



**REPORT for EXECUTIVE ORDER THIRTY-EIGHT (EO38)
FROM THE INTER-AGENCY TASKFORCE ON
MISCLASSIFICATION AND PAYROLL FRAUD**

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OVERVIEW

Importance of the Issue

The misclassification of actual employees as “independent contractors” creates a competitive disadvantage for Virginia businesses that follow the law, deprives the Commonwealth of millions of dollars in tax revenues necessary to supply services to Virginia’s citizens, and prevents workers from receiving protections and benefits to which they legally are entitled.

A 2012 report of the Joint Legislative Audit and Review Commission (JLARC) found that up to one-third of audited employers in certain industries misclassify employees. By failing to purchase workers' compensation insurance, pay unemployment insurance and payroll taxes, or comply with minimum wage and overtime laws, employers reduce their labor overhead as much as 40%, placing employers who properly classify employees at a competitive disadvantage.

Based on state and national studies, the 2012 JLARC report estimated that worker misclassification lowered Virginia’s state income tax collections as much as \$28 million a year. Agencies with relevant enforcement responsibilities, including the Virginia Employment Commission, the Workers’ Compensation Commission, the Department of General Services, the Department of Labor and Industry, the Department of Professional and Occupational Regulation, the Department of Small Business and Supplier Diversity, the Department of Taxation, and the Office of the Attorney General each address only one or more components of this practice and may not fully coordinate their efforts. In its study, JLARC recommended the establishment of a task force to analyze and address misclassification in the Commonwealth.

Background

For over a decade the General Assembly has considered the harm of misclassification in Virginia.

During the 2007 General Assembly, HB2217 sought to direct the Commissioner of Labor and Industry to establish and maintain a toll-free telephone number and make available paper forms and on-line electronic forms that may be used by persons to report suspected instances of misclassification of employees as independent contractors. The hotline and forms were to be used to report suspected instances of workers' compensation insurance fraud and unemployment tax fraud. It further directed the Commissioner to forward reports of suspected instances of misclassification or fraud to the Insurance Fraud Investigation Unit of the Virginia State Police, the

Virginia Employment Commission, or both, as appropriate, for their investigation. This bill was tabled in the Committee on Commerce and Labor in the House of Delegates.

During the 2010 General Assembly, SB34 sought to create a Misclassification Act which would have prohibited an employer from classifying an individual as an independent contractor if the worker was actually an employee. Violators were to be subject to criminal penalties, civil penalties, and debarment from public contracts, private actions and stop-work orders. This bill was continued to 2011 by the Committee on Commerce and Labor in the Senate.

In 2011, the Virginia General Assembly passed a Joint Resolution (SJ345) directing the Joint Legislative Audit and Review Commission (JLARC) to study “any misclassification of employees as independent contractors in Virginia.”

The following year, in June 2012, JLARC issued its report. It found that up to one third of audited employers in certain industries misclassified their employees. Specifically, the report extrapolated figures for Virginia indicating that the Commonwealth might have up to 40,000 misclassifying employers and upwards of 214,000 misclassified workers.

The JLARC study also reported that, by failing to purchase workers' compensation insurance, pay unemployment insurance and payroll taxes, or comply with minimum wage and overtime laws, employers lower their costs as much as 40%, placing other employers at a competitive disadvantage. Furthermore, JLARC estimated that worker misclassification lowered Virginia's state income tax collections as much as \$28 million a year.

The JLARC findings and recommendations to the General Assembly included defining “employee” in the state code, sharing information among oversight and enforcement agencies, making it illegal to misclassify and establishing a schedule of fines associated with violating the law.

Following the 2012 report, the Virginia Senate considered SB879 during the 2013 General Assembly, which would have established an interagency taskforce. SB879 passed the Senate unanimously, but failed in the House of Delegates.

In 2014, Governor McAuliffe issued Executive Order 24 forming a Misclassification and Wage Theft Taskforce directing that a report with recommendations be submitted to him no later than December 2014. Based on taskforce recommendations, several successful combined enforcement actions were conducted at Northern Virginia and Hampton Roads worksites during the McAuliffe Administration.

In August of 2018, Governor Northam issued Executive Order 16, which directed the reconstitution of the Interagency Taskforce and requested updated recommendations on how to measure and combat misclassification in Virginia.

Extending the work of the Taskforce, Governor Northam issued a new order, Executive Order 38, which directed the Taskforce to produce a written report with recommendations ahead of the 2020 General Assembly.

The presentation of this report is deemed to fulfil the reporting requirement of Executive Order 38.

REPORT FOR EXECUTIVE ORDER THIRTY-EIGHT (EO38)

Initiatives

The purpose of the Taskforce included, but was not limited to:

1. Reporting on statutes and regulations related to worker misclassification and payroll fraud and, if appropriate, recommending changes or additions to relevant legislation or administrative rules including an assessment of whether existing definitions of “employer” and “employee” are satisfactory or should be updated in light of current employment practices;
2. Reporting on current enforcement practices of the agencies involved and recommending procedures for more effective interagency cooperation and joint enforcement;
3. Reporting on the findings of efforts in other states and providing examples of effective methods for education and outreach;
4. Identifying effective ways to hold accountable companies working on state contracts that commit payroll fraud through the intentional misclassification of workers; and
5. Identifying ways to address misconduct through incentives for compliance and meaningful penalties for non-compliance.

