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## A New Framework for ABC Test Exemptions: When Should an Employee Not Be an Employee?

Charles Lam

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# A NEW FRAMEWORK FOR ABC TEST EXEMPTIONS: WHEN SHOULD AN EMPLOYEE NOT BE AN EMPLOYEE?

*Charles Lam\**

*In recent years, several states have implemented a new test to determine whether a laborer for remuneration is an employee or an independent contractor known as the “ABC test.” California is one of the latest states to adopt that test. But the state exempted by statute several categories of specific industries and business relationships. This Note, relying on public choice theory, argues for a broader and generally applicable exemption framework to the ABC test. I reject the current exemption system because it invites wasteful lobbying and slows governmental response to labor issues. Instead, I propose a framework that incorporates the main requirements of the ABC test: that the employer does not have control over the alleged independent contractor and that the independent contractor is actually entrepreneurial. The framework also incorporates the policy rationale for the ABC test by requiring some indicia proving those policies.*

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## I. INTRODUCTION

It was the most expensive initiative battle in California history.<sup>1</sup> On one side: Uber, DoorDash, Lyft, and their allies.<sup>2</sup> On the other: organized labor.<sup>3</sup> The prize: an exemption for “app-based drivers” from California’s new law that determines whether workers are “employees” or independent contractors.<sup>4</sup> The tech companies, armed with a more-than-\$180-million advantage over labor,<sup>5</sup> won out by nearly twenty percentage points.<sup>6</sup>

While California’s fight over Proposition 22 has likely garnered the most headlines and spending, it is by no means the only struggle over exemptions to California’s new employment test, which was adopted by the California Supreme Court in a limited context in 2018<sup>7</sup> and codified a year later as a general test in Assembly Bill 5 (“AB 5”).<sup>8</sup> The new “ABC test”<sup>9</sup> makes it more difficult for employers to prove that someone working for them is an independent contractor. The old common law test<sup>10</sup> classified a worker as an independent contractor if the would-be employer did not have the right to control the details of how the work was accomplished.<sup>11</sup> By contrast, the ABC test first presumes a worker is an employee.<sup>12</sup> To overcome that presumption, the employer must prove that the employer does not have the right to control (the common law test) *and also* “that the worker performs work that is outside the usual course” of the employer’s business *and also* “that the worker is customarily engaged in” the type of

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1. Michael Hiltzik, *Uber and Lyft Just Made Their Campaign to Keep Exploiting Workers the Costliest in History*, L.A. TIMES (Sept. 8, 2020), <https://www.latimes.com/business/story/2020-09-08/uber-lyft-most-expensive-initiative> [<https://perma.cc/DE4Z-NLJ3>].

2. Ryan Menezes et al., *Billions Have Been Spent on California’s Ballot Measure Battles. But This Year Is Unlike Any Other*, L.A. TIMES (Nov. 13, 2020), <https://www.latimes.com/projects/props-california-2020-election-money/> [<https://perma.cc/Y86B-FQJ8>]. The Yes on 22 Campaign spent more than \$204 million on Proposition 22. *Id.*

3. *Id.* Opponents of Proposition 22 spent about \$20 million. *Id.*

4. See CAL. BUS. & PROF. CODE §§ 7448–7467 (West Supp. 2021); CAL. REV. & TAX. CODE § 17037 (West Supp. 2021); Taryn Luna, *California Voters Approve Prop. 22, Allowing Uber and Lyft Drivers to Remain Independent Contractors*, L.A. TIMES (Nov. 3, 2020), <https://www.latimes.com/california/story/2020-11-03/2020-california-election-tracking-prop-22> [<https://perma.cc/QU43-D7TX>] (explaining the details of Proposition 22).

5. Menezes et al., *supra* note 2.

6. *2020 California Election Results*, L.A. TIMES, <https://www.latimes.com/projects/2020-california-election-live-results/> [<https://perma.cc/7VF4-ZBUU>].

7. See *Dynamex Operations W., Inc. v. Superior Ct.*, 416 P.3d 1, 40 (Cal. 2018).

8. Assemb. B. 5, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

9. *Id.*; see also *Dynamex*, 416 P.3d at 7.

10. See *infra* Section II.A.

11. See *infra* notes 43–46 and accompanying text.

12. See *infra* note 79 and accompanying text.

work performed.<sup>13</sup> The legislature included in AB 5 a set of narrow exemptions that apply to specific professions and relationships.<sup>14</sup> If an employer or worker fits within one of those exemptions, then AB 5 prescribes that courts use the old common law test to classify workers.<sup>15</sup>

The new law immediately disrupted many industries.<sup>16</sup> One news publisher ended relationships with hundreds of California-based writers and editors,<sup>17</sup> truckers working out of the ports of Los Angeles and Long Beach formed their own corporate entities in hopes of qualifying for an exception,<sup>18</sup> and workers who had traditionally been contractors anecdotally reported a decline in work.<sup>19</sup> In addition, industry groups including journalism, music, trucking, court reporting, youth sports leagues, and community theaters lobbied for their own exemptions from AB 5's ABC test.<sup>20</sup> The COVID-19 pandemic worsened employment issues.<sup>21</sup> And despite the upheaval, relief in the form of amendments to the law took nearly a year to arrive.<sup>22</sup> Given the success of Proposition 22 and the desire for some states to reform their employment laws,<sup>23</sup> the question of how to structure exemptions to the ABC test remains open.

This Note, relying on public choice theory,<sup>24</sup> argues for a broader and generally applicable exemption framework to the ABC test. I reject the current exemption system, which provides narrow exemptions for specific professions and working relationships,<sup>25</sup> because it invites wasteful lobbying and slows governmental response to labor issues.<sup>26</sup> Instead, I propose a framework that incorporates the main requirements of the ABC test: that the employer does not have control over the alleged independent contractor and that the independent contractor

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13. *See infra* notes 80–82 and accompanying text.

14. Assemb. B. 5, 2020 Leg., 2019–2020 Reg. Sess. § 2 (Cal. 2019).

15. *See infra* notes 93–100 and accompanying text.

16. *See infra* notes 105–113 and accompanying text.

17. *See infra* note 107 and accompanying text.

18. *See infra* note 105 and accompanying text.

19. *See infra* note 109 and accompanying text.

20. *See infra* notes 114–117 and accompanying text.

21. *See infra* note 113 and accompanying text.

22. *See infra* note 120 and accompanying text.

23. *See infra* notes 170–173 and accompanying text.

24. *See infra* Section III.A.1.

25. *See infra* Section II.D (discussing the current exemptions within the relevant California Labor Code provisions (i.e., CAL. LAB. CODE §§ 2776–2784)).

26. *See infra* Section III.A.

is actually entrepreneurial.<sup>27</sup> The framework also incorporates the policy rationale for the ABC test by requiring some indicia proving those policies.<sup>28</sup>

Part II of this Article discusses the history of the employer-employee relationship in California from the common law to the modern test. Part III argues that the current California exemptions are inefficient because they invite wasteful lobbying and slow government response to labor issues. Part IV proposes a new framework for exemptions that would apply to most industries and that would require businesses prove prongs A and C of the ABC test along with some other indicia to obtain an exemption to the ABC test. Part V offers the conclusion that a general exemption test is preferable to the current statutory scheme.

## II. CALIFORNIA'S EMPLOYEE VERSUS INDEPENDENT CONTRACTOR TEST

In California, statute controls the determination of whether a person who provides “labor or services for remuneration” is an employee or an independent contractor under the Labor Code, Unemployment Insurance Code, and state wage orders.<sup>29</sup> The relevant sections of the Labor Code (signed in 2019<sup>30</sup> and amended in 2020<sup>31</sup>) codified *Dynamex Operations West, Inc. v. Superior Court* (“*Dynamex*”),<sup>32</sup> added exemptions to the test adopted in that case,<sup>33</sup> and expanded the test to additional labor contexts.<sup>34</sup> But the statute is not the end of the story. In work arrangements where the legislature provides for an exemption from *Dynamex*, the statute applies the test announced in *S. G. Borello & Sons, Inc. v. Department of Industrial Relations* (“*Borello*”),<sup>35</sup> which sets out the common law test that *Dynamex* overruled.<sup>36</sup> Understanding both cases and the current statutory exemptions is critical to understanding California employee-classification law.

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27. See *infra* Section IV.

28. See *infra* Section IV.A.2.

29. CAL. LAB. CODE § 2775 (West Supp. 2021).

30. Assemb. B. 5, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2019).

31. Assemb. B. 2257, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

32. 416 P.3d 1 (Cal. 2018).

33. CAL. LAB. CODE §§ 2776–2784.

34. *Dynamex* only considered wage orders. Cf. CAL. LAB. CODE § 2775(b)(1) (broadening the scope of the ABC test beyond Industrial Welfare Commission wage orders to the Labor Code and the Unemployment Insurance Code).

35. 769 P.2d 399 (Cal. 1989).

