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# Joint Enforcement Strike Force

*On the Underground Economy*

## 2017 REPORT



This report was prepared by the Tax Branch of the California Employment Development Department (EDD).

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June 30, 2018

The Honorable Members of the California State Legislature  
California State Senate and Assembly  
State Capitol  
Sacramento, CA 95814

Dear Members of the California State Legislature:

Executive Order W-66-93 established the Joint Enforcement Strike Force (JESF) on the Underground Economy to combat the underground economy by pooling resources and sharing data among the state agencies charged with enforcing licensing, labor, and payroll tax laws. On January 1, 1995, Section 329 was added to the California Unemployment Insurance Code (CUIC), which placed the provisions of the Executive Order into law. This section contains a provision requiring the strike force to report to the Governor and the Legislature annually regarding its activities. This letter is being sent pursuant to Government Code Section 9795(a) that requires each legislative mandated report to include a summary of its contents not to exceed one-page in length, which is distributed to each member of the Legislature.

The JESF 2017 Report provides the annual summary of activities and outcomes from the JESF in accordance with Section 329(d) of the CUIC. This report includes the following contents:

- An overview of the JESF including information about strike force partners.
- Background information about the underground economy and the JESF's goals.
- Efforts made by the strike force to publicize its activities and to receive referrals from the public including web page view statistics.
- Informant contact statistics for the toll-free JESF hotline and other outlets.
- Narrative information about collaboration among the strike force partners and statistical results from collaborative efforts.
- Statistics and narratives about blatant violations and noncompliance with licensing, labor and payroll tax laws identified, audited, investigated, or prosecuted through civil actions or criminal prosecution.

Printed copies of this report are available to any legislative member upon request. The report can also be viewed online at [www.edd.ca.gov/About\\_EDD/EDD\\_Legislative\\_Reports.htm](http://www.edd.ca.gov/About_EDD/EDD_Legislative_Reports.htm).

Sincerely,

/s/ PATRICK W. HENNING  
Director

## **JOINT ENFORCEMENT STRIKE FORCE OVERVIEW, MEMBERS, AND PARTICIPATING ENTITIES**

This legislatively mandated report provides the annual summary of activities and outcomes from the Joint Enforcement Strike Force (JESF) on the Underground Economy in accordance with Section 329(d) of the California Unemployment Insurance Code (CUIC). In October 1993, Executive Order W-66-93 established the JESF to combat the underground economy by pooling resources and sharing data among the state agencies charged with enforcing licensing, labor, and payroll tax laws.

On January 1, 1995, Section 329 was added to the CUIC, which placed the provisions of the Executive Order into law. The Employment Development Department (EDD) is the designated lead agency of the JESF, and the EDD Director or designee serves as its chair. The JESF members are as follows:

The **EDD – Tax Branch** works with employers to collect California’s payroll taxes and data to support the employment security, child support, and personal income tax programs. The Tax Branch ensures the integrity of the employment tax program by collaborating with our customers to provide efficient, responsive, and innovative services. The Tax Branch is committed to providing service to California employers and Unemployment Insurance (UI), Disability Insurance (DI), and Paid Family Leave (PFL) benefit claimants; and to increasing voluntary compliance with payroll tax laws through education, simplified reporting processes, and the promotion of fair business competition. The Tax Branch is responsible for coordinating the EDD’s efforts at combating the underground economy and is also responsible for leading and coordinating the activities of the JESF as a whole.

The **EDD – Investigation Division (ID) Criminal Tax Enforcement Program** conducts criminal investigations at the county, state, and federal levels and seeks prosecutions of employers who commit payroll tax fraud against the EDD. Tax fraud includes employer failure to register with the EDD as an employing unit, failure to report or underreporting wages paid to employees, and failure to remit tax contributions to the EDD. The program also seeks restitution that includes recovery of benefit overpayments, tax liabilities, penalties, interest, and investigation costs. Court ordered restitution, imprisonment, and probation serve as fraud deterrents. The ID, Tax Branch, UI, and DI Branch work together to address fictitious employer schemes created to perpetrate fraud against the EDD. They identify potential fictitious employer schemes based on thorough and ongoing evaluation of the characteristics and elements of such schemes. The identification of these fictitious employer schemes allows the EDD to increase detection and elimination of fraudulent UI and DI benefit claims filed against the EDD.

The **Department of Consumer Affairs (DCA)** protects and serves California consumers and ensures a competitive and fair marketplace. The DCA helps consumers learn how to protect themselves from unscrupulous and unqualified individuals. The DCA protects professionals from unfair competition by identifying unlicensed practitioners.

The **DCA – Contractors State License Board (CSLB)** protects consumers by licensing and regulating California's construction industry. There are approximately 290,000 licensed contractors in the state, in 44 different licensing classifications. In addition to consumer education on contractor and construction law, CSLB activities include: administer prospective licensee examinations; issue licenses; investigate complaints against licensed and unlicensed contractors; issue citations; suspend or revoke licenses; and seek administrative, criminal, and civil sanctions against violators. The Statewide Investigative Fraud Team is set up to monitor and combat illegal activity. They have teams throughout the state that conduct sting operations on a regular basis and sweep construction sites. They also conduct joint operations and sweeps with other state agencies dedicated to combatting the underground activity.

The **DCA – Bureau of Automotive Repair (BAR)** investigates general auto repair complaints and ensures that shops comply with Smog Check statutes. The BAR staff investigates complaints related to auto repair and/or Smog Check inspections and negotiates with the shop on the consumer's behalf to achieve a mutually agreeable resolution. The bulk of complaints are resolved by mediation. Each year, the BAR negotiates millions of dollars in rework, refunds, and adjustments on behalf of consumers.

