



Bill Analysis

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Bill Number: AB 2257

SUBJECT

Employee Classification-Employees and Independent Contractors

SUMMARY

This bill would exempt additional occupations and business relationships from the presumption that a worker is an employee unless certain conditions are met.

This bill would also recast the Labor Code section. Specifically, the bill would repeal section 2750.3 of the Labor Code related to determining if a worker is an employee or independent contractor under the "ABC" test and add Article 1.5 (commencing with section 2775) to Chapter 2 of Division 3 of the Labor Code to revise and recast these provisions.

The bill would also amend the Revenue and Taxation Code (R&TC) to add definitions of "employee" to specific parts of the R&TC by reference to the Labor Code.

REASON FOR THE BILL

The reason for the bill is to modify exemptions for certain services and provide new exemptions for specific occupations from the presumption that a worker is an employee unless specified criteria are met.

ANALYSIS

This bill would revise and recast provisions of the Labor code relating to worker status and recast and clarify the bona fide business-to-business contracting relationship, referral agency and professional services exemption.

Bona fide Business-to-Business Contracting Relationship

This bill clarifies that when two bona fide businesses are contracting with one another, the determination of whether an individual working for a business service provider is an employee is governed by the test set forth in the California Supreme Court's decision of *S.G. Borello & Sons, Inc. v. Department of Industrial Relations* (1989) 48 Cal.3d 341 (*Borello*) if certain criteria are met.

The determination of whether an individual worker who is not acting as a sole proprietor or formed as a business entity, is an employee or independent contractor is governed by the "ABC" test.

The "ABC" test was adopted in *Dynamex Operations W. v. Superior Court* (2018) 4 Cal.5th 903 (*Dynamex*) and required a hiring entity to demonstrate that all of the following conditions are satisfied for a worker to be considered an independent contractor:

- A. The person 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 person performs work that is outside the usual course of the hiring entity's business.
- C. The person is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed.

Relationship between Referral Agency and a Service Provider

If a sole proprietor, or business entity formed as a partnership, limited liability company (LLC), limited liability partnership (LLP), or corporation (service provider) provides services through a referral agency, the determination of whether the service provider is an employee or independent contractor of the referral agency is generally governed by *Borello* if the referral agency meets certain conditions.

This bill also expands and defines the type of services qualifying under this exemption to include but not limited to tutors, youth sports coaching, interpreting services, consulting and animal services.

Contract for Professional Services

For a contract for professional services, the determination of whether the individual is an employee or independent contractor is governed by *Borello* if the hiring entity demonstrates certain factors are met.

This bill also added the following occupations to the professional services exemption: advisor, producer, narrator, cartographer, a specialized performer hired by a performing arts company to teach a master class for no more than one week, appraiser, registered professional foresters, and a home inspector.

Relationship between Two individuals/Single-Engagement Event

The relationship between two individuals where each is acting as a sole proprietor or separate business entity, formed as a partnership, a LLC, a LLP, or a corporation, pursuant to a contract to provide services at the location of a single engagement event is governed by *Borello* if certain conditions are met.

This bill also defines single engagement event as a stand-alone non-recurring event in a single location, or a series of events in the same location no more than once a week.

This bill clarifies that qualifying services for this exemption do not include those services provided in an industry designated by the Division of Occupational Safety and Health or the Department of Industrial Relations as a high hazard industry, or janitorial, delivery, courier, transportation, trucking, agricultural labor, retail, logging, in-home care, on construction services other than minor home repair.

Individual Performance Artist

The determination of employee or independent contractor status is governed by *Borello* for individual performance artist performing material that is their original work, creative in character, and the result of which depends on the individual's imagination, invention or talent if certain requirements are met.

This bill defines individual performance artists to include, but not limited to improvisation, stage magic, performing comedy, illusion, mime, spoken word, storytelling or puppetry.

Individuals participating in a theatrical production, musician or musical are subject to the "ABC" test.

