like that, then clearly you will get a lot of free agents out there trying to do things. So trying to sort through this would seem to be very difficult.

I wanted to talk to you about the strategic targeting a little bit and explore that. Could you tell us a little bit more about the process? You said that you have a strategic planning session each year. You devote I forget how much of your resources to that? Could you tell us a little bit more about the process and how you go through that?

Mr. DECAMP. Well, each year we try to plan our targeted enforcement priorities for the coming fiscal year. Now, it is an annual process. It takes several months.

And it is an iterative process where we will get our senior leadership team involving career professionals, as well as the leadership of the agency, together in the same room to brainstorm, largely to talk about, you know, are there particular industries where we are seeing emerging problems of compliance? Has there been confusion? Is there willful conduct in a particular industry or a particular region? Or other types of issues where we feel that expendi-

ture of resources and targeted investigations can really affect compliance in a positive way.

And so we have several sessions over the course of the year where we refine our plans for targeted enforcement.

And we know that each year we are going to focus on low-wage industries. We know that each year we are going to focus on agriculture, child labor and several other areas that traditionally don't necessarily lead to high volumes of complaints for a variety of reasons. We know we need to be active in those areas or else the rights will go unprotected.

And so we try, on an annual basis, to fine-tune those enforcement plans and figure out, you know, this year is re-forestation a problem, H2B workers in the Pacific Northwest or Gulf Coast work, in light of some of the federal government contracting issues, you know, in and around the Hurricane Katrina area? And we try to focus on what are the real compliance problems where expenditure of targeted, directed resources would be most beneficial.

Dr. BOUSTANY. Thank you.

Have you seen any trends with regard to workforce shortage in how this is playing out?

Mr. DECAMP. Well, certainly in the Gulf Coast. We have seen issues in Louisiana, Mississippi, Alabama of a large influx of inexperienced employers who are not used to the rules, who don't know the rules and don't necessarily care about the rules applicable to government contracting or the other federal wage and hour laws. Many of these folks may be trying to comply with the law, and many of them don't know the law.

And what we see is—and we see this across the board in industries—that compliance rates for newer businesses, smaller businesses, tend to be lower, in part because the wage and hour laws—not just the FLSA, but across the board—tend to be fairly voluminous, fairly complicated. And we are dealing with many employers who haven't yet invested in compliance with wage and hour laws, and so they make mistakes. And sometimes it is willful; sometimes it is accidental.

But what we have seen in the Gulf Coast especially is a lot of contractors who are less like traditional businesses and more like folks who aggregate teams of workers and bring them to a worksite to be integrated into an existing contracting regime.

And so, one thing that we have tried to do to address that issue is to be more aggressive in asserting joint employment so that these workers are employees, not just of the contractor who rounds them up, but of the higher-level contractors on the project who are actually directing the work.

Dr. BOUSTANY. And one final question. Year to year, have you seen variances in the results of your targeted enforcement program, or strategic targeting program, or is it fairly consistent?

Mr. DECAMP. Well, I think it is fairly consistent in terms of the violation rates that we see on targeted cases.

We are always looking to improve our targeting so that we have a higher likelihood that, when we are going to expend resources and send an investigator into a workplace, that it is actually a workplace where there is a problem, as opposed to a workplace

where everybody is in compliance. So we are always looking to improve that.

Dr. BOUSTANY. Thank you.

And, Mr. Chairman, I would submit maybe there is an education component here for new employers and small employers that might be of benefit.

So I yield back. Thank you.

Chairman ANDREWS. I thank the gentleman for his time.

And the chair recognizes the gentleman from Illinois, Mr. Hare, for 5 minutes.

Mr. HARE. Thank you, Mr. Chairman.

Mr. DeCamp, I just have three questions for you.

You stated that you have a record of aggressive enforcement in protecting the workforce. And of the more than 132,000 workers who were misclassified in the 2008 national U.I. tax audit, can you tell me in how many of those cases did the Department of Labor conduct a follow-up investigation to determine whether those workers were receiving adequate back pay?

Mr. DECAMP. I don't have that information.

Mr. HARE. Could you get that for us?

Mr. DECAMP. We can look and see whether we can provide that information.

Mr. HARE. I would appreciate that.

You also said in your testimony that a policy of automatic referrals would discourage employees from reporting violations of wage and hour laws and to provide other information. Can you explain this to me? Because I am a little bit perplexed by that.

Mr. DECAMP. The main issue comes about when we are dealing with undocumented workers. If we take information that we receive involving undocumented workers and refer that information over to ICE or refer it over to IRS, for example, then those workers themselves may find themselves in jeopardy of being arrested and deported for their immigration violations.

The last thing that undocumented workers want to do, generally, is to be dealing with the federal government in any of its respects. But certainly they don't want to be dealing with enforcement agencies dealing with the immigration laws.

The same concern arises when a lot of undocumented workers use fraudulent Social Security numbers, for example. So if the IRS or other agencies start investigating employer records dealing with tax payments, and they start to notice that, you know, three workers for this employer have the same Social Security number, that may then lead to prosecution or at least further inquiry and scrutiny of those workers, which may make the workers very uncomfortable.

And if word gets out that Wage and Hour is providing information in significant quantities to other agencies, then workers may elect to forgo their wage and hour rights so as to avoid having to deal with enforcement of immigration laws.

Mr. HARE. You also said that employers would be less likely to produce copies of written documents or the records if they believe the documents are going to other law enforcement authorities. Well, what if they were required to do so?

Mr. DECAMP. What if who were required to do so?

Mr. HARE. If the employers——

Mr. DECAMP. If they were required to give us the documents?

Mr. HARE. Yes.

Mr. DECAMP. Well, right now, when we get the documents, it is generally a very cooperative process. We don't have to use subpoenas. We don't have to use formal legal process to get that information. We can use those processes if we need to, if an employer refuses to give us information. But we generally don't have to go the formal route to get documents.

I think that if we were to more aggressively use employer documents to refer them to other agencies, employers would be more likely to require a formal process, which would then present a severe resource drain in terms of the number of investigations that we can conduct.

Mr. HARE. And then just one final question before I run out of time.

You said that, you know, you need some additional personnel or the resources. Can you tell us how many additional investigators would you need, in your professional opinion, to adequately do what it is you want to do? I mean, how short are you?

Mr. DECAMP. It is hard to know what the right number is. I know that the right number is north of where we are now. And I think that the request that we have now seeks about 40 additional investigators. But I think that we need to go well beyond that at some point.

There is also an issue of if we get too many investigators at once, that actually has negative effects for the agency, because training resources are very intensive, for example.

Chairman ANDREWS. Will the gentleman yield?

Mr. HARE. I certainly would.

Chairman ANDREWS. If I could just take some of his time.

You made the statement earlier about needing more. These data are for overall inspectors, not just this target, but I want you to explain this to us.

In fiscal 2001, there were 4,334 positions requested for inspectors. For fiscal 2006, the request was 4,282, from the administration. For fiscal 2007, the request was 3,889. Now, it is back up to 4,082 for fiscal 2008.

So the number of people the administration asked for went down from 2006 to 2007, and in 2006 was considerably less than what you inherited when you took over in fiscal 2001.

You have been asking for fewer people, haven't you?

Mr. DECAMP. With all due respect, those are not the Wage and Hour numbers. Those are not the numbers of investigators that have been requested for Wage and Hour. That might include personnel for ESA.

Chairman ANDREWS. They are.

Mr. DECAMP. But that is not reflective of the number of investigators that we have been requesting. We actually did request——

Chairman ANDREWS. But the numbers of personnel that you have been asking is going down generally, right?

Mr. DECAMP. But we have also asked for increases in the Wage and Hour investigators.

Chairman ANDREWS. That is how your presentation was made to the Appropriations Committee?

Mr. DECAMP. I don't know how the presentations were made in previous years, but I can say that, in terms of the 2008 request, the 2007 request, we have specifically asked for increased—

Chairman ANDREWS. Okay.

Mr. DECAMP. We asked for specific amounts for increased numbers of investigators for Wage and Hour.

Chairman ANDREWS. But not in the overall.

I thank the gentleman for his time.

Mr. HARE. I yield back, Mr. Chairman.

Chairman ANDREWS. I would recognize the gentleman from Michigan, Mr. Walberg, for 5 minutes.

Mr. WALBERG. Thank you, Mr. Chair. I have no questions at this time.

Chairman ANDREWS. The chair would recognize the gentleman from New York, Mr. Bishop, for 5 minutes.

Mr. BISHOP. Thank you.

I just want to quickly follow up. When you are saying "the request that we made" with respect to inspectors, is the "we" here the Wage and Hour Division making a request to OMB, or is the "we" here the administration making a request to Congress?

Mr. DECAMP. The latter.

Mr. BISHOP. Thank you.

I want to pursue this issue of automatic referral. And I want to use a specific case. And it is the case that is raised by a witness on the second panel. I don't know whether you have had access to the testimony, but Mr. Williams outlined the case in which I think, to any reasonable person, he was an employee.

The relationship that he had with his employer was a traditional employer-employee relationship. And, as I say, I think that would be the case to a layman. I think it would be the case by looking at the ABC test, by looking at the IRS 20-point test.

Let us assume that his testimony were submitted to the Wage and Hour Division. And let us assume that you had sufficient staffing to pursue an investigation.

Your investigation, if I understand the constraints under which you feel you are working, would limit your findings, so to speak, to whether or not he was being paid minimum wage, whether or not he was being paid overtime, and so on. Is that correct?

Mr. DECAMP. I think that is largely correct. We wouldn't require a finding of independent contractor versus employee.

Mr. BISHOP. Let us assume that you look at this. And he is being paid overtime, and minimum wage is not a problem. But clearly he is an employee. Therefore, his employer is not paying in to the Social Security Trust Fund, not paying into the Medicare Trust Fund.

What does Wage and Hour Division do with that finding? Do they refer?

Mr. DECAMP. We might. We might refer it to IRS.

Mr. BISHOP. Stay on that for a second. Why would there be hesitation? Why is your answer you "might"? Why isn't it "absolutely"?

Mr. DECAMP. I think what we would need to do in a case like that is to balance whether referring would do more harm than good, in particular, with the workers.

Mr. BISHOP. Okay. I understand the testimony you just gave about exposing illegal immigrants to retaliation and so on. But, again, this is a national reputable company. And this is clearly a U.S. national that we are dealing with here who is being treated as an independent contractor.

So I guess my frustration is—and this goes to the question Ms. Woolsey asked—if it isn't the Department of Labor that is going to act on what is clearly, at least to this person, clearly an egregious violation, what agency within the federal government can either employees turn to or can the Congress turn to?

Mr. DECAMP. Well, again, first of all, there is a significant chance that in a case like that, we would refer the matter to IRS, given the facts that you have described. In addition, the IRS and the state agencies dealing with unemployment insurance certainly have jurisdiction to enforce their laws. And they can do that, as well.

Mr. BISHOP. Okay.

The commissioner of labor for New Jersey, Mr. Socolow, in his testimony, he recommends that the federal government take action in five areas. One of them is that we establish a strong universal federal definition of an employee.

What is your response to that?

Mr. DECAMP. Not knowing enough about the tax laws or the other laws to understand whether there are differences in the policies that would dictate a different outcome, I think it would certainly make things easier for everybody if there were one definition.

Mr. BISHOP. And would that enhance your—by “your,” the Wage and Hour Division—would that enable or enhance your enforcement capabilities?

Mr. DECAMP. I don't think it would enhance our enforcement capabilities. But it would make it clearer when we ought to be considering referring information over to other agencies.

One issue is that, because the tests are different, we don't know, for example, in every case—now, maybe in a clear case, that is a different matter—but in one of these gray areas, we have a broader definition of “employee” under the FLSA than exists under most other laws.

We don't want to be referring information over to other agencies that might not even be a violation of their laws. And we don't train our investigators in the tests used by the other laws.

Mr. BISHOP. I am about to run out of time, but I want to ask you one more quick question.

On the issue of resources, we just had a hearing in the Budget Committee in which the people from CMS estimated that for every dollar of enforcement they receive, they will get back somewhere between \$4 and \$13 of savings.

Has your division conducted any form of assessment of that kind of ratio?

Mr. DECAMP. Not that I am aware of. We just know that we want to be able to do more investigations.

Mr. BISHOP. Okay. Thank you.

I am out of time. Thank you, Mr. Chairman.

Chairman ANDREWS. Thank you very much.

Next on our list is the gentleman from Iowa, Mr. Loeb sack, for 5 minutes.

Mr. LOEB SACK. Thank you, Mr. Chair. I have no questions.

Chairman ANDREWS. Next on our list is the gentle lady from New Hampshire, Ms. Shea-Porter, for 5 minutes.

Ms. SHEA-PORTER. Thank you.

You know, without trying to sound facetious, I have to wonder if you are working for the same government that we are working for. And I will tell you some of my concerns here, and ask you to please address them.

For example, we know that we have the largest deficit in history. And the IRS reports that they are losing an estimated \$2.72 billion in 2006 alone. And yet I heard you say that you might report it to the IRS and, then again, you might not. And you also do not train your workers about these violations and where to take them.

Are we all on the same page, working for the same government, with the same goals?

Mr. DECAMP. Right. I appreciate the question.

There is certainly a tension there. We certainly appreciate the importance of all of the federal laws, including the immigration laws, the revenue laws and the other laws. And I don't want my testimony to be misunderstood as suggesting that we somehow don't value those laws.

Our approach to not referring every case is more a focus of the pragmatic consequences of referring matters and thereby deterring workers from reporting violations. That is the concern.

Ms. SHEA-PORTER. Well, I have trouble with that answer, also. Because earlier, you said your mission of protecting the workers—and I need to ask you how. If we don't protect them about accidents and Medicare and Social Security and unemployment compensation and retirement and benefits, exactly how are you protecting them?

Mr. DECAMP. Well, the concern is that if we are deterring workers from coming forward to us—because, frankly, we know that the workers would much rather not come to us at all than risk being deported or having other adverse consequences like that—if we deter workers from coming to us, then we are going to be getting less good information about violations in the workplace.

And if the labor standards for the undocumented workers and other low-wage workers are not protected, that undermines the labor standards for all the workers. And that is the concern.

We are not just concerned about the one worker who may have the issue. We are concerned about the integrity of the labor standards for all the workers in the workplace. And to protect those standards, we need to protect the undocumented worker and every other worker.

Ms. SHEA-PORTER. Well, I will tell you that it smacks of protecting the people who are breaking these rules.

And also, as somebody who did a lot of social work, there are ways to protect identities without, you know, having them lose their jobs. What have you pursued? Have you looked at ways to be able to allow employees to announce these violations without having them prosecuted or lose their status?

What exactly are you doing to take steps? Because to do nothing is not acceptable.

Mr. DECAMP. Well, we certainly conduct investigations, and we enforce our laws vigorously.

We don't require necessarily employees to submit a complaint with their name on it. We will take information sometimes from media sources, sometimes from workers reporting things anonymously. We get out there and we investigate and we protect those rights.

The concern comes into play if we refer a matter over to another enforcement agency that then comes in and starts scrutinizing the employer's records and sees that, you know, there are problems with the Social Security numbers or problems with I-9s or problems with other issues.

Then, even if we haven't, you know, announced the identity of any particular worker who is complaining, the fact that the worker is part of a workplace that is now being investigated by another enforcement agency may put that worker in jeopardy for having tax problems or immigration problems. And that would have a very chilling effect on workers.

Ms. SHEA-PORTER. Have you worked with communities that work with, say, illegal immigrants or people who have green cards? Is there anything specific that you are doing with these organizations so that they could protect them?

Mr. DECAMP. Well, absolutely. We do a lot of outreach to exactly that kind of group: to religious groups, to groups that advocate on behalf of immigrants, in particular, undocumented workers. We do a lot of outreach to educate those individuals and those groups about the protections that apply for those workers under our laws.

Ms. SHEA-PORTER. Well, I will tell you, I am sure you could accomplish that and still do what your mission is. And I am disturbed that you haven't done that.

Earlier, you were talking about not wanting to bring in more people because—and let me see if I had this right—that it is intensive training. When you are talking about how many people do you really need, and you said something along the lines of: Well, it is intensive training. So we wouldn't really want to bring in too many because it is a rigorous process.

Do you recall saying that? Am I quoting you right?

Mr. DECAMP. Well, what I said was that if we add staff too quickly, if we add investigators too quickly, it overwhelms the agency. Because in talking about how it is resource-intensive, we want to grow. But if we grow too quickly, it overwhelms the capacity of the agency to absorb these investigators.

Ms. SHEA-PORTER. Well, I have to say that you can look at all kinds of work like that—say, air traffic controllers. Remember when they all were let go for a while, and they managed to bring a lot in because they knew they needed them? It was essential.

And I would suggest that it is essential. And it almost sounds like stonewalling, whether it is the intention of the agency or not. By saying that we can't have these people come help us because they would be a burden on us sounds, at best, weak.

Thank you. My time has ended. Thank you.

Mr. DECAMP. Can I respond to that briefly?

Chairman ANDREWS. Of course.

Mr. DECAMP. The training process is very intensive. As I noted, it takes about 3 years, because of so many laws that we enforce, to get investigators fully trained.

In addition, during their training, before they are really fully ready to go out and conduct investigations on their own, they are often accompanied by senior investigators, who then have to mentor them and teach them how to conduct investigations properly. That is part of why it is a drain.

We want to grow our staff, certainly. We want to have more investigators. But we have to do it in a way that is not overwhelming the agency by bringing in so many inexperienced investigators that they can't really do their job and, at the same time, they drag down the productivity of our senior investigators.

Ms. SHEA-PORTER. Well, one last comment. When you talk about productivity, the Department of Labor found a 50 percent increase in the number of misclassified workers in the past 6 years—a 50 percent increase. I would say that, whether it drags down your supervisors' productivity or not, it is probably a good time to start.

Thank you.

Chairman ANDREWS. I thank the gentlelady.

The gentleman from Massachusetts has no questions, is that correct?

Mr. TIERNEY. Yes.

Chairman ANDREWS. The gentleman, my friend from New Jersey, Mr. Payne, is recognized for 5 minutes.

Mr. PAYNE. Thank you very much, Mr. Chairman.

And sorry that I missed your testimony.

However, just generally speaking, we have seen in a number of areas of employment the question of the workers being considered in a different category, as independent contractors.

