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MEMORANDUM

To: Legislative Joint Fiscal Committee – Rep. Michael Obuchowski, Chair
From: Bryan Bouchard – Vermont Building & Construction Trades Council
Date: August 18, 2009
Re: Comments on FY2010 Budget Rescission Proposal, Sec. B4.00

- There's no doubt that these are tough times for everyone in Vermont. We understand that it's time for hard decisions; we're all making them already.
- You as a committee are looking for savings across state government, which is why it was very surprising to find a revenue-producing position on the chopping block.
- According to the rescission proposal, Section B.400, the Department of Labor is planning to not fill one for four new authorized investigator positions. These new positions were added to combat misclassification fraud across the state.
- Many on this committee will remember the detailed testimony about misclassification fraud in Vermont and across the United States.
- There is a pervasive problem in many sectors of the economy, including construction, package delivery, etc, where fraudulent employers will call their employees "independent contractors" and thus fail to pay appropriate payroll taxes, unemployment insurance contributions, and workers' compensation insurance premiums.
- This kind of cheating undercuts law-abiding employers, denies workplace protections to workers, increases everyone's cost of doing business, and deprives the state of revenue.
- The motivation for this fraud is obvious: misclassification can save employers upwards of 30 percent on payroll costs. But that savings for cheating employers and their clients are actually costs borne by law-abiding businesses, misclassified employees, and the Vermont taxpayers.
- In a presentation to the Labor Advisory Council last fall, the Vermont Department of Labor reported that 14% of the businesses selected for unemployment insurance verification audits over four quarters did not report one or more workers for unemployment coverage who should have been covered. The Department also reported that during the first 9 months of 2008, the department conducted 258 additional audits, and 40% of those audits found misclassified workers.



Just last week, the Workers' Compensation Task Force heard testimony from the contractor members of the Homebuilders & Remodelers Association in which they estimated seeing misclassification on 50-60% of projects!

Numerous studies have been performed across the country. These estimate hundreds of millions of dollars in unpaid unemployment taxes, workers' compensation premiums, and payroll taxes.

Several states' governors have signed executive orders creating inter-agency task forces to study the magnitude of the problem and coordinate and strengthen enforcement actions.

These enforcement actions proven what studies have indicated: For example, in four months, the New York misclassification taskforce found \$19.4 million in unreported wages, 2,078 misclassified workers, and assessed \$1.4 million in unemployment taxes, penalties and interest. They found 646 employees were owed \$3 million in wages.

Vermont took a good step forward in creating these four enforcement positions at the Department of Labor. It's a shame to eliminate 25% of the added capacity to combat an activity that costs the state and its businesses and worker so much money every year.

Numerous new investigator positions were also added to the Department of Taxes. We think it might make more sense to not fill one of the tax department slots given that the DOL investigators will sweep in state revenues as well as UI, Workers' Comp. etc. If the DOL position cannot be fully restored, perhaps a ½-time position for DOL and ½ for Tax would be workable.

We hope the committee will see the real value of more investigators to everyone's bottom line.

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HBJ SPECIAL REPORT

State Lags In Enforcement Resources

By Diane Weaver Dunne

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Today

A team of five Connecticut labor department employees issued 220 stop-work orders during the past 22 months in their efforts to stop employee misclassification and "under-the-table" cash payments. That's nearly 200 more stop-work orders than the number issued by New York and Massachusetts.

However, the state lags significantly behind in the collection of back taxes compared with neighboring states that have developed a comprehensive, multi-agency approach to tackling the problem.

New York has taken the lead in the Northeast in its battle against the underground economy, establishing its task force in September 2007. It has identified more than \$4.8 million in unpaid unemployment taxes, issued more than \$1 million in unemployment insurance fraud penalties, and issued more than \$1.1 million in workers' compensation fines and penalties. The task force also discovered more than \$12 million in unpaid wages.

Notably, New York's crackdown included just 27 stop-work orders. But it collects much more in fines and back taxes because each order triggers additional action not generally taken in Connecticut.

