



## Bill Analysis

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Sponsor:

Bill Number: AB 25

Related Bills: See Legislative  
History

Introduced: December 7,  
2020

### SUBJECT

Worker Classification: Employees and Independent Contractors

### SUMMARY

This bill would make changes to the California Labor Code for the determination of worker classification as an employee or independent contractor.

This bill would replace the application of the 3-part test, commonly known as the "ABC" test as provided for in Article 1.5 (commencing with section 2775) of Chapter 2 of Division 3 of the Labor Code with the multifactor test decided in *S. G. Borello & Sons, Inc. v. Department of Industrial Relations* (1989) 48 Cal.3d 341 (*Borello*) for the determination of the worker classification as an employee or independent contractor.

### RECOMMENDATION

No position.

### SUMMARY OF AMENDMENTS

Not Applicable.

### REASON FOR THE BILL

To restore the multi-factor test from *Borello* as the standard for evaluating a worker's status as an employee or independent contractor so that many workers who are treated as employees under current law would be treated as independent contractors.

### ANALYSIS

This bill would add Labor Code section 2750.7, which would adopt the multi-factor test provided in *Borello* as the test to determine if a person is an employee or independent contractor:

- Whether the one performing services is engaged in a distinct occupation or business;

- 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;
- The skill required in the particular occupation;
- Whether the principal or the worker supplies the instrumentalities, tools, and the place of work for the person doing the work;
- The length of time for which the services are to be performed;
- The method of payment, whether by the time or by the job;
- Whether or not the work is a part of the regular business of the principal; and
- Whether or not the parties believe they are creating the relationship of employer-employee.

This bill would also amend Section 2750.5 of the Labor Code to remove the "ABC" test factors required to be met as proof of independent contractor status for workers performing services for which a contractor's license is required.

This bill would also repeal sections 2775-2787 of the Labor Code, which states that a person providing labor or services for remuneration is an employee unless the hiring entity demonstrates that the "ABC" test is satisfied, and made certain professions and professional relationships exempt from the "ABC" test.

#### *Effective/Operative Date*

If enacted, this bill would be effective and operative on January 1, 2022.

#### *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*

Under Article 1.5 (commencing with section 2775) of Chapter 2 of Division 3 of the Labor Code provides that a person providing labor or services for remuneration shall be considered an employee rather than an independent contractor unless the hiring entity demonstrates that the "ABC" test is satisfied:

- 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.

This article also provides exemptions from this rule for certain professions and professional relationships.

Under the Revenue and Taxation Code (R&TC), the provisions of Article 1.5 (commencing with section 2775) of Chapter 2 of Division 3 of the Labor Code govern the determination of whether an individual is an employee for the purposes of Part 10, Part 10.2, Part 10.7, Part 11, and Part 32 of the R&TC.

### *Implementation Considerations*

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

If enacted, AB 25 would repeal Article 1.5 (commencing with section 2775) of Chapter 2 of Division 3 of Labor Code, rendering cross references in R&TC sections 17020.12, 18406, 21003.5, 23045.6, and 61001 inaccurate. It is recommended to amend the bill to address whether the new provisions would apply for purposes of California's income tax laws.

#### *Technical Considerations*

None noted.

#### *Policy Concerns*

None noted.

### **LEGISLATIVE HISTORY**

Proposition 22 - On November 3, 2020, California voters approved ballot initiative in Proposition 22. Proposition 22 classifies app-based drivers as independent contractors.

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 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. This bill's operation was contingent on the enactment of AB 5.

AB 323 (Rubio, 2019/2020, Chapter 341, Statutes of 2020) amended Section 2750.3 of the Labor Code to modify the exemption related to newspaper distributors and carriers. AB 323 included double-jointing language with AB 2577.

AB 2257 (Gonzalez, 2019/2020, Chapter 38, Statutes of 2020) - Governor Newsom signed AB 2257 on September 4, 2020, which repealed section 2750.3, and added Sections 2775 – 2787 (collectively referred to as Article 1.5) of the Labor Code. The new law provided exemptions for specified business relations and occupations from the application of the holding in *Dynamex* and instead provided that most of these exempt relationships and occupations are governed by the tests adopted in *Borello*. This bill also amended R&TC sections 17020.12, 23045.6, and 61001 and added R&TC sections 18406 and 21003.5 with references to Article 1.5 (commencing with section 2775) of Chapter 2 of Division 3 of the Labor Code relating to the determination of employee status for the purposes of specified parts of the R&TC.

## **PROGRAM BACKGROUND**

None noted.

## **FISCAL IMPACT**

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

## **ECONOMIC IMPACT**

### *Revenue Estimate*

This bill as introduced on December 7, 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 FTB 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. 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 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 noted.

## **SUPPORT/OPPOSITION**

To be determined.

## **ARGUMENTS**

To be determined.

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**LEGISLATIVE CONTACT**

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