When I was elected to Congress, in my federal building, the Peter Rodino Building—that was my predecessor and a good friend of mine, and every day I went into the building, I certainly remembered him because the building had his name.

But the terrible thing that occurred was that when I began, the federal government decided to privatize the custodial workforce. People had worked there for many, many years, had benefits. And it was really a very disturbing thing because then they turned to contractors.

And it took about 6 months before they put out bids, or a year or so. But the same people—the same work that was done, people had reduced salaries, had no benefits.

It might have been a great day for the GAO or the Office of Budget, but it was a terrible day for those hardworking people who had worked, had stayed on the job, took pride in their work, worked to send their children to school, where, in the flip of a pen, they lost health benefits, they lost pensions. They had to do more than the previous—the workload, at less money.

Now, I just wonder, just quickly, I understand you did outreach and you sort of did some surveys. So, let me just ask you this. Can you quantify what effect your outreach efforts have had on misclassification of workers?

I mean, mine, it was less misclassification, but it is all in the same general trend. We are pushing down wages.

You know, this country was great because people tended to be able to do better as time went on. Now, there are people who are doing better, believe me. I mean, these funds on Wall Street are going through the roof.

However, the typical, average, hardworking person that lives in my city of Newark, New Jersey, is doing worse every year. The cost of fuel goes up. Cost of housing goes through the roof. And they are taken out of jobs that is reducing their benefit.

How in the world can we continue to do this?

We have got some serious external problems with terrorism and people hating us around the world and all that. Internally, we are turning our backs on our own people right here, which just complicates the situation.

So let me just ask you, since my time is probably expiring, what has been the effect of your outreach efforts? What effect have they had on misclassification of workers? Because it appears that the number of misclassified workers have increased pretty steadily since 2000, so what is going on?

Mr. DECAMP. Well, I don't think that we have data that would quantify the effects of outreach. But it is important to keep in mind that outreach is not all that we do in this area. We also devote about 60 percent of our enforcement resources to low-wage industries, including the custodial industry that you mentioned, and construction and landscaping and many of the other industries where this misdesignation issue is a concern.

Mr. PAYNE. Just concluding, you know, on Wall Street, where a union, SEIU 32BJ, was attempting to organize the custodians and the doormen at these condos in the area. You know, the owners fought them tooth and nail to prevent the custodians from being organized because maybe they will take away from their profits.

I mean, it is a sad day in this country when we continually see hardworking people being beaten down daily.

Thank you, Mr. Chairman.

Chairman ANDREWS. Thank you, Mr. Payne.

The chair recognizes the gentleman from Oregon, Mr. Wu, for 5 minutes.

Mr. WU. Thank you, Mr. Chairman.

I would like to ask the witness from the Department of Labor about the factors that are considered by the federal government in a determination of whether someone is an independent contractor.

When I was practicing law in Oregon, I believe Oregon has roughly half the number of factors to be considered about whether someone is an independent contractor than the IRS.

What factors does DOL look to to make the determination of whether someone is an independent contractor or not? And how much weight is given to each factor?

Mr. DECAMP. Well, actually, this is set forth on page two of the written testimony, but I will be happy to address that.

Mr. WU. So I understand.

Mr. DECAMP. I will just read through them. One is the extent to—

Mr. WU. Why don't you just tell me?

Mr. DECAMP. All right. Well, I mean, the main concern is the extent to which the business is operating as a business versus operating as an employee would be.

So we are looking at ability to gain profit and control the revenue stream. We are looking at the ability to assign one's own work versus being directed as to what to do. We are looking at the permanency of the relationship.

We are looking at the extent of investment by the individual in the supplies and tools and other costs of doing business, other materials for doing business, versus, you know, is another entity providing that kind of material.

Those are really the main factors.

Mr. WU. In terms of immediate factors that one might look to, for example, if someone is holding out their business to others, they would have business cards. Are those things that you look at?

Mr. DECAMP. That would be part of the mix, yes, sir.

Mr. WU. Okay. And if someone were to mischaracterize someone as an independent contractor as opposed to an employee, how large is the discrepancy in costs to the employer and the costs to the employee?

Mr. DECAMP. I don't think that is an issue that the department has described. I know that some other witnesses, in the previous hearing, have weighed in on that issue.

Mr. WU. Do you have any knowledge of this?

Mr. DECAMP. Not in my capacity, no.

Mr. WU. So you have no idea how much tax savings or tax costs is incurred by an employer or incurred by the independent contractor/employee.

Mr. DECAMP. All I know is what was attested to at the previous hearing, sir.

Mr. WU. Which is what?

Mr. DECAMP. I think they were saying on the order of 15 to 20 percent.

Mr. WU. That seems a little low.

Mr. DECAMP. I think that is what was said. I am not disputing the numbers or vouching for the numbers. I am just saying that is my understanding of what was said.

Mr. WU. When the marginal tax rate is in the what, mid-to low-30s, and then there are taxes for FICA and FUTA and all the other things that come off the paycheck?

Mr. DECAMP. Sir, I am agreeing with your premise that there are economic incentives to—

Mr. WU. I am just trying to get my arms around it. And you are from the Department of Labor, so I sort of thought you might know.

Mr. DECAMP. It is not an issue that the Wage and Hour Division studies. It is not relevant to our enforcement mission.

Mr. WU. The gross savings isn't relevant to your enforcement mission?

Mr. DECAMP. In other words, we are looking at: Is this a worker who is an employee under the statute? And, if so, were the worker's rights under the statute protected?

That is our concern, not why did the employer do it, necessarily, unless it was willful. And then there are added penalties that would come into play, if we are talking about a willful violation.

Mr. WU. So you don't care about the size of the motivation, if you will?

Mr. DECAMP. That would bear on whether the violation was willful. In which case, for example, a longer statute of limitations could apply.

Mr. WU. Well, it would also bear on the size of the problem that you have. Don't you think?

Mr. DECAMP. When we are looking at remedies for the worker, we are looking at whatever minimum wage or overtime the worker was denied. In terms of the employer's motivation for doing so, if we conclude that the violation was willful, we could pursue back wages for 3 years instead of 2. We would be more likely to pursue liquidated damages in a case like that—

Mr. WU. I am just trying to understand the scope of the problem. And if an employer saves 10 percent, that doesn't seem like that is much motivation, but if an employer saves 50 percent or 100 percent, you know, that is a different scale of problem.

I am just trying to get my arms around this. And I thought you would have those kind of numbers right off the top of your head.

Mr. DECAMP. Again, that doesn't affect how we would carry out our enforcement mission. We are looking to protect the workers under the statutes and—

Mr. WU. How long have you been working in this arena?

Mr. DECAMP. I have been involved in labor and employment law since about 1995.

Mr. WU. Okay. So in 12 years, you have never had reason to inquire as to the scope of potential savings that employers or contractors would experience as a result of characterizing or mischaracterizing the relationship?

Mr. DECAMP. That is correct, sir.

Mr. WU. Thank you.

Chairman ANDREWS. The gentleman's time has expired.

Thank you, Mr. DeCamp, for your testimony here this morning. I know the committee will be interacting with you as we go down the line on this issue. And I thank you very much for your attendance this morning.

Mr. DECAMP. Thank you.

Chairman ANDREWS. Thank you.

I am going to ask if the witnesses from the second panel would approach the table and wait for their name tags to be set up.

I am going to turn over the prerogative of the chair to my friend from California, Ms. Woolsey, and she will conduct the balance of the hearing.

Ms. WOOLSEY [presiding]. As Chairman Andrews said, if you have not testified here before, you may note that we have a lighting system, 5-minute rule. And everyone, including members, is limited to 5 minutes of presentation and questioning.

The green light is illuminated when you begin to speak. When you see the yellow light, it means you have 1 minute remaining. When you see the red light, it means your time is expired and you

need to conclude your testimony. You don't have to stop mid-sentence, believe me.

Be certain, as you testify, to turn on your microphone. Otherwise, we will all be yapping after you from up here, and you will wonder what we are trying to tell you. So just turn it on, and then we can hear you.

And now we would like to introduce our witnesses. And Chairman Andrews will introduce David Socolow.

Chairman ANDREWS. I appreciate that privilege.

David Socolow is the commissioner of labor for the state of New Jersey. He is a graduate of Harvard University. Again, someone else has overcome that liability to be with us today. [Laughter.]

I am especially proud of David for several reasons. He and I had the privilege of working together here in Washington when he served first as my legislative director, then my chief of staff.

He then went to work for Secretary of Labor-elect Herman. He worked for the state of New Jersey's Unemployment Division and was the director of that division for a number of years, and became our commissioner of labor last summer.

He is an outstanding public servant. He is an authority in this field. He has done a great job on this issue in the state of New Jersey.

And I must confess some personal affection. He is fortunate enough to be married to my sister-in-law, Erin. [Laughter.]

And they have two spectacular children, one of whom is my goddaughter. And we are just very proud of the work that he has done. I am delighted he is here with us today.

David, welcome. Great to have you with us.

Ms. WOOLSEY. We welcome you, too, David.

Robert Williams is currently a transportation recruiting and operations consultant to numerous transport companies in New England. Between the year 2000 and the year 2005, he worked first as a temporary driver and then as a contracted driver for FedEx Home Delivery in Northborough, Massachusetts. Prior to that position, he worked for over 30 years in a number of senior management positions at UPS, Federal Express, Airborne Express, and United States Line. Mr. Williams served for 28 years in the U.S. Reserve and retired as a sergeant major in 1996.

Sara Stafford is president of Stafford Construction located in Saugus, Massachusetts. In 1993, after working as manager for a supply company for 13 years, Ms. Stafford opened her own union drywall and plastering contracting firm. Her company's portfolio involves about 50 percent public and 50 percent private work. Sara Stafford has been a resident of Raleigh, Massachusetts, for 15 years.

Christine Walters is an independent consultant in human resources and employment law at the FiveL Company in Glyndon, Maryland, and is testifying on behalf of the Society of Human Resources Management. Ms. Walters has over 20 years of combined experience in H.R. administration, management law and teaching. She has been gauged as an expert witness regularly, presenting at conferences across the country. And she is a columnist for national publications. Walters serves in a variety of volunteer leadership

roles at the national, state and local levels for the society and is currently on its employee relations panel.

Thank you all for being here.

We will begin with you, Mr. Williams.

STATEMENT OF ROBERT WILLIAMS, TRANSPORTATION RECRUITING AND OPERATIONS CONSULTANT, FORMER FEDEX EMPLOYEE

Mr. WILLIAMS. Thank you, Chairman Andrews and Chairwoman Woolsey, for inviting me to testify today. Thanks also to the members of the subcommittees who are interested in the misclassification issue that is hurting so many FedEx Ground and Home Delivery drivers today.

After retiring, I read an advertisement in the Worcester Telegram and Gazette in April of 2001 for independent contractors at the FedEx Home Delivery in Northborough, Mass. The ad basically stated, "Run your own business. Become a business owner with a national leader. Be your own boss."

When I applied for the position as an independent contractor, I was told there were none available at present. The manager offered to train me as a temporary driver before I could become a contractor and do any work at all at FedEx Home Delivery. I completed the mandatory training course and went to work as a temporary driver.

I was paid by the hour as a temp for a firm called Adecco and eligible for overtime. I was furnished a uniform and rental van supplied by FedEx, but I was not a FedEx employee. I did not pay any expenses while a temp. State and federal withholding were taken out of my weekly check by Adecco.

I continued working as a temporary driver until June 2002, when a route position became available. At that time, I signed a FedEx Home Delivery standard contractor operating agreement. I purchased a small commercial van that had to be white and inspected by FedEx for approval.

After utilizing this van for a period of time, I was told it would no longer accommodate the number of packages for my area. I was told I would have to have a larger vehicle.

So, through FedEx, I leased a larger vehicle called a P400. This vehicle was painted white and had all of the FedEx logos on permanent decals. This vehicle was also arranged for by FedEx, who took care of all of the paperwork.

I worked with this new van until October 15, 2002, when I was involved in a serious accident and hospitalized. I did not return to work for 13 months. I did not pursue worker's compensation. I was not able to work until early November 2003, and returned as a temporary driver.

I worked on and off as a temporary driver, driving a rental van supplied by FedEx and being paid by the temp agency Adecco. I was offered a different route and soon became a so-called contractor again in June 2004.

I was told I had to lease or buy a much larger truck than I had before. This new truck was called a P500 and was obtainable only through FedEx. It was white and colored with logos, numbered in a FedEx series, and showed USDOT markings on it.

FedEx had a supply of these vehicles in their Manchester, New Hampshire, terminal. And FedEx arranged the financing through one of the leasing companies they offered. The whole transaction, leasing arrangements, and credit information, et cetera, all flowed through FedEx.

This was the only type of vehicle that FedEx approved. There were no exceptions.

As a contractor, I was responsible for the cost of the vehicle, for the fuel, for the tires, for the maintenance, and all of the operating costs, including breakdown and emergency expenditures. I paid a worker's accident policy in lieu of workman's comp weekly deductions. I also paid weekly for liability insurance for protective insurance.

These expenses were taken out of my settlement by FedEx. There were no other insurance services or policies that were made available to us. We were told we could get our own insurance. But having personally checked with a number of insurers, I found the cost prohibitive.

Additional expenses that were taken out from time to time were for uniforms, scanners, claims against me, mapping software, random drug-testing, annual DOT inspection, and truck-washing.

No taxes or Social Security were ever deducted from my settlements. We were issued a 1099 form annually. I was responsible for reporting my federal and state tax to the federal and state tax authorities.

In the holiday period of 2004, things began to change drastically. We were being monitored more and more by the use of the scanner. The scanner was a tracking device used to monitor our daily delivery areas.

We are required each morning to report early to load our trucks. The number of packages and stops were the means by which we were compensated. We were paid by the package, and not an hourly wage.

FedEx Home Delivery controls the number of packages tended to the drivers and controls the amount a driver can make through their computer systems. This means of controlling a driver is ongoing today.

There were many times when FedEx managers would not allow us to leave the building and go out on our routes until all the packages were accounted for. This could severely impact our earnings by reducing the time we would have to make deliveries. Packages were added or subtracted to our routes, affecting our earnings on a daily basis.

I remain in contact with numerous drivers who are still with FedEx Home Delivery throughout the country. I contact many drivers in the New England area on a regular basis, especially Northborough, Mass. The same issues, treatment and procedures I experienced still go on today.

Due to my many years of working in the transportation industry, I understand clearly the differences between an employee and an independent contractor. The control that FedEx Home Delivery had over me and over the drivers it has today shows these drivers are controlled like employees but called contractors.

FedEx Home Delivery drivers must pay for uniforms worn to FedEx standards with a black belt, proper shoes, no sneakers.

They must purchase or lease a FedEx truck, purchased by FedEx, prescribed by FedEx for size, color and logos, numbering, et cetera.

To purchase or lease a FedEx scanner—this is a mandatory item. The daily package deliveries cannot be performed without it. It is monitored by FedEx.

Drivers must pay for all maintenance prescribed by FedEx and USDOT. Drivers must furnish all fuel, tires and other costs related to the operation of their vehicle.

Drivers must pay for a weekly worker's accident policy and liability policy deducted by FedEx to protective insurance.

Drivers who cannot work on a given day and cannot find a FedEx-approved temp driver are regularly threatened with contract terminations.

To me, the biggest personal issue I had was the time-off program. Drivers—can I continue?

Ms. WOOLSEY. You need to sum up now, Mr. Williams. And then you will bring some of that into your questions and answers.

Mr. WILLIAMS. All right.

I could now just finish up and say I was terminated by FedEx in December 2005. The National Labor Relations had ordered an election before the company fired me and a number of other people who were attempting to support the union. The board filed a complaint against FedEx for illegally terminating me for protected union activities.

There are more charges pending against the company for unfair labor practices in the Northborough location. A hearing is set for August.

After I was terminated, I filed for unemployment benefits in Massachusetts, and I did receive those benefits. I was the first one to do so under the FedEx Ground or Home Delivery.

Many present FedEx Ground or Home Delivery drivers would be too scared of the company's reaction if they testified. I am here to state my professional opinion with over 45 years of experience in the industry. The FedEx Ground model rests clearly on the misclassification of its drivers as so-called contractors.

Thank you.

[The statement of Mr. Williams follows:]

Prepared Statement of Robert V. Williams, Transportation Recruiting and Operations Consultant, Former FedEx Employee

Thank you Chairman Andrews and Chairwoman Woolsey for inviting me to testify today. Thanks also to the members of the Subcommittees who are interested in the misclassification issue that is hurting so many FedEx Ground and Home Delivery drivers today.

After retiring, I read an advertisement in the Worcester Telegram and Gazette in April 2001 for Independent Contractors at FedEx Home Delivery in Northboro, MA. The ad basically stated: "Run your own business, Become a business owner with a national leader, Be your own boss". When I applied for a position as an "Independent Contractor" I was told that there were none available at present. The manager offered to train me as a temporary driver before I could become a "contractor" and do any driving work at FedEx Home Delivery.

I completed the mandatory training course and went to work as a temporary driver. I was paid by the hour by a temp firm named ADECCO and eligible for overtime. I was furnished a uniform and rental van supplied by FedEx but was not a FedEx

employee. I did not pay for any expenses while a temp. State and federal withholding were taken out of my weekly check by ADECCO.

I continued working as a temporary driver until June of 2002, when a route position became available. At that time, I signed a FedEx Home Delivery standard contractor operating agreement. I purchased a small commercial van that had to be white and inspected by FedEx for approval.

After utilizing this van for a period of time, I was told it no longer could accommodate the number of packages for my area. I was told I had to have a larger vehicle, so through FedEx I leased a larger vehicle called a P400. This vehicle was painted white and had all of the FedEx logos on permanent decals. This vehicle was also arranged for by FedEx who took care of all the paperwork. I worked with this new van until October 15, 2002, when I was involved in a serious accident, and hospitalized.

I did not return to work for 13 months. I did not pursue workers compensation. I was not able to work until early November of 2003, and returned as a temporary driver. I worked on and off as a temporary driver, driving a rental van supplied by FedEx and being paid by the temp agency ADECCO.