36. *Dynamex*, 416 P.3d at 35.

### A. Before Dynamex

Distinguishing employees from independent contractors has proved difficult across jurisdictions.<sup>37</sup> California courts have struggled with the issue since at least the 1940s.<sup>38</sup> Prior to *Dynamex*, *Borello* was “the seminal case for determining employment classifications in California.”<sup>39</sup> *Borello* dealt with whether “agricultural laborers engaged to harvest cucumbers under a written ‘sharefarmer’ agreement” were employees or independent contractors for the purposes of California’s workers’ compensation statute.<sup>40</sup> In that case, the court summarized the California jurisprudence on the employee-independent contractor question<sup>41</sup> and approved of a multi-factor test that applied the common law “control of details” test followed in combination with consideration of “‘secondary’ indicia of the nature of a service relationship.”<sup>42</sup>

The control-of-details test asks “whether the person to whom service is rendered has the right to control the manner and means of accomplishing the result desired.”<sup>43</sup> The hiring party need not retain control of all the details, just “‘all *necessary* control’ over its operations.”<sup>44</sup> And the hiring party does not need to exercise actual control, just retain the right to control.<sup>45</sup> If the hiring party retains control, a court applying the test would find an employer-employee relationship.<sup>46</sup>

The secondary indicia considered under the *Borello* test included whether a principal could discharge a worker “at will, without cause”—which would weigh for an employee-employer relationship—and factors derived from § 220 of the Restatement (Second) of Agency:

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37. See Nat’l Lab. Rels. Bd. v. Hearst Publ’ns, Inc., 322 U.S. 111, 121 (1944) (“Few problems in the law have given greater variety of application and conflict in results than the cases arising in the borderland between what is clearly an employer-employee relationship and what is clearly one of independent, entrepreneurial dealing.”).

38. Benjamin Powell, Note, *Identity Crisis: The Misclassification of California Uber Drivers*, 50 LOY. L.A. L. REV. 459, 463 (2017); see, e.g., *Empire Star Mines Co. v. Cal. Emp. Comm’n*, 168 P.2d 686 (Cal. 1946).

39. Powell, *supra* note 38, at 463.

40. S.G. Borello & Sons, Inc. v. Dep’t of Indus. Rels., 769 P.2d 399, 400 (Cal. 1989).

41. *Id.* at 403–04.

42. *Id.* at 404.

43. *Id.* (quoting *Tieberg v. Unemployment Ins. Appeals Bd.*, 471 P.2d 975, 977 (Cal. 1970)).

44. *Ayala v. Antelope Valley Newspapers, Inc.*, 327 P.3d 165, 172 (Cal. 2014) (quoting *Borello*, 769 P.2d at 401).

45. *Id.*

46. See *id.*

(a) whether the one performing services is engaged in a **distinct occupation or business**; (b) 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**; (c) the **skill required** in the particular occupation; (d) whether the principal or the worker supplies the **instrumentalities, tools, and the place of work** for the person doing the work; (e) the **length of time** for which the services are to be performed; (f) the **method of payment**, whether by the time or by the job; (g) **whether or not the work is a part of the regular business** of the principal; and (h) whether or not the **parties believe** they are creating the relationship of employer-employee.<sup>47</sup>

If a worker is engaged in a **distinct occupation or business**, that suggests that the worker is an independent contractor rather than an employee. The *Borello* court noted that the agricultural workers “engage[d] in no distinct trade or calling” and did not “hold themselves out in business.”<sup>48</sup> Rather, they “perform[ed] typical farm labor for hire wherever jobs [were] available,” “invest[ed] nothing but personal service and hand tools,” and “incur[red] no opportunity for ‘profit’ or ‘loss.’”<sup>49</sup> Several other cases agreed with this line of reasoning, “finding employment status when workers were not operating an independent business apart from that of the alleged employer.”<sup>50</sup>

The **supervision** factor is tied to the primary control of details test, “as close supervision is clearly indicative of an employer’s ability to control the details of the work.”<sup>51</sup> More supervision weighs toward employee status.<sup>52</sup>

The test also considers the **skill required** to complete the work. If no skill is required to complete the work, the required-skill factor

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47. *Borello*, 769 P.2d at 404 (emphasis added) (citations omitted).

48. *Id.* at 409.

49. *Id.*

50. Powell, *supra* note 38, at 469; *see, e.g.*, *Antelope Valley Press v. Poizner*, 75 Cal. Rptr. 3d 887, 892–93 (Ct. App. 2008) (finding employee status when there was no evidence that newspaper deliverers held themselves out as independent delivery services); *Air Couriers Int’l v. Emp. Dev. Dep’t*, 59 Cal. Rptr. 3d 37, 47 (Ct. App. 2007) (finding employee status when a group of couriers worked for a courier company and not “in a separate profession or operating an independent business”).

51. Powell, *supra* note 38, at 469.

52. *Malloy v. Fong*, 232 P.2d 241, 249 (Cal. 1951) (“The existence of the right of control and supervision establishes the existence of an agency relationship.”).



will weigh for finding employee status.<sup>53</sup> The *Borello* court noted that the agricultural workers “performed manual labor requiring no special skill” and found that they were employees.<sup>54</sup> Courts have also weighed the factor for employee status (i.e., lacking special skill) when considering knife salespeople,<sup>55</sup> cab drivers,<sup>56</sup> newspaper deliverers,<sup>57</sup> and delivery truck drivers.<sup>58</sup>

Courts are more likely to weigh in favor of employee status when an alleged employer provides the “**instrumentalities, tools, and place of work.**”<sup>59</sup> This includes the hirer not directly providing the tool but leasing and maintaining the equipment.<sup>60</sup>

The **length of time** is also relevant. A work agreement with a contemplated end point, as opposed to an ongoing agreement, is likely to weigh in favor of independent contractor status rather than employee status.<sup>61</sup>

While not determinative, an hourly **method of payment** generally weighs in favor of employee status, while payment per job weighs in favor of independent contractor status.<sup>62</sup>

If a laborer’s work is found to be the **same kind as the regular business of the employer**, the factor weighs in favor of an employee relationship.<sup>63</sup>

The **parties’ understanding** of the kind of relationship they are entering can also weigh on a court’s determination but “will be ignored

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53. *Borello*, 769 P.2d at 407.

54. *Id.*

55. *Harris v. Vector Mktg. Corp.*, 656 F. Supp. 2d 1128, 1139 (N.D. Cal. 2009).

56. *Yellow Cab Coop., Inc. v. Workers’ Comp. Appeals Bd.*, 277 Cal. Rptr. 434, 441 (Ct. App. 1991) (“The work did not involve the kind of expertise which requires entrustment to an independent professional . . . and the skill required on the job is such that it can be done by employees rather than specially skilled independent workmen.” (quoting *Emps. Ins. v. Greater Omaha Transp. Co.*, 303 N.W.2d 282, 283–84 (Neb. 1981))).

57. *Antelope Valley Press v. Poizner*, 75 Cal. Rptr. 3d 887, 900 (Ct. App. 2008) (“Delivering papers requires no particular skill.”).

58. *JKH Enters. v. Dep’t of Indus. Rels.*, 48 Cal. Rptr. 3d 563, 579 (Ct. App. 2006) (“[T]he functions performed by the drivers, pick-up and delivery of papers or packages and driving in between, did not require a high degree of skill.”).

59. Powell, *supra* note 38, at 471.

60. *See Ruiz v. Affinity Logistics Corp.*, 754 F.3d 1093, 1104 (9th Cir. 2014).

61. *See id.* at 1105 (finding employee status when “there was no contemplated end to the service relationship when Affinity and the drivers signed their contracts, and drivers often stayed with Affinity for years” (internal quotation marks omitted)).

62. *Alexander v. FedEx Ground Package Sys., Inc.*, 765 F.3d 981, 996 (9th Cir. 2014) (“This payment method cannot easily be compared to either hourly payment (which favors employee status) or per job payment (which favors independent contractor status).”).

63. Powell, *supra* note 38, at 472.

if their conduct establishes otherwise.”<sup>64</sup> The parties cannot override a court’s determination by contract.<sup>65</sup>

### B. After Dynamex

In *Dynamex*, the California Supreme Court rejected the *Borello* test for wage orders<sup>66</sup> and instead adopted the ABC test.<sup>67</sup> In *Dynamex*, two delivery drivers sued Dynamex, the delivery company that they worked for.<sup>68</sup> They argued that the company misclassified its workers as independent contractors when instead they were, in fact, employees.<sup>69</sup> The plaintiffs argued that, because they were employees, they were protected by California wage orders, which “impose obligations relating to the minimum wages, maximum hours, and a limited number of very basic working conditions (such as minimally required meal and rest breaks) of California employees.”<sup>70</sup>

In making that decision, the court noted that, unlike the federal common law test, *Borello* focused on the statutory purpose of the workers’ compensation law at issue.<sup>71</sup> While early federal cases relied on statutory purpose,<sup>72</sup> legislation following those cases “has been interpreted to require that federal legislation generally be construed, in the absence of a more specific statutory standard or definition of employment, to embody a more traditional common law test for distinguishing between employees and independent contractors,” with the control factor given “considerable weight.”<sup>73</sup> Notably, after *Borello*, the California Legislature did not react the same way as Congress did, and, unlike Congress, it imposed more penalties on businesses that misclassified employees.<sup>74</sup>

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64. *Id.* at 472. See *Estrada v. FedEx Ground Package Sys., Inc.*, 64 Cal. Rptr. 3d 327, 335 (Ct. App. 2007) (“The parties’ label is not dispositive and will be ignored if their actual conduct establishes a different relationship.”).

