AB 5 Contractor-Classification Battles Set To Heat Up In 2021

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Employers grappling with independent-contractor classification had a busy 2020 — and should expect a flurry of additional activity this year.

Few areas in employment law are changing as rapidly.

Last year, many concerned about the future of contractor-classification laws paid careful attention to California and A.B. 5, which went into effect on Jan. 1, 2020, and codified the California Supreme Court's landmark decision in Dynamex Operations West Inc. v. Superior Court of Los Angeles.[1]

For most workers, California now uses the ABC test for determining whether a worker may be classified as an independent contractor.

According to the ABC test, a worker is only an independent contractor if the worker (a) is free from the hiring entity's control in connection with the performance of the work, (b) performs work that is outside the usual course of the hiring entity's business and (c) is customarily engaged in an independently established business of the same nature as the work performed for the hiring entity.

Multiple challenges to A.B. 5 occurred in 2020, including lawsuits filed by various industry associations, such as the California Trucking Association and numerous proposed bills to exempt certain industries from its coverage.

On Sept. 4, 2020, certain businesses achieved success when California expanded the list of workers who are exempt from A.B. 5. While this was good news for some, it resulted in further outcry by others who continue to be within A.B. 5's reach.

For the trucking industry, a decision from the U.S. Court of Appeals for the Ninth Circuit as to whether A.B. 5 is preempted by the Federal Aviation Administration Authorization Act is expected this year and many practitioners believe the battle may end up before the U.S. Supreme Court.

For California employers, there will be no shortage of continued legislation and court challenges surrounding A.B. 5 and the resulting fallout this year.

The gig economy, long grappling with restrictions imposed by independent contractor laws, created a third way of classification through California's voter-supported Proposition 22.

Proposition 22 exempts certain app-based transportation and delivery drivers from A.B. 5. Instead, it provides covered workers with limited health care subsidies, accident insurance, reimbursement for some expenses and minimum wage protections during certain periods of work while allowing covered companies to continue to classify workers as independent contractors.

Employers familiar with the phrase "As California goes, so goes the nation," predict many states will soon have their own battles over legislatively codifying their respective ABC tests as well as creating a third class of worker.

For example, legislators in states including Massachusetts, Minnesota, New Jersey, New York, Pennsylvania, Rhode Island and Washington indicated they would immediately follow California's A.B. 5 and pass similar legislation to clamp down on the use of independent contractors.

However, many of those efforts appear stalled because of industry group lobbying and delays caused by the COVID-19 pandemic.

Employers should see these stalled efforts make a resurgence in 2021. It remains to be seen whether states will pursue their own A.B. 5 type legislation or if lessons will be learned from the Proposition 22 battle and a more compromised approach will prevail.

Given that California's legislation received a barrage of attacks on all fronts — in the courts, in the legislature and among its constituents — a compromise might be the end result.

In contrast, with regard to federal wage and hour law, on Sept. 22, 2020, President Donald Trump's outgoing U.S. Department of Labor issued proposed regulations, which, if finalized, would make it easier for employers to classify workers as contractors under the Fair Labor Standards Act.

The proposed regulations focus on (1) the nature and degree of the worker's control over the work; (2) the individual's opportunity for profit and loss; (3) the amount of skill required for the work; (4) the degree of permanence of the working relationship, and (5) whether the work is part of an integrated unit of production.

Essentially, the DOL's ultimate inquiry is one of economic dependence. If a worker is, as a matter of economic reality, dependent on the employer for work, then the worker is classified as an employee.

However, if a worker is in business for himself or herself as a matter of economic reality, then they are an independent contractor. The deadline for comments on the proposed rule was on Oct. 26, 2020, and the DOL declined to extend the deadline for comments.

The DOL has not yet issued its final findings or rule. However, given the pending change in administration, employers should prepare for the DOL to take action before the Biden administration takes office Jan. 20 and then should prepare again, for the DOL to reverse course.

In the meantime, on Feb. 6, 2020, the United States House of Representatives passed the Protecting the Right to Organize Act of 2019, otherwise known as the PRO Act by 224 to 194, mostly along party lines. The Republican-controlled Senate did not take action on the bill and is expected to stall its passage in 2021.[2]

Among other things, the PRO ACT seeks to modify the National Labor Relations Act's definition of independent contractors to track the ABC test.

