



# The Future of Work: Alternative Work Arrangements in Colorado

Heidi McNamara · January 2020

## Executive Summary

Much has been written about the future of work, the changing economy, and the shift away from traditional employer-employee relationships, yet we know very little about what alternative work arrangements look like in Colorado specifically. Who works in “alternative” positions, what are these jobs, and why do people choose these nontraditional positions? What benefits do workers and employers receive from different types of work arrangements? What are the costs — to workers, employers, and the state? This report maps the landscape of alternative work arrangements in Colorado. The report’s findings, summarized here, highlight the prominence of the alternative workforce and the importance of protecting these workers in future policy.

### Important Takeaways

**Ten percent of Colorado’s workers are independent contractors without basic workplace protections in their primary occupation.**

When including other alternative workers — day laborers, temp workers, and on-call workers — this percentage increases slightly, accounting for about 12 percent of Colorado’s workforce. This jumps to as many as 25 percent of workers when incorporating those working for supplementary income as part of the gig economy. Those classified as independent contractors (the vast majority of the alternative workforce) don’t have access to unemployment insurance if their contracts are ended unexpectedly, workers’ compensation if they are injured on the job, minimum wage and overtime protections that ensure fair compensation for hours worked, or workplace discrimination and harassment protections. Alternative workers of all kinds also miss out on any workplace benefits offered to traditional employees, which can include paid time off — for sick leave, family and medical leave, or vacation — health insurance, retirement benefits, or other workplace perks.

**Alternative workers aren’t evenly distributed across the workforce.**

In Colorado specifically, alternative workers are more likely to be white, female, and well-educated than the national population of alternative workers.

**At the very least, tens of thousands of Coloradans are misclassified as independent contractors each year, despite possibly meeting the requirements of regular employee status.**

By misclassifying employees, employers can save up to 30 percent on payroll expenses and respond more nimbly to market demands, but these benefits come at the expense of their workers, their competitors, and the state’s budget.

**Poor data significantly limits knowledge and examination of the alternative workforce.**

There is very little available data, particularly within Colorado, that measures independent contractors, gig workers, and other alternative workers. In the datasets that do exist, it’s difficult to differentiate between self-employed workers and true contract workers. There are large discrepancies between self-reports of independent work in national surveys and the number of 1099-MISC tax forms — the form independent contractors receive from employers instead of a W-2 — filed each year. It’s especially difficult to assess any equity challenges within this workforce because what’s known becomes even more limited as we examine smaller and smaller subpopulations. In order to better understand this subset of the workforce, we need new and better data measuring who these workers are, what types of jobs they do, when, and how.

The alternative work phenomenon is not new, but it has newly important implications for the future of work. As we develop policy to guide the economy of the future, it’s important to understand how these policies impact more than one-fourth of Colorado’s workers who operate outside the traditional confines of an employer-employee relationship. This can be done by crafting policies that extend workplace protections to alternative workers, creating a system of portable benefits open to both traditional employees and nontraditional workers, increasing penalties for misclassification of workers, and requiring additional reporting on the state of alternative work in Colorado.

## Policy Recommendations:

1. Expand unemployment insurance and workers' compensation programs to include independent contractors. Increase penalties for misclassification of employees as independent contractors.
2. Increase transparency around unemployment audits and require the Colorado Department of Labor and Employment (CDLE) to report random and targeted audits separately.
3. Include independent contractors and other nontraditional employees in portable benefits systems.
4. Require CDLE and the Department of Revenue to report on the current landscape of independent contractors in Colorado.

## Glossary:

**Alternative work arrangement (AWA):** Alternative work arrangements are defined in this report to include independent contractors, on-call workers, day laborers, and temp workers. This encompasses workers who use these positions as their primary source of income and those who engage in the gig economy for supplemental income.

**Gig economy:** This report defines the gig economy to be a subset of alternative work arrangements that provide individuals the opportunity to participate in "on-the-side" work to supplement their primary income. It's typically made up of workers on short-term contracts, doing freelance work, or contracting through online platforms.

**Independent contractor:** Independent contractors are workers who are contracted to perform work or services for another entity as a nonemployee. Their earnings are reported using a 1099-MISC form instead of a W-2, and the contracting entity doesn't withhold any taxes from the contractor's pay. To be classified as an independent contractor in Colorado, the relationship between company and contractor must meet a set of requirements as outlined by CDLE.

**W-2 vs. 1099-MISC:** Both W-2 and 1099-MISC forms are tax forms used to report earnings at the end of the year. W-2 forms are used to report employees' earnings. Employers providing W-2 forms have typically already withheld payroll taxes from employees' earnings. 1099-MISC forms are used to report payments made to independent contractors, who are responsible for withholding and paying their own payroll taxes.

**Misclassification:** Misclassification occurs when workers who meet the requirements of a traditional W-2 employee are instead classified as an independent contractor and their earnings are reported using a 1099-MISC form.

## What Are Alternative Work Arrangements?

The economy is changing. The traditional social contract between an employer and long-term employees, where the employer provides reliable wages, benefits, and training in exchange for the hard work and loyalty of their employees, no longer applies to many workers. In Colorado, more than 12 percent of workers use alternative work arrangements for their main source of income.<sup>1</sup> At least a [quarter of the workforce](#) makes some income through side gig-work. Figure 1 displays the distribution of alternative workers in the national economy.<sup>2</sup>

**Figure 1: Number of National Workers Participating in AWAs**



Definitions of alternative work vary widely, but as you can see in Figure 1, the phenomenon is much broader than just well-known online platforms like Uber and TaskRabbit. Generating the right policy solutions to meet the challenges presented by alternative work arrangements requires an honest assessment of what the landscape looks like and the implications of different work arrangements. This report strives to provide that assessment.

