

EMPLOYMENT DEVELOPMENT DEPARTMENT UNDERGROUND ECONOMY OPERATIONS

Background

The underground economy imposes significant burdens on the State of California, on businesses that comply with the law, and on workers who lose benefits and other protections provided by State law. The ultimate impact of the underground economy is erosion of the economic stability and working conditions in this State.

Businesses operating in the underground economy gain an unfair competitive advantage over businesses that comply with the law. Employees of the businesses that do not comply are also impacted. Their wages may be less than required by law and benefits could be denied or delayed because their wages are not properly reported. Additionally, their working conditions may not meet legal requirements, which can put them in danger.

Consumers can also be affected by businesses operating in the underground economy as frequently these businesses do not comply with State licensing provisions which are designed to ensure certain levels of skill and knowledge to protect the consumer.

Underground Economy Operations (UEO)

The UEO enforcement efforts are a strategic blend of education, partnerships, and investigative activities. The UEO staff make presentations to employer groups, trade associations, labor organizations, government agencies, and others to discuss the impact the underground economy has on tax revenues, law abiding businesses, and employees. To maximize resources and increase overall program efficiency, UEO has developed partnerships with various federal, State, and local agencies, as well as trade and labor organizations to work collaboratively to identify underground economy activity and to take appropriate enforcement action.

Joint Enforcement Strike Force (JESF)

The JESF was enacted into law by the addition of Section 329 of the California Unemployment Insurance Code (CUIC). The purpose of the JESF is to develop and share information necessary to combat the underground economy; to improve the coordination of enforcement activities; and to develop methods to pool, focus, and target the enforcement resources of all JESF members in support of the enforcement activities of individual agencies. Members of the JESF include the Employment Development Department (EDD),

Department of Industrial Relations (DIR), Department of Consumer Affairs (DCA), and Department of Insurance. Other agencies such as the Franchise Tax Board and the Board of Equalization also participate. The EDD has been designated as the lead agency for the JESF. The JESF is empowered to form joint enforcement teams to utilize the collective investigative and enforcement capabilities of the participating members. Through the formation of JESF, a joint agency operation called the Employment Enforcement Task Force was created.

Employment Enforcement Task Force (EETF)

The EETF is the first joint enforcement project created by the JESF. Participating agencies include EDD and DIR with strong support from the Contractors' State License Board (CSLB) and the Bureau of Automotive Repair within DCA. The EETF agents from participating agencies jointly conduct on-site investigations of businesses by interviewing owners, managers, and workers to determine if businesses are in compliance with payroll tax, labor, and licensing laws. To minimize the disruption of compliant businesses, EETF conducts investigations only if there is reasonable belief that there are violations of the CUIC, Labor Code, and/or the Business and Professions Code.

The EETF has focused on numerous industries over time including construction, automotive repair, garment manufacturing, bars, restaurants, nightclubs, furniture manufacturers, adult entertainment establishments, bakeries, produce markets, car washes, pallet repair businesses, cabinet manufacturers, as well as janitorial and building maintenance providers. Although EETF focuses on industries known to have a high degree of noncompliance, investigations of businesses not included in the target groups are also conducted when underground economy activity is suspected.

Economic and Employment Enforcement Coalition (EEEC)

The EEEC was created as a multi-agency enforcement program consisting of investigators from EDD, DIR (Division of Labor Standards Enforcement and Cal/OSHA), CSLB, and the U.S. Department of Labor. The EEEC partnering agencies conduct field compliance inspections on targeted industries within designated geographic areas to determine the existence of noncompliance and/or underground economy activities.

Tax Enforcement Group (TEG)

The TEG staff conducts investigations in situations where traditional on-site investigations are not practical or effective in detecting payroll tax evasion. Staff utilizes techniques such as revenue-to-labor ratios typical for certain industries, various internal and external database analysis, income tax return analysis, discussions with workers, and other techniques to determine the existence of noncompliance and underground economy activities.

Questionable Employment Tax Practices (QETP) Program

The QETP Program was initiated in 2007 as a collaborative approach between EDD and the Internal Revenue Service (IRS). A Memorandum of Understanding was created to allow for exchange of case information between EDD and the IRS. The goal of the program is to achieve a reduction in the tax gap for both federal and State payroll tax authorities. The EDD uses the IRS case information to issue assessments for amounts owed to EDD, saving significant time associated with conducting an audit. This collaborative effort leverages our existing resources, achieves increased voluntary compliance, and sends a consistent message to all taxpayers. This multi-agency compliance approach presents a united effort to taxpayers and their representatives.

Unemployment Insurance Rate Equity Group (UIREG)

In an attempt to circumvent the experience rating system that determines Unemployment Insurance (UI) tax rates, some employers deliberately try to manipulate their rates by using schemes such as creating new business entities or transferring payroll between these entities to reduce their payroll tax liabilities. This practice is known as UI rate manipulation and is in violation of the CUIC. The UI rate manipulation causes other employers to pay more than their fair share for UI and creates an uneven playing field for businesses. The UIREG staff focuses on detecting employers who attempt to use

UI rate manipulation schemes to lower their payroll tax liabilities. To maintain the integrity of the experience rating system, EDD is increasing efforts to identify employers who use rate manipulation schemes and will assess fraud penalties in cases that involve intentional rate manipulation.

Summary

The EDD's detection of underground economy activities has had a significant impact on the underground economy in California in the areas of employment, employee safety, and labor laws. The EDD remains vigilant in detecting new tax avoidance schemes, directs resources to combat them, and continues to partner with other agencies to combine efforts to level the playing field for employers. These efforts send a strong message to the employer community on the financial risks of participating in the underground economy and aid in supporting fair competition for employers within this State.

ADDITIONAL INFORMATION

If you would like additional information regarding this program or to report suspected underground economy activity, please contact the EDD's Underground Economy Operations at (800) 528-1783, or visit the EDD's Web site at www.edd.ca.gov/Payroll_Taxes/Underground_Economy_Operations.htm. You may also e-mail information to ueo@edd.ca.gov, send a fax to (916) 227-2772, or send mail to:

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The EDD is an equal opportunity employer/program. Auxiliary aids and services are available upon request to individuals with disabilities. Requests for services, aids, and/or alternate formats need to be made by calling (888) 745-3886 (voice) or TTY (800) 547-9565.

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