65. Powell, *supra* note 38, at 472.

66. *Dynamex Operations W., Inc. v. Superior Ct.*, 416 P.3d 1, 6–7 (Cal. 2018).

67. *Id.* at 7.

68. *Id.* at 5.

69. *Id.*

70. *Id.*

71. *Id.* at 19 (“[I]t appears more precise to describe *Borello* as calling for resolution of the employee or independent contractor question by focusing on the intended scope and purposes of the particular statutory provision or provisions at issue.”).

72. *Id.* at 20.

73. *Id.*

74. *Id.* (“Instead, in response to the continuing serious problem of worker misclassification as independent contractors, the California Legislature has acted to impose substantial civil penalties on those that willfully misclassify, or willfully aid in misclassifying, workers as independent contractors.”).

The court then looked to its decision in *Martinez v. Combs*,<sup>75</sup> which addressed the meanings of “employ” and “employer” in the context of California wage orders.<sup>76</sup> Looking at the statutory history of the law granting the Industrial Welfare Commission authority to issue wage orders, the *Martinez* court held that the definition of employ was broader than the common law test for employee status.<sup>77</sup> Relying on that reasoning, the *Dynamex* court adopted the “ABC” test to determine employee status in the context of wage orders.<sup>78</sup> Under the *Dynamex* version of the test, there is a presumption of employment status.<sup>79</sup> To overcome that presumption, the hiring party must establish each of three factors:

“that the worker is free from the control and direction of the hiring entity in connection with the performance of the work”;<sup>80</sup> and

“that the worker performs work that is outside the usual course of the hiring entity’s business”;<sup>81</sup> and

“that the worker is customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed.”<sup>82</sup>

The court then discussed each part of the test.<sup>83</sup>

### 1. Part A: Free from Control and Direction

To overcome the presumption that a laborer is an employee, a hiring entity must prove that the laborer is “free from the control and direction of the hiring entity in connection with the performance of the work.”<sup>84</sup> The *Dynamex* court reasoned that because the suffer or

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75. 231 P.3d 259 (Cal. 2010).

76. *Dynamex*, 416 P.3d at 20.

77. *Id.* at 22 (“The *Martinez* court summarized its conclusion on this point as follows: ‘To employ, then, under the IWC’s definition, has three alternative definitions. It means: (a) to exercise control over the wages, hours or working conditions, or (b) to suffer or permit to work, or (c) to engage, thereby creating a common law employment relationship.’” (quoting *Martinez*, 213 P.3d at 278)).

78. *Id.* at 35–36. The court tied the ABC test to the suffer or permit to work language in the wage orders. *Id.* at 36. The “ABC” test is used in several other states in various contexts. See generally Anna Deknatel & Lauren Hoff-Downing, *ABC on the Books and in the Courts: An Analysis of Recent Independent Contractor and Misclassification Statutes*, 18 U. PA. J.L. & SOC. CHANGE 53, 65–71 (2015) (collecting state statutes). The *Dynamex* court cited the Massachusetts version of the test approvingly. *Dynamex*, 416 P.3d at 34 n.23.

79. *Dynamex*, 416 P.3d at 35.

80. *Id.*

81. *Id.*

82. *Id.* (citations omitted).

83. *Id.* at 36–40.

84. *Id.* at 35–36.

permit to work language embodied in the ABC test was meant to be broader than the common law employee test, a laborer considered an employee under the common law test should also be considered an employee under the ABC test.<sup>85</sup> Part A of the test, therefore, “essentially adopts the ‘control’ factor from the *Borello* standard.”<sup>86</sup>

## 2. Part B: Outside the Usual Course of Business

A hiring entity must also prove “that the worker performs work that is outside the usual course of the hiring entity’s business” to overcome the presumption that the worker is an employee.<sup>87</sup> The *Dynamex* court noted that workers “who would ordinarily be viewed by others as working in the hiring entity’s business and not as working, instead, in the worker’s own independent business” were most likely to be doing work in the hiring entity’s course of business.<sup>88</sup>

## 3. Part C: An Independently Established Trade

Finally, to overcome the presumption that a worker is an employee, the hiring entity must prove “that the worker is ‘customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed.’”<sup>89</sup> The *Dynamex* court noted in its discussion of this part of the ABC test that an independent contractor “generally takes the usual steps to establish and promote his or her independent business—for example, through incorporation, licensure, advertisements, routine offerings to provide the services of the independent business to the public or to a number of potential customers, and the like.”<sup>90</sup>

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85. *Id.* at 36.

86. Natalie Kalbakian, Note, *Workers of the Gaming World, Unite! The Uncertain Future of the Video Game Industry in the Aftermath of AB 5*, 40 LOY. L.A. ENT. L. REV. 351, 359 (2020).

87. *Dynamex*, 416 P.3d at 35.

88. *Id.* at 37. The court offered the situation of a retail store hiring a plumber or an electrician as an example of an independent contractor relationship and the situation of a clothing manufacturer hiring a work-at-home seamstress or a bakery hiring a cake decorator as examples of an employee relationship. *Id.* This part closely tracks the **whether or not the work is a part of the regular business** of the employer indicia of the *Borello* test. See *supra* note 63 and accompanying text.

89. Kalbakian, *supra* note 86, at 361.

90. *Dynamex*, 416 P.3d at 39. This part closely tracks the **distinct occupation or business** indicia of the *Borello* test. See *supra* notes 48–50 and accompanying text.

### C. Assembly Bill 5, Aftermath, and Amendment

The year after *Dynamex* was decided, the California Legislature passed, and Governor Gavin Newsom signed, AB 5.<sup>91</sup> The law codified the *Dynamex* decision and expanded the ABC test's use to the Labor and Unemployment Insurance Codes.<sup>92</sup> It also added exceptions to the ABC test and applied the *Borello* test to business-to-business contracting relationships;<sup>93</sup> referral agencies;<sup>94</sup> "professional services," including marketing, HR administration, travel agencies, etc.;<sup>95</sup> partnerships;<sup>96</sup> construction subcontracting;<sup>97</sup> data aggregation;<sup>98</sup> various named professions, including doctors, lawyers, architects, and engineers;<sup>99</sup> and motor clubs.<sup>100</sup> These exceptions were later amended and will be discussed below.<sup>101</sup>

In proposing the law, its author noted that the "the misclassification of workers . . . undermines the hard-fought laws passed by the Legislature that have historically positioned California as a national leader in creating the strongest worker protections in the country."<sup>102</sup> The law intended

to ensure workers who are currently exploited by being misclassified as independent contractors instead of recognized as employees have the basic rights and protections they deserve under the law, including a minimum wage, workers' compensation if they are injured on the job, unemployment insurance, paid sick leave, and paid family leave.<sup>103</sup>

Writing in support of AB 5, the California Labor Federation noted that the ABC test "prevents the common practice in many industries of a company forcing an individual to act as an independent business while

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91. John Myers et al., *Newsom Signs Bill Rewriting California Employment Law, Limiting Use of Independent Contractors*, L.A. TIMES (Sept. 18, 2019), <https://www.latimes.com/california/story/2019-09-18/gavin-newsom-signs-ab5-employees-independent-contractors-california> [<https://perma.cc/T4Q6-2NWC>].

92. CAL. LAB. CODE § 2775(b)(1) (West Supp. 2021).

93. *Id.* § 2776.

94. *Id.* § 2777.

95. *Id.* § 2778.

96. *Id.* § 2779.

97. *Id.* § 2781.

98. *Id.* § 2782.

99. *Id.* § 2783.

100. *Id.* § 2784.