The Secretary of Commerce and Trade and the Governor’s Chief Workforce Advisor were appointed to co-chair the taskforce, which included representatives from the Virginia Employment Commission, the Workers’ Compensation Commission, the Department of General Services, the Department of Labor and Industry, the Department of Professional and Occupational Regulation, the Department of Small Business and Supplier Diversity, the Department of Taxation, and the Office of the Attorney General.

The Taskforce was directed to meet with and receive input from stakeholder groups impacted by misclassification statutes and regulations, including the business community representatives and labor organizations. The taskforce conducted outreach efforts, holding a public input session on October 1, 2019 and receiving and reviewing written submissions throughout the month of October 2019

Taskforce Recommendations

The members of all working groups of the Task Force expressed general agreement with the following recommendations.

It is recommended:

1. Virginia is a tax conformity state, and has long conformed to the IRS standards both for the “test” of employment and for its approach for penalties that are assessed. The Taskforce believes that penalties should be substantial enough to deter misclassification, which is not presently the case in Virginia.
2. That penalties apply even when an employer received advice, consultation or counsel to engage in worker misclassification as a “business model.”
3. That legislation provides for a private cause of action against an employer for recovery of damages for misclassification to include wages, taxes, and value of benefits lost, and attorney’s fees.
4. That legislation provides “whistleblower protection” for those who report suspected misclassification or other workplace fraud.

5. That the Board for Contractors at the Department of Professional Occupational Regulation (DPOR) be directed to promulgate a regulatory violation of “intentional improper classification of workers” as an element of unprofessional conduct for a licensed contractor firm, subject to sanction by the Board.
6. That bidders be debarred for graduated periods of time, based upon repetition or severity of violations, from bidding on and receiving awards of contracts under the Virginia Public Procurement Act (VPPA) when the bidder is found to have violated requirement of proper worker classification. It is recommended that this be added to the VPPA.
7. That legislation or Executive Directive cause the Virginia Employment Commission (VEC), the Department of Taxation (TAX) and other Commonwealth agencies to undertake specific workplace fraud and misclassification investigations in a joint fashion to gather evidence for enforcement actions that the task force continue its work under Executive Order 38 to determine the procedures, processes, organizational structures, and inter agency authorities that must be developed to streamline the continuing exchange and sharing of information to achieve joint enforcement. These efforts will include a thorough review of internal policies, procedures, and processes which will help streamline misclassification, payroll fraud, and wage theft claims.
8. That an agency be identified, and given authority to lead these efforts in the new organizational structure.
9. That additional funding be provided for educational outreach to educate and inform the general public, workers and employers explaining the definition and responsibilities of being classified as an independent contractor and the benefits and protections of being classified as an employee.
10. That funding be provided to support the interagency model that is developed to continue joint cooperation, information sharing, investigation and enforcement, including the hiring of investigators.
11. Finally, there is a consensus that it would be advantageous to the Commonwealth for the Taskforce to remain in place for the duration of the Executive Order and reconvene as needed.

Findings of Efforts in Other States

According to testimony before the US House of Representatives Subcommittee on Workforce Protections on September 16, 2019, over 20 states have enacted laws to combat worker misclassification and another 15 states have initiated what the Chairwoman, Alma Adams (NC-13) called “innovative government taskforces to do the same.” She used as an example her own state of North Carolina, which recently launched the Criminal Investigations and Employee Classification Division.

States that have enacted penalties for misclassified workers include: Alaska, California, Colorado, Connecticut, Delaware, Florida, Illinois, Kansas, Louisiana, Maine, Maryland, Massachusetts, Missouri, Nebraska, New Jersey, New Mexico, New York, North Carolina, Pennsylvania, Rhode Island, Texas, Utah, Vermont, and Wisconsin.

The following sections represent research into the efforts by other states that may be worth exploring further as the work of the interagency taskforce continues. Efforts are organized by topic.

Definitions

Defining who is an “employee” and state tests to determine whether a worker is an employee or an independent contractor fall into two broad approaches. They either establish a complex analysis of duties or an assessment of control.

In a number of states, there is a rebuttable presumption that workers are employees, and the laws and regulations establish a burden that an employer must overcome to show that a worker is an independent contractor.

Alternatively, instead of shifting burdens, states such as Montana and Nebraska have experimented with issuing certification to anyone who wishes to work as an independent contractor. In this approach, a worker “knowingly chooses to work as an independent contractor,” signifying and certifying an understanding of the implications of that choice, and making his or her own arrangements with state and local government entities for licensure, taxes, and collection and payment of worker benefits. An employer may not hire a worker as an independent contractor unless they have proof of their certification, and are thereafter protected from penalty in the event there is an employment status challenge. Employers are subject to fines if they do not verify independent contractor status through this state issued certificate.

Some states developed their own unique standards. For instance, Tennessee courts use a six-factor test.

The IRS does not have a specific definition and instead offers a 20 question survey to help determine a worker's status and we understand that it is further refining its approach this year. The Virginia Department of Taxation uses the same type of analysis of worker relationship as the IRS.

