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Contract Employees vs Independent Contractors Policy

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Introduction

This policy, which is jointly issued by the Operational Services Division, Office of the Comptroller and Human Resources Division, highlights the differences between the two types of individual workers: **contract employees** and **independent contractors**. It provides guidance to departments in determining whether to hire a contract employee or to contract with an independent contractor and then provides guidance pertaining to the recruitment and contract execution for contract employees. This guidance includes the Commonwealth's three-part test, which incorporates the requirements of state and federal law and which must be utilized by departments in determining whether an individual is a contract employee or an independent contractor.

When a department requires the services of an individual, it must determine, before acquiring the services, if the service is a competitive procurement exception (contract employee) or if it must conduct a competitive procurement (independent contractor). In addition, when a department has conducted a competitive procurement, which was not specifically for the services of an individual but which has resulted in the selection of an individual, the department must review the specific working circumstances of the contract and the individual's work status to determine if the individual will be deemed a contract employee or independent contractor in their working relationship with the department.

Employment Status Form (Combined State and Federal Tests for Employment Status)

An Employment Status Form has been developed to assist departments in two ways:

1. To make the determination PRIOR to the procurement of services, as to whether the type of work to be performed will trigger an employment relationship (contract employee) or a non-employment relationship (independent contractor) in order to determine the proper procurement method to be used to acquire the services, and
2. To confirm the employment status when a contract is signed with an individual contractor selected from either an RFR (independent contractor) or posting (contract employee), which is a required attachment to the Standard Contract Form.

The checklist on the Employment Status Form reconciles the Federal IRS 20 factors (which are focused primarily on whether an employee falls under the "supervision and control" of a department) with the stricter Massachusetts presumption that an individual will be considered a contract employee "unless" the individual passes all three parts of the Massachusetts three-part test.

While the IRS factors consider the work context and the overall balance of the 20 factors, the Massachusetts law requires that the employer/employee relationship be definitively established. The Massachusetts Attorney General has interpreted this test to be rigid, thus resulting in the presumption that an individual contractor will be considered a contract employee unless the three-part test under

M.G.L. c. 149, s. 148B is met. The burden is on the department to defend a determination of independent contractor status. Massachusetts law imposes strict penalties when a worker is misclassified. Therefore, a department must complete the Employment Status Form in order to certify the status for all individual contractors and attach it to the Standard Contract Form.

Posting or Procurement?

A department does not always know in advance whether services can be best performed by an individual contractor or by a company or firm. Therefore, whenever services are being performed, the department should make the following determinations:

1. **Identify the Business Needs of the Department:** The hiring department should develop performance specifications for the services necessary to meet the department's business needs, including where the work needs to be performed, the level of control and supervision that will be required for performance, whether the work hours or schedule will be set by the department or the contractor, whether the work is performed as part of or outside the usual course of business of the department.
2. **Apply the Commonwealth Three-Part Test to the Business Needs: *(Employment Status Form):*** The department must determine if the type of work to be performed can be performed by a firm or an individual and if the type of oversight relationship will trigger an employer-employee relationship or that of an independent contractor. To make this determination, the department must **review** the Employment Status Form to determine if an employer-employee relationship will be created if an individual is selected for performance, as follows:
    a. If the work can be performed by a firm or an individual, or the department is unsure of how best to perform the requisite service, and the review of the Employment Status Form three-part test indicates that there will not be an employer-employee relationship, the department is required to conduct a procurement for these services. See *How to Do a Competitive Procurement* in the OSD Procurement Information Center).
    b. If the work can only be performed by an individual, and the review of the *Employment Status Form* 3-part test indicates that there will be an employer-employee relationship, the department is required to post the contract notice for a contract employee, as outlined below.

Commonwealth Three-Part Test

Current employment law establishes separate tests for determining employment status under both state and federal law. State law, M.G.L. c. 149 § 148B, establishes a three-part test that presumes an individual is a contract employee unless:

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.
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.

This test is a much stricter test than the federal IRS SS-8 test, which departments have used in the past to determine employment status. Any individuals who were classified as independent contractors using the SS-8 test should be reassessed to determine whether they are also independent contractors under the Commonwealth's laws. If the individual would be classified as an independent contractor under the SS-8 test, but as a contract employee under the Commonwealth three-part test, the individual should be

reclassified as a contract employee. The Attorney General's Office may impose penalties if the three-part test shows that an individual should be a contract employee, and the individual was misclassified as an independent contractor.

Federal IRS SS-8 Test

Under federal law, the Internal Revenue Service (IRS) has established 20 factors and its corresponding SS-8 Form that are used to determine whether an individual is a contract employee or an independent contractor.

