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AB-5 Trucking Compliance in 2025 What California Construction Companies Need to Know

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Disclaimer



This seminar and its accompanying materials are an educational update concerning an important issue affecting the construction industry. Nothing herein should be construed as legal advice. Always contact your attorney if you have require legal advice or have questions.



Key Questions That We Will Address



- Background & Legislative History
 - Sunset of the Construction Exemption
- Consequences of Misclassification
- AB 5 & Teamsters Signatories
- What options do contractors have?
- Dealing with Owners / Agencies
- Dealing with GCs
- Dealing with Subcontractors



Background & Legislative History



- In 2019, AB 5 codified the *Dynamex* decision, which shifted the burden to “the hiring entity” to determine whether an individual is an independent contractor versus an employee.
- Before AB 5 passed industry successfully negotiated two critical concessions:
 - (1) the elimination of potential liability accrued under the *Dynamex* decision prior to the signing of AB 5, saving contractors hundreds of millions of potential liability – without it many construction companies would not be in business today; and
 - (2) an exemption of AB 5 with “safe harbor” provisions (see *Labor Code* § 2781(h)(5)) for the construction industry, thus providing some relief to this drastic change in the law.



Background & Legislative History



- **However, these concessions came at a price: the AB 5 construction exemption would sunset on January 1, 2025.**
 - Prior to the CTE expiration, industry associations, led by AGC and UCON, joined forces to engage with the Building Trades and eventually the Teamsters to negotiate an extension to the sunset. Some of the industry's most influential contractors, experienced bargainers, and expert attorneys combined forces with the singular focus of protecting the construction industry.
 - Notwithstanding months of negotiations and exhaustive efforts at and away from the negotiations table, an agreement to extend the sunset could not be reached.



AB-5 and the ABC Test



High-Level Summary



- AB-5 codified the ABC test following Supreme Court decision in *Dynamex Operations West, Inc. v. Superior Court*, 4 Cal.5th 903 (2018)
- Presumes a worker is an employee unless a hiring entity satisfies the three-factor test.
- The ABC test replaces the multi-factor *Borello* test and applies to the Wage Orders **and** to the Labor Code and Unemployment Insurance Code (UIC) when a definition of employee is not otherwise provided.
- Exempts certain occupations from the application of ABC test and instead applies, for these occupations, the definition of an employee set forth in *Borello*.



What Is The ABC Test?



When determining whether a worker is an independent contractor, the *hiring entity* must prove **each factor** in the ABC test:

- A. Is the worker free from the control and direction of the hiring entity in the performance of the work, both under the contract for the performance of the work and in fact? **and**
- B. Does the worker perform work that is outside the usual course of business of the hiring entity? **and**
- C. Is the worker customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed for the hiring entity?



THE CHALLENGE



- There is a **shortage of trucking companies** with sufficient employee drivers.
- **Most contractors are not in a position to hire drivers as employees**
- Workers who were not paid wages owed to them as employees often can sue not only the company with whom they did business, but also other parties:
 - **On public projects**, unpaid workers can sue the surety on the project payment bond.
 - **On private projects**, unpaid workers can sue the general contractor even if the workers were hired by a subcontractor or lower tier subcontract. Labor Code § 218.7.
 - **Unpaid workers** can also serve stop notices, and on private jobs, can record mechanic's liens.



CONSEQUENCES



- Full panoply of minimum labor protections available under wage orders and Labor Code:
 - Minimum wage, overtime, meal and rest periods, reimbursement for expenses, timely and accurate payment of wages, including final wages, compliant itemized wage statements, etc.
- Payroll Tax and Workers Compensation Audits
- Prime Contractor Joint Liability for Prevailing Wage and Apprentice Violations
- Prime Contractor Joint Liability for Private Works (Labor Code 218.7)



CONSEQUENCES (Cont'd)



- Civil Penalties (PAGA) and Criminal Penalties
 - For underlying Labor Code and Wage Order violations.
 - Labor Code § 226.8 imposes penalties of up to \$25,000 per violation if there is a pattern of “willful misclassification” of employees as independent contractors.
- Labor Code § 2753 states: “A person who, for money or other valuable consideration, knowingly advises an employer to treat an individual as an independent contractor to avoid employee status for that *individual shall be jointly and severally liable with the employer* if the individual is found not to be an independent contractor.”
 - Exception only for attorneys, not accountants, consultants, managers, etc.



Additional Considerations: Teamsters Signatories



- Contractors that are signatory to the Teamsters anywhere in California may have different and additional considerations with AB 5.
 - For example, the use of an “owner-operator” as a sub must take on considerations of both AB 5 and the applicable Teamsters’ collective bargaining agreement
 - Since each contractor’s situation is unique, it is advisable to immediately reach out to your association representative and your legal counsel on how to best maintain an independent contractor relationship with such owner-operators.



