Employment, Labor and Benefits Advisory: Massachusetts Federal Court Holds Franchisees To Be "Employees" of Franchisor

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By H. Andrew Matzkin and Paula Lyons

In a decision that reinforces the broad definition of "employee" under Massachusetts law—and the penalties that result from a misclassification of employees as independent contractors—the Massachusetts Federal District Court recently held, in *Awuah, et al. v. Coverall North America, Inc.*, that specific franchisees of Coverall were employees rather than independent contractors.

The Massachusetts Wage Act (M.G.L. c. 149, § 148B) requires an employer to satisfy a three-prong test in order to prove that an individual is not an employee. First, the worker at issue must be free from control and direction in connection with the performance of services, both under contract and in fact. Second, the services must be performed outside the usual course of business of the employer. Third, the worker must be customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the service performed. **All** three prongs of the test must be satisfied in order for a worker to be classified as an independent contractor rather than an employee.

The plaintiffs in *Awuah*, a group of Coverall's Massachusetts franchisees, sought a judicial declaration that Coverall was their "employer" under Massachusetts law. In analyzing whether the franchisees were properly classified as employees or contractors, the court held that Coverall failed the second prong of the independent contractor test because both Coverall and its franchises sold cleaning services.

The court found that Coverall contracted with most of the franchisee's customers, billed to all of the franchisee's customers, and required trainings, uniforms, fees, and other systems in its relationship with its franchisees—confirming that both Coverall and the franchisees were engaged in the business of cleaning services and, therefore, that the workers did not perform services outside the usual course of business of the employer, as required under the second prong of the independent contractor test. Indeed, the court specifically rebutted Coverall's argument that its business was the franchising itself, stating: "Describing franchising as a business in itself, as Coverall seeks to do, sounds vaguely like a description for a modified Ponzi scheme—a company that does not earn money from the sale of goods or services, but from taking in more money from unwitting franchisees to make payments to the previous franchisees."

In light of the determination that Coverall failed the second prong of the independent contractor test, the court held that the franchisees were misclassified as independent contractors and granted their motion for partial summary judgment against Coverall.

Action Items for Employers

Under the Massachusetts Wage Act, regardless of the contract between or intent of the parties, a worker performing services for an entity is considered an employee unless all three prongs of the independent contractor test are satisfied. As the decision in *Awuah* demonstrates, businesses may not hire individuals in Massachusetts to perform the same work the company performs without treating the individual as an employee, including for purposes such as minimum wage and overtime payments, health care benefits, unemployment contributions, and workers' compensation coverage. Furthermore, an entity that misclassifies a worker as an independent contractor and fails to treat the worker as an employee may be subject to significant liability, including repayment of lost wages and overtime, retroactive unemployment contributions, disqualification of benefit plans, and related penalties and fines.

In light of the above, all companies with Massachusetts employees should review their independent contractor relationships. Additionally, in light of the specific holding of the *Awuah* case, franchisors in Massachusetts need to examine their relationships with franchisees to determine whether their franchisees are classified correctly. Employers are encouraged to contact Mintz Levin with any questions regarding their employment and independent contractor relationships, and specifically regarding whether their workers are properly classified as independent contractors.

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If you have any questions regarding the subject covered in this Alert, or any related issue, please feel free to contact any the attorneys in Mintz Levin's Employment, Labor and Benefits Practice (listed at right).

For assistance in this area please contact one of the attorneys listed below or any member of your Mintz Levin client service team.

MEMBERS

David Barmak
(202) 585-3507
DBarmak@mintz.com

Andrew J. Bernstein
(212) 692-6742
AJBernstein@mintz.com

Richard H. Block
(212) 692-6741
RHBlock@mintz.com

Bret A. Cohen
(617) 348-3089
BCohen@mintz.com

Raymond D. Cotton
(202) 434-7322
RDCotton@mintz.com

Micha "Mitch" Danzig
(858) 314-1502
MDanzig@mintz.com

Robert M. Gault
(617) 348-1643
RMGault@mintz.com

James R. Hays
(212) 692-6276
JRHays@mintz.com

H. Andrew Matzkin
(617) 348-1683
HMatzkin@mintz.com

Jennifer B. Rubin
(212) 692-6766
JBRubin@mintz.com

Donald W. Schroeder
(617) 348-3077
DSchroeder@mintz.com

Henry A. Sullivan
(617) 348-1746
HASullivan@mintz.com

OF COUNSEL

Martha J. Zackin
(617) 348-4415
MJZackin@mintz.com

ASSOCIATES

Michael S. Arnold
(212) 692-6866
MArnold@mintz.com

Katharine O. Beattie
(617) 348-1887
KOBeattie@mintz.com

Gregory R. Bennett
(212) 692-6842
GBennett@mintz.com

Jessica W. Catlow
(212) 692-6843
JCatlow@mintz.com

Jennifer F. DiMarco
(212) 692-6260
JFDiMarco@mintz.com

Kelley L. Finnerty
(617) 348-1819
KFinnerty@mintz.com

David M. Katz
(212) 692-6844
DKatz@mintz.com

Paula Lyons
(617) 348-1831
PLyons@mintz.com

James M. Nicholas
(617) 348-1620
JNicholas@mintz.com

Maura M. Pelham
(617) 348-1851
MMPelham@mintz.com

Tyrone P. Thomas
(202) 434-7374
TPThomas@mintz.com

Brandon T. Willenberg
(858) 314-1522
BTWillenberg@mintz.com