Figure 2 provides an overview of the different possible relationships between workers and employers, as this report sees them. The relationship between employers and workers varies not just in how, when, and where workers conduct their work, but also in who is responsible for covering payroll taxes, whether or not workers qualify for employer-provided benefits, and whether or not workers qualify for state-backed workplace protections and insurance.

**Figure 2: Different Types of Alternative Work Arrangements**

Work Arrangement Type	Alternative Work Arrangement	Gig Worker	Paid Wage/Salary	Access to Employer-Paid Benefits	Workplace Protections	<a href="#">Eligible for Unemployment</a>
Traditional FT	No	No	Yes	Yes	Yes	Yes
Traditional PT	No	No	Yes	Some	Yes	Yes
Independent Contractor	Yes	Some	Some	No	No	No
On-Call Worker	Yes	No	Yes	Some	Yes	Yes
Temporary Worker	Yes	No	Yes	Some	Yes	Yes
Day Laborer	Yes	Some	No	No	No	No
Self-Employed (incorporated)	No	No	Some	Some	Yes	Some
Self-Employed (unincorporated)	Some	Some	No	No	No	No
On-Demand/Platform Worker	Some	Some	No	Some	Yes	No

<sup>1</sup> Any unattributed statistics in this report come from the Bell's analyses of the 2017 Contingent Worker Supplement to the Current Population Survey. For more information and to download the data [click here](#).

<sup>2</sup> Source: <https://www.gigeconomydata.org/basics/how-many-gig-workers-are-there>

### **Independent Contracting: A Dog-Eat-Dog World**

*The following is based on a conversation with Jed Sanford. He worked as an independent contractor in architectural design for four years and is now a salaried employee at an architecture firm.*

Jed Sanford fell into independent contracting accidentally. A family friend who was an architect knew Jed was computer savvy and needed some help with a new design program. He asked Jed to come work for him for a bit to help him learn the program. After a few months of this, Jed became adept in the complex program and went to look for work in other architectural offices.

What he found, though, was most small architectural offices only wanted to work with him as an independent contractor. He was told he would need to get his own insurance and bid the architectural firms for each new project. Just starting out in this new field, Jed had no idea how to realistically bid or set the scope of a project. Despite this, he agreed and worked as an independent contractor in architectural design for four years.

While Jed was an independent contractor on paper, his first major client treated him as an employee: He was expected to be there every day, leased a desk in the client's office, and expected to be available at all hours of the day. After working with this particular client/employer on and off for four years, Jed's perception is this company hires workers as independent contractors in order to dodge responsibility and not have to worry about paying payroll taxes as a small business. Jed found this was a common strategy for small architectural firms who had slightly more work than their few employees could handle.

As he settled into independent contracting, Jed began working for multiple clients simultaneously. He found it challenging to balance the demands of multiple clients — each of whom saw themselves as his primary and only client — especially when timelines changed unexpectedly or the scope of work wasn't clearly defined in his contract, which was a common occurrence. Often when working with repeat clients, he wouldn't even have a formal contract until near the end of a project. Instead, he would work, potentially for months, without knowing when or how much he would be paid for his work.

Another common trend in Jed's work as an independent contractor was running into clients who were abusive and difficult to work with. They wouldn't be able to treat employees in such a way and, therefore, had a hard time retaining staff. This would turn into working with independent contractors instead. Though Jed was lucky to have an abundance of options for clients and was able to step away from some of the more abusive contracts he encountered, not all independent contractors have the financial buffer to allow that. Independent contractors don't enjoy any of the labor law protections designed to protect traditional employees from abusive working conditions and are entirely responsible for protecting themselves.

Jed found the financial volatility of independent contracting to be challenging. It's hard to keep a budget when your finances are yearly. Additionally, Jed says independent contracting is difficult because you have to fight for every penny and project you get. He says while he makes less money in his current, more traditional position, his stress level has decreased substantially now that he doesn't worry about when or if he will be paid for his work.

In this report, alternative work is defined to include independent contractors, temp workers, day laborers, and on-call workers. However, much of the data and many of the key problems associated with alternative work discussed here apply only to independent contractors, so the bulk of this report's analysis discusses the particular challenges of independent contracting. This is not only because there is more robust data on independent contracting, but also because independent contractors make up 80 percent of Colorado's alternative workforce. When broadly defined, alternative workers account for about 12 percent of Colorado's primary workforce, while independent contractors alone make up about 10 percent of Colorado's total workforce. This means day laborers, temp workers, and on-call workers comprise about 2 percent of the state's total workforce.

These are important distinctions. There has been much discussion about the negative impacts of misclassifying workers as independent contractors, particularly following the recent passage of [AB 5 in California](#). However, 85 percent to 90 percent of self-identified alternative workers prefer this arrangement, according to the recent [Contingent Worker Supplement](#), asked along with the May 2017 Current Population Survey (CPS). The flexibility and independent nature of these arrangements can make them desirable for many workers, as they provide

more options for balancing work with other responsibilities. Still, the public policy implications of having a significant portion of Colorado's workforce uncovered by workplace protection laws and benefits programs means even if workers purposefully seek out these alternative opportunities, the societal implications still warrant examination.

Few states have taken the initiative to confront these contemporary challenges. The evolving nature of the social contract between employers and workers provides a unique opportunity to restructure our system of social support. Colorado can capitalize on this moment as a catalyst for change, motivating a shift toward a system of portable benefits, and a more reliable safety net that stabilizes the state's economy and serves as the foundation for economic mobility for all Coloradans.

