

# HOUSE BILL REPORT

## HB 1519

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### As Reported by House Committee On: Labor

**Title:** An act relating to simplifying and enforcing employee status under employment laws to ensure fairness to employers and employees and address the underground economy.

**Brief Description:** Simplifying and enforcing employee status under employment laws to ensure fairness to employers and employees and address the underground economy.

**Sponsors:** Representatives Riccelli, Reykdal, Robinson, Takko, Walkinshaw, McBride, Sells, Peterson, Fitzgibbon, Goodman, Ryu, Pollet, Pettigrew, Moscoso, Ormsby, Cody, Dunshee, Tharinger, Kagi, Lytton, Moeller, Stanford, Hudgins, Orwall, Van De Wege, Bergquist, Santos and Farrell.

#### **Brief History:**

##### **Committee Activity:**

Labor: 1/27/15, 2/3/15 [DP].

#### **Brief Summary of Bill**

- Creates the Employee Fair Classification Act, which prohibits misclassification of employees as independent contractors and creates remedies, including civil penalties and damages.
- Defines "independent contractor" for purposes of the Employee Fair Classification Act and establishes the same definition for purposes of the Minimum Wage Act, unemployment insurance, industrial insurance, and other employment laws.

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### HOUSE COMMITTEE ON LABOR

**Majority Report:** Do pass. Signed by 4 members: Representatives Sells, Chair; Gregerson, Vice Chair; Moeller and Ormsby.

**Minority Report:** Do not pass. Signed by 3 members: Representatives Manweller, Ranking Minority Member; G. Hunt, Assistant Ranking Minority Member; McCabe.

**Staff:** Joan Elgee (786-7106).

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

## **Background:**

Employment standards and benefits generally apply only if an employer-employee relationship exists rather than an independent contractor relationship. Various multi-part tests are used to determine whether an individual is an independent contractor. For purposes of prevailing wage, industrial insurance, and unemployment insurance, a six-part statutory independent contractor test is applied. This test requires that:

1. The individual has been and will be free from direction and control, both under the contract and in fact.
2. The individual's services are outside the usual course of business for which the service is performed, or outside all the places of business, or the individual must pay the costs of the principal place of business where the services are performed.
3. The individual has an independently established business, or a principal place of business that qualifies for an Internal Revenue Service (IRS) deduction.
4. The individual is responsible for filing a schedule of expenses with the IRS.
5. The individual has a separate set of books and records that reflect all items of income and expenses.
6. The individual has an active and valid registration with the Department of Revenue, has a unified business identifier number, and has any other required state accounts for the payment of taxes.

In the construction industry, a seventh required element is that the individual be registered as a contractor or licensed as an electrical contractor. For industrial insurance, a threshold question is whether a person under contract brings more than their personal labor to the job and for unemployment insurance, persons outside construction may also be independent contractors under an alternative three-part test.

For purposes of the Minimum Wage Act, which also addresses overtime, a common law economic dependence test applies. The inquiry under this test is whether the worker is economically dependent on the alleged employer or is instead in business for himself or herself. Other wage laws also do not have statutory tests. These include the Wage Payment Act, which provides for an administrative or court action to collect wages under the Minimum Wage Act and other wage laws, as well as establishes other requirements. Other laws address deductions from wages and otherwise address failure to pay wages.

If an employer treats a worker as an independent contractor rather than as an employee, the employer may be liable under the various employment laws. Some employment laws address the liability of general contractors for violations of a subcontractor. For example, for purposes of unemployment insurance and industrial insurance, a general construction contractor is not liable for a subcontractor's taxes under certain circumstances.

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## **Summary of Bill:**

Employee Fair Classification Act. The Employee Fair Classification Act (EFCA) is enacted.