The **DCA – Bureau of Security and Investigative Services (BSIS)** protects consumers by licensing and regulating the following industries: alarm company operators and alarm company employees, locksmith companies and locksmith company employees, private investigators, private patrol operators and security guards, proprietary private security employers and officers, reposessor agencies and reposessor agency employees, and training facilities and training instructors. As part of its mission, the BSIS actively investigates complaints against its licensees and works to punish unlicensed business operations. This includes the suspension and revocation of licenses and seeking administrative, criminal, and civil sanctions against violators. Undercover sting and sweep operations are conducted on an ongoing basis throughout California. The BSIS also educates consumers, administers examinations to validate prospective licensees, and issues licenses and permits.

The **Department of Industrial Relations (DIR) - Division of Labor Standards Enforcement's (DLSE), Bureau of Field Enforcement** is responsible for the investigation and enforcement of statutes covering workers' compensation insurance coverage, child labor, cash pay, unlicensed contractors, Industrial Welfare Commission orders, and group claims involving minimum wage and overtime claims. The Bureau of Field Enforcement also handles criminal investigations involving these group claims.

The **DIR – Division of Occupational Safety and Health's (DOSH) (Cal/OSHA)** enforcement unit has jurisdiction over every employment situation and place of employment in California, which is necessary to adequately enforce and administer all occupational safety and health standards and regulations. They conduct inspections of California workplaces in response to a report of an industrial accident, a complaint about an occupational safety and health hazard, or as part of an inspection program

targeting industries which have a high rate of occupational hazards, fatalities, injuries, or illnesses.

The **California Department of Insurance (CDI)** ensures that consumers are protected; the insurance marketplace is fostered to be vibrant and stable; the regulatory process is maintained as open and equitable; and the law is enforced fairly and impartially. The **Fraud Division** is charged with investigating insurance fraud, which includes the crimes of intentional misrepresentation of payroll and employee staffing in order to obtain lower rates for workers' compensation insurance. Studies suggest that the aggressive anti-fraud campaign by the CDI, the district attorneys, the insurance industry, and California employers continue to play a substantial role in reducing crime and help lower workers' compensation insurance premiums for employers statewide.

The **Franchise Tax Board's (FTB)** primary function is to administer the California Revenue and Taxation Code (R&TC). Elected officials determine the tax policy for raising revenue. Under the direction of the FTB's Chief Law Enforcement Officer, the **Criminal Investigation Bureau (CIB)** enforces the criminal provisions of the R&TC. The CIB's principal mission is to identify, investigate, prosecute, and deter tax evasion and fraud, and encourage compliance with California income tax laws while maintaining the public's trust through publicity. Special agents with full peace officer powers investigate alleged criminal violations of the R&TC, principally income tax fraud and evasion, and assist in prosecuting non-compliant individuals. The special agents' efforts are supported by forensic auditors, collectors, analysts, and support staff; basically a micro-organization all in one bureau. The CIB also relies on a strong collaborative enterprise to accomplish their mission.

The **California Department of Tax and Fee Administration (CDTFA)** administers sales and use tax, special tax, and fee programs. These tax and fee programs were administered by the Board of Equalization (BOE) prior to July 1, 2017. The CDTFA's **Investigations Division** plans, organizes, directs, and oversees all criminal investigative activities for the various programs administered by the CDTFA. Its goals are to identify tax evasion and new fraud schemes, and actively investigate and assist in the prosecution of individuals who are violating the laws administered by the CDTFA.

The **Department of Justice's** Attorney General works to protect California's workers, legitimate businesses, and taxpayers through the **Underground Economy Unit**. The Underground Economy Unit brings civil and criminal actions against persons engaged in the underground economy. It has used California laws to obtain restitution of unpaid wages, civil penalties, and injunctions to bring businesses into compliance with applicable labor, tax, and licensing laws. These enforcement efforts deter underground economy violations, recapture lost revenues, and protect workers and legitimate businesses from illegal and predatory enterprises. The Underground Economy Unit has prosecuted cases involving: wage, tax, and insurance issues including the theft of wages, unpaid overtime, denial of breaks, payroll tax evasion, and misclassification of employees as independent contractors; patterns of safety violations leading to fatal

workplace injuries; workers' compensation insurance premium fraud; and the illegal avoidance of workers' compensation coverage for employees.

The **California Department of Alcoholic Beverage Control's (ABC)** agents are peace officers under Section 830.2 of the California Penal Code (PC) and are empowered to investigate and make arrests for violations of the Business and Professions Code that occur on or about licensed premises. Agents are further empowered to enforce any penal provisions of the law in the state. Licensees who violate state laws or local ordinances are subject to disciplinary action and may have their licenses suspended or revoked. These licensees are entitled to a hearing before an Administrative Law Judge and an appellate process to the State Supreme Court.

The **United States Department of Labor's (USDOL)** mission is to foster, promote, and develop the welfare of the wage earners, job seekers, and retirees of the United States; improve working conditions; advance opportunities for profitable employment; and assure work-related benefits and rights. The **Fair Labor Standards Act** prescribes standards for wages and overtime pay, which affect most private and public employment. The act is administered by the **Wage and Hour Division**. It requires employers to pay covered employees, who are not otherwise exempt, at least the federal minimum wage and overtime pay of one and one-half times the regular rate of pay. For non-agricultural operations, it restricts the hours that children under age 16 can work and forbids the employment of children under age 18 in certain jobs deemed too dangerous. For agricultural operations, it prohibits the employment of children under age 16 during school hours and in certain jobs deemed too dangerous. The Wage and Hour Division also enforces the labor standards provisions of the **Immigration and Nationality Act** that apply to aliens authorized to work in the United States under certain non-immigrant visa programs (H-1B, H-1B1, H-1C, H2A).

