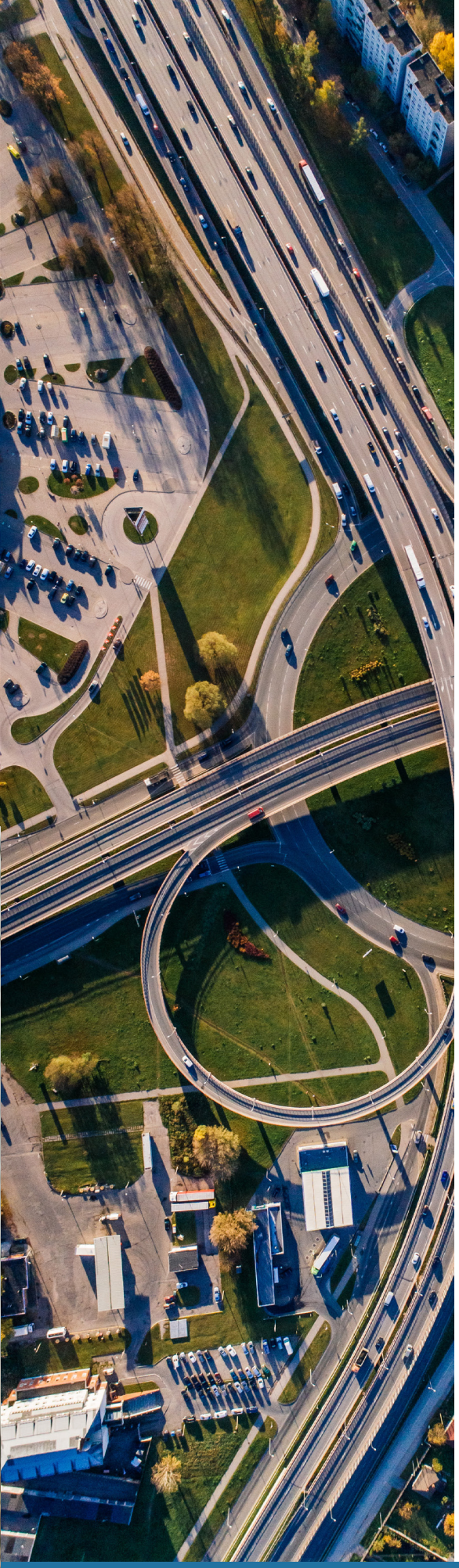


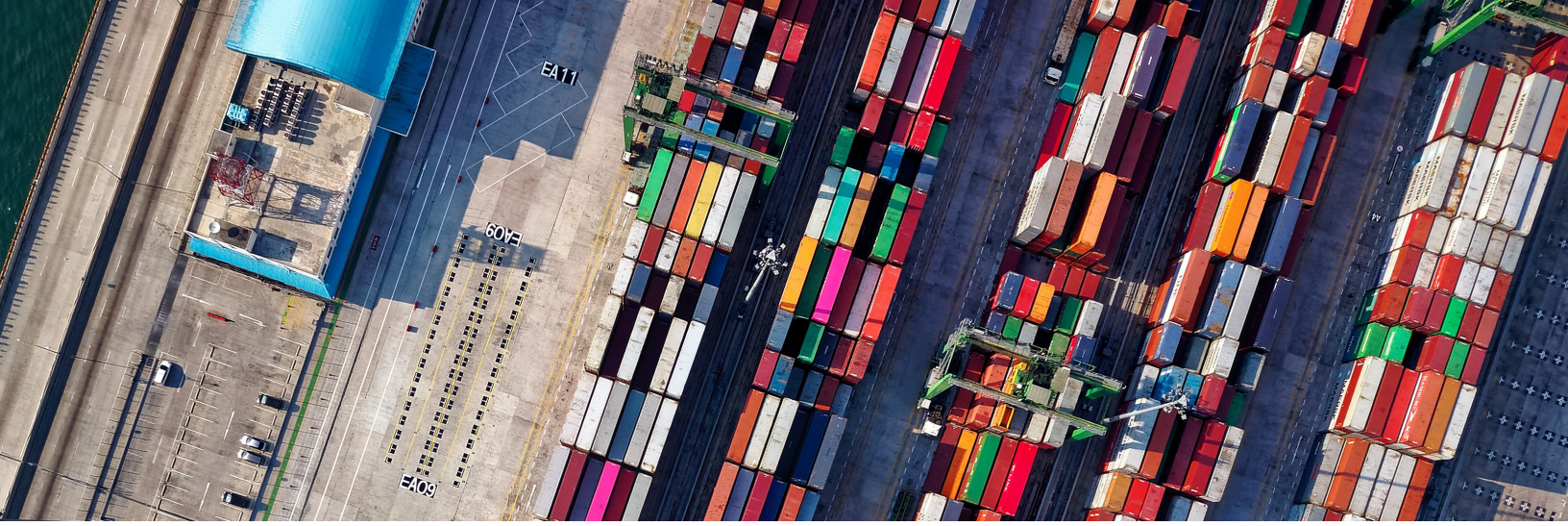
States Abusing Independent Contractor Models

