

## California Adopts Strict Independent Contractor Test in New Bill



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On September 18, California Governor Gavin Newsom signed AB 5, a bill that codifies and expands the application of the strict independent contractor test (the “ABC test”) set forth in last year’s decision (available at: <https://www.pepperlaw.com/publications/california-adopts-stricter-test-for-independent-contractor-status-2018-05-09/>) of the California Supreme Court in *Dynamex Operations West, Inc. v. Superior Court of Los Angeles*, 4 Cal.5th 903 (2018). The bill will go into effect on January 1, 2020.

AB 5 creates a presumption that workers are employees unless the “hiring entity” can meet the ABC test by demonstrating that each of the following three conditions is satisfied:

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(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.

Much of the text of AB 5 is devoted to the many and varied types of professions that are exempt from its provisions, reflecting successful lobbying by those groups. Among the exempted professions are licensed insurance workers, physicians, dentists, lawyers, engineers, accountants, registered securities broker-dealers or investment advisers, direct sales salespersons, real estate licensees, commercial fishermen, and workers providing licensed barber or cosmetology services. Also exempted are individuals who provide services under contracts for specific types of professional services if certain requirements are met, businesses that contract with other businesses if certain requirements are met, relationships between a contractor and subcontractor in the construction industry if certain requirements are met, and relationships between referral agencies and specified service providers if certain requirements are met. Instead of the ABC test, workers in the exempted groups will be subject to the more relaxed test set forth in *S.G. Borello & Sons, Inc. v. Department of Industrial Relations*, 48 Cal.3d 341 (1989), which involves the examination of 10 factors and does not require that each be met.

If a worker is not exempted from AB 5, he or she will be presumed to be an employee unless each of the factors in the ABC test is met, the most difficult of which is usually factor B. Hiring entities will be able to use independent contractors only if the services they perform are outside the usual course of the entity's business.

Although the *Dynamex* decision was confined to claims under California wage orders, AB 5 is broader and also applies the ABC test to independent contractor status under the California Unemployment Insurance Code and the California Labor Code. As a result, if an independent contractor relationship does not meet the ABC test, the contractor could be entitled to various employee protections under California law, including minimum wage, overtime pay, unemployment insurance, expense reimbursement, paid sick leave and paid family leave.

When AB 5 takes effect in January, it will become exponentially more difficult for entities with California workers to demonstrate that workers meet each factor of the ABC test and are classified properly as independent contractors. That is the result intended by the California Legislature, which stated, “It is also the intent of the Legislature in enacting this act to ensure workers who are currently exploited by being misclassified as independent contractors instead of recognized as employees have the basic rights and protections they deserve under the law.”

The passage of AB 5 likely will result in more misclassification claims by workers characterized as independent contractors. Indeed, on the heels of the California Assembly’s approval of AB 5, Uber drivers filed a putative class action against Uber in the U.S. District Court for the Northern District of California (*McCray v. Uber Techs., Inc.*, No. 19-5723 (N.D. Ca. Sept. 11, 2019)), alleging that they were misclassified as independent contractors and should have been reimbursed for business expenses and paid the minimum wage and overtime.

Although AB 5 will make it more challenging to establish compliant independent contractor relationships, it does not prohibit the use of independent contractors. Before the law becomes effective on January 1, 2020, entities that use independent contractors in California should review those relationships carefully to evaluate whether they meet the ABC test. If they do not, entities should assess whether they can restructure the relationships to satisfy the ABC factors or whether they should convert the independent contractors to employees.