



**Written Testimony of Secretary Michael Vovakes
Department of Labor & Industry**

Before the House Labor and Industry Committee

Harrisburg, Pennsylvania

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Good morning Chairman Kauffman, Chairman Galloway, Committee Members, and Committee Staff. I appreciate the opportunity to testify today before the House Labor and Industry Committee to provide information concerning House Bill 1781. My name is Michael Vovakes and I am the Deputy Secretary for Compensation and Insurance in the Department of Labor and Industry.

House Bill 1781 would create a new section, Section 304.3, in the Pennsylvania Workers' Compensation Act. Under this section, notwithstanding any other provision of law, a person may file a registration to certify the status of an individual as an independent contractor for workers' compensation purposes for individuals who are similarly classified for federal income tax purposes. By filing the registration, the person or business registering the individual would not be required to carry insurance coverage or be liable to provide workers' compensation benefits for the registered individuals. The bill defines an "independent contractor" as "an individual who performs services for a person for payment but who is not classified as an employee of the person for federal income tax purposes."

The Department certainly values this committee's efforts to facilitate discussions on the topic of independent contractor status; however, it has significant concerns with this bill. First, it conflicts with current law, both as that law has developed under the Workers' Compensation Act and with the Construction Workplace Misclassification Act (Act 72 of 2010). While Act 72 is enforced by the Department's Bureau of Labor Law Compliance rather than the Bureau of Workers' Compensation, the bill would create inconsistency in applicable standards and enforcement within the agency. Secondly, the bill would create confusion and litigation for all stakeholders in the workers' compensation system, as well as significant additional claim exposure for the Uninsured Employers Guaranty Fund, which is administered by the Department.

Currently, there is no definition of an "independent contractor" in the Workers' Compensation Act. Apart from the construction industry, the question of whether an individual is an

employee or an independent contractor under the Act is a question of law determined by a workers' compensation judge, based upon findings of fact. Pursuant to long-standing case law from the Pennsylvania Supreme Court, that determination is based upon a case-by-case review of several criteria to ascertain whether the alleged employer had the right to control the work to be done and the manner in which the work was performed. The criteria include the terms of agreement between the parties; the nature of the work or occupation; skill required for performance; whether the individual employed is engaged in a distinct occupation or business; which party supplies the tools; whether payment is by the time or by the job; whether work is part of the regular business of the employer; and whether there is a right to terminate the employment at any time. Because each case presented on this issue is fact-specific, all the factors need not be present to determine the type of relationship that exists.

In 2010, the General Assembly enacted the Construction Workplace Misclassification Act (Act 72), which established specific criteria for the construction industry to determine whether an individual performing work in the construction industry may be classified as an independent contractor. Like the existing case law under the Workers' Compensation system, the primary focus of Act 72's criteria are to determine who directs and controls the work performed, and to ensure that only bona fide independent contractors are classified as such. Act 72 was passed to address abuses in the construction industry, where misclassification occurred three times more often than in other industries and resulted in an unfair competitive advantage in the construction bidding process. The Department is charged with enforcement of the Act, which establishes procedures and penalties for violations. The provisions of House Bill 1781 are inconsistent with the Department's efforts to enforce the Act 72, as well as its broader goals of preventing misclassification of employees in all industries.

House Bill 1781 essentially creates a new classification and a new test for "independent contractor" status in all occupations throughout the Commonwealth, based solely on Federal income tax classification. This is inconsistent with long-standing case law that considers case-specific factors to determine direction and control of work, as well as the specific criteria applicable to work performed in the construction industry as set forth under Act 72 will undoubtedly lead to confusion and litigation.

To the extent that the new test for determining whether an individual is an independent contractor in all occupations now would be the proposed registration process alone, rather than the criteria set forth in case law, it would appear that failure to properly follow this procedure could result in an inability to argue that an individual was an independent contractor. If so, this legislation likely will have the effect of significantly increasing benefit costs related to additional claims against the Uninsured Employers Guaranty Fund, which has

no pre-existing relationship with the parties but could be liable in any case where this registration process was not properly followed.

Additionally, House Bill 1781 appears to oversimplify the ability to classify workers as independent contractors, basing it solely on the filing of a registration tied to federal income tax status, which may lead to further errors by businesses and individuals. The registration is to be filed by the business and is required to include the following documents signed by the individual: a written waiver of benefits under the Act and an affidavit agreeing that the individual is not an employee and is not entitled to workers' compensation benefits but may purchase workers' compensation coverage under the Act. Under the bill, the individual can revoke the registration at any time, by completing and filing a revocation form and providing notice by certified mail to the person who filed the registration. The Department is required to confirm receipt of the individual's revocation request to both parties, and the revocation becomes effective ten days after receipt. The business would, therefore, have a period of just ten days in which to secure workers' compensation coverage for that individual if it has not already done so, or be uninsured for any potential injury. In that event, there likely would be additional claim and litigation exposure for the Uninsured Employers Guaranty Fund where the business did not otherwise maintain insurance, as well as for an insurer if the business otherwise had coverage for other employees.

House Bill 1781 also prohibits businesses from offering incentives to individuals to complete waiver and affidavit forms or to refrain from filing requests for revocation of independent contractor status. Violators of this specific prohibition would be subject to criminal penalties prescribed under section 305 of the Workers' Compensation Act, which relates to failure to insure. However, the bill does not indicate whether such prohibited actions would render a filed registration "void," and if so, as of what date. This will also result in litigation, which again could result in the business being found to be uninsured for any potential injury, with claim and litigation exposure to the Uninsured Employers Guaranty Fund.

We anticipated an increase in litigation related to the registration, affidavit and waiver forms, regarding issues such as alleged misunderstanding, fraud, and coercion in connection with the forms, as well as whether the individual was properly classified for federal tax purposes. If a judge or court determines the agreement void based on these issues, once again, Uninsured Employer Guaranty Fund litigation and claim exposure would exist.

It is not clear whether the registration must be filed annually or if one-time filing is sufficient for future years unless revoked. The legislation provides that the registration shall be "valid for each future year," which is vague and subject to interpretation. Because employment status may vary by job, it may be inadvisable to allow a filing to extend for any length of time.

Finally, in terms of implementation, the sixty-day effective date is problematic given the involvement and obligations placed upon the Department in the proposed registration process. Under House Bill 1781, the registration must be on forms prescribed by the Department, including a registration form, a waiver, an affidavit, a revocation form and a confirmation. The Department will need to develop new forms and a process for registration and revocation, as well as a confirmation of form receipt. This new procedure may require additional Department personnel and will likely involve significant additional costs for design, creation and implementation in the Department's electronic Workers' Compensation Automation and Integration System (WCAIS), which would undoubtedly take longer than 60 days.

Furthermore, if the sponsors of the bill intend for the Department to investigate and verify employment status, rather than simply develop and maintain the proposed registry, associated administrative costs would be far greater. However, if increased oversight and enforcement of misclassification is a goal of this legislation, the Department is glad to engage in broader conversations both to ensure consistency with existing law and to identify necessary resources and enforcement tools.

I would again like to thank this committee for the opportunity to testify today to provide information regarding the House Bill 1781. The Department of Labor and Industry remains committed to working with this committee and all stakeholders to achieve improvements in the workers' compensation system in Pennsylvania.

Thank you, and I would be glad to answer any questions that you may have.