BY LESESNE PHILIPS

Over the past decade, certain states have ramped up scrutiny of the independent contractor model. New York, New Jersey, and California, to name a few, enacted legislation to severely limit the ability of employers to hire independent contractors. These laws, commonly referred to as "ABC" tests, determine whether an independent contractor should be classified as an employee. This standard was established in California through a landmark California Supreme Court case, Dynamex Operations West Inc. v. Superior Court. This case provided the presumption of an employee unless these three provisions could be met to prove independent contractor status: (a) the person is free from control of the hiring entity; (b) the service is performed outside the usual course of business of the hiring entity; and (c) the person is engaged in an independent business or trade of the same nature as the work that is performed. The test's second requirement makes designation of an independent contractor particularly difficult for motor carriers, creating a virtually impossible presumption to overcome because the owner operator hauls freight just like the motor carrier. In fact, he is hired to do precisely what the motor carrier does but on a contractor basis.

In 2014, New York enacted legislation specifically directed at the motor carrier industry. On January 10, 2014, Governor Cuomo signed into law the New York State Commercial Goods Transportation Industry Fair Play Act, effective April 10, 2014. The law created the presumption that a person performing services for a commercial goods transportation contractor is an employee unless it is demonstrated that the person is an independent contractor or a separate business entity. In order to show that the owner-operator is a legal independent contractor, their compensation must be reported on a Federal Income Tax Form 1099 and they must qualify as a separate business entity or pass the ABC test. Even if the hiring motor carrier and the owner-operator agree that the owner-operator is to be treated as an independent contractor, there is still an employee presumption. As shown above, the ABC test virtually eliminates the ability for owner-operators to be classified as independent contractors due to Prong B. The other option is to qualify as a separate business entity, which requires satisfying an 11-part test where all of the parts must be met. Those qualifications are as follows:

1. The owner-operator must be free to determine its own means and manner of providing services, limited by the requirements to meet the desired result or federal rule or regulation;
2. The owner-operator exists without the relationship to the hiring entity;



3. The owner-operator has substantial investment in the business entity beyond ordinary tools and equipment;
4. The owner-operator owns or leases the capital goods and bears the risk of loss and profit;
5. The owner-operator can perform services to the general public on a continuing basis;
6. The owner-operator provides services reported on a 1099;
7. There is a written contract between the owner-operator and the hiring motor carrier specifying the independent contractor relationship or separate business entities;
8. The owner-operator pays for required licenses or permits under its own name, or if allowed by law, pays for reasonable use of the hiring motor carrier's license or permit;
9. The owner-operator may hire its own employees without the hiring motor carrier's approval, and the owner-operator pays its employees directly without reimbursement from the hiring motor carrier;
10. The owner-operator is not required to present itself as an employee of the hiring motor carrier to the hiring motor carrier's customers; and
11. The owner-operator is free to perform similar services for others at any time and however it chooses.

Despite an owner-operator's potential ability to fit within this test, the presumption of an employee makes the future of owner-operators as independent contractors in New York unclear. Additionally, this law provides civil penalties in the amount of an initial $1,500 penalty for a first time violation and then a $5,000 penalty for each additional violation. Willful violations of the law can result in criminal penalties and an increased monetary penalty for those employers that misclassify an employee as an independent contractor. The state of New Jersey also has pending legislation that is similar to the recent bill passed in California discussed below.

Despite all of this, hope is coming. Recently, California codified the "ABC" test held in the Dynamex Operations case through Assembly Bill 5 (AB 5). A lawsuit, filed by the California Trucking Association (CTA), seeks to prevent the application of the "ABC" test to owner-operators as well as challenging California's AB 5 law. The cases are California Trucking Association v. Attorney General Xavier Becerra and California v. Cal Cartage Transportation Express LLC. On December 31, 2019, U.S. District Judge Roger Benitez, following the path trod by the court in Massachusetts Delivery Assoc. v. Coakley (1st Cir. 2014), issued an injunction in the California Trucking Association Case in favor of the CTA, ruling that the Federal Aviation Administration Authorization Act of 1994 (FAAAA), 49 USC 14501(c), preempts AB 5's B prong due to AB 5 essentially requiring motor carriers to treat owner-operators as employees. The FAAAA prevents the economic regulation by the states of motor carriers. The second case comes from the State of California suing Cal Cartage Transportation Express LLC. The judge in that case also provided a ruling relying on the FAAAA as preempting the states from regulating motor carrier services. These cases will likely determine how California treats owner-operators. If the Courts ultimately find that owner-operators must conform with AB 5, then there are potential consequences including fines and criminal penalties that could result in misclassifying owner-operators as independent contractors instead of employees. And motor carriers will have to switch to an all employee fleet or transition their independent contractor work to brokerage operations. As California remains one of the leaders in this area, these cases will likely have effects on how other states view their employee misclassification laws in the context of owner-operators.