A number of states have adopted what is commonly called the "ABC test" to determine employee status. According to a Harvard report on misclassification efforts around the country, "survey respondents and interviewers identified the duty or control analysis tests as a sources of confusion, while states having the ABC test reported (the approach) as workable and effective."

Policymakers in states with pro-business environments have been wary of California's recent efforts to target what has been referred to as "gig economy" business models that depend on independent contractors. California has also created a retroactive enforcement and penalty model that is being challenged in court.

Education and Reporting Methods

A number of states have funded efforts and infrastructure dedicated to educating employers, workers and the general public, and have established user friendly procedures for reporting suspected misclassification.

Methods include traditional media, public service announcements, websites, other social media and speaker panels who can be deployed to community groups and business associations. These help businesses and the general public understand websites that explain the differences between an employee and an independent contractor and hotlines to seek information or to report misclassification.

States using hotlines and websites for reporting indicate that they are commonly used, not only by workers, but also by business competitors who follow the rules and want to stop unfair competition from violators. Also, states that facilitate reporting of misclassification most often have anti-retaliation or "whistleblower protection" provisions in law.

Some states have developed mandatory notices that must be posted on websites or included in paychecks advising workers of the definitions of and differences between and employee and independent contractor.

Tennessee issues a first offense warning but has found that to be expensive and ineffectual. Their recent report and recommendations advises abandoning that for graduated penalties. Their survey of penalties is available for review and reference the types of penalties assessed in at least twenty other states.

Some states have marketing plans that include the use of traditional media and public service announcements, social media and established panels of speakers who are deployed to present to community groups and business associations.

Monitoring and Addressing

A number of states have established permanent commissions or task forces to engage in coordinated monitoring and enforcement of misclassification and payroll fraud.

Data Sharing Agreements and Technology

To facilitate effective enforcement, some states have increased interagency collaboration around enforcement and real-time data sharing across programs and agencies.

There is evidence that employers who skirt government mandates in one area are likely ignoring other laws. By joining state records on environmental violations, health and safety citations, worker misclassification, and other regulatory infractions, states are more accurately pinpointing which firms should experience enhanced scrutiny as the result of previous misbehavior. Predictive modeling has already been leveraged to increase investigatory efficiency and protect the public in other states.

Penalties

States vary in assessing civil and criminal penalties for companies found to misclassify their workers (See the Tennessee report for a survey). Fines in many states escalate by number of employees misclassified, by number of days in violations and by whether the misclassification was intentional.

Some states have passed legislation assessing higher civil penalties and bringing criminal charges when workers are intentionally underpaid or are paid cash wages “off the books”. These states also have penalties for failure to maintain proper payroll records.

Stop work orders and debarment from state contracts are tools used to punish companies who willfully misclassify workers and utilize this as part of their business model. Some of these states have also established “higher level” liability for contractors whose sub-contractors commit violations. These states have also developed strategies to target sham LLCs that are used to commit violations and then dissolve, only to reorganize and repeat the offense, as a different legal entity.

Suspension or revocation of licenses and forfeiting the ability to participate in any state procurement contracts are also being employed as further deterrents by various states.

Private Right of Action exists in many of the states that have misclassification and wage theft laws in their code. However, research indicates there are not methods for a private litigant to file a lawsuit against a company for failure to comply with workers compensation or unemployment insurance laws.

Multistate Agreements

Recently, states actively trying to reduce the incidence of misclassification are working together to prevent offending companies from operating just beyond their borders. Multistate agreements are being developed between and among neighboring states to crackdown on offenders.

Multistate Agreements also help employers more easily comply with the rules when they are doing business in several adjoining states. Uniformity in rules allows efficiencies in administration by multistate players.

APPENDIX I – CURRENT AGENCY ROLES AND RESPONSIBILITIES

Virginia Employment Commission

Current Efforts

The Virginia Employment Commission conducts random audits of employers as part of the Unemployment Insurance program. It also has a team of three special investigators who investigate complaints of alleged misclassification that are often reported by competitor businesses, worker advocacy groups, or employees. The Virginia Employment Commission (VEC) performs interagency investigations and supply suspected tax fraud information to the Department of Taxation.

Detection Methods

- A. The VEC conducts regular audits of employers to address worker misclassification within the federal-state Unemployment Insurance program. Tax Representatives positioned throughout the Commonwealth perform random field audits of 1% of Virginia employers (approximately 2,000) each year and identifies approximately 4,000 misclassified workers.
- B. In December 2015, the VEC established a Targeted Audit and Investigative Unit (“the unit”) utilizing supplemental funding from the United States Department of Labor to enhance federal and state initiatives to address worker misclassification. The unit became fully active in April 2016 with three special investigators who each have an extensive fraud investigation background. They are tasked with, in part, to: identify business models that may systematically lead to non-compliance; conduct joint enforcement sweeps with other Task Force partners; and use the best methods and tools to detect worker misclassification, and in some cases refer for criminal prosecution. Three full-time special investigators are now classified positions within the agency.
- C. On June 16, 2016, the VEC signed a Memorandum of Agreement (MOA) with the United States Department of Labor (USDOL) that enables the Wage and Hour Division of USDOL and the VEC to conduct joint investigations, coordinate enforcement activities, and keep each informed of potential violations of each other’s statutes.
- D. Beginning in 2017, VEC entered into an agreement with the Internal Revenue Service to receive the 1099 Miscellaneous Extract through their data exchange program. This extract is used by the Targeted Audit and Investigative Unit to detect possible instances of worker misclassification and to pursue targeted investigations.