Key to New York's success was coordinated enforcement sweeps, coordinated assignments and systematic referrals and data sharing between 15 state agencies.

Massachusetts, which modeled its task force after New York's, reported in June that it had "recovered" \$1.4 million in fines, unpaid wages and tax assessments within its first 12 months. Its collection of fines associated with workers' compensation was \$24,750, less than a third of the \$90,000 collected by Connecticut. However, Massachusetts collected about \$238,000 in unpaid taxes.

Although Connecticut's labor department makes referrals to the appropriate federal and state agencies when stop-work orders are issued, the state is not tracking tax collections related to worker misclassification enforcement efforts. Tax collection is the responsibility of the state's Department of Revenue.

Unlike Massachusetts and New York, Connecticut hasn't adopted a multi-agency



Stop-work orders were issued at the KBE Building Corp. construction site at 320 Universal Drive, North Haven in late June.

enforcement task force. But lawmakers did pass a law that became effective July 2008 that authorized the establishment of a Workers Misclassification Advisory Board — all volunteer — to be comprised of five state agencies and various construction management and labor representatives.

Connecticut's board met once, on Jan. 16.

In February, Gov. M. Jodi Rell proposed that the Employee Misclassification Advisory Board — along with 70 state boards and commissions — be eliminated. Rell's office did not return a request for comment as of press time.

Donald Shubert, president of the Connecticut Construction Industries Association, was appointed to the board and attended its first and only meeting. Shubert said that Chief State's Attorney Kevin Kane, who heads the state's workers' compensation fraud bureau, Attorney General Richard Blumenthal and labor department Commissioner Patricia Mayfield were very engaged during the meeting.

Unclear as to why the board has not met again, he said his organization considers enforcement very important. And while his organization applauds and respects the job that the state's labor department is doing with very limited resources, more enforcement is needed, he said.

"This is an investment in state government that more than pays for itself in more than one way," said Shubert. "We would strongly encourage Connecticut to follow [Massachusetts' and New York's'] lead."

To Massachusetts, its task force has been well worth it. "This is really found money," said George Noel, director of labor in Massachusetts, who referred to its recovery of more than \$1 million during its first year starting up.

And there's more money that could be found, according to numerous studies. Economist William Alpert, a University of Connecticut professor, estimates that the state could be losing up to \$1.5 billion in state income tax revenue alone from employee misclassification and workers being paid off the books.

"I feel that what we are working with, we have really started to make an impact. We are a unit of five, but that is not only what we do," said Resa Spaziani, a DOL supervisor who heads the state's stop-work order efforts. She noted that some of the five involved with stop-work orders also have caseloads of 150 to 200 pertaining to other matters.

Prior to launching its task force, Massachusetts dedicated about 11 labor department employees part time on workers misclassification and off-the-books enforcement. That number grew to 122 state employees when the task force was established.

George Noel, director of the Massachusetts Department of Labor, said the key to its enforcement success is its collaboration. "We break down the silos, work with each other."

The task force developed a shared database where complaints are input. It also developed a check list that helps the members readily identify which tax laws, labor

license regulations, and other laws may be violated, he said.

The Massachusetts collaboration has revealed that businesses not complying with one labor law are likely to violate other labor laws as well, Noel said.

The task force's most powerful compliance tool is its threat to pull a state-issued license, which allows the task force to leverage its power over compliance with other state agencies pretty quickly, he added.

The fines and penalties also increase substantially when multi-agency regulations are considered, he added. Some businesses make a conscious business decision to not comply with labor laws and consider the risk of getting caught and paying one fine simply the cost of doing business.

"But when you have to pay back unemployment taxes, income taxes, all kinds of back taxes, it increases the price of poker," Noel added.

Other states — Vermont, Maine, and New Hampshire — are looking at same model, Noel said, and will come together for a conference in October in Holyoke, Mass.

Send A Comment to the Hartford Business Journal