STATEMENT OF
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U.S. DEPARTMENT OF LABOR
BEFORE THE
SUBCOMMITTEE ON WORKFORCE PROTECTIONS
AND
SUBCOMMITTEE ON HEALTH, EMPLOYMENT, LABOR, AND PENSIONS
COMMITTEE ON EDUCATION AND LABOR
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Chairwoman Woolsey, Chairman Andrews, Ranking Members Wilson and Kline, and distinguished members of the Subcommittees:

Thank you for the opportunity to discuss the efforts of the Department of Labor's Wage and Hour Division (WHD) to promote compliance with the Nation's labor standards laws. WHD has a strong record of enforcement on behalf of workers in this country, including employees who have been misclassified as independent contractors.

WHD employs a number of strategies for ensuring that employees are paid in accordance with the laws WHD enforces. Many of these strategies address worker classification issues. Before discussing these strategies, however, it is important to understand the backdrop against which these strategies are implemented. The misclassification of an employee as an independent contractor is not itself a violation of the Fair Labor Standards Act (FLSA) or the many other laws that WHD enforces. The Government Accountability Office (GAO) acknowledged this fact in its 2006 audit, *Employment Relationships: Improved Outreach Could Help Ensure Proper Worker Classification (GAO-06-656)*. In that report, GAO also accurately noted that, despite the fact that such misclassification is not a violation of the FLSA, WHD nevertheless detects and addresses the issue of employees who have been misclassified as independent contractors in its investigations of employer compliance with the FLSA. It is critical to understanding WHD's approach to enforcing the provisions of the various statutes for which it is responsible that one also understand that the act of misclassification is not a violation of the FLSA.

Determining An Employment Relationship Under The Federal Wage And Hour Laws

Under most labor standards laws, an employer-employee relationship must be established in order for the law's provisions to apply. The FLSA, which establishes minimum wage, overtime, and child labor protections, defines "employee" more broadly than virtually any other federal statute. In cases such as *Rutherford Food Corp. v. McComb*, 331 U.S. 722 (1947), *United States v. Silk*, 331 U.S. 704 (1947), and *Bartels v. Birmingham*, 332 U.S. 126 (1947), the U.S. Supreme Court provided guidance for determining whether a worker is an employee under the FLSA, and those rulings continue to inform how WHD and the courts analyze the issue today. The Court provided that an employee, as distinguished from a person who is engaged in a

business of his or her own (*i.e.*, an independent contractor), is one who, as a matter of economic reality, is dependent on the business that he or she serves.

The Court further indicated that there is no single rule or test for determining whether an individual is an independent contractor or an employee for purposes of the FLSA. Instead, the determination must be based on the totality of the circumstances and not on a single criterion. The relevant factors include the following:

- The extent to which the services rendered are an integral part of the principal's business;
- The permanency of the relationship;
- The amount of the alleged contractor's investment in facilities and equipment;
- The nature and degree of control by the principal;
- The alleged contractor's opportunities for profit and loss;
- The amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor; and
- The degree of independent business organization and operation.

See, e.g., *Silk*, 331 U.S. at 716; *Brock v. Mr. W Fireworks*, 814 F.2d 1042 (5th Cir. 1987); *Donovan v. DialAmerica Mktg.*, 757 F.2d 1376 (3d Cir. 1985).

I mention these specific factors for two reasons. First, all WHD investigators must use these criteria to establish an employment relationship to pursue remedies on behalf of workers under most of the statutes the agency enforces, including the FLSA and the Family and Medical Leave Act (FMLA). As a consequence, investigators will, at various stages throughout the investigation, examine how an employer classifies its workers. For example, investigators will ask for information during the initial conference with an employer to establish the employer's classification practices. Investigators will review records including without limitation payroll records, cash disbursements journals, check registers, and 1099s to ensure that all workers are identified and that any worker not listed on the payroll is properly compensated. As a normal part of investigations, WHD investigators will tour an employer's establishment and question workers about their pay, their duties, and their working conditions, as well as those of their co-workers, looking for, among other things, potentially misclassified employees. As GAO noted in its audit, when WHD investigators suspect that employers are not properly classifying workers as employees, the investigator will pursue several avenues of investigation to ascertain whether a violation of a wage and hour statute has occurred.