- E. Wage investigations are also conducted as a result of UI claims filed for which no wage records exist or as a result of complaints received from other employers who suspect that their business is being undercut by fraudulent payroll activity of their competitors.
- F. VEC has a nonreciprocal data sharing agreement with the Department of Taxation to which it provides findings of misclassification.

Enforcement Authority

The VEC enforces Virginia's unemployment compensation laws under Title 60.2 of the Code of Virginia. The primary mission is to ensure that funding is available to pay benefits to individuals who become separated from work through no fault of their own and to ensure that all workers who should be covered under the unemployment compensation program are properly classified as employees. Authorizing statutes include § 60.2 -118, § 60.2-119, [§ 60.2-518.2](#), [§ 60.2-521](#), and [§ 60.2-536.3](#).

Prevention Measures

1. VEC engages in education outreach to employers about worker misclassification through inclusion of flyers on the topic in its correspondence and information posted on the agency website.
2. Worker Misclassification and Payroll Fraud is also one of the workshop topics offered at our three to four employer conferences held around the state each year.

Worker's Compensation Commission

Current Efforts

The Commission has no current efforts to report because it has no statutory authority (see Enforcement Authority section).

Detection Methods

The Commission established an Investigations Unit in 2015 that travels throughout the Commonwealth conducting Compliance Investigations on businesses. Although its primary focus is determining whether an Employer needs to be covered under the Workers' Compensation Act this often requires a determination whether workers are truly Independent Contractors or Employees.

The Commission also launched the public facing Virginia Employer Non-Compliance Alerts website, VENCA.com in 2016. The website gives the public an opportunity to advise the Commission of any non-compliance issues that it may not be aware of, such as employers operating without coverage and employee misclassification. This website also gives the public the opportunity to make investigative referrals to the Commission anonymously if they fear reprisal.

Enforcement Authority

The Commission has no direct statutory enforcement authority over misclassification of employees. However, when the Commission's Investigators perform an assessment of an employers' staff and determine that the employer lacks insurance coverage because it has misclassified its employees as Independent Contractors rather than employees, the Commission may issue an "Order to Obtain Coverage" under Va. Code Sec. 65.2-801 and advise of the potential penalties of not obtaining coverage under Va. Code Sec. 65.2-805. If that employer subsequently fails to obtain coverage as ordered, further enforcement action may be taken, up to and including issuance of an Order requiring the employer to cease and desist all business transactions and operations in Virginia until the Commission finds it to be in compliance with the insurance requirements of the Workers' Compensation Act. The Commission may also refer such an uninsured employer to the appropriate Commonwealth's Attorney for criminal prosecution under Va. Code Sec. 65.2-806.

Va. Code Sec 65.2-901 provides every employer shall upon request of the Commission report the number of its employees, hours of their labor and number of days of operation of business. The Commission does not currently mandate any reporting under this statute.

Prevention Measures

The Commission conducts education and outreach on the “Employee vs. Independent Contractor” topic, primarily for new businesses that are opening throughout the Commonwealth by providing our Employer Guide Handbook. The VEC also hosts seminars every year where Commission staff gives presentations on the coverage requirements mandated by the Workers’ Compensation Act. VEC investigators also use opportunities to have face-to-face interactions with employers to educate them on the requirements set forth by the Act.

Department of General Services

Current Efforts

The Department of General Services (DGS) currently does not have any efforts related to worker misclassification and payroll fraud by businesses. DGS authority is limited to contracts for non-technology goods, nonprofessional services, construction, and construction-related professional services. DGS requires contractors to comply with all applicable laws and conditions set forth in a contract.

DGS would recommend that input be sought from the Virginia Department of Small Business and Supplier Diversity (SBSD) [certification of businesses], the Virginia Information Technologies Agency (VITA) [technology procurements] and covered institutions [different procurement authority].

Detection Methods:

None, DGS has no authority or resources to detect noncompliance related to worker misclassification and payroll fraud by businesses.

Enforcement Authority:

None, DGS has no authority or resources to enforce compliance related to worker misclassification and payroll fraud by businesses.

Prevention Measures:

None, DGS has no authority or resources to prevent noncompliance related to worker misclassification and payroll fraud by businesses.

Department of Labor and Industry

Current Efforts

The Department of Labor and Industry (DoLI) takes misclassification of employees very seriously and its current efforts are included in “Detection Methods, Enforcement Authority and Prevention Measures” in more detail in each of the three sections that follow. Each of these efforts are ongoing.

One example is:

- A. Program policy on “Preventing Misclassification of Workers in Virginia Occupational Safety and Health (VOSH) Cases” is directed at identifying and preventing the misclassification of workers in VOSH cases which arose from VOSH inspections opened on or after July 1, 2015. (SEE PREVENTION METHODS below for more information)
- If VOSH penalties are proposed, penalty reductions for size (up to 70%) and good faith (up to 25%) will NOT be afforded to the employer.
 - In construction inspections, each contractor will be asked to provide its Department of Professional and Occupational Regulation (DPOR) contractor's license AND proof of the DPOR license for any subcontractors.
 - Make a referral to DPOR if a contractor has used an unlicensed subcontractor (DPOR sanctions may include fines, probationary terms, suspension or license revocation).
 - For contracts under \$1,000, VOSH will make a referral to the Virginia Employment Commission (VEC) and/or the Virginia Workers' Compensation Commission (VWCC) for potential audits of employment practices. Referrals may be made for contract values over \$1,000 as well.