Under the NLRA, employees are eligible to organize unions while independent contractors are not. If passed in current form, this provision would result in a significant expansion of the number and types of workers that would be able to organize labor organizations and seek other protections under the NLRA.

President-elect Joe Biden has indicated that he endorses the PRO Act and even more broad

sweeping legislative change. Whom Biden selects as U.S. secretary of labor might give an indication of what to expect on this front.

Another bill, the Worker Flexibility and Small Business Protection Act, was introduced in Congress in September 2020.

While this bill has yet to receive significant attention at the House thus far, this bill also seeks to make sweeping changes to federal employment laws and focuses heavily on revamping the classification tests applicable to independent contractors.

Among other things, the bill seeks to adopt California's ABC test as part of most federal employment laws, creates a presumption that a worker is an employee absent clear and convincing evidence, expand joint employer tests to make an employer responsible for employees of contractors or subcontractors and expand the penalties for misclassification to between $10,000 and $30,000 per violation.

If contractor classification is widespread, the bill proposes penalties which could amount to 1% of an employer's profits.

In addition, with a new administration will come a change to the makeup of the National Labor Relations Board, whose presiding majority changes depending on which party is in the White House.

As a result, employers should expect a change to the standard utilized by the NLRB to determine whether workers are correctly classified as employees.

In 2019, the Republican-majority NLRB found that in determining whether a worker is classified as an independent contractor or employee, the focus should be on whether the arrangement between the employer and the alleged employee provided an entrepreneurial opportunity to the individual.[3]

In other words, the NLRB accepted the potential for entrepreneurial opportunity as a key factor in its analysis.

The NLRB general counsel's division of advice subsequently issued an advice memo finding that drivers contracting for Uber Technologies Inc. were correctly classified as independent contractors under the NLRA.[4]

These decisions overruled the more-restrictive test enunciated by the Obama-era NLRB in 2014 in FedEx Home Delivery,[5] which resulted in expanding the ability of workers to see the protections of the NLRA.

In FedEx Home Delivery, the board placed less emphasis on the potential for entrepreneurial activity, and instead focused more on whether the workers are "in fact, rendering services as part of an independent business."[6]

The board went on to note that while entrepreneurial opportunity was a factor that should be considered, it was only one of the many factors the board would consider in the analysis and that the board should consider the "actual, but not theoretical, entrepreneurial opportunity" and the actual control exercised over the worker.

The above NLRB tug of war and politicizing of such issues is a long established political power struggle solely dependent on which party controls the White House.

Employers should expect that the newly constituted NLRB will roll back the less-restrictive Trump-era independent contractor test and will return to the Obama-era approach.

However, the U.S. circuit courts, charged with reviewing NLRB decisions, may push back against the political flip-flop on such issues and narrow its deference to the NLRB's expertise — especially given the number of new federal judges appointed under Trump.

Biden has also suggested that under his administration, he intends to place additional restrictions on employers' ability to utilize independent contractors.[7]

In addition to his support for the PRO Act, Biden has further indicated that he supports establishing a federal independent contractor test, which is modeled on the ABC test and would apply to all labor, employment and tax laws.

Moreover, he has made it clear that he endorses legislation that makes worker misclassification a substantive violation of law under all federal labor, employment, and tax laws, and imposes additional penalties beyond those imposed for other violations. Biden also supports funding new labor and employment agencies to facilitate these efforts.

Given the narrow majority held by the Democrats in the House and the narrow majority either party will hold in the Senate depending on what happens in the Georgia United States Senate runoff election, it is certain that Biden's attempt to rework classification laws will require compromise in the year ahead.

Conclusion

Employers and workers hoping 2020 would finally bring clarity and uniformity to independent-contractor classification tests end the year with small victories in California but looming uncertainty as to what 2021 will bring.

This year guarantees to be a battleground year over contractor classification tests, the joint employer test and the power of organized labor. Hold on!

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[1] (2018) 4 Cal. 5th 903.

[2] Whether the PRO Act will pass in the Senate may heavily depend on the results of the Georgia United States Senate runoff election scheduled for January 5, 2021.

[3] SuperShuttle DFW, Inc. ,367 NLRB No. 75 (Jan. 25, 2019).

[4] See NLRB Advice Memorandum, April 16, 2019, Case Nos. 13-CA-163062, 14-CA-158833 and 29-CA-177483.

[5] 361 NLRB No. 55 (September 30, 2014).

[6] Id.

[7] https://joebiden.com/empowerworkers/ (last visited December 9, 2020).