## Today's Landscape of Alternative Work in Colorado

In many ways, the landscape of alternative work arrangements in Colorado parallels the national setting. Based on data from the [2017 CPS Contingent Worker Supplement](#), a similar, but slightly higher percentage of workers (12.2 percent) self-report working in alternative arrangements in Colorado than nationally (10.1 percent). This is equivalent to nearly [380,000](#) Coloradan workers.

### Disparities by Age

Both nationally and within Colorado, the proportion of workers choosing alternative positions increases as workers age. Just 6.7 percent of Colorado's workforce under age 30 works in an alternative position, while 10.6 percent of workers aged 40 to 49 and 21.5 percent of workers aged 60 to 69 work in alternative arrangements. This pattern holds at the national level, too.

### Gender Differences

Concerning gender, Colorado's alternative workforce looks distinctly different than at the national level. Nearly 14 percent of Colorado women work in alternative positions, while only 8.4 percent of working women nationally do. Interestingly, however, the proportion of men alternative workers is relatively stable across samples — 11 percent in Colorado and 11.7 percent nationally.

The availability of independent contract work in Colorado may be particularly important for women who typically have to [balance work against more responsibilities at home](#). The imbalance of family caretaking responsibility has been recognized in statute for decades. [The Family and Medical Leave Act of 1993](#) finds "due to the nature of the roles of men and women in our society, the primary responsibility for family caretaking often falls on women, and such responsibility affects the working lives of women more than it affects the working lives of men."

Depending on how we look at it, the predominance of women alternative workers may be a good sign or a negative one for Colorado's economy. Women may look to AWAs to find positions that help balance home and work responsibilities, which could mean they may remain in the workforce at higher proportions. However, if more women are choosing independent contractor positions due to the lack of family-friendly work environments in traditional workplaces, Colorado women could miss out on important protections and benefits that come along with those roles. It's worth noting this also means a higher share of women — the [most common victims of workplace discrimination](#) and sexual harassment — go without workplace protections in Colorado when they're classified as independent contractors.

Figure 3: Percent of Colorado Workers by Age

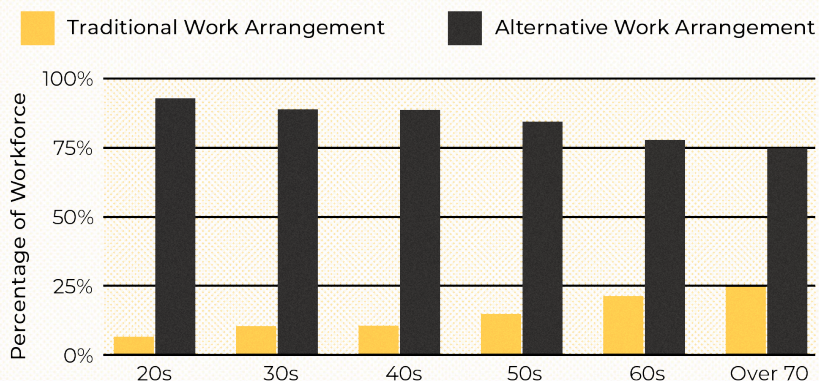
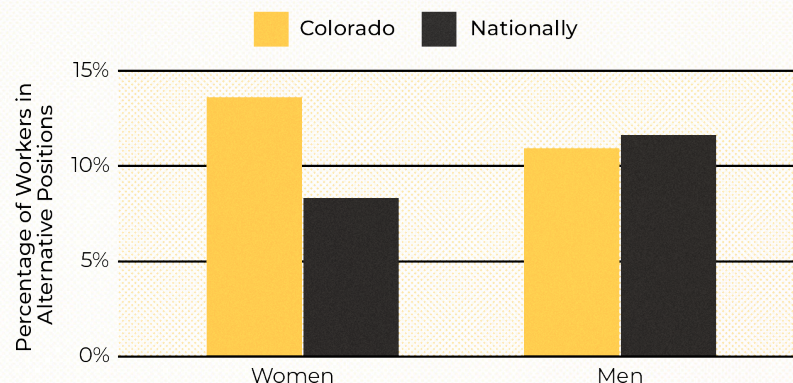


Figure 4: Percent of Alternative Workers by Gender



## Racial Inequalities

In Colorado, nearly 15 percent of white workers work in an alternative position, while nationally the proportion is only 10 percent. Conversely, nearly 10 percent of Hispanic workers nationally report being in alternative positions, while less than 5 percent do in Colorado.

From one perspective, a higher percentage of Hispanic Coloradans in traditional positions with regular paychecks and workplace protections could be a good sign, particularly from an equity lens. In Colorado, Hispanic households' median income is more than [\\$20,000 less](#) than white households, and alternative workers with lower incomes often work in less desirable positions in industries with higher historical rates of worker misclassification.

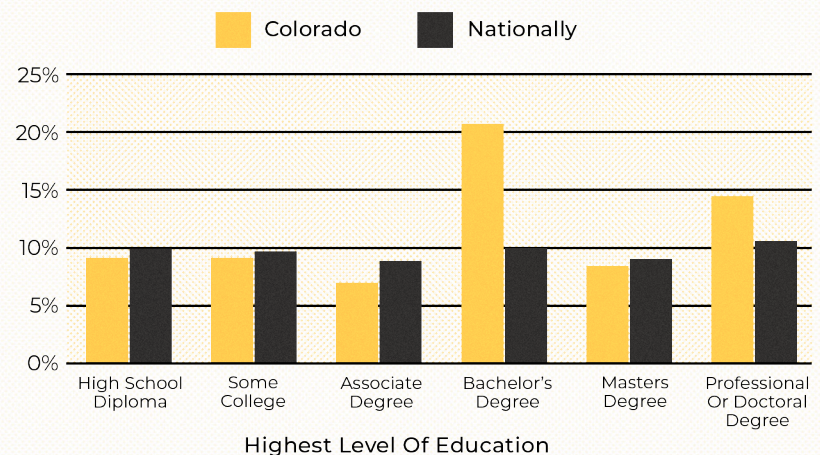
A less positive potential explanation is many Hispanic alternative workers in Colorado have been misclassified as independent contractors and don't understand or are unaware of their technical classification. The low rates of Hispanic alternative workers self-reported in surveys could then be the result of self-reporting bias rather than a true reflection of the distribution of workers in Colorado. However, it's unclear why this self-reporting bias would be more common in Colorado than other areas of the nation where misclassification also occurs.