Detection Methods

- A. The Labor Law Division reviews and investigates hundreds of claims for unpaid wages annually. The claim form requires information concerning the employment status of the claimant including if they worked as a subcontractor or an independent agent. Claimants indicating, they worked as a subcontractor or independent agent are advised the Division only has jurisdiction over employer/employee matters. If the claimant indicates they were classified incorrectly, they are referred to the VEC's misclassification ombudsman for an employment status determination.
- B. The Division also receives thousands of inquiries annually from the public concerning labor and employment law matters. Many allege they have been incorrectly classified as subcontractors or independent agents. They are advised to contact the VEC's misclassification ombudsman for an employment status determination.
- C. The Virginia Occupational Safety and Health Program adopted a new Virginia Occupational Safety and Health (VOSH) policy directed at identifying and preventing the misclassification of workers in VOSH cases effective July 1, 2015. The VOSH Program conducts thousands of occupational safety and health inspections annually, and began looking for evidence of worker misclassification during its inspections. The new policy and education and outreach materials can be found at <https://www.doli.virginia.gov/vosh-programs/misclassification-in-the-workplace/> (see summary in "Prevention Measures" below).

Enforcement Authority

- A. The Virginia payment of wage law is codified at Virginia Code § 40.1-29. This law mandates that employers establish a rate of pay and a regular pay period, and that employees be paid for all time worked and for all work performed in the Commonwealth.
- B. DoLI's VOSH Program administers occupational safety and health activities in the Commonwealth through the Virginia State Plan agreement with federal OSHA as required by Va. Code §40.1-1. The state plan covers employers and employees in general industry, agriculture, construction and state and local government. Section 18 of the Occupational Safety and Health Act of 1970 (the OSH Act) permits States to develop and operate their own job safety and health programs (29 USC 667).
- C. The VOSH program receives partial funding for the program from the U. S. Department of Labor, and is required by the OSH Act to be "at least as effective as" federal OSHA, including maximum penalty levels (29 USC 667(c)). VOSH maximum penalties are

\$12,726 for serious and other-than-serious violations, \$127,254 for willful and repeat violations, and \$12,726 per day for failure-to-abate penalties (see Va. Code §§40.1-49.4. G, -49.4.H, -49.4. I, -49.4. J and -49.4. K).

Prevention Measures

- B. The Agency entered into a Data Sharing Agreement with the Virginia Employment Commission in March, 2018 to allow for the exchange of confidential and sensitive unemployment compensation data to assist DOLI in the performance of its public duties of monitoring worker misclassification claims. Referrals on possible worker misclassifications from the Labor Law Division are investigated by the VEC and the results of the investigation are provided to DOLI. Once the worker has been determined by the Virginia Employment Commission to have been misclassified, the Labor Law Division can investigate their unpaid wage claim.
- C. DOLI began a coordinated outreach effort to stakeholders with the release of a public service announcement on June 2, 2015, and broadcast emails announcing the VOSH program's new policy on "Preventing Misclassification of Workers in Virginia Occupational Safety and Health Cases." The new policy took effect on VOSH inspections opened on or after July 1, 2015.
- D. The Department developed a brochure and poster explaining the impact of misclassification on workers, employers and the Commonwealth, and outlining the new VOSH Misclassification Policy. Copies of the brochure and poster were handed out during VOSH inspections, informal conferences and consultation surveys. A webpage dedicated to Misclassification was added to the Department's website (<https://www.doli.virginia.gov/vosh-programs/misclassification-in-the-workplace/>).
- E. The Department submitted an article to the Summer, 2015 Virginia Capitol Connections Quarterly Magazine entitled "What is Virginia Doing About Misclassification of Workers". http://www.vccqm.org/qm_summer_2015/#
- F. Department personnel have met with numerous employer organizations and provided training courses to discuss the VOSH Misclassification Policy; made a presentation on Misclassification in 2015 to the Virginia Small Business Commission; participated in a Misclassification in the Workplace panel with the Virginia Employment Commission (VEC) and the Department of Taxation at the 2015 Virginia Workers' Compensation Commission annual conference; participated in a Misclassification in the Workplace panel with the VEC and the Office of the Attorney General (OAG) at the 2017 Virginia Bar Association (VBA) Administrative Law Conference.

G. VOSH program's new policy on "Preventing Misclassification of Workers in Virginia Occupational Safety and Health Cases" took effect on VOSH inspections opened on or after July 1, 2015 directed at identifying and preventing the misclassification of workers in VOSH cases:

- If VOSH penalties are proposed, penalty reductions for size (up to 70%) and good faith (up to 25%) will NOT be afforded to the employer.
- In construction inspections, each contractor will be asked to provide its Department of Professional and Occupational Regulation (DPOR) contractor's license AND proof of the DPOR license for any subcontractors.
- Make a referral to DPOR if a contractor has used an unlicensed subcontractor (DPOR sanctions may include fines, probationary terms, suspension or license revocation).
- For contracts under \$1,000, VOSH will make a referral to the Virginia Employment Commission (VEC) and/or the Virginia Workers' Compensation Commission (VWCC) for potential audits of employment practices. Referrals may be made for contract values over \$1,000 as well.

