

LEGISLATIVE BUDGET BOARD  
Austin, Texas

FISCAL NOTE, 79TH LEGISLATIVE REGULAR SESSION

May 3, 2005

**TO:** Honorable Allan Ritter, Chair, House Committee on Economic Development

**FROM:** John S. O'Brien, Deputy Director, Legislative Budget Board

**IN RE: HB3191** by Bailey ( relating to the employment relationship, including certain requirements relating to reporting independent contractors; providing a penalty.), **Committee Report 1st House, Substituted**

**Estimated Two-year Net Impact to General Revenue Related Funds** for HB3191, Committee Report 1st House, Substituted: an impact of \$0 through the biennium ending August 31, 2007.

The bill would make no appropriation but could provide the legal basis for an appropriation of funds to implement the provisions of the bill.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2006	\$0
2007	\$0
2008	\$0
2009	\$0
2010	\$0

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue Gain/(Loss) from <i>UNEMPL COMP SP ADM ACCT</i> 165
2006	\$8,136,623
2007	\$8,136,623
2008	\$8,136,623
2009	\$8,136,623
2010	\$8,136,623

Fiscal Analysis

The provisions of the bill amend the Labor Code by assessing a penalty on employers that misclassify their employees as independent contractors implying the absence of an employment relationship, and stipulating the amount of a penalty to the Texas Workforce Commission (TWC) to be over and above any tax or interest due on wages.

If it is shown that the employer failed to report the wages after receiving a ruling from TWC or IRS that an employee is a misclassification, the penalty would be equal to the tax due on taxable wages or equal to three times the tax due on taxable wages. The penalty would apply to each employee misclassification.

The bill would take effect September 1, 2005.

### **Methodology**

According to TWC, in 2004 the TWC Tax Department audited over 8,000 employers. Of those audits 4,458 identified misclassified workers and would have resulted in assessment of the misclassified worker penalty. Assuming that each of these 4,458 employers had at least one misclassified worker that earned over \$9,000 during the calendar year at an average tax rate of 1.74 percent, the additional 100 percent penalty would be \$698,122.80 (4,458 times 9,000 times 1.74 percent).

According to TWC, each year the Unemployment Insurance (UI) Tax Department conducts approximately 150,000 "report due" investigations. Using the Internal Revenue Service and Department of Labor's estimate of 15 percent of all employers underreporting their employees, the Tax Department calculates that 22,500 of the report due employers are misclassifying their workers. Assuming that each of these 22,500 employers had at least one misclassified worker that earned over \$9,000 during the calendar year at an average tax rate of 1.74 percent, the additional 100 percent penalty would be \$3,523,500 (22,500 times 9,000 times 1.74 percent).

According to TWC, each year the Tax Department conducts approximately 25,000 block UI claim investigations. The investigations take place when a business or organization does not properly report the wages of an employee. Assuming that each of these 25,000 employers had at least one misclassified worker that earned over \$9,000 during the calendar year at an average tax rate of 1.74 percent, the additional 100 percent penalty would be \$3,915,000 (25,000 times 9,000 times 1.74 percent)

The revenue estimated from misclassified worker penalty is \$8,136,622.80 and would be a gain to the General Revenue Dedicated – Unemployment Compensation Special Administrative Account No. 165.

TWC estimates the additional examiner and supervisor time would be 6,062.1 hours. It is estimated that any additional costs associated with implementing the provisions of the bill could be absorbed within the agency's existing resources.

### **Local Government Impact**

No fiscal implication to units of local government is anticipated.

**Source Agencies:** 320 Texas Workforce Commission

**LBB Staff:** JOB, JRO, MW, DE