Tucker Ellis LLP

CLIENT ALERT

DYNAMEX IS HERE TO STAY: AB 5 WILL CHANGE HOW COMPANIES CLASSIFY CALIFORNIA WORKERS

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California's Assembly Bill No. 5 (AB 5), enacted on September 18, shrinks the class of workers who can be classified as independent contractors. Effective January 1, 2020, AB 5 codifies a 2018 California Supreme Court decision in *Dynamex Operations West, Inc. v. Superior Court of Los Angeles* (2018) 4 Cal. 5th 903, which changed the longstanding multifactor test for determining whether a worker is an employee or independent contractor. Both *Dynamex* and AB 5 have made headlines across the United States – so much so that gig companies just launched a $90-million campaign to escape AB 5's crackdown on the gig economy.

DYNAMEX ESTABLISHED THE "ABC" TEST

As a reminder, *Dynamex* established the "ABC" standard for determining independent contractor status:

> [A] worker is properly considered an independent contractor to whom a wage order does not apply only if the hiring entity establishes: **(A)** that the worker is free from the control and direction of the hirer in connection with the performance of the work, both under the contract for the performance of such work and in fact; **(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 for the hiring entity.

The *Dynamex* decision established a *presumption* that all workers are employees. It placed the burden on businesses to establish that classification as an independent contractor is proper under the newly iterated – and much stricter – ABC test. But *Dynamex* arguably applied only in some circumstances.

AB 5 CODIFIES DYNAMEX'S ABC TEST – WITH EXCEPTIONS

AB 5 adds the *Dynamex* ABC test to the California Labor Code effective January 1, 2020 to remove any doubt that it applies broadly; however, AB 5 does not limit the use of legitimate independent contractors, nor does it change their relationship with the companies who hire them. Further, as a result of lobbying efforts, AB 5 exempts many professions from AB 5's new standards, including psychologists, doctors, dentists, podiatrists, insurance agents, stock brokers, lawyers, accountants, engineers, veterinarians, direct sellers, hairstylists, barbers, aestheticians, real estate agents, fishermen, travel agents, marketing professionals, artists, graphic designers, grant writers, human resource administrators, payment processing agents, and repossession agents. Yet the exemptions leave out large sectors of the economy that will be subjected to the ABC test unless further action comes to pass. AB 5 will most notably impact California's app-based technology sector, which will surely continue to seek exemptions from any new mandate to classify certain workers as employees.

AB 5 IN PRACTICE

AB 5 will change the way many companies conduct their business and treat their workers. Employers must use care when determining that workers are independent contractors, and they must be prepared to defend that classification, as there are many wage and hour penalties for unpaid wages, unpaid overtime, and missed meal and rest breaks. Also, a fairly recent law, Labor Code section 226.8, added civil penalties from $5,000 to $25,000 for each violation. For workers who can no longer be classified as independent contractors, employers will have to provide unemployment and workers' compensation insurance. Consequently, AB 5 could result in substantial costs. Implementing the provisions of AB 5 will require detailed planning and immediate execution, but companies have little time before the bill becomes effective to assess their relationship with workers under the new ABC test and make essential structural changes where necessary.

AB 5 will be enforced via typical claims before the Labor Commissioner's Office, the Employment Development Department, and the Franchise Tax Board. AB 5 also gives the Attorney General, city attorneys, and local prosecutors the ability to bring actions for injunctive relief to prevent continued misclassifications. The City Attorneys of San Francisco and Los Angeles have made it clear that they are ready to aggressively enforce the new classification law.

BUT MY COMPANY DOESN'T HAVE WORKERS IN CALIFORNIA …

Although AB 5 is specific to California, other states – like New York – are considering similar bills and likely will follow closely behind. AB 5 may be only the beginning of a changing tide, expanding the definition of an employee, increasing the compliance obligations of companies, and bringing additional rights and benefits to workers who have previously operated independently.

The time to evaluate and plan for January 1, 2020 is now. And the wisest way to do that is to engage legal counsel to assist with the analysis, planning, and execution to ensure compliance with California labor laws.

ADDITIONAL INFORMATION

For more information, please contact:

- **Ndubisi Ezeolu** | 213.430.3239 | ndubisi.ezeolu@tuckerellis.com
- **Avril Love** | 213.430.3306 | avril.love@tuckerellis.com