

## in this issue:

MAY 2008

The Massachusetts Attorney General has issued an advisory opinion that clarifies when a worker is properly classified as an independent contractor under the state's extremely narrow independent contractor statute. With a new law requiring treble damages for *all violations* of the Massachusetts wage and hour law and the state's stepped-up enforcement activity, employers have even greater incentive to ensure that their workers are properly classified.

## East Coast Edition

*A Littler Mendelson East Coast-specific Newsletter*

### Massachusetts Attorney General Offers Guidance on the State's Strict Independent Contractor Law

By Martha M. Walz

In 2004, the Massachusetts Legislature considerably narrowed the definition of independent contractor, substantially increasing the risk of an enforcement action or lawsuit against Massachusetts employers who use independent contractors. The changed law has presented significant challenges for employers, as many traditional independent contractor relationships would not meet the narrower standard. To clarify the law and explain her enforcement priorities, Attorney General Martha Coakley recently issued an Advisory that provides guidance for employers in determining the classification of their workers. The Advisory supersedes two Advisories issued by her predecessors on the same topic.

In addition, Governor Patrick recently issued an Executive Order that steps up the state's activities against employers misclassifying workers. The stakes are even higher for Massachusetts employers now that treble damages are awarded for all wage and hour violations, including violations of the independent contractor law. Employers retaining independent contractors in Massachusetts should evaluate their classification decisions in light of the Advisory and keep in mind that punitive damages are automatically awarded upon a finding of misclassification.

#### Definition of Independent Contractor

Chapter 149, section 148B of the Massachusetts General Laws creates a presumption that an individual performing any service is an employee unless an employer can establish that each of three

factors is present. A worker must be an employee unless:

1. the individual is free from control and direction in connection with the performance of the service, both under his or her contract for the performance of service and in fact; and
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.

All three elements must exist in order for a worker to be classified as an independent contractor. The burden of proof is on the employer, and the inability of an employer to prove any one of the prongs is sufficient to conclude that the worker in question is an employee.

#### The Prong Two Problem

The definition of independent contractor was amended in 2004 when the legislature modified prong two. It is this change that has caused such consternation and risk for employers. Under the prior definition, prong two stated the service must be "performed either outside the usual course of the business for which the service is performed or the work is performed outside of all places of business of the enterprise." Under that definition, employers satisfying prongs number 1 and number 3 could classify a worker as an independent contractor if the worker had his or her own office or

worked at home. With that criterion no longer available following the 2004 amendment, many workers suddenly failed the independent contractor test.

Because Massachusetts courts have had limited opportunities to construe the meaning of “usual course of the business,” the scope of prong two remains uncertain. According to the Advisory, in its enforcement actions, the Attorney General’s Office will consider whether the service the individual is performing is “necessary to the business” or “merely incidental” to the business when determining whether the individual is properly classified as an employee or independent contractor under prong two. The Advisory notes, by way of example, that a drywall company that classifies an individual who is installing drywall as an independent contractor is violating prong two because the individual is performing an essential part of the company’s business. Similarly, a company that provides motor vehicle appraisals that classifies an appraiser as an independent contractor is violating the law because the appraiser is performing an essential part of the appraisal company’s business. In contrast, when an accounting firm hires an individual to move office furniture, prong two is satisfied because moving furniture is incidental rather than necessary to the accounting firm’s business.

Unfortunately, however, there are many less obvious scenarios where the outcome remains uncertain. Consider, for example, a situation where a retail company’s human resources department wants to conduct a training program and its in-house trainers do not have the relevant expertise. May the company properly hire an outside trainer as an independent contractor? One might argue that training employees is outside the usual course of the employer’s retail business, yet one might also argue that training is within the usual course of the business since the company has its own training staff.

## Factors Indicating Misclassification

The Advisory lists several factors that the Attorney General believes provide strong indications of misclassification, thereby warranting further investigation and potentially

resulting in an enforcement action. These include:

- An entity allows, requests, or contracts with corporate entities such as LLCs or S corporations that exist for the purpose of avoiding the law.
- Individuals providing services are paid off the books, under the table, in cash, or provided no documents reflecting payment.
- Insufficient or no workers’ compensation coverage exists.
- Individuals providing services are not provided 1099s or W-2s by any entity.
- The contracting entity provides equipment, tools and supplies to individuals or requires the purchase of such materials directly from the contracting entity.
- Alleged independent contractors do not pay income taxes or employer contributions to the Division of Unemployment Assistance.

Moreover, the Attorney General’s Advisory confirms the widespread understanding that an employer’s belief that a worker should be an independent contractor has no relevance in determining whether there has been a violation of the law. The above list is not intended to be comprehensive, and the Attorney General has made it clear that her office will take a case-by-case approach when attempting to determine if workers have been misclassified.

## The Challenge for Multi-State Employers

Employers who use independent contractors both within and outside of Massachusetts continue to face the possibility that two individuals performing the same function but working in different states should be classified differently. While this may be a human resources and employee relations nightmare, it may be the wisest course. As explained in Littler’s April 2008 ASAP *Massachusetts Mandates Treble Damages for Wage Violations*, treble damages are mandatory in Massachusetts if an employer violates the state’s wage and hour laws, including the independent contractor law.

## Enforcement Activity To Increase

In March, Governor Deval Patrick issued Executive Order #499 creating the Joint Enforcement Task Force on the Underground Economy and Employee Misclassification. The Task Force is charged with, among other things, the responsibility to crack down on employers that misclassify workers as independent contractors. As of May 1, the Task Force was conducting over 20 joint investigations of employer fraud and employment misclassification cases.

In addition, the state budget for the fiscal year beginning July 1 may include funding for increased enforcement of the worker classification law. Governor Patrick estimates that \$30 million in revenue will be generated by such enforcement. The Attorney General’s Office along with the Department of Revenue, the Department of Industrial Accidents (which enforces the workers’ compensation law), and the Division of Unemployment Assistance may be given extra funding for implementation of a statewide effort “to aggressively enforce” as well as “to encourage voluntary compliance” with the employee classification laws with the goal of increasing the collection of income tax revenues related to workers who are currently improperly classified as independent contractors.

Even if this language is not included in the final budget, employers should expect increased enforcement by the Attorney General. As she notes in the Advisory, the need for proper classification of workers “is of paramount importance to the Commonwealth.”

---

*Martha M. Walz is Of Counsel in Littler Mendelson’s Boston office. She is also a member of the Massachusetts House of Representatives. If you would like further information, please contact your Littler attorney at 1.888.Littler, info@littler.com, or Ms. Walz at mwalz@littler.com.*

---