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Counsel for the Road Ahead®

The *Dynamex* Decision: Will It Be a Catalyst or Will It Be Contained?

Richard A. Plewacki

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Introduction

As has been widely reported, the California Supreme Court on April 30, 2018, issued a decision in *Dynamex Operations West, Inc. v. The Superior Court of Los Angeles County* that rejected a long-standing flexible, multifactor test to determine whether a worker is an employee or an independent contractor for purposes of Wage Orders, deciding instead to embrace a more rigid classification test and imposing a presumption that all workers are employees until and unless an employer can prove otherwise.[1]

In *Dynamex*, the California Supreme Court adopted the Industrial Welfare Commission's (IWC's) "suffer or permit to work" definition of the term "employ" to determine the classification of workers in the Wage Order context. Also, noting the potential difficulty in literally applying the suffer or permit to work test, the California Supreme Court decided to embrace the "ABC" test, utilized in a few states, to determine the classification of workers for California Wage Order purposes.

The decision represents a sea change of significant magnitude to a tremendous number of businesses in the largest state economy in the country including, of course, transportation, but particularly those carriers' operations with independent contractors in the on-demand courier, B-2-B small package and parcel, and B-2-C last-mile segments of the transportation industry.

The Court's decision is arguably somewhat narrower in scope as it relates to transportation, thus begging the question whether other courts will expand its application beyond Wage

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Orders or whether judicial restraint will be used and confine its application for the intended purpose set forth in the Court's decision? Additionally, will the "ABC" test be found to be preempted under federal law due to its impact on interstate commerce?

The Starting Point

The old adage is that "bad facts make bad law," and it could not have been more evident than in the *Dynamex* fact pattern. Dynamex Operations West, Inc. is a nationwide package and document delivery company offering same-day pickup and delivery services. Prior to 2004, Dynamex classified individual drivers who performed work picking up and delivering shipments of typically small packages or parcels as employees. In 2004, Dynamex made the decision to convert all of its employee drivers to independent contractors after management concluded that such a conversion would generate economic savings for the company. Dynamex required all drivers to enter into a new contractual arrangement with Dynamex under which they were classified as independent contractors rather than employees.[2] Thus, there was this group of drivers who were performing the same work they did as W-2 employees, but suddenly became 1099 independent contractors who were now required to provide their own vehicles and pay for all their transportation expenses as well as all taxes and workers' compensation insurance.

Two delivery drivers sued on their behalf and on the behalf of a class of allegedly similarly situated drivers, alleging that Dynamex had misclassified the delivery drivers as independent contractors rather than employees for the purposes of the application of California's IWC Wage Orders, which impose obligations on hiring entities related to minimum wage, maximum hours worked, and working conditions.

From a procedural standpoint, the issue before the trial court that caused the ultimate appeal to the Supreme Court was whether the class of workers had more common issues than individual issues, i.e., sufficient commonality for class certification. The trial court applied the law from the *Martinez* decision (which is explained below) and concluded that common issues predominated and certified the class.

Ultimately, the issue before the Supreme Court was whether the test/definitions of "employee" and "employer" set forth in *Martinez* were applicable in determining if a worker was misclassified as an independent contractor rather than an employee.

Read broadly, the *Dynamex* decision has the potential to have wide, sweeping effect across all employment issues. However, it is important to remember the context of the decision. On several occasions, the California Supreme Court reminded that its decision to adopt the suffer or permit standard for worker classification purposes (and the "ABC" test) was only in the Wage Order context.

With that said, however, and as we discuss in more detail below, the putative class was rather narrow in scope, which is a key consideration to the trucking industry. The class of eligible plaintiffs included those *individuals* who: (1) were classified as independent contractors and performed pickup and delivery service for Dynamex between April 2001 and the date of the Class Certification Order; (2) used their personally owned or leased vehicles weighing less than 26,000 pounds; and (3) had returned questionnaires, which the Court deemed timely and complete.[3] As such, the decision deals with the applicability of Wage Order No. 9, which is the Transportation Wage Order for *individuals* who had a one-on-one contractual relationship with Dynamex and used smaller, personally owned or leased vehicles such as automobiles or small cargo vans weighing less than 26,000 GVW. The case does not involve the Workers'

Compensation Statute or the reimbursement for business expenses, etc., nor does it deal with independent contractor fleet owners or individual drivers for fleet owners.

The Pre-*Dynamex* Rules of the Road

Prior to the decision in *Dynamex*, California courts utilized the *Borello* standard to classify workers as employees or independent contractors. Developed and articulated in *S.G. Borello & Sons, Inc. v. Dep't of Indus. Relations*, the *Borello* standard involves the principle factor of "whether the person to whom services is rendered has the right to control the manner and means of accomplishing the result desired."[4]

In connection with this principle factor, the Court identified nine distinct additional factors that would be balanced to determine whether the worker should be classified as an employee or as an independent contractor. These additional factors are: (1) the right to discharge at will, without cause; (2) whether the one performing the services is engaged in a distinct occupation or business; (3) the kind of occupation, with reference to whether in the locality the work is usually done under the direction of the principal or by a specialist without supervision; (4) the skill required in a particular occupation; (5) whether the principal or the work supplies the instrumentalities, tools and place of work for the person doing the work; (6) the length of time for which the services are performed; (7) the method of payment, whether by time or by the job; (8) whether or not the work is part of the regular business of the principal; and (9) whether or not the parties believe they are creating the relationship of employer-employee. *Id.* "[T]he individual factors cannot be applied mechanically as separate tests; they are intertwined and their weight depends often on particular combinations."[5]

Thus, for 30 years, California courts utilized the *Borello* standard for worker classification cases, establishing a robust and detailed history of case law that laid stable ground for worker classification. During that time, *Borello* was often referred to as a "right of control" test with ancillary factors to consider in determining who possessed the right of control between an individual worker and the hiring entity. It is interesting to note, however, that the Supreme Court reminded us in *Dynamex* that *Borello* actually calls for application of a *statutory purpose* standard that considers the control of details and other potentially relevant factors identified in prior California and out-of-state cases in order to determine which classification (employee or independent contractor) best effectuates the underlying legislative intent and objective of the statutory scheme."[6] This reminder is rather telling when considering the underlying fact pattern for the lawsuit.