I was offered a different route and became a so-called "contractor" again in June 2004. I was told I had to lease or buy a much larger truck called a P500. This vehicle, only attainable through FedEx, was white in color with logos, numbered in a FedEx series and showed USDOT markings on it. FedEx had a supply of vehicles at their Manchester, NH terminal, and FedEx arranged financing with one of the leasing companies it offered. The whole transaction, leasing arrangements, the credit information, etc., all flowed through FedEx. This was the only type of vehicle that FedEx approved. There were no exceptions.

As a "contractor" for FedEx, I was responsible for the cost of the vehicle, for the fuel, for the tires, for the maintenance, and all operating costs, including breakdown and emergency expenditures. I paid for a worker's accident policy, in lieu of Workmen's Comp weekly deductions and I also paid weekly for liability insurance from Protective Insurance. These expenses were taken out of my settlement by FedEx. There were no other insurance services or policies that were made available to us.

We were told we could get our own insurance, but having personally checked a number of insurers, I found it to be cost prohibitive. Additional expenses taken from my settlement were for uniforms, scanners, claims against me, mapping software, random drug testing, annual DOT inspection and truck washing.

No taxes or Social Security were ever deducted from our settlements. We were issued a 1099 form annually. I was responsible for reporting my income to federal and state tax authorities.

In the Holiday period of 2004, things started to change drastically. We were being monitored more and more by the use of the scanner. The scanner was used as a tracking device to monitor our daily delivery areas. We were required each morning to report early to load our trucks. The number of packages and stops were the means by which we were compensated. We were paid by the package and not an hourly wage. FedEx Home Delivery controls the number of packages tendered to drivers and controls the amount a driver can make through their computer systems. This means of controlling drivers is on going today. There were many times when FedEx managers would not allow us to leave and go out on our routes until all packages were accounted for. This could severely impact our earnings by reducing the time we would be able to make deliveries. Packages were added or subtracted to our routes, affecting our earnings on a daily basis.

I remain in contact with numerous drivers who are still with FedEx Home Delivery throughout the country. I contact many drivers in the New England area on a regular basis especially Northboro, MA. The same issues, treatment and procedures I experienced still go on today.

Due to my many years of working in the transportation industry, I understand clearly the differences between an employee and independent contractor. The control that FedEx Home Delivery had over me and has over the drivers today shows that the drivers are controlled like employees but called "contractors."

- FedEx Home delivery drivers must pay for uniforms worn to FedEx standard, with a black belt, proper shoes, no sneakers.
- Purchase or lease a FedEx truck; prescribed by FedEx for size, color, logos, numbering, etc.
- Purchase or lease a FedEx scanner; this is a mandatory item. The daily package delivery duties cannot be performed without it and it is monitored by FedEx.
- Drivers must pay for all maintenance prescribed by FedEx and USDOT. Drivers must furnish all fuel, tires, and any other costs related to the operation of the vehicle.

- Drivers must pay for a workers accident policy, and liability policies, deducted by FedEx to Protective Insurance Company.
- Drivers who cannot work on any given day and cannot find a FedEx approved temp driver are regularly threatened with contract termination.

To me the biggest personal issue I had was the Time Off program. Drivers participate at the rate of \$17.50 per week to join into the "Drivers Time off" program. Time off requests are made in May of each year according to "contractor" seniority. Any holiday falling in the week off would be included as part of the week off with no compensation. A "contractor" who signs up for the time off program, must remain in the program for the entire year. All selected weeks must be honored by "contractors" and managers. So we were paying FedEx to book two weeks away from delivering with no return to us. No interest was paid on this account. We don't know where this money went. No one in management could explain how the program really worked.

In August 2005, FedEx terminated the Senior Manager who had been there approximately 3 years. He was replaced by a number of additional roving managers, until a new manager was appointed, in September. At this point, nearly all drivers signed authorization cards to join Teamster Local Union 170. From the time that FedEx was notified of these actions by the drivers there was a drastic change in management. This continued through November 2005 when a hearing was held by the NLRB. I testified at that hearing as I am testifying today. We were found to be employees.

I was terminated by FedEx in December 2005. The National Labor Relations Board ordered an election but after the company fired me and a number of other union supporters the election was postponed. The Board filed a complaint that charged FedEx for illegally terminating me for protected union activities. There are more charges pending against the company for unfair labor practices at the Northboro location. A hearing is set for August.

After I was terminated, I filed for unemployment benefits in Massachusetts. The state investigated my work conditions. The company argued that I was a so-called "contractor" and not eligible for benefits. The state concluded that FedEx controlled me as an employee and I was awarded unemployment. Since that ruling, other FedEx Ground and Home Delivery drivers have also been found eligible for Massachusetts unemployment coverage. With the Chairman's permission, I ask that the Massachusetts ruling in my unemployment case be submitted with my statement for the record.

Many present FedEx Ground or Home Delivery drivers would be too scared of the company's reaction if they testified. I am here to state my professional opinion. With over 45 years of experience in the industry, the FedEx Ground model rests clearly on the misclassification of its drivers as so-called "contractors." Thank you.

Ms. WOOLSEY. Thank you, Mr. Williams.
Ms. Stafford? Turn on your microphone.

**STATEMENT OF SARA STAFFORD, PRESIDENT, STAFFORD
CONSTRUCTION SERVICES, INC.**

Ms. STAFFORD. Thank you, Chairwoman Woolsey and Chairman Andrews and the members of the subcommittees. It is a pleasure to address you here today on this important issue.

I have been in the construction industry for about 30 years. I am the president and sole owner of the Stafford Construction Services Incorporated. Primarily, we are a subcontractor working in the union arena. And we do drywall plastering, metal framing, that type of thing, in the metropolitan Boston area. I do both public and private work.

I am a union company. I have been since the day I opened my business 14 years ago. And I have agreements with the New England Regional Council of Carpenters, as well as three other unions.

The construction industry is particularly prone to illegal practices. And the industry is very competitive, with jobs frequently being awarded to the lowest bidder. Under those circumstances, it

is difficult to compete against others that misclassify workers as independent contractors.

We at Stafford play by the rules. And for the 50 to 70 employees that work for me that means regular audits of my employment records are shown to the union. They are shown to my workers' compensation company. They are shown to my bank. My bonding company has access to them. It is an open book.

We have common interests in having a market of high standards and fair competition as a rule. The basic rule is abiding by the law. And my company's employees are all on the payroll.

They get overtime pay and workers' compensation. We pay federal and state unemployment taxes, Social Security, Medicare, and we withhold state and federal from every dollar that we pay out in employment. And many of these funds, of course, go to the support of the health benefits for these underinsured people.

That is okay because that is the law. But it becomes difficult when I have to compete against other companies that routinely misclassify their workforce and do none of those things. Automatically, they get at least a 30 percent advantage in labor costs and this all goes to profits.

The bill for this gap in taxes paid and employee benefits comes due to every employer, like myself, that follows the rules. It is an unequal taxation through misclassification of employees.

Another rule basic to many responsible companies, like mine, is to provide employees with good family medical and retirement plans, a foreign concept to most businesses that misclassify workers.

The result of that kind of conduct is not difficult to fathom.

More of the insurance and tax burden is put on responsible employers, such as myself, that play by the rules, because less people are paying into the system. Also, my company has lost work and my employees have lost income because the bids were won by employers that misclassify workers.

There are whole market segments, such as residential construction, that are almost impossible for legitimate companies to enter into, especially in the interior trades. That is not fair and more concern needs to be shown to law-abiding companies. Otherwise, they will either have to go out of business or become one of the cheaters.

And what about the workers? Misclassified workers don't have the benefits of union protection. They do not have a cop on the beat, so to speak, that will make sure that the employer is playing by the rules. If they want union representation, their irresponsible employer will make them jump through hoops to prove that they are employees.

That is the driving force behind the continuing misclassification problem in our industry.

As I said earlier, I have a common interest with the union to provide high standards and to make sure the competition in the construction industry is fair. When union representation is made more difficult by misclassification, then misclassification becomes an even bigger problem, threatening the existence of employers like me who are paying into the system and hoping that the system will recognize the need for a level playing field.

Thank you.
[The statement of Ms. Stafford follows:]

Prepared Statement of Sara Stafford, President and Sole Owner, Stafford Construction Services, Inc.

Chairwoman Woolsey, Chairman Andrews and members of the subcommittees it is a pleasure to address you today on an important subject adversely affecting the construction industry—the misclassification of workers as independent contractors.

I have been in the construction industry for many years. I am the President and sole owner of Stafford Construction Services, Inc. Primarily, we do interior framing, drywall and plastering in metropolitan Boston. I am a union company—I have collective-bargaining agreements with local unions of the New England Regional Council of Carpenters as well as three other unions.

The construction industry is particularly prone to illegal practices. The industry is very competitive, with jobs frequently awarded to the lowest bidder. Under those circumstances, it is difficult to compete against others that misclassify their workers' as independent contractors.

I play by the rules, and I work with a union that makes sure that is the case. Don't be mistaken, I'm not complaining. We have a common interest in having a market where high standards and fair competition are the rule. And a basic rule is abiding by the law. My company's employees are all on the payroll. They get overtime pay and workers' compensation coverage and we pay federal and state unemployment, Social Security and Medicare taxes and we withhold state and federal income taxes. That is okay, because that is the law. But it becomes difficult when I have to compete against other companies that routinely misclassify their workforce and do none of those things. Automatically, they get a least a 30 percent advantage on labor costs.

Another rule, basic to many responsible companies like mine, is to provide employees with a good family medical and retirement plans—a foreign concept to companies that misclassify workers.

The results of that kind of conduct are not difficult to fathom. More of the insurance and tax burden is put on responsible employers (union and non-union) that play by the rules because less people are paying into the system. Also, my company has lost work, and my employees have lost income because bids were won by employers that misclassify workers. There are whole market segments, like residential construction, that are almost impossible for legitimate interior companies like mine to work in. That is not fair, and more concern needs to be shown to law-abiding companies. Otherwise; they will either go out of business or join the cheaters.

And what about the workers? Misclassified workers don't have the benefits of union protection. They do not have a cop-on-the beat, so to speak, that will make sure their employer plays by the rules. If they want union representation their irresponsible employer will make them jump through hoops to prove that they are employees. That is a driving force behind the continuing misclassification problem harming our industry.

As I said earlier, I have a common interest with the union to promote high standards and to make sure competition in the construction industry is fair. When union representation is made more difficult by misclassification then misclassification becomes an ever bigger problem threatening the existence of employers like me who play by the rules.

Ms. WOOLSEY. Thank you, Ms. Stafford.
Ms. Walters?

STATEMENT OF CHRISTINE WALTERS, CONSULTANT, FiveL COMPANY

Ms. WALTERS. Thank you, Madam Chair, Chairman Andrews, Ranking Members Wilson and Kline, and distinguished members of the committee. Thank you for this opportunity to testify on the issue of misclassification of employees and independent contractors. And I do commend your two subcommittees for holding this joint hearing on this important issue.

My name is Christine Walters, and by way of introduction, I would share with you that I have over 20 years of experience in

human resources or H.R. administration, management law, and teaching.

Today, I work as an independent human resources and employment law consultant with FiveL Company. And I served as an adjunct faculty member of the Johns Hopkins University teaching graduate, undergraduate and certification level courses from 1999 through 2006.

Today, I appear before you on behalf of the Society for Human Resource Management, or SHRM.

Today, as organizations compete in an everchanging global marketplace, labor costs are never far from mind. In addition to managing these costs, many employers in a variety of industries are also facing a lack of talented, skilled people to compete in today's economy.

With this changing landscape come new challenges for human resource professionals and employers to reach out and find new employment relationships that may not mirror the traditional models, including part-time employment, flex-time, and telecommuting schedules. Employers may also use leased employees, direct hire temps, per diem workers, as well as independent contractors to meet a particular workforce need.

While these types of working relationships are of value to employers, they help meet the individual employees' and workers' needs, as well.

Sandwich-generation workers—those caring for their own children, as well as their parents—seek working hours that meet their demanding personal needs. Entrepreneurs seek a work situation that gives them mobility and an opportunity to engage in multiple working relationships. And some workers just like the flexibility that the independent contractor status provides.

With the increased interest in these various working relationships, more employers are faced with making the sometimes complicated classification analysis. In my experience, employers do, on occasion, unwittingly misclassify employees as independent contractors.

Much of the difficulty in making an accurate determination lies with the fact that there is not a single definition of an employee. Rather, there are numerous definitions and statutes which apply, depending upon the context in which you are asking the questions, including the IRS's 1099 rule, or 20-factor test, National Labor Relations Act, Americans with Disabilities Act, in addition to federal court interpretations under the Fair Labor Standards Act, Title VII of the Civil Rights Act of 1964, the Family Medical Leave Act, and the Age Discrimination in Employment Act.

The problem with much of the above, however, is that the tests applied come after the working relationship has been established. There is little guidance for employers to use, other than the IRS guidance, to apply when the working relationship is first formed. So the dilemma arises when an employer properly uses the IRS guidance, but is later challenged, and when a different test is used, is held to have misclassified a worker.

Finally, add to the above state definitions, such as in each state's unemployment insurance code, where you will likely find yet another definition of employee.

The use of independent contractors is a common practice in some industries. Health care, particularly hospitals, often uses per diem or contract nurses to supplement emergent unforeseen staffing shortages, such as in the case of an external disaster.

Or consider a small business owner with 10 employees that provides audio-visual support services to clients. Of its 10 employees, the organization employs just one sound engineer, who is a highly skilled and valued employee.

One day, that employee tells the business owner that he wants to start his own business. The employee offers that, "In lieu of resigning, I will continue to work for you on an as-needed, part-time basis, as an independent contractor."

The parties agree, and both are delighted, until that business owner is advised by legal counsel of the possible pitfalls of proceeding with this type of relationship. And the relationship does not proceed.

While my experience demonstrates that the vast majority of employers are trying to comply with the law, I recognize that there may be some employers and perhaps some industries in which there are deliberate attempts to skirt the law. I do not think, however, that additional legislation attempting to clarify the law would provide the intended benefit.

Additional law in this area is likely to only add to the existing confusion. And I think we need to focus on clarification, education and enforcement.

Thank you.

[The statement of Ms. Walters follows:]

Prepared Statement of Christine V. Walters, MAS, JD, SPHR, Independent Consultant, FiveL Company, On Behalf of the Society for Human Resource Management

Introduction

Chairpersons Woolsey and Andrews, Ranking Members Wilson and Kline, distinguished members of the committee. Thank you for this opportunity to testify on the issue of misclassification of employees as independent contractors (IC). I commend your two subcommittees for holding this joint hearing on this important topic. My comments today will focus on my experience with employers who have faced challenges during or after this classification process.

My name is Christine Walters. By way of introduction, I have over 20 years combined experience in HR administration, management, law and teaching. Today I work as an independent human resources and employment law consultant with the FiveL Company and served as an adjunct faculty member of the Johns Hopkins University teaching a variety of courses in graduate, undergraduate and certification level programs from 1999 to 2006.

I appear today on behalf of the Society for Human Resource Management (SHRM). SHRM is the world's largest association devoted to human resource management. Representing more than 225,000 individual members, the Society's mission is to serve the needs of HR professionals by providing the most essential and comprehensive resources available. As an influential voice, the Society's mission is also to advance the human resource profession to ensure that HR is recognized as an essential partner in developing and executing organizational strategy. Founded in 1948, SHRM currently has more than 550 affiliated chapters within the United States and members in more than 100 countries.

SHRM is well positioned to provide insight on how employers classify individuals as employees or ICs. HR professionals are responsible for applying the law to the situation in their workplace and properly determining, through a mix of factors, whether a person should be classified as an employee or an IC.

The Workplace of the 21st Century

As organizations compete in today's ever changing global marketplace, labor costs are never far from mind. In addition to managing these costs, many employers in a variety of industries are also facing a lack of talented, skilled, people to compete in today's economy. With this changing landscape come new challenges for human resources professionals and employers to reach out and find new employment relationships that may not mirror the traditional models. Depending on the needs of employers and employees, these working arrangements may include part-time employment, or flex-time and telecommuting schedules. In some instances, employers may also use leased employees, direct-hire temps, agency temps, per diem workers, as well as IC's to meet a particular workforce need. Employers may hire contingent workers for a variety of reasons including filling temporary absences, dealing with workload fluctuations, meeting employee requests for part-time work, and continuing to utilize the skills of an employee who has left employment.

While these types of working relationships are of value to employers, they help to meet individual employees and workers needs as well. Sandwich generation workers, those caring for this own children as well as their parents, seek working hours that meet their demanding personal needs; entrepreneurs seek a work situation that gives them mobility and opportunity to engage in multiple working relationships; and some workers just like the flexibility that the IC status provides. Regardless of the motivations, however, every new working relationship brings with it the challenge of asking the right questions to ensure the working relationship is being properly classified as an employee or non-employee worker.

Classification Challenges

With the increased interest in these various working relationships, more employers are faced with making the sometimes complicated classification analysis. In my experience, employers do on occasion unwittingly, misclassify employees as independent contractors.

Much of the difficulty in making an accurate determination lies with the fact that there is not a single definition of an employee; rather, there are numerous definitions and statutes which apply depending on the context in which you are asking the question. Section 825.105 of the federal Family and Medical Leave Act (FMLA) regulations provide, "The courts have said that there is no definition that solves all problems as to the limitations of the employer-employee relationship under the Act; and that determination of the relation cannot be based on "isolated factors" or upon a single characteristic or "technical concepts", but depends "upon the circumstances of the whole activity" including the underlying "economic reality."

In 1992, the U.S. Supreme Court reiterated its position that, where a statute contains the term "employee" and does not "helpfully define it, this Court presumes that Congress means an agency law definition unless it clearly indicates otherwise." The Court then reiterated the following factors, "In determining whether a hired party is an employee under the general common law of agency * * *"

1. the hiring party's right to control the manner and means by which the product is accomplished. Among the other factors relevant to this inquiry are the;
 2. skill required;
 3. the source of the instrumentalities and tools;
 4. the location of the work;
 5. the duration of the relationship between the parties;
 6. whether the hiring party has the right to assign additional projects to the hired party;
 7. the extent of the hired party's discretion over when and how long to work;
 8. the method of payment;
 9. the hired party's role in hiring and paying assistants;
 10. whether the work is part of the regular business of the hiring party;
 11. whether the hiring party is in business;
 12. the provision of employee benefits; and
 13. the tax treatment of the hired party. *Nationwide Mutual Ins. Co. v. Darden*, 503 U.S. 318 (1992)

Then in 2003, the U.S. Supreme Court, in a separate decision, citing guidance from the U.S. Equal Employment Opportunity Commission, used a different test when trying to assess whether a managing partner of a firm (physician practice) should be counted as an employee for purposes of the Americans with Disabilities Act These factors include whether:

1. The organization can hire/fire the individual or set the rules and regulations of the individual's work
2. And, if so, to what extent organization supervises the individual's work;
3. The individual reports to someone higher in the organization;

4. And, if so, to what extent the individual is able to influence the organization;
 5. The parties intended that the individual be an employee, as expressed in written agreements or contracts;

6. The individual shares in the profits, losses, and liabilities of the organization (Clackamas Gastroenterology Associates, P.C. v. Wells (April 22, 2003).)