## Differences by Education

Colorado's alternative workforce is more traditionally educated than the national alternative workforce. Regardless of educational attainment, the percentage of workers in alternative arrangements nationally remains relatively steady around 10 percent. The share of AWA workers in Colorado with less than a bachelor's degree matches this, but that percentage jumps to more than 22 percent for individuals with bachelor's degrees and remains high — about 15 percent — for workers with professional degrees and doctorates. Overall, the alternative workforce in Colorado is whiter, more female, and more educated than the national AWA workforce.

The prevalence of well-educated workers could also be a symptom of privilege. If the benefits of alternative work are primarily being accessed by well-educated white Coloradans, it suggests workers from other races, ethnicities, and socioeconomic backgrounds may be cut out of a helpful strategy for balancing work with other responsibilities — a problem that's even more acute for Coloradans with fewer resources.

Figure 5: Percent of Alternative Workers by Education



## Protections & Benefits for Alternative Workers

One of the frequently highlighted drawbacks of alternative work arrangements and independent contracting in particular is the separation of employment from workplace protections. This disadvantage has both legal and individual consequences for workers in nontraditional employment.

The legal framework that has been built over the last century to protect workers from unfair and unsafe work conditions doesn't often apply to workers who aren't considered employees. This applies to both social insurance programs the state runs — primarily funded by employers — to provide a safety net when things go wrong on the job and to protect workers from unsafe conditions. Specifically, independent contractors aren't covered by unemployment insurance if they lose their job, workers' compensation if they are injured while working (unless they purchase their own coverage), minimum wage and overtime protections, or workplace and sexual harassment protections.

Additionally, employers don't have to provide accommodations for independent contractors under the Americans with Disabilities Act (ADA), nor are independent contractors entitled to leave under the Family Medical Leave Act (FMLA). Because they aren't employees, independent contractors also typically aren't allowed to join unions or collectively bargain.

Beyond legal protections, independent contractors and other nontraditional workers are often cut out of employer-provided benefit programs, such as health insurance and retirement plans or pensions, as well as any paid leave customarily provided to employees. This leaves independent contractors to either purchase these important benefits independently, receive coverage through a spouse, or go uncovered and unprepared.

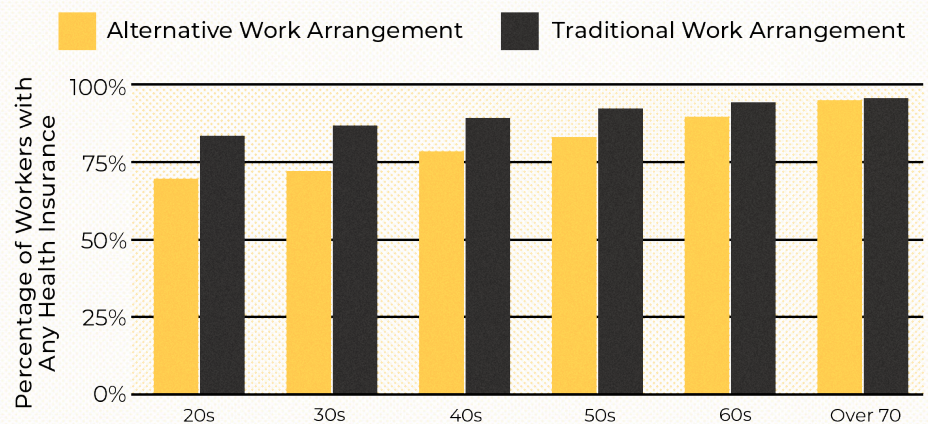
## Health Insurance

In Colorado, about 85 percent of respondents to the [2017 CPS Contingent Worker Supplement](#) say they had health insurance, regardless of their status as a nontraditional worker. Nationally, there is about a nine-point difference, with regular employees covered at about 89 percent and alternative workers about 80 percent of the time. The lack of a difference in Colorado may suggest the state's [health insurance exchange](#) is working relatively well compared to other states.

Yet when examined in combination with type of employment, health insurance coverage raises a few specific equity concerns.<sup>3</sup> In particular, the [2017 CPS Contingent Worker Supplement](#) identifies racial gaps in health insurance coverage for Hispanics and Native Americans nationally. For Hispanic workers, 74 percent of traditional employees have health insurance coverage while only 61 percent of Hispanic workers in nontraditional positions are covered. About 82 percent of Native American workers in traditional employment have health insurance coverage, while only 64 percent of Native American workers in alternative work arrangements have coverage. These disparities are much smaller for other racial groups.

There are also large disparities in health insurance coverage by age, when examined in conjunction with type of employment. For instance, there is a 12-point gap for workers in their 20s, with 84 percent of traditional workers covered and nontraditional workers only covered at 72 percent. This gap remains consistent through workers in their 30s and 40s, and then begins to close until coverage levels are nearly the same as workers enter their 60s and 70s. This convergence of coverage between those in traditional workplaces and alternative work arrangements can likely be explained by older workers' eligibility for Medicare — portable health insurance untied to a specific employer or occupation.

