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Senator Kerry, distinguished guests and all other invitees:

On behalf of Massachusetts Attorney General Martha Coakley, I would like to thank Senator Kerry and the United States Senate Committee on Small Business and Entrepreneurship for the opportunity to make some observations on the underground economy in Massachusetts and its effect on small businesses and workers. Further, I would like to mention the efforts that we have made over the past year to address issues of the underground economy and the impact our efforts have made on the economic climate in Massachusetts.

First, as has been well documented and discussed by other presenters to this committee, the underground economy has direct, systemic negative impact on workers, on legitimate businesses and on the tax revenues received by the Commonwealth, and the United States Government. There are also indirect costs, both for government and the economy in general. For example, extra costs assumed by government for health care or other social services for workers not provided them through their employers are shared by all taxpayers. Employees who do not receive the timely payment of wages or any wages are likely to have difficulty paying their rent, their utilities, and making other payments all of which impact the economy.

The Fair Labor Division of the Office of the Attorney General is statutorily mandated to enforce the wage and hour laws of the Commonwealth. This includes minimum wage, overtime, prevailing wage, vacation, commission, and child labor laws to name several. We handle over 3000 complaints annually. A vast majority of these can be considered within the underground economy designation. The underground economy encompasses a wide variety of offenses:

- An employer who pays employees in cash, often below minimum wage;
- Employees who work hours significantly above 40, but don't get paid the statutorily required time and a half for all hours worked. Often, employees get a cash payment that covers only some of the time worked, or may get only straight time for overtime hours worked. It is not uncommon for unscrupulous employers to pay overtime from a separate account to shield the overtime payments from scrutiny and taxes.

- There are employers who give employees, often minimum wage workers, checks that bounce, week after week, or intermittently. Employees are reluctant to seek other employment without getting back wages; but staying leaves them vulnerable to additional weeks without a paycheck.
- Even in the public construction arena, the underground economy issues flourishes. Employers fail to pay prevailing wage, take credit for deductions for health or pension plans but never remit the premiums to the plans, or pay less than the full rate or fail to register apprentices.
- Some employers hire undocumented workers, despite the federal requirement that they confirm immigration status, and then exploit the status of the workers by not paying them, paying them less than the law requires, or requiring illegal offsets for transportation, tools and other costs, knowing that they are unlikely to report the employer to governmental authorities.
- In one particularly egregious case, an employer never paid any employee. Instead he hired a crew of undocumented workers, worked them for several weeks, let them go and then kept cycling through new crews of undocumented workers every few weeks, never paying any of them.
- One of the most pervasive practices within the underground economy is the misclassification of employee by companies. Although this is commonly referred to as classifying individuals as independent contractors, not as employees, as they should be classified, this is somewhat of a misnomer. Often the individuals are not just misclassified, they are not classified at all. They are not true independent contractors, running their own businesses, having independence and autonomy, being paid by check and then reporting income on Form 1099s and paying appropriate taxes. Instead, these individuals receive a set sum of money, usually in cash, often below the proper rates of pay, with no pay stub or other record, no reporting to the taxing authorities or payment of taxes, and no ability to obtain restitution later because of the lack of records, undocumented status of the employees and other variables.

## IMPACT ON EMPLOYEES AND SMALL BUSINESSES

The impact on employees is unmistakable. Employees deprived of their just wages, or any wages, cannot live. They cannot pay rent, utilities, buy food for their families, provide health care, transportation or any of the other basic necessities for their lives and their families. Often, they are unskilled, perhaps undocumented, frequently uncomfortable reporting violations to government agencies, and rarely with the discretionary time to pursue cases against their employers.

We should not tolerate, in Massachusetts or anywhere in the United States, the exploitation of workers. Not only are workers harmed economically, they are demoralized by being treated so poorly. It is hard enough to live paycheck to paycheck, but when the checks don't come in, life becomes impossible.

The AG recognizes that small businesses face challenges different than, and probably greater than, larger businesses. They find it hard to sustain viability. Clearly,

expenses and taxes, and the challenges of running a small business make success more elusive. Some find it tempting to skimp on employee obligations, particularly when a business is struggling.

Yet interestingly, we hear from many legitimate small businesses that they are thrilled that Attorney General Martha Coakley is vigorously enforcing the wage and hour laws. They concur with the AG's assumptions that enforcement of the law will level the playing field within the small business community and allow them to become more successful, as they will no longer be undercut by businesses that are not playing by the rules.

I have been advised that for the first time in many years, small businesses are filing complaints against competitors who are not playing by the rules, because they are comfortable that the AG will take appropriate action. In a number of industries, such as car washes, flooring and drywall, all of which are rife with underground economy problems, the AG's actions have led to a change in the culture of the industries and businesses being more receptive to playing by the rules.

One noteworthy example of our success is a small drywall company that employs between 10 and 50 and complies with wage and hour laws. The company has historically bid 30-40% higher than many of its competitors who do not play by the rules in order to treat its employees right and pay proper taxes. Now that the Attorney General has demonstrated her commitment to enforcement by actual enforcement actions in the construction industry and her notice to the dry wall industry that she will do strategic enforcement of wage and hour laws within the industry, the drywall industry has already begun changing. This drywall company reports that his competitors are bidding in the same range as he is, as they are in greater compliance with the law, so that he is right in the mix of the bid range. As a result, he is often selected by general contractors, who know that his work is good, that he is legitimate and now that his price is competitive, he has more work than he can handle. A success story within an industry which knows that enforcement has been and will continue to happen.

So in looking at the effect of the underground economy on small business, it is crystal clear to the AG that continued, meaningful enforcement of wage and hour laws will have a positive, sustained impact on legitimate small businesses.

## ENFORCEMENT

The Attorney General of Massachusetts has made enforcement of wage and hour laws, particularly for those employees and businesses that are in the underground economy a priority. She has devoted resources and personnel to the issue and been supportive of all efforts of the Fair Labor Division to take on this important task.

Some of the highlights of the first year:

- Consistent, visible, vigorous enforcement of the wage statutes, with focus on those businesses and employees part of the underground economy;
- Processing of complaints more quickly and efficiently;
- Issuance of citations with orders of restitution to workers and fines commensurate with the violations;
- Obtaining of criminal complaints against those businesses whose wage and hour violations meet the criteria for criminal enforcement.
- Advising businesses that failure to comply with our procedures no longer results in a minimal fine, but subjects the business to significant fines and orders of restitution.
- An open door policy for businesses, unions, workers and advocacy groups who want to discuss issues and resolve complaints.
- Outreach to all stakeholders; revision of materials for distribution.
- Increased language capacity to reach employees in the underground economy for whom English is their second language;
- Presentations and information sessions to industry groups, unions, law firms, legal and other professional associations;
- Revision of the Independent Contractor/Misclassification Advisory to give all stakeholders a better understanding of enforcement guidelines;
- Participation in the Underground Economy Task Force and cooperation with other state agencies to target companies who are violating multiple state laws.
- Meetings and cooperate activities with the Fair Wage Campaign and advocacy groups.
- The assignment of two victim advocates to the Fair Labor Division, who assist employees, in recognition that individuals who are victims of wage statute violations are victims.

Thank you for the opportunity to make this presentation. We look forward to working with your committee and federal agencies towards elimination of the underground economy which would result in fair and legal payment for all workers, a level playing field for small (as well as large) businesses and the opportunity to compete and an assurance that the tax revenues that should come to the state and the federal government will be paid.