

# MISCLASSIFICATION OF EMPLOYEES

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Testimony before the Oregon House Interim Committee on Business and  
Labor

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# Agenda

- What is “misclassification” and who does it affect?
- What are the consequences of being misclassified for workers?
- What are the cost of misclassification to the government and the economy?
- How can we respond to the problem?

# What is misclassification (payroll fraud)?

When employees have been misclassified in one of the following ways:

- Employers treat employees as “independent contractors,” even when workers are not running their own businesses;
- Employers require employees to form a limited liability corporation or franchise company-of-one as a condition of getting a job;
- Employers pay employees off the books, without any payroll treatment at all.

# Who does misclassification affect?



# Who does misclassification affect?

- 78% of TNC drivers in CA are Black, Latinx, Asian or multi-racial and 56% are immigrants
- Latinx workers make up 30% in construction industry nationwide (17% of population)
- Black workers make up 22% in transportation & warehousing nationwide (12% of population)

US Bureau of Labor Statics, "2019 Labor Force Statistics from the Current Population Survey,"  
<https://www.bls.gov/cps/cpsaat18.htm>

# When is someone an employee?

- Under ORS Chapter 652 and 653, we look at the “economic realities”:
  - Does the company have the right to control the work?
  - Does the worker have an opportunity for profit or loss based on a capital investment in the business?
  - Does the work require specialized skill and independent initiative?
  - Is the worker an integral part of the business?
- Under ORS 670.600, someone is an independent contractor, and not entitled to some employee protections/benefits, if they are:
  - Free from direction and control over the means and manner of providing the services;
  - Customarily engaged in an independently established business;
  - Is responsible for obtaining other licenses or certificates necessary to provide the services.

# What are the consequences of being an independent contractor?

- No minimum wage and overtime protections
- No workers' compensation insurance
- No sick leave or medical leave rights
- No unemployment insurance (except for in the case of pandemic)
- No anti-discrimination or harassment protections
- No right to form a union or collectively improve working conditions
- No employer-provided retirement benefits

# What are the costs of being an independent contractor to the worker?

- Worker pays entire 15.3% of federal self-employment rate, instead of splitting with employer.
- Worker must pay for insurance or the cost of any workplace injury.
- Worker is responsible for operating costs, such as gas, tools, etc.

One government expert calculated that a construction worker earning \$31,200 a year before taxes would be left with an annual net compensation of \$10,660.80 if paid as an independent contractor, compared to \$21,885.20 if paid properly as an employee.

NELP Fact Sheet "Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries," <https://www.nelp.org/publication/independent-contractor-misclassification-imposes-huge-costs-on-workers-and-federal-and-state-treasuries-update-2017/>



# What are the costs of misclassification to Oregon?

## Interagency Compliance Network in 2018:

- 14 Joint OED-DOR Audits completed in 2018
  - 6,986 misclassified workers identified
  - \$73,057,510 in unreported payroll discovered in audits
  - \$1,821,070 assessed in lost UI payroll taxes
- 1,433 OED audits completed in 2018
  - 3,429 misclassified workers identified
  - \$27,533,624 in unreported payroll discovered in audits
  - \$598,274 assessed in lost UI payroll taxes

Source: Interagency Compliance Network Report to Oregon Legislature, March 2019

[https://www.oregonlegislature.gov/citizen\\_engagement/Reports/2019-ICN-Interagency-Compliance-Network-Report.pdf](https://www.oregonlegislature.gov/citizen_engagement/Reports/2019-ICN-Interagency-Compliance-Network-Report.pdf)

# What are the costs of misclassification to Oregon?

2019 Report to Legislature by Interagency Compliance Network:

- 2,175 DOR investigations completed in 2018
  - \$58,285,541 in unreported payroll discovered in audits
  - \$4,228,193 in additional payments
- DCBS completed 14,006 investigations in 2018
  - 452 Orders Issued
  - \$8,238,235 in penalties assessed
- Unpaid workers' compensation premiums lead to delayed medical care, claims out of public funds, and potentially additional strain on public health resources

Source: Interagency Compliance Network Report to Oregon Legislature, March 2019

[https://www.oregonlegislature.gov/citizen\\_engagement/Reports/2019-ICN-Interagency-Compliance-Network-Report.pdf](https://www.oregonlegislature.gov/citizen_engagement/Reports/2019-ICN-Interagency-Compliance-Network-Report.pdf)

# What are the costs of misclassification to the federal government?

- A 2000 study commissioned by the U.S. Department of Labor (USDOL) found that **between 10 and 30 percent** of audited employers misclassified workers.
- Researchers found that misclassifying just 1 percent of workers as independent contractors annually results in a \$198 million hit to unemployment insurance trust funds.

NELP Fact Sheet "Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries," <https://www.nelp.org/publication/independent-contractor-misclassification-imposes-huge-costs-on-workers-and-federal-and-state-treasuries-update-2017/>

# What are the costs to high road employers?

- Competitors have an unfair business advantage by benefiting from artificially low labor costs.
- Unemployment insurance and workers' compensation costs become inflated because of "free riders."
- Race-to-the-bottom pushes compliant employers out of business, while low-road employers gamble on lack of private and public enforcement.

# Standard test would help protect workers

- One Oregon test of for the definition of who is and is not an employee would help enforcement and employer compliance.
- Use of historical “economic realities” definition would avoid rolling back protections for workers.
- Presumption of employee status for those performing labor or service for a fee would be harder to manipulate.
- Preventing industry carve outs protects workers and tangential or similar industries.

# Steps to Sufficient Enforcement

- Strong protection against retaliation.
- Deterrent measures through enforcing penalties.
- Public/private enforcement:
  - Adequately fund public enforcement;
  - Attorneys' fees to prevailing plaintiffs, and no prevailing party awards to defendants;
  - Community partnerships (Seattle, San Francisco, LA);
  - Guaranteed collection (wage liens in Wisconsin, wage bonds in California).
- Include independent contractors into labor standards and benefits (PFMLI is an example)



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