Data Aggregator

The holding in *Dynamex* does not apply to the relationship between a data aggregator and the individual providing feedback to the data aggregator and instead, the holding in *Borello* applies if certain conditions are met.

This bill also defines a data aggregator as a business, research institution, or organization that request and gathers feedback on user interface, products, services, people, concepts, ideas, offerings or experiences.

Minimum wage is defined as the greater of the local or state minimum wage.

Other Occupations

This bill was amended to exempt additional occupations which includes:

- A manufactured housing salesperson;
- A newspaper distributor working under contract with a newspaper publisher and a newspaper carrier working under contract with either a newspaper publisher or distributor (This subdivision becomes inoperative on January 1, 2021 unless extended by the Legislature);
- An individual engaged by an international exchange visitor program that has obtained and maintains full official designation by the United States Department of State; and
- A competition judge with a specialized skill set or expertise that exercises discretion and independent judgment in determining the outcome or enforcing rules of a competition. This includes but is not limited to an amateur umpire or referee.

This bill also added a severability clause.

The Labor Code Provisions Made Applicable To Select Revenue and Taxation Code Provisions

This bill would amend sections 17020.12 and 23045.6 of the R&TC and adds sections 18406 and 61001 to the R&TC to provide that the provisions of Article 1.5 (commencing with section 2775) to Chapter 2 of Division 3 of the Labor Code will govern the determination of whether an individual is an employer for the purposes of Part 10, Part 10.3, Part 10.5, and Part 11 of the R&TC.

The bill also includes an urgency clause.

Effective/Operative Date

As an urgency measure, this bill would be effective immediately upon enactment, and would apply for work performed on or after January 1, 2020, unless the application of the provisions would relieve an employer from liability, then those provisions would be applied retroactively to existing claims and actions to the maximum extent permitted by law.

Federal/State Law

Federal Law

To determine whether a worker should be classified as an employee or independent contractor, federal law applies a two factor test, the Control and Relationship Test.

Control. Behavioral control is exerted if the business controls what work is accomplished and directs how it is done. Financial control is exerted if the business directs or controls financial and certain relevant aspects of a worker's job. Some of the factors to consider include:

- The extent of the worker's investment in the facilities or tools used in performing services and the extent to which the worker makes his or her services available to the relevant market.
- How the business pays the worker, and the extent to which the worker can realize a profit or incur a loss.

Relationship. It is also important in determining the worker's classification to understand how the employer and worker perceive their relationship. Items to consider include:

- The extent to which services performed by the worker are a key aspect of the regular business of the company and if the worker has unreimbursed business expenses.
- Written contracts describing the relationship the worker and company intended to create.
- Whether the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation or sick pay and the permanency of the relationship.

State Law

AB 5 was signed by Governor Newsom on September 18, 2019, which, among other things, added Section 2750.3 to the Labor Code.

AB 170 was also signed by Governor Newsom on October 2, 2019, which amended section 2750.3, as it was added by AB 5, to include a temporary exemption for newspaper distributors and newspaper carriers from the presumption that a worker is an employee unless the "ABC" test is met.

Section 2750.3 of the Labor Code provides under the Labor Code, Unemployment Insurance Code, and for the purpose of wage orders of the Industrial Welfare Commission, except for specified statutory exemptions, a person providing labor or services for remuneration will be considered an employee unless the hiring entity satisfies the "ABC" test adopted in *Dynamex*.

Existing law exempts specified business relations and occupations from the application of the holding in *Dynamex* and the presumption that a worker is an employee unless the hiring entity demonstrated the "ABC" test, and instead provides that these exempt relationships and occupations are governed by the test adopted in *Borello*, specified provisions in the Business and Professions Code, the Unemployment Insurance Code, and the Labor Code, or a combination of these.

***Borello*:**

The California Supreme Court, in *Borello*, adopted the "economic realities" test. In applying this test, a significant factor to be considered is whether the person to whom service is rendered has the right to control the manner and means of the work performed.