**Figure 6: Percent of National Workers with Health Insurance**



## Retirement Savings

[Retirement savings](#) are another area where alternative workers lose out. In the [2017 CPS Contingent Worker Supplement](#), 64 percent of Coloradans working in traditional positions had some form of tax-deferred retirement savings account, but only 40 percent of alternative workers had similar accounts. This disparity is even more concerning given the fact that as workers age they become more likely to work in nontraditional arrangements, so it's likely older workers who have the lowest rates of retirement savings.

## Other Workplace Benefits

In addition to health insurance and retirement savings, alternative workers and independent contractors in particular are cut out of a variety of other workplace benefits. Though the 2017 CPS Contingent Worker Supplement did not ask questions about paid leave, independent contractors are typically excluded from employer-funded paid leave programs. This means independent contractors are left to rely on savings or working more to compensate for any lost work time when they become ill or need a day (or more) to care for a loved one. They receive no guaranteed leave, paid or otherwise, after the birth of a child or major injury. They risk losing their contracts, and therefore their livelihood, if they are unable to deliver contracted goods on time as a result of unexpected injury or illness.

Though the majority of Colorado's independent contractors [report](#) they prefer the flexibility of their position to a more traditional employment arrangement, the lack of workplace benefits and protections has implications for their own economic security and the stability of the state's economy. Without the safety net of paid leave and/or unemployment insurance, independent contractors are just one typical life event away from financial insecurity.

<sup>3</sup> These analyses were done at the national level, due to small sample sizes within Colorado.

## The Problem of Misclassification

Though many alternative workers are genuinely in alternative relationships with employers and should be classified as such, the financial benefits of working through contractors can lead to abuse of the system. Consequently, many independent contractors are wrongly classified.

Misclassification occurs when workers who meet the legal standard of an employee are instead classified as independent contractors by their employers. This transfers the responsibility for payroll taxes to workers and leaves them without access to traditional workplace protections and benefits, all while saving employers up to [30 percent](#) on labor costs. Every state treats this issue slightly differently and has unique requirements for independent contractor classification, but [under Colorado law](#), workers are presumed to be employees unless they are shown to be free from control and direction in the performance of services and are customarily engaged in an [independent trade relating to the work performed](#).

### Consequences for Workers

Beyond [losing the safety](#) and assurance of workplace protections and benefits, independent contractors also have their tax burden substantially increased. Independent contractors become liable for both the employer and employee contributions to Social Security and Medicare (self-employment tax), accounting for an additional 15.3 percent of their income.

For those who have chosen to be independent contractors purposefully, these various drawbacks may be worthwhile in exchange for the flexibility they get from their alternative work arrangement. For workers who are treated as employees and required to meet employee expectations, but who did not decisively opt into an independent contractor relationship with an employer, being misclassified as an independent contractor can be uniquely harmful.

### Misclassification as a business model

*The following profile is based on a conversation with Joe Deras, lead organizer for IUPAT DC81, who currently works with workers to help them to resolve conflict with their employer. Names have been excluded to maintain the workers' privacy.*

A painting company based in Parker, Colorado has come to dominate the luxury multifamily residential painting market in the last 10 years, in no small part due to their early adoption — and exploitation — of the 1099 contractor model. Their standard model for hiring workers goes something like this: They interview a worker and hire them, but say they need to work a week to see if it works out. After that week, the worker gets called back into the office and given a new, lower wage rate than they were originally offered and told if they want to continue to work, they need to form an LLC and take out their own workers' compensation and liability insurance. Additionally, they need to procure their own tools. This can run up to \$500 initially, with another \$150 in yearly maintenance costs. If they want to get paid, the workers will need to submit their own invoices for their work. In other words, after just a week of employment, this company shifts every worker to a 1099 contract.

Once their contract is sorted out, workers are dispatched to a job site where they are effectively treated as employees: They are required to clock in and out with supervisors at predetermined times and their work is closely monitored and dictated by those supervisors. All "contractors" work nine-hour days and often an additional six hours on Saturdays, but aren't compensated for their overtime because they're classified as contractors. If workers fail to show up on time or take a side job with another company, they are reprimanded or fired. These workers are independent contractors on paper only.

The misclassification of workers is central, and essential, to this company's business model. In an incredibly competitive market where the costs of supplies are fixed and effectively the same for every company, the only way to lower costs and underbid the competition is to lower labor costs. This puts incredible pressure on companies to race to the bottom in terms of wages, benefits, and overall labor conditions. This is particularly true in construction industries that are less regulated by the state, where contracting companies have more leeway in who they hire and how well those workers are trained.

Businesses become successful at the expense of their workers. Because the practice of misclassification has become so widespread, workers have no other options and are forced to accept lower pay, worse conditions, and fewer protections.

## Industry-Wide Ramifications

The practice of misclassifying workers, while common in some industries, is harmful from an industry-wide perspective. Take the construction industry as an example: If some companies routinely misclassify their workers as independent contractors to lower costs, they will be able to underbid responsible companies that treat employees fairly under the law. This drives down the profit margin for the entire industry and makes it more difficult for law-abiding firms to survive. Shirking payments into the unemployment insurance system also [redistributes the costs](#) back onto law-abiding firms, making it more costly for good actors while bad actors are able to cheat the system.

When we spoke with one community activist, Joe Deras — the lead organizer for the International Union of Painters and Allied Trades District Council 81, which covers Colorado, Iowa, Nebraska, Western Illinois, and Wyoming — he suggested misclassification in less-regulated portions of the construction industry (painting, dry walling, etc.) has become so common in Colorado that it's practically impossible for a contractor to survive if they don't exploit the 1099 business model. Construction misclassification has become so widespread that Colorado instituted a [task force specifically to address it](#); however, work in this area is still ongoing and misclassification continues to be rampant.

