

Joint Legislative Task Force on the Underground Economy in the Construction Industry
Responses to Proposed Recommendations (November 19, 2007)

	BUSINESS and LABOR TASK FORCE MEMBERS		AGENCY LIAISON MEMBERS		
	BUSINESS	LABOR	ESD	L&I	REVENUE
1) ENFORCEMENT					
a) Funding					
i) Increase resources – general.	YES	YES	OTHER Increased resources would be beneficial provided they are tied to a funding source and made in conjunction with OFM and the Governor’s Office.	YES See handout.	OTHER Especially helpful for technological improvements for data sharing and project coordination.
ii) Increase judicial system funding.	YES	YES		YES See handout.	OTHER Would depend on how intended to use in what capacity, need more information.
iii) Give agencies incentive money.	YES Supportive, but enhanced accountability for agency efforts needed, too. See 6) c) below	YES Possible, depending on deliverables by the agencies.		OTHER This item needs to be fleshed out in order to respond.	OTHER DOR would prefer to not tie collections and enforcement to funding mechanisms which may create unintended consequences.
iv) Earmark penalties collected to fund more staff.	OTHER Generally supportive of enhanced revenue, but not only restricted for more staff. Resources are needed for increased salaries for existing staff; education and outreach efforts; and electronic data sharing.	YES I think this is a critical element of what needs to be done.	NO In 2007, the Legislature enacted SHB 1407, ESD’s request bill to increase the flexibility of funding unemployment insurance administration, including use of funds from penalties. ESD needs to retain flexible funding rather than earmarking penalties for a specific purpose.	OTHER There are potential issues with FTE allocation and restrictions by using this method. More details would be needed for the agency to respond.	OTHER If a legislative directed enforcement program is developed it would require additional funding.
b) Auditors					
i) Improve recruitment, retention, and training.	YES	YES	YES	YES We are actively working with the Dept. of Personnel on recruitment and retention issues.	YES In conjunction with interagency effort for recruitment and retention.
ii) Create apprenticeship program for auditors.	YES	YES If needed they have training now but for the sake of being on	OTHER Participate in the pilot project on this issue which was	OTHER We already have an approved apprenticeship	OTHER In conjunction with pilot program to determine

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		the Apprenticeship and Training Council I will say yes.	recommended in the attached Final Report on Auditor Recruitment & Retention Assignment for the Governor's GMAP - Economic Vitality Accountability Forum.	program in place, as well as in-training alternatives, and a formal training plan to bring auditors up to a journey level.	effectiveness.
iii) Increase pay scale.	YES Enable successful competition with private sector. Simple salary enhancements may not be the only approach. Examine the use of incentive based compensation schemes (i.e., collection activities) where appropriate.	YES It sounds like this is the major problem in terms of retention.	YES. ESD is part of the Interagency Work Group that submitted the attached Final Report on Auditor Recruitment & Retention Assignment for the Governor's GMAP - Economic Vitality Accountability Forum.	YES. We are actively working with the Dept. of Personnel on recruitment and retention issues.	YES In conjunction with interagency effort for recruitment and retention.
iv) Create a joint multi-agency state-wide collections unit.	OTHER Consolidation of units may not be needed. Better coordination of agency efforts may be more productive. Coordinated audits (using separate teams and criteria, but conducted at the same time); clarify and coordinate approaches to recovering monies due to separate programs, but sought from a potentially limited resource (distressed business).	YES	NO ESD supports a coordinated interagency approach for enforcement and collection in targeted cases, but not a joint unit for day-to-day operations.	NO ⁱ	NO Believe that there exists significant differences in agency statutes, taxpayer base and roles and would be less effective than current structures.
v) Separate audit and collection functions.	OTHER Generally supportive of greater focus for job duties; could lead to agreement to separate functions.	YES/OTHER Where needed - by collective activities wherever possible.	NO ⁱⁱ	OTHER This appears to apply to ESD only, as L&I already separated those functions years ago. That separation was effective, and increased production of both programs.	OTHER Dept. of Revenue has separate functions currently.
c) Data					
i) Improve data sharing by identifying barriers and making changes where necessary.	YES	YES I think this is another key area we need to address.	YES See handout.	YES The agencies are meeting before the 19 th to explore barriers.	YES
ii) Improve access to third party records. (<i>Miles</i> case)	YES Care must be taken to build in protections against abuse of agency	YES	YES <i>Miles</i> was determined on constitutional grounds; ESD, DOR,	YES This may be difficult, as <i>Miles</i> was a constitutional	OTHER Problematic as this is constitutional issue would