"Borello was often referred to as a "right of control" test with ancillary factors to consider, however, the Supreme Court reminded us in Dynamex that Borello actually calls for application of a statutory purpose standard that considers the control of details and other potentially relevant factors."

In 2010, the case of *Martinez v. Combs* was decided.[7] In that case, the Court addressed the meaning of the terms "employ" and "employer" as they were used in California Wage Orders, but in the context of a joint employer issue. *Martinez* involved a strawberry grower that employed seasonal workers but failed to pay the workers the required minimum or overtime wages earned. The workers contended that the action of unpaid minimum or overtime wages constituted applicable standards for determining who was a potentially liable employer; i.e., a "joint employer." *Martinez* did not directly involve the classification of workers as employees or as independent contractors.

The *Martinez* court concluded that the term "employ" used in IWC Wage Orders has three alternative definitions: (1) to exercise control over the wages, hours or working conditions; (2) to "suffer or permit to work"; or (3) to engage, thereby creating common law relationships.[8] The second definition above was at the heart of the *Dynamex* case.

The *Dynamex* Decision: What the Court Did

The Court, in its decision, noted the existence of a continuing serious problem of worker misclassification as independent contractors, which the California legislature has addressed by enacting laws that impose substantial civil penalties on those that willfully misclassify, or willfully aid in misclassifying, workers as independent contractors."[9] Thus, discretely "signaling" its recognition of an applicable statutory purpose.

The task before the California Supreme Court, therefore, was to identify what standard should be applied to determine the proper classification of workers in the Wage Order context; the *Borello* standard, or the *Martinez* standard's "suffer or permit to work" component. Dynamex argued that the "suffer or permit to work standard" was only applicable to the joint employer context, similar to the question involved in the *Martinez* case. The *Dynamex* court rejected this argument, instead identifying that "there is nothing in the language of the Wage Order indicating that the standard is so limited."[10] Additionally, the Court pointed to the discussion of the origin and history of the "suffer or permit to work standard" within the *Martinez* decision as evidence that the standard was intended to apply beyond the joint employer context.

The Court, by holding that the "suffer or permit to work standard" applied beyond the joint employer context and to classification issues, rejected the *Borello* multifactor standard and instead held that in the Wage Order context, to determine the classification of workers, the *Martinez* "suffer or permit" to work standard will apply. "The adoption of the exceptionally broad 'suffer or permit to work standard' in California Wage Orders finds its justification in the fundamental [statutory] purposes and necessity of the minimum wage and maximum hour legislation in which the standard has traditionally been embodied."[11]

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Long-Awaited Win for NVOCCs

Stephanie S. Penninger

John C. Gentile

Ending a process that started back in 2004, the Federal Maritime Commission (FMC) voted unanimously on June 6, 2018, to exempt Non-Vessel Operating Common Carriers (NVOCCs) from certain filing requirements related to their service contracts (NSAs) and rate agreements (NRAs). This vote culminated in the publication of new regulations addressing the same, which will take effect at the end of next month.

History Is a Relentless Master

By way of background, NVOCCs were required to file their NSAs and any amendments to those agreements with the FMC. NVOCCs were also required to publish the essential terms of the service agreements in their rules tariffs. The NRAs were limited in how they could be used, as they could not be amended, even when NVOCCs were faced with changing trade lane conditions, and could only include actual freight rates; no other economic terms were permitted. These rules impaired an NVOCC's ability to adapt to the ever-changing landscape of the ocean shipping marketplace and impeded the sustainability of the NVOCC business model.

Crying Out for Change

After numerous petitions to the FMC in an effort to free NVOCCs from these burdensome regulations (some of which requested the elimination of 46 CFR part 531 altogether), and in response to comments submitted responsive to the FMC's proposed regulatory amendments, the FMC decided to publish a Final Rule amending 46 CFR Parts 531 and 532, "Amendments to Regulations Governing NVOCC Negotiated Rate Arrangements and NVOCC Service Arrangements" (Docket No. 17-10) in the Federal Registrar, Volume 83, No. 141.

The Final Rule, effective on August 22, 2018, is intended to enhance efficiency and reduce costs in the competitive NVOCC industry while still allowing NVOCCs to continue their existing operations, whether under negotiated service contract models or on a rate quotation basis (without engaging in formal contract negotiation processes). Once the regulations become effective, they will make a handful of significant changes.

Taking a Different Tack

First, the prohibition against amending NRAs will be lifted. As a result, NVOCCs and their customers will be able to amend their agreements, if mutually agreed upon by all contracting parties, to be responsive to changes in the ocean shipping arena. The NRAs themselves will have the ability to be longer term between NVOCCs and customers, without serious loss of revenue, since they will have the benefit of amending during the course of their agreement rather than terminating an agreement early and entering into a new one or issuing single-day or week NRAs. This will likely result in direct cost savings for NVOCCs and their customers, along with more consistency in pricing arrangements.

Second, non-rate economic terms will be allowed in the NRAs. This will allow NVOCCs to agree with customers on a broad range of terms in NRAs that are akin to NSAs and to ocean service agreements with ocean carriers instead of only rates. NVOCCs and shippers value flexibility in being able to negotiate minimum volumes, volume rates, rate or service amendments and their processes, liability, liquidated damages, credit terms, service guarantees or benchmarks, surcharges, GRIs or other pass-through charges from carriers or ports, free time, demurrage, per diem, EDI services, and dispute resolution which were not to previously allowed to be included in an NRA. Allowing NVOCCs the freedom to contract in this manner in NRAs should result in greater market efficiencies.

Third, shippers will now have the ability to accept the terms of an NRA by booking a shipment after receiving the NRA terms from the NVOCC, if the NVOCC incorporates a prominent written notice that booking constitutes acceptance of the NRA terms in the NRA or an amendment, rather than the burdensome process of filing the NRA with the FMC. This change makes it clear that the tender of cargo in response to an NRA will satisfy acceptance and formation of a contract.

