INDEPENDENT CONTRACTOR OR EMPLOYEE

The California Supreme Court, on April 30, 2018 in Dynamex Operations West, Inc. v. The Superior Court of Los Angeles County, adopted a standard, called the “ABC” test, to distinguish employees from independent contractors. Effective January 1, 2020 the CA state legislature passed Assembly Bill 5 (AB 5), which codified this decision and the ABC test.

Under this test, 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 hiring entity in connection with the performance of the work, both under the contract for the performance of such work and in fact. Examples of such freedom may include:
   - the worker is able to set his/her own schedule; work without supervision;
   - purchases all materials and supplies and pays for those materials him/herself;
   - collects his/her own income from the client; has his/her own business license; books her/his own appointments, etc.

B. That the worker performs work that is outside the usual course of the hiring entity’s business. Examples include:
   - If a retail store hires an outside plumber to do plumbing work, the services of the plumber are not part of the store’s usual course of business.
   - If a clothing manufacturer hires an at home seamstress to make dresses from cloth provided by the company, the worker would not be classified as an independent contractor. The worker would be a part of the hiring company’s usual business operation.

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. An individual who independently has made the decision to go into business generally takes the usual steps to establish and promote that independent business. Examples of this include:
   - Incorporation, licensure, advertisements;
   - Routine offerings to provide the services of the independent business to the public or to a number of potential customers, and the like.

The hiring entity’s failure to prove ALL of the above tests will result in the finding that the worker is to be classified as an employee. Employers have the burden of proof in establishing workers are independent contractors.
This law contains exceptions for certain occupations, according to an analysis by the law firm Miller, Munson, Peshel, Pollack & Horshaw, attorneys at law. The list includes:

- insurance agents, doctors, dentists, podiatrists, psychologists, and veterinarians;
- lawyers, architects, engineers, private investigators, accountants, and enrolled agents;
- stock brokers and investment advisors;
- direct sellers and commercial fishermen;
- marketing professionals, human resource professionals, travel agents;
- graphic designers, grant writers, fine artists;
- photographers, photojournalists, freelance writers, editors or newspaper cartoonists who make 35 or fewer submissions per year;
- licensed: estheticians, electrologists, barbers, cosmetologists, and until 2022, also manicurists, if they set their own rates, hours, appointments and client list, process their own payments, and have a book of business; and
- real estate agents and repossession agents.

Subject to additional tests, business-to-business contractors, construction industry contractors, referral agencies, and motor clubs may be exempt.

However, such exceptions are not exemptions. For the listed occupations, the Borello test (S.G. Borello & Sons, Inc. v. Dept. of Industrial Relations (1989) 48 Cal.3d 341) applies. The test relies upon multiple factors to make a determination of employment, including whether the potential employer has all necessary control over the manner and means of accomplishing the result desired, although such control need not be direct, actually exercised or detailed. This factor, which is not dispositive, must be considered along with other factors. For a list of other factors, see question 5 in the link provided below for the CA Department of Industrial Relations.

Employers must be careful in making the determination as there are many wage and hour penalties for unpaid wages, unpaid overtime and missed meal and rest breaks in addition to large civil penalties under the new Labor Code 226.8 with penalties from $5,000 to $25,000 for each violation of misclassifying an employee as an independent contractor. Penalties and interest may also apply to failure to withhold and pay payroll taxes, such as Social Security, Medicare, State Disability Tax, and Federal and State Unemployment Tax, as well as failure to procure workers’ compensation insurance.

Owners of businesses who have independent contractors should immediately conduct an audit of their use of contractors given the new standards and seek legal advice about their specific situations. It is likely that many current contractors may not qualify as independent contractors under the new CA Supreme Court test.

We recommend you talk with an attorney with any questions you have. You may view the complete description of the new law by clicking this link for the CA Department of Industrial Relations. [https://www.dir.ca.gov/dlse/faq_independentcontractor.htm](https://www.dir.ca.gov/dlse/faq_independentcontractor.htm).