The **United States Internal Revenue Service's (IRS)** mission is to provide America's taxpayers quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness. In fiscal year 2016, the IRS collected \$3.3 trillion in taxes (gross tax receipts before tax refunds of \$426 billion) and processed over 244 million tax returns and other forms. The IRS provides the EDD with leads that are used for various JESF activities, including investigating employers with unreported wages and/or misclassified workers.

## BACKGROUND AND PROGRAM INFORMATION

### The Underground Economy

*“America has two economies, and one is flourishing at the expense of the other. First, there’s the legitimate economy, in which craftsmen are licensed and employers and employees pay taxes. Then there’s the fast-growing underground economy, where millions of workers are paid off-the-books, their incomes largely untaxed.”*

--“Going Underground”, Barron’s Online, January 3, 2005.

The size of the underground economy is difficult to measure but the following data points help to illustrate its magnitude:

- The tax gap is defined as the amount of tax liability faced by taxpayers that is not paid on time. Tax gap estimates for tax year 2006, released by the IRS in 2012 and adjusted for audit and collection activities, estimate that in 2006 the net national tax gap was approximately \$385 billion.
- In its March 2015 report, California’s Little Hoover Commission indicated, “The underground economy also robs the state of an estimated \$8.5 billion to \$10 billion in uncollected tax revenue, money that could fund education, law enforcement or long-overdue infrastructure investments or reduce taxes for the majority of Californians who play by the rules.”

Reports on the underground economy indicate it imposes a significant burden on revenue needed to fund critical state programs and on businesses that comply with the law. When businesses operate in the underground economy, they gain an unfair advantage over businesses that comply with labor, licensing, and payroll tax laws. This causes unfair competition in the marketplace and forces law-abiding businesses to pay higher taxes and expenses due to socialized costs.

Workers of non-compliant businesses are also affected. Their working conditions may not meet the legal requirements, which can put them in danger. Their wage earnings may be less than what is required by law, and benefits they are entitled to can be denied or delayed because their wages are not properly reported. Consumers can also be affected when contracting with unlicensed businesses. Licensing provisions are designed to ensure sufficient skill and knowledge to protect consumers.

## Joint Enforcement Strike Force Goals

The JESF's goals are to help restore economic stability and to improve working conditions and consumer and worker protection in the state. Specifically, the JESF works to:

- Eliminate unfair business competition.
- Protect workers by ensuring that they receive all compensation, benefits, and worker protections they are entitled to by law relating to their employment.
- Protect consumers by ensuring that all businesses are properly licensed and that they adhere to the state's consumer protection regulations.
- Reduce the burden on law-abiding citizens and businesses by ensuring that all businesses and individuals comply with the state's licensing, regulatory, and payroll tax laws.
- Reduce the tax gap by increasing voluntary compliance with the state's payroll tax laws to maximize the state's General and Special Funds.

## INFORMATION REQUIRED BY SECTION 329(d) OF THE CALIFORNIA UNEMPLOYMENT INSURANCE CODE

### Informant Contacts

Allegations of violation of payroll tax, labor, and licensing laws may be reported by telephone to the toll-free JESF hotline at 800-528-1783. Informants may also submit information about state payroll tax fraud by the following methods:

- Completing a [Fraud Reporting Form](#)
  - online via the EDD website
  - via e-mail to [ueo@edd.ca.gov](mailto:ueo@edd.ca.gov)
  - via correspondence by fax to 916-227-2772
- Completing and mailing an *Underground Economy Operations Lead Referral/Complaint Form*, available in English ([DE 660](#)) and Spanish ([DE 660/S/](#)).

In 2017, the EDD received a total of 3,513 allegations broken down as follows:

- 1,641 allegations via telephone calls to the JESF hotline
- 1,668 allegations via online submission (EDD website or email)
- 204 allegations via correspondence (fax or mail)

## Publicity and Marketing Outreach Strategies

The JESF publicizes its activities, outreach, and education on the underground economy through the following:

- The [Joint Enforcement Strike Force website](#) received 1,146 page views in calendar year 2017. It was created to:
  - Provide information on how to report fraud to the JESF.
  - Educate readers about the harm caused by the underground economy.
  - Publicize the work being done by California state government and partner agencies.
  - Deter fraudulent activity by communicating that California state government will actively pursue and punish those who participate in the underground economy.
  - Provide contact information for each of the partner agencies.
- Information on the underground economy is included on the following website: [www.edd.ca.gov/Payroll\\_Taxes/Underground\\_Economy\\_Operations.htm](http://www.edd.ca.gov/Payroll_Taxes/Underground_Economy_Operations.htm). It provides the viewer with data, access to prior reports, program and operation information, etc. In calendar year 2017, the website received 4,733 page views.
- The EDD has a web section dedicated to [fraud and penalties](#). It provides information so that both benefit recipients and employers can avoid serious costs and consequences by learning more about their roles and responsibilities when it comes to providing required information for collecting benefits or reporting employee data. In calendar year 2017, it received 84,615 page views. Within the fraud and penalties section is a special page dedicated to informing the public about cases the EDD is involved with for [prosecuting fraud](#). In calendar year 2017, it received 54,727 page views.
- The EDD includes articles about efforts to combat the underground economy in its *California Employer* newsletter and internally in the *EDD Scene* employee newsletter. The *California Employer* newsletter, [third quarter of 2017 edition](#), included an article about fraud titled, *Fraud Hurts Everyone: If You See It, Report It*.
- The EDD receives speaker requests from employer groups, trade associations, and others asking for information about what the EDD is doing to combat the underground economy. The EDD shares information such as results of its Investigation Division and the JESF as well as its Compliance Development Operations, Audit, and Collection Programs.
- The Small Business Employer Advisory Committee is a group of diverse associations representing small business employers throughout California. The committee interactively provides the EDD with recommendations on how to better serve California's small businesses and disseminates information to their respective members.
- A variety of information sheets and publications are available to the public, businesses, taxpayers, and tax practitioners. These include:

- *Joint Enforcement Strike Force Brochure* ([DE 665](#))
  - *Information Sheet: Employment Enforcement Task Force* ([DE 631](#))
  - *Information Sheet: Employment Development Department Underground Economy Operations* ([DE 631UEO](#))
- The JESF member agency staff conducts outreach presentations to business and labor organizations throughout the state and to representatives of local government agencies.

