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California Supreme Court's *Dynamex* Decision Sets High Bar to Classification of Workers as Independent Contractors

The California Supreme Court recently issued an important and long-awaited decision, *Dynamex Operations West, Inc. v. Superior Court of Los Angeles*, establishing a new, more stringent three-part test to determine whether a worker should be classified as an independent contractor or as an employee subject to extensive regulations under California's Industrial Welfare Commission wage orders. Such wage orders regulate, among other things, employees' minimum wages, minimum hours, and working conditions in various industries. Critically, under this new test – referred to as the "ABC" test – a worker is presumed to be an employee unless the hiring entity is able to satisfy each part of the test. This decision has an immediate and significant impact on California businesses and those businesses engaging workers in California.

Background

Whether a worker is an employee or independent contractor is a critical distinction. If a worker is an employee, the business employing the worker must not only comply with federal and applicable state laws and regulations governing the wages, hours and working conditions of the employee, but also be responsible for paying the employee's payroll and Social Security taxes, unemployment insurance and state insurance taxes, and providing worker's compensation insurance. For that reason, many businesses hire workers as independent contractors so as to avoid these expenses and legal obligations.

Prior to 2004, Dynamex Operations West, Inc. ("Dynamex"), a nationwide package and document delivery company, had classified its delivery drivers as employees. In 2004, however, Dynamex adopted a new policy for a contractual arrangement under which its drivers would be treated as independent contractors. Dynamex was then sued by two individual delivery drivers in a putative class action alleging that they were misclassified as independent contractors in violation of the wage order applicable to the transportation industry, as well as under various sections of the California Labor Code.

The California Supreme Court's Decision

For nearly 30 years prior to *Dynamex*, California courts determined whether a worker was an employee or independent contractor by employing a multi-factor analysis under which the most important factor was the employer's "right to control" the manner and means by which the worker performed his/her duties. The multi-factor analysis also considered various secondary factors, including the degree of skill required to perform the work, the method of payment, and the nature of the company's regular business.

Dynamex disregards the multi-factor analysis for purposes of the California wage orders. Under the new "ABC" test, a worker is considered an independent contractor to whom wage orders do not apply if, and only if, the hiring entity establishes that:

> (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 such work and in fact;
>
> (B) the worker performs work that is outside the usual course of the hiring entity's business; *and*
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> (C) 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.

The Court held that it is the burden of the *hiring entity* to establish *each* of the three foregoing factors. Notably, a number of other states have adopted similar, but narrower, versions of the "ABC" test for classifying employees. In those states, a hiring entity can satisfy part (B) by establishing *either* (1) that the work provided is outside the usual course of the business for which the work is performed, *or* (2) that the work performed is physically located outside of the hiring entity's places of business. Unlike in those states, a hiring entity in California can satisfy part (B) only if the work itself falls "outside the usual course of" the hiring entity's business. For example, a delivery company, like Dynamex, will have to establish that the delivery of products to consumers by its drivers falls outside of the company's usual course of its business.

Impact of *Dynamex* on Businesses

Many businesses will now be required to reclassify their workers as employees. This is especially true for those businesses operating in California's gig economy, which engage workers as independent contractors and who perform work that is not "outside the usual course of the hiring entity's business."

Companies that rely on the independent contractor designation of their workers should promptly discuss their designations with counsel. Attorneys at Kasowitz Benson Torres LLP have extensive experience and familiarity with the legal standards governing the proper classification of a company's workforce under California, New York, and other state and federal law. If you would like to discuss these issues, please contact **Mark W. Lerner** (212-506-1728) or **Jessica T. Rosenberg** (212-506-1789).

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