The second reason for highlighting the FLSA employment relationship factors is to distinguish these criteria from the test used by the Internal Revenue Service (IRS) in applying the common law "right to control" test often used by the courts and from the definitions and standards set forth in other statutes. WHD acknowledges that the issue of employee misclassification raises a number of concerns wholly outside the responsibility or authority of

WHD. The misclassification of workers may affect some state programs such as worker compensation and unemployment insurance programs, in addition to other federal and state worker protection statutes. Finally, misclassification issues may involve the IRS and the Social Security Administration.

Consequently, in establishing an employment relationship under the FLSA, there may be instances where WHD investigators identify potential misclassification issues of other programs or statutes. WHD has no authority or expertise, however, to interpret or to enforce provisions outside its jurisdiction. In many instances, the misclassification of a worker under the FLSA will not, given the broad interpretation of the FLSA, result in a violation of another statute or program.

WHD Strategies For Enforcing Labor Standards Provisions Relating To Independent Contractor Issues

The labor standards that WHD enforces provide basic protections for all workers in this country. Although they differ in scope, all of the statutes enforced by WHD are intended to protect the welfare of the Nation's workforce and to ensure fair compensation for work performed. Minimum wage, overtime, and child labor cases constitute the majority of WHD's enforcement responsibilities. FLSA cases represent approximately 84 percent of all WHD cases, and FMLA investigations an additional one percent. The Migrant and Seasonal Agricultural Worker Protection Act (MSPA), the Davis-Bacon Act (DBA), and the McNamara-O'Hara Service Contract Act (SCA) are other key statutes enforced by WHD.

Misclassified workers may be identified during the course of investigations that cover many provisions and statutes enforced by WHD. For example, WHD investigators must establish an employment relationship under the FMLA and most of the MSPA provisions. Investigations into compliance with these program areas necessarily contain an element of inquiry into the status of workers as employees.

Under DBA and SCA, however, WHD does not need to establish such an employment relationship. According to the statutory language of the DBA, laborers and mechanics are entitled to prevailing wage rates "regardless of the contractual relationship that is alleged to exist between a contractor or subcontractor and such persons." Similar language applies to service employees performing on Federal service contracts. Under these two statutes, the individuals performing work are entitled to prevailing wage and fringe benefit compensation even if they are classified as independent contractors.

Because erroneous classification of an employee as an independent contractor is not itself a violation of the federal wage and hour laws, WHD does not maintain data regarding how many cases present that issue. Thus, WHD cannot provide statistics regarding the prevalence of misclassification. However, there have been instances in which a misclassification resulted in a minimum wage or overtime violation. These cases clearly demonstrate WHD's attention to potential violations that may result from the improper designation of workers. The following are some recent examples:

- In November 2006, WHD collected nearly $75,000 in back wages for 76 employees of an Ohio construction contractor that had misclassified its workers as independent contractors.

- In October 2006, a Houston construction company paid nearly $130,900 in back wages to 81 employees who had been misclassified.

- The Department sued a Houston drywall company in August 2006, to recover over $500,000 in back wages on behalf of misclassified employees who were working to rebuild the Mississippi Gulf Coast casinos following Hurricane Katrina.

- In a similar case involving the employees working to rebuild the Gulf Coast region, WHD collected over $362,000 in back wages from three construction firms that had misclassified employees as independent contractors.

- In March 2006, the Department sued a Glendale, California, janitorial company for $900,000 in back wages that resulted from the company's improper practice of classifying the workers as independent contractors.

WHD has, for a number of years, prioritized its statutory enforcement responsibilities to maximize protections for workers, including the most vulnerable in the workforce: low-wage, immigrant, and young workers. WHD receives approximately 30,000 complaints during a fiscal year and utilizes approximately 70% to 78% of the program's enforcement resources to resolve complaints. In addition to its responsibilities to respond to allegations of noncompliance, WHD has devoted between 22% and 30% of its enforcement resources to targeted investigations (*i.e.*, investigation initiated without a complaint), the focus of which is in low-wage industries that employ large numbers of vulnerable, low-skilled workers.