The Internal Revenue Service (IRS) historically has used another test, the s 1099-Rule or 20 factor test to ensure the working relationship is being properly classified as an employee or non-employee worker. Those 20 factors include:

1. Is the individual, who is providing services, required to comply with instructions concerning when, where and how the work is to be done?

2. Is the individual provided with training to enable him or her to perform a job in a particular manner?

3. Are the services that are performed by the individual integrated into your business' operations?

4. Must the services be rendered personally by the individual?

5. Does your business hire, supervise or pay assistants to help the individual performing the services under contract?

6. Is the relationship between the individual and the person for whom he or she performs services a continuing relationship?

7. Does the employer/company set the hours of work for the individual?

8. Is the individual required to devote full time to the person for whom he or she performs services?

9. Does the individual perform work on your business premises?

10. Does the employer/company direct the order or sequence in which the work must be done?

11. Are regular oral or written reports required?

12. Is the method of payment at set intervals of regular amounts?

13. Are business or traveling expenses of the individual reimbursed?

14. Does the employer/company furnish tools and materials necessary for the provision of services?

15. Does the individual performing services lack a significant investment in resources used to perform services?

16. Is the individual providing the services without realizing a profit or loss from his services?

17. Is the individual restricted from providing services for a number of firms at the same time?

18. Has the individual not made his/her services available to the general public?

19. Is the individual who is providing services, subject to dismissal for reasons other than non-performance of contract specifications?

20. Can the individual providing services terminate his or her relationship at any time without incurring a liability for failure to complete a job?

Still other situations may require review under the National Labor Relations Act.

Then you have the federal courts. When assessing a working relationship under the federal Fair Labor Standards Act the "Right to Control" or "Manner and Means" tests are usually applied. When assessing a working relationship under Title VII of the Civil Rights Act of 1964, the FMLA or the Age Discrimination in Employment Act, the "Economic Realities" test is usually applied. While slightly different, all three of the tests have four common factors:

- Who had power to hire and fire?
- Who supervised and controlled employees' work schedules and conditions of employment?

- Who determined rate and method of payment?

- Who maintained employee records?

The problem with much of the above, however, is that the tests applied come after the working relationship has been established. There is little guidance for employers to use, other than the IRS guidance to apply when the working relationship is first formed. So the dilemma arises when an employer properly uses the IRS guidance but is later challenged and, when a different test is used, is held to have misclassified a worker.

Finally, add to the above, state definitions such as in each state's unemployment insurance code. There you will likely find yet another definition of employee.

The use of independent contractors is a common practice in some industries. Health care, particularly hospitals often use per diem or contractors nurses to supplement emergent, unforeseen staffing shortages, such as in the case of an external disaster. These health care workers often work two, three or more different jobs, choosing their preferred shifts and work schedules at each health care institution.

Consider a small business owner with ten employees that provides audio-visual support services to clients. Of its ten employees, the organization employs just one

sound engineer. The engineer is highly skilled, quick and remarkably adept at assessing a problem and fixing it. He is a highly valued employee. One day that employee tells the business owner that he wants to start his own business specializing in sound engineering only. They agree this would not be direct competition. The employee needs significant periods of time off from work to begin marketing and setting up his new business. The employer's policies do not provide for the kind of time off that this employee wants. The employee then offers that in lieu of his resigning, his willingness to be available to work on an independent contractor on an as-needed basis. The employer is delighted to be able retain access to this worker's skills and agrees to the relationship. They then agree to a part-time on-call work schedule, agree the (former) employee may continue to use and have access to company equipment, will be paid on the same basis but as an independent contractor. Both parties are delighted to have worked out an arrangement that is amenable to both. That is, until the business owners is advised by legal counsel of the possible pitfalls of proceeding with this type of relationship. The business owner now has to decide, does he risk a possible determination that he may have misclassified this worker in order to keep this highly skilled worker or does he take no risk but keep the worker and both are happy?

There are many other similar stories to share: workers who want or need income while they are between jobs; mothers returning to the workforce after a number of years and seeking a flexible or occasional opportunity to gain working experience before returning to full time status; and more.

SHRM and FiveL Educational Efforts on the Issue

As the largest association for human resource professionals, SHRM provides extensive resources and educational opportunities to help our members comply with workplace laws. Understanding how to properly classify workers is an issue in constant demand by SHRM members. Last year, our knowledge center received approximately 1,485 calls about independent contractors—questions ranging from “I have a former employee that I would like to keep on in an independent contractor status, how do I do it?” to “What forms do I need to file with the IRS and DOL?” SHRM hosts several educational conferences a year and we offer educational sessions on the topic of worker classification. In addition, our online products are constantly updated and include our “Independent Contractor Toolkit” containing articles, frequently asked questions, links to IRS and DOL resources, checklists and sample agreements. In my experience and that of SHRM, employers are sincere in their attempts to comply with the law. Similarly, in my capacity as a consultant, I have given numerous educational presentations to audiences comprised from industry groups, local chambers of commerce and professional associations, like SHRM, on this topic. I have also posted IRS publications 1779 and 15-A on my website and direct new clients and other to these for guidance, and in some cases IRS Form SS-8.

Possible Solutions to Problem of Misclassification: Unintentional and Intentional

While my experience demonstrates that the vast majority of employers are honestly trying to comply with the law, I recognize that there are some employers and perhaps some industries in which there are deliberate attempts to skirt the law. I do not think, however, that additional legislation attempting to clarify the law would provide the intended benefit. Instead, additional law in this area is likely to only add to the existing confusion. Instead, solutions need to focus on the education and the enforcement aspects of the problem.

In many ways, the confusion created by the multiple agency and statutory jurisdiction over the issue of who qualifies as an independent contractor is similar to confusion and overlap created by requirements under the Health Insurance Portability and Accountability Act. In this situation, the Departments of Labor, Health and Human Services and the Internal Revenue Service were faced with issuing guidance on this new, and complex law. The agencies working together, issued joint guidance to the regulated community on the various requirements of the law. The same needs to be done with worker classification. Joint guidance from the various agencies on the classification of employees would greatly assist employers in complying with the law.

Secondly, increased and targeted education should be combined with increased and targeted enforcement. I concur with the general consensus that emerged from the March 27 Workforce Protection Subcommittee hearing that additional legislation is not needed and the focus should be on improved enforcement, clarification and information-sharing. Enforcement of existing law should not only be increased, it should be coordinated among the relevant federal agencies.

Employers need a one-stop shop for guidance on employee classification. This combined with enhanced and targeted enforcement would go a long way toward addressing current problems with misclassification.

Again, I thank the subcommittees for listening to our perspective on the issue of misclassification of employees and SHRM looks forward to working with you on this issue. I will be happy to answer any questions you may have.

Ms. WOOLSEY. Mr. Socolow?

**STATEMENT OF DAVID SOCOLOW, NEW JERSEY
COMMISSIONER OF LABOR**

Mr. SOCOLOW. Thank you, Chairwoman Woolsey, Chairman Andrews, honorable members of the subcommittees. Good morning. It is my honor to appear before you to discuss this problem of independent contractors.

And before I begin, I want to recognize some of the other wonderful New Jerseyans here. Not only Congressman Andrews, Congressman Payne, Congressman Holt who was here before, and even the minority counsel, Mr. Paretti.

So I wanted just to send greetings to all of you—

Chairman ANDREWS. We should strike the rest of his testimony. [Laughter.]

Mr. SOCOLOW [continuing]. Send greetings to all of you, from New Jersey and from Governor Corzine.

Companies that misclassify workers as independent contractors in order to lower their labor costs hurt their workers, hurt the public, and unfairly gain an advantage in the marketplace.

And much has been said already. I will not reiterate all that is in my written testimony on how workers are, in fact, harmed by misclassification.

Governor Corzine of New Jersey has led our state in an important initiative to protect workers by fighting independent contractor misclassification and rooting out the abuses of the underground economy.

Our governor has recognized that the misclassification of employees as independent contractors, in addition to putting workers at risk and unfairly disadvantaging honest employers, costs the state millions of dollars in foregone tax revenue. And my full testimony does lay out the prevalence of this problem.

Let me just say briefly that, even in our random audits of this problem, 38 percent of employers were found to be misclassifying their workers and much, much higher rates of misclassification found in certain industries. And so our auditors will tell you, and I will testify today, that this cannot possibly all be merely unwitting or inadvertent misclassification.

And also, by and large, this is not the request of the employee coming to their employer asking to be treated as a 1099 contractor or misclassified. This is something done to workers by their employers.

We are addressing the challenge, as I said.

The governor directed me, when I took office in January of 2006, to form a task force, which included our Unemployment Insurance Tax group, our Wage and Hour Division in the Department of Labor, Workers' Compensation, and also our State Division of Taxation, which is in the Treasury Department, to identify the com-

mon areas of concern and develop a process to jointly refer cases and share information. By leveraging the resources and findings of each agency, one agency's findings can be used by the other without the need to duplicate the entire investigative process.

And following up on Governor Corzine's initiative, a new law now provides that New Jersey's gross income tax law, wage and hour laws, unemployment insurance law, temporary disability insurance law, all use the same legal test to distinguish between an independent contractor and an employee: the ABC test. And, again, therefore, by using the same legal definition, Division of Taxation staff can use the audit findings of our labor unemployment insurance tax auditors without the unnecessary duplication of effort.

We have also begun cross-matching audit data with workers' compensation data to identify employers who are not properly providing workers' compensation coverage for their employees.

And, most recently, just on July 13, 2007, Governor Corzine signed into law the Construction Industry Independent Contractor Act, which provides even stronger enforcement tools and, for the first time in our state, criminal penalties for employers who cheat their employees, the government, and their competitors by misclassifying workers as independent contractors in the construction industry.

I have included in my testimony five recommendations for action by the Congress and for your consideration to reduce the misclassification of workers as independent contractors.

The first one is, as I mentioned, we recently amended our statutes to have a unified ABC test, a strong test to determine the employer-employee relationship and whether or not an employee is, in fact, an employee or an independent contractor. We recommend that the federal law should also use that test.

The second recommendation that I made is to enhance collaboration. And I want to say, particularly, we heard the testimony earlier of the federal Department of Labor Wage and Hour Division that they are still thinking about whether or not to implement the GAO's recommendation that they refer potential cases of misclassification to their sister agencies.

In this regard, I want to urge that they stop thinking and start actually referring those cases in all cases. If not to the IRS—and they made some points about whether there might be a chilling effect of referring to the IRS—then, at a minimum, to their sister agency within the Department of Labor, which is the Employment and Training Administration, which has jurisdiction over unemployment insurance.

Because we certainly in the state U.I. agencies could use those referrals to collect unpaid tax contributions to the U.I. trust funds, and certainly then in states like New Jersey where we are sharing all those referrals, we could use them to collect state income tax. We could use them to insure that Wage and Hour Division rules were followed.

By increased data sharing, joint enforcement efforts, unified definition of the employer-employee relationship, and a collaborative approach, you really can bring a broad array of resources to bear on this problem.

Another comment that I had made related to the safe harbor provision, we certainly think that it is well past time to reform that provision, which really, in the IRS test, lets a lot of employers get away with misclassifying their workers.

And I also want to just say about the comment that was made by the U.S. Department of Labor Wage and Hour Division mentioned something—

Ms. WOOLSEY. Mr. Socolow?

Mr. SOCOLOW. Yes.

Ms. WOOLSEY. Somebody will ask you that question.

Mr. SOCOLOW. Sure. Absolutely. And then—

Ms. WOOLSEY. We are actually going to have votes in a few minutes, so even if you are Mr. Andrews's brother-in-law—

[Laughter.]

Mr. SOCOLOW. Then let me just quickly finish my final point, Madam Chairwoman, with your indulgence, is that we do believe that if the USDOL expanded the types of unemployment insurance tax audits that could count toward the statistics, that would provide an incentive to state U.I. tax agencies to increase their enforcement.

Thank you very much.

[The statement of Mr. Socolow follows:]

**Prepared Statement of David J. Socolow, Commissioner, New Jersey
Department of Labor and Workforce Development**

Chairman Andrews, Chairwoman Woolsey, honorable Members of the Subcommittees: good morning. I am David J. Socolow, New Jersey's Commissioner of the Department of Labor and Workforce Development. I am honored to have the opportunity to appear before you today to discuss the problem of misclassification of workers as independent contractors.

Our state and national labor laws are designed to protect all of the nation's workers. Unfortunately, it has become all too common for unscrupulous employers to find loopholes in order to unfairly reduce their tax burden and increase their profits, while risking their workers' future health, safety, and security. Companies that misclassify workers as independent contractors to lower their labor costs hurt their workers, hurt the public, and unfairly gain an advantage in the marketplace.

New Jersey Governor Jon S. Corzine has led our state in an important initiative to protect workers by fighting independent contractor misclassification and rooting out the abuses of the underground economy. Our Governor recognizes that the misclassification of employees as independent contractors, in addition to putting workers at risk and unfairly disadvantaging honest employers, costs the state millions of dollars in foregone tax revenue.

Employer Avoidance of the Obligations of the Employer-Employee Relationship

There are two related employee practices by which employees are improperly classified: (1) those workers who should get a W-2 form from their employer but instead are given a 1099 form and treated as if they were self-employed; and (2) those workers paid in cash "off the books." In both of these situations, workers are denied their rights as employees, including the right to organized representation, safety and health protections on the job, family and medical leave, whistleblower protections, vital social insurance benefits and health insurance and retirement benefits offered to employees.

When employers misclassify their employees, those workers and their families are left vulnerable when they are in greatest need of the benefits routinely accrued through employment. The practice not only threatens the ability of honest businesses to effectively compete, but it also leads to reduced tax revenue and less funding for benefit programs.

In our experience in New Jersey, employee-employer relationships are being deliberately severed by employers driven by the quest to improve their bottom line. Many employers are intentionally, and illegally, cutting their legitimate business costs by choosing to treat bona-fide employees as if they were self-employed contractors. In so doing, these employers leave it to their employees to pay for social insurance pro-

grams and take on their own tax withholding liabilities. While some misclassification may be due to legitimate misunderstanding of the law, the primary reason that most employers choose to misclassify employees is a desire to avoid the employer costs of payroll taxes for social security, unemployment and disability insurance as well as worker's compensation insurance premiums.

Deliberate misclassification of employees as independent contractors is not the benign issue that offenders engaging in this practice would have us believe. Even if, as several have argued, some workers voluntarily participate and find this practice advantageous, it still does not remove any of the injuriousness of misclassification. Many employees who find themselves misclassified are ill-prepared and undereducated as to the responsibilities of self-employment.

A report released by Cornell University in April of this year indicated that "[w]ith less tax revenues flowing into government coffers, public resources are strained. State unemployment insurance systems, for example, are forced to compensate by raising contribution rates for employers who comply with the regulations. According to the Government Accountability Office, underpayment of Social Security, unemployment insurance, and income taxes in 2006 due to misclassification amounted to an estimated \$2.72 billion; the researchers here argue that the real cost is substantially higher, particularly when losses at the state level are factored in."

Employers who pay workers in cash "off the books" create additional difficulties. When an employer issues a 1099 form to an individual, enforcement agencies at least have a paper trail to follow. Individuals who work "off the books" for cash payment are hidden still further in the underground economy. Sometimes these workers are exploited because they are undocumented residents. Other times employers hire a worker for a short time without keeping proper records, paying insurance premiums, or arranging for withholding.

How prevalent is the problem?

In the New Jersey Department of Labor and Workforce Development's recent yearly audits of 2.2 percent of employers—around 6,000 annually—we have found either independent contractor misclassification or workers being paid in cash "off the books" in 42 percent of cases. Even among the more than 750 employers selected totally at random for an audit, 38 percent of these firms violated the law by misclassifying their employees. The Department also conducts approximately 1,500 targeted investigations annually. Some of these investigations are triggered when misclassified workers apply for unemployment insurance, temporary disability, or workers' compensation benefits that they assumed their employers were paying on their behalf. When these workers attempt to file for benefits, their claims are often initially denied because they are not recorded in the system as an employee. In most cases, subsequent investigations show that the individual was misclassified and should have been treated as an employee.

Overall, in 2006, our audits found nearly 25,000 workers misclassified and uncovered more than half-a-billion dollars in misclassified or unreported wages (\$565 million). In 2005, New Jersey's audits found 28,286 misclassified workers, with misclassified or unreported wages of \$644 million. In calendar year 2004, these audits turned up more than 26,000 workers whose employers misclassified their employment and failed to provide these workers with New Jersey unemployment and disability insurance coverage.

We find an even greater level of non-compliance when we target our investigations to industries known to have widespread abuses. This practice first attracted our attention as a result of audit patterns and complaints about building contractors filed with the Division of Wage and Hour Compliance, which led the Department to uncover a significant number of misclassification violations in the construction industry. In 2006, out of 871 audits and investigations in the construction industry, 41 percent found misclassification of employees, identifying nearly 3,000 misclassified construction workers, \$78.2 million in under-reported gross wages and \$2.1 million in under-reported contributions. However, the misclassification of employees is no longer primarily limited to the construction industry. We have also found significant patterns of violation in food processing plants, courier services, dental assistants, waitresses, nail salons, nurses, secretaries and landscaping.

