Article

Suffering Work, a New Road to the Meaning of Employment

12.09.20

Texas Lawyer

California again leads the way in challenging norms. Its efforts to redefine the meaning of "employee" and "employment" has resulted in several other states following its lead. New Jersey, Connecticut, Delaware, Illinois, Indiana, Massachusetts, Vermont, Washington, West Virginia and Nebraska all have recently begun applying some version of California's stricter test for when a worker may legally be classified as an independent contractor rather than an employee. Excluding Washington, these states all have another common feature; they all have a state income tax. With the employer making deductions from wages, state income tax is easier to collect from employees than from independent contractors.

Some History of the Definition

One of the oldest employment laws in the United States is the Fair Labor Standards Act ("FLSA"). Signed into law on June 25, 1938, by President Franklin D. Roosevelt—along with 120 other pieces of federal legislation—the FLSA only covers employees. It does not cover contractors. The FLSA addresses federally mandated minimum wage and overtime requirements. The statute defines *employee* as "any individual employed by an employer." It defines *employ* as "to suffer or permit to work." Neither are very helpful. Most other Federal laws have different definitions and tests for defining who is an employee. An employee under the IRS definition may not be an employee for EEO laws or under OSHA. However, there are common threads in all of the statutes and regulations as to what workers are employees and what workers are contractors. Gray areas exist. Some workers are hard to put in one category or the other. However, those cases are generally the exception under existing federal laws.

Likely, the most well-known test for whether a worker is an employee came from the IRS in 1987—the 20 factor or 20 question test. As the name implies, it posed twenty questions, none of which are determinative on their own. They are:

1. Instructions: Is the worker required to comply with employer's instructions about when, where, and how to work? A contractor typically does not. 2. Training: Is training required? Does the worker receive training from or at the direction of the employer, includes attending meetings and working with experienced employees? Contractors normally do not need training. 3. Integration: Are the worker's services integrated with activities of the company? Does the success of the employer's business significantly depend upon the performance of services that the worker provides? Not so for contractors. 4. Services Rendered Personally: Is the worker required to perform the work personally? Contractors generally do not. 5. Authority to hire, supervise and pay Assistants: Does the worker have the ability to hire, supervise and pay assistants for the employer? Contractors may have their own employees. 6. Continuing Relationship: Does the worker have a continuing relationship with the employer? If so, likely an employee. 7. Set Hours of Work: Is the worker required to follow set hours of work? If so, likely an employee. 8. Full-time Work Required: Does the worker work full-time for the employer? This tends to show employment status. 9. Place of Work: Does the worker perform work on the employer's premises and use the company's office equipment? Contractors tend not to do so. 10. Sequence of Work: Does the worker perform work in a sequence set by the employer? Does the worker follow a set schedule? If so, likely an

employee. 11. Reporting Obligations: Does the worker submit regular written or oral reports to the employer? If so, likely an employee. 12. Method of Payment: How does the worker receive payments? Are there payments of regular amounts at set intervals? Employees typically receive an hourly or salary pay. 13. Payment of Business and Travel Expenses: Does the worker receive payment for business and travel expenses? If so, supports employee status. 14. Furnishing of tools and materials: Does the worker rely on the employer for tools and materials? Contractors typically provide their own tools of the trade. 15. Investment: Has the worker made an investment in the facilities or equipment used to perform services? Contractors do. 16. Risk of Loss: Is the payment made to the worker on a fixed basis regardless of profitability or loss? If so, reflects employee status as they do not suffer risk of financial loss for a job poorly done. 17. Working for more than one company at a time: Does the worker only work for one employer at a time? Contractors are typically not bound to one company. Employees typically work for one employer at a time. 18. Availability of services to the public: Are the services offered to the employer unavailable to the public? If so, reflects contractor status (generally not subject to a non-compete). Employees work for one employer, usually. 19. Right to discharge: Can the worker be fired by the employer at any time? Reflective of employment at-will. 20. Right to quit: Can the worker quit work at any time without liability? Contractors generally must give notice of termination of contract.