H. The new policy and education and outreach materials can be found at <https://www.doli.virginia.gov/vosh-programs/misclassification-in-the-workplace/>

I. VOSH personnel have also participated in inter-agency enforcement actions with the VEC, the OAG and other members of the Virginia Misclassification Task Force.

Department of Small Business and Supplier Diversity

The Virginia Department of Small Business and Supplier Diversity (SBSD) currently has no defined role regarding the detection, enforcement or prevention of worker misclassification and wage theft in the Commonwealth. To the extent the SBSD can be of assistance in this area or should a future role be defined for the Department by the Governor or the General Assembly, its leadership has participated in the work of the interagency taskforce.

The SBSD mission is the following:

The SBSD's mission is to ensure only bona fide Small, Woman-owned, and Minority-owned Businesses (SWaM), Disadvantaged Business Enterprises (DBE), and Employment Services Organizations (ESO) are certified to participate in Virginia's specialized procurement and contracting opportunities.

Besides Agency Administration the SBSD has three divisions: [Business Certifications](#); [Business Development and Outreach Services](#); [Virginia Small Business Financing Authority](#).

1. The Certification Division is responsible for the administration of Virginia's business certification programs.
2. The Business Development and Outreach Services (BDOS) Division is the economic development arm of the SBSD. BDOS is often the first point of contact for small businesses interested in growing their business by obtaining more information about the Virginia Small Business Financing Authority or learning the marketing advantages of the Commonwealth of Virginia's certification as a SWaM (Small, Woman-owned, or Minority-owned) business and Micro business.
3. The Virginia Small Business Financing Authority (VSBFA) is the Commonwealth's business and economic development financing arm. Aligned within the SBSD, the VSBFA offers programs to provide businesses, not-for-profits, and economic development authorities with the financing needed for economic growth and expansion throughout the Commonwealth.

Department of Professional and Occupational Regulation

Current Efforts

Since January 2015, the Department of Professional and Occupational Regulation (DPOR) has received 330 Virginia Occupational Safety and Health (VOSH) referrals and 23 Virginia Employment Commission (VEC) referrals reporting potential improper hiring of subcontractors.

From those referrals, 225 cases (64%) have been forwarded to the Board for Contractors for disciplinary action. Licensed contractors found in violation of Board regulations may be sanctioned with a monetary penalty not to exceed \$2,500 per violation (Va. Code § 54.1-202). Ninety-six cases were closed administratively and 32 remain open in intake or investigation.

Licensed contractors alleged to have hired an unlicensed or improperly licensed subcontractor may provide proof of payment or similar employment documentation to claim a statutory exemption. As of July 1, 2018, the subcontractor exemption for work performed for licensed building or home improvement contractors is \$5,000 per project, excluding trade-related work (e.g., electrical, plumbing, HVAC, etc.). Unlicensed or improperly licensed subcontractors are notified of the statutory requirements for licensure with the goal of obtaining compliance.

Detection Methods

DPOR has no direct jurisdiction over employee misclassification activities. Entry requirements for occupational licensure generally do not rely on the status of an employer-worker relationship.

Licensed contractors are required to name Designated Employees and Qualified Individuals who, if not members of the firm's responsible management, must be full-time employees (i.e., not 1099 workers). Currently, the agency does not routinely obtain employment or tax documentation as a condition of licensure or otherwise engage in misclassification detection.

Enforcement Authority

DPOR enforces statutes and regulations pertaining to the Department and its regulatory boards under Title 54.1 of the *Code of Virginia*. Its primary mission is to protect the public's health, safety, and welfare by ensuring minimum competency and enforcing standards of practice.

As part of the ongoing Task Force effort, DPOR receives referrals from VOSH and VEC involving unlicensed or improperly licensed contractors discovered in the course of those agencies' on-site inspections. Board for Contractors regulations require licensed contractors to hire only properly licensed subcontractors, unless the project is exempt.

The General Assembly has amended the exemptions each year for three consecutive years: first to clarify that clean-up work does not require any license (Chapter 527 of the 2016 Acts of Assembly); then to exempt subcontractors performing work valued at up to \$2,500 for licensed building contractors (Chapter 132 of the 2017 Acts of Assembly); and most recently to increase the subcontractor exemption amount to \$5,000 and extend it as well to contractors with the home improvement designation (Chapter 767 of the 2018 Acts of Assembly).

Prevention Measures

DPOR continues to promote awareness about employee misclassification on its website. Disciplinary action by the Board for Contractors against licensed contractors, and notification by the Department to improperly licensed or unlicensed subcontractors, may deter continued employee misclassification activity.

Department of Taxation

Current Efforts

The Department of Taxation (Virginia Tax) currently employs several detection and enforcement efforts. In support of the prevention of employee misclassification and payroll fraud, Virginia Tax conducts both desk and field audits.

