

# **CLASSIFICATION OF WORKERS IN THE CONSTRUCTION INDUSTRY TASK FORCE**

## **Minutes of the 2nd Meeting of the 2020 Interim**

**September 10, 2020**

### **Call to Order and Roll Call**

The 2nd meeting of the Classification of Workers in the Construction Industry Task Force was held on Thursday, September 10, 2020, at 8:30 AM, in Room 171 of the Capitol Annex. Senator Matt Castlen, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Matt Castlen, Co-Chair; Representative Jason Nemes, Co-Chair; Senator Karen Berg; Representatives Terri Branham Clark and Sal Santoro; Jason Clark, Spencer Coates, Billy Doelker, Tommy Gumm, Marty Hammons, Patrick Jennings, Ken Lyons, Gary Morris, Anthony Russell, Kevin Sell, Allyson Smith, and Robert Swisher.

Guests: Scott Gasser, Director, Division of Security and Compliance, Department of Workers' Claims.

LRC Staff: Andrew Manno, Audrey Ernstberger, Drew Baldwin, and Sasche Allen.

### **Approval of Minutes**

A motion to approve the minutes of the August 6, 2020 meeting was made by Representative Sal Santoro, seconded by Co-Chair Jason Nemes, and approved by voice vote.

### **Labor Cabinet Perspectives**

Robert Swisher, Commissioner of the Department of Workers' Claims (DWC); Scott Gasser, the Director of the Division of Security and Compliance; and Anthony Russell, the Director of the Division of Wages and Hours, provided anecdotal evidence and information regarding classification of workers from the Labor Cabinet's perspective. The Department of Workers' Claims is statutorily tasked with administering workers' compensation claims and ensuring compliance of employers and employees with workers' compensation laws. According to KRS Chapter 342, every employer having one or more employees must obtain a workers' compensation policy on the voluntary market or must be certified by the Commissioner of the DWC to be self-insured. As a result, the DWC is effected by the misclassification of workers from a claims standpoint and a compliance standpoint.

From the claims standpoint, the issue of misclassification of employees is determined by the employer and employee relationship. In workers' compensation, an employer is defined as "Any person, other than one engaged solely in agriculture, that has in this state one (1) or more employees". An employee is defined as any person "in the service of an employer under any contract of hire" either expressed or implied and also any person "performing service in the course of the trade, business, profession, or occupation of an employer at the time of the injury." According to Commissioner Swisher, each definition is broad and nonspecific which could lead one to conclude, by default, an injured worker is deemed to be an employee of the punitive employer. Each year the DWC adjudicates between 3,500 and 4,500 claims in which the employer and employee cannot come to an agreement for a settlement. Claims in which the employer alleges the injured worker was not an employee but instead an independent contractor total an estimated 35 to 50 yearly. These cases are spread across all industries and are not exclusive to the construction industry. To resolve these types of claims, the DWC uses a nine part test to evaluate four major sections. The factors include the extent to which the employer controlled the work, the nature of the work as it relates to the work of the employer, the professional skill of the alleged employee, and the true intentions of both parties. This test is not universal amongst state agencies, and Commissioner Swisher said he believes it would be best to have a unified test for determination of employment status. If an employee is deemed as such and the employer does not have workers' compensation insurance, then the Uninsured Employers' Fund (UEF) pays for those benefits. The actuary assessment for the UEF for 2019 showed a liability of \$145 million, and annually the Workers' Compensation Funding Commission transfers about \$7.5 million to the UEF to pay administrative expenses and current claims.

The Division of Security and Compliance within the Labor Cabinet has 11 field investigators that are each responsible for 10 to 12 counties and are required to perform 96 to 100 investigations a month. Investigations are performed as a result of complaints made to the Division of Security and Compliance and employer reported information obtained from the Department of Revenue. Investigations can also be opened to verify "Affidavit of Exemption from the Kentucky Workers' Compensation Act" forms that have been submitted by local fiscal courts. In most cases, independent contractor determinations are made by administrative law judges. Citations for noncompliance are issued for those that do not have workers' compensation insurance, and the DWC general counsel either issues a fine or files action against the company or business. The Division of Security and Compliance performed 553 investigations in 2019 to determine if employees were independent contractors relating to construction related employers. Commissioner Swisher added that most construction related employer investigations do find that there is workers' compensation coverage carried, but the issue comes in when the policy only covers part of the employer's workforce.

