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Not So Independent After All:
Time to Reevaluate Your Independent Contractor Arrangements

Presented By

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Overview of today's discussion

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- A myriad of independent contractor tests
- Review of the *Dynamex* decision
- Implications for specific industries
- Actions since the issuance of the decision
- Potential exposure associated with a misclassification determination
- Avoiding misclassification claims

Prior to *Dynamex* Decision…

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- There were numerous tests for CA employer to consider in determining if a worker is properly classified as an independent contractor
  - *S. G. Borello & Sons, Inc. v Dept. of Industrial Relations* (1989) – multi-factor test
    - Followed by the Division of Labor Standards Enforcement (DLSE) in matters regarding wage, hour and workers' compensation ins. laws
    - Also adopted by Employment Development Department (EDD) - employment-related taxes
  - Internal Revenue Service's 20 Factor Test
  - U.S. Department of Labor – to comply with the Fair Labor Standards Act and Family and Medical Leave Act will look to the "economic realities" test
  - U.S. Supreme Court's 13-factor common law based test adopted in *Nationwide Mt. Ins. Co. v. Darden* to determine whether a worker is an employee under ERISA
  - Other CA agencies have their own tests as well!

The Issue Presented in *Dynamex*:

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- What Standard Applies Under California's Wage Orders to Determine Whether a Worker Is an Employee or an Independent Contractor?
- *Dynamex Operations West, Inc. v. Superior Court*, No. S222732, 2018 Cal. LEXIS 3152 (Cal. Apr. 30, 2018).

The facts in *Dynamex*

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- Two individual drivers filed a class action against a nationwide package and document delivery company, Dynamex
- The drivers claimed Dynamex misclassified its delivery drivers as independent contractors instead of employees
- Dynamex had previously classified the drivers as employees, and later re-classified them as contractors under a new company policy and entered into agreements with the workers that stated that each was a contractor, not an employee
- The plaintiff drivers said the work was the same

The claims in *Dynamex*

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- Did the lower court use the correct definitions of the terms "employ" and "employer" to decide whether a worker is properly classified as an independent contractor under California Wage Order # 9?
  - Generally under the Wage Orders, the term "[e]mploy" means "to engage, suffer, or permit to work," while the term "employee" means "any person employed by an employer"
  - The Wage Orders set forth significant obligations for employees (as opposed to independent contractors), including but not limited to, requirements regarding minimum wage, overtime, pay records, and meal/rest periods
- In *Dynamex*, the company argued the court should follow the *Borello* test

The California Supreme Court disagrees

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- Rejects that the court was obligated to follow *Borello*
- At issue was the "suffer or permit to work" part of the wage order's definition of "employ"
- "[T]he wage order's suffer or permit to work definition must be interpreted broadly to treat as 'employees,' and thereby provide the wage order's protection to, all workers who would ordinarily be viewed as working in the hiring business."

The ABC Test

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- The hiring entity has the burden to establish that a worker is an independent contractor and not an employee covered by a wage order
- To meet this burden, the hiring entity must establish each of the three factors embodied in the ABC test:

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 for the performance of the work 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 performed by the worker

Deeper dive on ABC

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- Is your worker the cake decorator or the plumber?

Deeper dive on ABC

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Factor “A”

- How much control?
- What is “free from the control”?
- Actual control versus right to control
- How broad is the term “performance”?
- Lesson Learned from Connecticut:
  - Part A of the ABC test provides that "[s]ervice performed by an individual shall be deemed to be employment . . . unless and until it is shown to the satisfaction of the administrator that . . . such individual has been and will continue to be free from control and direction in connection with the performance of such service, both under his contract for the performance of service and in fact . . . ." *See Tianti v. William Raveis Real Estate, Inc*., 231 Conn. 690, 651 (1995) (confirming that claimants were employees rather than independent contractors, holding that the company had the right to control its salespersons on the basis of findings that they "were required to attend mandatory office meetings . . . did business under the defendant’s name . . . used the company letterhead, business cards and supplies . . . were required to attend training sessions . . . and . . . were threatened with discharge if they did not comply with these requirements.”)

