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California's Expansion of Dynamex's ABC Test Severely Restricts When Employers May Properly Classify Workers as Independent Contractors

Last month, California Governor Gavin Newsom signed Assembly Bill 5 into law. This lengthy bill generally codifies and expands the applicability of the three-part ABC test from the *Dynamex* decision in determining whether a worker is an employee or independent contractor for purposes of California Labor Code, Unemployment Insurance Code, and the Wage Orders.

The ABC Test

As this blog previously discussed, the Supreme Court decision in *Dynamex* held that for purposes of the California Wage Orders, a worker who performs services for hire is an employee, rather than an independent contractor, unless the hiring entity establishes each of these three factors:

(A) that the worker is free from the control and direction of the hiring entity in performing the work;

(B) that the worker performs work that is outside the usual course of the hiring entity's business; and

(C) that the worker is customarily engaged in an independently established trade, occupation or business of the same nature as the work performed.

This ABC test made it more difficult to properly classify workers as independent contractors than under the previously applicable *Borello* multi-factor test.

As we previously noted here, AB 5 expanded upon *Dynamex* by making the ABC test applicable under the Labor Code and Unemployment Insurance Codes, in addition to the Wage Orders. This means the ABC test also applies for purposes of unemployment benefits claims and wage and hour claims under the Labor Code.

The Numerous Exceptions

At the same time, AB 5 carves out a number of exceptions from the ABC test that were not specified in *Dynamex*, including, among others:

- Licensed insurance agents;
- Certain licensed health care professionals, including physicians, surgeons, dentists, podiatrists, psychologists, and veterinarians;
- California licensed lawyers, architects, engineers, private investigators, accountants;
- Registered securities broker-dealers or investment advisers or their registered agents and representatives;
- Direct sales salespersons;
- Commercial fishermen (exemption is applicable only until January 1, 2023);
- Workers providing licensed barber or cosmetology services (exemption for licensed manicurists is applicable only until January 1, 2022);
- Workers performing certain types of marketing, human resources, or travel agent services;
- Graphic designers, grant writers, fine artists, certain tax professionals, payment processing agents, photographers or photojournalists, freelance writers, editors, or newspaper cartoonists;
- California real estate licensees and repossession agencies;
- Business to business contracts;
- Those performing work pursuant to a subcontract in the construction industry;
- Relationships between referral agencies and service providers.

Note the exceptions are numerous and each one has different conditions that must be met for it to apply. The conditions touch on everything from specific licensing requirements to whether the service provider is truly free from the control and direction of the contracting business entity. Great care must be taken in reviewing the potential exceptions and analyzing whether they might apply. Some exceptions also alter the test that will apply in determining employee or independent contractor status. For example, AB 5 specifically recognizes that whether a real estate licensees and repossession agencies are employees or independent contractors may be governed by other California code sections or standards.

The Borello Test Lives On

Generally, however, where the ABC test does not apply, the longstanding multi-factor test from *S.G. Borello & Sons, Inc. v. Dept. of Industrial Relation* will apply to determine employee or independent contractor status. As we noted previously, the *Borello* test considers multiple factors such as the right to control, whether the parties believed they were creating an employer-employee relationship, the right to discharge, the distinctiveness of the services provided, the method of payment, and the length of time that services were provided, among others. Not all of these factors have to be met to establish independent contractor status.

The Road Ahead

There will likely be continued developments in the application of AB 5. The complex exceptions will raise more questions than they answer. We have already seen leaders in the gig economy state their position that the ABC test does not preclude them from classifying workers as independent contractors. A clean-up bill is expected next year and there will most certainly be continued efforts by industry groups to include additional carve-outs from the ABC test. In the meantime, businesses are encouraged to consult with employment counsel in evaluating whether classifying workers as independent contractors is still proper in light of AB 5.

For workers who no longer meet the test for independent contractor status, care should be taken to reclassify them to employees or other measures should be taken to ensure compliance with the law. For example,

businesses may consider whether to use staffing agencies to h ire workers who cannot be properly classified as independent contractors. Keep in mind that when using a staffing agency, due to joint employer considerations, businesses should ensure that workers are classified as employees by the agency and the contract with the agency should include indemnification protections for the business. Businesses should carefully review any consulting agreements with purported independent contractors in light of AB 5 as well as consider the state laws where the consultant is working.

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