101. See *infra* Section III.D.

102. CAL. ASSEMB., THIRD READING OF ASSEMBLY BILL NO. 5, 2019–2020 Reg. Sess. (Cal. 2019) (as amended May 1, 2019).

103. Assemb. B. 5, 2020 Leg., 2019–2020 Reg. Sess. § 1(e) (Cal. 2020).

the company maintains the right to set rates, direct work, and impose discipline.”<sup>104</sup>

The effects of the law were quick. Within two months of it taking effect, “hundreds of truckers” who transported cargo from the ports of Los Angeles and Long Beach incorporated as independent businesses in hope of qualifying under the business-to-business exception, and a nonprofit theatre canceled one of its annual productions.<sup>105</sup> A youth baseball league decided to transition its umpires to volunteers.<sup>106</sup> Vox Media ended hundreds of contracts with freelance writers who contributed to the company’s sports websites.<sup>107</sup> The music industry pushed for an exemption from the law, which industry personnel felt was poorly suited to their kind of work.<sup>108</sup> Anecdotally, workers and business owners from industries that had previously hired independent contractors (including pediatric therapy, online teaching, freelance writing, blogging, sign language interpretation, music, tax preparation, and medical transcription) reported a decline in work.<sup>109</sup> The law also provoked lawsuits by groups of writers,<sup>110</sup> a business that contracts with court reporters,<sup>111</sup> and an association of truckers.<sup>112</sup> The COVID-19 pandemic and its economic effects exasperated the issues.<sup>113</sup>

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104. CAL. ASSEMB., *supra* note 102.

105. Margot Roosevelt, *New California Labor Law AB 5 Is Already Changing How Businesses Treat Workers*, L.A. TIMES (Feb. 14, 2020), <https://www.latimes.com/business/story/2020-02-14/la-fi-california-independent-contractor-small-business-ab5> [<https://perma.cc/TBK5-W6JL>].

106. Lev Farris Goldenberg, *New Year, New Rules for Davis Little League Umpires*, DAVIS ENTER. (Jan. 4, 2020), <https://www.davisenterprise.com/sports/lev-farris-goldenberg-new-year-new-rules-for-davis-little-league-umpires/>.

107. Suhauna Hussain, *Vox Media Cuts Hundreds of Freelance Journalists as AB 5 Changes Loom*, L.A. TIMES (Dec. 17, 2019), <https://www.latimes.com/business/story/2019-12-17/vox-media-cuts-hundreds-freelancers-ab5> [<https://perma.cc/Z2VJ-8RE2>].

108. See Mitch Glazier et al., *AB5 Could Crush Independent Music in California (Guest Column)*, VARIETY (Sept. 4, 2019), <https://variety.com/2019/music/news/ab5-could-crush-independent-music-in-california-guest-column-1203322730/> [<https://perma.cc/CXP9-V3FK>].

109. Michael Lotito et al., *AB 5: The Aftermath of California’s Experiment to Eliminate Independent Contractors Offers a Cautionary Tale for Other States*, J.D. SUPRA (Mar. 10, 2020), <https://www.jdsupra.com/legalnews/ab-5-the-aftermath-of-california-s-40627/> [<https://perma.cc/KW6V-ZK8F>].

110. *Am. Soc’y of Journalists & Authors, Inc. v. Becerra*, No. 19-10645, 2020 WL 1444909, at \*1 (C.D. Cal. Mar. 20, 2020).

111. Complaint for Declaratory Relief at 2–3, *Williams, Weisberg & Weisberg v. California*, No. 34-2020-00273530 (Sacramento Cnty. Super. Ct. Jan. 16, 2020).

112. *Cal. Trucking Ass’n v. Becerra*, 433 F. Supp. 3d 1154, 1159 (S.D. Cal. 2020), *rev’d sub nom.*, *Cal. Trucking Ass’n v. Bonta*, 996 F.3d 644 (9th Cir. 2021).

113. See Johana Bhuiyan, *Coronavirus Is Supercharging the Fight over California’s New Employment Law*, L.A. TIMES (Mar. 26, 2020), <https://www.latimes.com/business/technology/story/>

AB 5 also provoked action in the statehouse. Legislators introduced more than thirty bills to amend the law.<sup>114</sup> Proposals ranged from amendments exempting music industry workers,<sup>115</sup> little league umpires,<sup>116</sup> and livestock judges<sup>117</sup> to amendments proposing different tests<sup>118</sup> or revoking AB 5.<sup>119</sup> The legislature consolidated several of the bills as AB 2257, which Governor Newsom signed.<sup>120</sup> The amendments clarified and expanded some of the existing exemptions and added a new exemption for the music industry.<sup>121</sup> Uber, Lyft, and other tech companies also proposed a ballot proposition, which passed.<sup>122</sup> The proposition, “the costliest ballot measure fight in California history,”<sup>123</sup> categorized “app-based drivers” as independent contractors as long as the apps for which they work met several conditions.<sup>124</sup>

#### D. The Current Exemptions

As amended by AB 2257, California generally applies the ABC test to determine whether a worker is an employee or an independent contractor for the purposes of the Labor Code, the Unemployment Insurance Code, and California wage orders.<sup>125</sup> The law provides for nine conditional exemptions where the *Borello* test applies instead.<sup>126</sup>

##### 1. Business-To-Business

The first exemption applies to “bona fide business-to-business contracting” relationships.<sup>127</sup> To qualify for this exemption, the two

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2020-03-26/coronavirus-disrupted-their-income-now-their-calls-for-california-to-take-action-on-ab5-are-getting-louder [https://perma.cc/3PPY-G33S].

114. John Myers, *A Flood of Proposed Changes to California's AB 5 Awaits State Lawmakers*, L.A. TIMES (Feb. 28, 2020), <https://www.latimes.com/california/story/2020-02-28/proposals-change-ab5-independent-contractors-labor-law-california> [https://perma.cc/E7ZS-J3KA].

115. S.B. 881, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

116. Assemb. B. 3185, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

117. Assemb. B. 2497, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

118. S.B. 806, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

119. Assemb. B. 1928, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

120. CalMatters, *Here Are the 2020 Bills Gov. Newsom Rejected or Signed into California Law*, LAIST (Oct. 1, 2020), <https://laist.com/news/here-are-the-2020-bills-gov-newsom-rejected-or-signed-into-california-law> [https://perma.cc/K377-EW6Y].

121. Assemb. B. 2257, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

122. Luna, *supra* note 4.

123. Menezes et al., *supra* note 2. More than \$220 million was spent on advertising for and against Proposition 22. *Id.* Uber, DoorDash, Lyft, Instacart, and Postmates contributed more than \$200 million combined in support of the proposition. *Id.*

124. See CAL. BUS. & PROF. CODE §§ 7448–7467 (West Supp. 2021).

125. CAL. LAB. CODE § 2775(b) (West Supp. 2021).

126. *Id.* § 2776–2784.

127. *Id.* § 2776.

businesses involved must be individuals “acting as . . . sole proprietor[s]” or business entities “formed as a partnership, limited liability company, limited liability partnership, or corporation.”<sup>128</sup> If this threshold condition is met, the laboring party qualifies as an independent contractor if the hiring party proves the twelve conditions in **Figure 1** (below).<sup>129</sup>

**Figure 1**<sup>130</sup>

(1) the laboring party is free from control and direction both in fact and under the contract
(2) the laboring party provides services to the contracting party, not the contracting party’s customers
(3) the contract is in writing, includes the payment amount and any applicable rate, and the payment due date
(4) the laboring party holds any required business licenses or tax registrations
(5) the laboring party maintains a business location, which may be their residence, separate from the contracting party’s location
(6) the laboring party is “customarily engaged in an independently established business of the same nature” as the work performed
(7) the laboring party has the ability to contract with other businesses to “provide the same or similar services and maintain a clientele without restrictions” from the contracting party
(8) the laboring party actually advertises its services
(9) “[c]onsistent with the nature of the work,” the laboring party “provides its own tools, vehicles, and equipment to perform the services, not including any proprietary materials that may be necessary”
(10) the laboring party can negotiate its rates
(11) “[c]onsistent with the nature of the work,” the laboring party can set its own hours and location of work
(12) the laboring party is not doing work described in a separate California code controlling construction contracting

## 2. Referral Agencies

The second exemption applies to referral agencies—businesses that connect laboring parties to clients—and the laboring parties they refer.<sup>131</sup> For the referral agencies to qualify for the exemption from the

128. *Id.* § 2776(a).

129. *Id.*

130. *See id.* § 2776.

131. *Id.* § 2777.



ABC test, the laboring party must be “an individual acting as a sole proprietor, or a business entity formed as a partnership, limited liability company, limited liability partnership, or corporation” that “provides services to clients through a referral agency.”<sup>132</sup> If the laboring party meets this threshold condition, the referral agency must show that it satisfies the eleven conditions in **Figure 2** (below) to qualify for exemption from the ABC test.<sup>133</sup>

**Figure 2**<sup>134</sup>

(1) the laboring party is free from control and direction both in fact and under the contract
(2) the laboring party holds any required business licenses or tax registrations
(3) if the work done is described in a separate California code controlling construction, the laboring party has all the appropriate licenses
(4) the laboring party certifies to the referral agency that it has any required licenses, and the referral agency maintains those records for at least three years
(5) the laboring party delivers services to the client under its own name without requirement that it deliver its services under the name of the referral agency
(6) the laboring party provides its own tools and supplies
(7) the laboring party “is customarily engaged, or was previously engaged, in an independently established business or trade of the same nature as, or related to, the work performed for the client”
(8) “[t]he referral agency does not restrict the service provider from maintaining a clientele and the service provider is free to seek work elsewhere, including through a competing referral agency”
(9) the laboring party “sets their own hours and terms of work or negotiates their hours and terms of work directly with the client”
(10) the laboring party—without a deduction from the referral agency—sets its own rates, or negotiates their rates with the client through the referral agency, or negotiates their rates directly with the client, or is free to accept or reject rates set by the client
(11) “[t]he laboring party is free to accept or reject clients and contracts, without being penalized in any form by the referral agency” except if the laboring party accepts a job and fails to fulfill any of its obligations

132. *Id.* § 2777(a).