## **Blatant Violations and Non-compliance**

The EDD works with the JESF partner agencies to conduct joint on-site business inspections to identify employers who operate in the underground economy. The EDD also conducts desk investigations using various databases and income tax return analysis to detect non-compliance and fraud. When these inspections and investigations reveal non-compliance, the case is referred as an audit lead to the EDD’s Audit Program. In addition, the EDD receives verified audit leads from the IRS through the Questionable Employment Tax Practices (QETP) Program.

### Employment Development Department Cumulative JESF Results

Following are the EDD’s cumulative results from JESF inspections, investigations, and QETP leads, as well as the audit and collection actions stemming from JESF activities:

<b>Calendar Year*</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Joint Inspections	583	600	569
EDD Audit Referrals	1,145	658	510
EDD Payroll Tax Audits Completed	664	512	408
EDD Payroll Tax Assessments on Above Audits	\$27,596,182	\$21,185,695	\$18,120,024
Previously Unreported Employees on Above Audits	9,981	6,329	6,165
Payroll Tax Assessments Collected	\$6,038,304	\$5,437,986	\$6,391,525

\*Results fluctuate year-to-year based on the complexity of cases, staffing, and external lead referrals.

The following is additional information on the cumulative results from JESF activities:

<b>Calendar Year*</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
EDD Payroll Tax Audits with Fraud Penalty Assessed (included in figures above)	26	12	7
EDD Payroll Tax Assessments on Fraud Audits (included in figures above)	\$5,245,162	\$2,148,204	\$4,443,031
Previously Unreported Employees on Fraud Audits (included in figures above)	429	278	183

\*Results fluctuate year-to-year based on the complexity of cases, staffing, and external lead referrals.

### Criminal Tax Enforcement Program Results

For cases warranting criminal investigation, the EDD ID's Criminal Tax Enforcement Program works with law enforcement agencies and the JESF partner agencies throughout California to identify and prosecute those responsible for the criminal activities. Following are the EDD Criminal Tax Enforcement Program results for the calendar years 2015, 2016, and 2017:

<b>Calendar Year*</b>	<b>2015</b>		<b>2016</b>		<b>2017</b>	
Type of Action	# of Cases	Amount of Tax Liability	# of Cases	Amount of Tax Liability	# of Cases	Amount of Tax Liability
Payroll Tax Evasion Cases in Progress	187	\$99,915,619	139	\$93,844,110	144	\$97,305,930
EDD Criminal Complaints Filed	10	\$2,617,289	25	\$11,499,801	10	\$1,867,242
EDD Criminal Prosecutions Completed	51	\$56,650,246	7	\$1,667,143	22	\$4,683,279

\*Results fluctuate year-to-year based on the complexity of cases, staffing, and external lead referrals.

### Criminal Restitution Cases Monitored and Payments Received

When the court orders restitution to the EDD as part of the sentencing during criminal prosecutions, the EDD monitors these cases to ensure that the restitution is made. Following are the results of restitution monitored for the calendar years 2015, 2016, and 2017:

<b>Calendar Year</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Criminal Restitution Cases Monitored	79	84	91
Payments Received on Restitution Cases	\$1,022,994	\$329,584	\$2,459,397

### Contractors State License Board Legal Actions

Each month, the CSLB conducts stings and sweeps, which resulted in 1,848 legal actions for the calendar year 2017. As a result of the 761 licensee and non-licensee citations, the CSLB assessed \$700,250 in civil penalties.

<b>Calendar Year</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Accusations	3	10	12
Administrative Licensee Citations	350	409	432
Criminal Referrals – Licensee	33	90	170
Criminal Referrals – Non-Licensee	743	791	905
Administrative Non-Licensee Citations	426	347	329
Total Legal Actions	1,555	1,647	1,848

### Contractors State License Board Stop Orders

In calendar year 2017, there were 667 stop orders served on construction employers, which prohibits the use of employee labor until workers' compensation insurance is obtained.

<b>Calendar Year</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Licensee Stop Orders Issued	259	258	366
Unlicensed Operator Stop Orders Issued	231	178	301
Total Stop Orders Issued	490	436	667
Policies Obtained	200	165	241
Licenses Suspended	31	49	26

### Contractors State License Board Stings and Sweeps

The CSLB performed 76 stings and 320 sweeps during the calendar year 2017. The sting operations targeted unlicensed repeat offenders and wanted criminals who work in the construction industry. The stings involved the CSLB's Statewide Investigative Fraud Team inviting the suspected unlicensed contractors and wanted criminals to homes to

place bids on home improvement projects. The suspects were found by searching advertisements on Craigslist and local Yellow Pages and leads from the CSLB's Intake Mediation Center. Construction site inspections or sweeps are also an effective way that the CSLB ensures contractor compliance with California's licensing and workers' compensation insurance requirements. Investigators with CSLB's Statewide Investigative Fraud Teams fan out throughout the year with investigators from partner agencies, showing up unannounced at active construction sites to check for appropriate licenses, permits, workers' compensation insurance for employees, and adherence to safety rules.

<b>Calendar Year</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Stings	91	84	76
Sweeps	148	243	320

United States Department of Labor Garment Industry Investigations

Following are results of the USDOL, Wage & Hour Division garment industry investigations in California for the last three calendar years.