Fourth, NSAs may now be exempted from both filing and the publication of essential terms requirements. These amendments should ensure that NSAs continue to be an option for shippers and NVOCCs, but with a reduced regulatory burden. NVOCCs will still have to retain NSAs, amendments and associated records for five years from the termination of the NSA and provide them within 30 days upon request by the FMC. The removal of the filing requirement was reported to reduce NVOCCs' burden by 162 hours and enable a savings of approximately $10,728.37. Of course, those who prefer NSAs will still be able to enjoy the extra formality and other benefits of NSAs.

Lastly, under the Final Rule, if an NRA rate is not an "all-in rate," then the NRA has to specify

which surcharges or assessorial charges will apply by including the specific charges in the rules tariff. Applicable charges in the rules tariff are to be fixed once the first shipment has been received by the NVOCC until the last shipment is delivered, subject to a shipper's and NVOCC's further amendment by mutual agreement. As to pass-through charges and ocean carrier GRIs for which the NRA or rules tariff does not provide a specified amount, the NVOCC can invoice the shipper only for charges actually incurred by the NVOCC (a markup is not allowed). The removal of the prohibition on pass-through ocean carrier GRIs should increase efficiency and flexibility within the NRA framework.

Freedom to Regulate Their Own Pursuits of Industry

The significance of these changes cannot be understated. NVOCCs now may engage their customers more freely from regulation. For many years, NVOCCs have been unable to compete on an equal playing ground with exempted ocean carriers. Now, NVOCCs and their customers will be able to negotiate rates and services easily, better serving the interests of both NVOCCs and shippers. As Commissioner Rebecca Dye aptly stated: "The Final Rule will provide [the] industry with the flexibility and freedom to fully meet the business needs of their customers, not the government—as should be the case."

For more information, please contact **STEPHANIE S. PENNINGER** at spenninger@beneschlaw.com or (312) 212-4981, or **JOHN C. GENTILE** at jgentile@beneschlaw.com or (302) 442-7071.

On August 3, 2018, Benesch will be hosting The Admiralty and Maritime Law Committee Roundtable at its Chicago office. Stephanie will be a co-moderator of the event, John and Kelly E. Mulrane will be in attendance.

In-Bond Transport Modernization Arrives

Jonathan Todd

John C. Gentile

Regulatory changes are coming to in-bond transportation that will impact the operations of bonded carriers in the United States. The practice of in-bond transportation permits motor carriers to lawfully transport freight from one port of entry to another where the goods are then entered for warehousing, admitted to a foreign trade zone, entered for consumption in the U.S., or exported from the U.S. This flexibility can be a valuable tool for the effective management of traffic flows in global supply chains.

The administrative process supporting these operations is now set to modernize. U.S. Customs and Border Protection (CBP) published a final rule in September 2017 that adopted several key amendments to CBP regulations regarding the in-bond process (82 Fed. Reg. 45366). Chief among these new requirements is the elimination of the infamous CBP Form 7512 as a paper document in favor of the mandatory electronic filing of in-bond applications. The electronic filing may be submitted via the Automated Commercial Environment (ACE) or QP/WP, which is an ABI-hosted in-bond system that will allow all parties to submit electronic filings directly to CBP. As a result of the electronic filing, CBP will gain real-time information on goods in transit, and that is expected to allow for easy reconciliation of shipments.

CBP's compliance deadline is currently August 6, 2018. As of this date, CBP will no longer accept Form 7512 in paper form and electronic reporting will become mandatory. The new system includes other process changes that may cause headaches for bonded carriers. For example, the in-bond application will require additional information that includes the six-digit Harmonized Tariff Schedule (HTSUS) number. This classification will of course come from the importer or its customs broker and must be received together with sufficiently accurate descriptions to describe the cargo as necessary to any U.S. government agency having jurisdiction. Carriers must receive and submit a Facilities Information and Resources Management System (FIRMS) code with the application. Carriers will be required to electronically request and receive permission from CBP before diverting in-bond merchandise from its intended destination port to another port. Finally, the arrival and location of in-bond merchandise also must be electronically reported within 48 hours following arrival at the ultimate port of entry into the U.S. or the port of exportation from the U.S.

Fortunately, certain operational changes included in the final rule will yield greater efficiency in today's fast-paced transit environment. For example, in-bond cargo may now be hauled with non-bonded cargo in the same unsealed container or compartment if the in-bond items are corded, sealed or labeled as in-bond. Additionally, CBP permission is no longer required to break and replace a seal provided that the activity of breaking and replacing seals is adequately documented for the in-bond cargo. These are welcome changes for day-to-day transportation operations.

Bonded carriers are facing a challenge to get up to speed with these new CBP regulations. CBP is providing a 90-day flexible enforcement period intended to take into account the challenges associated with compliance. This enforcement posture is of course discretionary and depends in large part on making good-faith efforts and marking progress toward compliance. The use of paper documentation will not likely end overnight and very well may continue in parallel to these electronic requirements as carriers and others adapt to this new operating environment.

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TORT TRIAL & INSURANCE PRACTICE

THE ADMIRALTY AND MARITIME LAW COMMITTEE

of the American Bar Association TIPS Practice Section presents

Transportation, Logistics and Insurance Roundtable:

What keeps in-house transportation and logistics counsel and insurance claims professionals up at night and what are outside counsel doing to cause or help their insomnia?

August 3, 2018 | 4:00 – 5:00 p.m.

Where:

Benesch, Friedlander Coplan & Aronoff LLP

333 W. Wacker, Suite 1900 | Chicago, IL 60606

Food and Drink to Follow at Punch Bowl Social Chicago

310 N. Green St. | Chicago IL 60607

(*Details to follow to attendees*)

Speakers:

- MICHELLE HAYS, Director
  Aon Risk Solutions – San Francisco, CA
- JOSH JUBELIRER, Associate General Counsel
  Echo Global Logistics – Chicago, IL
- D. MICHAEL KAYE, Chief Counsel – Origination Business Unit
  Archer Daniels Midland Company – Chicago, IL
- MARK STOSE, Sr. Consultant
  Aon Risk Solutions – Morristown, NJ

Moderators:

- STEPHANIE PENNINGER, Partner, Maritime Group Chair
  Benesch, Friedlander, Coplan & Aronoff LLP – Chicago, IL
- CHRIS NOLAN, Partner, Transportation and Infrastructure Industry Sector Group Co-Chair, *Holland & Knight LLP – New York, NY*

Register for this event by emailing:

STEPHANIE PENNINGER at spenninger@beneschlaw.com and CHRIS NOLAN at chris.nolan@hklaw.com

This course is pending approval by the MCLE of the Supreme Court of Illinois for 1 hour. Reciprocity will be available for New York and New Jersey once program is approved. Should your state not be preapproved, Benesch will help you to obtain CLE credit at the completion of the seminar.