These industries, such as construction, janitorial, restaurants, landscaping, agriculture, garment manufacturing, and health care, are often characterized by the employment of immigrant workers who are particularly vulnerable to exploitation, as well as young workers who are not fully versed in FLSA protections. Investigations in these industries tend to disclose high rates of FLSA minimum wage and overtime violations. Moreover, it is the experience of WHD that undocumented workers, many of whom may have been misclassified as independent contractors or have been engaged in contingent employment relationships, account for an increasing percentage of employees in these industries.

WHD initially focused its low-wage program on the three nationally targeted industries of garment manufacturing, agriculture, and health care. While compliance efforts continue in those identified industries, in FY 2004 WHD began expanding its low-wage program to include a broader group of identified low-wage industries. Working with external evaluators, WHD identified approximately 33 low-wage industries in which workers were most likely to be the subject of a minimum wage or overtime violation. This research enabled the agency's local and regional offices to identify and to target in their geographic areas industries with the most serious compliance issues.

In FY 2006, WHD collected nearly $50.6 million in back wages for approximately 86,700 workers in nine of the larger group of low-wage industries, an increase in back wages collected in the same low-wage industries of over 10% as compared to the previous fiscal year. Over a third of WHD enforcement resources are attributed to investigations in nine low-wage industries, which include day care, restaurants, janitorial services, landscaping, and temporary help. This fiscal year, WHD is conducting over 100 initiatives in low-wage industries. These compliance initiatives are concentrated in restaurants, retail, construction, janitorial, hotels and motels, and health care. WHD offices in garment manufacturing centers are continuing their enforcement efforts to increase compliance in that industry. WHD offices also have enforcement and compliance assistance activities in agriculture and reforestation. Again, these industries share common characteristics with the industries in which employees are most likely to be misclassified as independent contractors.

As a complement to its enforcement activities, WHD has an active compliance assistance program that takes advantage of opportunities to educate employers and employees about the laws that it enforces. WHD outreach to the employer and employee community is a critical component of its overall compliance program because it aims to ensure that employers have information on the statutory and regulatory requirements in a clear and concise manner and that employees are versed in their rights and the remedies available to them. In its 2006 audit, GAO acknowledged WHD's outreach to workers and to employers on employment relationship concepts and the agency's procedures for its field staff in identifying and reporting potential misclassification issues to other Federal agencies.

Among the examples of compliance assistance information noted by GAO is *Fact Sheet 13: Employment Relationship Under the Fair Labor Standards Act (FLSA)*, which describes the factors involved in determining whether an individual is an employee under the FLSA and where to find additional information or help in making such a determination. This fact sheet is available in Chinese, Korean, Spanish, Thai, and Vietnamese, as well as English. The Employment Relationship fact sheet and others like it, including various industry specific fact sheets, are available on WHD's web site. The Employment Laws Assistance for Workers and Small Businesses (***elaws***) FLSA Advisor, also on the web site, is another tool that provides an interactive mechanism for employers and workers to determine whether a worker is an employee under the FLSA.

In addition to these electronic and printed materials, WHD field personnel participate in a variety of outreach activities such as seminars, training programs, and community-based activities, including Spanish-language radio and television programs. WHD distributes worker rights cards to day laborers, health care workers, garment workers, and farmworkers, among others, in order to inform workers of their rights and to prevent misclassification from happening in the first place.

To further increase awareness of relevant labor laws, to encourage greater employer compliance with those laws, and to assist vulnerable workers in achieving the protections to which they are entitled, WHD has also developed strategic partnerships and collaborations with businesses and trade associations; labor unions; federal, state and local government agencies; faith- and community-based organizations; and foreign agencies. Just one example is the *Justice and Equality in the Workplace Program* established in Houston, Texas, to educate low-wage

immigrant and non-immigrant workers about their rights under federal law and to bring the employers of these workers into compliance through education and enforcement.

In summary, WHD balances three complementary strategies—compliance assistance, partnerships and collaborations, and strong complaint-based and targeted enforcement—to promote and achieve compliance on behalf of all employees, including those who have been misclassified as independent contractors.

