



The Independent Contractor Law in Massachusetts and the Risks of Misclassification

BY SHEHZAD RAJWANI

In January 2008, the Attorney General's Office ("AGO") issued an advisory regarding the Massachusetts Independent Contractor Law located at M.G.L. c. 149, s. 148B (the "MICL" or the "Law"). The MICL was amended in the summer of 2004, and it will likely increase the cost of doing business in Massachusetts for some companies. In its advisory, the AGO emphasized the need for enforcement of the Law because of the following: (1) misclassification of employees as independent contractors deprives these individuals of benefits enjoyed by employees, including unemployment insurance and worker's compensation benefits; (2) misclassification deprives the Commonwealth of tax revenue from payroll taxes and adds various additional burdens upon the Commonwealth, such as providing health insurance for uninsured workers; and (3) misclassification undermines fair market competition and negatively impacts the business environment in the Commonwealth.

Governor Deval Patrick signed Executive Order No. 499 on March 12, 2008, "Establishing a Joint Enforcement Task Force on the Underground Economy and Employee Misclassification." The task force consists of various governmental agencies and is charged with coordinating joint efforts to combat the underground economy and employee misclassification. Among other responsibilities, the task force must submit an annual report to the Governor summarizing its activities during the preceding year.

Effective July 15, 2008, employers in Massachusetts became subject to mandatory treble damages for violations of Massachusetts wage and hour laws. This includes innocent violations where the employer has tried to comply with the laws in good faith.

Based on the above governmental actions, as well as potentially broad civil and criminal liability for misclassification of individuals as independent contractors, employers would be well served to examine their independent contractor relationships to assure that those relationships meet the MICL's strict three-part

test to overcome the presumption that an individual performing any service is an employee. To properly classify a worker as an independent contractor, the employer must show:

(1) the individual is free from control and direction in connection with the performance of the service, both under his contract for the performance of service and in fact; (2) the service is performed outside the usual course of the business of the employer; and (3) the individual is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in the service performed.

When the legislature amended the MICL in 2004, it made the biggest change to the second element of the test above. Previously, prong two required that "such service [be] performed either outside the usual course of business for which the service is performed or [be] performed outside of all places of business of the enterprise." Though deletion of the phrase "or is performed outside of all places of business of the enterprise" may have been unintended and may have gone unnoticed for some time, it affects many businesses who can no longer properly classify workers as independent contractors. When the Law was amended in 2004, there was some hope among Massachusetts businesses that the legislature would correct the unintended impact of the MICL. It appears now, however, that the law will be enforced as interpreted by the AGO. In fact, the recent legislation requiring triple damages for wage violations provides motivation for employees and their attorneys to file wage claims.

The Attorney General's advisory states that an employer violates the Law when two acts occur. First, the employer classifies or treats a worker as an independent contractor even though the worker does not meet all of the criteria in the above three-part test. Second, in receiving services from the individual, the employer violates one or more of the following laws of the Commonwealth: the wage and hour laws; the minimum wage law;

Continued on next page >>

>> *From page one*

the overtime law; the law requiring employers to keep true and accurate employee payroll records and to furnish the records to the Attorney General upon request; provisions requiring employers to take and pay over withholding taxes on employee wages, and the worker's compensation provisions punishing knowing misclassification of an employee.

In addition, the AGO has issued guidelines instructing that it will consider the following factors to be strong indicia of misclassification that warrant further investigation and may result in enforcement; these include:

- Individuals providing services for an employer that are not reflected on the employer's business records;
- Individuals providing services who are paid "off the books," "under the table," in cash or employers are unable to provide documents reflecting payment;
- There is insufficient or no workers' compensation coverage;
- Individuals performing services are not provided 1099s or W-2s by any entity;
- The contracting entity providing equipment, tools, and supplies to individuals or requiring the purchase of such materials directly from the contracting entity; and
- Alleged independent contractors not paying income taxes or employer contributions to the Massachusetts Division of Unemployment Assistance.

Though the emphasis of this article is the MICL, employers are subject to various federal and Massachusetts laws requiring proper classification of workers as independent contractors or employees. For example, the Internal Revenue Service and Massachusetts Department of Revenue use a twenty-factor common law test to consider whether a business has retained the right to direct and control a worker to a sufficient extent to classify him or her as an employee. These factors, along with common law elements of direction and control, are analyzed to determine whether a person is an "employer," and is thus obligated to withhold income tax on the wages of an employee for federal and state withholding purposes. For sure, the classification of a worker as an employee affects the cost of doing business, but employers should at least be aware of and examine the risks of misclassification.

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