More recently, the 20 Factor test has been modified and shortened by the IRS to cover three general areas of inquiry. They are:

Behavioral: Does the company control or have the right to control what the worker does and how *the* worker does his or her job?

Financial: Are the business aspects of the worker's job controlled by the payer (these include things like how worker is paid, whether expenses are reimbursed, who provides tools/supplies, etc.)?

Type of Relationship: Are there written contracts or employee type benefits (i.e. pension plan, insurance, vacation pay, etc.)? Will the relationship continue and is the work performed a key aspect of the business?

Each area is then broken down into further descriptions of the nature of the relationship which indicates either employee or contractor status. It is a detailed coverage of the underlying factors to for consideration when determining the worker's classification.

The Social Security Administration ("SSA") relies on the Common Law test to determine who is an employee. The issue of determining coverage for social security purposes—a very big and costly deal—was first addressed in 1950. The SSA's website presents a very good overview with Questions & Answers on that history. It is very similar to the themes that flow through the IRS 20 Factor test and its more recent Behavioral Control test.

In 1992, the United States Supreme Court entered the workers' classification fray deciding *Nationwide Mutual Ins. Co, v. Darden*, where it applied the Common Law Right to Control test for ERISA and federal anti-discrimination statutes. In *Darden*, the Court relied on old common law agency and master/servant doctrines applied to the question of when masters (employers) should be held liable for the wrongdoing of their servants (employees). Many of the elements in *Darden* also lined up with those in the 20 Factor and Common Law tests.

So, Why all the Current Commotion and Change?

Enter the gig economy, where the internet and electronic applications rule the day. Where you "hire" Uber drivers who show up at your curbside with the click of your phone. Where there are workers who provide services without ever meeting face to face with a supervisor, workers without a defined work schedule, workers who have no well-defined standards of behavior, no dress code, no holidays, no vacations, and no workplace to report to for duty. Traditional rules of the employer/employee relationship simply do not apply.

For companies with such contractors, they are cheaper labor. Contractors are not paid health, welfare or retirement benefits, no vacation or sick leave, no matching taxes, no unemployment taxes, no claims for discrimination, no immigration compliance, no workers compensation premiums or claims, no health and safety protections. Independent contractors cost much less than employees do.

Working as a contractor typically means no mandated work schedule, no supervisor, no annoying rules or personnel policy manuals, no training sessions or yearly benefit forms to fill out. If a contractor is being paid $5,000.00 a month. The monthly check is for $5,000.00. Come tax time, however, a contractor pays the full amount of all taxes including social security and income tax. In addition, there are no fringe benefits as a contractor. Contractors are on their own. In this time of COVID-19, they have no access to unemployment compensation, sick days and other benefits, even if they are deemed "essential" workers.

Enter the Government—Let the Casting Begin.

The State of California has most recently lead the charge on redefining the status of workers. In short, its goal is to cast a broad net to define most workers as employees. The stated reasoning is to provide workers with the above listed benefits—health insurance, workers compensation, protections against discrimination and, a working wage. Another reason is that the State of California assuredly takes in more tax dollars on employees than from contractors. Like the companies' interests, money talks. Tax revenue moves federal, state and local governments to take actions to maximize income. From a different angle, contractors are cheaper (from a tax collection perspective) than employees. California benefits financially by casting a wider net on defining workers as employees. This has led the Golden State down a winding road through the courts, its legislature and most recently through California voters casting ballots on who is and who is not an employee.

