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CONTRIBUTORS

SAN FRANCISCO

Lloyd W. Aubry, Jr., Editor
laubry@mofo.com

Karen J. Kubin
kkubin@mofo.com

Eric A. Tate
etate@mofo.com

PALO ALTO

Christine E. Lyon
clyon@mofo.com

Tom E. Wilson
twilson@mofo.com

LOS ANGELES

Tritia M. Murata
tmurata@mofo.com

Janie F. Schulman
jschulman@mofo.com

Timothy F. Ryan
tryan@mofo.com

NEW YORK

Miriam H. Wugmeister
mwugmeister@mofo.com

LONDON

Annabel Gillham
agillham@mofo.com

BERLIN

Hanno Timner
htimner@mofo.com

BEIJING

Paul D. McKenzie
pmckenzie@mofo.com

HONG KONG

Stephen Birkett
sbirkett@mofo.com

TOKYO

Mitsuyoshi Saito
msaito@mofo.com

DYNAMEX V. SUPERIOR COURT: CALIFORNIA SUPREME COURT CLARIFIES STANDARD FOR INDEPENDENT CONTRACTOR CLASSIFICATION UNDER CALIFORNIA WAGE ORDERS

By Tritia M. Murata

On April 30, 2018, the California Supreme Court issued its highly anticipated opinion in *Dynamex Operations West, Inc. v. Superior Court*, clarifying the standard that applies to determine whether a worker is properly classified as an independent contractor for purposes of the Industrial Welfare Commission (IWC) wage orders.[1] *Dynamex* rejects application of the multi-factor test set forth in *S.G. Borello & Sons, Inc. v. Department of Industrial Relations*,[2] and instead adopts a three-part "ABC test" for evaluating whether a worker is an independent contractor or an employee covered by the wage orders. Unless the

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hiring company establishes all three requirements of the ABC test, the worker is an employee.

The first requirement of *Dynamex*'s ABC test (that the worker must be free from the hiring company's control and direction in connection with the performance of the work, both under the contract and in fact) aligns with the common law "right to control" standard and is not a novel concept. However, the second requirement (that the worker *must* perform work that is outside the company's business) and the third requirement (that the worker *must* be customarily engaged in an independently established trade, occupation, or business of the same nature as the work being performed for the company) will make it more difficult for businesses to classify workers as independent contractors in California.

BACKGROUND

Dynamex provides on-demand pick-up and delivery services to individual and business customers. Before 2004, Dynamex classified its California drivers as employees. In 2004, Dynamex converted its drivers to independent contractors after determining the conversion would be economically advantageous.

The plaintiffs are former drivers who had independent contractor agreements with Dynamex to provide delivery services. In their putative wage and hour class action lawsuit, the plaintiffs alleged Dynamex misclassified its California drivers as independent contractors and violated various provisions of the Labor Code and wage orders as a result.[3]

Dynamex obtains its own customers and sets the rates to be charged to customers for deliveries. Generally, Dynamex drivers are expected to wear Dynamex shirts and badges when making deliveries, and they are sometimes required to attach a customer's decals to their vehicle if making a delivery on behalf of a Dynamex customer. Dynamex drivers are generally free to set their own schedules, but they need to notify Dynamex of the days they intend to work. Drivers are assigned deliveries at Dynamex's sole discretion and must complete all deliveries on the date assigned. Typically, drivers are hired for an indefinite period of time, with Dynamex reserving the right to terminate the agreement without cause, with three days' notice.[4]

Dynamex drivers are permitted to hire other individuals to make deliveries that Dynamex assigns. Drivers are also free to make deliveries for other delivery companies or on their own behalf, when not making deliveries for Dynamex. Drivers use their own vehicles to make deliveries and are generally free to determine the routes they take and the sequence in which they make deliveries, unless a customer requires otherwise. Dynamex negotiates driver compensation on an individual basis, and the amounts and manner in which drivers are paid varies from driver to driver.[5]

The trial court certified a modified class of Dynamex drivers who were classified as independent contractors, who used their personally owned or leased vehicles that weigh less than 26,000 pounds (Basic Class C License), and who had timely returned a questionnaire sent by the parties. The class specifically excluded (1) drivers for any pay period in which the driver provided services to Dynamex as either an employee or subcontractor of another person or entity or through the driver's own employees or subcontractors, and (2) drivers who provided services concurrently for Dynamex and for another delivery company that did not have a relationship with Dynamex or for the driver's own personal delivery customers.[6]

