# Legislative Analysis

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**WORKERS COMPENSATION:**
**INDEPENDENT CONTRACTOR STATUS**

**House Bill 5962**
**Sponsor: Rep. Andrew Kandrevas**
**Committee: Labor**

**Complete to 5-11-10**

**A REVISED SUMMARY OF HOUSE BILL 5962 AS INTRODUCED 3-17-10**

House Bill 5962 would amend the Worker's Disability Compensation Act to establish standards and enforcement protocols when determining independent contractor status.

***Contractors classified as employees***. Under the bill, in the case of principals and contractors in the ***commercial carrier and construction industries***, a contractor is considered to be classified as an employee of the principal, and must be treated as an employee under the act, unless the principal demonstrates the following to the satisfaction of the director of the Worker's Compensation Agency: (1) the contractor, encompassing all provisions of Section 161(1)(n), is not an employee; and (2) the contractor has been and will continue to be free from direction and control of the principal, both in fact and under the contract, express or implied, between the parties.

***Penalties***. The bill specifies that a principal who failed to properly classify an individual as an employee, and that failed to pay benefits or other contributions required by the act, would be guilty of the following: (1) for knowingly violating this subsection, a felony punishable by imprisonment for not more than 18 months or a fine of not more than $15,000, or both, for a first offense, and imprisonment for not more than seven years or a fine of not more than $30,000, or both, for a second or subsequent offense; (2) for unintentionally violating this subsection, a misdemeanor punishable by imprisonment for not more than six months or a fine of not more than $2,5000, or both, for a first offense, and imprisonment for not more than one year or a fine of not more than $5,000, or both, for a second or subsequent offense.

***Stop-work orders***. If he or she determined that a violation had occurred, the director of the Worker's Compensation Agency could issue a stop-work order requiring the cessation of all business operations within 72 hours. The stop-work order would take effect when served upon the employer or, for a particular employer worksite, when served at the worksite. The stop-work order would remain in effect until the director issued an order releasing it, or upon finding that the employer had properly classified the individual as an employee. Under the bill, the director could impose a probationary period not to exceed two years, and require the employer to file with the department periodic reports demonstrating the employer's continued compliance with requirements of this section. (The bill requires that the department promulgate rules under the Administrative Procedures Act to determine filing times and report requirements.) A stop-work order

and penalty would be effective against any successor corporation or business entity that had one or more of the same principals or officers as the employer against whom the stop-work order was issued, and that was engaged in the same or equivalent trade or activity. The director would be required to assess an administrative penalty of $1,000 per day against an employer for each day that the employer conducted business operations that were in violation of a stop-work order issued under this subsection.

***Civil actions***. A contractor improperly classified as a contractor, or an organization or union representing the employee, could bring a civil action (including a class action), in a court of competent jurisdiction to enforce the classification. An individual's representative, including a labor organization, would have standing to bring the action on behalf of the individual (or on behalf of a class of individuals). Upon prevailing in an action, the court could award attorney fees and other costs of the action, in addition to damages, to an individual or class of individuals who had not been properly classified as employees.

***Cumulative remedies; rules***. The bill specifies that the remedies under this section would be cumulative, and would not prohibit the bringing of any administrative, civil, or criminal action under the act. Further, the director could promulgate rules under the Administrative Procedures Act to enforce this section.

***Show cause; debarment***. Under the bill, if the director of the Worker's Compensation Agency received information indicating that an employer (or officer or agent of the employer) had knowingly and intentionally violated the act, or had been convicted of a violation of the act, the director would be required to issue an order to show cause why the individual should not be found in violation of the act and subject to debarment. An individual served with an order to show cause would have 14 days to file an answer in writing. If he or she failed to do so, the director would issue an immediate debarment order, or immediately assess administrative penalties, as provided in this section, or both. After the date a debarment order was issued, the director would also notify all public bodies in Michigan of the name of the employer, and no contract would be awarded to the employer or to any firm, corporation, or partnership in which the employer had an interest until a period of up to three years, as determined by the director.

***Administrative penalties; factors to consider***. As an alternative to, or in addition to, any other sanctions provided by law for a violation of this act, the director would be authorized to assess and collect administrative penalties up to a maximum of $2,500 for the first violation and up to a maximum of $5,000 for each subsequent violation. When determining the amount of the administrative penalty imposed due to a violation, the director would be required to consider factors that included the history of previous violations by the employer, the seriousness of the violation, the good faith of the employer, and the size of the employer's business.

***Subpoenas***. The bill specifies that the department may subpoena witnesses, administer oaths, examine witnesses, take testimony, and compel the production of documents. Upon application of an attorney representing the state, the department can issue a

subpoena to compel the production of the documents, computer records, and information relating to compliance with the act. In addition, the director can seek enforcement in the circuit court of any order or subpoena issued by the department.

