

Alerts & Publications

California Lawmakers Send AB5 to Governor's Desk

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The California Legislature has passed legislation designed to make it much more difficult for companies—including but not limited to those in the “gig economy”—to treat workers as independent contractors. [Assembly Bill 5 \(AB5\)](#), first introduced in December 2018, codifies, extends, and puts certain parameters around the California Supreme Court’s opinion in *Dynamex Operations West, Inc. v. Superior Court (Lee)*, 4 Cal. 5th 903 (2018).¹ In that case, the court adopted a more rigid method of determining employee status under California’s Wage Orders than had previously applied. To justify independent contractor status under *Dynamex*, an alleged employer must establish **each** of the following three factors under the so-called “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; (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. If signed into law, AB5 could result in the reclassification of a substantial number of workers under state law.

AB5’s Current Status

The bill passed in a 29-to-11 vote along party lines in the State Senate on September 10, 2019, and in a 61-to-16 vote in the State Assembly the following day. It next heads to Governor Gavin Newsom—who endorsed the bill on Labor Day—for signature. Governor Newsom has told *The Wall Street Journal* that he is still engaged in talks with Uber, Lyft, and other gig economy companies about the bill. Additionally, Uber, Lyft, and DoorDash have collectively contributed \$90 million in support of a state ballot initiative intended to preserve the independent contractor status of their workers while offering protections and benefits to their contractors, including a minimum earnings floor and access to health care plans. If signed by Governor Newsom, the bill will go into effect on January 1, 2020.

Bill Content Overview

A. ABC Test

AB5 adopts the ABC test outlined in *Dynamex* verbatim and expands its reach, for most industries, beyond the Industrial Welfare Commission Wage Orders to the California Labor Code and Unemployment Insurance Code as well. The legislation's stated intention is to "ensure workers who are currently exploited by being classified as independent contractors instead of recognized as employees have the basic rights and protections they deserve under the law, including a minimum wage, workers' compensation if they are injured on the job, unemployment insurance, paid sick leave, and paid family leave."

B. Exemptions

AB5 creates a number of exemptions for certain occupations, industries, and relationships. To the extent an exemption applies, in most circumstances, the pre-*Dynamex* multifactor *Borello* test will continue to apply (rather than the ABC test). Under the *Borello* rule—based on the California Supreme Court decision *S.G. Borello & Sons, Inc. v. Department of Industrial Relations*, 48 Cal. 3d 342 (1989)—courts focus on whether a company has the right to control the manner and means by which the worker performs work. They also take into account secondary factors such as whether the company had the right to hire/fire the worker, whether the company or the worker provided the tools and instrumentalities necessary for work, and the degree of skill required to perform the work.

AB5 lists several specific occupations to which the traditional *Borello* test will continue to apply, including: insurance brokers; physicians, surgeons, dentists, podiatrists, psychologists, or veterinarians; lawyers, architects, engineers, private investigators, and accountants who hold an active license from the State; securities broker-dealers, investment advisors, and their agents; direct sales salespersons as described in Section 650 of the Unemployment Insurance Code; and commercial fishermen. Certain contracts for "professional services" are also exempted, so long as they meet certain enumerated requirements, such as maintaining a business location and setting or negotiating their own rates. "Professional services" are defined as: marketing (provided the work is "original and creative in character"); administrator of human resources; travel agent services; graphic design; grant artist; fine artist; services by an enrolled agent who is licensed by the US Treasury Department to practice before the IRS; services by a still photographer or photojournalist; services by a freelance writer, editor, or newspaper cartoonist; and services by a licensed esthetician, electrologist, manicurist, barber, or cosmetologist. Several exemptions contain precise requirements that must be met in order for the exemption to be applicable.

The bill also contains several other miscellaneous exemptions, including for: real estate licensees; repossession agencies; the construction industry; and relationships between referral agencies and service providers. Several of these exemptions will apply if certain specific enumerated criteria are met, which vary from exemption to exemption. Interestingly, there is also a general "business to business" exemption. The exemption specifically recognizes that sole proprietorships can qualify, but states that the exemption is limited to

“bona fide” business to business relationships. To qualify as a bona fide relationship, the relationship must satisfy 12 separate criteria. For example, the relationship must be governed by a written agreement, the business providing the service must similarly provide services to other businesses (aside from the alleged employer), and the business must provide services directly to the other business (as opposed to providing services to the other business’ customers). Conversely, AB5 also contains a provision stating that “[n]o provision of this measure shall permit an employer to reclassify an individual who was an employee on January 1, 2019, to an independent contractor due to this measure’s enactment.”

Since AB5 will be codified in the Labor Code, violations of its provisions will presumably be actionable under the Labor Code Private Attorney Generals Act, Labor Code §§ 2698 *et seq.* AB5 also provides that claims for injunctive relief to prevent misclassification may be initiated by the Attorney General of California, or by various city attorneys.

Finally, AB5 contains a savings clause that states that if its ABC test is found by a court to be inapplicable in a particular context, the traditional *Borello* test should apply. Presumably this provision is intended to cover situations where the ABC test may be preempted—for example, under the Federal Aviation Administration Authorization Act, 49 U.S.C. § 14501(c)(1).

Takeaways

AB5 is a complicated law, the full scope of which is beyond this alert. That said, assuming that AB5 is signed into law in its current form, companies in California should keep the following in mind:

- Under AB5, virtually any independent contractor relationship—no matter how well-intended or generally accepted—could be invalidated, resulting in significant exposure. Companies should review all independent contractor relationships and ensure that an exception applies or that the ABC test can be satisfied.
- Do not assume that an independent contractor relationship will be protected by an exemption for a particular industry or profession, because many of AB5’s exemptions are subject to lengthy requirements and restrictions. To take just one example, it appears to be impossible to have a bona fide business-to-business independent contractor relationship without a written agreement.
- The ABC test itself, and many of the qualifying criteria for AB5’s exemptions, are conjunctive in nature. This means that if one part of the ABC test is not met, or if one criteria for an exemption is not satisfied, then the contractor may be misclassified. This is very different than the traditional *Borello* test, where no one factor is truly dispositive.
- Keep in mind that AB5’s effective date is January 1, 2020, which provides a short timeline for compliance. In addition, AB5 expressly states that its codification of the ABC test “does not constitute a change

in, but is declaratory of, existing law with regard to wage orders of the Industrial Welfare Commission and violations of the Labor Code relating to wage orders.”

If you have any questions regarding AB5 or how it may impact your company's policies or practices, please contact the authors of this alert or your O'Melveny advisor.

¹ Our client alert on the *Dynamex* decision can be found [here](#).

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