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Pass this copy of *InterConnect* on to a colleague, or email **MEGAN THOMAS** at mthomas@beneschlaw.com to add someone to the mailing list.

Red Sky in Morning, Shippers Take Warning: California's Dignity in the Driver's Seat Bill

Stephanie S. Penninger

Emily C. Fess

What's Happening?: Potential Joint Liability for Drayage Carrier Customers

California retailers and shippers beware. In another move by California lawmakers to deter companies from classifying truck drivers as independent contractors, Senate Bill 1402 (SB 1402), entitled "Dignity in the Driver's Seat," was introduced into the California Senate in April 2018. The bill seeks to discourage labor and employment abuses by port drayage motor carriers by making retailers jointly liable for violations of state labor and employment laws when they hire port drayage motor carriers with unpaid final judgments for misclassifying workers, not providing worker's compensation insurance, and other violations.

Should SB 1402 add Section 2810.4 to the California Labor Code, retailers who hire these port drayage motor carriers would be jointly liable for any future labor and employment law violations. SB 1402 contains an exception to joint liability for retailers who hire union trucking firms with collective bargaining agreements that specifically waive retailer liability.

The bill has support from the mayors of port cities Long Beach, Los Angeles and Oakland. Like the California Supreme Court decision in *Dynamex*, SB 1402 will likely increase the number of cases in which port drayage motor carriers will be found to have misclassified drivers as independent contractors.

In *Dynamex*, the California Supreme Court liberalized the test for employee status in California and created a rebuttable presumption that an individual working for a company or another individual is an employee as opposed to an independent contractor. This is significant because employers are responsible for paying federal social security and payroll taxes, unemployment insurance taxes, and state employment taxes as well as providing workers compensation insurance for their employees. Not so for independent contractors. Moreover, employees, and not independent contractors, are covered by a plethora of state and federal employment laws that regulate wages and hours and others terms and conditions of employment. (See the comprehensive article on the *Dynamex* decision on page 1.)

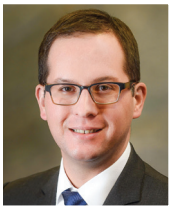
What Can I Do to Minimize Exposure?

SB 1402 contains language stating that parties may contract for and enforce a right of contribution and indemnity against each other for liability created by acts of a port drayage motor carrier. As such, we recommend that you work with your legal counsel to review and update any existing contracts you have with port drayage motor carriers in order to disclaim any liability and impose indemnification obligations to the extent that you are held responsible for a contracting party's failure to properly classify its workers or for violations of state labor and employment laws, including those implicated by SB 1402.

Your legal counsel can also advise you on how to protect against secondary boycotting by union shops. Increasingly retailers and other shippers are experiencing picketing and related activity, sometimes without any notice, in an attempt to dissuade them from conducting business with drayage carriers who fail to unionize.

For more information, please contact **STEPHANIE S. PENNINGER** at spenninger@beneschlaw.com or (312) 212-4981, or **EMILY C. FESS** at efess@beneschlaw.com or (312) 624-6326.

Handing Over the Keys? Consider Alternate Pricing Models for 3PL Outsourcing



Jonathan Todd

Enterprise shippers are often attracted to the opportunities presented by outsourcing certain operational functions. Credible third-party logistics (3PL) providers are available to run warehousing, distribution, fulfillment and last-mile operations seamlessly at the flip of a switch. These outsourcing strategies can permit enterprises to deploy time and resources elsewhere in the interest of advancing core competencies while yielding tangible benefits to the balance sheet. Outsourcing can also produce positive effects in inventory management and even expense management as savvy 3PLs exercise their core strengths.

Any outsourcing relationship is critical to an enterprise's value proposition. It is intended to be long-term and strategic in nature, which requires a great deal of trust between the enterprise that is "handing over the keys" to its supply chain and the 3PL that is receiving them. "Trust" is of course code for a heavily negotiated services agreement complete with all the key performance indicators, standard operating procedures and implementation planning necessary to ensure a smooth transition for the respective supply chain.

One of the key negotiation points at the heart of any such relationship is the pricing model. Any decision to outsource a supply chain function will depend in large part on the anticipated financial benefits, which can be significant. They may range from opportunities for improved visibility and planning, lower cost variance or lower total cost, and monetizing certain assets or transferring certain liabilities. Regardless of the desired financial objectives, their basic shape often takes form in the pricing model that is selected. The three dominant 3PL outsourcing pricing models in the market today are (1) Transactional, (2) Cost Plus, and (3) Gainshare.

Transactional Models – Transactional models are the traditional "retail" approach for pricing any single or combined supply chain services. Contractual rates and charges, including respective service commitments or volumes, are determined without regard to any profit margin that may be included in the pricing. Administration of transactional models is akin to traditional procurement and operational management, where pricing may be established at the level of product, service, lane, volume or other metrics. Penalties for failure to perform or to tender minimum volumes are negotiable as are possible bonuses for positive performance against key performance indicators.

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Governor Appoints Jonathan Todd to Executive Order

Benesch is pleased to announce that **JONATHAN TODD**, an attorney in the firm's Transportation & Logistics Practice Group, was recently appointed by Governor John Kasich to the Executive Order of the Ohio Commodores.

The Executive Order was established by Governor Rhodes in 1966 to honor the Ohio business leaders who accompanied him on the State's first international trade mission. The name "Commodores" refers to Commodore Oliver Hazard Perry, who was the hero of the Battle of Lake Erie in 1813. Today the not-for-profit nonpartisan organization is primarily tasked with supporting the Office of Governor and Lieutenant Governor in efforts to advance Ohio's economy. Appointment is considered Ohio's "most distinguished honor" and is granted to citizens in recognition of business acumen, accomplishments and leadership.