133. *Id.*

134. *See id.*

The statute describing the exemption also contains a list of examples of industries that qualify for the exemption if the eleven conditions are met and a list of industries that are exempted from the exemption.<sup>135</sup> Examples of industries that qualify include, “but are not limited to, graphic design, . . . youth sports coaching, . . . wedding or event planning, . . . minor home repair, moving, errands, . . . dog walking, . . . and interpreting services.”<sup>136</sup> Industries that are exempted from the exemption are industries designated as highly hazardous under California statute and businesses “that provide janitorial, delivery, courier, transportation, trucking, agricultural labor, retail, logging, in-home care, or construction services other than minor home repair.”<sup>137</sup>

### 3. Professional Services

The third exemption applies to contracts for “professional services” as defined by statute.<sup>138</sup> Under this exemption, the laboring party qualifies as an independent contractor if it provides professional services and if the hiring entity proves the six conditions in **Figure 3** (below).<sup>139</sup>

**Figure 3**<sup>140</sup>

(1) the laboring party maintains a business location, which may include their residence, that is separate from the hiring entity
(2) the laboring party holds any required business licenses or tax registrations and any required professional licenses or permits
(3) the laboring party has the ability to set or negotiate their own rates
(4) “[o]utside of project completion dates and reasonable business hours,” the laboring party has the ability to set its own hours
(5) the laboring party “is customarily engaged in the same type of work performed under contract with another hiring entity or holds themselves out to other potential customers as available to perform the same type of work”
(6) the laboring party “customarily and regularly exercises discretion and independent judgment in the performance of the services”

135. *Id.* § 2777(b)(2).

136. *Id.* § 2777(b)(2)(B).

137. *Id.* § 2777(b)(2)(C).

138. *Id.* § 2778.

139. *Id.*

140. *See id.* § 2778(a).

The statute contains fifteen different categories of “professional services,” including marketing, HR administration, grant writing, graphic design, art, and freelance writing.<sup>141</sup>

#### 4. Two Individuals

The fourth exemption applies when two individuals act “as a sole proprietor or separate business entity formed as a partnership, limited liability company, limited liability partnership, or corporation”<sup>142</sup> to perform work for 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.”<sup>143</sup> To qualify for the exemption, the entity must meet the eight conditions in **Figure 4** (below).<sup>144</sup>

**Figure 4**<sup>145</sup>

(1) neither party controls or directs the other “in connection with the performance of the work,” both under the contract and in fact
(2) each party can “negotiate their rate of pay with the other”
(3) the parties’ written contract states “the total payment for services provided by both individuals at the single-engagement event, and the specific rate paid to each individual”
(4) each party maintains their own business location, which may include their residence
(5) each party “provides their own tools, vehicles, and equipment to perform the services under the contract”
(6) each party has any required business license or tax registration
(7) each party “is customarily engaged in the same or similar type of work performed under the contract or each individual separately holds themselves out to other potential customers as available to perform the same type of work”
(8) each party can “contract with other businesses to provide the same or similar services and maintain their own clientele without restrictions”

The statute also exempts from the exemption highly hazardous industries and “janitorial, delivery, courier, transportation, trucking, agricultural labor, retail, logging, in-home care, or construction services other than minor home repair.”<sup>146</sup>

141. *Id.* § 2778(b)(2)(A)–(O).

142. *Id.* § 2779(a).

143. *Id.* § 2779(b).

144. *Id.* § 2779(a).

145. *See id.*

146. *Id.* § 2779(c).

## 5. The Music Industry

The fifth exemption applies to the music industry generally.<sup>147</sup> The statute exempts certain “occupations in connection with creating, marketing, promoting, or distributing sound recordings or musical compositions.”<sup>148</sup> Covered occupations include songwriters, lyricists, composers, and proofers; musician managers; record producers; and vocalists,<sup>149</sup> but not film and TV crews and non-independent music publicists.<sup>150</sup> The law also allows any collective bargaining or union agreements between “the applicable labor unions and respective employers” to govern the determination of employee status.<sup>151</sup> The exemption includes additional, specific rules for “recording artists, musicians, and vocalists” that allow for collective bargaining.<sup>152</sup> Further, the law treats musicians and vocalists who do not collect or are not entitled to royalties as employees for overtime and minimum wage purposes.<sup>153</sup>

The statute also includes an exemption from the ABC test for some performances.<sup>154</sup> It provides that the *Borello* test applies to determine employee status *unless* (1) “[t]he musical group is performing as a symphony orchestra, the musical group is performing at a theme park or amusement park, or a musician is performing in a musical theater production;” or (2) “[t]he musical group is an event headliner for a performance taking place in a venue location with more than 1,500 attendees;” or (3) “[t]he musical group is performing at a festival that sells more than 18,000 tickets per day.”<sup>155</sup>

Finally, the music industry’s exemption includes a general application of *Borello* to “[a]n individual performance artist performing material that is their original work” if (1) the artist “is free from the control and direction of the hiring entity in connection with the performance of the work, both as a matter of contract and in fact”; and (2) the artist “retains the rights to their intellectual property that was created in connection with the performance”; and (3) “[c]onsistent with the nature of the work,” the artist “sets their terms of work and

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147. *Id.* § 2780.

148. *Id.* § 2780(a)(1).

149. *Id.* § 2780(a)(1)(A)–(J).

150. *Id.* § 2780(a)(2)(A)–(B).

151. *Id.* § 2780(a)(3).

152. *Id.* § 2780(a)(4)(A)–(C).

153. *Id.* § 2780(a)(4)(B).

154. *Id.* § 2780(b).

155. *Id.* § 2780(b)(1).

has the ability to set or negotiate their rates”; and (4) the artist “is free to accept or reject each individual performance engagement without being penalized in any form by the hiring entity.”<sup>156</sup> The statute includes a non-exhaustive list of professions qualifying as performance art, including “an individual performing comedy, improvisation, stage magic, illusion, mime, spoken word, storytelling, or puppetry.”<sup>157</sup>

## 6. Construction Subcontracting

The sixth exemption applies to construction subcontractors, allowing for the *Borello* test and other statutory tests to apply when (1) “[t]he subcontract is in writing”; (2) “[t]he subcontractor is licensed by the Contractors’ State License Board and the work is within the scope of that license”; (3) the subcontractor holds any required business licenses or tax registrations; (4) “[t]he subcontractor maintains a business location that is separate from the business or work location of the contractor”; (5) [t]he subcontractor has the authority to hire and to fire other persons to provide or to assist in providing the services”; (6) [t]he subcontractor assumes financial responsibility for errors or omissions in labor or services” through insurance or similar methods; and (7) “[t]he subcontractor is customarily engaged in an independently established business of the same nature as that involved in the work performed.”<sup>158</sup> The exemption includes several additional conditions for “construction trucking services.”<sup>159</sup>

## 7. Data Aggregation

The seventh exception applies to businesses, research institutions, or organizations that request and gather “feedback on user interface, products, services, people, concepts, ideas, offerings, or experiences” and the survey respondents providing the information.<sup>160</sup> The aggregating party must prove four conditions: (1) the respondent “is free from control and direction from the data aggregator with respect to the substance and content of the feedback”; (2) “[a]ny consideration paid for the feedback provided, if prorated to an hourly basis, is an amount equivalent to or greater than the minimum wage”; (3) “[t]he nature of the feedback requested requires the individual providing feedback to

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156. *Id.* § 2780(c)(1).

157. *Id.* § 2780(c)(2).

158. *Id.* § 2781(a)–(g).

159. *Id.* § 2781(h).

160. *Id.* § 2782(a).

the data aggregator to exercise independent judgment and discretion”; and (4) “[t]he individual has the ability to reject feedback requests, without being penalized in any form by the data aggregator.”<sup>161</sup>

### 8. Specific Occupations

The labor code’s eighth exemption applies to a variety of named occupations, many of which are defined in separate provisions of the labor code.<sup>162</sup> These occupations include doctors, lawyers, architects, engineers, private investigators, accountants, direct salespeople, commercial fisherman on American vessels, newspaper distributors, international exchange workers, and competition and sports judges.<sup>163</sup> In total, the law exempts twenty occupations or work arrangements.<sup>164</sup>

### 9. Motor Clubs

The ninth and last exemption created by the legislature applies the *Borello* test when a motor club contracts with a third-party to provide services to a client “if the motor club demonstrates that the third party is a separate and independent business from the motor club.”<sup>165</sup>

### 10. App-Based Drivers

Californians voted to exempt “app-based drivers” from the ABC test in the November 2020 election.<sup>166</sup> To qualify for the exemption, the app must pay a subsidy tied to the cost of health insurance on California’s healthcare exchange<sup>167</sup> and provide “occupational accident insurance” to its drivers,<sup>168</sup> among other requirements.<sup>169</sup>

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161. *Id.* § 2782(a)(1).

