

Massachusetts Supreme Judicial Court Rules that Independent Contractor Test Applies to Franchisees

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Key Takeaways:

- The three-pronged “ABC test” for independent contractor status set forth in the Massachusetts independent contractor statute may apply to franchisors-franchisee relationships in Massachusetts.
- Where a franchisee is an “individual performing any service” for a franchisor, the franchisee is presumptively an employee, unless the franchisor can rebut the presumption by establishing each prong of the ABC test.
- Businesses that engage individuals as independent contractor franchisees must be able to satisfy the ABC test to avoid potential liability for employee misclassification.

On March 24, 2022, the Massachusetts Supreme Judicial Court (SJC) ruled in *Patel v. 7-Eleven* that the test for independent contractor status set forth in the Massachusetts independent contractor statute applies to the relationship between a franchisor and its franchisee. Accordingly, where a business enters into a franchisor-franchisee relationship with an individual in Massachusetts and classifies that franchisee as an independent contractor, the relationship must meet the three prongs of the statutory independent contractor test to avoid liability for misclassification.

The independent contractor statute, Mass. Gen. Laws. ch. 149, § 148B, sets forth a presumption that “an individual performing any service” for an alleged employer is an “employee.” The alleged employer may rebut that presumption by establishing the three-prong ABC test set forth in the statute for determining whether an individual performing services for another is an employee or an independent contractor. Under that test, the worker is an employee unless the alleged employer can 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.

If the alleged employer fails to establish any one of these prongs, the individual is an employee under the law and thus entitled to the legal protections afforded employees under Massachusetts’ wage laws, such as a minimum wage, overtime pay, and timely payment of earned wages, among other things.

The plaintiffs in *Patel* entered into franchise agreements with 7-Eleven, Inc. (“7-Eleven”) that, according to the plaintiffs, improperly classified them as independent contractors. The question before the SJC, certified to it from the First Circuit, was whether the ABC test applies to the relationship between a franchisor and its franchisee, where the franchisor must also comply with a Federal Trade Commission regulation known as the Franchise Rule. The FTC Franchise Rule sets forth certain disclosure requirements that are triggered when a prospective franchisor elects either “to exert a significant degree of control over the franchisee’s method of operation, or to provide significant assistance in the franchisee’s method of operation.” 7-Eleven argued that the Franchise Rule preempted the

application of the independent contractor statute due to a purported conflict between their respective “control” prongs.

The SJC concluded that the legislature did not intend to exclude franchisees from the independent contractor statute and otherwise found no conflict between the Franchise Rule and the ABC test. Thus, the Court held that the independent contractor statute does apply to the relationship between a franchisor and its franchisee.

The SJC provided additional guidance that may bring comfort to franchisors who fear that all franchisees will be classified as employees under the ABC test. First, the Court noted that “nothing in the independent contractor statute prohibits legitimate franchise relationships among independent entities that are not created to evade employment obligations under the wage statutes.” Second, the Court reiterated that distinguishing between independent contractors and employees “requires examination of the facts of each case, which begins with a threshold determination whether the putative employee ‘perform[s] any service’ for the alleged employer.” According to the Court, this threshold is not satisfied merely because the relationship benefits the parties’ mutual economic interests. Third, the Court suggested that, where appropriate, a franchisor may charge an employee-franchisee a franchise fee deductible from gross revenue without running afoul of the Wage Act’s prohibition against assignment of an employee’s future wages to his employer.

The Court expressed no opinion as to how the ABC test applies to the facts in *Patel*. The case will return to federal court for further proceedings. However, the ruling provides clear guidance to franchisors in Massachusetts that they must be able to satisfy the ABC test when classifying individuals as independent contractors or face potential liability for employee misclassification, which can be significant given Massachusetts’ steep penalties for Wage Act violations, such as mandatory treble damages and attorneys’ fees.

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