In Big Loss For Gig Companies, 9th Circuit Says Dynamex And ABC Test Should Be Applied Retroactively

Insights
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There's no way to sugarcoat this one. Today the 9th Circuit handed a big loss to gig economy companies by concluding that last year's *Dynamex* decision from the California Supreme Court and its wide-reaching ABC test should be applied retroactively. That means that the ABC test – which makes it very difficult for gig economy businesses to properly classify their workers as independent contractors rather than employees – will be applied to federal cases when evaluating relationships that businesses thought were to be adjudged under a much more flexible standard.

Brief Background On How We Got Here

Rewind back to April 2018 when the California Supreme Court sent shockwaves through the gig economy industry (and the business community generally) by adopting the notorious "ABC" test in *Dynamex v. Superior Court*. The court scrapped the flexible legal test used since 1989 to determine whether a worker was an independent contractor or employee and installed a rigid three-pronged test that soon appeared in the nightmares of your average gig economy business executives. The new test announced that the burden is now on the business to demonstrate that every worker is not an employee by proving all three of these elements:

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

Prongs B and C were immediately viewed as especially troublesome for your average gig economy business, and business scrambled to comply with the ruling. But at the same time, they noted that they had been living in a world where the flexible test had been applied for decades, and constructed their business models and operated their businesses in reliance upon that test before the rug got pulled out from under them. It wasn't fair, they said, to face legal liability for alleged misclassification under a new and different test when they had been operating under the assumption that complying with the then-existing test was the right thing to do.

Companies Argue "No Retroactivity"

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To counter this perceived unfairness, many businesses that had already been caught up in legal battles over misclassification argued that *Dynamex* and the ABC test should not be applied retroactively. A good example is the legal arguments raised in the *Lawson v. Grubhub* case, the nation's very first gig economy case to reach a judicial merits determination at trial. Although Grubhub won at trial when a federal court judge concluded that the delivery driver in question was properly classified as an independent contractor, that decision came just weeks before the *Dynamex* decision came down. Once the new test was announced, the plaintiff argued that the ABC test should be retroactively applied on appeal, and that appeal is still pending.

In response, Grubhub argued that the old test should be applied in order to comport with "basic principles of fairness and due process." It characterized the ABC test as "a new legal standard not announced until years after the parties ended their relationship, and months after trial concluded"—indeed, "a tectonic shift in California law, completely unforeseen by the parties and the courts." Grubhub relied on a 2004 state appellate case for the proposition that "courts [should] generally decline to apply a decision retroactively when a judicial decision changes a settled rule on which the parties below have relied." And, of course, it pointed out that it reasonably relied on the longstanding flexible standard when contracting with the plaintiff, classifying him as a contractor, and litigating the case to trial. In fact, it pointed out, the trial court acknowledged that the company wrote its independent contractor agreement with that flexible test in mind, amply demonstrating its reasonable reliance. Because *Dynamex* radically altered the legal landscape by introducing a substantive change in established law—which the plaintiff himself contended over and over again in his opening brief—it would be unfair to hold the company to that standard in this particular case.

Federal Appeals Court: *Dynamex* Should Be Applied Retroactively

Today, the 9th Circuit Court of Appeals rejected the call from businesses to apply *Dynamex* only on a go-forward basis, clearing the way for retroactive application of the new standard and creating headaches in the gig economy industry (and for just about any business that utilizes contract labor). In a longstanding misclassification battle against a janitorial franchising operation, the appeals court ruled in favor of the workers and concluded that the ABC test should be applied to the case that has been ongoing since 2008. The business argued that several justifications existed to reject retroactive application: its long-standing reliance on the former misclassification standard; the fact that the changes was substantive in nature; and overall effect the change would have on the fair administration of justice.

The court had none of it. It noted:

- The California Supreme Court rejected the chance to re-hear the *Dynamex* case after the parties had explicitly called for it to rule on the retroactivity question. "By denying the petition, even without comment, the court strongly suggested that the usual retroactive application, rather than the exception, should apply to its newly announced rule," the 9th Circuit said. "To be sure, a denial of a request for clarification is not a holding on the merits. But in an unusual case such as

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this, it is a data point for us to consider in light of California's general tradition that judicial pronouncements have retroactive effect."

- The new test "remains faithful" to the fundamental nature of California's wage and hours law, which is to remedy the problem of workers not being paid the amount to which they are entitled. It said that such remedial legislation must be liberally construed in a manner that services its remedial purpose.
- Most shockingly, the 9th Circuit said that the adoption of the ABC test was a "clarification rather than a departure from established law."

What Does This Mean?

In a nutshell, this is just about the worst news that gig economy companies could have heard about the ABC test. For the optimists out there, there are still a few chances to snatch a victory from the jaws of defeat. Perhaps this case will be heard by a full panel of the 9th Circuit and overturned (though unlikely), or even accepted by the U.S. Supreme Court and reversed (even more unlikely). Perhaps the California Supreme Court will decide that it needs to weigh in and finally issue a clear pronouncement about this standard and rebuke the 9th Circuit (doubtful). Or perhaps the California legislature will pass a law scrapping the ABC test altogether (uphill battle). But all of those outcomes seem unlikely at this point, meaning that you should probably adjust to the new reality sooner rather than later. We recommend that you consult with your legal counsel as soon as possible to discuss business formation and contractor classification under the ABC test, and the risks and exposure that have been opened up given the possibility that you could face retroactive enforcement of a new standard to any past classification structure you had in place.

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