The epicenter of the worker classification issue in California has been on drivers, in the ridesharing, food delivery and general delivery industries. Uber and Lyft have been front and center. As is widely recognized, however, the driver industry is the tip of the net being cast by California. The initial salvo on the issue was lawsuits filed by the California Attorney General's office seeking the reclassification of drivers as employees (and seeking associated back taxes and damages on wage claims). The California Attorney General's office or private attorneys bringing wage claims on behalf of the AG's office sued various companies providing transportation and delivery services. That litigation ended with a decision by the California Supreme Court in *Dynamex Operations West, Inc. v. Superior Court*, 4 Cal. 5th 903 (Cal. 2018). It established the so-called ABC test for determining a worker's status as an employee or contractor. In short, the test placed the burden of proof on the company to show that the worker:

1. Is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract of performance and in fact;
2. Performs work that is outside the usual course of the firing entity's business; and
3. Is customarily engaged in independently established trade, occupation or business of the same nature as the work performed.

Most but not all commentators panned the new ABC test, particularly parts B and C, as a drastic change that could force hundreds of thousands of contractors into employee status, along with the attendant cost and administrative issues for their newfound employers. The new ABC test was immediately followed up by the California legislature codifying the test—the now infamous Assembly Bill No. 5 (AB-5). With that, the court created legal standard was signed into law by Governor Newsome in September 2019 and took effect on January 1, 2020.

Enter Democracy (and Big Corporate Money)

The new law in California encompassed all workers in the state but initially began with a focus on the ride share and related delivery industries. Uber and Lyft had vigorously defended against the initial litigation and then the

legislative process in codifying the high court's ABC standard. Suffering losses in both branches, these industries took the issue to the people of California seeking their support on a state referendum narrowing the issue—whether ride share and delivery drivers should be excluded from AB-5's scope and continue to be classified as contractors. More than Two Hundred Million Dollars later, money spent by Uber, Lyft, Doordash, Instacart and Postmates, among others, to promote passage of California Proposition 22; a referendum named the Exempt App-Based Transportation and Delivery Companies from Providing Employee Benefits to Certain Drivers. On November 3, 2020, the citizens of California voted to pass the measure and allow the ride share and delivery drivers to remain contractors. Under California's most expensive ballot proposition in history, what was once an employee (ever so briefly), was now back to being an independent contractor.

Although Proposition 22 modified the AB-5 statute, the law remains in place for all other contractors and companies. In particular, the law has a significant impact on those involved in the gig economy in California, where contractors provide services that are at the heart of the particular business model (See Part B of the ABC test, above). The law covers all entities that use contractors—from sole proprietors to high tech companies and brick and mortar businesses. The law remains a very big deal. Consider some of the other gig-economy service providers. For example, there are tens of thousands of service providers that do not provide transportation. There are home services providers, legal service providers, short-term health care providers, technical service providers and a myriad of other service providers who set up brief service relationships via the internet. Most all of these companies rely on work and services from independent contractors—lots of independent contractors. They all remain under the relatively new ABC legal test.

Where Will it End?

Approximately 10 other states continue to apply some form of the ABC test. The immediate impact on workers and those that pay them will undoubtedly be significant. The ultimate response to the new standards may also bring great change. States like Texas and Florida, with no income tax and who have not meddled with the definition of employee, will most certainly benefit with an influx of both companies and workers. Time will tell.

The simple answer to the question of where this issue will land is that it will not land with any permanence. The state and federal government's mostly unstated desire to collect more taxes and the commendable effort to provide working people with more protections and benefits will continue to push current standards towards broadening the net towards capturing more workers as employees. The business world's financial interests will push back seeking continued applications of the generally known classification standards, which have been applied for decades (and keeps the government's tax revenue collecting net from growing). On a macro scale, states like California will push the boundaries of the worker status definition to meet their financial and social desires. The impact of those changes will have consequences. Businesses and workers will react to the changes. The immediate trend has been for companies to begin abandoning the states and moving to more employer friendly locations like Texas. However, it is hard to ignore the beauty of the Golden State and its 45 million consumer-spending residents. Where the issue will ultimately go, and the impact on its constituents, is firmly secured in today's tea leaves.

The full article can also be viewed here.

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