CALIFORNIA SUPREME COURT APPLIES AN "ABC" TEST FOR EMPLOYERS TO USE WHEN ASSESSING WHETHER WORKER IS AN EMPLOYEE OR INDEPENDENT CONTRACTOR

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By: Judith M. Sasaki and
Gregory J. Norys

For years, even the most conscientious California employers have had difficulty determining whether a worker can correctly be classified as an independent contractor. The distinction is significant. Workers classified as employees are entitled to the benefits of a complex web of federal and state labor statutes (particularly in California). In addition, employers bear the responsibility for paying payroll and employment taxes, as well as unemployment insurance for their employees. Misclassification of a worker subjects the employer to a myriad of problems and liability.

The Department of Labor Standards Enforcement (DLSE) starts with the presumption that the worker is an employee. Labor Code ' 3357. However the presumption is rebuttable depending on the application of a number of factors. The common law test for employment which has been followed for many years is set forth in S. G. Borello & Sons, Inc. v. Dept. of Industrial Relations (1989) 48 Cal.3d 341. In Borello, the determination whether a worker is an employee or independent contractor depends upon a number of factors, commonly known as the "multifactor" or "economic realities" test. In Martinez v. Combs (2010) 49 Cal.4th 35, 109 Cal Rptr.3d 514, the California Supreme Court determines employee status for Wage Order claims using a broader IWC definition of an employee construed as the Aengage, suffer, or permit to work test. The coexistence of these two tests and the inconsistent application of these tests has been the source of some confusion by employers.

In a landmark decision issued on April 30, 2018, the California Supreme Court provided businesses with more guidance in making the distinction between independent contractors and employees. In Dynamex Operations v. Superior Court, the California Supreme Court defined the issue on appeal as whether, in a misclassification case, a

class may be certified based on the expansive definition of employee as outlined in the Wage Order language construed in Martinez (2010), or on the basis of the common law test for employment set forth in Borello (1989). In short, the Supreme Court focused on whether to continue using the Borello test or whether to apply a different analysis. The Supreme Court held that the Aengage, suffer or permit to work standard determines employee status for Wage Order claims, requiring a defendant disputing employee status to prove:
(A) the worker is free from the hirers control and direction of the hirer in connection with performing the work, both under contract and in fact;
(B) the worker performs work 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 for the hirer.

The Supreme Court conceded that the phrase A suffer or permit cannot be interpreted literally in a manner that would encompass workers such as independent plumbers or electricians who have traditionally been viewed as genuine independent contractors and who work only in their own independent business.

The first prong is similar to the prior test in which the hiring company cannot exercise the same or similar control (i.e., means, manner, time, etc., Y) that it exercises over its own employees. The second and third prongs, however, could significantly change the status of who is classified as an independent contractor. The court provided specific examples of who would qualify as independent contractors under the second prong of the ABC Test. For example, the Court explained: When a retail store hires an outside plumber to repair a leak in a bathroom on its premises or hires an outside electrician to install a new electrical line, they would be independent contractors because they are not part of the store's usual course of business and the store would not reasonably be seen as having suffered or permitted the plumber or electrician to provide services to it as an employee. In these types of scenarios the workers will be deemed independent contractors.

On the other hand, when a clothing manufacturing company hires work-at-home seamstresses to make dresses from cloth and patterns supplied by the company that will thereafter be sold by the company or when a bakery hires cake decorators to work on a regular basis on its custom-designed cakes, the workers are part of the hiring

companies usual business operation and the hiring business can reasonably be viewed as having suffered or permitted the workers to provide services as employees. In these types of scenarios the workers will be deemed employees.

The third prong of the test requires evidence that the worker independently has made the decision to go into business for himself or herself (risk with loss of profit). Such an individual generally takes the usual steps to establish and promote his or her independent business. For example, the individual may incorporate the business, get the business properly licensed, market and advertise the business, make routine offerings to provide the services of the independent business to the public or to a number of potential customers, and the like.

Employers should carefully evaluate their practice of classifying potential employees as independent contractors. Misclassification of workers carries serious fines and penalties, including back wages, and possibly back taxes.

Judith M. Sasaki and Gregory J. Norys are partners with Coleman & Horowitt, LLP.

Judith M. Sasaki's practice has encompassed a broad range of subject matters and she has handled all aspects of litigation in the areas of complex commercial, entertainment, real estate, business and unfair competition cases. She has handled numerous court and jury trials as well as mediations and arbitrations. She has regularly represented clients before the Independent Film and Television Alliance (IFTA) and the International Chamber of Commerce for entertainment related arbitrations. In addition, Judy frequently serves as a speaker for continuing legal education services, including The Rutter Group, on topics relating to trial practice.

Gregory J. Norys manages the firm's Visalia office. As head of the firm's labor & employment practice group, Greg works in the firm's litigation department representing clients in complex commercial and real estate litigation, construction litigation, labor and employment counseling and litigation, and professional liability defense litigation. He has been named a Northern California Rising Star® by Super Lawyers (Thomson Reuters) and is a member of the Tulare and Fresno County Bar Associations and the Association of Business Trial Lawyers. Greg can be reached at gnorys@chlaw.com or (559) 248-4820, ext. 161.