<b>Calendar Year</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Completed Investigations	182	265	149
Back Wages	\$1,763,682	\$3,604,675 (+\$116,290 liquidated damages)	\$1,950,076 (+\$127,887 liquidated damages)
Civil Money Penalties	\$275,687	\$292,077	\$66,941
Number of Employees Affected	1,492	2,306	1,609

United States Department of Labor Recycling Center Investigations

Following are results of the USDOL, Wage & Hour Division recycling center investigations in California for the last three calendar years.

<b>Calendar Year</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Completed Investigations	39	101	174
Back Wages	\$404,861 (+\$313,088 liquidated damages)	\$597,688 (+\$509,121 liquidated damages)	\$509,331 (+\$360,309 liquidated damages)
Number of Employees Affected	288	288	292

## Division of Labor Standards Enforcement Results

Following are results by industry of the Division of Labor Standards Enforcement JESF inspections for the last three calendar years.

	Number of Inspections			Number of Citations		
	2015	2016	2017	2015	2016	2017
Automotive	19	6	8	19	6	12
Car Wash	2	16	1	5	24	1
Construction	79	22	2	35	23	5
Garment	1	1	0	2	1	0
Other	101	74	97	87	101	129
Restaurant	78	58	31	87	56	29
Retail	24	16	16	27	12	33
Total	304	193	155	262	223	209

Total Dollar Amount of Penalties Assessed			
	2015	2016	2017
Automotive	\$205,807	\$33,331	\$113,986
Car Wash	\$27,300	\$161,520	\$10,000
Construction	\$178,080	\$77,300	\$41,250
Garment	\$6,050	\$1,900	\$0
Other	\$860,695	\$814,328	\$1,082,514
Restaurant	\$1,085,354	\$803,421	\$659,191
Retail	\$340,825	\$202,796	\$228,155
Total	\$2,704,111	\$2,094,596	\$2,135,096

## License Suspensions/Holds Requested

The ability of state agencies to suspend/hold a license needed to legally operate certain types of businesses in this state is a valuable collection tool for resolving delinquent tax liabilities and for compelling corrective action. There are three types of licenses that the EDD can request other state agencies to suspend/hold if the licensee is delinquent in paying amounts due to the EDD:

- Contractor License (CSLB Hold): The Business and Professions Code Section 7145.5 authorizes the CSLB to take disciplinary action against a license holder. Once the CSLB receives the request from the EDD to place a hold, the CSLB will suspend the license. In addition, the CSLB will search their database for all licenses with the same personnel of record and suspend those licenses as well. The licenses remain suspended until the delinquency that led to the suspension has been resolved or arrangements have been made to pay it.
- Liquor License (ABC Hold): The Business and Professions Code Section 24049 authorizes the EDD to request from the ABC a hold to be placed on certain types of liquor licenses. A hold establishes a priority for the EDD to any monies received from

the sale of the liquor license and prevents the transfer of a liquor license from the seller to a buyer until the conditions of the hold have been met.

- **Farm Labor Contractor License (FLC Hold):** The EDD is authorized by Section 1141 of the CUIIC to notify the Labor Commissioner (of the DLSE) in writing that an FLC is delinquent in payment of worker contributions either by self-assessment or by a final EDD assessment. California Labor Code (LC) Section 1690.1 authorizes the Labor Commissioner to refuse to issue or renew any license until the licensee has fully paid the amount of the delinquency.

License Suspensions/Holds by Category Requested by the Employment Development Department for the Last Three Calendar Years

Type of Hold	2015	2016	2017
CSLB	631	557	578
ABC	111	88	40
FLC	8	15	16

Contractors State License Board License Suspensions

A license can be suspended by the CSLB if the licensee is delinquent in paying amounts due to the CSLB or other state agencies. The table below summarizes amounts due to state agencies that were collected or resolved in calendar years 2015, 2016, and 2017 to avoid a license suspension or to have a suspended license reinstated.

Calendar Year	Amounts Collected or Resolved		
	2015	2016	2017
CSLB	\$130,980	\$132,782	\$123,507
EDD	\$22,730,753	\$13,707,896	\$14,000,400
DIR-Cal/OSHA	\$815,684	\$784,421	\$445,698
DIR-DLSE	\$937,674	\$661,066	\$1,270,108
FTB	\$2,926,488	\$5,985,942	\$7,141,353
Totals	\$27,541,579	\$21,272,107	\$22,981,066

**Information Sharing**

Businesses that operate in the underground economy constantly develop new schemes to avoid detection of their illegal activities. As these new schemes are identified by the JESF members, information regarding the schemes is shared with member agencies, business associations, and labor organizations. There is an ongoing need for the JESF staff to be aware of the various types of schemes used in industries prone to underground economy activity. This knowledge transfer facilitates the development of detection and enforcement techniques necessary to deter and stop the illegal activities. Information is shared as follows:

- On-the-job.
- Informal ad-hoc joint management meetings.

- Quarterly meetings with member agencies.

## Collaboration

As the lead agency, the EDD participates in all JESF inspections. The other JESF partners participate in inspections when there is a potential violation of the laws they enforce. The table below highlights JESF collaboration efforts. It shows the number of business inspections that partner agencies participated in during calendar years 2015, 2016, and 2017.

Agency	Calendar Year		
	2015	2016	2017
EDD	583	600	569
DLSE	304	193	155
CSLB	183	303	342
Local Police	95	79	44
District Attorney	80	74	40
ABC	23	25	8
CDTFA	1	1	1
BAR	0	9	2
BSIS	8	13	1
CDI	*	49	11
FTB	*	25	0
Cal/OSHA	*	19	3
DMV	*	6	0
Other	96	64	48

\* Participation by these entities was included in the "Other" category in calendar year 2015.

As a result of numerous complaints about nail salons misclassifying workers as independent contractors, paying unreported cash wages, labor law violations, etc., the EDD along with the DIR conducted two successful operations on nail salons during calendar year 2017. Below are the results from these operations.

