FOR CONTRACTORS

EMPLOYEE OR INDEPENDENT CONTRACTOR?

The Rules Just Changed. Massively.

On April 30, 2018, the California Supreme Court issued a landmark decision that should be of critical interest to all California businesses that engage workers as a usual part of their business.

In short, the new decision shifts the rules for determining whether a worker is an employee or an independent contractor in the context of California's wage and hour laws.

The case was Dynamex Operations West, Inc. v. Superior Court.

Until now, employers applied a nebulous analysis that required review and weighing of numerous factors on a case by case basis. That analysis sometimes resulted in unwanted risk taking – sometimes even manipulation -- when determining whether a worker was an employee or independent contractor, but oftentimes, the worker could indeed qualify as an independent contractor. In the Dynamex case, the Supreme Court adopted a clearer but tougher standard that distinctly narrows the options for claiming a worker is an independent contractor.

The new standard – called the "ABC Test" – closely tracks federal law.

A worker will be presumed to be an employee UNLESS the hiring entity proves ALL of the following:

(A) The worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract and in fact; and

(B) The worker performs work that is outside the usual course of the hiring entity's business; and

(C) The worker is customarily engaged in an independently established trade, occupation, or business of the same nature as the work he or she performed for the principal.

Part A of the test, about control and direction, is the most abstract of the ABC Test criteria. The question at Part A is whether the employer in fact controls the worker in the manner and to the degree that an employer might control or direct a regular employee. The employer need not control the precise manner and detail of the work for the worker to be classified as an employee. Further, a contractual clause that asserts that the worker will control the manner and degree is not determinative; only the facts are determinative. If the employer is found to control the worker in the manner and to the degree that an employer would ordinarily control an employee, then the worker is considered an employee.

Part B of the test, about whether the work performed is a usual part of the hiring entity's business, is clearer, but very restrictive. This portion of the test requires that an independent contractor perform work not usually conducted as part of the hiring businesses normal operation. As applied, a delivery business that engages workers to make routine deliveries is carrying out a usual part of its business. As such, those workers would be classified as employees. In the alternative, a restaurant that calls upon a plumber to fix a plumbing leak is hiring an independent contractor.

Part C of the test, about whether the worker is actually an independent business, is also clearer but restrictive. In short, for a worker to be considered an independent contractor, the worker must actually operate an independent business (evidenced by having its own separate clients, business license, resale permit, equipment, advertising, business cards, invoicing, etc.).

This is a dramatic shift from the prior rules. **The good news is that the new ABC Test is a favor to businesses in the sense that it takes much of the guesswork out of determining who is and who isn't an independent contractor. The bad news is that the vast majority of persons working regularly for companies as independent contractors will now be viewed as employees.**

It is absolutely imperative that every California business review its relationships with workers presently classified independent contractors to ensure that they are in fact independent contractors under the ABC Test. Doing so proactively will help the employer avoid serious liabilities or penalties associated with misclassification of employees/independent contractors. Ignoring the new ABC Test or hoping that independent contractor agreements with your workers won't be noticed is unrealistic and risky.

As a practical matter, it makes sense to apply Part B and C of the ABC Test first.

Assuming that both Parts B and C indicate that the worker is an independent contractor, next apply the more abstract and vaguer Part A. This approach is suggested by the California Supreme Court.

The new ABC Test will be sorted out in litigation in the months and years to come. It is wise for nearly every small business to do everything it can to avoid being a part of that litigation, and to avoid the expense, penalties, and distractions that come with it.

By
Mark Alcorn, Attorney at Law
Alcorn Law Corporation
1000 Q Street | Sacramento CA 95814

Mark Alcorn serves as Legal Counsel to PDCC Inc.
Employers should confer with their legal counsel to determine if any of their workers should be reclassified.