Prohibitions and Requirements. Certain actions by employers and other persons are prohibited. These are:

- willfully misclassifying an employee as an independent contractor. "Misclassification" is designating an employee as a nonemployee. "Willful" is a knowing and intentional action that is not accidental or the result of a bona fide dispute;
- charging a misclassified employee a fee or making unlawful deductions from compensation;
- requiring or requesting an employee to agree to or sign a document that results in misclassification;
- forming, assisting in, or inducing the formation of a business entity or paying or collecting a fee for the use of a business entity, or the purpose of facilitating or evading detection of a violation of the EFCA; and
- conspiring with, aiding and abetting, assisting, or advising an employer (for remuneration) with the intent of violating the EFCA.

Employers who engage independent contractors must post a notice stating that a worker has a right to be classified as an employee if the worker does not meet independent contractor requirements, and that a complaint may be filed with the Department of Labor and Industries (Department) or in court if a person believes misclassification has occurred. The notice must be in English, Spanish, and any other language primarily spoken by the majority of the workforce.

Bona fide independent contractors, commissioned outside salespeople, individuals employed on a casual and sporadic basis, and volunteers are not employees under the EFCA.

Employer-Employee Relationship. An employer-employee relationship exists when an individual performs labor or services for an employer. Proof that an individual is not an employee must be established by a preponderance of the evidence.

A person may be an employee of two or more employers at the same time.

Definition of Independent Contractor. An "independent contractor" is an individual who performs labor or services under either of two tests. The ABC test requires that:

- the individual is and will continue to be free from control or direction, both under the contract and in fact. Control or direction includes the right to control or direct as well as general control or direction over the individual's physical activities;
- the labor or service is either outside the usual course of business for which the labor or service is performed or outside of all the places of business of the enterprise for which the labor or service is performed; and
- the individual is customarily engaged in an independently established trade, occupation, business, or profession that is of the same nature as that involved in the contract.

An alternative test requires that:

- the individual is and will continue to be free from control or direction, both under the contract and in fact. Control or direction includes the right to control or direct as well as general control or direction over the individual's physical activities;

- the individual's business is not financially dependent on the relationship with the party engaging the individual and the business continues after the relationship ends;
- the individual has a substantial investment of capital in the business;
- the individual gains profits and bears losses as a result of managerial skills and capital investment;
- the individual makes his or her labor or services available to the public or business community on a continuing basis;
- the individual files a schedule of expenses with the IRS;
- the party engaging the individual does not represent the individual as an employee; the individual has the right to perform similar labor or services for others;
- the individual has an active and valid registration with the Department of Revenue and any other state agencies for purposes of taxes; and
- the individual has a separate set of books and records.

Acts taken to comply with laws are not proof of independent contractor status.

Enforcement. Administrative enforcement as well as a private cause of action are authorized under the EFCA.

*Administrative.*

The Department may investigate violations and for any of the prohibited acts may order payment of:

- a civil penalty of \$1,000 to \$10,000 per employee, or \$10,000 to \$25,000 if the person engaged in a pattern or practice;
- damages of three times the wages and benefits denied or withheld and reimbursement for taxes and the value of benefits paid by the employee. Liability is joint and several for employers and other persons; and
- taxes owed.

The Department may also order reinstatement and reclassification of the employee, or front pay in lieu of reinstatement.

For a notice violation, the Department may order payment of a civil penalty of \$1,000 to \$10,000.

*Cause of Action.*

Individual and class actions are authorized. If the court determines that a person, including an employer, engaged in any of the prohibited acts, the court must order payment of damages of: (1) the greater of (a) three times the wages and benefits unlawfully denied or withheld, or (b) statutory damages of \$1,000 to \$10,000 per employee or \$10,000 to \$25,000 per employee if a pattern or practice is shown; and (2) attorneys' fees and costs. The court may also order employers and other persons to reimburse the employee for taxes and the value of benefits paid by the employee. Liability is joint and several for employers and other persons.

Employers may also be ordered to pay taxes, and may be subject to injunctive or other relief, including reinstatement and reclassification or front pay in lieu of reinstatement.

