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Why Insurers and Coverage Lawyers Need to Care About *Dynamex*

By Andrew B. Downs

Earlier this week the California Supreme Court adopted a new standard for who is and is not an employee in the case of *Dynamex Operations West, Inc. v. Superior Court*, No. S222732. While *Dynamex* has potential significant disruptive effects on the so-called "Gig Economy," companies who rely upon independent contractors to perform the services they sell to their customers, it also has important insurance coverage ramifications.

What the Supreme Court did in *Dynamex* was make it more difficult for companies to classify their workers as independent contractors as opposed to employees. But, status as an employee, as opposed to an independent contractor, is important for much more than payroll, taxes, employee benefits, and workers compensation. Many insurance policies condition or exclude coverage based on the employment status of the person seeking coverage or the third-party claimant. For example, employees often qualify as insureds under liability insurance policies, but claims by employees against their employer generally are excluded by most liability policies. Similarly, employee status is important for fidelity policies offering commercial crime coverage.

Dynamex is a delivery company. Two of its drivers brought a class action alleging they had been improperly classified as independent contractors rather than employees for wage and hour purposes.

Courts, and employers, have struggled with defining when a worker is an independent contractor, as opposed to an employee. Historically, the California courts had used a multi-part test focusing heavily on the employer's ability to control the manner in which the employee performed his or her services. What the Supreme Court did here was abandon the traditional multi-factor test in favor of what is colloquially referred to as the "ABC" test. In the court's words:

> The ABC test presumptively considers all workers to be employees, and permits workers to be classified as independent contractors only if the hiring business demonstrates that the worker in question satisfies each of three conditions: (a) that 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 the work and in fact; and (b) that the worker performs work that is outside the usual course of the hiring entity's business; and (c) that the worker is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed.

The labor law consequences of this case are beyond the scope of this article. Several features of the ABC test will be important to future determinations regarding insurance coverage. First, there is now a presumption that the worker is an employee. In the employer-worker context, the employer bears the burden of proving independent contractor status. Between an insurer and a policyholder, we don't yet know who will bear the burden, but if the courts act consistently, the burden may well be placed on the party seeking to prove independent contractor status, whether that's the insurer or the policyholder.

The "(a)" control standard is similar to the traditional control standard except for being worded

in a way that puts the burden on the employer to disprove control. The most significant difference from prior California law is the use of the "(b)" and "(c)" standards, which are more categorical in nature. Both of those, and in particular the highly categorical "(b)" standard, are likely to be important in future coverage determinations because if the worker performs work inside the usual scope of the employer's business, he or she is an employee. A lot of analysis of factor "(b)" will depend on how the "employer" defines the scope of its business. It's not accidental that many ridesharing companies describe themselves as Transportation Network Companies – companies who match willing customers with willing drivers and arrange for the mechanics of payment, not as carriers who undertake to transport the customer from one point to another.

The change in standard may well have unintended consequences for both policyholders and insurers. Injuries to workers treated as independent contractors usually are outside the employee exclusion in typical Commercial General Liability policies, while they usually are excluded under Workers Compensation policies. Now, coverage for claims based on those injuries is more likely to focus on the Workers Compensation policy. Also, if the courts apply the ABC standard to the exclusive remedy defense to worker injury claims, more of those claims will end up in the workers compensation system than the civil courts.

Going in the other direction, if the worker is a defendant or a tortfeasor, and is now treated as an employee, not an independent contractor, the "employer" is more likely to be vicariously liable and the worker is more likely to be entitled to a defense and indemnity under the policy, in addition to the statutory right to defense costs and indemnity enjoyed by all employees under California Labor Code § 2802.

California is not the first state to adopt the ABC standard. Several states in New England have done so, along with scattered states elsewhere. It remains the minority standard. Ultimately, there may be legislative action which further modifies the standard.