Jonathan Todd practices law in the areas of supply chain management, international trade compliance, logistics and transportation. He represents manufacturers, retailers, third-party logistics providers and carriers in transactional and regulatory matters. Those issues span the wide range of challenges and opportunities that arise when managing domestic and international supply chains and business operations. Jonathan may be reached at (216) 363-4658 or jtodd@beneschlaw.com.

The *Dynamex* Decision: Will It Be a Catalyst or Will It Be Contained?

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In adopting the "suffer or permit to work standard," the Court acknowledged the difficulty of a literal application of the standard. "[W]e conclude that the 'suffer or permit to work' definition is a term of art that cannot be interpreted literally in a manner that would encompass within the employee category the type of individual workers, like independent plumbers or electricians, who have traditionally been viewed as *genuine* independent contractors who are working only in their own independent business."[12] Because of this difficulty, the Court decided to employ a more bright-line test, the "ABC" test, to determine the classification of workers under this standard.

"[W]e conclude that in determining whether, under the 'suffer or permit to work' definition, a worker is properly considered the type of independent contractor to whom the Wage Order does not apply, it is appropriate to look to a standard, commonly referred to as the 'ABC' test, that is utilized in other jurisdictions in a variety of contexts to distinguish employees from independent contractors."[13]

The "ABC" Test

Having noted that the "ABC" test is utilized in other jurisdictions to distinguish employees from independent contractors, the Supreme Court failed to mention that in the jurisdictions upon which it relied and cited to, the "ABC" test is a creation of statute, which was the subject of debate, dialogue and discernment by elected officials serving the state legislatures and not a decision by seven people in black robes.[14]

As mentioned earlier, the "ABC" test is a "bright-line" test under which a worker is properly considered an independent contractor to whom a Wage Order does not apply, only if the hiring entity is able to establish the presence of all the following distinct factors: (1) that the worker is free from the control and direction of the hiring in connection with the performance of the work, both under the contract for the performance of such work and in fact; (2) that the worker performs work that is outside the usual course of the hiring entity's business; and (3) that the worker is customarily engaged in an independent established trade, occupation or business in the same nature as the work performed for the hiring entity.[15]

"[T]he Supreme Court failed to mention that in the jurisdictions upon which it relied and cited to, the 'ABC' test is a creation of statute, which was the subject of debate, dialogue and discernment by elected officials serving the state legislatures and not a decision by seven people in black robes."

Part A of the "ABC" test seeks to classify as employees those individuals who are subject to the control of the entity either "as a matter of contractual right or in actual practice."[16] Basically, a common law right-of-control factor.

Part B of the "ABC" test seeks to classify as employees "all individuals who are reasonably viewed as providing services to the business in a role comparable to that of an employee, rather than in a role comparable to that of a traditional independent contractor."[17] Part B is the most troublesome for the trucking industry particularly in a one-on-one contractual relationship with an individual.

Part C of the "ABC" test seeks to classify as employees those individuals "who have not independently decided to engage in an independently established business."[18] Such as those who were in the class that was certified in this case—individuals working in their individual capacities.

With the "ABC" test, the Court has created a presumption that all workers are employees until and unless the hiring entity can prove otherwise. The Court acknowledged that the placing of the burden on hiring entities to establish that a worker is indeed an independent contractor who was not intended to be included within the coverage of the Wage Order is consistent with the history and purpose of the "suffer or permit to work standard" discussed in *Martinez.*[19] By adopting the "ABC" test for classification of workers for Wage Order purposes, the California Supreme Court has rejected several decades of case law establishing the use of the *Borello* test for classification determination.

It is evident by the Court's language in the case that it sought to create a more rigid and bright-line test for determining employee status in the context of Wage Orders compared to the long-standing *Borello* test. The Court's decision will have a lasting impact on employment relationships in California. Under this new standard, workers will be more likely to be classified as employees than independent contractors.

Social Welfare Language

Throughout the *Dynamex* decision, the Court repeatedly noted that its decision to adopt the "ABC" test was in line with the purpose of social welfare statutes and consistent with the true spirit of the *Borello* decision. "The *Borello* decision repeatedly emphasizes statutory purpose as the touchstone for deciding whether a particular category of workers should be considered employees rather than independent contractors for purposes of social welfare legislation."[20]

According to the California Supreme Court, "the 'suffer or permit to work standard' has a long and well-established history and in other jurisdictions has regularly been held applicable to the question of whether a worker should be considered an employee or an independent contractor for the purposes of social welfare legislation embodying that standard."[21] Based on this language, it seems like the Court is attempting to justify its rejection of over 30 years of case law establishing the *Borello* standard as the standard to apply in worker classification cases by connecting the "suffer or permit to

work standard" to enhancing the spirit of the social welfare language discussed in *Borello*.

"[United States Supreme Court Justice] Hugo L. Black, described [the 'suffer or permit to work'] standard as 'the broadest definition' that has been devised for extending the coverage of a statute or regulation to the widest class of workers that reasonably fall within the reach of a social welfare statute."[22] The Court reasons that by adopting the "suffer or permit to work standard" and directly employing the "ABC" test to interpret the standard, it has extended those protections to workers that are to be afforded to them by social welfare legislation. In essence, it is fulfilling the spirit of the *Borello* decision even though it is rejecting the standard developed by the *Borello* decision.

The Implications of *Dynamex*

The implications of *Dynamex* are significant. The California Supreme Court, by adopting the "ABC" test, has placed the burden on the hiring entity to establish that workers are independent contractors instead of employees. This rebuttable presumption of employee can only be overcome if the hiring entity can establish the presence of all three factors of the "ABC" test. Because of *Dynamex*, it is now more difficult to establish an independent contractor business model and more care and strategy must go into developing business operations to avoid the pitfalls that accompany misclassification lawsuits. In the courier, B-2-B small package and parcel, and B-2-C last-mile segments, it will be virtually impossible to satisfy Part B of the "ABC" test if the carrier has a direct one-on-one contractual relationship with an individual.

The risk of misclassification can be extreme. In a memorable instance, FedEx Ground incurred liability of over $220 million in 2015 after it settled a misclassification lawsuit in California. Roadrunner Intermodal Services, Central Cal Transportation and Morgan Southern agreed to a settlement of $9.5 million to settle a misclassification class action lawsuit in California. These settlements seem to occur with regularity, and businesses must be aware of them.