162. *Id.* § 2783.

163. *Id.* § 2783(b)–(j).

164. *Id.*

165. *Id.* § 2784.

166. CAL. SEC’Y OF STATE, STATEMENT OF VOTE: GENERAL ELECTION NOVEMBER 3, 2020, AT 67, <https://elections.cdn.sos.ca.gov/sov/2020-general/sov/complete-sov.pdf> [<https://perma.cc/4HVC-Z2UG>]. A California superior court judge ruled the law unconstitutional in August 2021. See Suhauna Hussain, *Prop. 22 Was Ruled Unconstitutional. What Will the Final Outcome Be?*, L.A. TIMES (Aug. 25, 2021), <https://www.latimes.com/business/technology/story/2021-08-25/after-prop-22-ruling-whats-next-uber-lyft> [<https://perma.cc/G5LY-6EGL>]. Gig economy companies said they would appeal the ruling. *Id.*

167. CAL. BUS. & PROF. CODE § 7454 (West Supp. 2021).

168. *Id.* § 7455.

169. *Id.* §§ 7456–7462.

### E. Future Developments

It is unclear what developments are possible given the passage of Proposition 22—which requires any change to the applicable sections to be “consistent with” and further the purpose of the law *and* be approved by a seven-eighths majority vote of the legislature<sup>170</sup>—and AB 2577. But other states are looking to regulate gig-economy companies. Massachusetts sued Uber and Lyft over the categorization of its workers,<sup>171</sup> and New York had planned on drafting a law regulating gig companies before the COVID-19 pandemic disrupted the state’s plans.<sup>172</sup> Following the passage of Proposition 22, Uber’s CEO said on an earnings call that “[g]oing forward, you’ll see us more loudly advocate for new laws like Prop. 22.”<sup>173</sup>

## III. CALIFORNIA’S EXEMPTIONS FROM THE ABC TEST ARE INEFFICIENT AND SHOULD BE REPLACED

### A. Piece-Meal Exemptions Are Inefficient

The current framework for exemptions to California’s ABC test, where the legislature sets out specific industries and job titles that are exempt, is inefficient. For one, the fact that the exemptions are tied to specific industries and job titles invites lobbying, which is economically wasteful and advantages industries that have resources to lobby over those that do not.<sup>174</sup> Further, the rigid way exemptions are handled requires that the legislature foresee any possible issues that may arise. If the legislature fails to identify issues, any possible fixes can be delayed.

#### 1. Lobbying, Waste, and Public Choice

Because the exceptions framework is based on specific industries and job titles, it invites political lobbying on behalf of industries and

170. *Id.* § 7465(a).

171. Kate Conger & Daisuke Wakabayashi, *Massachusetts Sues Uber and Lyft over the Status of Drivers*, N.Y. TIMES (July 14, 2020), <https://www.nytimes.com/2020/07/14/technology/massachusetts-sues-uber-lyft.html> [<https://perma.cc/8A4M-K8ED>].

172. Noam Scheiber & Kate Conger, *Fight over Gig Workers Persists Despite Win for Uber and Lyft*, N.Y. TIMES (Aug. 23, 2021), <https://www.nytimes.com/2020/11/11/business/economy/california-gig-workers-ballot-uber-lyft.html> [<https://perma.cc/B4D8-4EDR>].

173. *Id.*; see, e.g., Edward Ongweso, Jr., *Gig Companies Spend Millions on Anti-Labor PACs in Illinois and New York*, VICE: MOTHERBOARD (Nov. 19, 2020), <https://www.vice.com/en/article/m7avyp/gig-companies-spend-millions-on-anti-labor-pacs-in-illinois-and-new-york> [<https://perma.cc/R2C3-SVJW>].

174. See *infra* Section III.A.1.

professions. For example, following the passage of AB 5, the music industry lobbied for an industry exception that placed much of the labor associated with producing music under the *Borello* test.<sup>175</sup> Legislators wrote the exception<sup>176</sup> with input from music industry groups, Hollywood guilds, and unions.<sup>177</sup> The exception also included individuals “performing comedy, improvisation, stage magic, illusion, mime, spoken word, storytelling, or puppetry,”<sup>178</sup> again following lobbying from those groups.<sup>179</sup> These successes may attract further lobbying activity from other industries.<sup>180</sup> And, because of California’s system of direct democracy through ballot initiatives,<sup>181</sup> industries can campaign directly to the people for exemptions such as Proposition 22.<sup>182</sup>

Proponents of the public choice theory call such special interest legislation “rent-seeking.”<sup>183</sup> “Public choice [is] the economic study of nonmarket decisionmaking, or simply the application of economics to political science.”<sup>184</sup> It often treats the law-making process as “determined by the efforts of individuals and groups to further their own interests.”<sup>185</sup> The theory’s strength compared to traditional political science is that, while political science “has created ‘good descriptive information about how certain legislatures work,’”<sup>186</sup> public choice

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175. Sidney S. Fohrman & Ariel D. Shpigel, *The Music Industry Receives Relief from AB5*, THE RECORDER (May 4, 2020), <https://www.law.com/therecorder/2020/05/04/the-music-industry-receives-relief-from-ab5/> [https://perma.cc/ZSG8-KX7E].

176. CAL. LAB. CODE § 2780 (West Supp. 2021).

177. Fohrman & Shpigel, *supra* note 175.

178. CAL. LAB. CODE § 2780(c)(2).

179. David Albert Pierce, LINKEDIN (Sept. 2020), <https://www.linkedin.com/feed/update/urn:li:activity:6708953753082568704/> [https://perma.cc/N5J9-6UC5].

180. *See* Fohrman & Shpigel, *supra* note 175 (“In the wake of these new amendments, it remains to be seen whether leaders of other industries will work with California government officials to create additional industry-specific exceptions to AB5, or whether other approaches through bills or lawsuits will be successful.”).

181. *See generally* 38 CAL. JUR. 3D *Initiative and Referendum* § 1, Westlaw (database updated Aug. 2021).

182. *See* Suhauna Hussain, *What Prop 22’s Defeat Would Mean for Uber and Lyft—and Drivers*, L.A. TIMES (Oct. 19, 2020), <https://www.latimes.com/business/technology/story/2020-10-19/prop-22-explained>. To get an initiative on to the ballot, a proponent must present the initiative to the California Secretary of State with the certified signatures of voters numbering five percent of the number of voters in the preceding election for California governor. CAL. CONST. art. II, § 8.

183. *See generally* DANIEL A. FARBER & PHILIP P. FRICKEY, LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION 34 (1991).

184. Daniel A. Farber & Philip P. Frickey, *The Jurisprudence of Public Choice*, 65 TEX. L. REV. 873, 878 (1987) (alteration in original) (quoting DENNIS C. MUELLER, PUBLIC CHOICE 1 (1979)).

185. *Id.* (quoting Gary S. Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 Q.J. ECON. 371, 371 (1983)).

186. *Id.* at 879.



“facilitates the construction of powerful formal models” for lawmaking in general.<sup>187</sup> The theory has a “well developed and influential body of scholarship” and has been “central to several social science disciplines” for several decades.<sup>188</sup> While critics note that the theory fails to explain phenomena like why people vote at all or why legislators vote the way they do,<sup>189</sup> public choice has influenced several leading jurists, among them Judge Richard Posner and Judge Frank Easterbrook.<sup>190</sup>

Rent-seeking occurs when “individuals or groups devote resources to capturing government transfers, rather than putting them to a productive use.”<sup>191</sup> The fiscal inefficiencies of rent-seeking are represented not only in just the cost of lobbying, but also in “the inefficiency of the lobbyist-produced legislation itself.”<sup>192</sup> Economists consider rent-seeking “not justified on a cost-benefit basis: it costs the public more than it benefits the special interest, so society as a whole is worse off.”<sup>193</sup>

One concern about rent-seeking applicable to the employee-independent contractor determination is that lobbying by special interests will disadvantage workers and industries that cannot afford to lobby. “[L]obbying skews public policy away from the interests of the poor.”<sup>194</sup> It does this through the functions of collective action: “those with resources and with narrow (as opposed to diffuse) interests in particular legislation can more easily overcome collective action problems and engage in political activity such as hiring lobbyists who have easy access to elected officials and their staffs.”<sup>195</sup> The music industry’s successful effort is an example of such an effort. Not every industry that logically deserves an exemption is likely to have as much access to lawmakers as the music industry.

