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## Report Highlights

# Detection and Prevention of Worker Misclassification

## Louisiana Workforce Commission

Audit Control # 40180017

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### Why We Conducted This Audit

We evaluated whether the Louisiana Workforce Commission (LWC) has developed effective processes to detect and prevent worker misclassification. Worker misclassification occurs when an employer improperly classifies a worker as an independent contractor instead of an employee. Worker misclassification is a longstanding problem affecting numerous industries nationwide and results in a significant loss of tax revenue. The United States Treasury Department estimated in 2013 that preventing worker misclassification would generate \$8.32 billion in federal revenue over 10 years. LWC's activities to prevent and detect misclassification include performing audits, assessing and collecting penalties for worker misclassification, and conducting education/outreach efforts for employers in the state on worker misclassification.

### What We Found

Overall, we found that while LWC's audit performance during calendar years 2014 through 2018 ranked high nationally, we identified some areas where it can improve its detection and prevention of misclassified workers. Specifically, we identified the following issues:

- **Since calendar year 2012, LWC has met federal audit criteria that require it to audit 1% of employers and 1% of total employee wages each year. However, LWC could strengthen how it selects employers to audit by determining which audits identified the highest number of misclassified workers.** This analysis would enable LWC to focus its audit efforts on industries with the highest risk of worker misclassification. We found that audits initiated based on tips and referrals generated the highest number of misclassified workers as shown in the table on the following page.

The cost of worker misclassification to the state can be significant. For example, from calendar years 2014 through 2018, LWC conducted 3,042 audits that identified employers that misclassified workers and failed to pay the state nearly \$3 million in unemployment taxes. Based on the wages associated with these unpaid unemployment taxes, we estimated the state potentially did not receive approximately \$9 million in state income taxes.

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### What We Found (Cont.)

LWC Audits and Results by Selection Source Calendar Years 2016 through 2018				
Audit Selection Source	Number of Completed Audits	Percent of Total Audits	Number of Misclassified Workers Identified	Misclassified Workers Identified Per Audit
Fraud Tips/Agency Referrals	66	2.3%	2,346	35.6
Follow-up Audits	10	0.4	127	12.7
Independent Contractor Form 1099s	1,561	54.0	8,081	5.2
Employer Reported Wage Data	1,214	42.0	1,306	1.1
Unknown*	38	1.3	502	13.2
Blocked Claims	0	0	0	0
Total	2,889	100.0%	12,362	4.3

\*No selection source documented by LWC.  
**Source:** Prepared by legislative auditor's staff using unaudited data from LWC and USDOL.

- LWC could further strengthen its audit selection process by using data from other state agencies to compare to its quarterly wage data from employers.** For example, we analyzed the Louisiana Department of Health's and the Department of Transportation and Development's contractor payroll and time sheet data and identified 383 employers that did not report employee wages to LWC for as many as 22,850 workers as required by law, thus potentially misclassifying workers.
- LWC's enforcement process is not effective at deterring employers from misclassifying their workers. Louisiana is the only state that mandates LWC to send warning letters to employers that misclassify workers on their first offense as opposed to assessing penalties.** This requires LWC to use its limited resources to conduct follow-up audits in order to impose applicable penalties. If LWC could impose penalties for first-time offenses, we estimated it could have assessed approximately \$3.3 million in penalties for the 13,106 misclassified workers it identified during calendar years 2016 to 2018.
- Louisiana law does not impose liability on contractors for misclassification of workers hired by labor brokers.** As a result, contractors have no responsibility to ensure that workers provided by labor brokers are properly classified, which increases the risk of worker misclassification and makes it more difficult for LWC to deter worker misclassification.