Transportation businesses should consider implementing alternative approaches and exercise due diligence at the onset of establishing an independent contractor relationship to ensure that they are able to satisfy each of the three elements of the "ABC" test to avoid misclassification allegations. As mentioned earlier, transportation businesses will have difficulty structuring business operations to satisfy Part "B" of the "ABC" test and should ensure that if they are attempting to establish an independent contractor business model, their relationships with their workers remain at arm's length. This may involve a complete overhaul of the business operations and shifting to brokerage operations instead of motor carriage operations or incorporating third-party resources to facilitate a more arms-length relationship. Because of the burden placed on hiring entities, and because of the potential liability associated with misclassification, we may see more and more transportation companies that do work in California shifting from an independent contractor business model to an employee business model or other hybrid arrangements.

What's Next?

As to what's next, the quick answer is "uncertainty." Currently, it is a mixed bag.

On the positive front, the Court of Appeals for the Fourth Appellate District in the State of California decided within a few weeks of the *Dynamex* decision to reject the "ABC" test in the context of determining whether an individual was employed by joint employers.[23] In the case *Curry v. Equilon*, the Court concluded that the "ABC" test set forth in *Dynamex* is directed toward the very narrow issue of whether individuals who fall within the defined scope as set forth in that opinion were misclassified as independent contractors for purposes of Wage Order No. 9, stating that the Supreme Court's policy reasons in selecting the "ABC" test are uniquely relevant to the issue of allegedly misclassified independent contractors. Placing the burden on the alleged employer to prove that the worker is not an employee is meant to serve policy goals that are not relevant in the joint employer context.

In rejecting the "ABC" test, the *Curry* court latched on to the test promulgated by the court in *Estrada v. FedEx Ground Package System, Inc.*, a test very similar to the *Borello* standard.[24] "The essence of the common law employment test 'is the control of details'—that is, whether the principal has the right to control the manner and means by which the worker accomplishes the work—but there are a number of additional factors in the modern equation, including (1) whether the worker is engaged in a distinct occupation or business, (2) whether, considering the kind of occupation and locality, the work is usually done under the principal's direction or by a specialist without supervision, (3) the skill required, (4) whether the principal or worker supplies the instrumentalities, tools, and place of work, (5) the length of time for which the services are to be performed, (6) the method of payment, whether by time or by job, (7) whether the work is part of the principal's regular business, and (8) whether the parties believe they are creating an employer-employee relationship. [Citations]."[25]

By adopting and applying the *Estrada* test, the Court of Appeals for the Fourth District of the State of California explicitly stated that the "ABC" test discussed in detail in the *Dynamex* case does not apply in the joint employment context.[26] It will be interesting to see if other courts decide to follow the Fourth District's lead and continue to narrow the scope of *Dynamex*.

On the other hand, a recent plaintiff in a case against the gig company Grubhub has made a filing in a California appeals court attempting to have said court apply the *Dynamex* decision retroactively against Grubhub. If allowed, this decision could have a lasting effect on the transportation industry as years of contractual arrangements are placed under the microscope. Notably, as support, the Grubhub plaintiff cites the fact that the defendant in *Dynamex* attempted to petition the Supreme Court to clarify that its decision only applies prospectively. The California Supreme Court denied the defendant's motion. This denial leaves the decision to the lower court on deciding whether *Dynamex* applies retroactively or not—a question that many will be eagerly awaiting an answer to.

Additionally, on a slower track, a coalition of businesses and advocacy groups, as well as the California Chamber of Commerce, has penned a letter to California Governor Jerry Brown and the state legislature asking for relief from the *Dynamex* decision. They propose a postponement or suspension of the application of *Dynamex* until interested parties could come together to

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The *Dynamex* Decision: Will It Be a Catalyst or Will It Be Contained?

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develop a more "balanced test" for determining independent contractor versus employee status. They argue that the legislature, not the judiciary, should be responsible for constructing statewide policy. Whether the legislature and the Governor agree with the businesses and the Chamber is yet to be seen, but it is a debate that will be hotly contested as the reverberations of the *Dynamex* decision continue to be felt throughout the economic landscape.

Furthermore, on July 19, 2018, the Western States Trucking Association (WSTA) filed a lawsuit in California federal court against the California department of Industrial Relations and the California Attorney General seeking to nullify the *Dynamex* decision.[27] In the lawsuit, the WSTA contends that the *Dynamex* decision conflicts with the 1994 Federal Aviation Administration Authorization Act, which prohibits states from enacting laws that interfere with "prices, routes and service" of interstate motor carriers.[28] The WSTA also argues that the *Dynamex* decision violates the Commerce Clause as well as the Supremacy Clause of the U.S. Constitution. Though the case is in its early stages, this will be a development to watch as the court determines whether to uphold or invalidate the influential *Dynamex* decision.

For more information, please contact **RICHARD A. PLEWACKI** at rplewacki@beneschlaw.com or (216) 363-4159 or **KRISTOPHER J. CHANDLER** at kchandler@beneschlaw.com or (614) 223-9377.

[1] *Dynamex Operations W. v. Superior Court*, 4 Cal. 5th 903 (Cal. 2018)).
[2] *Id.* at 8.
[3] *Id.* at 11.
[4] *S.G. Borello & Sons, Inc. v. Dep't of Indus. Relations*, 48 Cal. 341, 350 (Cal. 1989).
[5] *Id.* at 351.
[6] *Dynamex* at 33.
[7] *Martinez v. Combs*, 49 Cal. 4th 35 (Cal. 2010).
[8] *Id.* at 64.
[9] *Dynamex* at 34–35.
[10] *Id.* at 47.
[11] *Id.* at 58.
[12] *Id.* at 7.
[13] *Id.*
[14] In New Jersey, the "ABC" test is incorporated into the New Jersey Unemployment Compensation Act (N.J. Stat. Ann. § 43:21-19(i)(6)(A)-(C)). *See also* Mass. Gen. Laws, ch. 149, § 148B; Del. Code Ann., tit. 19, § 3501(a)(7).
[15] *Dynamex* at 7.
[16] *Id.* at 69.
[17] *Id.* at 70.
[18] *Id.* at 74.
[19] *Id.* at 66.
[20] *Id.* at 34 (citing *Borello* at 351, 353–354, 357, 358, 359).
[21] *Id.* at 47.
[22] *Id.* at 58 (citing *United States v. Rosenwasser* (1945) 323 U.S. 360, 363, fn. 3)
[23] *Curry v. Equilon Enterprises, LLC*, 23 Cal.App.5th 289 (Cal. Ct. App. 2018).
[24] *Estrada v. FedEx Ground Package System, Inc.*, 154 Cal.App.4th 1 (Cal. Ct. App. 2007).
[25] *Curry* at 306 (citing *Estrada* at 10).
[26] *Id.* at 314.
[27] Western States Trucking Association v. Andre Schoorl, *et al*, Case 2:18-at-01206 (U.S. Dist. Eastern Dist. CA).
[28] Sec. 601(b)(1), Federal Aviation Administration Authorization Act of 1994, Public Law No: 103-305.

