AB 5: New Requirements for Independent Contractors

Does Your Association Have Independent Contractors Providing Services?

If so, Assembly Bill 5 Will Further Impact the Ability of Companies Including Associations to Classify Workers as Independent Contractors.

What Are the New Laws?

You may have seen or heard the recent uproar in the news by Uber and Lyft over the so-called "gig worker bill." Unfortunately, this new bill will impact not just the "Gig Economy," but almost all California businesses including community associations and community management companies.

On September 18, 2019, California Governor Gavin Newson signed into law Assembly Bill 5 ("AB 5") to be incorporated into the California Labor Code beginning January 1, 2020, as Labor Code section 2750.3, with an amendment to the definition of "employee" in Labor Code section 3351 and other related amendments to the Unemployment Insurance Code at sections 606.5 and 621.

What is the Proper Classification of Individual Workers?

This new law essentially requires employers to comply with the California Supreme Court decision in *Dynamex* (*Dynamex Operations West, Inc. v. Superior Court of Los Angeles County* 4 Cal.5th 908 (2018)) concerning classification of workers as independent contractors rather than employees and creates statutory liability for not complying with these new limitations on worker classifications. AB 5 and the *Dynamex* case permit California hirers to classify individual workers as independent contractors only if it meets the ABC Test, which provides workers are employees unless: (A) the worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under contract and in actual fact; (B) whether 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 being performed for the hiring entity. AB 5 includes some exceptions for certain businesses or industries. However, there are no specific exceptions for community associations or community management companies.

What if There is a Bona Fide Business-to Business Relationship? Should Associations or Management Companies Be Worried?

Yes. AB 5 also provides guidance when there is a "bona fide business-to-business contracting relationship." AB 5 defines what is a legitimate "business-to-business contracting relationship" and sets forth further requirements to determine whether a "business service provider" is a properly classified independent contractor (e.g., janitorial services, etc.).

- First, the two parties contracting must both be "business service providers" which are either a business entity formed as a sole proprietorship, partnership, limited liability company, limited liability partnership, or corporation, which includes nonprofit mutual benefit corporations, such as many common interest developments (Labor Code section 2750.3(e)(a)(1)).

- Second, the determination of employee or independent contractor status of the business service provider in a business-to-business relationship shall be governed by a different test as opposed to the ABC Test that applies to individuals (Labor Code section 2750.3(e)(a)(1)). This business-to-business test is known as the *Borello* Test from the California Supreme Court case that historically and previously set forth the applicable test to determine proper worker classification (*S.G. Borello & Sons, Inc. v. Dept. of Industrial Relations* (1989) 48 Cal.3d 341). The *Borello* Test has been in use since approximately 1989 and sets forth 12 factors, all of which must be satisfied to have a bona fide business-to-business/independent contractor relationship, not an employer-employee relationship:

    1. The business service provider is free from the control and direction of the contracting business in connection with the work, both under the contract for the performance of the work and in fact.
    2. The business service provider is providing services directly to the contracting business rather than to customers of the contracting business.
    3. The contract with the business service provider is in writing.
    4. If the work is performed in a jurisdiction that requires the business service provider to have a business license or business tax registration, the business service provider has the required business license or business tax registration.
    5. The business service provider maintains a business location that is separate from the business or work location of the contracting business.
    6. The business service provider is customarily engaged in an independently established business of the same nature as that involved in the work performed.
    7. The business service provider actually contracts with other businesses to provide the same or similar services and maintains a clientele without restrictions from the hiring entity.
    8. The business service provider advertises and holds itself out to the public as available to provide the same or similar services.
    9. The business service provider provides its own tools, vehicles, and equipment to perform the services.
    10. The business service provider can negotiate its own rates.
    11. Consistent with the nature of the work, the business service provider can set its own hours and location of work.

12. The business service provider is not performing the type of work for which a license from the Contractor's State License Board is required, pursuant to Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code.

    (Labor Code section 2750.3(e)(a)(1)(A)-(L); *S.G. Borello & Sons, Inc. v. Dept. of Industrial Relations* (1989) 48 Cal.3d 341.)

Are There Any Other Considerations Related to Misclassification of Employees?

In addition to this new law, associations should continue to be cognizant of the risks of being deemed a joint employer and plan ahead to minimize their liability for these potential joint employer risks. For example, an association should understand that when it has onsite workers who are employed by their management companies or vendors, these onsite workers could also be deemed employees of the association under the joint employer doctrine and under AB 5 which amends the definitions of "employee" and "employer" in Labor Code section 3351 and Unemployment Insurance Code sections 606.5 and 621.

What Can Associations Do In Response to These New Laws?

Community associations should consult with legal counsel about whether to reclassify all of their workers as employees unless they are confident their workers can meet the ABC Test set forth in the *Dynamex* case and AB 5. If employees are misclassified as independent contractors, these workers could file a lawsuit in state court or initiate a claim with the Labor Commissioner's Office, the Employment Development Department, and the Franchise Board, all of which have jurisdiction and authority over worker misclassification matters. If such a claim or lawsuit is filed against an association, these claims are considered "wage and hour" or "misclassification" claims and are typically not covered by the standard Employment Practices Liability Insurance ("EPLI") policies that cover associations or their management companies. Nonprofit corporations and smaller companies are not financially equipped to participate in protracted litigation or administrative proceedings in an attempt to prove their workers are properly classified.

What are Some Options to Minimize the Risks of Misclassification?

What can associations do to try to protect themselves if they are concerned about workers providing services that may be misclassified as independent contractors by the association or its vendors or contractors?

- Classify association workers as employees and ensure that your onsite workers are being classified as employees by your vendors or contractors if these workers cannot satisfy the ABC Test.
- Contact your insurance agent to obtain an EPLI policy for the association that covers wage and hour claims, misclassification claims, third party claims as well as coverage for your independent contractors, especially if there are independent contractors providing services for the association. It is best to make this inquiry now before the next budget disclosures are distributed to the owners in case the association will need to increase assessments to cover increased insurance costs.

- Timely and immediately notify any applicable EPLI carrier of facts or circumstances that may give rise to a claim if you have any concern you may have misclassified workers as independent contractors.
- Carefully draft new written contracts or revise existing contracts with vendors or contractors, in order to minimize risks of liability for misclassification claims because it is possible that the association may be deemed a joint employer of the workers provided by the vendors or contractors. For example, an association can require its vendors or contractors to (i) indemnify the association for employment-related claims; (ii) have EPLI insurance including wage and hour, misclassification, independent contractor and third party coverage; and (iii) require an additional insured endorsement in favor of the association on these EPLI policies, if available.