In granting the plaintiffs' motion for class certification, the trial court noted that the parties disagreed regarding the proper legal standard for determining whether a worker is an employee or an independent contractor for purposes of the wage orders. Dynamex argued for the application of the *Borello* factors. The plaintiffs argued that the trial court should apply the broad definition of "employ" articulated in *Martinez v. Combs*,[7] a case assessing whether an entity that had a relationship with a primary employer was a joint employer under the wage orders. The trial court agreed with the plaintiffs.[8]

Dynamex petitioned to the Court of Appeal for a writ of mandate. The Court of Appeal denied the writ petition in part, concluding that the trial court had properly relied upon the *Martinez* standard with respect to plaintiffs' claims that fell within the scope of the applicable wage order. The Court of Appeal also granted the writ petition in part, finding that the *Borello* standard properly applied to claims falling outside the scope of the wage order. Dynamex petitioned the California Supreme Court for review.[9]

THE CALIFORNIA SUPREME COURT'S DECISION

The California Supreme Court granted review to consider whether, in a wage and hour class action involving claims that the plaintiffs were misclassified as independent contractors, a class can be certified based on the IWC definition of "employ" as construed in *Martinez*, or whether the common law *Borello* test controls.

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The 82-page unanimous opinion authored by Chief Justice Tani Cantil-Sakauye meticulously reviews the relevant IWC wage order provisions (which define "employ" as meaning "to engage, suffer, or permit to work") and decades of history of the key California cases evaluating independent contractor classification, including pre-*Borello* cases, *Borello*, *Martinez*, and *Ayala v. Antelope Valley Newspapers, Inc.*[10]

Dynamex interprets *Borello* as "call[ing] for application of a statutory purpose standard" rather than embodying the common law test or standard for distinguishing employees and independent contractors in California.[11] The Supreme Court concluded that the statutory purpose of the wage orders was best served by adopting the ABC test, which it considered to be a "simpler, more structured test" for determining whether the "suffer or permit to work" standard has been met.[12] The Court viewed the ABC test as offering the advantages of avoiding uncertainty and unpredictability with respect to the classification of workers, and preventing abuse by entities seeking to evade responsibilities under the wage and hour laws.[13]

The ABC test has been applied in other jurisdictions, primarily (though not exclusively) in the unemployment insurance context.[14] Under the ABC test, the worker is presumed to be an employee, and the hiring entity bears the burden to establish that (A) the worker is free from the control and direction of the hirer in connection with the performance of the work, (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 for the hiring entity. Only where the hiring entity establishes all three of these factors will the worker be an independent contractor, rather than an employee, for purposes of the wage orders.[15]

The Supreme Court emphasized that its interpretation of the "suffer and permit to work" standard does not expand the reach of the wage orders to "the type of traditional independent contractor who has never been viewed as an employee of a hiring business and should not be interpreted to do so."[16] The Court agreed with Dynamex that the trial court's literal interpretation of the "suffer and permit to work" language of the wage orders was too broad and "could potentially encompass the type of traditional independent contractor — like an independent plumber or electrician — who could not reasonably have been viewed as the hiring business's employee."[17]

Notwithstanding, the Supreme Court concluded that under the B and C parts of the ABC test, the trial court did not abuse its discretion in determining that there was a well-defined community of interest sufficient to certify a class. Under part B of the test, the Court found common issues of fact and law predominated because the question of whether the work performed by the delivery drivers was within the scope of Dynamex's business is "clearly amenable to determination on a class basis" and "Dynamex's entire business is that of a delivery service."[18] Under part C, the Court determined that the question of whether the drivers in the certified class were "customarily engaged in an independently established trade, occupation, or business" was an issue that could be resolved on a class basis. Dynamex had reclassified its drivers from being employees to being independent contractors in 2004, and the certified class excluded drivers who performed delivery services for another delivery service or for their own personal customers, and who had employees of their own.[19] The Court suggested that in many cases, factors B and C are easier to determine and should be considered first.[20]

IMPLICATIONS FOR BUSINESSES IN CALIFORNIA

The *Dynamex* ruling has significant implications for all entities that engage independent contractors in California.