A "Yes" response to the following questions means the individual may be a contract employee:

1. Does the principal provide instructions to the worker about when, where, and how he or she is to perform the work?
2. Does the principal provide training to the worker?
3. Are the services provided by the worker integrated into the principal's business operations?
4. Must the services be rendered personally by the worker?
5. Does the principal hire, supervise and pay assistants to the worker?
6. Is there a continuing relationship between the principal and the worker?
7. Does the principal set the work hours and schedule?
8. Does the worker devote substantially full time to the business of the principal?
9. Is the work performed on the principal's premises?
10. Is the worker required to perform the services in an order or sequence set by the principal?
11. Is the worker required to submit oral or written reports to the principal?
12. Is the worker paid by the hour, week, or month?
13. Does the principal have the right to discharge the worker at will?
14. Can the worker terminate his or her relationship with the principal any time he or she wishes without incurring liability to the principal?
15. Does the principal pay the business or traveling expenses of the worker?

A "Yes" response to the following questions means the individual may be an independent contractor.

1. Does the worker furnish significant tools, materials and equipment?
2. Does the worker have a significant investment in facilities?
3. Can the worker realize a profit or loss as a result of his or her services?
4. Does the worker provide services for more than one firm at a time?
5. Does the worker make his or her services available to the general public?

Contract Employees - Procurement Exception Under 801 CMR 21.05(6)

The hiring of contract employees is a competitive procurement exception under 801 CMR 21.05(6) since individuals deemed contract employees will be hired under the normal personnel procedures of the department, as follows:

Determine the compensation of the contract

Departments should determine the rate or range of compensation based on the performance and qualifications requirements and available funding. Departments may adjust the rate or range to reflect the lack of fringe benefits for contract employees and the selected candidate's qualifications. Then, departments should determine the total compensation for the anticipated contract duration.

Post the contract notice

Departments should post, advertise or solicit contract candidates as deemed appropriate, e.g., colleges and universities, newspapers, trade journals, electronically (Commonwealth Employment Opportunities), and in accordance with any internal procedures on recruitment developed for the department. The posting should include the description of performance requirements or functions, any minimum qualifications, the compensation rate or range, expected duration and possible options to renew. It should also include instructions for how and when candidates should respond to the posting.

Select the contractor

Selection of a contract employee should be in accordance with the department's standard interview process. The evaluation should take into account the performance requirements and minimum qualifications of the posting. See HRD's Model Hiring Plan Structured Interview Guidelines. See the Massachusetts Commission Against Discrimination Pre-Employment Inquiries Fact Sheet for additional information on appropriate interview questions and topics.

Contract Forms

Contract employees must execute the Commonwealth Terms and Conditions and the Standard Contract Form. The attachments should include a copy of the contract posting or an alternative attachment containing the description of the contract performance, any minimum qualifications, the compensation rate or range and a copy of the contractor's résumé (or statement of qualifications). Include completed Employment Status Form.

Amendments

After contract execution, annual or other options to renew or amendments to the contract are exercised at the department's option in accordance with the duration listed in the posting by executing a Standard Contract Form amendment prior to the termination date of the contract.

Payroll System Requirements

- Contract employees must be paid through the state payroll system that automatically makes tax deductions and alternative retirement contributions.
- Contract employees are subject to alternative retirement contributions under COBRA 1990.
- Contract employee labor will be distributed the same way regular employee labor is distributed. By default, all charges will be attributed to the HR/CMS position accounting line (Department, Unit, and Appropriation). If the position distribution needs to be changed or additional data needs to be captured for labor history reporting, a default distribution, pay period exception, or labor adjustment should be created in LCM. Contract employee payroll payments will be incorporated into LCM predictive/production payroll reports so that departments can monitor and manage funded/unfunded payroll accounts. LCM Labor History and CIW reports can be used to track contract employee payroll expenses.
- The Immigration Reform and Control Act of 1986 (IRCA) makes it illegal for an employer to hire an unauthorized worker. Employers must comply with this requirement by verifying the identity and right to work of all employees hired after November 6, 1986. Prior to hiring any individual, employers can protect themselves by obtaining proof of the right to work in the U.S. This proof of right to work is known as Form I-9, Employment Eligibility Verification, available on the U.S. Citizenship and Immigration website.
- The individual's name must match Social Security Administration records. Correct names and social security numbers (SSN) on W-2 wage reports are the keys to successful processing of the

Commonwealth's annual wage report submission. Not only can the Commonwealth be subject to penalties when employee names and SSNs don't match Social Security Administration records, but also unmatched wage reports can cause earnings that are not posted to your employees' records. To verify the name and SSN match, call the SSA toll-free number for employers at 1-800-772-6270 provide Social Security Number, date of birth and gender. The Commonwealth EIN is 04-6002284. Double check to make sure you have entered the SSN correctly into the payroll system.

- Upon hiring or rehiring an individual, verify Medicare Status. For Rehires, verify that a "break in service" has not occurred. Validate that Income and Medicare taxes are appropriately withheld from wages paid to contract employees, in amounts determined by the employees' withholding certificates and governmental withholding tax tables."
- Contract employees receive a Form W-2 for state and federal tax purposes.