Finally, rent-seeking itself costs society money because of “the diversion of human and other capital away from productive activity

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187. *Id.* at 878.

188. Tom Ginsburg, *Ways of Criticizing Public Choice: The Uses of Empiricism and Theory in Legal Scholarship*, 2002 U. ILL. L. REV. 1139, 1141–43.

189. Farber & Frickey, *supra* note 184, at 893–95.

190. *Id.* at 879–80.

191. Richard L. Hasen, *Lobbying, Rent-Seeking, and the Constitution*, 64 STAN. L. REV. 191, 191 (2012).

192. *Id.* at 228–29.

193. FARBER & FRICKEY, *supra* note 183, at 34.

194. Hasen, *supra* note 191, at 226.

195. *Id.*

(such as lawyers drafting contracts) to purely redistributive activity (lobbying).”<sup>196</sup>

Therefore, reducing rent-seeking should be a priority for legislators. Less money spent on lobbying and fewer inefficient laws may help improve economic productivity.<sup>197</sup> Legislators should endeavor to draft an employment classification law that is robust and does not require continual amendments.

## 2. The Exemptions Slow Responses to Crises

Another detriment to the crystalized exemption system to California’s ABC test is that it can hurt workers and businesses during times of crisis as any relief may be delayed by the legislative process. The passage of AB 5 disrupted numerous industries like freelance journalism, where several publishers declined to work with California-based freelancers; amateur sports leagues, which stopped paying judges; trucking, where hundreds of long-haul truckers incorporated; music; and the performing arts.<sup>198</sup> Given the exemptions passed in AB 2257 targeted at those industries,<sup>199</sup> these results were not intended. But, despite the immediate threat that AB 5 posed to these industries,<sup>200</sup> it took the legislature nearly nine months to modify the law.<sup>201</sup> It is entirely possible new businesses and industries will also experience unanticipated consequences at a later point. Because of these risks, the legislature should adopt an exemption test that is robust and flexible. This would help reduce pressure on the legislature to act too quickly when critical industries are threatened.

### *B. The Conditions Underlying the Exemptions Are Just Factors Showing the Satisfaction of the ABC Test*

As currently formatted, most exemptions to the ABC test require the employer to prove that the A prong of the test, that the laborer is free from control, is met. For example, the first condition in the business-to-business contracting exemption is that the service provider “is

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196. *Id.* at 230.

197. *Id.* at 231–32.

198. *See supra* Section II.C.

199. *See* Assemb. B. 2257, 2020 Leg., 2019–2020 Reg. Sess. (Cal. 2020).

200. *See id.* In fact, the A.B. 2257 passed with an emergency bill designation, allowing it to take effect immediately. *Id.*

201. Karen Anderson, Opinion, *Even with Exemptions, AB 5 Is Still Rotten to the Core*, ORANGE CNTY. REG. (Apr. 24, 2021), <https://www.oregister.com/2021/04/24/even-with-exempt-ions-ab-5-is-still-rotten-to-the-core/> [<https://perma.cc/ZX92-69CBJ>].

free from the control and direction of the contracting business entity in connection with the performance of the work, both under the contract for the performance of the work and in fact.”<sup>202</sup> This tracks the language used by the *Dynamex* court when discussing the first prong of the ABC test.<sup>203</sup> Any facts that meet the first condition of the *Dynamex* test necessarily fulfill the A part of the ABC test. Similar language appears in the referral agency exemption,<sup>204</sup> the two individuals exemption,<sup>205</sup> the portion of the music industry exemption applying to performance artists,<sup>206</sup> and the data aggregator exemption.<sup>207</sup> And while the professional services exemption does not contain the *Dynamex* language, it still contains a condition tending to prove the A prong: that “[t]he individual customarily and regularly exercises discretion and independent judgment in the performance of the services.”<sup>208</sup>

The remaining exemptions appear particularly unique. They apply to professions that require licensure from the state or federal government (subcontractors<sup>209</sup>; doctors, lawyers, and insurance underwriters, among others<sup>210</sup>), state-authorized motor clubs,<sup>211</sup> and the music industry.<sup>212</sup>

Likewise, most of the exemptions also require that the C prong of the ABC test—that the laborer “is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed”<sup>213</sup>—is met. For example, the sixth condition for the business-to-business exemption is that the service provider is “customarily engaged in an independently established business of the same nature as that involved in the work performed.”<sup>214</sup> Any facts that meet this condition necessarily fulfill the C prong of the ABC test. Similar language appears in the referral agency

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202. CAL. LAB. CODE § 2776(a)(1) (West Supp. 2021).

203. *Dynamex Operations W., Inc. v. Superior Ct.*, 416 P.3d 1, 35 (Cal. 2018) (“[T]he worker is free from the control and direction of the hiring entity in connection with the performance of the work.”).

204. CAL. LAB. CODE § 2777(a)(1).

205. *Id.* § 2779(a)(1).

206. *Id.* § 2780(c)(1)(A).

207. *Id.* § 2782(a)(1)(A).

208. *Id.* § 2778(a)(6).

209. *Id.* § 2781.

210. *Id.* § 2783.

211. *Id.* § 2784.

212. *Id.* § 2780.

213. *Id.* § 2775(b)(1)(C).

214. *Id.* § 2776(a)(6).

exemption<sup>215</sup> and the subcontractor exemption.<sup>216</sup> While the professional services exemption does not contain that exact language, it requires a similar condition: that “[t]he individual is customarily engaged in the same type of work performed under contract with another hiring entity or holds themselves out to other potential customers as available to perform the same type of work.”<sup>217</sup> The same is true for the two-party exemption.<sup>218</sup> Again, it is the unique industries—those that require state licensure,<sup>219</sup> the music industry,<sup>220</sup> data aggregation,<sup>221</sup> and motor clubs<sup>222</sup>—that do not include the condition.

Generally, the other conditions necessary to fit an exemption are facts that would tend to show either the A or C prongs of the ABC test. For example, of the remaining ten conditions needed to meet business-to-business exemption, two tend to show that the A prong of the test is met<sup>223</sup> while six tend to show that the C prong is met.<sup>224</sup> Similar conditions appear in five of the other exemptions.<sup>225</sup>

Therefore, most of California’s statutory exemptions to the ABC test appear to be situations where parts A and C of the test are met and the legislature has chosen to exempt the industry from part B—outside the usual course of business—of the ABC test.

#### IV. A NEW FRAMEWORK

AB 5’s current framework encourages wasteful spending and advantages rich industries.<sup>226</sup> Fixes can take months to take effect.<sup>227</sup> With future changes still an open question in California and more states looking to revamp their employment laws, state legislatures seeking to address this issue should consider adopting exemption

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215. *Id.* § 2777(a)(7).

216. *Id.* § 2781(g).

217. *Id.* § 2778(a)(5).

218. *Id.* § 2779(a)(7) (“Each individual is customarily engaged in the same or similar type of work performed under the contract or each individual separately holds themselves out to other potential customers as available to perform the same type of work.”).

219. *See id.* § 2783.

220. *Id.* § 2780.

221. *Id.* § 2782.

222. *Id.* § 2784.

223. *Id.* § 2776(a)(3), (11).

224. *Id.* § 2776(a)(4)–(5), (7)–(10). The remaining two conditions require that the business not be a construction contractor, *id.* § 2776(a)(12), and that the service provider provides services to the business, not the business’s customers, *id.* § 2776(a)(2).

225. *Id.* §§ 2777, 2778, 2779, 2781, 2782.

226. *See supra* Section III.A.1.

227. *See supra* Section III.A.2.

frameworks that are flexible enough not to require continual amendment. Such a framework should include ad-hoc exemptions for work relationships that require higher education and licensure or that are especially unique in operation. It should also employ a broad exemption test that creates an exemption when prongs A and C of the ABC test are satisfied along with one of several indicia protecting the policy purposes of the ABC test. As parts of the ABC test are similar to the *Borello* test's secondary indicia,<sup>228</sup> legislatures may look to the other *Borello* factors to guide their exemptions.

#### A. Exemptions for Unique Industries and Professions Requiring Licensure

It seems unlikely that any test, no matter how well designed, can account for all situations where the legislature may want an exemption. Therefore, even a robust exemption scheme will need some categorical exemptions as determined by the legislature.

Legislatures should be careful in not providing too many of these exemptions; lest the exemptions swallow the rule. For instance, exemptions should be applied to unique industries like music production, which had historically been given “flexibility” from the common law employee test because the hiring party did not control how the laboring party did their work.<sup>229</sup> Without an exemption, these industries may not survive a shift to the ABC test. For example, musician Ari Herstand, one of the parties behind the music industry exemption in AB 2257,<sup>230</sup> criticized AB 5 for not taking into account that an individual working musician may act as an employer or employee under the ABC test more than a dozen times in just one week and that requiring them to conform to the ABC test might add thousands in costs.<sup>231</sup> Similar industries could qualify for an ad hoc exemption. Further, while these exemptions will be determined by the legislature, they would likely fulfill one of *Borello*'s secondary indicia: that “the

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228. Compare *supra* notes 87–90 and accompanying text, with Section II.A.

