BLOGS
Legislation and Rulemaking

California Legislature Passes AB-5

Making major changes to employment law in California, AB-5 codifies the holding in *Dynamex Operations West, Inc. v. Superior Court*, which established the so-called "ABC test" for determining whether a worker is an "employee" or an "independent contractor" in California. The ABC test creates a rebuttable presumption that a worker who performs services for hire in exchange for remuneration is an employee, unless the hiring entity can demonstrate that: (a) the individual is free from the control and direction of the hiring entity in connection with the performance of the work, both in practice and on paper; (b) the individual performs work that is outside the usual course of the hiring entity's business; and (c) the individual is customarily engaged in an independently established trade, occupation, or business. If an individual is determined to be an "employee" under AB-5, then the California Labor Code, Unemployment Insurance Code, and California Industrial Welfare Commission Wage Orders apply to that individual. California AB-5 will take effect on January 1, 2020.

AB-5 ostensibly applies to companies like Uber, Lyft, and other businesses engaged in the "gig economy," not franchising. However, the passage of AB-5 is particularly concerning to franchisors because in May 2019 one California court used the ABC test to come very close to concluding that a franchisor was the employer of its franchisees in *Vazquez v. Jan-Pro Franchising International, Inc*. The outcome in Vazquez may ultimately be a result of the structure of the Jan-Pro system, where most franchisees are individual owner-operators performing janitorial services contracts executed between a master franchisee and the client, rather than between the franchisee and the client.

Regardless, all three prongs of the ABC test could be problematic for most franchise structures. As for the first prong, the franchisor's obligation to protect its trademarks in the form of operating procedures and brand standards could be cited as evidence of control over the performance of a franchisee's work. With regard to the second prong, the franchisor's advertising and uniform promotion of the brand and marks could be viewed as evidence that the franchisor and its franchisees are engaged in the same type of business. Further, franchisors with company-owned units will have difficulty satisfying the second prong because the company-owned units engage in the exact same business as the franchised units. A franchisor must satisfy all three prongs to avoid having its franchisees classified as employees. However, the ABC test is not new and has been used in the context of different employment law regulatory schemes in several states — including

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