Additional factors that may be considered under this test include:

1. Whether the person performing services is engaged in an occupation or business distinct from that of the principal;
2. Whether or not the work is a part of the regular business of the principal or alleged employer;
3. Whether the principal or the worker supplies the instrumentalities, tools, and the place for the person doing the work;
4. The alleged employee's investment in the equipment or materials required by his or her task or his or her employment of helpers;
5. Whether the service rendered requires a special skill;
6. The kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the principal or by a specialist without supervision;
7. The alleged employee's opportunity for profit or loss depending on his or her managerial skill;
8. The length of time for which the services are to be performed;
9. The degree of permanence of the working relationship;
10. The method of payment, whether by time or by the job; and
11. Whether or not the parties believe they are creating an employer-employee relationship may have some bearing on the question, but is not determinative since this is a question of law based on objective tests.

However, all of the factors must be considered in light of the facts and circumstances surrounding the worker's relationship with the hiring entity and no one factor is given more weight than another.

Implementation Considerations

None noted.

Technical Considerations

The amendment to R&TC section 17020.12 does not contain the correct reference to the Labor Code. It currently references "Section 1 of Article 1.5 of the Labor Code"; however, the correct code reference intended is "Article 1.5 (commencing with Section 2775) of Chapter 2 of Division 3 of the Labor Code." This incorrect cross-reference will not materially impact the implementation of this bill.

LEGISLATIVE HISTORY

AB 5 (Gonzalez, 2019/2020, Chapter 296, Statutes of 2019) created a presumption that a person providing labor or services for remuneration will be considered an employee rather than an independent contractor unless the hiring entity demonstrates that the "ABC" test provided for in the holding of *Dynamex* and in Labor Code section 2750.3 is satisfied.

AB 170 (Gonzalez, 2019/2020, Chapter 415, Statutes of 2019) amended Labor Code section 2750.3 as added by AB 5 to exempt newspaper distributors and carriers until January 1, 2021, from the "ABC" test adopted in *Dynamex*. This bill's operation was contingent on the enactment of AB 5.

AB 323 (Rubio, 2019/2020) would extend the exemption for newspaper distributors or carriers to January 1, 2022. It would also require the Department of General Services to issue a public report on its website beginning July 1, 2021. As of August 31, 2020, the bill status is in engrossing and enrolling.

AB 1850 (Gonzalez, 2019/2020), would exempt additional occupations and business relationships from the presumption under Labor Code section 2750.3 that a worker is an employee unless certain conditions are met. It would recast the exemption for referral agencies. It would also add specialized performers hired by a performing arts company or organization to teach a master class, real estate appraisers, videographers and photo editors to the professional services exemption. This law would also exempt certain individuals in the music industry, insurance inspectors and competition judges. As of September 3, 2020, this bill is in the Senate Labor, Public Employment & Retirement Committee.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This bill as amended on August 25, 2020, does not generally change the way income or franchise tax is calculated under the R&TC. However, it could change the amount of income and expenses reported to the Franchise Tax Board and would have an unknown impact on general fund revenue.

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

Revenue Discussion

This bill could result in some workers who are currently treated as employees being reclassified as independent contractors under the proposed exclusion. This reclassification would shift responsibility for a number of business related expenses from businesses to the workers. An increase of qualified business expenses to the workers would likely decrease their tax liability, while the decrease in expenses to businesses would increase their tax liability. The net effect of these changes would depend on the marginal tax rates of the businesses and workers involved, and any adjustment that may take place in compensation levels or related business expenses. The net effect of all these changes on tax liability is not known.

LEGAL IMPACT

None noted.

APPOINTMENTS

None.

VOTES

Location	Date	Yes Votes	No Votes
Concurrence	August 31, 2020	74	0
Senate Floor	August 31, 2020	39	0
Assembly Floor	June 11, 2020	77	0

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