

# HOUSE BILL REPORT

## ESHB 1701

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### As Amended by the Senate

**Title:** An act relating to the underground economy by addressing the loss in state revenue through misclassification of workers as independent contractors in the construction industry.

**Brief Description:** Concerning the misclassification of contractors as independent contractors in the construction industry.

**Sponsors:** House Committee on Labor & Workforce Development (originally sponsored by Representatives Ormsby, Green, Sells, Kenney, Van De Wege, Hasegawa, Hudgins, Moeller, Miloscia, Sullivan, Upthegrove, Pettigrew, Seaquist, Hunter and Frockt).

#### **Brief History:**

##### **Committee Activity:**

Labor & Workforce Development: 2/11/11, 2/16/11 [DPS].

##### **Floor Activity:**

Passed House: 3/4/11, 54-43.

Senate Amended.

Passed Senate: 4/4/11, 25-23.

#### **Brief Summary of Engrossed Substitute Bill**

- Provides that it is a contractor registration violation for a contractor to engage more than two independent contractors with no covered workers to work on or in a single building on the same task involving a similar material.

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### HOUSE COMMITTEE ON LABOR & WORKFORCE DEVELOPMENT

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 7 members: Representatives Sells, Chair; Reykdal, Vice Chair; Kenney, Miloscia, Moeller, Ormsby and Roberts.

**Minority Report:** Do not pass. Signed by 6 members: Representatives Condotta, Ranking Minority Member; Shea, Assistant Ranking Minority Member; Fagan, Green, Taylor and Warnick.

**Staff:** Joan Elgee (786-7106).

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

## **Background:**

The Contractor Registration Act (Act) requires general and specialty contractors to register with the Department of Labor and Industries (Department). The Act sets forth penalties for specific violations of the Act. For example, a contractor who fails to register is subject to a fine of not less than \$1,000 and not more than \$5,000.

With limited exceptions, all workers in the state are covered by mandatory industrial insurance. Some independent contractors are exempt from mandatory coverage. The term "independent contractor" is not defined in law; rather, this concept is embodied in several exception tests to the definition of "worker." If a worker fulfills the tests, the worker is not covered for purposes of workers' compensation and no industrial insurance premiums are due. Otherwise, the worker is a covered worker and premiums are due.

In 2009, as part of underground economy legislation, the Legislature directed the Department, together with the Employment Security Department and the Department of Revenue, to report each year on the effectiveness of efforts to address the underground economy.

## **Summary of Engrossed Substitute Bill:**

Legislative intent is stated that the state loses over \$100 million per year in underground economy construction activity. The Legislature finds that if multiple contractors are working on the same task on a job site, the contractors must be working under direction and control such that they are not exempt independent contractors but are, in fact, covered workers. The Legislature further finds that prohibiting certain contracting, which by its nature creates a situation in which taxes due are not paid, will provide clarity to contractors and reduce the underground economy.

It is a contractor registration violation for a contractor to engage more than two independent contractors to work on or in a single building who: (1) are working on the same task involving a similar material; (2) bring no workers to that job site covered by industrial insurance; and (3) are not being treated as covered workers. A "task" is a risk classification for purposes of industrial insurance. Work on residential wood frame construction up to four stories is exempt.

Penalties are established of \$500 for the first offense, \$2,500 for the second offense, and \$5,000 for the third or subsequent offense. For a first time offense, the fine is waived if the contractor registers for a training class within 10 days, and completes the class within 120 days, of receiving the infraction. The contractor must also pay the class fee. For the third or subsequent offense, the Director must also suspend the contractor's certificate of registration for one year. The Director must also suspend the registration of any contractor until payment of penalties that have become final are paid in full.

Beginning on December 1, 2012, the underground economy report must include a report on the effectiveness of the new violation. The underground economy report provision is codified.

## **EFFECT OF SENATE AMENDMENT(S):**

The Senate amendments: (1) exempt contractors with fewer than 50 employees from the provisions; and (2) provide that no more than two independent contractors who meet the criteria specified in the bill (working on or in a single building on the same task involving a similar material, with no covered workers) may be under contract at the same time. It is not a violation if proof is provided, both in written contract and in fact, that any independent contractors beyond the first two are not working during the same time period. The amendment further provides that the exemptions provided in the amendment are broad and in no way exempt independent contractors from industrial insurance coverage. Independent contractors must separately pass the tests to be exempt from coverage.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect 90 days after adjournment of the session in which the bill is passed.

### **Staff Summary of Public Testimony:**

(In support) This bill addresses the prevalent problem of worker misclassification. It is hard for a contractor complying with the law to compete with contractors who classify their workers as independent owner operators to avoid paying unemployment and workers' compensation taxes. People are told "this is the way to do it." Contractors who used to get 30 to 35 percent of jobs bid now only get 1 to 5 percent of jobs. The bill will have a positive fiscal impact as the Department fraud team has a 7:1 return rate. The Legislature's help is needed so people can stay in business. The Department has technical amendments and these are supported. This bill is one step.

(Opposed) There is a serious underground economy problem but a simple prohibition in law is not the way to fix it. More conversation is needed. Current law already addresses the situation with the seven part independent contractor test. More enforcement of current laws, using the fees contractors pay, is needed. The Underground Economy Task Force did not recommend this controversial approach, which infringes on how people do business. The terms such as "same task" are too vague. It is not clear how the bill will affect job order contracting or truck drivers on a large project, and some legal people are left out. Prevailing wage definitions should not be used. The bigger problem is unregistered contractors. Fix the problem with the Department's website not indicating that a contractor is violating various laws to proceed with this bill.

**Persons Testifying:** (In support) Dave Johnson, Washington State Building and Construction Trades Council; Susan Bittner, Fryer-Knowles, Inc.; and Gregg Greenstreet, Herzog Glass.

(Opposed) Rick Slunaker, Associated General Contractors; Brian Minnich, Spokane Home Builders Association; and Gary Smith, Independent Business Association.

**Persons Signed In To Testify But Not Testifying:** (In support) Dave O'Meara, International Union of Painters and Allied Trades; Randy Loomans, International Union of Operating Engineers Local 302; Craig Munson, Seattle Flooring; Michael Heinz, Heritage Floors; and Eric Gustafson, Ironworkers Local 86.

(Opposed) Bill Stauffacher, Building Industry Association of Washington.