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held that state agencies cannot issue subpoena to a third party (e.g., bank) without prior judicial review and most agencies do not have authority to seek judicial review.)	discretionary authority.		and L&I will collaborate with the Attorney General's office on this issue to develop an appropriate response.	issue. We are currently working with the AG's office to explore options, and will coordinate with ESD and DOR as well.	need more specifics regarding how to incorporate <i>Miles</i> decision into changes. Recommend agencies work with AG to determine impacts and limits of <i>Miles</i> jointly.
iii) Address other difficulties of gaining access to financial information – e.g., record retention limitations, difficulty of identifying records or possessor of records.	YES	YES	YES Further collaboration and study is still needed. ESD is interested in partnering with other agencies on this issue.	YES Clearing barriers to information sharing between state agencies and with local government entities is important. More specific details are needed about this item.	OTHER Need more clarification.
d) Local governments					
i) Require local governments to notify L&I of construction activity.	YES Notification of issuance of building permits allowing state agencies to flag some for early investigation may help; criteria should be established.	YES	OTHER Defer to L&I.	OTHER From a data-sharing standpoint for enforcement targeting on our end, this could be helpful, but funding would need to be secured for those local government entities to ensure that this would not be a new and unfunded mandate.	OTHER Would be supportive of any program that would create statewide database on building permit information. Funding would be required to assist locals in this effort.
ii) Provide an incentive to local governments for enhanced education/enforcement.	YES Revenue sharing or other resource considerations could help. ** Another possibility would be to require local governments to verify state compliance with registration and other requirements prior to issuing any local business license.**	YES/OTHER Possibly, depending on the training and benchmarks.	OTHER Defer to L&I.	YES	YES
iii) Require subcontractors to be identified in permitting process.	NO Not a workable approach.	YES	OTHER Defer to L&I.	OTHER This may be very difficult to implement, as subcontractors are typically not known at the time of issuance of the permit.	OTHER Defer to L&I on this issue, but unlikely this information is available at permitting. See (d)(i).
iv) Make changes to allow	OTHER Could be a possibility;	YES	YES This assumes the AG's office	OTHER Our agency works	YES

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agencies to more easily prosecute their own cases.	enhanced enforcement tools and increased AAG staff may help.		would prosecute, not ESD.	through the AG's office for prosecution of cases that are not taken up by local jurisdictions.	
2) OUTREACH AND EDUCATION					
a) General					
i) Enhance education and outreach.	YES Foundational to effectiveness of any other effort.	YES	YES	YES. See handout.	YES
ii) Involve local government.	YES Explore practical options for identification of situations suggesting heightened attention.	YES	OTHER Defer to L&I.	YES More details are needed on this item.	YES
b) Consumer education					
i) Identify strategies to educate consumers, including creating a list of questions consumers should be encouraged to ask contractors.	YES Include plain talk about perils to consumers if they don't pay attention, or intentionally try to take advantage of the system.	YES	OTHER Defer to L&I.	YES Our contractor registration and compliance program already does work regularly to produce information for consumer, including periodic media coverage. If more is desired in this area, funding would be necessary.	OTHER Defer to L&I as lead agency on this issue.
ii) Air public service announcements about homeowners who have been harmed.	YES	YES , but I'm not sure how much good it will do.	OTHER Defer to L&I.	YES See (b)(i) above. These can be useful, but we compete with any other entity for this free airtime, which can often be at the wrong time of day to target the audience we are trying to impact.	OTHER Defer to L&I as the lead agency on this issue.
iii) Encourage the media to get involved with their consumer protection segments on their newscasts.	YES Provide PSA and other type materials which can be easily used by media, especially in smaller communities, where receptiveness for copy may be better.	YES	OTHER Defer to L&I.	YES. See (b)(i) above. Both TV and newsprint media tend to cover these issues with our assistance on a periodic basis, either through specific "horror stories," or general "here's how to protect yourself" pieces.	OTHER Defer to L&I as the lead agency on this issue.