For example, the New Jersey Department of Labor and Workforce Development recently conducted a program of unannounced investigations of nail salons and found workers not properly classified as employees in more than two-thirds of all establishments examined (350 investigations, 240 assessments). Field investigations of several hundred landscapers disclosed failure to classify worker as employees in nearly 62 percent of all businesses examined. Our investigations of dentists found that 53 percent of the employers improperly treated their dental assistants as independent contractors and not employees. The Department has also greatly benefited

from data-sharing with the Internal Revenue Service (IRS). Investigations initiated as the result of analysis of 1099 information provided by the IRS since 2003 resulted in findings of non-compliance in 75 percent of cases (111 cases, 84 assessments).

In another example, for unemployment insurance tax purposes, New Jersey law treats an employee leasing company as the employer of the workers of its various clients. The tax accounts of the client companies are then recorded as inactive accounts while the leasing company reports the payroll for the workers. Our examination of inactive client company records, however, has disclosed that many of these companies continue making payments for services, generally to “independent contractors” or other temporary workers not included on the new payroll reports from the employee leasing company. Our recent investigations have found this type of non-compliance in 61.5 percent of all these investigations (367 investigations, 226 assessments).

The New Jersey Department of Labor and Workforce Development also has uncovered significant patterns of employers’ misclassification of workers through monthly enforcement sweeps by our State Division of Wage and Hour Compliance. These enforcement efforts are targeted in the residential and commercial construction sectors, the garment and apparel industry and large-scale farming operations. Employers who refuse to provide timesheets or payroll records are issued subpoenas. Employers who ignore the subpoenas are subject to prosecution as disorderly persons for a first offense and even more serious criminal penalties for subsequent or egregious violations. During the first six months of 2007, the Wage and Hour Compliance Task Force has made 158 referrals to the New Jersey Division of Workers’ Compensation and 228 referrals to the Unemployment Insurance Division of Employer Accounts for suspected misclassification of workers.

We find that employees who are misclassified rarely feel that they are in a position to demand that they be correctly classified as an employee. By contrast, true independent contractors choose to be self-employed. They not only receive a 1099 form that they use to declare their income for taxes but also must assume much of the tax and insurance liabilities normally paid by employers, including paying both the employer and employee portions of Social Security taxes, contributing to unemployment insurance, and providing their own workers’ compensation insurance. True independent contractors set their compensation at levels high enough to cover payroll taxes, insurance and other expenses for which they are responsible. This is not possible for employees who are expected to work for their employer as independent contractors while receiving relatively the same pay as an hourly worker.

How we are addressing the challenge

In April 2006, soon after taking office, New Jersey Governor Corzine directed the Treasury Department’s Division of Taxation and the Department of Labor and Workforce Development to work together to combat the practice of misclassification of employees. We formed a task force that included the Divisions of Employer Accounts, Wage and Hour Compliance, Workers’ Compensation, and Taxation to identify common areas of concern and develop a process to exchange information. By leveraging the resources and findings of each agency, findings from one department could be used by the other without the need to duplicate the entire investigative process. The sharing of information among agencies and programs is an important part of this initiative, which aims to break down “silos” within government and have the various agencies of government cooperate on tips, leads, and investigations.

Following up on the Governor’s initiative, last summer the Legislature sent a bill to the Governor’s desk to support our efforts. This law, P.L. 2006, Chapter 85, now provides that New Jersey’s Gross Income Tax law, wage and hour laws, Unemployment Insurance law, and Temporary Disability Insurance law use the identical legal test to decide whether an individual is an employee or an independent contractor—the “ABC test.”

Under the “ABC test,” an individual paid for services is presumed to be an employee unless he or she meets all three characteristics of a self-employed, independent contractor. These are: (A) that the individual has been and will continue to be free from control or direction over the performance of such service, both under his contract of service and in fact; (B) The service provided is either outside the usual course of the business for which service is performed, or that the service is performed outside of all the places of business of the enterprise for which such service is performed; and

(C) The individual is customarily engaged in an independently established trade, occupation, profession or business, so that the individual would not routinely become unemployed when his or her relationship with this particular employer ended.

Because these sister state agencies use the same legal definition of a true independent contractor, Division of Taxation staff, for example, can use the Labor Department's findings to enforce the income tax law without the unnecessary duplication of effort. The Division of Taxation is also able to use the findings of compliance audits by Labor Department auditors to pursue income taxes owed to the state. The Labor Department also can follow up on audits by the Division of Taxation to ensure that employees are properly paid and covered for Unemployment Insurance and Temporary Disability Insurance benefits.

Additionally, we have recently begun a cross match of audit data with Workers' Compensation data to identify employers who are not properly providing Workers' Compensation coverage for their employees. This innovative data-sharing procedure has led to more than 75 investigations of employers involving more than 1,300 workers. Investigators from both Wage and Hour and Employer Accounts now check for Workers' Compensation Insurance coverage. In addition, by sharing tax-audit information with the Compensation Rating and Inspection Bureau that oversees Workers' Compensation insurance premiums, the State can better identify employers who are underpaying Workers' Compensation premiums.

New Jersey was also an original volunteer, one of four states, to join a partnership with the Internal Revenue Service in dealing with Questionable Employer Tax Practices, or QETP. This federal-state partnership is developing and implementing a federal/state approach to addressing worker misclassification and other attempts to avoid employment taxes. Our State has gained positive results from previous exchanges of information from the IRS. As mentioned above, 75% of the leads from these IRS 1099 data have found non-compliance. We anticipate similar results under the QETP federal-state partnership, which has been designed to enhance enforcement of tax laws, protect accurate worker classifications and discover and address tax avoidance schemes through the sharing of information and by leveraging federal and individual state resources.

Most recently, on July 13, 2007, Governor Corzine signed into law the Construction Industry Independent Contractor Act (P.L. 2007, c. 114). This law provides even stronger enforcement tools and more effective penalties, including criminal penalties for the first time, for employers who cheat their employees, their government and competitors by misclassifying workers as independent contractors. Under this law, a contractor that has knowingly misclassified workers can be guilty of a crime of the second degree. Such a contractor can be held liable to make up any loss to the employees if they were underpaid in connection with the misclassification. The law also authorizes the Commissioner of Labor and Workforce Development to assess and collect administrative penalties, up to \$2,500 for a first violation and up to \$5,000 for each subsequent violation. Contractors that engage in this practice can be made ineligible to receive public contracts.

Recommendations for Federal Action

The Congress should address five areas that can be improved to reduce the misclassification of workers as independent contractors:

1. Establish a strong, universal federal definition of employee: As I mentioned, New Jersey recently amended its statutes to have enforcement agencies use the strong "ABC test" to determine the employee-employer relationship. Similarly, federal laws should adopt the "ABC test," as used in New Jersey, to distinguish an employee from an independent contractor. A strong, consistent test for independent contract status would enhance federal enforcement of such laws as the National Labor Relations Act, the Civil Rights Act, the Internal Revenue Code, the Fair Labor Standards Act, the Occupational Safety and Health Act, and the Employee Retirement Income Security Act.

2. Enhance collaboration: New Jersey's aggressive multi-agency approach to addressing the problem of employee misclassification provides a model for improved coordination among federal enforcement agencies. New Jersey's increased data sharing, joint enforcement efforts, unified definition of the employee-employer relationship, and our collaborative approach bring a broad array of resources to bear on this problem. Similarly, federal agencies should adopt universal standards for all investigators that clarify the procedures for referring misclassification cases to the other appropriate federal and state agencies charged with enforcement. This recommendation was also made in May 2007 by the GAO in its testimony on employee misclassification to the Subcommittees on Income Security and Family Support and on Select Revenue Measures, which referenced GAO's finding that USDOL district offices have varying referral procedures and inconsistently referred misclassification cases.

3. Amend Section 530 of the Revenue Act of 1978: Section 530, commonly referred to as the "safe harbor" provision, prevents the IRS from reclassifying workers prospectively as employees, contains deficient reporting requirements on employers who

make payments to independent contractors, and establishes insufficient penalties for employers who pay their workers under the table and fail to file 1099's. Section 530 also allows employers to misclassify workers as independent contractors in certain industries, regardless of the employment relationship, if, in a particular industry, there is a "long-standing recognized practice" of classifying the workers as independent contractors or if the employer underwent an IRS audit anytime in the past. Reforms to Section 530 are long overdue and both the GAO and the IRS are on record urging reforms that would increase the effectiveness of compliance programs and increase collection of tax revenue by the US Treasury.

4. Empower workers to assist in ensuring proper classification: Workers and their representatives should have the option of receiving an employee status determination from the IRS to ensure their proper classification. When requesting a determination, the workers should have their confidentiality maintained to the greatest extent possible, should be protected from retaliation by employers when requesting a determination, and should be afforded appeal rights. Also, the Fair Labor Standards Act workplace poster should be revised to include information that informs workers how and where to file complaints.

5. Increase enforcement: The USDOL should expand the types of unemployment insurance tax audits that states may count in the statistics reported to USDOL, including those audits that fail to find a source document (such as a cancelled check or an original time sheet). This would provide state unemployment insurance agencies with an incentive to pursue audits in cases where employers fail to produce or maintain payroll records. Additionally, enforcement by USDOL's Wage and Hour Division could be improved by establishing adequate administrative penalties for the knowing and willful misclassification of workers and for record-keeping violations. The New Jersey Division of Wage and Hour Compliance has enjoyed the statutory authority to assess and collect administrative penalties since 1991 and this has proven to be a useful compliance tool. Lastly, the USDOL should be urged to target enforcement in industry sectors known to have high rates of misclassification and to assist states in their enforcement efforts through supplemental funding.

I thank you for the opportunity to testify and I would be happy to answer any questions you may have.

Ms. WOOLSEY. Thank you very much.

We are going to have votes soon. But we are going to have questions until we get down to the last minutes of having to run, and then we will come back.

Ms. Walters, I, too, am a human resources manager for over 20 years. Now, I have been here for 15, so I have been away from it for a while. But it was always clear to me—I mean, my company had 800 employees. We started with 12, and I grew up to 800 before I started my own independent consulting firm. And I could always tell when my clients knew the difference between an independent contractor and not. And I would guide them to do the right thing.

It is complex. And it is more complex now when we have—just about any kid that has parents, if they are lucky to have two—are in the workforce. And we have to do things so that parents can bridge work and family. But we don't have to, at the same time, take away the protections that these employees need and deserve.

And they might be glad to have flex-time, absolutely. But if that means when they have an accident, they don't have any kind of health protection, what good is that?

So what we are trying to do here is ask you—I am going to ask you what your association is doing to—I mean, do you have a task force that would be working on how to help the federal government make clear what would be a part-time employee that is misclassified? How are you doing that?

That is what your association needs to be working on. Not telling us we shouldn't do it, that we should leave it just as complicated as it is. That is ridiculous.

Have you looked at Mr. Socolow's five actions? Those are great actions. I would love to have your association's opinions on those.

Ms. WALTERS. A flight of ideas in response.

One, for example, the society absolutely doesn't mean to just leave things the way they are. And I don't want you to hear that as my testimony today.

As an example, guidance on HIPAA compliance: The Department of Labor, Health and Human Services, and the Internal Revenue Service worked together to provide guidance to the regulated community on various aspects of HIPAA compliance. I think that was a great move. It was a multi-agency initiative to, again, provide clarification, education on how employers can best comply.

That is, day to day, every day the commitment of the society is to serve the professional and advance the profession. And we do that when we provide education and information to help employers comply with the law, not skirt the law.

It is trying to figure out with when there is, you know, economic realities test and a manner and means test, an IRS 1099 rule, how do I know, you know, it is difficult to comply. Which test do I use?

Ms. WOOLSEY. But if you would yield to me just a little bit. I am asking you, are you looking at providing some information that would streamline this so that, indeed, you don't have—I mean, like Mr. Socolow has?

Ms. WALTERS. The society today—SHRM provides on its Web site—I think not dissimilar from what I heard perhaps the representative from the Department of Labor describe provides—we actually have an independent contractor toolkit that our members can go to the Web site and receive guidance and information. We post the IRS Publication 1779, Publication 15-A.

So, again, trying to be proactive to provide as much education and information as we can on this topic.

Ms. WOOLSEY. So, Mr. Socolow, would you like to finish that one thought I cut off before I pass the microphone?

Mr. SOCOLOW. Yes, Chairwoman Woolsey. Thank you very much.

The final point I had wanted to make was about this point, which was made repeatedly, by the U.S. Department of Labor Wage and Hour Division that misclassifying an employee is not, in and of itself, a violation of any of the 70-plus laws that they enforce.

In New Jersey, we have a statutory authority under our wage and hour laws to assess administrative penalties for essentially failing to keep records. And if you are not counting somebody on your payroll books as an employee, you are not keeping records on them. That, in and of itself, is a violation of wage and hour laws.

And if the Congress sees fit, it seems that that would be an area to give the Wage and Hour Division, which is going to be probably the first line of defense against these problems, a new tool—a tool we enjoy in New Jersey and have since 1991—to go after the employers that are willfully and wrongly doing this.

Ms. WOOLSEY. Thank you so much.

Mr. Wilson?

Mr. WILSON. Thank you, Madam Chairman.

And, again, thank you for being here today.

In particular, before I was selected, I served as a real estate attorney. I worked with the construction industry, Ms. Stafford, very closely. And in our region, construction is just the basis, I believe, of the sound economy we have, the booming economy we have. It is the tax base for the schools. Just everything comes together.

And so I want to make sure that what we are doing is beneficial to the people working and to the economy—and again, that is why I appreciate drywall—everything that you do.

And so keeping that in mind, Ms. Walters, what would be the impact on the construction industry if Congress were to get it wrong or legislate a solution that threatens the viability of bona fide independent contractor status?

Ms. WALTERS. I think I wouldn't want to respond to a particular industry. But I think there is a potential for multiple industries that if there is legislation, as you put it, that doesn't quite get it right, the impact could be then for those that are today properly classified as independent contractors may lose that status, may walk away from the status not wanting to do so, for fear of, I guess, being reclassified as an employee and not wanting that relationship either.

Mr. WILSON. And, again, I want your input on that because construction, hospitality, landscaping, all of these are extraordinary opportunities for people at ground level. And then they can, as Ms. Stafford, own their own business. So that is great.

At our last hearing, we heard from one representative of a trade association that those efforts of his association were made to assist its members in compliance with the wage and hour classification laws.

Can you expand, in your testimony, Ms. Walters, as to the activities of the Society for Human Resources Management in helping its members ensure that the laws are being followed correctly?

Ms. WALTERS. Sure, yes. Again, as I mentioned, on the society's Web site there is actually an independent contractor toolkit. That toolkit provides a variety of resources, including links to governmental agencies, government publications.

The society also sponsors conferences every year, throughout the year, multiple conferences. I have had the honor, as have others, in presenting and providing educational programs and information on managing your contingent workforce, the different types of working relationships, how to determine whether a working relationship is or is not an employment relationship—some of the factors to consider there.

Mr. WILSON. And, Ms. Walters, the question was asked at our first panel and now I am going to ask you, and that is that at a Workforce Protections Subcommittee hearing earlier this year, one person noted that the question of whether an individual worker is a contractor or an employee isn't that complex. Based on your 20 years of experience as a human resources professional, do you agree?

Ms. WALTERS. I think it is nice we have heard consensus here this afternoon—or at least I have heard consensus—that it can be

simple and it can be complex. And it is always a case-by-case analysis.

And what can appear today to be a very straightforward, appropriate independent contractor relationship may in 4 months, 6 months evolve into something that looks very different than what we intended today. Some are clearcut, and some are not.

So I think it can be very complex.

Mr. WILSON. Thank you very much.

Ms. WALTERS. Thanks.

Ms. WOOLSEY. Mr. Andrews?

Chairman ANDREWS. Thank you very much. I appreciate that.

Thank you, first of all, everyone, for their testimony.

Ms. Walters, early in your statement, you talk about the problem of a lot of the complexity coming from the fact that there is not one definition of what an employer is; many different statutes, many different definitions.

Then on page nine of your statement, you say that you do not think that additional legislation attempting to clarify the law would provide the intended benefit.

I have trouble reconciling those two points. What is wrong with Mr. Socolow's suggestion that there be a single, strong, clear, unitary definition of what an employer is? Why shouldn't we do that?

Ms. WALTERS. I think part of the concern would be one, I think it would be a fascinating process to watch for Congress—I guess the question is, what would supersede what?

If we were to abolish—and I am not sure that is what I am hearing today is a suggestion to take ERISA and ADA and FMLA and all the different federal statutes, abolish every definition federal and then state also, and have one definition that would apply to everything.

Chairman ANDREWS. I am going to let him speak to it himself. I don't think that is the proposal. I think that the idea was to have a uniform definition without abolishing something.

Mr. Socolow, what exactly are you proposing?

Mr. SOCOLOW. I think that the difference is between a definition of an employee versus a definition of independent contractor, right?

The ABC test that we have in New Jersey, that a number of other states use as well, and that, as I said, we now use for taxation and for unemployment and a number of other things, the ABC test is just about distinguishing whether or not someone is an independent contractor.

There are plenty of other definitions you can have about what is covered by FMLA and what isn't. But it seems to me that for the purposes of defining an independent contractor, the ABC test is clear. It has got lots and lots of case law that now is behind it. And it works.

Chairman ANDREWS. I think under the ABC test Mr. Williams probably wouldn't be sitting here today. I think that his facts were crystal-clear that he would have been treated as an employee.

Mr. SOCOLOW. As is evidenced by the fact that he received unemployment compensation, which was determined, I am almost certain, by the ABC test.

Chairman ANDREWS. So I think, as a practical matter, for Mr. Williams's case, it would have given him more justice more quickly, which, I think, is what we want to accomplish.

And, Ms. Stafford, if I can ask you, would a single definition of employer under these various statutes be easier for you to deal with as a businesswoman?

Ms. STAFFORD. Absolutely. I think that it seems to me that it centers so much around the 1099. If I were this committee, I would be looking hard at the 1099 and what employers really use that as a tool for.

It seems to me that that is the disconnect between people that pay taxes and make sure that they withhold taxes from employees to people that hand out 1099s like they are irrelevant pieces of paper that people never pay taxes on. And it is not followed up, apparently not, not at 38 percent, as Mr. Socolow—

Chairman ANDREWS. Mr. Williams, you were about to say something. What I wanted to ask you was, did you ever doubt in your ordeal that your employer intended to misclassify you, or do you think the employer was just mistaken in interpreting what the law was?

