CALIFORNIA SUPREME COURT DELIVERS A HARD BLOW TO THE GIG ECONOMY

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Employment Law Reporter, Ervin Cohen & Jessup LLP

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In a new ruling with dramatic consequences for the gig economy, the California Supreme Court made it harder to classify workers as independent contractors. For the past thirty years, the test for determining whether a worker qualifies as an independent contractor chiefly relied on the level of control the company exerted over the worker, a rather malleable concept that could be applied to qualify a wide range of workers as independent contractors, which companies had seen as beneficial since independent contractors generally cost companies less and are not subject to government regulations requiring tax withholdings, overtime compensation, minimum wage, and meal and rest breaks. However, in the class action case of *Dynamex Operations* West, Inc. v. Superior Court, the California Supreme Court did away with the old, flexible rules and instituted the more restrictive, albeit easier to apply, "ABC test" already used in New Jersey and Massachusetts.

Under the "ABC test," the Court presumes all workers qualify as employees. A worker may be classified as an independent contractor only if the employer can demonstrate that the worker:

(A) is free from the control and direction of the employer in connection with the performance of the work, both under the contract for the performance of the work and in fact;

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

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

The employer must be able to prove all three criteria. While part A of the test is similar to, and a key part of, the prior tests used by California courts as well as several government agencies, parts B and C represent significant departures from past tests and are particularly difficult for employers to meet. To explain these requirements, the Court provided examples: A plumber temporarily hired by a store to repair a leak or an electrician to install a line would be an

independent contractor. In contrast, a seamstress who works at home to make dresses for a clothing manufacturer from cloth and patterns supplied by the company, or a cake decorator who works on a regular basis on custom-designed cakes would be employees. An employer may evade classification of its worker as an employee "only if the worker is the type of traditional independent contractor" who would be understood as working "in his or her own independent business."

The *Dynamex* ruling turns California's gig economy on its head. Trucking companies, entertainment productions, and app-driven service businesses, such as Uber and Lyft, had relied upon the old, vague test to classify businesses with whom they routinesly contracted to complete various operations associated with their core or usual business operations as independent contractors. The defendant in this case, *Dynamex Operations West, Inc.*, is prototypical of these gig industries. *Dynamex* is a package and document delivery service that hires drivers as independent contractors. Dynamex's delivery drivers may set their own schedules, remain free to choose whether to accept or reject an assignment, and receive pay based on a flat fee or percentage of the delivery fee. Although the Dynamex decision did not resolve whether *Dynamex*'s drivers had in fact been misclassified as independent contractors, but rather provided guidance for lower courts that had been struggling with the issue, it is hard to imagine that the drivers will be allowed to remain classified as independent contractors after the ABC test is applied.

The reason for the *Dynamex* Court's overthrow of the old, flexible classification standards was stated as follows: "When a worker has not independently decided to engage in an independently established business but instead is simply designated an independent contractor … there is a substantial risk that the hiring business is attempting to evade the demands of an applicable wage order through misclassification." The Court stressed that California's wage and hour laws were adopted to enable people to earn a subsistence standard of living and to protect workers' health and safety. Moreover, the Court observed that the laws shield the public from having to assume financial responsibility for workers earning substandard wages or working in unhealthy or unsafe conditions.

Although the ABC test is certainly easier to apply than the prior test, the *Dynamex* decision leaves unanswered questions. The Court limited its ruling to California's wage orders, which set rules on basic working conditions and minimum pay. It is thus unclear what test or standard should apply for workers' compensation and tax purposes, leaving open the possibility that a worker may be classified in different ways for different purposes. This is likely to be a topic of future litigation.

All companies in California need to reevaluate their relationships with their independent contractors and adjust them as necessary to comply with the ABC test imposed by *Dynamex.* Failure to properly classify workers can result in steep fines for employers. In the very near future, we can expect to see a wave of class actions alleging misclassification and large-scale restructuring for California's gig-based business models. Without a doubt, the Dynamex decision is a game-changer that requires a fresh look at worker classifications to minimize potential exposure.