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c) Other					
i) Provide information on what happens if persons do not follow the rules.	YES See b) i) above	YES	YES	YES	OTHER Defer to L&I as the lead agency on this issue.
ii) Find ways to encourage legitimate contractors and the public to report fraud.	YES	YES	YES	YES	OTHER Defer to L&I as the lead agency on this issue.
3) PENALTIES					
a) General					
i) Provide an incentive and penalty system for enforcement that leads to greater compliance and encourages all levels of the contracting system to conduct due diligence with subcontractors.	YES	YES	YES Depends on the specific proposal. In general, ESD supports holding a prime contractor liable if it does not exercise due diligence with its subcontractors, but this depends on the definition of "due diligence." The system should not unfairly burden legitimate businesses.	YES What would incentives look like? That portion may need more detail.	NO Department has strong penalties in place for failing to file and report taxes. 50% for evasion, up to 30% for failure to register, 25% for failure to file and interest on all taxes. Main issue for DOR is resale fraud which has 50% automatic penalty. We believe these are sufficient. Additional penalties, we believe, will not increase compliance.
a) Degree and types of penalties					
i) Make penalties stronger. How do you suggest making penalties stronger?	YES Publicize imposition of penalties, identifying those penalized. Include mandatory training requirements before registration/licensure reinstated.	YES	YES It would be helpful to have greater flexibility in penalties, ranging up to the ultimate authority in extreme cases to close down a business which disregards the law and continues to operate in defiance of requirements. This would be similar to L&I's and DOR's current authority.	YES. See handout.	NO. See a)i) above.
ii) Make penalties high.	YES Must find a balance, though, that doesn't result in driving people further underground.	YES	OTHER See b)i).	YES This appears to be the same as b)i).	YES. See a)i) above.
iii) Create penalties for	YES Care must be taken to not	YES	OTHER Defer to L&I.	NO	OTHER Homeowners are

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homeowners who intentionally do not follow the rules.	overly emphasize "intentionally" -- strengthening the incentive for homeowners to pay attention.				currently penalized for failing to pay appropriate sales and use taxes.
iv) Create penalties for falsifying information on contractor registration documents.	YES	YES	OTHER Defer to L&I.	YES See handout.	OTHER Already have this authority for evasion and gross misrepresentation.
v) Create penalties for persons who accept cash for payment.	YES Penalties should be established for those who offer and accept undocumented cash payments.	YES	OTHER Create penalties for untraceable record-keeping.	OTHER The issue is not cash payment, but record-keeping. Cash is a valid form of payment if the bookkeeping is properly handled behind it. There are penalties for failure to keep records and for willful misrepresentation. We also have statutory authority to hold final assessments where a firm does not have or will not provide records.	OTHER May be constitutional concerns.
vi) Create criminal penalty for contractor who intentionally and willfully reports that an employee is an independent contractor.	OTHER Not necessarily opposed, but this is part of the larger "Independent Contractor" issue discussion.	YES This is another issue that I think is a priority.	YES ESD supports criminal penalties for repeatedly misclassifying employees as independent contractors. However, as the standard of proof in a criminal case is 'beyond a reasonable doubt,' it would be very difficult to prove that employers acted 'intentionally and willfully.'	OTHER This appears to already be in place. There is a civil and matching criminal penalty for willful misrepresentation of industrial insurance premiums due. The independent contractor angle is just one method by which firms do that. The "willful" part is difficult to prove, versus misunderstanding of the law. It often requires previous interaction by the agency to educate and continued action by the firm, or more egregious actions by the employer.	OTHER Not applicable to DOR as they would be taxable under RCW 82.32 if independent contractor.

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vii) Provide contractor registration penalties for person convicted under vi).	YES As long as criteria are clear.	YES	OTHER Defer to L&I.	OTHER More detail is needed in order to respond.	OTHER Defer to L&I as lead agency.
4) DEFINITIONS					
a) Create one statutory definition of independent contractor for L&I; ESD; and DOR. How should independent contractor be defined?	OTHER Needs more discussion.	YES One way would be placing the currently used tests in statute, and work with the agencies to define how these could be made clearer or streamlined with better definition. There is also an issue with having the complete 6 part test used by L&I and ESD apply toward DOR. If we cannot make the statute uniform we should try and make it as consistent as we possibly can. Other states have created statutory definitions that we should consider in terms of how they could apply to Washington State Law.	YES ESD is meeting with business, labor, and other agency stakeholders to explore a single definition.	YES A subcommittee has formed to discuss this matter, and see if opportunities exist to increase clarity.	NO Not necessary as currently taxable, would not support specific definition that might lead to loophole in requirement to report excise taxes.
b) Provide for clear, consistent cross-agency definitions.	OTHER If that is possible. Emphasis may be more appropriately placed in assuring that there aren't unintended contradictions, gaps or "Catch 22s."	YES	YES	YES See a).	OTHER Defer to ESD employee definition.
c) Change reference to IRS test (IRS test has changed so contractors can no longer meet this criteria).	YES	YES	NO IRS home-office rules have changed and are not highly restrictive. This test is currently part of the uniform 6-part test which both L&I and ESD use, but merely as an alternative qualification. Replacing this part of the test would impact independent contractors outside of the construction business.	OTHER Unless other sweeping changes were made to the test that ensured that covered workers were not removed from workers' comp. This test has actually become much easier over the years, not more difficult.	OTHER Defer to ESD and L&I.
d) Make test more clear. Specify how.	OTHER Part of the larger discussion.	YES	YES ESD is considering developing and publishing	YES Clarify is important, and if changes could be made that	OTHER Not applicable to DOR.

