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EMPLOYEE MISCLASSIFICATION - THE NEW WORLD ORDER?

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With several companies engaging a section of their workers as independent contractors, these companies are not complying with labor and employment laws in relation to such workers...

Possibly, the current biggest HR-legal issue faced by on-demand and gig economy companies globally is whether their workers are being misclassified. Several companies in this sector have been engaging a section of their workers as independent contractors and not as employees. As a result, these companies do not comply with the labor and employment laws in relation to such workers.

Various courts have been examining this issue of whether workers have been misclassified as independent contractors and accordingly be entitled to employmentrelated benefits and protection. On April 30, 2018, the California Supreme Court passed an important decision on this topic. The judgment is likely to have a huge impact on such arrangements and can potentially change the legal landscape for gig economy companies in California, USA, and possibly worldwide!

The case relates to Dynamex Operations West Inc. v. The Superior Court of Los Angeles County. Dynamex, which is a package and document delivery company in the US, had adopted a new policy and contractual arrangement under which its truck drivers were regarded as independent contractors instead of employees, contrary to its previous practice. The drivers filed a class action lawsuit stating that they have been misclassified as independent contractors. The basis of their argument was that they continued to perform the same tasks as they had when they were employees

of Dynamex and the fact that Dynamex continued to exercise the same level of control on them.

The California Supreme Court, while deciding on the matter, confirmed the trial court's decision that the drivers were indeed misclassified as independent contractors and were actually employees of Dynamex. In this case, the Supreme Court adopted the 'ABC' test, which basically states that all of the following three factors must be established by an employer in order to successfully claim that a worker is an independent contractor:

> An employee called by any other name remains an employee. The actual relationship does not depend on the nomenclature devised to defeat the law

A. A worker is free from an employer's control and direction in connection with the performance of the work, both under the contract and in fact;

B. The work performed takes place outside the usual course of an employer's business and off the site of such business; and

C. A worker is customarily engaged in an independently established trade, occupation, profession, or business which is of the same nature as the work performed by a worker for an employer.

If any of the above tests are not satisfied, a worker is likely to be categorized as an employee instead of an independent contractor, triggering liabilities relating to minimum wage, working hours, working conditions, social

security, insurance coverage, health & safety, etc. Employers in California may also face monetary fines ranging from US$5,000-25,000 per violation. Incidentally, in the 'ABC' test, there is a presumption that a worker is an employee, unless proved otherwise. Accordingly, the burden to establish that a worker is indeed an independent contractor lies upon the company engaging such workers.

This new test is fairly wide and is likely to result in several independent contractors being reclassified as employees. In fact, not just in the gig economy, but organizations operating in varied sectors including information technology, pharmaceuticals, media and entertainment, logistics, journalism, financial services, etc. are also likely to be adversely impacted. Point B of the 'ABC' test is in particular going to be a challenge for most employers to comply with. In fact, it has already been previously ruled that if a service contract has a 'work made for hire' clause, a worker is automatically deemed to be an employee. This new test will make it more difficult for employers to engage independent contractors.

Indian courts have also been examining similar issues in the past. One of the earliest judgments in this context was that of the Supreme Court of India in relation to *Dhrangadhara Chemical Works v. State of Saurashtra*[1] where it was held that the prima facie test that determines the relationship is the right of control of the manner in which the work is to be done. The nature or extent of control as such varies from business to business, and hence, it is not possible to precisely define it.

Accordingly, it is necessary to distinguish between a 'contract of service' and a 'contract for service' — the former involves control and supervision, and accordingly, it is likely to be construed as an employment relationship, while the latter does not since the independent contractor undertakes to perform a service or complete an assignment based on his/her expertise and experience. The Bombay High Court ruled in the case of *Electronic Corporation of India*[2] that control is important but not decisive and that there is no single test to distinguish between a contract of service and a contract for service. In this case, 'retainers' appointed to carry out repairs and maintenance services had claimed permanency on the grounds that they were employees.

In the same year, the Supreme Court of India passed a ruling in the case of *Ram Singh v. Union Territory of Chandigarh*[3] that the tests to be considered include control, integration with the employer's business, power to appoint and dismiss, liability to pay remuneration and deduct contributions, liability to organize work and supply equipment, nature of mutual obligations, and finally, the terms of the contract between the parties.

There have also been several cases in India relating to non-contribution of provident fund and insurance contributions and on the extent of tax deducted at source. For example, *Lakshminarayan Ram Gopal & Sons Ltd. v. Government of Hyderabad*[4] laid down the factors distinguishing servant from an agent, such as (i) generally, a master can tell his servant what to do and how to do it, (ii) generally, a principle cannot tell his agent how to carry out his instructions, (iii) a servant is under more complete control than an

agent, (iv) generally, a servant has no authority to make contracts on behalf of his master, and an agent can be authorized to do so, etc. It must be noted that the Internal Revenue Service (IRS), which is a U.S. government agency responsible for the collection of taxes and enforcement of tax laws, has already laid down an extensive 20-factor test for determining common law employment relationship.

This development reminds us of the fact that an employee called by any other name remains an employee. The actual relationship does not depend on the nomenclature devised to defeat the law.

1. 1957 LLJ 478;
2. 2004 II CLR 256;
3. 2004 1 CLR 81;
4. (1954) 25 ITR 449 (SC)