In a competitive business where other costs are fixed, the only way to get ahead of the competition is to cut labor costs, but this leads to an industry-wide race to the bottom in wages and labor conditions. Misclassification, therefore, doesn't only hurt the workers, but also has ripple effects through the whole market.

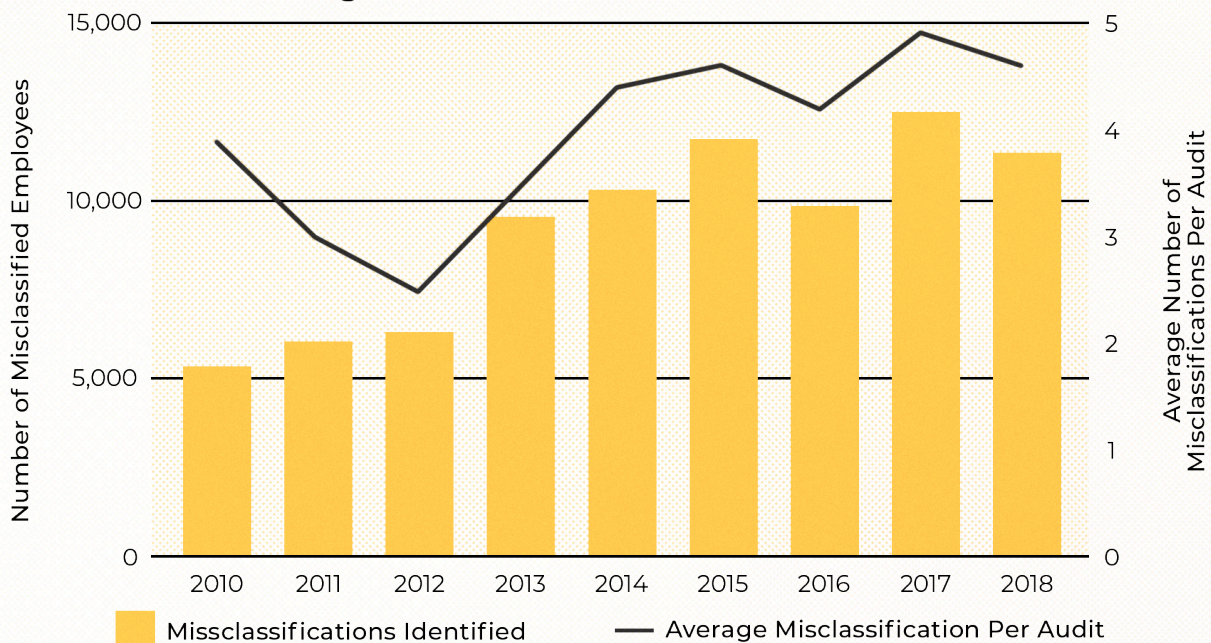
## Harmful for Colorado's Economy

An analysis by the U.S. Department of Labor estimates Colorado annually loses approximately [\\$167 million in income tax revenues](#) and more than \$700,000 of revenue for unemployment insurance from companies misclassifying their employees. The state also expends resources to investigate claims of misclassification, to provide classification opinions for companies, and to audit unemployment claims from misclassified employees.

Colorado companies found to have misclassified employees may be fined up to \$5,000 for the first misclassification and up to \$25,000 for each subsequent misclassification. Additionally, [when companies have been found to misclassify](#) more than one employee they are prohibited from contracting with or receiving any funds from the state for up to two years. These higher penalties may occasionally be [assessed on first-time offenders](#) if they are found to be willfully misclassifying with knowledge of their actions. Employers must also pay back the unemployment insurance premiums they owe for misclassified employees, with interest.

Though the possibility of these fines should help discourage companies from misclassifying employees, they aren't assessed frequently. To be caught, a company must have a complaint filed against it and be unable to justify its classification decisions or be randomly audited by the state. The savings companies can gain from misclassification frequently outweigh these potential fines from the state.

**Figure 7: Number of Misclassified Colorado Workers & Average Number of Misclassifications Per Audit**



## Unemployment Insurance Audits

In 2018, Colorado performed [2,469 unemployment insurance audits](#), amounting to an audit of 1.4 percent of all contributing employers. These audits uncovered [11,342 misclassified](#) employees, an average of 4.6 per audit. 2017's audits found a similar number of misclassified employees: [12,529 misclassifications were uncovered with 2,565 audits](#), a rate of 4.9 misclassifications per audit.

Unfortunately, it's difficult to extrapolate from these numbers to calculate a broader estimate of the total number of misclassified employees in Colorado because only some of the audits performed by Colorado are randomly assigned, while others are prompted by complaints against specific employers. One would expect that targeted audits likely result in a higher rate of misclassification findings than random audits, so they cannot be treated the same statistically. If we had estimates of the average number of misclassified employees per random audit and the number of random audits that were conducted, we could estimate the number of misclassified independent contractors statewide.

Based on the information we do have, the trends of misclassification uncovered by Colorado's audits suggest either CDLE's audits are becoming more effective, or the problem of misclassification is becoming more widespread. Audits for 2010-2013 found an average of 3.2 misclassifications per audit, while audits from 2013-2018 found an average of 4.54 misclassifications per audit.<sup>4</sup> Unfortunately, because of the non-random basis for selecting audits, we don't know which of these explanations is correct.

At least at the national level, [other reports](#) suggest the trend of misclassification is becoming more widespread. Either way, misclassification of employees in Colorado is a common problem depriving at least tens of thousands of workers basic workplace protections and benefits, creating unfair advantages for bad-actor companies, and depriving the state's coffers of substantial resources.