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			guidelines on independent contractor status for specific industries.	would increase clarity without easing the test and removing covered workers from the system, we would welcome them. The sub-committee is working on this issue.	
e) Create independent contractor criteria.	OTHER Part of the larger discussion. However, increased educational and outreach efforts on this matter will help.	YES	OTHER See d) above.	OTHER This may or may not be required, and if reviewed, should be looked at with the current definition of covered worker vs. exempt from coverage.	NO Currently taxable under excise tax definition.
5) CONTRACTOR REGISTRATION/LICENSING a) Requirements for registration/licensure					
i) Require a competency test. What should the test cover?	OTHER Could be a possibility in the future. Short term, any consideration of this matter should focus on statutory requirements.	YES Knowledge of state contracting, WACs, RCWs and responsibilities of contractors and subcontractors.	OTHER Defer to L&I.	OTHER While we support strengthening the laws from contractor registration to some form of licensure, there may be an interim step that requires education prior to licensure and ongoing education on the laws but no testing.	OTHER Defer to L&I as lead agency.
ii) Require independent contractors to carry workers' compensation (and unemployment insurance) coverage.	OTHER Requires further examination. UC not a realistic option, but WC bears some interest.	YES	NO ⁱⁱⁱ See handout.	NO See handout.	OTHER Defer to L&I as lead agency.
iii) Require a showing at time of registration that contractor meets tests for independent contractor.	NO Registration doesn't equate with "independence" in work activities.	YES This requirement would be a valuable tool for stopping the problem before it starts.	It is important to distinguish between a registered contractor (a type of business under chapters 18.27 and 19.28 RCW) and independent contractor status (a tax determination, which may vary with different contracts, regardless of registered contractor status).	NO This would be difficult if not impossible, to implement. At first registration, the firm isn't really in existence –they haven't done any work for another firm, and wouldn't have any books and records yet. Distinguishing between	OTHER Defer to L&I as the lead agency.

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				contractor registration under RCW 18.27 and 19.28 and workers' compensation requirements under RCW 51 is important.	
b) Outreach/education					
i) Require additional information on contractor registration form.	YES	YES	YES L&I form should refer to ESD by asking for ESD reference number or telling contractor to contact ESD if the contractor has employees and does not have an ES reference number.	YES We will form a work group to look at the form.	OTHER Improve coordination by UBI with revocation and closed account changes and contractor registration data changes.
ii) Provide disclosure that person will not be receiving workers' compensation.	OTHER Providing information about the circumstances which may effect coverage seems to be the practical approach. "One size" does not fit all here.	YES	OTHER Defer to L&I.	YES The work group will look at this. Balancing that communication with our concerns about individuals registering that are truly covered workers that should be able to file for benefits is a detail that needs to be worked out.	OTHER Defer; not applicable to DOR.
iii) Have question on form asking whether the applicant has been asked to be an independent contractor.	OTHER May be helpful, but not always dispositive. If used the question could be added asking who you were asked by.	YES I suspect there are workers that are being told to become independent contractors that don't understand all that is required of them if they do.	YES Should be on master business application form.	YES The work group will review this.	OTHER Defer; not applicable to DOR.
iv) Provide additional training opportunities for contractors and in multiple languages.	YES Prepare web-based, CD or other electronic tools which leverage staff resources.	YES	OTHER Defer to L&I.	YES See handout.	YES DOR currently provides multilingual services.
v) Require contractors (and employees) to have cards in field.	OTHER Merits further examination.	YES particularly if employees are being considered as independent contractors.	OTHER Defer to L&I.	OTHER We would need much more detail on this item in order to respond. It has legal barriers, potential federal issues if employees are required to have them as well, in addition to funding and staffing.	OTHER Defer to L&I.