229. Concurrence in S. Amendments, Assemb. B. 2257, 2020 Leg., 2019–2020 Reg. Sess. at 3 (Cal. 2020) (as amended Aug. 25, 2020).

230. Andrea Domanick, *The Music Industry Gets Relief from California's AB5 Gig Economy Law*, KCRW (Apr. 21, 2020), <https://www.kcrw.com/music/articles/musicians-ab-5-gig-economy-law> [<https://perma.cc/74GD-KUD3>].

231. See Ari Herstand, *California's Music Economy Is About to Crash*, ARI'S TAKE (Nov. 20, 2019), <https://aristake.com/AB5> [<https://perma.cc/UX3D-C96P>]; Alicia Spillias, *Help Independent California Music Professionals Secure Exemption Under AB5*, CHANGE.ORG, <https://www.change.org/p/help-independent-california-music-professionals-secure-exemption-under-ab5> [<https://perma.cc/N79U-YYNN>].

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**.”<sup>232</sup> Legislatures could look at industries unique to their jurisdictions where work is done with little or no supervision to determine categorical exemptions.

Exemptions for professions that require government licensing, like lawyering, medicine, and construction, also make sense. These license requirements are connected to training and education,<sup>233</sup> and historically, independent contractors had been “entrepreneurial individuals with specialized skills that demanded higher pay on the open market.”<sup>234</sup> Because these individuals were highly educated, “legislatures rationalized that this group of laborers was not as vulnerable as their less-skilled counterparts and therefore did not need the protections of employment law.”<sup>235</sup>

### 1. A and C Prongs

Outside of the limited categorical exemptions, a general framework for exemptions should require that the employer prove that the A and C prongs of the ABC test remain fulfilled, as they appear to be the two most important parts of the ABC test.

### 2. Additional Factors

With the A and C prongs fulfilled, legislatures should allow for an exemption if the employer shows the existence of one additional indicia supporting the policy reason of the law—“prevent[ing] the common practice in many industries of a company forcing an individual to act as an independent business while the company maintains the

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232. See *supra* notes 51–52 and accompanying text.

233. See, e.g., CAL. PUB. RES. CODE § 752 (West 2015) (“‘Professional forester,’ . . . means a person who, by reason of his or her knowledge of the natural sciences, mathematics, and the principles of forestry, acquired by forestry education and experience, performs services . . .”); CAL. BUS. & PROF. CODE § 2064.5(a) (West 2019) (“[M]edical school graduates shall obtain a physician’s and surgeon’s postgraduate training license. To be considered for a postgraduate training license, the applicant . . . shall successfully pass all required licensing examinations . . .”); *id.* § 6060 (“To be certified to the Supreme Court for admission and a license to practice law, a person . . . shall: . . . [h]ave passed the general bar examination given by the examining committee.”).

234. John A. Pearce II & Jonathan P. Silva, *The Future of Independent Contractors and Their Status as Non-Employees: Moving on from a Common Law Standard*, 14 HASTINGS BUS. L.J. 1, 12–13 (2018).

235. *Id.* at 13.

right to set rates, direct work, and impose discipline”<sup>236</sup>—are fulfilled. These indicia should include:

- A written contract that specifies the payment amount and time boundaries of the work.
- A written contract that states that the laborer cannot be dismissed without penalty before completion of the work.
- A written contract that allows the contractor to work with other businesses.
- Evidence that the contractor has worked or is currently working with other businesses.
- Evidence that negotiations over the rate of pay have taken place.

### *B. A New Framework Applied*

Applying the test to a hypothetical situation illustrates how it would apply in practice. The facts of the hypothetical are: Ms. Nguyen is a pharmacist. To become a pharmacist, Ms. Nguyen attended a graduate-level pharmacy school for four years and completed more than 1,000 clinic hours. Her jurisdiction has not adopted an exemption for pharmacists. From Monday to Friday, she dispenses drugs at LLR Pharmacy. LLR pays her hourly. Customers occasionally submit reviews and Ms. Nguyen’s pay raises are based on those reviews. Occasionally, Ms. Nguyen also dispenses drugs on the weekend at Good Loyolan Hospital. She has a written contract with the hospital which states that she may accept additional work at her leisure and that she is due \$2,000 for each weekend she works at the hospital. The contract is reviewed every six months, has been revised to increase Ms. Nguyen’s rate several times, and cannot be unilaterally cancelled by the hospital. Ms. Nguyen occasionally offers to work at other hospitals in the area and has previously done so.

Here, LLR Pharmacy would not be able to prove an exemption for Ms. Nguyen. They control the details of her work, both through the scheduling and through the reviews, and therefore fail the A prong of the test. But, Good Loyolan would be able to prove an exemption for Ms. Nguyen. The hospital lacks real control of Ms. Nguyen, having to pay the same amount no matter how she accomplishes the work, therefore satisfying the A prong. Ms. Nguyen offers to dispense drugs

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236. CAL. LAB. FED’N, AFL-CIO, FACT SHEET—AB 5 (GONZALEZ): DEFEND *DYNAMEX* & REBUILD THE MIDDLE CLASS 1 (2019), [https://calaborfed.org/wp-content/uploads/2019/02/Factsheet-AB-5-Dynamex-LOBBY-DAY.final\\_-1.pdf](https://calaborfed.org/wp-content/uploads/2019/02/Factsheet-AB-5-Dynamex-LOBBY-DAY.final_-1.pdf) [<https://perma.cc/SNX6-PY27>].

at other hospitals and has previously done so, proving the exemption test's C prong. And finally, she satisfies several of the indicia: she is currently working at other businesses, has negotiated her rate, and her contract specifically states her pay and the duration of work.

### *C. Arguments Against*

While this test reduces and simplifies exemptions to the ABC test, one criticism of this test might be that even though it purports to simplify the exemptions process, adopting a new test could confuse industry and courts. Another argument against this test is that its broadness could leave businesses unaware of whether or not they fulfill the exemption.

The first argument is not persuasive. For one, because of the novelty of the ABC test, few California courts have actually applied the ABC test and its exemptions. California's attorney general did not sue Uber and Lyft for allegedly misclassifying their workers until May 2020.<sup>237</sup> Apparently, only nine cases have cited the code section that contains the ABC test as of October 2021.<sup>238</sup> No cases available on Westlaw cite the business-to-business exemption to the ABC test as of October 2021.<sup>239</sup> Therefore, adopting a new exemptions test poses little risk of confusing the courts and businesses as they have no mandatory precedent to rely on. But, even if there had been cases construing the statutes, there would be little difficulty for the courts as the new test is simpler than the old exemptions, given that they require many fewer conditions, and actually include the two most prominent conditions from the current exemptions.

The criticism that the broadness of the test can lead to industry confusion is also not persuasive. Sophisticated businesses that would have qualified under one of the old exemptions would have no issues as the facts qualifying them under the former exemptions would likely qualify them under the new standard. And while smaller businesses may have issues to start, they can be educated through California's Department of Industrial Relations. The state's 2021 budget includes \$17.5 million earmarked to hire 103.5 staffers to implement AB 5 and

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237. Press Release, State of Cal. Dep't of Just., Att'y Gen. Becerra and City Att'ys of Los Angeles, San Diego, and San Francisco Sue Uber and Lyft Alleging Worker Misclassification (May 5, 2020), <https://oag.ca.gov/news/press-releases/attorney-general-becerra-and-city-attorneys-los-angeles-san-diego-and-san> [https://perma.cc/U24Y-PV65].

238. Westlaw search for "Cal. Lab. Code § 2775" (Oct. 30, 2021).

239. Westlaw search for "Cal. Lab. Code § 2776" (Oct. 30, 2021).



“address increased investigations of worker status, wage claim filings, and workplace health and safety inspections.”<sup>240</sup> Some of that funding could be directed to educate less sophisticated businesses on the new exemption.

## V. CONCLUSION

What framework a state adopts to exempt working relationships from its underlying employment test can have wide ranging effects. If a state adopts too narrow or complicated of a test, it may disrupt long-established businesses and careers and invite wasteful lobbying. To avoid that result, California and other states considering the ABC test to determine employee status should implement a broad and flexible exemptions framework that considers the control businesses exert over their workers and whether the workers are actually operating businesses of their own in combination with other indicia supporting the policy goals of the worker protection laws of the state.

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240. DEP'T OF FIN., CALIFORNIA STATE BUDGET 2020–21: LABOR AND WORKFORCE DEVELOPMENT 2, <http://www.ebudget.ca.gov/2020-21/pdf/Enacted/GovernorsBudget/7000/7350.pdf> [<https://perma.cc/D3DS-BJ2T>].