WHD Response To GAO Recommendations
To Improve Outreach To Facilitate Proper Worker Classification

As mentioned previously, GAO examined WHD's role in identifying and addressing instances in which workers were misclassified as independent contractors. While recognizing WHD's efforts in addressing instances of worker misclassification under the FLSA, GAO had two recommendations for WHD. Both have been addressed by WHD.

First, GAO recommended that because WHD's enforcement program was primarily complaint-based, the FLSA poster should be modified to provide additional contact information. This revision was intended to facilitate the reporting of possible misclassification complaints that also alleged minimum wage or overtime violations. WHD agreed with the recommendation, and the new FLSA poster prominently displays the agency's toll-free number and web site address. Calls to the toll-free number are answered by call center staff who refer complainants to the appropriate WHD local office. The call center has Spanish-speaking customer service representatives and an interpreter service that supports 150 languages.

Second, GAO recommended that WHD evaluate the extent to which misclassification cases identified through FLSA investigations are referred to the appropriate federal or state agency potentially affected by employee misclassification, and take action to make improvements as necessary. GAO also suggested that WHD build upon efforts by its district offices currently engaged in such referrals. Finally, GAO indicated that any referral of cases should include notifying the employer that the misclassification case has been forwarded to the appropriate agency.

WHD agreed with GAO that there is value in sharing potential employee misclassification with appropriate federal and state programs. As a result, WHD reviewed its internal processes for referral of potential employee misclassification to other agencies with all first-line field managers during a national managers training conference in May 2007. To ensure that all WHD district offices refer employee misclassifications that could lead to potential violations of laws enforced by other agencies, the first-line managers were reminded to follow the agency's longstanding Field Operations Handbook instructions and to refer such violations using the established form WH-124.

We believe that an explicit policy of automatic referrals to all other agencies, however, could have an adverse impact on WHD's mission and ultimately harm those workers whom the agency is tasked with protecting. If it becomes common knowledge that WHD routinely refers potential violations to some agencies it would hinder the agency's ability to persuade employees to report violations of the wage and hour laws or otherwise voluntarily provide workplace

information. Moreover, employers would be less likely to produce copies of written documents or records if they believed such documents were going to other law enforcement authorities for reasons unrelated to the labor standards investigation. As a result, WHD would be required to compel the release of information through the courts, a timely and costly means of enforcing federal labor standards. In addition, because the definition of "employee" under the FLSA is more inclusive than the definition used in many other statutes, a determination of misdesignation of an employee as an independent contractor by WHD may not be applicable for other purposes. Accordingly, WHD disagrees with GAO that referral is appropriate in all instances and believes that determinations as to whether to refer a matter to another agency must be made after considering the particular circumstances. In terms of the worker protections that WHD is trying to ensure, there are tradeoffs in reporting to other agencies, and whether or not reports are made represents the outcome of a balancing of benefits and costs for the workers the agency is trying to help.

WHD also does not agree with GAO's recommendation that employers be notified when WHD refers potential misclassification cases involving laws not enforced by the WHD to another agency. As WHD explained, this type of process would place WHD staff in the untenable position of explaining or defending a referral based upon interpretations of laws concerning which WHD has neither expertise nor interpretive or enforcement authority.

Future WHD Compliance Activities

Over the last several years, WHD has planned a number of compliance initiatives in low-wage industries to address the more common violations, such as off-the-clock violations and misclassification of executive, administrative, and professional employees as exempt personnel. In support of its compliance priorities in low-wage industries, WHD's FY 2008 performance plan focuses on addressing the violations that may arise from employment relationships not designated as such, especially those involving contingent workforces, misclassified employees, and subcontracting structures. Each of the agency's regional and local district offices' low-wage initiatives will include compliance activities in at least one of the low-wage industries in which independent contractor misclassifications are common. WHD is committed to promoting compliance in low-wage industries and to ensuring that the designation of workers as independent contractors does not result in violations of the labor standards laws that we enforce.

Madam Chairwoman, Mister Chairman, this concludes my prepared remarks. I will be happy to answer any questions that you or the Members of the Subcommittee may have.