Nail Salon Inspections	Number Found With Unreported Workers and Wages	Number Referred to EDD Audit Program	Number Found With DIR Labor Law Violations	DIR Stop Orders Issued	DIR Issued Citations
23	16	16	18	18	\$256,200

The Interagency Tax Collection Committee is an alliance with the EDD, FTB, CDTFA, IRS, Attorney General, State Controller, and various county recorders. It provides a forum to share common collection practices in order to increase compliance and resolve collection issues. It also allows the agencies to meet and share information about their collection programs, focusing on common, competing, and overlapping functions including bankruptcy, lien, and levy issues. It is intended to foster communications and

allow collection staff to meet their counterparts, establish working relationships, and encourage cooperation on common tax collection issues.

During the past several years, Memoranda of Understanding have been developed to facilitate the sharing of information and data between enforcement partner agencies and to enhance collaboration and joint enforcement of labor, tax, and licensing laws.

#### The Joint Enforcement Strike Force/Labor Enforcement Task Force Collaborative Enforcement Partnership

To help combat California's underground economy and protect workers' rights, the DIR and EDD have joined efforts through their respective enforcement programs, namely, the JESF and Labor Enforcement Task Force (LETF), to coordinate activity and share effective strategies.

The JESF/LETF Collaborative Enforcement Partnership merges best practices based on a wide range of experiences and innovation. The joint effort draws upon both programs' respective strengths through training, refinement of targeting methods, and strategic planning. While the JESF and LETF remain under the guidance of their respective agencies, enforcement coordination has allowed a streamlining of administration to leverage resources and mitigate overlap. The results include broader statewide operations, stronger communications, and knowledgeable cross-trained staff.

The DIR periodically hosts JESF/LETF joint training sessions, at which investigators and supervisors from around the state come together to share best practices on joint enforcement operations.

Attachment A to this report offers some examples of JESF cases, both blatant violation investigations and joint criminal prosecutions.

## **BLATANT VIOLATOR CASES**

The following examples of blatant violation cases detected by the JESF include the most flagrant cases where schemes were used by businesses to avoid payroll tax, labor, insurance, and licensing laws, and where the EDD found fraud or intent to evade payment of payroll taxes.

### **Blatant Violator Investigation Cases**

- The EDD received a complaint from a former employee of a security guard business indicating that no deductions were made from her paycheck and she did not receive a pay stub. She indicated the business had approximately 100 employees. An initial investigation indicated the business was registered with the EDD but the wages of the former employee had not been reported to the EDD. The business only reported wages for 27 employees. A review of databases revealed that the business underreported its workers and wages to the EDD. The amount reported as salaries and wages on the business's corporate income tax return was significantly more than the employee wages that had been reported to the EDD for the year. An EDD audit was conducted and revealed that the employer maintained a second set of records and had misclassified workers such as security guards, telemarketers, and office workers as contractors. The business did not issue pay stubs, Form 1099s, W-2s, or any other wage documents to these workers. The audit covered the period of 2011 to 2016. A fraud penalty was charged under Section 1128 of the CUIIC. The company was assessed \$2,585,767 for unpaid payroll taxes, penalties, and interest.
- The DLSE received a complaint about a retail furniture store operating as a sole proprietorship. The complaint indicated the business required its employees to work a 60 hour workweek but did not pay them the correct overtime rate. The DIR conducted an inspection and found additional violations. The DLSE inspection report, the complaint form, and some payroll records were provided to the EDD. Employees of the business were interviewed and some indicated they had worked for the company for many years. The employees worked as delivery drivers and sales staff. They were paid in cash and worked 60 hours a week. The business was not registered as an employer with the EDD but it had a workers' compensation insurance policy indicating the business had only two employees. The city business license application also indicated that the business had only two employees. The owner of the business refused to provide records for an audit. A fraud penalty was charged under Section 1128 of the CUIIC for intent to evade. The employer was assessed \$704,971 for unpaid payroll taxes, penalties, and interest.

## ATTACHMENT A (Continued)

- The EDD and the CSLB conducted an inspection of a contractor who specializes in home remodeling. During the inspection, three workers were observed performing construction labor. The business which is a corporation had registered with the Department in 2001 and reported approximately five workers each quarter. A subsequent audit revealed the corporation paid its acknowledged employees through a corporate checking account and correctly reported them as employees to the EDD. However, other workers performing the same type of service were paid from a separate business checking account and were not reported as employees. Additional workers were paid in cash and not reported to the EDD. Minimal records were provided for the audit and no explanation was given as to why some workers were reported and others were not. Since the business concealed wage payments to the workers, a fraud penalty was charged under Section 1128 of the CUIA for intent to evade. The corporation was assessed \$663,413 for unpaid payroll taxes, penalties, and interest.
- The EDD and CSLB conducted an inspection of a general contractor operating as a sole proprietorship who specializes in framing, renovation/remodeling, home additions, and custom home construction. During the inspection, 10 workers were observed on the construction site. Some of the workers interviewed indicated they had worked for the company consistently for up to three years. The workers indicated they were paid in cash. A preliminary investigation revealed since its inception in 2000, the business has only sporadically reported a minimal number of employees to the EDD. A subsequent audit revealed that when the business started in 2000, the employer registered as an employer with the EDD and reported wages. The employer then inactivated its EDD employer account in 2005 indicating it had no business activity, and then reinstated its account in 2013. However, information was found indicating the business had been active and operational with employees since its inception. In addition, the employer issued 1099s to workers that were previously reported as acknowledged employees. The same employees were reported to the EDD as acknowledged employees again in later years. The employer also failed to report the workers whom the EDD and CSLB inspectors observed performing services during the site inspection. Despite repeated requests, the employer failed to provide the required records for an audit. The employer acknowledged paying cash to the workers without providing deduction statements, and not keeping records of the cash payments. The employer had knowledge of the reporting requirements and chose to evade the tax liabilities by paying cash and concealing the cash payments. A fraud penalty was charged under Section 1128 of the CUIA for intent to evade. The employer was assessed \$408,230 for unpaid payroll taxes, penalties, and interest.