Mr. WILLIAMS. No, I think the whole intent of the operating agreement was to classify us as independent contractors and to keep us as independent contractors, thereby shifting all the costs to us and making us pay, you know, having to pay for the entire situation.

In Massachusetts, there are three simple situations: the 123 test they call it in Massachusetts, which is if you control the employee, or if the employee is not allowed to work for others, or if the employee is in a different business or if the employee is in the same business, then you can't classify him as an independent contractor.

All three of those tests, very clearly in the FedEx model, have proven to be employees.

Chairman ANDREWS. And, Commissioner Socolow, if you had to just take an educated guess at the percentage of enforcement actions your department has engaged in that are intentional misclassifications versus confused or inadvertent ones, what is your estimate of that breakdown?

Mr. SOCOLOW. Congressman, it is hard to put an exact number on that. But I will say that when you see the industries in which 60, 70 percent of the employers are routinely and continually engaging in this practice, when you see, furthermore, unfortunately that when we do follow-up audits of those who we have found violating it and go back and look at them 2 and 3 years later, that 60 and 70 percent continue to misclassify their workers, I would say that a very substantial share of employers are doing this intentionally.

Chairman ANDREWS. Do you have any reason—I see my time is up. Thank you very much.

Ms. WOOLSEY. Mr. Kline?

Mr. KLINE. Thank you, Madam Chair.

I want to thank the panel for being here with us today, for their testimony and for answering the questions. I have a couple of different directions I want to go, because I am finding this to be still fairly complex.

Just for the record, Mr. Williams, I want to make sure that I understand the status of your cases. You have a hearing scheduled before the National Labor Relations Board later this fall, is that correct?

Mr. WILLIAMS. That is correct, sir.

Mr. KLINE. And you have some action in state court with a lawsuit, is that correct?

Mr. WILLIAMS. That is also correct.

Mr. KLINE. And neither of those have been resolved yet, is that correct?

Mr. WILLIAMS. No, sir.

Mr. KLINE. So those are pending. All right. Thank you.

Ms. Walters, I want to go back to this issue of definition. We have, in the previous hearing and in this hearing today in the discussion with the administrator on the first panel, recognized that there is a lot of confusion over this definition. And it does seem that it would be helpful if we didn't have so many definitions, if we could make it simpler.

And yet, as you said in your testimony and your discussion with Mr. Andrews, that you don't think that we should try to change the statutes, and, as I understand your answer, that is because, as Mr. Andrews said, there are various statutes. There are many statutes, and just the process—knowing how we work or don't work here in Congress—that could be pretty problematic as we went in and tried to fix these definitions for all the statutes.

But you discuss something in your testimony called joint guidance. Can you tell us how that might help this problem?

Ms. WALTERS. Sure, I would be happy to.

Just giving consideration to, again, multiple agencies that have purview in administering and enforcing some of the laws where this issue comes up—again, Title VII, ADA, Family Medical Leave—so perhaps the Department of Labor, the EEOC, the IRS coming together, as they did in the example we gave with regard to HIPAA compliance, coming together to try and develop guidance for employers in how to, you know, clarify applying the different tests, is there guidance that would be and it is the society's position that could be extremely helpful to employers to move toward some consistency in the application of the different interpretations.

Mr. KLINE. So this guidance, then, would not require a statute change? But it would do a couple things. It would make it easier for employers, presumably, to understand. But it also would make it easier for employees and others to understand if there was a willful misclassification. Is that correct?

Ms. WALTERS. That is correct. That is what we believe.

Mr. KLINE. And so it would achieve, presumably, both goals: make it less likely that there would inadvertent misclassification, and certainly make it easier for other members of the panel and employees across the country to understand if they are being taken advantage of.

Ms. WALTERS. I believe so, yes.

Mr. KLINE. Okay. Thank you.

I yield back.

Ms. WOOLSEY. Mr. Kildee?

Mr. KILDEE. Thank you, Madam Chair.

Mr. Williams, when you were injured in 2002, you did not file for workman's compensation benefits. Why not? And who paid for your medical bills at that time?

Mr. WILLIAMS. Eventually, the medical bills were paid by the person that caused the accident, by that particular company's—that person is insured, as he was found to be at fault and be at fault in a major situation.

The only income I had at the time was for the worker's accident policy, which was provided in the contract in FedEx, which I paid for every week. But that is the only thing I had to live on at that time. I had no other income coming in.

I was ineligible for workman's compensation. FedEx would not—did not—contribute to workman's compensation. Therefore, I was ineligible. The only thing I had was this worker's accident policy, for which I paid.

Mr. KILDEE. And that was a private worker's accident policy?

Mr. WILLIAMS. Yes, provided through FedEx through an insurance company.

Mr. KILDEE. But you did not qualify for the regular workman's compensation benefits?

Mr. WILLIAMS. No. I was told I could not qualify.

Mr. KILDEE. So eventually, because the other party was at fault, you eventually collected from—

Mr. WILLIAMS. Recouped for the hospital expenses, et cetera, yes.

Mr. KILDEE. Were you told you that you could not file for workman's compensation?

Mr. WILLIAMS. Yes. It is very specific in the FedEx operating agreement and also in the policy that the protective insurance company provides for you. It says, "You are not, under any circumstances, covered by workman's compensation."

Mr. KILDEE. Thank you very much.

Thank you, Madam Chair.

Ms. WOOLSEY. Thank you.

Mr. HARE?

Mr. HARE. Thank you, Madam Chair.

Mr. Williams, just a few other questions about it. I am assuming your van was damaged in the accident?

Mr. WILLIAMS. Yes, sir.

Mr. HARE. And who paid for that?

Mr. WILLIAMS. Well, it was my van. It was totaled in the accident. And it was paid for by the other party's insurance company. My insurance company paid for it first.

Mr. HARE. And then at some point you went back to work and you were required to replace your P400 vehicle—

Mr. WILLIAMS. Yes.

Mr. HARE [continuing]. With another one selected. And what happened to that vehicle?

Mr. WILLIAMS. Well, when I was terminated in December of 2005, I was on the hook for that vehicle, if you will. I was liable for the payments. It was a leased vehicle that was set up through FedEx. And when they terminated me, I had to get rid of the vehicle.

I was one of the few fortunate ones to be able to get rid of the vehicle through the leasing company. I called them the day after

I was terminated, told them what had happened. They told me to take it to a certain location. I took it to that location and turned it in. And then approximately 6 months later, my vehicle was sold.

In the meantime, I had to make all those monthly payments. I did not make them because I told them I didn't have the income to make them. But they did eventually sell the vehicle.

Mr. HARE. Ms. Stafford, just a couple of questions for you. You said that in residential construction it is impossible for companies like yours to compete. Is misclassification rampant in that industry? And, if so, why do you suppose that is the case?

Ms. STAFFORD. It certainly—it is rampant.

And the difficulty we have is the market supporting our prices to do the work because we are paying—when you talk about the difference in percentage from one company to another, my federal, state, Medicare and all the employee contributions run about 16.2 percent to my company.

But if you are misclassifying an employee, and you are also skirting a workman's compensation payment that should be made, that is another 10 to 15 percent, depending on what the classification that you are using, if you have an insurance policy.

If you don't have either of those two things, you are talking about somewhere in the neighborhood of a 30 percent price advantage.

Mr. HARE. Well, in your experience, what happens to the workers when they are misclassified as independent contractors? In other words, you know, how do they cope when they are injured, and how do they handle the cost of being an independent contractor?

Ms. STAFFORD. There have been a lot of documented cases of what happens in the housing industry. And basically, there have been cases when there has been a major accident and the person goes on the payroll that day. And all of a sudden shows up under the employer's workers' compensation policy. However, prior to that, he was never on the employer's records and was being paid cash under the table.

Mr. HARE. Chairman Andrews, I would like to yield to you. You had a question that you didn't get to finish.

Chairman ANDREWS. Thank you.

I did want to ask Mr. Socolow if the experience he has had in New Jersey, if he has seen any evidence that it is atypical of states across the country; in other words, this prevalence of intentional misclassification.

Mr. SOCOLOW. Yes, Chairman Andrews. The colleagues in the other U.I. tax agencies in the other wage and hour divisions of state governments collaborate. There are conferences. And this topic is topic number one at both of those conferences. All the states are seeing the same patterns.

Chairman ANDREWS. I thank my friend for yielding.

And I thank the commissioner.

Ms. WOOLSEY. Mr. Bishop?

Mr. BISHOP. Thank you, Madam Chair.

Ms. Walters, you have indicated that you don't believe that this is an issue that suggests new law ought to be passed on the part of the federal government, but that you do believe that the way to

approach this problem is through improved enforcement and clarification of existing law and information-sharing.

That is essentially the position of your organization?

Ms. WALTERS. It is. Just the one point of clarification is adding a new federal law to those that already exist I think would not be the best approach to enhancing clarification.

Mr. BISHOP. But would enforcement and clarification be enhanced if there were this automatic referral notion that has been recommended by the GAO? How would you feel about that?

Ms. WALTERS. My first impression in response to that is I think that would not help with clarification because it is still going to come after the fact.

Mr. BISHOP. Would it not help with enforcement?

Ms. WALTERS. It could help with enforcement. But I am not sure how it would help with the initial appropriate—

Mr. BISHOP. Would not enforcement ultimately yield clarification? I mean, wouldn't people, in effect, get the message?

Ms. WALTERS. They would. But, again, I would think everyone's goal here is to what can we do to prevent this from happening in the first place, proactively to get clarification, education so that there is—rather than needing the increased need for enforcement because there is more misclassifications than there used to be—what can we do proactively to prevent the misclassifications in the first place?

That is the society's goal is to try and, you know, get this, nip it in the bud, if you will and—

Mr. BISHOP. And in an ideal world, I would agree with you. I think you would also agree that none of us live in that ideal world. I mean, if I were to follow that logic, the IRS's function would be to simply provide information to help people fill out the forms. [Laughter.]

Ms. WALTERS. You know, I would go back to, with regard to the multi-agency guidance that was given out before, I don't know if there is statistics to measure the number of alleged violations before and after that, but, you know, it is an effort that I think is well worth consideration.

Mr. BISHOP. I guess the point I am trying to make is—what I am struggling to understand is, in the absence of a unitary definition, which I think I would support a unitary definition, but it seems as if you do not—but in the absence of a unitary definition, and in the absence of mandated or automatic referral, I don't see how we can be effective in terms of targeted enforcement. I just fail to understand how we would have sufficient tools to target enforcement if we didn't have those two tools.

Ms. WALTERS. SHRM supports the idea of enforcement. Absolutely. Absolutely.

And I think the other question on the table is—and, again, I think a point of clarification is I don't know the answer to the question, but what comes to my mind, what the society is considering is if there is consideration of one definition, how is that applied when a claim comes up under ERISA, when a claim comes up—I don't know the—

Mr. BISHOP. I am not suggesting for a moment that to divine a definition would be easy. It wouldn't be. But we step up to the

plate on lots of complex issues. And I think simply because this is complex, we ought not to allow that to deter us.

Mr. Socolow, if I may? In New Jersey, it is considered a violation of the law to misclassify an employee, correct?

Mr. SOCOLOW. Yes, Congressman.

Mr. BISHOP. And have you found that to be a deterrent?

Mr. SOCOLOW. Yes, we have. We have been doing a lot of education and information and clarification. And we have found over time that having a strong enforcement process, in fact, does complement those compliance assistance efforts, as well.

Mr. BISHOP. Thank you very much.

Thank you, Madam Chair.

Ms. WOOLSEY. Mr. Payne?

Mr. PAYNE. Thank you very much.

Mr. Socolow, you mentioned that in your testimony you highlighted New Jersey's new law, known as the ABC test.

Although the law has not been in effect for long, do you believe it has been effective in determining whether an individual is an employee or an independent contractor? And do you know if other states use the same test? And if so, what states? And do you believe that it is effective, as well, with them?

Mr. SOCOLOW. Congressman Payne, thank you.

The chief thing that happened a year ago last summer was that our taxation division adopted—or the statute was changed so that the taxation division has the same ABC test that we have had for many, many years in unemployment insurance.

And what that has been effective over the last 12 months—or 7 months, because it took effect in January of this year—it has given us the opportunity now that, when one agency does an audit or an investigation, those findings can be used by the other agency to double up on the enforcement without having to double up on the work.

So that is the chief—from an enforcement perspective, it just streamlines and breaks down those silos between agencies of state government.

As to the ABC test, it is widely used by unemployment insurance programs—you know, prong C, the third prong of the test, which goes to whether or not the worker would be able to survive the loss of that client as an independent contractor or whether they would be unemployed, obviously comes from the question of whether somebody should get unemployment benefits.

And, yes, I would advocate that every state use it for their income tax, as well.

Mr. PAYNE. Let me ask another question in regard—and you may not have the answer at hand. But, as you know, FedEx and UPS are the big competitors in the whole delivery system. Actually, you know, FedEx used to keep up with UPS's benefits to, I guess, show that unionization is not necessarily necessary to get benefits and so forth and so on.

However, there is a new guy on the block—not so new—but they are DHL. And I don't know if you have taken a look at that operation. One, as you know, it is part of the Federal Republic of Germany's subsidized mail system. Therefore, indirectly, they have un-

fair advantage. But secondly, they make it, I believe, mandatory that every driver is an independent contractor.

And I wondered, do you know of that situation?

Mr. SOCOLOW. Congressman Payne, I guess I would have to get back to you specifically about that situation.

I do know that we found in that industry certain instances where drivers were misclassified as independent contractors. We have one of them here today on the panel. And we have found that, as well, in New Jersey. And we are enforcing to make sure that that is corrected.

Mr. PAYNE. It is probably even a little more difficult one at this time.

Our federal post office—I should have asked our federal witness—had begun in the last year or so to hire independent contractors, can you believe it? They are hiring people to—if you have got a pickup truck, you can just go and we will contract with you to pick up mail and, you know, deliver it to a sub-post office.

And it seems to me like the federal government is violating the law. It would appear to me that they are overreaching. It appears to me that they are trying to break the union—postal workers union—by this contracting out. As a matter of fact, even in the post office delivery system, there is the same kind of situation happening.

And so I would really like to get together with your department and see whether we need to sue the federal government about the state of New Jersey. [Laughter.]

But I am serious about these practices, once again, of the federal government coming in, as they did in our—

Mr. SOCOLOW. Rodino Building.

Mr. PAYNE. Right. And now it is in the new federal building where I moved next door when the new building was built.

But I would certainly like to talk about and see whether there is some serious violations by the federal government.

Mr. SOCOLOW. I look forward to following up with you on that, Congressman. Thank you.

Mr. PAYNE. Thank you very much.

Ms. WOOLSEY. Mr. Holt?

Mr. HOLT. Just as the bells ring.

Thank you, Madam Chair.

And I welcome the witnesses, particularly Commissioner Socolow, whose career has shown that intelligence, competence and skill can be rewarded.

I think New Jerseyans can take pride on this subject, as Mr. Andrews and Mr. Payne have pointed out. I think this is one area where we have shown ourselves, our state, to be progressive.

Let me follow up on two subjects. One is the declaration that this is unlawful behavior: misclassification. What do you say in response or do in response to those employers who say, "Well, this is really by mutual agreement," or, "This is what the employee wanted?"

Mr. SOCOLOW. Like with any labor standard, you often have that thrown back at you. People say, you know, the worker agreed and didn't want to be paid overtime for working more than 40 hours in

a work week. People say that the worker didn't want to be paid the minimum wage.

Well, that is really not relevant. I mean, you cannot contract, you cannot voluntarily, even in a mutual agreement, give up the rights that are there for workers. And that is because it is arguable that such an agreement really would be voluntary. It would almost certainly have elements of coercion.

And so, that is really not a matter. The law is very clear as to whose call that is. That is the call of the enforcement agency and, if we are challenged, up ultimately to the courts. But it isn't between the employer and the employee to go ahead and break the law.

Mr. HOLT. And that is not difficult to uphold in the courts.

Mr. SOCOLOW. No, not at all. Again, there is lot of case law on that test.

Mr. HOLT. Now, to the definition, Ms. Walters and others have suggested that it might be very hard to come up with a definition. As I understand it, you are proposing, or you would propose, a definition that is similar to the ABC test that is applied in New Jersey.

Mr. SOCOLOW. Yes.

Mr. HOLT. That test, you say, has been used in various agencies, is now used uniformly across agencies. When you adopted it for these new applications, was there wrangling over the wording?

Mr. SOCOLOW. No, Congressman, not at all.

And I just want to point one thing out. Just because you use this test to define an independent contractor doesn't mean that other tests can't be elsewhere in those laws.

It was mentioned on page three of the U.S. Department of Labor's testimony that in certain of their statutes individuals performing work are covered even if they are classified as an independent contractor.

So you can do that. You can have all different definitions of who is covered, but still say, nonetheless, covered or not, this is what an independent contractor is. And, again, what that does is it provides ease of training of the auditors and investigators because they all know they are using the same test.

Mr. HOLT. Do you happen to know how close your language is to the language of other states? You mentioned that a number of states—I don't think you gave the number, and maybe you don't know the number—use a uniform test.

Mr. SOCOLOW. Well, Congressman, I don't know how many use the ABC test. I do know that many of the state unemployment insurance programs—I believe it is the vast majority of them—use the ABC test, with all three prongs being required, to distinguish whether someone is or is not an independent contractor.

Again, whether that has been adopted beyond unemployment insurance by those states, I don't know. I know that we have now done it beyond that.

Mr. HOLT. And the commonality of the language that you are familiar with, how close is that?

Mr. SOCOLOW. It is identical. That ABC test, you know, has essentially been codified almost identically in many, many state unemployment compensation programs.

Mr. HOLT. Well, I think you have made our decision here on a couple of these issues easier. Thank you.

Chairman ANDREWS [presiding]. Does the gentleman yield back his time?

Mr. HOLT. Yes.

Chairman ANDREWS. I want to thank all the witnesses today.

Mr. DeCamp, thank you for your contribution and for staying for the second panel. So we appreciate very much the fact that you stayed and listened. And we look forward to working with you further.

Mr. Williams, your story was compelling and well-told. And I think we have a shared consensus to prevent this from happening to other people in the future.

Ms. Stafford, it was refreshing to hear from someone who is actually running a business every day and dealing with these issues. And your contribution was quite notable.

