

Contractor law update vexes firms

Mass. businesses failing 3-part test

Michael A. Rowe believed in good faith that the people his company hired to handle auto accident injury claims for insurers at home on their own time and with their own computers were independent contractors.

His business, Claims Outsource Inc. of Worcester, at one time had more than 50 independent contractors handling claims.

But now Mr. Rowe is shutting down the business because he cannot afford to pay a \$56,000 assessment levied by the state Division of Unemployment Assistance after a hearing examiner ruled that a work-at-home claims handler was an employee, not an independent contractor.

The finding launched an audit of the company's records and a determination that Mr. Rowe owed back taxes to the unemployment insurance trust fund for other workers he had hired as independent contractors.

"I am not paying it," said an angry Mr. Rowe. "These were subcontractors, not employees."

Mr. Rowe's workers are equally upset. After he told them about his decision to close, one wrote back in an e-mail: "I'm sitting here crying and wondering why someone who knows nothing about what we really do decided to pull the rug out from under us hard-working at-home moms. It's a very mean thing to do, you know? Talk about power elite control!"

Mr. Rowe's predicament may well be faced by other small Massachusetts businesses as they struggle to understand and comply with the state's year-old amendment of the independent contractor law, which requires independent contractors to meet a three-part test that is far more stringent than traditional state and federal law tests.

"He was at the front end of the tsunami and others will get caught up in it," said Jon Coppelman, senior vice president at LynchRyan & Associates, a workers' compensation consulting firm in Wellesley. "It will take a while to figure out what this means and how it will play out in Massachusetts."

Part of the 2004 Act Further Regulating Public Construction in the Commonwealth, the amendment to the existing law on inde-

pendent contractors was an attempt to solve an issue in the construction trades, said Mr. Coppelman.

"The problem was that a lot of subcontractors were going around without insurance. It wasn't that they intended to collect workers' compensation benefits, but when they got seriously hurt they would look around, because their livelihood was impacted, and would tend to try to attach themselves to the general contractor's policy, or if that failed, they would be compensated out the fund for the uninsured. This whole effort is trying to tighten that up."

A 2004 study by Harvard University and the University of Massachusetts found that from 2001 to 2003, as many as 14 percent to 24 percent of Massachusetts construction employers misclassified workers as independent contractors. Across all industries, the study estimated 13 percent to 19 percent of employers had misclassified workers and that the number of workers affected statewide ranged from 125,725 to 248,206.

Misclassified workers cost the state millions of dollars in lost tax revenue, including as much as \$35 million in unemployment insurance taxes that were not levied on payrolls and as much as \$152 million in lost state income tax revenue for under-reported personal income among misclassified workers, the study claimed.

Workers' compensation insurers also lost out on millions of dollars in premiums not paid and in payments made for workers "surreptitiously" added to policies after injuries but for whom premiums were not paid, the study said.

"They have tightened the criteria for independents," said Mr. Coppelman. "If you are general contractor and have a sub on the job, if you cannot prove they have workers' comp, the auditors are likely to add the cost of those people to your payroll ... That is what they are trying to solve by determining who is an independent contractor and who is an employee."

But it is a broad net and doesn't just apply to construction, he said. "It's become a kind of hot issue."

How did the net catch Mr. Rowe? When work got slow, one of the company's independent contractors filed a claim for jobless benefits.

Mr. Rowe challenged the claim, saying that the woman was hired as an independent contractor and that Claims Outsource Inc. wasn't responsible for unemployment, workers' compensation or disability benefits.

The hearing examiner rejected the argument and found that the woman, and others like her at the company, were employees.

The examiner said their work didn't

meet the three exceptions required under the amended law to be independent contractors. (The three tests require that a worker be free from control and direction; perform a service outside the usual course of an employer's business, and work in an independent trade, occupation, profession or business.)

Mr. Rowe appealed, but the decision was upheld in December.

The state declined to discuss the case or the examiner's decision.

In April, the Division of Unemployment Assistance audited three years of wage reports and told Mr. Rowe he owed \$55,567.26 in back unemployment insurance taxes for workers the state had reclassified as employees, even though the amended independent contractor law didn't go into effect until July 2004.

Adding insult to injury for Mr. Rowe, unemployment insurance costs per worker have risen about 100 percent since 2003 as the state tries to build a surplus in the recently insolvent fund.

Mr. Rowe's accountant, Albert L. Bisceglia, said more businesses are likely to get caught up in the same net.

"Businesses will find themselves under severe constraints because they won't really fully understand which classification the employee or subcontractor will be in without expensive services to provide them with guidance on the issue," he said. "It's a rule that adds a burden to small business, in my opinion."

He said Mr. Rowe believed that he followed the correct interpretation of the law at the time he hired workers. "They all signed agreements; a lawyer drafted them. So I don't know how much more you need," Mr. Bisceglia said.

Mr. Rowe asked that if his independent contractors are considered employees, why has the state not sought reclassification of FedEx Ground and FedEx Home Delivery workers whom FedEx says are independent contractors?

FedEx drivers have filed suits against the company, and courts in Montana, New Jersey and California have determined they are employees. FedEx has appealed. In May, a similar suit was filed in U.S. District Court in Boston by four FedEx contractors.

"When I look at the FedEx business, they are not independent contractors by Massachusetts standards," said Mr. Coppelman.

Newly reclassified as employees, Claims Outsource workers no longer have jobs. Mr. Rowe is telling them to file for unemployment.



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