***Prohibit retaliation***. The bill also prohibits an employer or any other party from discriminating in any manner, or taking adverse action against a person in retaliation for exercising rights protected under the act. The rights protected include, but are not limited to, the right to file a complaint or inform any person about an employer's noncompliance with the act, and the right to inform any person of the person's potential rights and to assist the person in asserting those rights.

A person who, in good faith, alleged noncompliance with the act, would be afforded the rights provided by the act, notwithstanding the person's failure to prevail on the merits. Taking adverse action against a person within 90 days after the person's exercise of rights would create a rebuttable presumption of having done so in retaliation for the exercise of those rights. A person alleging a violation could bring an action in a court of competent jurisdiction to seek compensation for economic and non-economic losses, including the assessment of punitive damages.

***Worker's Compensation Administrative Revolving Fund***. Finally, any assessments and administrative penalties collected under the act would be placed in the Worker's Compensation Administrative Revolving Fund, created in Section 835a, and applied in the manner provided in Section 835(5) of the act.

MCL 418.171 et al

**FISCAL IMPACT:**

**State Expenditures:** The Department of Energy, Labor, and Economic Growth (Workers Compensation Agency) indicates that it could carry out the additional responsibilities imposed on it under the bill within existing staffing and budgetary resources. These responsibilities include reviewing compliance with the employee classification requirements on the commercial carrier and construction industries under the bill, the issuance of stop-orders, and the issuance of show-cause hearings.

**State Revenue:** The imposition of administrative penalties would increase revenue to the Workers Compensation Administrative Revolving Fund (WCARF) by an indeterminate amount, depending on the volume of violations and the amount of any associated penalties. The administrative penalty is a fine of up to $2,500 for a first violation and up to $5,000 for any subsequent violation, with the amount of the fine based on the history of previous violations by the employer, the seriousness of the violation, the good faith of the employer, and the size of the employer's business. Any such revenue would be credited to the WCARF and, by statute, would be expended to support the operations of the Workers Compensation Agency, the Workers Compensation Board of Magistrates and the Workers Compensation Appellate Commission, including the agencies' responsibilities for education and training, case management, claims

reviews, and administrative hearings. The act provides that any revenue in the WCARF remaining in the fund at the close of the fiscal year is carried forward into the next year rather than lapsing to the General Fund.

In addition to the direct revenue impact on the Workers' Compensation Agency, the bill could potentially have an ancillary impact on income and unemployment taxes, to the extent that certain employers that have "misclassified" employees and have thus far avoided paying employment-based taxes by classifying employees as self-employed (contractors) or by under-reporting income will now be brought into the fold. This amount can be fairly substantial. For example, in a review of Unemployment Insurance Agency audits of employers conducted in 2003 and 2004, researchers from the Michigan State University, School of Labor and Industrial Relations (MSU-SLIR), estimated that, on the whole, 30% of Michigan employers misclassified employees as self-employed or underreported employee payroll. For the two industries that are the subject of this bill – construction and trucking – the proportion of employers misclassifying employees was slightly lower at 26.4% and 24.4%, respectively. The study estimated that the misclassification of employees within the construction and trucking industries resulted in a loss of $2.6 million in unemployment insurance taxes and an additional $2.7 million in state income tax revenue.[1]

**Local Fiscal Impact:** The bill would have no direct fiscal impact on the local units of government.

**Other Information:** The issue of employee misclassification is one of increasing interest to states, the federal government, workers' rights advocates, and employer interests. On this issue, it has been said that workers' compensation is the driving factor behind the decision of certain employers to misclassify employers. A 2000 study for the U.S. Department of Labor found that, "[t]he number one reason for misclassifying workers or hiring independent contractors is the savings in not paying workers' compensation premiums and thereby not being subject to workplace injury and disability-related disputes."[2] In its July 2009 report, the state's Interagency Taskforce on Employee Misclassification estimated that, in 2004, $97.9 million of workers' compensation premiums were not properly paid because of employee misclassification.[3]

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.

[1] See, Dale L. Belman and Richard Block, *The Social and Economic Costs of Employee Misclassification in Michigan*, 9 December 2008, [http://www.ippsr.msu.edu/Publications/BEBelman.pdf].

[2] See, Planmatics Inc., *Independent Contractors: Prevalence and Implications for Unemployment Insurance Programs*, February 2000, [http://wdr.doleta.gov/owsdrr/00-5/00-5.pdf].

[3] *Michigan Interagency Task Force on Employee Misclassification*, 1 July 2009, [http://www.michigan.gov/documents/dleg/rpt_to_g_284925_7.pdf].