

California Assembly Bill 5 (AB5)

What Is California Assembly Bill 5 (AB5)?

[California Assembly Bill 5 \(AB5\)](#), popularly known as the “[gig worker](#) bill,” is a piece of legislation signed into law by Governor Gavin Newsom in September 2019. Scheduled to go into effect on Jan. 1, 2020, it will require companies that hire [independent contractors](#) to reclassify them as employees, with a few exceptions. The bill expands on a ruling made in a case that reached the California Supreme Court in 2018, *Dynamex Operations West, Inc. vs. Superior Court of Los Angeles*.

KEY TAKEAWAYS

- California Assembly Bill 5 (AB5) extends employee classification status to gig workers.
- Companies must use a three-pronged test to prove workers are independent contractors, not employees.
- AB5 is designed to regulate companies that hire gig workers in large numbers, such as Uber, Lyft, and DoorDash.

Understanding California Assembly Bill 5 (AB5)

In the 2018 *Dynamex* case, the California Supreme Court ruled that companies must use a three-pronged test in determining whether to classify workers as employees or independent contractors. This test assumes that workers are employees unless the company that hires them can prove the following three things.

1. The worker is free to perform services without the control or direction of the company.
2. The worker is performing work tasks that are outside the usual course of the company’s business activities.
3. The worker is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed.

This test holds companies to a higher standard in proving workers are independent contractors than was previously used in California. AB5 makes this

test the new gold standard requirement for companies that hire workers in the state of California.

Advantages and Disadvantages of AB5 for Workers

The most immediate implication of AB5 and its one-two-three test is that it turns independent contractors into employees. “The key factor for gig companies is ‘2,’ which says that anyone performing work for a company that is the same as the business of that company is presumed to be an employee,” says Danielle Lackey, chief legal officer at [Motus](#), which provides reimbursement solutions for businesses with mobile-enabled workforces.

Lackey says that, under the new bill, if employers begin classifying gig workers as employees, it means these workers will be entitled to a minimum wage, expense reimbursements, employee benefits, rest breaks, and the other benefits afforded to employees under California state law. In that sense, the bill creates a level playing field between those working in the gig economy and those hired as regular employees.

There are potential downsides, however, if gig workers who are treated as employees are, because of this, expected to adhere to a new set of standards regarding how they perform their work. For example, one major appeal of being a driver for a ride-sharing or delivery company is the ability to choose when and when not to work.

As an employee, a former gig worker may lose that choice. “Certain people are very attracted to this type of work and flexibility and will most likely drop out, as they may not like fixed schedules or other rules and requirements,” says Elliot Dinkin, president and CEO of [Cowden Associates](#), a Pittsburgh-based consulting and actuarial firm. “It has seemingly been a very popular job, based solely on the numbers of drivers.”

Lackey says the new law doesn’t mandate the elimination of flexibility altogether. “But if employers begin incurring [the greater cost of paying for employees](#) instead of contractors, they may decide to take advantage of the ability this gives them to exert more control.”

Advantages and Disadvantages of AB5 for Companies

The signing of California AB5 into law affects many, but not all, businesses that rely on gig workers in California. More than 50 professions and types of businesses are exempt, including insurance agents, attorneys, real estate agents, and certain types of business-to-business contractors and referral agencies. Companies that are not exempt will have to take a closer look at how they classify employees and independent contractors to ensure that they're not violating the terms of the bill.

For companies that do reclassify gig workers as employees, the question of how easy the transition will be centers on cost. If companies now have to pay a minimum wage, offer paid time off and health insurance, and pay unemployment insurance and worker's compensation benefits for this new crop of employees, that could have a significant impact on the bottom line.

AB5 puts ride-sharing and delivery companies, such as Uber, Lyft, and DoorDash, in the spotlight. Uber and Lyft have both vowed to fight the bill. At least one report suggests that the cost of reclassifying gig workers as employees could potentially bankrupt both companies, destroying the gig worker business model in the process. Dinkin says that if these types of companies want to preserve their profit position, then the additional costs of reclassifying will likely be passed on to the consumers who use their services.

Special Considerations of AB5

As the controversy surrounding AB5 continues, gig workers and companies that hire them in other states should pay close attention to the bill's reception. The state of Illinois has already passed legislation that mirrors the guidelines established by AB5. In the state of New York, plans are in the works to introduce legislation that would protect gig workers on a similar scale. If the trend continues to spread, [it could create widespread disruption within the gig economy](#). At the same time, consumers should be paying attention to what it could mean from a cost perspective if the prices of goods and services offered by companies that use gig workers increase.