Deeper dive on ABC

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Factor "B"

- What is the "usual course" of business?
- Who determines what that is?
- Is it enough to physically work outside of the company's usual place of business?
  - Is that going to be required?
- Lesson learned from New Jersey:
  - *Trauma Nurses, Inc. v. Board of Review*, 242 N.J. Super. 135, 141 (1990) (finding that providing healthcare services was "clearly beyond the purview and usual course of TNI's business" of brokering healthcare personnel)

Deeper dive on ABC

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Factor "C"

- What is "customarily engaged"?
- Individual versus another entity
- What is meant by "independently established"?
- Lesson learned from New Jersey:
  - *Philadelphia Newspapers, Inc. v. Board of Review*, 397 N.J. Super. 309 (2007) - The requirement that the claimant be customarily engaged in an independently-established trade, occupation, profession or business "calls for an enterprise that exists and can continue to exist independently of and apart from the particular service relationship. The enterprise must be one that is stable and lasting--one that will survive the termination of a relationship." If the claimant is "dependent on the employer, and on termination of that relationship would join the ranks of the unemployed, Prong (C) is not satisfied."

Implications for specific industries

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- Gig economy
- Healthcare
- Real estate/mortgage brokers
- Financial advisors
- Construction
- Cosmetologists
- Etc., etc., etc.!

Aftermath of *Dynamex*

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- Is it retroactive?
- Application beyond the Wage Orders?
- Filings since *Dynamex*
- Potential for legislative changes

Potential Exposure

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- Unpaid wages and overtime
  - Possible arguments for exempt status
- Liquidated damages
- Interest
- Attorneys' fees and costs

- Penalties for violation of federal and state labor laws (such as missed meal periods/rest breaks)
- Penalties for failure to pay applicable federal, state and local taxes

Potential Exposure *cont'd*

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- Cost of litigation
- Potential PAGA claims, class actions, and audits
- Media exposure

Other considerations

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- LC Section 226.8 makes it unlawful to willfully misclassify an individual as an independent contractor
- Stiff penalties attach to such violations
  - pattern and practice violation civil penalties of not less than $10,000, and not more than $25,000 for each violation
  - any other penalties or fines the law permits
- Potential individual liability – officers and directors of a company may be found personally liable for misclassification claims under LC section 558.1

Other considerations *cont'd*

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- Reclassifying a contractor as an employee may raise questions as to whether the worker was properly classified in the first instance, and in some instances result in legal action

What should employers do now?

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1. Ensure that HR and decision-makers understand, through training or otherwise, how to properly classify workers
   – for California workers sole reliance on guidelines such as the *Borello* and/or IRS "20-factor" test could result in classification problems
2. Consider adding mandatory arbitration and class action waiver provisions in consulting agreements

What should employers do now?

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3. Consider alternative scenarios
4. Review form contracts used with contractors
   - The contract's language will not ultimately determine independent contractor status (as *Dynamex* makes clear), but it may nevertheless be relevant to the analysis and helpful in establishing a contractor relationship
5. Take disputes with contractors seriously whether in a private action or before the EDD, DLSE, IRS, etc.

Questions?

THANK YOU!

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Equal Pay for Equal Work: How to Ensure Your Company is in Compliance

June 20, 2018
Noon to 1PM PST

Pay equity is now a daily headline – from disparities in pay between your favorite male and female movie stars to gender wage gaps between the folks that serve up your morning cup of brew. The laws, regulations, and norms in this space are swiftly evolving. Join us to learn how to better protect your organization from the legal liability — as well as public relations risks — that come with underpaying certain segments of your employee population.

In this webinar, employment law attorneys from Buchalter will offer perspectives to help you ensure your organization is in compliance with the Equal Pay Act and relevant state/local legal requirements, including California's stringent requirements.

A corporate gender equity consultant from Portola Advisors will advise you on avoiding common root causes of the pay gap, and on improving gender equity & advancing women leaders in your company.