

The Complete Guide to Navigating Freelancer Laws

Like California's Assembly Bill 5



Overview and Assessment of the Impact of the California AB-5 Bill

Employers who use independent contractors in California and other states need to evaluate and potentially adjust how they analyze independent contractor status. California has a new law codifying a worker classification test for independent contractors that was first introduced in the state in 2018 in an opinion issued by the California Supreme Court, commonly referred to as Dynamex.

On September 18, 2019, Assembly Bill 5 (AB- 5) was signed into law by California Governor Gavin Newsom. AB- 5 becomes effective on January 1, 2020 not leaving employers much time to assess the impact of this law on their operations.

The law adopts a three-part (ABC) test to determine whether a worker is an employee. According to California's version of the ABC test, a worker is considered an employee unless the hiring entity established all of the following factors:

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

Under AB-5, a worker is presumed to be an employee unless all three factors of the ABC test are met.

AB-5 extends the application of the ABC test to apply to claims under California's Labor and Unemployment Insurance Codes in addition to claims arising from California's Wage Orders. AB-5 also creates expanded enforcement powers for California's Attorney General and city attorneys of large cities as they may file lawsuits to prevent businesses from misclassifying independent contractors.

The ABC test replaces a previously used flexible multi-factor test, commonly referred to as the Borello test after a California Supreme Court decision issued in 1989. The Borello test focused on the primary consideration of whether the worker had control over the work done, the manner it was done, and the means in which it was performed, and also included consideration of many secondary factors in order to determine whether a worker should be classified as an employee or as an independent contractor.

The secondary factors included:

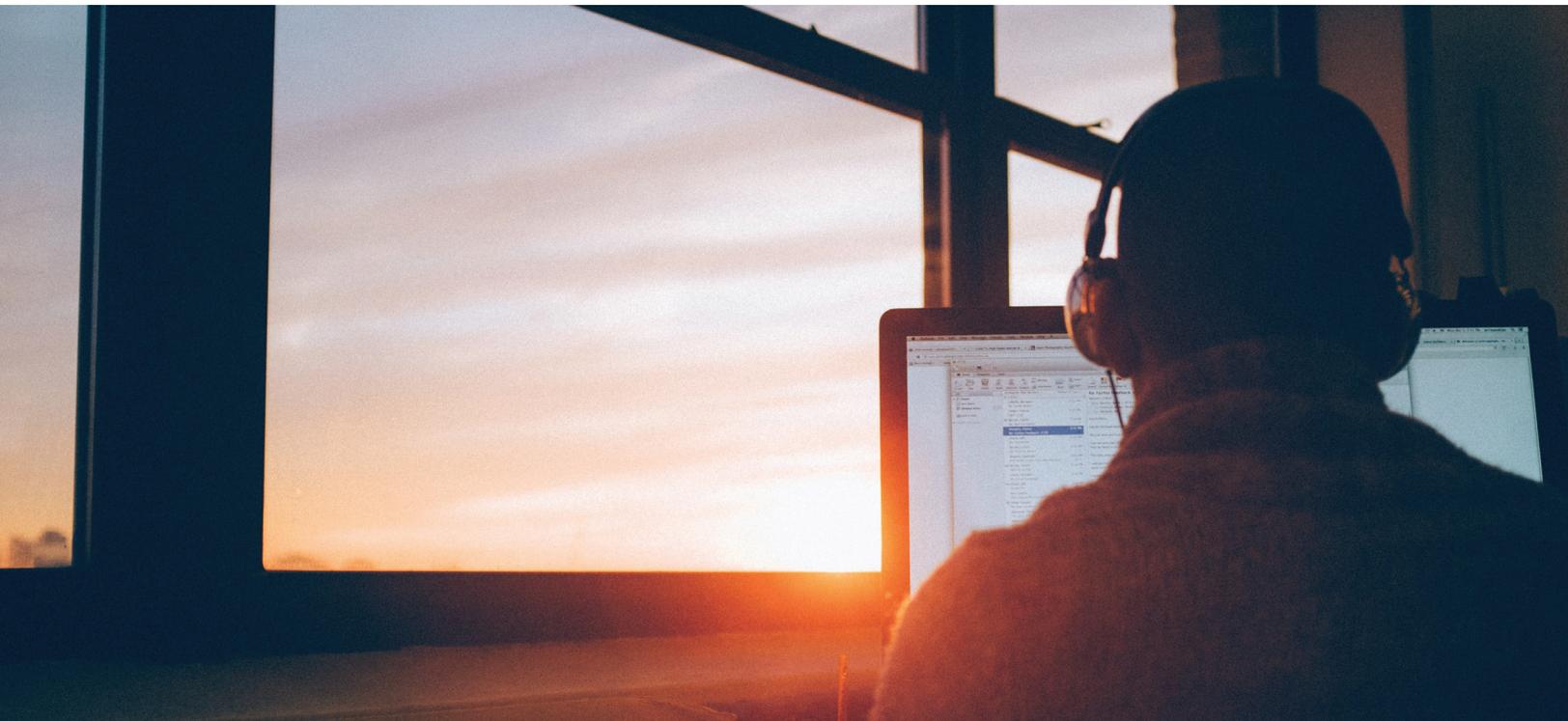
1. Whether the person performing services is engaged in an occupation or business distinct from that of the principal;
2. Whether or not the work is a part of the regular business of the principal or alleged employer;
3. Whether the principal or the worker supplies the instrumentalities, tools, and the 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.

