California Passes Landmark Bill Restricting Classification of Contract Workers

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09 / 16 / 19

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As of September 11, 2019, the California Senate and Assembly had both passed an employment bill (AB5) that, if signed by Gov. Gavin Newsom, would codify the recent extension of employment protections to workers previously classified as independent contractors. AB5 codifies the recent California Supreme Court decision in *Dynamex v. Super. Ct. of Los Angeles*, 4 Cal. 5th 903 (2018) (*Dynamex*): It adds Section 2750.3 to the California Labor Code and tracks the *Dynamex* three-part "ABC" test, stating that "a person providing labor or services for remuneration shall be considered an employee rather than an independent contractor unless the hiring entity demonstrates that all of the following conditions are satisfied:

A. The person is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact.

B. The person performs work that is outside the usual course of the hiring entity's business.

C. The person is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed."

AB5 expands the reach of the *Dynamex* "ABC" test by applying it for purposes of the provisions of the Labor Code as well as California's Unemployment Insurance Code and the wage orders of California's Industrial Welfare Commission. AB5 explicitly exempts various occupations, industries and contracting relationships from application of the *Dynamex* three-part test, instead requiring application of other tests to determine employment status of such relationships. For example, licensed physicians, surgeons, lawyers, engineers, accountants, and registered securities broker-dealers and investment advisers, among others, are exempt from application of the *Dynamex* test. Their employment status is governed by the California Supreme Court's decision in *S.G. Borello & Sons, Inc. v. Dep't of Indus. Relations*, 48 Cal. 3d 41 (1989) (*S.G. Borello*), which sets forth a flexible 10-factor test that is a facts-and-circumstances balancing test and does not require all 10 factors to be met in order to establish independent contractor status. In addition, workers in "professional services" roles, including, for example, certain roles in marketing, human resources administration, travel agency services, graphic design and fine art, are exempt from application of the *Dynamex* three-part test, and the 10-factor *S.G. Borello* test applies to those roles only if a hiring entity first shows that a preliminary six-factor test is fully satisfied, including that the worker is engaged at a separate business location and the worker can set or negotiate rates for services performed. Similarly, the *Dynamex* three-part test does "not apply to a bona fide business-to-business contracting relationship," which requires, among other things, that a business exist as a legally recognized entity, execute written contracts and provide services directly to another business (rather than to another business' customers). Also, the *Dynamex* three-part test does not "apply to a relationship between a contractor and an individual performing work pursuant to a subcontract in the construction industry."

If a court rules that the *Dynamex* three-part test cannot be applied to a particular context based on grounds other than an express exception to employment status as discussed above, then the determination of employee or independent contractor status in that context will be governed by the 10-factor *S.G. Borello* test.

AB5 provides that the addition of the *Dynamex* three-part test to the California Labor Code "does not constitute a change in, but is declaratory of, existing law with regard to wage orders of California's Industrial Welfare Commission and violations of California's

Labor Code relating to wage orders." To the extent that *Dynamex* exemptions in the bill would relieve an employer from liability, those provisions of the bill apply retroactively to existing claims and actions to the maximum extent permitted by law, while other provisions apply to work performed on or after January 1, 2020. AB5 does not permit an employer to reclassify an individual who was an employee on January 1, 2019, to an independent contractor following the bill's enactment.

AB5 is expected to have a significant impact on the gig economy, including the ride-hailing and food delivery industries. Though AB5 as currently drafted does not exempt workers in these specific industries from the *Dynamex* three-part test, companies, workers and other stakeholders in these industries have lobbied for such exemptions and are expected to continue to do so.