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vi) Post registration on job site.	YES May have some practical difficulties, but worth consideration.	YES The same process as posting an intent on a prevailing wage project.	OTHER ESD defers to L&I.	YES	YES
vii) Provide more education regarding responsibilities as part of the UBI process.	YES Also include local licensing processes.	YES	YES	YES	YES
6) OTHER					
a) Conduct more research focusing on craft specific or county based underground economy data.	YES	YES It would be helpful to know if this is an issue that is more prolific in particular geographic areas or is it population density that drives it or both.	YES Contingent on availability of funding.	YES This is a worthy goal, but the nature of the underground economy would make this very expensive to implement. Funding would need to be allocated to accomplish this level of research.	OTHER Would need resources to provide additional research beyond current underground data.
b) Provide an option to waive workers' compensation.	OTHER Part of broader discussion.	NO	OTHER Defer to L&I.	NO This would dramatically increase the underground economy, and make compliance nearly impossible. Firms could coerce or force workers into signing this waiver on a mass basis. Even if they had not previously, a firm could easily do so once we initiated an audit.	OTHER Defer.
c) Set benchmarks to measure any recommendations.	YES Benchmarking seems an essential element of success. Measurements should not only focus on efficiency of efforts, but should also emphasize whether the efforts are effective at producing the expected results (ie. did they actually make a difference?). In addition to Performance Audit benchmarking, regular progress reports should be published by the agencies. Perhaps a formal Sunset Review audit should be set up to	YES	YES	YES Some recommendations would be difficult to track from a "results" basis, such as increased education for consumers at the point of sale for a permit or changes to the contractor registration form.	YES

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	provide a comprehensive and inter-related review of whatever is implemented.				
d) Create employee reporting requirement.	OTHER Unclear.	YES	OTHER Require clarification on this suggestion.	OTHER This needs more detail for L&I to respond.	OTHER Defer.
e) Require registered contractors to file quarterly reports with L&I.	OTHER Unclear.	YES	OTHER Defer to L&I.	OTHER This needs more discussion before L&I can respond. It would definitely require increased staffing for the agency in order to process such reports. The goal this is trying to achieve must be clearer and spelled out.	OTHER Defer to L&I.
7) ADDITIONAL COMMENTS	Task Force should be continued, with specific charges.				

ⁱ In reviewing this option previously, our agency believes that the gains made by reducing overlap are offset by three factors: decreased depth of knowledge due to the incredible expansion of laws any one staff would need to know, specific issues with combining L&I collections, which often involve complex issues with ongoing claims or other matters much different from our premium collections, and the loss of connection with day-to-day field staff in the safety and construction compliance fields. Those daily interactions result in hundreds of referrals and millions of dollars collected by our revenue collections staff each year.

ⁱⁱ ESD needs the flexibility, particularly in small field offices, to use Tax Specialists for both audit and collection functions. Many Tax Specialists currently prefer the variety of doing both functions, while ESD also is able to accommodate individuals who prefer either audit or collection. Separating the functions will decrease flexibility both for the agency and for the individual Tax Specialists. Requiring separate classification into collectors and auditors would significantly restrict ESD's ability to use small, localized District Tax Offices because of overspecialization and inability to cover others in a small office.

ⁱⁱⁱ Requiring unemployment insurance (UI) coverage for independent contractors would significantly alter the principles of unemployment insurance, which is based on employer-employee relationships. Initial eligibility issues: Eligibility for benefits is based on an employee working at least 680 hours as an employee, not as a business owner. Business owners are ineligible for benefits and are not given the option of voluntarily electing UI coverage. Continuing eligibility issues: UI claimants must be able, available, and seeking work; an independent contractor looking for business leads would not meet work search requirements. A contractor would have to be available for work in the customary occupation, including applying for work with a competitor. A contractor could be denied benefits if it refused a contract, even if for other reasons. Funding issues: UI taxes are based on hourly wages rather than business income or profits; a new basis for funding would be required. Independent contractors are not covered by FUTA, which pays for administrative costs of the UI system. Cost and fraud issues: Controlling costs, preventing fraud, and ensuring taxes are currently based on checks and balances between employers and employees; there are no similar independent sources of information for independent contractors. There is no independent information on layoffs, since the independent contractor would lay himself or herself off. It would be difficult to verify when an independent contractor is working or idle.

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Prepared For: Joint Legislative Task Force on Underground Economy in the Construction Industry, November 19, 2007

Prepared By: Joan Elgee, Office of Program Research