§ 58.1-103 of the Code of Virginia states that “all records and documents...shall be available during regular business hours for inspection by the Tax Commissioner or his duly authorized agents.” § 58.1-460 of the Code of Virginia defines the terms “employer,” “employee,” and “wages” as used by Virginia Tax. § 58.1-461 of the Code of Virginia requires employers to withhold, and § 58.1-474 makes the employer liable for failure to withhold.

Detection Methods

- Virginia Tax Field Audit staff reviews payroll data of taxpayers during an audit to determine if they have employees liable for Virginia withholding. Discrepancies are most likely to be discovered in the review of taxpayers on bordering states, such as businesses in Tennessee and North Carolina who have employees working in Virginia. Tennessee does not have a state income tax, so they may not withhold any Virginia state income tax, and Virginia Tax does not have reciprocity with North Carolina, so those employers may withhold North Carolina tax in error. Also, with the out-of-state employers, they may properly withhold on Virginia residents, but not on non-residents working in Virginia, or on non-residents who perform work both in and outside Virginia.

To determine misclassified employees and/or contractors, auditors may look at 1099s and determine that the taxpayer has 1099s for several individuals' Social Security Numbers versus businesses with Federal Employer Identification Numbers. A review of payroll-related accounts in the general ledger helps to identify individuals who are receiving payments and other benefits similar to the other employees but who are not having any taxes withheld.

- Virginia Tax Desk Audit staff conducts a match and compare between withholding and the wages reported on the income tax returns filed. For example, an employer may have multiple individual income tax returns with W-2s claiming Virginia withholding from that employer, but the employer is not registered with Virginia Tax for withholding. In that situation we would create an audit case for that employer and send the employer a letter requesting additional information. If the employer cannot verify they are in compliance with Virginia's tax laws or if they do not respond, a bill will be created.

Similar audits are created for under-reporters. For example, if Virginia Tax identifies from individual returns that an employer has withheld \$11,000 in Virginia withholding from their employees but the employer has reported and only paid \$7,000, Virginia Tax creates an audit case and sends the employer a letter. If the employer cannot verify they are in compliance with Virginia's tax laws or if they do not respond, Virginia Tax will create a bill for the discrepancy and interest.

As an audit is conducted, if Virginia Tax identifies an employer who was not in compliance for the year under review, we may expand the audit by looking at prior years to determine if the employer was in business for those years and either not filing or under-reporting Virginia withholding.

Enforcement Authority

In both cases, if anomalies are identified, the agency notifies the taxpayer of the discrepancy and allows them to provide supporting documentation. If supporting documentation cannot be obtained or no response is received, Virginia Tax will create an assessment and bill the taxpayer based on available information. This assessment compares what has been reported versus what can be determined from a taxpayer's payroll records. If Virginia Tax discovers that a taxpayer has underreported their withholding or misclassified one or more employees for the current year, a more in-depth review of previous tax returns going back at least 3 years may be conducted.

As mentioned in a previous section, § 58.1-461 of the Code of Virginia requires employers to withhold, and § 58.1-474 makes the employer liable for failure to withhold. § 58.1-475 imposes a penalty — 6% per month up to a maximum of 30% — for employers who fail to withhold or to remit amounts withheld. (Virginia Tax typically does not assess a penalty on first audits for failure to withhold, but it does if tax has been withheld and not remitted.) § 58.1-308 provides that if the failure to pay tax is false or fraudulent with the intent to evade that tax, a fraud penalty of 100% shall be assessed together with interest on the tax from the time the return was required by law to be filed until paid. § 58.1-312 states that the tax can be assessed at any time if a false or fraudulent return is filed with the intent to evade tax. (However, Virginia Tax usually limits its audits to a maximum of six years.) § 58.1-485 provides that willful failure by an employer to file a required return, withhold the required tax, or pay the required tax is a Class 1 misdemeanor. § 58.1-485.1 makes it unlawful to knowingly and falsely claim an individual's employment status for the purpose of evading the withholding of taxes required; a violation of this section is also punishable as a Class 1 misdemeanor.

Virginia has a Taxpayer Bill of Rights that guarantees taxpayers certain rights in their contacts with Virginia Tax. If a taxpayer does not agree with the amount owed, the method used to compute the balance due, or Virginia Tax's interpretation of tax law or agency policy, that taxpayer has the right to appeal. In the appeals process, a taxpayer has the right to:

- Receive simple and non-technical information about informal reviews and formal appeals, as well as the taxpayer's rights in those processes;
- Receive an informal review when a taxpayer disagrees with a bill or with the denial of a refund;
- Appeal the case to the Tax Commissioner and request a formal ruling if a taxpayer disagrees with the finding of an informal review or if the taxpayer chooses not to request an informal review;
- Appeal the bill to a circuit court if the taxpayer disagrees with the decision of the Tax Commissioner in his or her case;
- File a protective claim with the Tax Commissioner to protect the taxpayer's right to claim a refund of taxes paid in error; and
- Request an offer in compromise to seek full or partial relief from the amount assessed.

To protect a taxpayer's rights of appeal, the taxpayer is responsible for requesting explanations and informal reviews as early in the assessment process as possible. If the taxpayer chooses to file a formal appeal to the Tax Commissioner, he or she must do so no later than 90 days after the date of assessment. Taxpayers may not file a formal administrative appeal of an assessment more than 90 days after the date of assessment, even if the bill remains unpaid.