Businesses should carefully examine each of their independent contractor relationships and review the language of each of their independent contractor agreements to determine whether the relationships meet the ABC test articulated in *Dynamex*. Part A (whether the worker is free from the control and direction of the hiring entity, both under the contract and in fact) aligns with the common law "right to control" standard. Thus, many businesses will want to pay particular attention to parts B (whether the work performed is outside the hiring entity's business) and C (whether the worker is customarily engaged in an independently established trade, occupation, or business), which had previously been relevant considerations in assessing independent contractor status under *Borello*, but are now strict requirements under *Dynamex*.

In a footnote, *Dynamex* states there is "no question" that the "suffer and permit to work" standard is intended to cover joint employer relationships, where an entity has a relationship with a worker's primary employer, such as larger businesses that contract out some of their operations but retain substantial control over the work. However, *Dynamex* also makes clear that this does not mean that the larger business is prohibited from entering into subcontractor relationships or from obtaining benefits that may result from outsourcing certain services to a separate entity. So long as it is authorized by contract, the larger business can seek reimbursement for any such

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liability from the subcontractor.[21] Accordingly, in reviewing their independent contractor agreements, businesses should look closely at indemnification provisions, to ensure that they are appropriately protective.

While the *Dynamex* opinion may trigger a rise in wage and hour class actions alleging independent contractor misclassification, it is important to note that the decision is limited in subtle, but important, ways:

- The ABC test adopted in *Dynamex* applies only with respect to the IWC wage orders. The Supreme Court specifically declined to extend its reach to other contexts, including other provisions of the Labor Code that are not dependent on the wage orders, such as Labor Code section 2802.[22]

- Dynamex argued that both the "exercise control over wages, hours or working conditions" and "suffer and permit to work" standards articulated in *Martinez* are applicable only in determining whether an entity is a joint employer. Because it found that the "suffer and permit to work" standard applies to determine worker classification and supported the trial court's certification order, the Supreme Court specifically declined to consider whether the exercise of control over wages, hours, or working conditions applies outside the joint employer context.[23]

- The certified class in *Dynamex* contained several key exclusions that significantly narrowed the size and scope of the class and addressed issues that might otherwise have prevented certification. Even under the ABC test, a plaintiff seeking to certify an overly broad putative class of allegedly misclassified independent contractors might still not be able to establish the community of interest required for class certification, if individualized issues predominate each of the three parts of the test.[24]

Entities that engage independent contractors should consult with legal counsel to determine how the standard articulated in *Dynamex* will impact their businesses, and how best to implement any steps they may take in response.

Tritia M. Murata is a Litigation partner in the firm's Employment and Labor Practice Group in the Los Angeles office and can be reached at (213) 892-5765 or at tmurata@mofo.com.

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1 *Dynamex Operations West, Inc. v. Superior Court*, No. S222732 (Cal. Sup. Ct. Apr. 30, 2018).

2 *S.G. Borello & Sons, Inc. v. Department of Industrial Relations* (1989) 48 Cal.3d 341.

3 Slip Op., pp. 10-11.

4 Slip Op., pp. 8-9.

5 Slip Op., pp. 9-10.

6 Slip Op., pp. 11-12.

7 *Martinez v. Combs* (2010) 49 Cal.4th 35.

8 Slip Op., pp. 12-18.

9 Slip Op., p. 19.

10 *Ayala v. Antelope Valley Newspapers, Inc.* (2014) 59 Cal.4th 522.

11 See Slip Op., p. 33.

12 Slip Op., p. 64, 66.

13 Slip Op., pp. 62-63.

14 Slip Op., p. 65, fn. 23.

15 See Slip Op., pp. 7, 64, 66-67, 76-77.

16 Slip Op., pp. 77-78, fn. 32.

17 Slip Op., pp. 78-79.

18 Slip Op., p. 79.

19 Slip Op., pp. 69-76.

20 Slip Op., p. 76.

21 Slip Op., pp. 48-49, fn. 17.

22 Slip Op., pp. 3, 6, fn. 5.

23 Slip Op., p. 46.

24 Slip Op., pp. 11-12, 80-81.