Ms. Walters, your association has been a valued advisor to this committee for a long time. And we hope that continues to be the case.

And, Commissioner Socolow, we very much appreciate the fact that you brought some specific ideas as to how to fix this problem, as well as simply a description of it.

So we are very grateful to everyone who participated today.

As previously ordered, members will have 14 days to submit additional materials for the hearing record, without objection. And any member who wishes to submit follow-up questions in writing to the witnesses should coordinate with the majority staff within 14 days.

Without objection, the hearing is adjourned.

[The prepared statement of LIUNA, submitted by Mr. Andrews, follows:]

**Prepared Statement of the Laborers' International Union of North America
(LIUNA)**

The Laborers' International Union of North America (LIUNA) is submitting this statement on behalf of the 520,000 workers it represents who are employed in many of the industries which are particularly impacted by the misclassification of workers as independent contractors, including the construction industry.

LIUNA commends the Subcommittee for seeking solutions to the severe and "growing problem for the public and private sector" of worker misclassification which has now been conclusively established to have "direct and significant impacts on workers, employers, insurers, and tax revenue basis"¹.

The Growing Problem of Worker Misclassification

Worker misclassification is an important public policy issue with broad implications. Employers who play by the rules are put at a competitive disadvantage with companies that misclassify their employees. In cases of misclassification, employees are unable to access basic worker protections, such as unemployment insurance, social security benefits, overtime payments, and workplace injury benefits. Insurance companies are deprived of workers compensation premiums requiring legitimate employers to bear those costs. Law-abiding citizens bear the taxes of others as they are forced to make up for unscrupulous companies that evade their legal responsibilities.

The practice of worker misclassification occurs when employers label workers on their payrolls as independent contractors in order to illegally lower labor costs. An employer who misclassifies a worker as an independent contractor evades his obligation to withhold any pay to the federal government for income tax Social Security, Medicare and unemployment (FUTA) tax on behalf of that worker. In addition, the employer is evading similar requirements under state law, including the failure to pay workers compensation premiums on behalf of that worker and fringe benefits

to which the worker might be entitled if he or she were properly classified. Moreover, misclassification deprives workers of a wide variety of labor and employment protections, most particularly the right to receive minimum wages and overtime payments. The practice not only seriously harms workers, many of whom are low-wage and minority workers, but it constitutes tax and insurance fraud.

These and previous hearings have established the scope of severity of the problem.² The testimony presented thus far confirms the conclusions of a growing number of studies which establish the impact of independent contractor/worker misclassification abuse.³ Misclassification negatively impacts both the federal and state governments and all of our citizens in the following ways:

- *Impact upon workers*

Workers who are incorrectly classified as independent contractors lose the protection of a wide variety of labor and employment laws, including the overtime provisions of the Fair Labor Standards Act, Social Security, Unemployment Insurance and Workers Compensation.⁴

If misclassified workers need to apply for workers compensation or unemployment insurance benefits, they are denied those benefits. Workers who are misclassified rarely receive pensions. It is also well established that workers who are misclassified do not receive health insurance benefits at the same rate as properly classified workers. GAO Report at p. 14. The Illinois Study found that the “lack of health insurance coverage exacts a large toll on the uninsured—avoidable deaths, poorly managed chronic conditions, and underutilizes life-savings medical procedures.” Illinois Study at p. 11.

In addition, when workers are deprived of employer—provided health insurance or workers’ compensation coverage, taxpayers bear the economic costs of the uninsured and under-insured. Federal, state, and local governments support care of the uninsured through public clinics, and payments to health care facilities that care for the uninsured.

- *Impact upon fair, law-abiding employers*

The conditions for a fair and competitive marketplace are undermined because firms that misclassify workers illegally lower their labor costs as much as 30%. This places employers who play by the rules and properly classify their employees at a competitive disadvantage by shifting costs to them from the violating employers. Recent studies have documented the harm done to responsible honest employers by worker misclassification:

“[T]he conditions for a fair and competitive are sabotaged [by misclassification]. Firms that misclassify can bid for work without having to account for many normal payroll-related costs. This illegal practice can decrease payroll costs by as much as 15 to 30%. This places employers who correctly classify their employees at a distinct competitive disadvantage * * * [T]he violating employer will have been able to gain business illegally by exploiting their competitive advantage during the bidding process and they will have profited by avoiding other payroll related expenses * * * Employers can avoid the high cost of paying workers’ compensation premiums by mandating that persons who work for them have an exemption. This allows employers who misclassify to underbid the legitimate employers who provide coverage for their employees. In the construction sector, the workers’ compensation effect from misclassification further destroys the fairness and legitimacy of the bidding process.” The Economic Cost of Employee Misclassification in the State of Illinois, supra at note 1 at pp. 2-3.

- *Impact upon Federal and State Revenue*

Studies at the federal income level have established that “misclassification can reduce tax payments, Medicare payments, and Social Security payments. At the state level, misclassification can affect payments into state tax, workers’ compensation and unemployment insurance programs.” GAO Report at p. 8.

According to published data, income is reported on Form 1099’s at a 31% lower rate than that of income reported on Form W-2’s; as a result, both the federal and state governments suffer a loss of income tax revenue when employers misclassify workers, thereby pushing them out of wage-earner tax status. Illinois Study at p. 6. The studies have estimated that millions in federal and state income taxes are lost annually due to misclassification. For example, in Massachusetts, lost state tax revenues due to misclassification for all industries in 2001-2003 was \$91 to \$125 million.

- *Impact upon State Unemployment and Workers Compensation Systems*

State workers’ compensation and unemployment insurance systems are adversely affected as well. Businesses that misclassify employees as independent contractors

pay no unemployment insurance nor do they obtain workers' compensation coverage on those workers. Employers who correctly classify workers pay both federal tax under FUTA and state UI tax. In 2000, a federal DOL study found that nearly \$200 million in Unemployment Insurance tax revenue was lost per year through the 1990's due to misclassification of workers as independent contractors. In Illinois, for example, it is estimated "that the unemployment insurance system has lost an average of \$39.2 million annually from 2001-2005 in unemployment insurance taxes that are not levied on the payroll of misclassified workers as they should be. For 2005, [it is] estimate[d] that the unemployment insurance system in Illinois lost \$53.7 million in unemployment insurance taxes." Illinois Study at p. 6.

Misclassification is Endemic in the Construction Industry

Recent studies have confirmed that "the moderate rate of misclassification [of workers in all industries] was from 13-23%." In certain industries such as the construction industry, the rate of misclassification of workers is at the high end of the spectrum and it is safe to say that misclassification has become all but endemic in the construction industry: "In two states, Massachusetts and Maine, the incidence of misclassification in the construction industry is higher than all other industries in their states. For Massachusetts, the moderate statewide rate is 19%, while the rate of misclassification in the construction sector is 24%; * * * In a report by the General Accounting Office (1996), it was reported that the percentage of misclassified workers * * * in the construction sector was 20%. Illinois Report at p. 3.

Because the misclassification problem is especially severe in the construction industry, a growing number of states are using targeted industry enforcement as a way to most effectively utilize scarce governmental resources to focus on sectors where the practice is widespread.

For example, Illinois has recently enacted the Illinois Employee Classification Act of 2007 (HB 1735) which provides new remedies and penalties to address construction contractors who misclassify their workers. It gives new enforcement authority to the state Department of Labor and creates an Employee Classification Fund from penalties collected under the new law to provide for additional investigators. Important anti-retaliation procedures are included to protect workers who utilize the law's new remedies to file a complaint. The law specifically directs cooperative information sharing among Illinois' Labor, Employment Security, Workers Compensation and Revenue Agencies. Most important, the new law "presumes" employee status for an individual performing service for a construction contractor.

In his recent testimony before this Subcommittee, New Jersey's Labor Commissioner described targeted audits and investigations in 2006 in the construction industry which revealed that there were instances of misclassification in 41% of construction audits and investigations revealing \$78.2 million in under-reported wages in one year alone. Statement of New Jersey Commissioner of Labor David J. Socolow at p. 3.

Other states have focused their resources in the construction industry as well. For example, California's Labor Code 2819 creates a presumption of employee status in several industries including construction. New Mexico creates a presumption of employee status for workers in the construction industry as well. New Mexico Stat. 60-13-3.1.

The public construction contracting system is particularly undermined by independent contractor abuse because misclassification allows unfair contractors to sabotage the competitive bidding process by underbidding contractors who comply with the law. As a result, several states have specifically included misclassification violations as a basis for debarment from state construction contracts, including Massachusetts (Massachusetts Gen. Laws Ch. 149, section 14B (d)); Illinois (Illinois Employee Classification Act of 2007, HB 1735) and New Jersey (PL 2007, chapter 114).

New Policies and Practices to Address the Growing Problem of Worker Misclassification

New Policies and practices to address the growing problem of misclassification of workers as independent contractors should be considered in the following areas:

- *Close the Section 530 "Safe Harbor" Loophole*

Closing the so-called "safe harbor" loophole will allow the IRS to collect employment taxes from violating employers and to require the proper reclassification of workers in the future. Without closing this loophole, the impact of misclassification cannot be effectively addressed at the federal level and there is simply no credible justification for retaining this tax loophole.

- *Reevaluate Federal Law Regarding Presumptive Employee Status*

Impediments to joint agency enforcement which has worked successfully in many states will be removed if employee status is presumptively established under the IRC. This will allow scarce investigatory resources to be leveraged when relevant investigatory agencies begin at the same starting point of presumptive employee status. See GAO Report at pp. 25 & 33. For example, the New Jersey Commissioner of Labor identified the importance to his state's new enforcement measures of having "an individual paid for services [to be] presumed to be an employee." Statement of New Jersey Labor Commissioner at p. 5.

- *Strengthen Current Federal Enforcement Mechanisms and Penalties for Violators*

Additional penalties and remedies to deter employers who engage in misclassification should be considered. In this connection, innovative approaches in several states can provide guidance. For example, Illinois amended its code to make the classification of workers as independent contractors a separate statutory violation. Other states have separate reporting, licensing and registration requirements for independent contractors, including:

California <http://www.edd.ca.gov/taxrep/txicr.htm>;

Kansas <http://kdor.org/misclass/mcfaq.htm>;

And Montana <http://erd.dli.mt.gov/weregs/iccu.asp>.

The Subcommittee should consider whether the Department of Labor requires increased authority to investigate and remedy misclassification in addition to addressing its need for increased resources to initiate routine and targeted audits; an increased number of investigators to conduct field and job-site inspections and audits designed to uncover the misclassification of workers.

- *Promote Information Sharing Among Federal and State Agencies*

Procedures can be established to coordinate and promote federal agency sharing of information regarding the misclassification as well as procedures to strengthen and coordinate federal and state agency enforcement efforts. These efforts should include establishing interagency collaboration on worker misclassification enforcement among the Department of Labor, IRS and state workers compensation, unemployment security, labor and revenue agencies. See GAO Report at p. 33-34.

- *New Procedures for Targeted Investigations in Construction*

New procedures for targeted investigations, increased audit capacity and field inspections in industries such as construction should be established. This approach conserves resources and focuses limited staff on investigations which will expose endemic problems.

Conclusion

Worker misclassification reform will not only benefit workers, but also fair employers, insurers, taxpayers, and federal and state tax authorities. It will ensure fair and competitive markets and it will protect the integrity of the public works bidding process. LIUNA urges the Subcommittee to strongly consider new practices and policies as set forth above and presented by many witnesses which not only protect workers, but also promote the "administration of many federal and state programs, such as payment of federal taxes and pension benefits" harmed misclassification.⁵

ENDNOTES

¹The Economic Costs of Employee Misclassification in the State of Illinois, Michael P. Kelsay, PhD; James I. Sturgeon, Ph.D.; Kelly D. Pinkham, M.S.; Department of Economics, University of Missouri—Kansas City (December 6, 2006) (Illinois Study at p. 9 & 1"; see also The Cost of Worker Misclassification in New York State, Linda H. Donahue, James R. Lamare and Fred B. Kotler, Cornell University ILR School (February 2007); The Social and Economic Costs of Employee Misclassification in Construction, Elaine Bernard, PhD Robert Herrick, ScD, Francoise Carre, Ph.D.; Randall Wilson, University of Massachusetts, Boston; Construction Policy Research Center Labor & Work Life Program, Harvard Law School and Harvard School of Public Health, (December 17, 2004); The Social and Economic Costs of Employee Misclassification in the Maine Construction Industry, Elaine Bernard Ph.D., Robert Herrick, ScD, Francoise Carre, Ph.D. and Randall Wilson, University of Massachusetts, Boston Construction Policy Research Center Labor & Work Life Program, Harvard Law School and Harvard School of Public Health (April 25, 2005).

²Statement of Kelly D. Pinkham, University of Missouri-Kansas City, Assistant Director, Center for Full Employment, House Subcommittee on Income Security and Family Support, Hearing on the Effects of Misclassifying Workers as Independent Contractors, (May 8, 2007); see also House Workforce Protections Subcommittee Hearing on Providing Fairness to Workers Who Have Been Misclassified as Independent Contractors, (March 27, 2007).

³Supra at note 1.

⁴ Employment Arrangements: Improved Outreach Could Help Ensure Proper Worker Classification, US Government Accountability Office No. 06656 (July 11, 2006) (“GAO Report at pp. 21-22”).

⁵ GAO Report at p. 7.

[Additional statements submitted by Mr. Kline follow:]
 [Statement of the Associated Builders and Contractors, Inc., follows:]



July 24, 2007

The Honorable Robert Andrews
 Chairman
 House Committee on Education and
 Labor
 2181 Rayburn House Office Building
 Washington, D.C. 20515

The Honorable John Kline
 Ranking Member
 House Committee on Education and
 Labor
 2322A Rayburn House Office Building
 Washington, D.C. 20515

Dear Chairman Andrews and Ranking Member Kline:

On behalf of Associated Builders and Contractors (ABC) and its more than 24,000 merit shop contractors, subcontractors, materials suppliers, and related firms from across the country, we appreciate you for holding this hearing on “The Misclassification of Workers as Independent Contractors: What Policies and Practices Best Protect Workers.”

In construction, independent contractors are often the perfect answer to a pressing need for special skills and experience needed on short-term projects. The flexibility an independent contractor provides to a small, fledging operation as well as larger enterprises creates numerous advantages for all parties involved. The independent contractor has freedom to choose his or her work schedule, while the small business owner maintains the flexibility to adjust work demands with current business activity, and the consumer enjoys the benefit of a reasonably priced, quality product. Lawful utilization of independent contractors provides a good source of labor for projects where the contractor does not need to exercise the type of control that would necessitate the hiring of an employee.

While the construction industry provides significant opportunities for independent contractors, all parties must function under a confusing framework of rules that inadequately address the classification of workers as either employees or independent contractors. Initially, it is critical to distinguish between *wrongful* classification and misclassification. In construction, *wrongful* classification by a competitor can result in a competitive disadvantage to other contractors. Contrast this with misclassification, which can easily occur because current law and rules are extremely complex.

Those companies not paying employee taxes or worker compensation by *wrongful* classification can undercut the competition by offering lower bids. ABC in no way condones intentional misclassification by businesses that shirk their duties to society and their workers. We endorse a level playing field for all businesses and workers. For those workers who are faced with improper misclassification we believe they should be

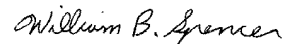
accorded every opportunity to have their financial situation corrected. Also employment agencies that do not properly pay workers should face severe enforcement.

Under current tax law, taxpayers use a 20-factor common law test that can be controversial and cumbersome because it is so subjective, leading to disputes between the IRS and businesses. Even if misclassification is unintentional the ramifications can be dramatic to both the worker and business owner in the form of back taxes, interest, applicable penalties, and even the possible disqualification of retirement plans.

Adding further confusion is that in addition to the IRS methodology for determining status a business owner may confront other methodologies for differing purposes. For example, the Common Law "Right to Control" test which is often used by courts to determine employee status in various types of cases, including employment discrimination and benefit cases, tax cases, and tort liability cases. And, the Department of Labor uses a model of analysis known as the "economic realities test" to determine coverage under, and compliance with, the minimum wage and overtime requirements of the Fair Labor Standards Act. Further many states have similar but not identical methods for state purposes.

Again, thank you for holding this hearing. Independent contractors play an integral role for the construction industry. They are also the seeds of many new small businesses in America. We look forward to working with you on this important issue.

Sincerely,



William Spencer
Vice President, Government Affairs

[Statement of Travis Boardman follows:]

Submission of Travis Boardman into the Record
Before the
Health, Employment, Labor and Pensions Subcommittee
And
Workforce Protections Subcommittee
Committee on Education and Labor
United States House of Representatives
Joint Hearing on
"The Misclassification of Workers as Independent Contractors:
What policies and Practices Best Protect Workers?"
July 24, 2007

Travis Boardman
FedEx Ground, Independent Contractor
30575 Heather Glen Drive
Salisbury, MD 21804

August 1, 2007

To Whom It May Concern:

The testimony of Robert Williams gave a distorted picture of my contractor dealings with FedEx Ground, and I'd like to share my views with you so that you have a better understanding.

First of all, virtually everything he said misses a single and important point: When people like me sign a contract with FedEx, I know exactly what I'm getting into concerning equipment needs, insurance, things like uniforms and scanners, which are needed to keep track of packages. All of these things are necessities that I was well aware of before I signed the contract. They are also tools to help be successful in running this business.

Trucks, insurance and maintenance of equipment are totally up to me to purchase or lease and I have 100 percent flexibility on where to get these. Contrary to his testimony, I determine where to get my trucks, where they are maintained, and which insurance companies I use. It's totally up to me to go on my own or use some services FedEx provides.

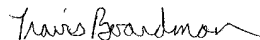
Other than the uniforms, scanner, and standard logos on the trucks, the only thing required of me is to service my area, which is what I agreed to do when I signed the contract. The harder I work, and the more packages I deliver, means a higher settlement check. It all comes down to getting out of this business what you are willing to put in. I've been a contractor since 1995 and it's worked out quite well for me. I have five people working for me, and I can tell you from experience, this kind of work isn't for everyone.