[Other studies](#) have shown misclassification varies by industry and, as one might expect, is most prevalent where it's most profitable for employers. For example, workers' compensation insurance premiums are especially high in construction, incentivizing misclassification so companies do not have to buy insurance for their workers. Misclassification is also common in industries where workers perform their duties at dispersed worksites and often in isolation, such as housecleaning, in-home care, and trucking. These industries are also known for employing large numbers of workers with less education and workers who are immigrants and may not have the resources to effectively advocate for themselves. This is compounded by independent contractors' inability to organize collectively. Additionally, these are low-wage industries where workers would be unlikely to be able to save their own rainy day fund to cover unexpected layoffs or days off for sick leave or caring for family members.

While only affecting a subset of the alternative workforce, misclassification presents clear problems for the state of Colorado, misclassifying firms' competitors, and workers themselves. Unfortunately, CDLE doesn't release any information breaking down common industries where misclassification is found, or any information about geographic dispersion of these misclassifications around the state. Raising the penalties for misclassification and increasing CDLE's audit capabilities could decrease the prevalence of misclassification, protecting workers, the state, and the broader competitive market.

## The Problem with Self-Reported Data

Like the misclassification phenomenon, there's broad disagreement about whether or not alternative workers in general are becoming more or less common in the American economy. The Census's Current Population Survey and other household surveys suggest self-employment, including independent contracting, has been trending down since the 1990s, and yet [administrative data from tax filings](#) suggest nontraditional work arrangements are increasing. This divergence in workers' self-reported understanding of their relationship with employers and their legal status is displayed in Figure 8.

The truth is, unfortunately, no one really knows if the independent contractor and broader alternative work arrangement phenomenon is becoming more prevalent. In order to assess these important questions, we need better data, which could be collected at the state level.

## Stronger, More Reliable Data Needed

Many of the findings in this report are derived from self-reported assessments of workers' circumstances. By using the survey data, we are able to evaluate differences based upon demographics such as gender and ethnicity, which are not available using tax records, however, we increase the likelihood of some reporting error. This reporting error may be particularly egregious in misclassified workers who may not see themselves

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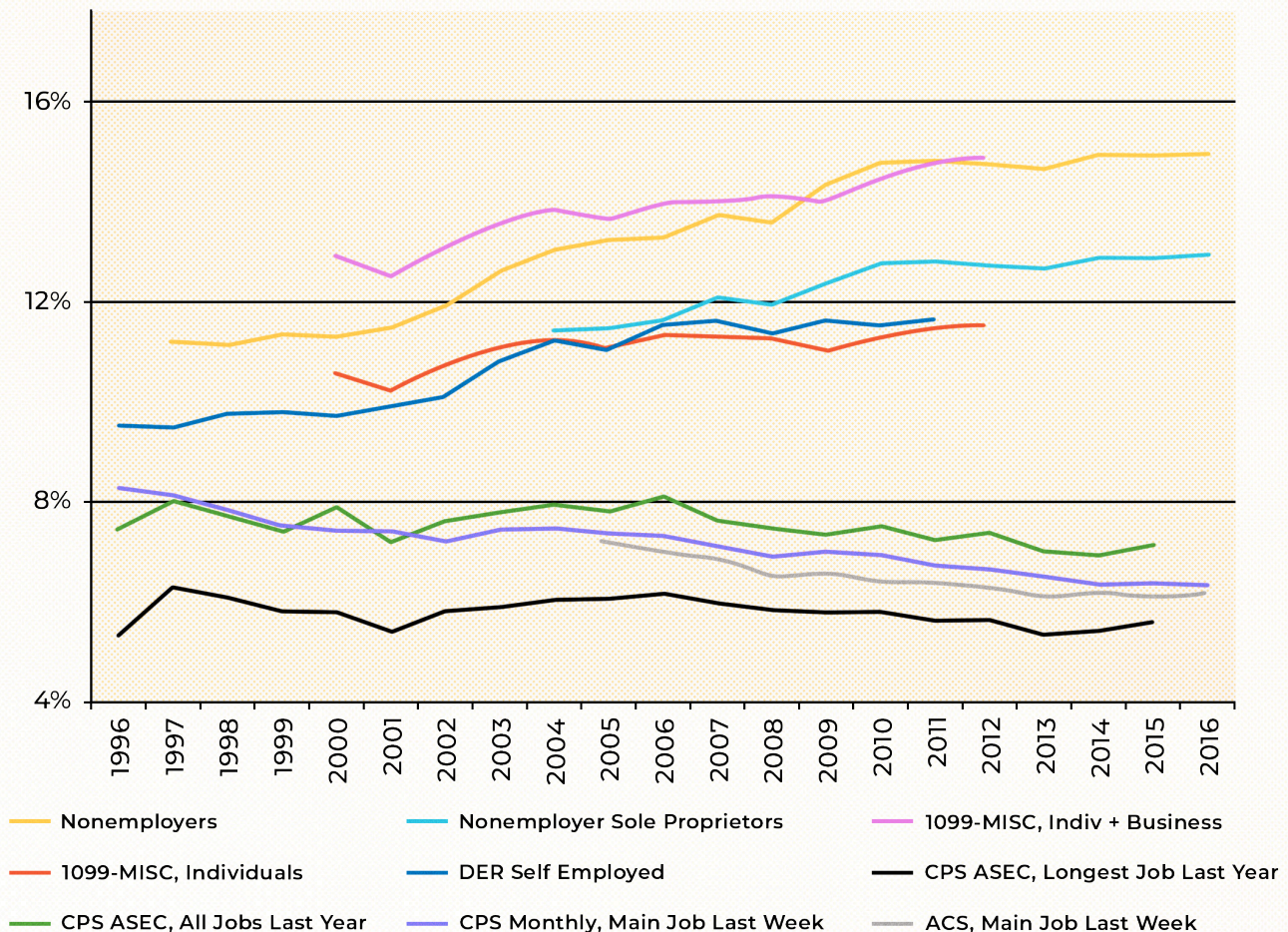
<sup>4</sup> 2010 audit results available [here](#), [2011](#), [2012](#), [2013](#), [2014](#), [2015](#), [2016](#), [2017](#), [2018](#)

as independent contractors or even know they are not technically employees. [Economists' work](#) suggests the self-reported numbers available from national surveys may substantially underestimate the phenomenon of independent contractors and alternative work arrangements.