*Other Enforcement Provisions.*

A three-year statute of limitations for both administrative and court actions is tolled during any period that an employer deterred an action. A "pattern or practice" means that within the previous 10 years, the employer was convicted for nonpayment of wages or delinquent in payment of a court-ordered or administrative assessment for nonpayment of wages. The Department may initiate collection procedures for unpaid premiums and may send its determination to the Employment Security Department.

A general construction contractor is liable for violations of an independent contractor or subcontractor only when the general exerts substantial control over the day-to-day work of the subcontractor or independent contractor.

Account. The EFCA Account (Account) is created. Civil penalties must be deposited into the Account, which is appropriated, and moneys in the Account may be used only for enforcement of the EFCA.

Implementation. The Department has rule-making authority and may develop a plan for strategic enforcement of the EFCA, prioritizing industries and workplaces with a high concentration of violations.

Existing Employment Laws. The EFCA independent contractor tests apply to prevailing wage, wage deductions, the Wage Payment Act, the Minimum Wage Act, unemployment insurance, and industrial insurance. Most existing statutory tests are repealed. The EFCA provisions on the employer employee relationship also apply to these other laws.

The EFCA provisions on general construction contractor liability also apply to wage deductions, the Wage Payment Act, and the Minimum Wage Act.

An employer who engages in a pattern or practice of violations is barred from bidding on a public works contract for one year and is also subject to other sanctions.

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**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect 90 days after adjournment of the session in which the bill is passed.

**Staff Summary of Public Testimony:**

(In support) Some people play by the rules and some bad actors game the system. Treating employees as independent contractors cheats workers from pay and workers' compensation benefits. Misclassification robs public schools and hurts people. People in direct sales or who have independent businesses are exempt. The Department of Labor and Industries returned millions of dollars to workers and collected \$12.7 million in unpaid premiums in 2013 because of misclassification and wage theft. Since 2010, 25 other states have addressed

misclassification. The simple ABC test is used by 37 states. The test will be consistent for all wage and hour laws.

The construction industry needs to know that misclassification will not be tolerated. It has become mainstream to tell someone "you will be an independent contractor" but they are not in control. Truck drivers are told they cannot drive for another company and get no benefits. Wage theft and labor abuse is taking place. Current law is inadequate. Misclassification is complicated for employees. Vulnerable people such as those in the janitorial industry, are being taken advantage of. Misclassified workers sometimes get in trouble with the IRS. Workers can't make ends meet. Misclassification is a stepping stone to the underground economy.

(Opposed) There are multitudes of concerns with this bill. It creates new risks and liabilities for honest employers and will lead to a myriad of lawsuits. It gives organized labor standing to bring new class action lawsuits. This bill does not simplify the test. It creates an A through K test that small businesses will never figure out. Better enforcement of the current law is needed. The bill would eliminate use of independent contractors in the trucking industry and put Washington trucking companies at a competitive disadvantage. Federal law permits the trucking company business model and preempts state regulation of price, routes, and services. Stating that complying with federal rules may not be considered in determining status creates legal issues.

This bill is an end-run around the Construction Underground Economy Advisory Committee process at the Department of Labor and Industries. There will be a presumption that a homeowner hiring a plumber is an employer. The "exercise of physical control" language is a concern. Under the Stute case, the employer's duty is not delegable. The bill will have a chilling effect on the self-employed. Franchisees should not be reclassified as employees.

**Persons Testifying:** (In support) Representative Riccelli, prime sponsor; Rebecca Smith, National Employment Law Project; Nicole Grant, International Brotherhood of Electrical Workers; Elizabeth Hanley, Washington State Association for Justice; Matt Haney, SEIU Local 6; Cariño Baragan, Casa Latina; and Zach Abebe.

(Opposed) Bob Battles, Association of Washington Business; Jerry Vanderwood, Associated General Contractors; Tom Kwieciak, Building Industry Association of Washington; Sydney Tribe, Talmadge-Fitzpatrick Law Firm; Gary Smith, Independent Business Association; Patrick Connor, National Federation of Independent Business; and Mark Johnson, Washington Retail Association.

**Persons Signed In To Testify But Not Testifying:** None.