Being my own boss, which is what FedEx advertises, has given me the flexibility to develop my business and build it up to the point that I now get off work by most mornings about 10 am. So it really frustrates me when people like Mr. Williams stand up to complain, and his complaints are viewed as issues at FedEx. Just because some people have issues with their business, or fail at it, doesn't mean the whole system is bad. Something else that I have a very hard time with, is the fact that Mr. Williams worked as a temporary driver, and as a contractor for around two years, then leaves the business because of his accident, then comes back and contracts again with the company. This just doesn't make sense to me. Mr. Williams says the contractor agreement we sign isn't good, and the company has too much control over us. However, he got out of one contract after a couple of years, then returns and signs another contract with the same company. This totally amazes me.

I don't know why he left, but I know that it takes a lot of hard work to start up a business. Every driver will have a different story about their business, because no two businesses are the same, and no two people have the same work ethic and style. Over the years of running my business, the people that I have seen struggle, usually are not very business savvy. To me it all comes down to whether or not you are willing to put in the time necessary to develop your service areas, and get to know your customers and their needs.

The only thing FedEx wants is for us to service the areas that we agreed to in our operating agreement. FedEx wants us to succeed. If we don't succeed, then FedEx doesn't succeed either. That's why people like myself came to FedEx in the first place, and why, after 13 years, I'm still proud to do business with FedEx.

Sincerely,



[Statement of Randy Eystad follows:]

Submission of Randy Eystad into the Record

Before the

Health, Employment, Labor and Pensions Subcommittee

And

Workforce Protections Subcommittee

Committee on Education and Labor

United States House of Representatives

Joint Hearing on

**“The Misclassification of Workers as Independent Contractors:
What policies and Practices Best Protect Workers?”**

July 24, 2007

Randy Eystad letter –

I read over Mr. Williams testimony and it doesn't reflect at all my feelings or relationship with Federal Express. I like being a contractor and the flexibility it gives me to run a successful business.

Unlike other delivery companies, like UPS where they think Fed Ex has the advantage, we truly are running our independent businesses. I couldn't make as much money as I do if it weren't for FedEx.

Mr. Williams looks to me as having become unhappy after he came back to work from his accident and, obviously, he couldn't do the job. The things he complained about were all stipulations in the contract we all sign.

He's acting as though he's trapped by working with FedEx when it looks to me that he just couldn't get the job done. This is a hard business but if you run your operations well, know your territory and get the packages delivered it's a good business to be in.

Unlike his testimony about being forced to buy a new truck, that isn't the case at all. I have purchased used trucks and they work just fine. Too many of the guys come in and buy new trucks and expensive equipment. You don't need to do that.

I just get irritated when I hear such things. Nobody forced me to sign a contract with Fed Ex and nobody forces you to stay there if it doesn't work out. But where else are you going to go to have the name recognition like with Fed Ex?

Like I've said, this is a hard business but Fed Ex does everything possible to help you out. That's why I wanted to do business with them and it's been very good to me.



[Statement of Michael P. Mannion follows:]

Submission of Michael P. Mannion Operations into the Record

Before the

Health, Employment, Labor and Pensions Subcommittee

And

Workforce Protections Subcommittee

Committee on Education and Labor

United States House of Representatives

Joint Hearing on

**“The Misclassification of Workers as Independent Contractors:
What policies and Practices Best Protect Workers?”**

July 24, 2007

FedEx Ground provides this supplemental statement for the official record of the Joint Hearing by the Health, Employment, Labor and Pensions Subcommittee and the Workforce Protections Subcommittee of July 24, 2007.

Through its predecessor company, FedEx Ground has had a long-established and mutually successful working relationship with independent contractors for more than 20 years. Simply put, we enter into contracts with local entrepreneurs who want the flexibility to run their own business delivering packages for us. It is an open and transparent relationship, and it is a win-win-win arrangement for our local business partners, our company and our mutual customers.

Indeed, when FedEx acquired Roadway Package System (RPS) in 1998, the parcel company's independent contractor model was well-established. And over the years, we've continued to refine and improve this model. FedEx Ground has grown dramatically in the intervening years, due in large part to the entrepreneurial spirit and customer-focused dedication demonstrated every day by a network of nationwide contractors and their employees.

In his July 24, 2007, remarks before this Joint Subcommittee, former independent contractor Robert V. Williams provided testimony that was fundamentally inaccurate and misleading. His contention that he was “mischaracterized” as an employee, after he voluntarily and purposefully pursued independent contractor relationships with FedEx Ground, is false. When an independent contractor route became available with FedEx

2

Ground, Williams purposefully pursued it as a business owner – not as an employee. And he was not treated as an employee.

Williams' own testimony contradicts his allegations. Williams confirmed that he answered an advertisement in a local paper to *"Run your own business. Become a business owner with a national leader. Be your own boss."* As an astute business man with 45 years of experience in owning consulting companies and other businesses, he certainly recognized the difference between *"a business owner"* and somebody's employee.

For example, as an independent contractor Williams was never required to personally drive his trucks or deliver any packages - he could have hired his own employees to drive for him, as many other FedEx Ground contractors have. Williams also had the flexibility to trade packages with other contractors, and had the ability to determine his own schedule, and the schedule of any replacement drivers or other employees he might have had. No true "employee" of any company has this kind of unilateral control and flexibility.

Moreover, independent contractors can buy and sell their routes, and hundreds have grown their operations into significant businesses by securing multiple routes and realizing efficiencies. For some entrepreneurs, their FedEx Ground route is only one in a series of local businesses that they operate in their community.

Today, more than 15,000 independent business owners are succeeding and growing their businesses in partnership with FedEx Ground. Contractors' annual income often ranges from \$80,000 to \$120,000, with hundreds of business people grossing \$250,000 a year or more.

For Williams, it was this entrepreneurial opportunity that he seemed to want when he not once, but twice, signed contract agreements to be an independent contractor with FedEx Ground. In his self-described long career as an independent business owner and consultant, Williams fully understood not only the upside potential, but the responsibilities of a small business owner before signing these contracts. These are the same responsibilities that business owners across America embrace as part of doing business.

This was an emphatic point that Williams confirmed repeatedly in his own testimony: *"I was responsible for the cost of the vehicle, for the fuel, for the tires, for the maintenance, and all operating costs, including breakdown and emergency expenditures."* Williams further testified that, as with other business owners in America: *"I paid for a worker's accident policy, in lieu of Workmen's Comp weekly deductions and I also paid weekly for liability insurance from Protective Insurance."* Williams also confirmed in his testimony that, as with every other business owner: *"I was responsible for reporting my income to federal and state tax authorities."*

3

Indeed, as he clearly testified, Williams ran his own business operation. As any other business owner, this meant that he had to ensure that his customers got dependable service every day, whether he did it himself or through his employees. This was an honor-bound commitment to his customers and a simple stipulation in his contract with us. In this regard, Williams failed to deliver the high quality of customer care agreed to in his contract. Although he stated repeatedly during his testimony that *"I was responsible,"* Williams now wants to blame others for his business failures.

What's even more tragic -- and a more important policy matter for this Joint Subcommittee's consideration -- is that Mr. Williams admits that he purposefully pursued the opportunity to *"run your own business, become a business owner . . . be your own boss,"* and now he wants to take that right away from others.

The entrepreneurial business model is at the foundation of America's economic success. It is the spirit of the American dream itself. It means that anyone and anybody has the ability to create their own company and determine their own financial success. Taking away this type of opportunity would mean that many entrepreneurial-minded individuals in America would only have the option of being someone else's employee. When one considers how many of today's local businesses started out as small companies run by independent contractors, it's quite amazing.

For FedEx Ground, our relationship with independent business owners is an honest partnership in each other's success. It also is an open partnership in which each participant shares certain responsibilities, and each has the opportunity to benefit in our mutual success.

In closing, and addressing the title given to this hearing, we would like to reiterate a point that Williams failed to mention: that every one of our independent business partners purposefully pursued their opportunities with FedEx Ground -- no one "misclassified" them, as some have alleged. These business entrepreneurs were -- and are today -- actively seeking partnership with successful companies such as FedEx Ground. If such people wanted to be someone else's employee, there are thousands of job postings listed everyday in newspapers and on the Internet.

Instead, our business partners sought us out because of the opportunity to partner with a company such as ours, and because they could pursue the opportunity to *"Run their own business. Become their own business owner. Be their own boss."* And we give them that opportunity everyday.

We appreciate your consideration of these facts.

Respectfully submitted,

Mike Mannion, SVP Operations
FedEx Ground
Pittsburgh, Pennsylvania

[Statement of the National Association of Home Builders follows:]

Statement from the
National Association of Home Builders

For the
Committee on Education and Labor
Subcommittee on Health, Employment, Labor, and Pensions
Subcommittee on Workforce Protections

on

*"The Misclassification of Workers as Independent Contractors: What Policies and Practices Best
Protect Workers?"*

Tuesday, July 24, 2007

Introduction

The 235,000 members of the National Association of Home Builders (NAHB) appreciate the opportunity to submit this statement for the Committee on Education and Labor, Subcommittee on Health, Employment, Labor, and Pensions and the Subcommittee on Workforce Protections regarding the issue of misclassifying workers as independent contractors. This issue is of great importance to the home building industry, which thrives on the efficiency and entrepreneurship that comes from both home builders and their workers being able to freely choose the form of their business relationship. At the same time, entrepreneurship only succeeds when all participants in the market play by the same rules and one entity cannot have an unfair advantage over others. NAHB supports enforcement of the current rules on the classification of workers, but would also support clarification of those rules to improve compliance across all industries.

This statement focuses on the economics surrounding the decision by home builders to contract with independent contractors as well as the motivations for employees to act as independent contractors. Further, it examines present law rules for the classification of workers and how they ensure a fair and equal marketplace for business. Finally, the statement identifies some potential enhancements to the current law that could improve compliance.

Economics of Independent Contracting

There are important business-related reasons why a home builder would want to use an independent contractor as part of a home construction project. Economic theory dictates that firms employ labor in-house only when the costs of doing so are less than the cost of contracting with another firm. In general, labor costs are lower for businesses that specialize in a particular activity compared to a business that attempts to do all tasks in-house. Consequently, it may be more efficient to contract with a business consisting of dedicated specialists than housing a single or few employees within the firm. This effect is also known as economies of scale and is likely to occur in industries associated with large fixed costs, low marginal costs and learning-by-doing, such as residential construction or the technology sector.

In addition to certain professional duties, such as management and administration, home building requires a large number of specialized tasks. The Census identifies some of these roles, including but by no means limited to: construction supervisor, brick mason, carpenter, flooring contractor, cement worker, general laborer, pile driver, engineer, drywaller, electrician, glazier, insulation contractor, painter, paperhanger, pipe plumber, plaster contractor, rebar worker, roofer, metalworker, quality inspector, fence, hazmat removal contractor, and septic and sewer specialist.

For a small home builder, who may only construct a few homes a year, there is not sufficient internal demand to justify hiring an employee for each of these specialized roles. For example, the total internal demand for an electrician may only be for one-half of a position per year. Consequently, it makes more economic sense to contract with an electrician who acts as an independent contractor. This contractor will likely own his own equipment, provide for his own training, and contract with other businesses. He may also employ his own staff. Therefore,

working with an independent contractor has the potential for significant efficiency gains. Proposals that would artificially alter the decision between hiring an employee and working with an independent contractor would increase overall construction costs and therefore result in higher prices for home buyers.

Furthermore, there are advantages for specialty trade workers to adopt independent contractor status. Data from the Census Bureau's Survey of Population demonstrates that independent contractors in the construction industry tend to be higher skilled than their employed counterparts. Not surprisingly given the demand issue discussed above, self-employed construction trades workers are more common in rural areas and smaller cities, where home building occurs at a smaller scale. Finally, independent contractor status affords the opportunity of growth and expansion, whereby a successful contractor hires his own staff to meet the increasing needs of his business. Indeed, many contracting business begin operation as a self-employed independent trade worker.¹

The result of the economic setting described above is a vibrant subcontractor market within the residential construction industry. NAHB survey data indicate that 80% of home builders subcontract at least three-quarters of their total work. The average home builder uses 24 subcontractors for the construction of a single-family home. For example, 53% of home builders subcontract their sales operations.²

Present Law Rules

The prevailing tax and regulatory system reflects the economic importance of allowing businesses to determine how services are provided. Under present law, the determination of whether a specialist is an independent contractor or an employee is made by a facts and circumstances evaluation. This evaluation examines the nature of the work completed, the means and control of the work, and the circumstances under which the work is performed, among other factors. Internal Revenue Service Ruling 87-41 provides 20 such factors that may be considered in performing this evaluation. These factors include training, payment by job/time status, tool/material provision, and whether the specialist works for more than one business. Further, Section 530 of the Revenue Act of 1978 allows a business to treat a worker as an independent contractor if the IRS or past industry practice has accorded such status to similar workers in the past. Section 530 is an important policy tool for ensuring that inappropriate tax policy considerations do not interfere with efficient market operation and established business practice.

NAHB supports enforcement of these present law rules. Businesses or individuals that are in violation of these rules, either through wrongful misclassification of workers or through failure to pay taxes in full, can achieve an unfair competitive advantage in the marketplace. This hurts law abiding businesses and individuals in the industry.

¹ For more information, consult "Construction Workers: Settling In." Michael Carliner. Housing Economics, October 2003; and "Self Employment in Construction." Elliot Eisenberg. Housing Economics, January, 2001.
² Builders' Economics Council Survey: Special Analysis. May 2005.

Policy Recommendations

Nonetheless, the present law system is complex and potentially confusing. In some cases, misclassification of employees can occur due to unfamiliarity with the rules. This is due in part to the nature of the facts and circumstances test that is available to businesses.

Section 530 is useful because it establishes a safe harbor, thereby providing certainty to potential employers. NAHB recommends that compliance in this area could be improved by establishing additional safe harbors for common scenarios involving subcontractors that provide specialized services to businesses. Further, additional education efforts by the appropriate tax authorities concerning the benefits and responsibilities of being an independent contractor would be helpful. This would be useful for individuals who are new to the experience of being a subcontractor, and thus would prevent surprises concerning tax treatment at the end of the year.

However, NAHB opposes any attempt to legislate the particular circumstances under which professionals must be defined as employees or independent contractors. Such efforts would be damaging to the marketplace, particularly as they would be driven by tax policy considerations and not the economics of the marketplace. Furthermore, such policies would be complex and administratively difficult to enforce. Consider the example of a specialist who theoretically would be required by statute to be classified as an employee, despite the fact that the specialist may work for several employers in a given year. Each employer would be required to withhold payroll taxes for FICA purposes, but no accounting could be made for withholding made by other employers. This would create an administratively difficult task to resolve for both the IRS and the employers, which would result in higher business costs and cash flow challenges. Indeed, this example illustrates one of the merits of the existing system.

NAHB also opposes any legislative effort to make general contractors liable for the legal and regulatory compliance of their subcontractors in areas such as verifying employee work authorization. Over the past couple of years, immigration reform efforts have turned frequently to the idea of holding employers accountable for the legal status of all of their subcontractors', or independent contractors', employees. NAHB believes it is fundamentally unfair to hold any U.S. employer accountable for the legal status of employees whom they do not have the power to hire, or to fire, and whom—in many instances—the employer will never even meet. Further, privacy laws and anti-discrimination laws preclude employers from being able to investigate the employees of their subcontractors, making efforts to hold them liable for those employees all the more unreasonable. We support holding all employers responsible for the legal status of their own, direct employees.

As a general principle, NAHB opposes tax proposals and policies that impose increased administrative burdens on businesses that play by the rules. For example, increasing information reporting requirements beyond present law rules would increase paperwork burdens on business, and small business in particular. Indeed, such small businesses are those firms that, due to the economics of utilizing specialists, rely on independent contractors the most and thus would shoulder the largest burden from increased paperwork requirements.

Conclusion

The classification of workers as either employees or independent contractors is important for all small businesses, but it is especially so for home builders. NAHB supports maintaining the efficiency and flexibility of the marketplace by continuing to allow employers to classify their workers as independent contractors, as merited. At the same time, we support enforcement of present law to ensure a level playing field for all small businesses. NAHB looks forward to working with the Committee and the Congress to achieve both of these goals.

[Statement of William Vazquez follows:]

Submission of William Vazquez into the Record
Before the
Health, Employment, Labor and Pensions Subcommittee
And
Workforce Protections Subcommittee
Committee on Education and Labor
United States House of Representatives
Joint Hearing on
"The Misclassification of Workers as Independent Contractors:
What policies and Practices Best Protect Workers?"
July 24, 2007

My name is William Vazquez and I am the owner of Vazquez Transportation, Inc., and do business as an independent contractor with FedEx Ground. It has been a great relationship to partner with such a large company.

I have read the testimony of Williams and think that some of what he said is true and some of the stuff is BS. At the beginning of his statement that part is pretty true and is the normal or routine of how we do business. That's how most people get in starting off as temporary driver contractors but what he said at the end was really stretching things a bit.

There are no restrictions I know of like he said he had to do all those things because that's what Fed Ex told him. Basically what we're actually told is to pick up the packages and deliver the packages. That's our livelihood and that's the contract agreement we sign to deliver the packages.

I've never had or heard of terminal problems like he said. At my terminal the manager will go above and beyond to help us cover a route by even calling other terminals. They do everything they can to help us because it's just good business sense to me.

We're not employees and I come and go as I please and no one tells me what to do. It's not complicated at all. You sign a contract to deliver packages and having your vehicle up to DOT standards. Other than that you report to work at no specific time and deliver your packages. That's pretty basic.

I got both of my trucks on my own but the first truck I did get from FedEx because I was just starting out and it was a good deal. But my second and third trucks I just got on my

own. That just made good business sense for me to get the equipment I needed to run my own business.

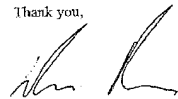
I've got two employes and currently have two routes that my company services. I had a third area but recently sold it while I'm looking to start business in a new area.

I use a payroll to pay my guys. I run my own company and am an independent contractor with the ability to grow my company and business. I am not an employee and never want to be one.

I have no issues with Fed Ex and most of the guys I know have no issues either. After all, we know what we're getting into. It's black and white and we sign the contract to deliver the packages. It's as simple as that.

I would like to share with you that I've been my own boss now for a little over two years and think the opportunities I've had with FedEx will just continue to grow for my business.

Thank you,

A handwritten signature in black ink, appearing to be the name 'John L.' written in a cursive style.

[Whereupon, at 12:56 p.m., the subcommittees were adjourned.]