Handing Over the Keys? Consider Alternate Pricing Models for 3PL Outsourcing

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Cost Plus Models – Cost plus models can be viewed as the "wholesale" approach to pricing. These require analysis of anticipated expenditures as well as negotiation of the 3PL's profit margin. An enterprise's experience with its own overhead and cost metrics helps to inform expectations for baseline costs following outsourcing. Some of those expenditures, such as equipment leases, may be transferred to the 3PL depending on the nature of the operation. The expertise and economy of scale brought by a large 3PL provider may also offer lower baseline costs than those prior to outsourcing. Recordkeeping, real-time reporting, substantiation of certain expenditures, and periodic management meetings are some of the tools available to manage costs throughout the relationship. The 3PL's margin is set at a percentage of cost, or a lump sum, or a combination of the two.

Gainshare Models – Gainshare models are intended to be a "win-win" for both the enterprise shipper and its 3PL. These are often attractive for projects that are significant in scale due to the promise of mutually incentivizing operational performance. A typical gainshare will establish agreed-upon metrics for a baseline based upon historic financial performance. Real or contingent adjustments to the baseline may be negotiated to account for changes in economic conditions or market demands. These can include inflation adjustments, expense controls, and even ceilings on certain overhead costs. The parties then negotiate anticipated operational benefit in subsequent years based in large part upon the 3PL's analysis of opportunities for cost improvement. The 3PL earns its profits from its percentage of cost savings and the enterprise experiences lower total cost than it would otherwise incur.

These common pricing models for 3PL outsourcing vary widely in their complexity and administrative burden, with the key distinction of difference in the degree of cost controls and allocation of respective risk. Creative hybrid models are also available to draw upon the desired characteristics of each throughout the term of the relationship or changing from one model to the other at certain milestones or at the option of the parties. The choice of a pricing model ultimately sets the tone for the operational relationship, including the parties' roles and responsibilities. It also sets the tone for how that relationship will end. The cost of change, in particular, can be extremely high following a significant transfer of operations and a highly integrated gainshare model.

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RECENT EVENTS

Transportation & Logistics Council (TLC) 44th Annual Conference

Marc S. Blubaugh participated in "The Transportation Attorney Panel" on the subject of liens. **Eric L. Zalud** presented *Outsourcing: Dealing with Contractors and Intermediaries*. **Martha J. Payne** moderated and **Stephanie S. Penninger** participated in the "Loss Prevention and Mitigation of Damages" panel.
March 19–21, 2018 | Charleston, SC

Columbus Logistics Breakfast Club

Marc S. Blubaugh presented *Blockchain in Transportation and Logistics*.
March 23, 2018 | Columbus, OH

Truckload Carriers Association (TCA) 80th Annual Convention

Stephanie S. Penninger, Matt Selby and **Jonathan Todd** attended.
March 25–28, 2018 | Kissimmee, FL

Trucking Industry Defense Association's Cargo Claims Seminar

Marc S. Blubaugh presented *Freight Claims in 2017: The Year in Review*.
April 4, 2018 | Tempe, AZ

Transportation Intermediaries Association (TIA) Capital Ideas Conference and Exhibition

Martha J. Payne presented *Ask the Expert—Transportation Attorney*. **Eric L. Zalud** presented *Kicking the Tires: Buying and Selling Logistics Businesses*. **Marc S. Blubaugh** participated in the panel "Avoiding Unintended Consequences and Stress on Relationships: Industry and Legal Perspectives." **Stephanie S. Penninger** participated in the panel "Real Life Claims Issues—How to Survive in the Jungle of Claims."
April 8–11, 2018 | Palm Desert, CA

2018 TerraLex Global Meeting

Eric L. Zalud attended.
April 18, 2018 | Barcelona, Spain

The Association for Corporate Growth (ACG) The Future of Food Conference

Stephanie S. Penninger attended.
April 19, 2018 | Chicago, IL

Greater New Orleans Barge Fleeting Association (GNOBFA) 36th River and Marine Industry Seminar

Stephanie S. Penninger attended.
April 24–27, 2017 | New Orleans, LA

National Shippers Strategic Transportation Council (NASSTRAC) Annual Shippers Conference & Transportation Expo

Marc S. Blubaugh presented *Check, Please! Who is Left Paying the Bill for Freight Charges, Cargo Claims, Detention and Demurrage, and Accidents?*
April 29–May 1, 2018 | Orlando, FL

National Customs Brokers and Forwarders Association (NCBFAA) Annual Conference

Jonathan Todd attended.
April 29–May 2, 2018 | Rancho Mirage, CA

ABA TIPS Section Conference and Admiralty & Maritime Law Committee Transportation Panel

Stephanie S. Penninger presented *Don't Be a Turtle! Handling the Reptile Theory and the High-Profile Transportation Case*.
May 3, 2018 | Los Angeles, CA

Intermodal Association of North America's Intermodal Operations & Maintenance Business Meeting

Marc S. Blubaugh attended.
May 2–4, 2018 | Lombard, IL

Maritime Law Association of the United States Spring Meetings

Kelly E. Mulrane attended.
May 2–5, 2018 | New York City, NY

Transportation Lawyers Association (TLA) Annual Conference

Stephanie S. Penninger presented *Facing Both Ways—Cargo Claims Handling for Transportation Intermediaries*. **Eric L. Zalud** presented *Legal Strategies for Risk Management in the Transportation Sector*. **Marc S. Blubaugh** attended.
May 2–6, 2018 | Orlando, FL

Warehousing Education and Research Council

Verlyn Suderman presented *Collaboration: The Key to Transformative Contracting*.
May 6–9, 2018 | Charlotte, NC

Columbus Logistics Conference

Marc S. Blubaugh presented *Transportation and Logistics: A Legal Update*. **Thomas B. Kern** attended.
May 16–17, 2018 | Columbus, OH

Columbus Roundtable of the Council of Supply Chain Management Professionals.