Massachusetts Labor Relations Commission Test

For the purposes of determining collective bargaining status, the Massachusetts Labor Relations Commission does not distinguish between a contract employee and an independent contractor. Only those individuals who meet the Labor Relations Commission's standard of independent contractor will be exempt from the definition of employee pursuant to M.G.L. c. 150E and, as such, exempt from union membership. In determining whether an employee is an independent contractor, the Labor Relations Commission examines whether the alleged employer retains control over the worker. In analyzing the control issue, the Labor Relations Commission examines the duties of the workers, the type of supervision they receive, how the employer treats the workers, and the method in which the workers are paid. The funding source for the position is irrelevant to the Labor Relations Commission's analysis.

Comparison Table for Contract Employees and Independent Contractors		
Item	**Contract Employee**	**Independent Contractor**
Employment status	Contract employee, based upon completion of Employment Status Form, a required contract attachment. Not considered in the Full Time Equivalent (FTE) count of Commonwealth employees.	Non-employee, independent contractor based upon completion of Employment Status Form, a required contract attachment. Not considered in the Full Time Equivalent (FTE) count of Commonwealth employees.
Can contractor be considered a "consultant"?	No. Contract employees are not considered consultants even if performing specialized or consultant-like services. Contract employees are classified under the CC object class in the Office of the Comptroller's Expenditure Classification Handbook.	Yes, if providing consultant services under the HH, N01-N14 and U05 object classes, when the value of the services for the duration of the need exceeds the incidental purchase threshold.
Procurement or posting required	Posting. If the review of the Employment Status Form determines that an employment relationship will exist, the department may hire a contract employee as a procurement exception under 801 CMR 21.05(6). A posting must be made under normal hiring process. Exception: Object Code C26 for legal services requires prior approval of the Governor's Chief Legal Counsel prior to selection under M.G.L. c. 30 § 65 and 801 CMR 21.01(2)(b) and prior Office of the Attorney General approval.	Procurement. If the review of the Employment Status Form determines that an employment relationship will not exist, the department must use an existing statewide contract. If there is no statewide contract, the department may: 1. use an incidental purchase if the total value of the services for the duration of the need is $10,000 or less, 2. Conduct a RFR/procurement if value of the services for the duration of the need exceeds $10,000. Exception: Object Codes H09 and N03 for legal services require prior approval of the Governor's Chief Legal Counsel prior to selection under M.G.L. c. 30 § 65 and 801 CMR 21.01(2)(b) and prior Office of the Attorney General approval.
Selection	Recruitment and interview are in accordance with department's internal hiring policy and HRD guidelines (if applicable).	Review of RFR response, or responses to Requests for Quotes from statewide contractors, or submissions from incidental purchase bidders for legal services only.
Fringe benefits	No (generally) Not entitled to state retirement program, employee insurance programs, sick,	No (generally) Not entitled to state retirement program, employee insurance programs, sick, vacation, personal leave or other fringe benefits.

	vacation, personal leave or other fringe benefits. Covered as an employee for Workers' Compensation, unemployment and torts liability under M.G.L. c. 258. Required to contribute to OBRA Retirement.	
Commonwealth Terms and Conditions	Required	Required
Standard Contract Form	Required Attach a copy of the posting or alternative description of performance requirements, compensation and contractor's resume or statement of qualifications and the Employment Status Form. Per Executive Order #444, attach Contract Employee Disclosure Form (HRD).	Required for all contracts that exceed the incidental purchase threshold. Attach procurement documents (RFR and response), required attachments, Employment Status Form. See OSD's Procurement Information Center.
Tax identification forms	Must complete a Form W-4.	Must complete a Form W-9 or W-8, as appropriate.
Payroll or accounting system	Must be paid through state payroll system (HR/CMS/LCD)	Must be paid through statewide enterprise accounting and financial reporting system (Mosaic)
Tax reporting form	Form W-2	Form 1099-MISC
Other contractor requirements	• Contractors **MAY NOT** be used as a substitute for a state position and may not supervise employees in state positions. • Contractors may not act as an "agent" for a department and therefore, may not be placed in a position that will allow or create the perception that a contractor can make decisions or commitments on behalf of a department. Therefore, a department may not delegate signature authorization or transaction approval responsibility or security to a contractor. • Contractors are required to maintain the security and confidentiality of any records or data of the department to which they have access during and after the contract period.	

Associated Resources

- 801 CMR 21.00: Procurement of Commodities or Services, Including Human and Social Services
- 29 USC §201 Fair Labor Standards Act
- IRS Form SS-8: Determination of Employee Work Status for Purposes of Federal Employment Taxes and Income Tax Withholding"
- Omnibus Budget Reconciliation Act of 1990 (OBRA)
- Expenditure Classification Handbook issued by the Office of the Comptroller
- M.G.L. c. 7 § 22
- M.G.L. c. 7A §§ 3, 7, 8
- M.G.L. c. 29 § 29A
- M.G.L. c. 30, §§ 51-52
- Employment Status Form