



As we reported last year, [state government agencies are increasingly scrutinizing the distinction between “employee” and “independent contractor” classifications.](#)¹ On August 10th, 2020, the California Superior Court in *California v. Uber Technologies Inc. and Lyft Inc.*, dealt an early blow to the “gig industry” in California when it granted a preliminary injunction, ordering Uber and Lyft to designate their drivers as employees, rather than independent contractors, in order to comply with Assembly Bill 5.² The judge put the injunction’s effective date on pause for 10 days –allowing time for Uber or Lyft to appeal the decision. The ultimate outcome of the dispute could have an impact on similar pending cases involving other gig giants, including DoorDash Inc. and Instacart.

Uber’s Drive to Stop California’s New Employee Classification Takes a Wrong Turn

By Mary Lundstedt, Esq. & Justin Liberatore

Why is Employment Classification Important?

The correct employment classification dictates whether the hiring entity is responsible for employment tax and income withholding, deposit, and reporting obligations. Furthermore, gig workers who are reclassified as employees are subsequently entitled to overtime, minimum wage, health care and have rights in cases involving wage claims, insurance, and compliance with employment laws and ordinances.

How the IRS and California Determine Employment Classification

According to the Internal Revenue Service (IRS), a common-law employee is defined in terms of the ability to control performance. Thus, generally, an employer-employee relationship:

*“exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished.”*³

Ultimately, the determination requires an examination of the facts and circumstances of each case. The IRS also considers twenty (20) common law factors useful in helping to make this determination.⁴

California’s Assembly Bill 5 codifies what is commonly referred to as California’s “ABC Test,” which was established in *Dynamex Operations West Inc. v. Superior Court of Los Angeles*.⁵ The ABC Test presumes that all workers are employees, rather than independent contractors, unless the hiring entity can show that the worker:

1. is free from control by their hiring entity,
2. performs services outside of their hiring entity’s usual course of business, and
3. is customarily engaged in an independently established business, which is similar to the work performed for the hiring entity.

Uber and Lyft: Buying Time?

Uber and Lyft have maintained that as technology companies, they are not responsible for the drivers, as they create an app allowing drivers to choose when and where to work, and simply connect riders to drivers as a technology company. And both companies' Presidents have clearly expressed that, in light of the injunction, the companies may be forced to temporarily shut down.⁶

With a California ballot measure up for vote in November which, if passed, would exempt app-based companies (such as Uber and Lyft) from the ABC Test, it appears that Uber and Lyft are doing everything they can to further pause the injunction until the appeals process has run its course. And their warning that services may be temporarily shut down, is almost certainly intended to motivate the public opinion to favor their position. In the event that California voters fail to side with the gig giants, Uber and Lyft may very well keep appealing for as long as possible.

Conclusion

Uber, Lyft and other similar ride-hailing businesses have already suffered huge losses given the COVID-19 travel restrictions, and

now they are facing lasting costly effects if they lose the employee classification battle. Although this is a California case, and an early strike against Uber and Lyft since the implementation of the ABC Test, the final outcome is likely to impact various other employers who use independent contractors in California—and perhaps even serve as a useful model for other states grappling with the same controversy.

If you have employees classified as contractors, contact the Frost Law team at 410-862-2834 or fill out our [online form](#) for any questions.

Footnotes

1. [Expanding “Gig Economy” Redefining Employee Classification](#)
2. Docket No. CGC20584402 (Cal. Super. Ct. Jun 15, 2020).
3. Reg. §31.3121(d)-1(c)(2).
4. Rev. Rul. 87-41, 1987-1 C.B. 296. See also Independent Contractor or Employee? Training Materials, IRS Training Course 3320-102, TPDS 842381 (Mar. 4, 1997).
5. No. S222732 (Cal. Sup. Ct. Apr. 30, 2018).
6. Sara Ashely O'Brien, Uber and Lyft could shut down in California this week. It may not help their cause, CNN (Aug. 16, 2020 11:21 AM), <https://www.cnn.com/2020/08/16/tech/uber-lyft-california-suspension/index.html>.

Additional Resources



President's Payroll Tax Memorandum Creates Temporary Deferral; Leaves Taxpayers with Uncertainty

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