### **Joint Criminal Prosecution Cases**

The JESF member agencies refer criminal cases to the EDD for joint investigation with their respective criminal investigation organizations. The following are cases that JESF

## ATTACHMENT A (Continued)

member agencies worked together with the ID to prosecute in 2017. They are also posted to the EDD's [prosecuting fraud](#) web page.

- The ID in participation with the Inland Empire Premium Fraud Task Force conducted an investigation of three corporations in Riverside County. Since 2005, three representatives of the corporations paid their employees in cash for overtime worked and failed to report additional wages with the intent to under report the wages to the EDD. Two of the employer representatives pleaded guilty to felony violations of the California Insurance Code (CIC) and PC. They were each sentenced to 36 months of formal probation with up to 16 days in custody. As part of the plea agreement, these two employer representatives were ordered to pay \$478,659 in restitution to the EDD. A third employer representative pleaded guilty to a felony violation of the CUIC and was sentenced to 36 months of formal probation with five days in custody. Two additional employer representatives each pleaded guilty to a misdemeanor violation of the PC and were each sentenced to 36 months of summary probation with up to 16 days in custody.
- The ID and San Mateo County District Attorney's Office conducted a joint investigation of an employer who was alleged to have been paying employees in cash and failing to pay some of its employees their wages. The investigation revealed the employer had failed to report employees and their wages to the EDD and knowingly misrepresented the number of employees and their wages to their insurance carrier to obtain a lower premium for workers' compensation insurance coverage. After the initial charges were filed, further investigation revealed the employer had used someone else's identity to fraudulently secure a business line of credit and had accrued over \$60,000 in uncollected debt. The employer had also failed to pay compensation to another individual for services rendered to the business. An EDD audit revealed \$467,909 in wages that had not been reported to the EDD from January 1, 2009 through December 31, 2012. The employment tax liability owed to the EDD was \$41,187. On August 3, 2017, the employer pleaded no contest to one felony violation involving the CUIC and one felony violation involving the CIC. The employer was sentenced to 90 days in county jail and five years of formal probation. A hearing to determine the amount of restitution owed to the victims is scheduled for a later date.
- The ID and Santa Clara County District Attorney's Office conducted a joint investigation of a construction company employer alleged to have underreported wages or failed to report his employees and their wages to the EDD. An EDD audit uncovered \$2,803,966 in wages that were not reported to the EDD from January 1, 2011 through September 30, 2014. The employment tax liability owed to the EDD was \$161,038. The employer pleaded no contest to one felony violation of the CUIC and one felony violation of the PC.
- The ID in participation with the Tax Recovery and Criminal Enforcement (TRaCE) Task Force conducted an investigation of an employer operating 50 retail

## ATTACHMENT A (Continued)

clothing stores in Los Angeles, Orange, San Diego, and Ventura counties who failed to report his employees and evaded payment of sales, income, and payroll tax. The employer also failed to report wages to his workers' compensation insurance carriers from 2010 through 2016. The investigation lasted two years. The investigation was led by the California Attorney General's Office who prosecuted the case in coordination with the TRaCE Task Force. The employment tax liability owed to the EDD is being determined. The employer pleaded guilty to felony violations involving the R&TC, CUIC, and CIC. Formal sentencing was scheduled to occur on a future date based on a plea agreement for the employer to pay \$7.6 million restitution to the governmental entities involved and two years of incarceration in county jail.

- The ID in participation with the Orange County Premium Fraud Task Force conducted an investigation of an employer who failed to accurately report, withhold, and remit employee wages of two construction companies to the EDD. The employment tax liabilities owed to the EDD for the two companies was \$240,819 and \$1,645,507. The employer pleaded guilty to felony violations involving the CIC and CUIC. The employer was sentenced to five years in state prison, sentence suspended. The employer was placed on three years of formal probation and was ordered to serve one year in county jail.
- The ID and Contra Costa District Attorney's Office conducted a joint investigation after receiving complaints filed with the DIR-DLSE against a restaurant employer with four owners/associates. The complaints included failure to pay overtime, failure to pay minimum wage, failure to provide meal and rest periods, and making late wage payments. An EDD investigation revealed the employers paid workers in cash and did not report workers or underreported wages paid to workers. The employer also kept a second set of books reflecting actual wages paid to workers. The employment tax liability owed to the EDD was \$975,828. Three of the owner/associates pleaded no contest to felony charges involving the CUIC, PC, R&TC, and CIC and were each sentenced to three years and four months in jail. A fourth associate pleaded no contest to a misdemeanor violation involving the LC. Each of the owners/associates was ordered to pay a portion of the total tax liability as total restitution to the EDD.
- The ID in participation with the Orange County Premium Fraud Task Force conducted an investigation of a dental surgeon who failed to report her employees to the EDD and pay taxes. The employer also failed to secure workers' compensation insurance. The employment tax liability owed to the EDD was \$78,230. A jury trial during January of 2017 found the employer guilty of felony violations involving the CUIC, PC, and LC. The employer was ordered to pay restitution to the EDD, serve 30 days in the Orange County jail beginning July 7, 2017, perform 50 hours of community service, and 60 months of formal probation.