According to Director Russell, there is very little statistical data available relating to the topic of classification of workers from the wage and hour perspective. The statutory definition of employer and employee as it pertains to wages and hours differs from the workers' compensation statutory definition. As a result, the test to determine the employer and employee relationship differs from the test that the DWC uses. The underlying factor of the tests that is consistent amongst the DWC and the Division of Wages and Hours is the control in the matter of which the daily work is to be performed. The Division of Wages and Hours carries between 400 and 500 cases a month with 16 investigators that cover the entirety of the Commonwealth. Most cases are driven by employee complaints, injuries, or an eminent danger situation. There are not usually inspections or investigations performed solely based on classification of employees. Those issues may be uncovered during a more typical investigation involving wages and hours or occupational safety. Over 90 percent of wages and hours cases are in the general industry area or in private industry establishments. Since the repeal of the prevailing wage law, fewer investigations are performed in public sector construction work. Director Gasser said that although in his experience most misclassification happens in the construction industry, the issue does arise in all industries.

In response to a question from Co-Chair Jason Nemes, Commissioner Swisher explained that having uniform definitions of employer and employee would provide clarity for all those tasked with making employment status determinations. Director Russell added that although he agreed with the need for uniformity, there would still need to be some differences as it pertains to federal law. Answering a follow up question, Commissioner Swisher stated from the DWC perspective, there are times that companies or businesses unintentionally misclassify employees, but it is not given much consideration because the Department assumes companies or businesses should be aware of the legal requirements. Director Russell also commented that under the occupational safety and health laws, there are specific regulatory and procedural allowances for those with a history of good faith and those that are repeat violators. Commissioner Swisher explained that the DWC's fines equate with the violation and the DWC does keep record of repeat violators.

Answering a question from Kenneth Lyons, Director Russell stated at one time the Division of Wages and Hours would share information with other divisions, departments and agencies, but currently do not in an effort to not be overly punitive.

Kevin Sell commented on the good work of the Labor Cabinet when it comes to classification. He also expressed the need for more statistics to produce legislation. He noted there may need to be more data sharing amongst state entities, and that classification is an issue in all industries, not just limited to construction.

Replying to Representative Terri Branham Clark, Commissioner Swisher said that independent contractors do not register with the state. The only way the DWC may discover if someone is alleging to be an independent contractor is if there has been a complaint filed or if a worker is injured.

For clarification purposes, Commissioner Swisher explained that an independent contractor is anyone who performs labor or service for compensation who is not directly employed by a statutory employer. This person would be a sole proprietor not be directed by an employer in terms of how they conduct their business.

Allyson Smith explained that from the perspective of Kentucky Employers' Mutual Insurance (KEMI), misclassification occurs in all industries, but KEMI sees it almost entirely in the private residential arena and in both the public and private sectors. In other states, employee status has to be provided to the state by employees and independent contractors.

### **Department of Revenue Perspective**

Garry Morris, the Executive Director of the Office of Tax Policy and Regulation with the Department of Revenue, gave a brief overview of how the Department of Revenue handles misclassification from a broad oversight perspective. Construction contractors doing business in the state are required to withhold Kentucky individual income tax from their employees performing work within the state. The tax and related forms are required to be submitted by the contractor to the Department of Revenue and employees are required to file a Kentucky Individual Income Tax return. The Department has long realized that some construction contractors claim they hire independent contractors to perform work within the state and not employees. Determining whether an independent contractor or employee is performing work at a Kentucky construction job site can be very challenging. When the Department receives information that indicates an independent contractor and employee determination situation exists, the Department will attempt to contact the contractor. If a dispute with the contractor arises, then staff relies on IRS guidelines for determining when a worker is an employee or independent contractor. In some cases the Department has requested the contractor obtain an IRS SS-8 Determination, which is a process that can take several months. If it is determined a contractor has employees, then the Department issues an estimated assessment for tax, interest, and penalties. The Department uses definitions of employer and employee that are found in the state income tax laws which reference the Internal Revenue Code. The Department of Revenue does not currently have dedicated staff to work on issues related to misclassified workers, but tips from the public or other government agencies that related to the issues are investigated to the extent that departmental resource levels allow. Executive Director Gasser added that the Department of Revenue is willing to share information with other state agencies and that an information sharing disclosure agreement is in place with the Labor Cabinet.

Co-Chair Jason Nemes suggested that small working groups be formed within the task force to address definitions of employer and employee and misclassification in the public and private sectors.

Co-Chair Matt Castlen said that the task force should determine if changes needs to be made from a legislative standpoint or a regulatory standpoint.

There being no further business, the meeting adjourned at 9:54 a.m.