This report offers a first look at the landscape of alternative work arrangements in Colorado, but it leaves many questions unanswered. How do the wages of alternative workers compare to those of traditional workers? Do workers choose alternative positions or are they forced into them by a lack of better options? Where do these workers get their benefits? Are there different trends in alternative work for different racial and ethnic groups? Different genders? Native Coloradans versus transplants? Parents? How have trends in alternative work changed over time, and how will they change in the future?

In order to answer these questions, we need better data on workers in alternative arrangements. We need to know their demographics, the type of work they are engaged in, their wages for this work, and how these patterns have changed, if at all, over time. Without this information, it's difficult to make informed decisions about this substantial portion of Colorado's workforce.

**Figure 8: Household Survey & Administrative Data Self-Employment Rates, 1996-2016**



Source: Recreated from [Measuring the Gig Economy: Current Knowledge and Open Issues](#).

## Policy Recommendations

In and of itself, the classification of workers as independent contractors is not problematic. What is problematic, however, is because of their classification, many Coloradans are left uncovered by the existing workplace safety net. There are a variety of steps that could be taken to maintain the flexibility of being an independent contractor while also extending basic workplace protections to all workers.

**Unemployment insurance and workers' compensation insurance should be expanded to require employers to cover independent contractors in addition to traditional employees.**

This could be done by requiring employers to pay into the state's unemployment insurance system at a fixed rate per hour worked by their independent contractors or a fixed percentage of independent contractors' wages, similar to how [Washington State proposed](#) funding a portable benefits marketplace for independent contractors. This would have the dual benefit of providing critical safety net coverage to an additional 10

percent of Colorado's workforce and increasing the costs of independent contractors for employers, thereby decreasing incentives to misclassify workers.

### **Penalties for misclassification should be increased.**

The current penalties for misclassification in Colorado do little to dissuade employers from shirking and misclassifying employees. It's estimated classifying an employee as an independent contractor saves employers up to [30 percent on payroll](#), and this number is likely even higher in industries with [expensive workers' compensation premiums](#) and frequent overtime hours. With current penalties only set at \$25,000 per misclassification when more than one employee is misclassified, if traditional employees cost employers \$75,000 or more per year, it may be cheaper to misclassify and pay the penalty than classify the employee correctly. When combined with the relatively small probability of actually being caught and fined, the cost-benefit calculation becomes worthwhile to employers at a much lower salary. For penalties to actually dissuade employers from misclassifying workers, they must be substantially higher.

### **In order to better understand the scope of misclassification in Colorado, CDLE should report audits disaggregated by whether they are random audits or targeted on the basis of complaints.**

Both types of audits are valuable, but only random audits can be used to extrapolate broader trends about misclassification over time. Greater transparency about the audit process could help us identify industries where misclassification is especially prevalent, as well as the types of workers most likely to be misclassified, and other important information.

### **As [discussions about a broader system of portable benefits](#) continue in Colorado, we must be mindful of what this would mean for nontraditional employees.**

In thinking about universal portable retirement plans, paid leave, health insurance, and other components of a broader benefits system, we need to be cognizant of how we plan to include independent contractors, part-time workers, temporary employees, and other nontraditional workers in these plans. Because they are already cut out of any existing workplace benefits employers may offer, these workers have even more to gain from a system of portable benefits than traditional workers. And yet, many existing proposals don't facilitate their inclusion.

Some states, [such as Washington](#), have proposed portable benefits programs intended specifically for independent contractors who do not have access to workplace benefits. And some existing portable benefits programs, such as [Oregon's portable retirement savings program](#), are open to individuals regardless of their employer, allowing independent contractors to opt in. [Massachusetts's paid leave program](#) goes further, requiring employers that utilize at least 50 percent independent contractors to contribute to those contractors' paid leave coverage.

All [three of the experts](#) commissioned by Colorado's FAMLI task force to study how to implement paid family and medical leave in Colorado mentioned the importance of covering self-employed and contract workers in some way. Without particular attention to this subpopulation of workers, it would be easy to design a portable benefits system that's open only through an employer, and therefore excludes independent contractors and other self-employed workers.

### **A critical first step will be gathering better and more comprehensive data about independent contractors and other alternative workers in Colorado.**

This report utilized the best publicly available data on the state of alternative work arrangements in Colorado, but our evaluation is limited by the lack of quality data assessing this phenomenon. We know there are substantial differences between self-reported independent contractors and data received from tax filings, but have very little insight into what creates this discrepancy or who these workers are. Due to small survey sample sizes, we also have limited information about the demographics of alternative workers or the types of industries they operate in within Colorado. Surveys, such as the Contingent Worker Supplement, also rely on self-reporting and in a complicated area such as independent contractor classification, self-reporting bias is more likely to underreport certain populations. Additionally, because surveys on alternative workers are not run regularly, we have limited information about how the alternative workforce has changed over time. By requiring the Department of Revenue and CDLE to collaborate and report on the landscape of alternative work arrangements in Colorado, we could gain invaluable information about a large, frequently overlooked subset of the workforce. This information could inform future policy decisions about worker classification, benefits systems, and workplace protections.