## ATTACHMENT A (Continued)

- The ID in participation with the TRaCE Task Force conducted an investigation of an employer subcontracted by the United States Postal Service (USPS) to transport mail to and from various post offices in California. The investigation was initiated based on an allegation received from the Office of Inspector General, USPS. The business employed approximately 10 to 15 individuals who were misclassified as corporate officers and weren't paid prevailing wages as required by the contract. The employer also failed to secure workers' compensation insurance. The investigation revealed the employer had not reported all of his employees and their wages to the EDD. An EDD audit uncovered \$905,982 in wages that had not been reported from January 1, 2009 through September 30, 2014. The employment tax liability owed to the EDD was \$36,890. On February 14, 2017, the employer pleaded no contest to one felony violation each of the CUIIC and the R&TC. The employer was sentenced to four years of formal probation and 18 months of home detention. He was also ordered to pay \$36,890 restitution to the EDD, \$6,755 restitution to the FTB, and \$10,000 to the BOE for the cost of the investigation.
- The ID and Sacramento County District Attorney's Office conducted a joint investigation of a Sacramento County construction company that failed to report employees and withhold and pay taxes to the EDD. The business also failed to obtain workers' compensation insurance coverage for the employees. The business was under-reporting wages to the EDD by paying some employees in cash. The employment tax liability owed to the EDD was \$77,242. The two principals of the business pleaded to felony violations of the CIC and CUIIC. As a condition of the pleadings, both defendants were ordered to pay restitution of \$77,242 to the EDD, jointly and severally.
- The ID, CDI, and Tulare County District Attorney's office conducted a joint investigation of a Tulare County farm labor contractor who issued payroll checks that he allowed to clear through his bank account and then voided them in his computer accounting system. Voiding the checks caused the payments not to appear on the payroll reports created by the accounting system. The employer then created a payroll journal omitting the voided checks and the remaining balance was reported to the EDD as the payroll. The amount of the unreported wages to the EDD was \$1,675,633 for the period of October 1, 2010 through June 30, 2011. The employment tax liability owed to the EDD was \$76,026. The employer pleaded guilty to one misdemeanor violation of the CUIIC and was sentenced to three years' probation and ordered to pay restitution of \$76,026 to the EDD.
- The ID and CDI conducted a joint investigation of a Kings County dairy employer who failed to accurately report employee wages to its insurance carrier, the State Compensation Insurance Fund (SCIF), and the EDD. The employer failed to remit payroll tax withholdings and deductions from employees' wages to the EDD and did not register timely with the EDD when it first became an employer. The employment tax liability owed to the EDD was \$61,358. The employer pleaded

## ATTACHMENT A (Continued)

guilty to three violations of the CIC. All other counts were dismissed with a Harvey Waiver including the EDD charges. (A Harvey waiver allows the court to consider dismissed charges during sentencing in a criminal case.) The employer was sentenced to five years of formal probation with the following conditions: 120 days in jail with credit for one day, fines including a \$10,000 state restitution fine, and restitution paid to the EDD of \$61,357. The employer also paid amounts owed to the SCIF and their insurance carrier prior to sentencing.

- The ID, FTB, and Santa Barbara District Attorney's Office conducted a joint investigation of a Santa Barbara County slurry seal coating employer who failed to withhold and remit payroll tax withholdings and deductions from their employees' wages and failed to accurately report employee wages to the EDD, SCIF, and their insurance carrier. The employment tax liability owed to the EDD was \$167,676. The employer pleaded guilty to one felony violation each of the CUIC, CIC, and R&TC, and one misdemeanor violation of the LC. During 2017, the employer was sentenced to 364 days in jail and ordered to serve three years of probation and to pay restitution to the EDD, FTB, SCIF, and their insurance carrier.
- The ID in participation with the Orange County Premium Fraud Task Force conducted an investigation of an Orange County roofing contractor who was underreporting employees to the EDD and misclassifying employees to their workers' compensation insurance carrier. The employment tax liability owed to the EDD was \$642,819. The employer pleaded guilty to 66 felony violations that included 20 violations of the CUIC. The employer was sentenced to state prison for six years, sentence suspended, was ordered to serve 364 days in County Jail, and was placed on supervised probation for ten years.
- The ID and Alameda County District Attorney's Office conducted a joint investigation of a construction engineering employer that did not have workers' compensation insurance and was not registered with the EDD. The employer pleaded guilty to misdemeanor violations of the LC, CUIC, and CIC. The employer was ordered to pay restitution based on a total tax liability to be determined by the EDD in addition to restitution ordered for payment to the SCIF. The employer was also ordered to pay \$270 in court fines and to serve four years of court probation.

## ATTACHMENT B

### ACRONYMS

ABC	California Department of Alcoholic Beverage Control
BAR	Bureau of Automotive Repair
BOE	Board of Equalization
BSIS	Bureau of Security and Investigative Services
Cal/OSHA	Division of Occupational Safety and Health
CDI	California Department of Insurance
CDTFA	California Department of Tax and Fee Administration
CIB	Criminal Investigation Bureau
CIC	California Insurance Code
CSLB	Contractors State License Board
CUIC	California Unemployment Insurance Code
DCA	Department of Consumer Affairs
DIR	Department of Industrial Relations
DI	Disability Insurance
DLSE	Division of Labor Standards Enforcement
DMV	Department of Motor Vehicles
DOSH	(Department of Industrial Relations) Division of Occupational Safety and Health
EDD	Employment Development Department
FLC	Farm Labor Contractor
FTB	Franchise Tax Board
ID	(Employment Development Department), Investigation Division
IRS	Internal Revenue Service
JESF	Joint Enforcement Strike Force
LC	(California) Labor Code
LETF	Labor Enforcement Task Force
PC	California Penal Code
PFL	Paid Family Leave
QETP	Questionable Employment Tax Practices
R&TC	(California) Revenue and Taxation Code
SCIF	State Compensation Insurance Fund
TRaCE	Tax Recovery and Criminal Enforcement
UI	Unemployment Insurance
USDOL	United States Department of Labor
USPS	United States Postal Service



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