Under Borello, the “principal question is whether the person [or company] to whom service is rendered has the rights to control the manner and means of accomplishing the result desired.” AB-5, however, includes several exemptions for certain workers and situations. Exemptions will need to be evaluated under the old Borello test instead of the ABC test. For example, if an exemption applies, a worker may still claim misclassification based on Borello instead of the new California ABC test.

Exemptions for specific occupations, include licensed insurance agents, certain health care professionals, registered securities broker-dealers or investment advisers, direct sales salespersons, real estate licensees, commercial fishermen, barbers and cosmetologists; and certain professionals including attorneys, architects, engineers, investigators and accountants, among others.

AB-5 also includes a limit on the number of assignments (35 annually) that freelance writers and photographers may do per media outlet before being considered an employee. There also is a business-to-business exemption that applies to “business service providers” that contract to provide services to another business and who are able to meet each prong of a 12-part test. It is important to note that this list is not exhaustive and hiring entities should check the exact language of the statute and consult with experienced counsel to see if an exemption applies to their particular situation.

It is possible that the list of exemptions will grow as different industry groups continue to lobby for an exemption. Gig economy companies Uber, Lyft, and DoorDash, announced an initiative to add a ballot measure to preserve the ability of drivers who use their technology to be considered independent contractors. Under the Project App-Based Drivers & Services Act, drivers would be classified as independent contractors under California law, but also be eligible for additional benefits. In order to earn a place on the November 2020 election ballot, supporters need to collect 650,000 signatures by June 2020.



According to Jens Audenaert, General Manager, WorkMarket, an AD P Company, "The passing of AB-5 does not mean that companies can no longer use freelance labor. We continue to see organizations of all sizes increase their use of freelance labor as they adapt to the evolving workforce. What laws like AB5 do mean, is that companies will need to be more thoughtful and deliberate around their processes as they engage with independent contractors, so the organization understands who it's engaging with, and how. A Freelance Management System is a technology-based approach that is designed to keep organizations safe with respect to compliance, by providing a comprehensive automated platform and audit trail."

The below chart serves as a quick reminder of some key differences between employees and independent contractors and freelancers. It is not to be used as legal advice nor is it all encompassing.

W-2 EMPLOYEE	1099 CONTRACTOR
When, how, and where an employee works is controlled by th employer.	Retains control over when, how, and where he/she works.
Entitled to minimum wage, overtime pay, vacation, sick days, holidays, paid leave.	Not entitled to traditional employee benefits.
Salary deductions, remittances, and severance are the responsibility of the employer.	Does not have taxes withheld, collected or paid by the employer.
Can be classified as indefinite or fixed term.	Does not require notice of severance from the employer.
	Can contract with other companies at the same time.



What You Need to Do to Prepare Your Organization for AB-5 (and Beyond)

The risks of worker misclassification are high, but employers can take steps to make sure their organization is compliant. Worker misclassification means classifying workers as 1099 independent contractors when they should be classified as W-2 employees.

Independent contractor (IC) misclassification risks include wage and hour risks, including minimum wage and overtime, federal and state tax liability, claims for benefits, immigration compliance risks, and for companies who rely heavily on independent contractors, the potential for class action claims.

Organizations who use independent contractors should put in place some risk reduction strategies. While all businesses, across all segments, should be aware of, and compliant with, applicable laws and regulations, organizations using ICs in California may need to take some additional steps first, in light of AB-5. Basically, they will need to check whether contractors continue to qualify as such under the new California ABC test, and consider establishing or revising formal policies and practices to minimize risk. Companies should check whether any AB-5 exemptions apply to their workforce.

All companies, whether or not they use independent contractors in California, must understand how they are engaging and paying workers. Given the increase in misclassification laws, organizations should consider the following:



Consult with appropriate legal and human resource professionals for assistance



Create a systematic process for evaluating worker classification



Avoid engaging ICs that provide services that are integral to the organization's normal course of business, or to augment current staff



Avoid exercising control over independent contractors



Verify that independent contractors are operating as an independent business



Monitor for applicable changes to laws and regulations (i.e., many state laws feature some variation of the tests discussed above, and the laws in this area are expected to continue to evolve over time.)

Finally, all companies should carefully review existing independent contractor relationships and agreements.

In addition, employers should consider using a Freelance Management System (FMS) to automate key aspects of your organization's contractor management activities, so you and your business are empowered with the ability to instantly track and report your worker engagements. An organization that does not have its contractor data and information readily available will certainly place itself at greater risk than one that does. But, that's only the half of it – the issue of classification will generally be paramount in the business's ability to protect itself in the case of alleged noncompliance.

In summary, you can prepare your organization for any of the potential ramifications of regulatory compliance, whether directly associated with California AB-5, or just in general, by leveraging technology as solutions such as an FMS. The two key assets that you will have at your disposal through an FMS are:

1. The complete automation of all of your Contractor Management activities, and
2. A comprehensive Audit Trail that can provide you with all of the supportive data and information you will need should you be faced with a regulatory audit.

What to Read Next

To learn about the ADP solution through the WorkMarket FMS, take a look at the [Why Working With an FMS Solution Provider is Essential](#).

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