Enforcement



An action for **injunctive relief** to prevent the continued misclassification of employees as independent contractors may be prosecuted against the putative employer in a court of competent jurisdiction by:

- the Attorney General;
- a city attorney of a city having a population in excess of 750,000;
- a city attorney in a city and county, with the consent of the district attorney; or
- a city prosecutor in a city having a full-time city prosecutor in the name of the people of the State of California upon their own complaint or upon the complaint of a board, officer, person, corporation, or association.



What options do contractors have?



- Business-to-Business Exception
- Use Bona Fide Brokers
- Use Material Haulers with Employee Drivers
- Reform Compensation System to Reduce Damage Exposure



PRELIMINARY RECOMMENDATIONS



Given the expiration of the construction trucking safe harbor exception, consider the following:

1. If your company is directly hiring individual drivers or truckers, hire and pay them as employees of your company;
2. If you are contracting with a company for trucking services, make sure that the company pays drivers as employees and include provisions in your contract with the company that requires compliances with all laws, including wage and hour laws.
3. Do business with established and well-run trucking companies. Don't use a trucker who shows up at the job site uninvited because it has heard there might be work.

Beyond these high-level recommendations, there are other recommendations explored in greater detail below.



Business-to-Business Exception – LC § 2776



1. The business service provider is **free from the control and direction of the contracting business entity** in connection with the performance of the work, **both under the contract** for the performance of the work **and in fact**.
2. The business service provider is **providing services directly to the contracting business rather than to customers of the contracting business**. This subparagraph does not apply if the business service provider's employees are solely performing the services under the contract under the name of the business service provider and the business service provider regularly contracts with other businesses.
3. The **contract** with the business service provider **is in writing and specifies the payment amount**, including any applicable rate of pay, for services to be performed, **as well as the due date of payment for such services**.
4. If the work is performed in a jurisdiction that requires the business service provider to have a business license or business tax registration, **the business service provider has the required business license or business tax registration**.



Business-to-Business Exception – LC § 2776



5. The business service provider ***maintains a business location***, which ***may include the business service provider's residence***, that is ***separate from the business or work location of the contracting business***.
6. The business service provider is ***customarily engaged in an independently established business of the same nature*** as that involved in the work performed.
7. The business service provider ***can contract with other businesses to provide the same or similar services*** and maintain a clientele without restrictions from the hiring entity.
8. The business service provider ***advertises and holds itself out to the public as available to provide the same or similar services***.

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Business-to-Business Exception – LC § 2776



9. Consistent with the nature of the work, the business service provider ***provides its own tools, vehicles, and equipment to perform the services***, not including any proprietary materials that may be necessary to perform the services under the contract.
10. The business service provider ***can negotiate its own rates***.
11. Consistent with the nature of the work, the business service provider can ***set its own hours and location of work***.
12. The business service provider is ***not performing the type of work for which a license from the Contractors' State License Board is required***, pursuant to Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code.



Business-to-Business Exception – LC § 2776



- The entity performing the work must be formed as a sole proprietorship, limited liability company, limited liability partnership, or corporation.
- This exemption does not apply to an individual worker, as opposed to a business entity, who performs labor or services for a contracting business.
- **Remains untested in construction trucking services.**



AB 5 & the Broker-Trucker Model



- The broker-hauler model has been the industry go-to for arranging trucking services for years, providing essential coordination services, business designations like MBE, DBEs, etc., and even insurance guarantees.
- However, under AB 5, that system will invite new legal scrutiny, which contractors will have to bear and defend against. In particular, contractors may now have to prove that truckers they are subcontracting with are not in fact employees under the ABC test. This will prove challenging.
- The broker system is also subject to these changes. In response, some are adapting by creating an employee relationship with the truckers they broker, while others are shifting to provide no trucking services directly.



Dealing with Owners / Agencies



- Most owner contracts include requirements that contractors and subcontractors comply with applicable law.
- A number of owners have begun including provisions specifically requiring contractors and subcontractors to comply with laws relating to the classification of individuals as employees.
- Going forward, we expect more agencies to introduce measures to enforce compliance with laws requiring individuals to be classified properly.
- **Regardless of what contracts may provide, contractors and subcontractors have an obligation to comply with the law.**
- In litigation relating to misclassification, we expect plaintiff's attorneys will argue that submitting an application for payment, when the contractor or a subcontractor is not in compliance with all laws (including those relating to classification of workers), constitutes a violation of the False Claims Act under an implied certification theory.



Dealing with GCs / Subcontractors



- General contractors and subcontractors will be searching for ways to reduce their risks.
- We expect general contractors and subcontractors will modify their standard contract forms to introduce new requirements, such as affidavits or other methods for verifying compliance or prohibitions on the use of independent contractors as drivers.
- Common industry contract forms already include robust provisions requiring compliance with laws and imposing duties of indemnity in the event of claims by third parties.



Q & A



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