Marc S. Blubaugh presented *Blockchain 101: What it is and What it's Not!*
May 22, 2018 | Columbus, OH

The Ohio State University Fisher College of Business

Marc S. Blubaugh presented *Blockchain: How Will Blockchain Affect the Supply Chain?*
May 23, 2018 | Columbus, OH

Eye For Transport's North American 3PL & Supply Chain Summit

Marc S. Blubaugh and **Eric L. Zalud** attended.
June 5–7, 2018 | Atlanta, GA

Conference of Freight Counsel

Eric L. Zalud attended.
June 9–11, 2018 | Old Town Alexandria, VA

The Association of Transportation Logistics Professionals's Annual Meeting

Marc S. Blubaugh presented *New Technologies: Transforming Transportation and Transforming the Law.*.
June 10–12, 2018 | Washington, D.C.

Transportation Lawyers Association's (TLA) Executive Committee Meeting

Marc S. Blubaugh, Eric L. Zalud and **Stephanie S. Penninger** attended.
June 15–16, 2018 | Los Angeles, CA

Global Cold Chain Expo

Stephanie S. Penninger presented *Perish the Thought: The Challenges of Transporting Food*.
June 26, 2018 | Chicago, IL

American Trucking Association (ATA) Forum for Motor Carrier General Counsel 2018

Margo Wolf O'Donnell presented *Top Workforce Legal Trends and Employment Law Trends: Probability and Preparation*. **Risto Pribisich** presented *Taking Control: Critical Provisions in Technology Contracts - From Licensing Agreements to SaaS and Beyond*. **Martha J. Payne** and **Eric L. Zalud** attended.
July 15–18 | Santa Ana Pueblo, NM

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ON THE HORIZON

National Tank Truck Carriers (NTTC) 2018 Summer Membership & Board Meeting
Richard A. Plewacki is attending.
August 8–10, 2018 | Vail, CO

Cleveland State University—Monte Ahuja College of Business
Marc S. Blubaugh is presenting *Blockchain 101: Will Blockchain Transform the Supply Chain?*
August 10, 2018 | Cleveland, OH

21st Annual Northeast Ohio Logistics Conference
Jonathan Todd is attending.
August 20, 2018 | Akron, OH

Intermodal Association of North America's (IANA) Intermodal Expo
Marc S. Blubaugh, Martha J. Payne and **Stephanie S. Penninger** are attending.
September 16–18, 2018 | Long Beach, CA

Arkansas Trucking Seminar
Eric L. Zalud is attending.
September 18–20, 2018 | Rogers, AR

Benesch Seminar: Privacy and Security—How to Protect What Your Company Values Most
Stephanie S. Penninger is presenting *Emerging Technologies for Transportation Service Providers and Mitigating Risk.*
September 20, 2018 | Chicago, IL

3rd Annual DAT User Conference
Martha J. Payne is presenting.
September 24–26, 2018 | Portland, OR

2018 Conference on Innovation and Cost Savings
Eric L. Zalud is attending.
September 25, 2018 | Ontario, Canada

Truckload Carriers Association (TCA) Fall Policy Committee and Board of Directors Meetings
Richard A. Plewacki is attending.
September 26, 2018 | Arlington, VA

Wreaths Across America Gala
Richard A. Plewacki is attending.
September 28, 2018 | Arlington, VA

Breakbulk Americas Exhibition
Stephanie S. Penninger is attending.
October 2–4, 2018 | Houston, TX

Trucking Industry Defense Association (TIDA) 26th Annual Seminar
Eric L. Zalud is attending.
October 3–5, 2018 | Austin, TX

The Essentials of Warehousing Conference
Marc S. Blubaugh is presenting on transportation law fundamentals.
October 10, 2018 | Atlanta, GA

ABA TIPS Fall Leaership Meeting
Stephanie S. Penninger is attending
October 10–14, 2018 | Amelia Island, FL

Armstrong 3PL Value Creation Summit
Eric L. Zalud is attending and presenting.
October 16–18, 2018 | Chicago, IL

Logistics and Transportation National Association (LTNA) National Conference 2018
Eric L. Zalud is attending.
October 17–19, 2018 | New Orleans, LA

Canadian Transport Lawyers Association (CTLA)—AMG & Educational Conference 2018
Martha J. Payne and **Eric L. Zalud** are attending and will each be presenting on *M&A in the Transportation & Logistics Sector.* **Stephanie S. Penninger** will present on *Bankruptcy Cases Involving Shipping Companies and Arresting Vessels.*
October 25–27, 2018 | Montreal, Canada

American Trucking Association Management Conference and Exhibition
Marc S. Blubaugh, Richard A. Plewacki and **Jonathan Todd** are attending.
October 27–31, 2018 | Austin, TX

The Capital Roundtable's Conference on Private Equity Investing in Transportation and Logistics
Marc S. Blubaugh, Eric L. Zalud, Peter K. Shelton, Julie M. Price and **Jonathan Todd** are attending.
November 1, 2018 | New York City, NY

51st Transportation Law Institute (TLI)
Eric L. Zalud, Marc. S. Blubaugh, Martha J. Payne, Stephanie S. Penninger and **Jonathan Todd** are attending.
November 9, 2018 | Louisville, KY

Women in Trucking 2018 Accelerate! Conference and Expo
Martha J. Payne is presenting. **Stephanie S. Penninger** is attending.
November 12–14, 2018 | Frisco, TX

For further information and registration, please contact **MEGAN THOMAS**, Client Services Manager, at mthomas@beneschlaw.com or (216) 363-4639.