Prevention Measures

Virginia Tax has also collaborated on two Virginia Employment Commission (VEC) led pilot projects (2015 and 2017) to identify Misclassifications and Payroll Fraud. Virginia Tax received employer data from previous VEC audits to determine potential tax audits to conduct. Some of the types of businesses and industries we assessed in the VEC pilot referenced above included construction, restaurants, trucking, movers, private bus lines, physician/dentists, cab drivers, towing truck drivers, adult care, and landscaping. While there is potential to mitigate misclassification and payroll fraud risk, the process to transfer data was highly manual, lacked sufficient detail, and the cost/benefit analysis of dedicating audit staff to this effort was not an effective use of resources. This pilot could be more beneficial in the future in the event of more structured, thorough and timely transferring of VEC data.

Office of the Attorney General

Current Efforts

Misclassification of employees potentially violates a number of laws. The Office of Attorney General (“OAG”) has worked with the Virginia Employment Commission (VEC) in the past several years, utilizing both civil and criminal avenues in an attempt to abate misclassification practices and prosecute offenders. OAG prosecutors are working with VEC investigators to determine the viability of prosecutions around the Commonwealth.

Detection Methods

The OAG does not employ investigators for the purpose of detecting misclassification but rather relies upon the VEC investigators.

Enforcement Authority

OAG attorneys provide legal representation to agencies impacted by misclassification, such as the VEC, Virginia Department of Taxation, and the Virginia Workers’ Compensation Commission. In addition, the OAG has a prosecution section, the Major Crimes & Emerging Threats Section, that employs a number of prosecutors who prosecute crimes set forth in Virginia Code §§ 2.2-511 and 19.2-215.10. However, the OAG has no direct legal enforcement authority over misclassification-related crimes and works with Commonwealth’s Attorneys to pursue prosecution of such crimes in a particular jurisdiction.

Prevention Measures

The OAG Civil Division conducted investigations into several companies. The underlying theory stems from the fact that, by misclassifying their employees, contractors have failed to provide workers' compensation insurance for all of their employees. Failure to properly insure every employee could cause insurance companies to improperly certify that the contractors are in compliance with Virginia's workers' compensation insurance requirements. Therefore, it potentially results in Virginia collecting less tax revenue than it otherwise should. While no formal cases have been brought, our efforts in this regard have brought greater awareness of the problem to businesses operating within the Commonwealth.

Second, as mentioned above, OAG criminal prosecutors are actively engaged with VEC investigators and commonwealth’s attorneys in an effort to prosecute misclassification-related crimes and serve as a deterrent for future crimes.

APPENDIX II – Taskforce and Stakeholder Directories

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Chief Workforce Advisor	Hon. Megan Healy	Deputy Chief, Jane Dittmar Jane.dittmar@governor.virginia.gov

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Labor Organizations

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Stephen Courtien,	President & Executive Director	Scourtien@bdcbt.org

Building & Construction Trades (DC, MD, VA)		
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UBC		
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Business Organizations

Organization	Name	Position	Email
Alliance for Construction Excellence	Andy Porter	ED	aporter@wdcneca.org
American Association of Occupational Health Nurses - VA	Sharon Elliott	President - VA	sharonelliott@ups.com
American Industrial Hygiene Association	Sue Marchese	Communications	smarchese@aiha.org
American Society of Safety Engineers - VA Chapter	Courtney Malveau	Gov. Affairs	ga@colonialva.assp.org
American Subcontractor's Association - VA (Metro DC)	Ike Casey	ED	ike@asamw.org
Associated Builders and Contractors of Virginia	Patrick Dean	President - VA	pat@abcva.org
Associated General Contractors of Virginia	Gordon Dixon	ED	gordon@agcva.org
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National Federation of Independent Businesses - Virginia	Nicole Riley	State Director	nicole.riley@nfib.org
Old Dominion Highway Contractors Association	Jonathan Williams	ED	jonathan.williams@easter.associates.com
Old Dominion Highway Contractors Association	Ben Dendy	Lobbyist	bdendy@vectrecorp.com
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Virginia Beer Wholesalers Association	Philip Boykin	Pres. CEO	phil.boykin@vbwa.org

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Virginia Council of CEO's	Scott McRoberts	CIO	smcroberts@vaceos.org
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Virginia Dairyman's Association	Eric Paulson	ED	info@vsdaonline.com
Virginia Distillers Association	Amy Ciarametaro	ED	amy@virginiaspirits.org
Virginia Farm Bureau	Andrew Smith	Gov. Affairs	Andrew.Smith@VAFB.com
Virginia Farm Bureau	Martha Moore	Gov. Affairs	Martha.Moore@VAFB.com
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Virginia Healthcare and Hospital Association	Sean Connaughton	President	sconnaughton@vhha.com
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Virginia Manufactured and Modular Housing Association	Randy Grumbine	ED	randy@vammha.org
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Virginia Bar Association	Yvonne Cockram	Executive Director	ycockram@vba.org
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Other Government Organizations

ORGANIZATION	NAME	TITLE	EMAIL
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