

## GOVERNOR SIGNS BILL CODIFYING ABC TEST FOR INDEPENDENT CONTRACTOR STATUS

*This Alert is a brief summary of Assembly Bill 5 (“AB-5”) and its implications. The bill and its effects will be covered in more detail at Stradling’s year-end employment law updates:*

*November 13 – Santa Barbara Hilton Garden Inn  
November 14 – Santa Maria Country Club  
(sponsored by Your People Professionals)  
November 19 – Newport Beach Stradling Office*

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Attendance is limited*

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On September 18, 2019, Governor Gavin Newsom signed into law AB-5, a bill that will have a major impact on any company that classifies workers or consultants as non-employee contractors.

The new law codifies the standard for determining independent contractor status adopted by the California Supreme Court last year in *Dynamex Operations West, Inc. v. Superior Court*. In that decision the Supreme Court adopted the “ABC” test when analyzing employment status under the California wage orders. AB-5 expressly approves the *Dynamex* decision and expands the ABC test to all questions of independent contractor status under the Labor Code, the Unemployment Insurance Code, and the Industrial Welfare Commission’s wage orders.

The bar is high for independent contractor status under the ABC test. In order for a worker to be properly classified as an independent contractor, the employer bears the burden of establishing all three prongs of the test:

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.”

AB-5 is designed to limit the scope of workers who can be classified as independent contractors. A stated motivation for this new law is the Legislature’s findings that the “misclassification of workers as independent contractors has been a significant factor in the erosion of the middle class and the rise in income inequality” as well a source of unfair competition against employers who properly classify their workers as employees and loss of tax revenue to the state. AB-5 thus expressly creates a presumption of employee status, with the company bearing the burden of proof to establish that a worker is properly classified as an independent contractor (i.e., meets all three prongs of the ABC test).

AB-5 does list a number of exemptions from the ABC test. But take heed - the exemptions do not establish that the workers are independent contractors. Rather, the listed workers are only exempt from the ABC test. Under AB-5, their employment status is analyzed under the independent contractor test established in the case *S. G. Borello & Sons, Inc. v. Department of Industrial Relations* that balances a number of

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factors to determine whether the worker can be classified as an independent contractor.

The exemptions listed in AB-5 that are subject to the *Borello* test, instead of the ABC test, include licensed insurance agents, registered securities broker-dealers or investment advisers, direct sales salespersons, real estate licensees, commercial fishermen, licensed workers providing barber or cosmetology services, and subcontractors in the construction industry. Also exempted are certain licensed health care professionals (physician and surgeon, dentist, podiatrist, psychologist, veterinarian) and licensed lawyers, engineers, private investigators and accountants.

Another set of exemptions applies to workers performing work under a contract for services in fields such as professional services such as marketing, human resources, travel agent services, graphic design, grant writing, enrolled agents, certain photographers and writers so long the relationship meets specified conditions.

AB-5 also includes an exemption from the ABC test for workers in other situations, again dependent on specified conditions being satisfied, such as a business entity that contracts with another business entity for the provision of services, the relationship between a referral agency and a service provider, PEOs, and employees of a company that loans those employees to provide services for another company. However, the governing standards are too complex to address in this Alert.

Many of these exemptions have their own specific requirements that involve a fact specific inquiry to determine if the individuals fall within the exemption. Again, these exemptions do not mean the individual is automatically considered

an independent contractor, but instead that their independent contractor status is determined under the balancing test established under the *Borello* decision.

While one of the other stated purposes of AB-5 is to clarify the application of the ABC test, the lack of certainty in the standards to apply in evaluating each of the three ABC factors in real life situations, as well in evaluating the scope of the exemptions, remains murky. Employers should not expect that California courts will look favorably on independent contractor classifications, no matter how common or long lasting the practice. It is recommended that companies take proactive steps to evaluate their non-employee workforce or service providers to assess their risks under AB-5 and the ABC test.

Please contact Jeff Dinkin or Sean Piers at Stradling if you would like discuss the application of AB-5 to your situation.

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(You can obtain a full copy of AB-5 at [http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill\\_id=201920200AB5](http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201920200AB5))