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## SENATE COMMITTEE ON APPROPRIATIONS

Senator Anthony Portantino, Chair  
2019 - 2020 Regular Session

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### AB 323 (Blanca Rubio) - Newspapers: state agency advertising: worker status: independent contractors

**Version:** August 7, 2020

**Urgency:** No

**Hearing Date:** August 17, 2020

**Policy Vote:** L., P.E. & R. 5 - 0

**Mandate:** No

**Consultant:** Robert Ingenito

**Bill Summary:** AB 323 would (1) extend an existing exemption for newspaper distributors from the 'ABC Test' from January 1, 2021 to January 1, 2023, and (2) grant a preference to local news organizations, including ethnic and community news organizations, when state agencies are placing marketing and outreach advertisements.

#### Fiscal Impact:

- The enacted 2020-21 state budget provides resources to implement AB 5 (see below), including \$17.5 million for the Department of Industrial Relations (DIR), and \$3.4 million for the Employment Development Department (EDD). Both agencies indicate that they can implement this bill's requirements with the above provided resources.
- The Department of General Services (DGS) indicates that it would incur annual General Fund costs of \$152,000 to implement its provisions of the bill.
- The Franchise Tax Board (FTB) indicates that the bill would have an unknown impact on revenues (see Staff Comments). FTB's implementation costs would be minor and absorbable.

**Background:** New business models and communications technologies have led many workers to supply their labor outside of the traditional employment relationship in recent years. An incentive exists for employers to misclassify their employees as independent contractors and illegally avoid paying the cost of benefits. Misclassified employees often are denied access to critical benefits and protections they are entitled to by law, such as the minimum wage, overtime compensation, family and medical leave, unemployment insurance, and safe workplaces. Employee misclassification generates substantial losses to the federal government and state governments in the form of lower tax revenues, as well as to state unemployment insurance and workers' compensation funds. Thus, the misclassification of employees represents a cost-shift from an employer to the employee and state taxpayers. Empirical evidence suggests the use of independent contractors has become more pervasive; one study concluded that the number of workers classified as independent contractors rose 30 percent during the years 2005 to 2015.

With respect to classification of employees, the primary court precedent is less than precise on who was an independent contractor and who was not. Specifically, in *S. G. Borello & Sons, Inc. v Dept. of Industrial Relations* (1989) 48 Cal.3d 341, the California

Supreme Court created an 11 point “economic realities” test on whether someone could lawfully be considered an independent contractor. Outside of particularly clear-cut instances, this made determining who was or was not an independent contractor complicated, expensive, and prone to litigation, resulting in considerable frustration for both worker and employer stakeholders.

In early 2019, the California Supreme Court revisited the independent contractor issue in *Dynamex Operations West v. Superior Court* (2018), and concluded that certain package delivery drivers were misclassified as independent contractors rather than employees under a California wage order specific to the transportation industry. Thus, under *Dynamex*, the test for whether a worker is an independent contractor or an employee is greatly simplified to a three-prong test: (A) 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, (B) the worker performs work that is outside the usual course of the hiring entity’s business, and (C) 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.

In 2019, the Legislature passed, and the Governor signed, AB 5. This measure codified the *Dynamex Operations West v. Superior Court* decision, creating a strict ABC test for determining who can be classified as an independent contractor. Importantly, however, AB 5 also provided explicit industrial categories where the long-standing Borello test would remain the standard for determining who is an employee. A companion measure, AB 170, exempts, among others, newspaper distributors working under contract with a newspaper from the ‘ABC’ test, instead placing such workers under the Borello standard. The newspaper distributor exemption expires on January 1, 2021

**Proposed Law:** The bill would do the following:

- Extend the newspaper distributor exemption to January 1, 2023.
- State that state agencies must grant a preference to local news organizations, including ethnic and community news organizations, when contracting or subcontracting for marketing or outreach advertising.
- Require DGS to report annually on each state agency that paid for marketing or outreach advertising, the amounts paid to each media platform, and the recipients of the amounts paid by a state agency for advertising.

**Related Legislation:**

- AB 5 (Gonzalez, Chapter 296, Statutes of 2019) codifies the recent *Dynamex* decision, requiring that employers prove that their workers can meet a three-part (ABC) test in order to be lawfully classified as independent contractors.
- AB 170 (Gonzalez, Chapter 415, Statutes of 2019) exempts, among others, newspaper distributors working under contract with a newspaper from the ‘ABC’ test, instead placing such workers under the Borello standard. The newspaper distributor exemption expires on January 1, 2021.

**Staff Comments:** DGS anticipates minor and absorbable one-time costs for developing the processes to report marketing and advertising contracts, but would face on-going cost of \$152,000 annually to compile the information submitted by departments, and drafting an annual report to be published by April 1. DGS notes that the bills tracking and report

FTB notes that bill could result in some workers who would be treated as employees under current law would instead be reclassified as independent contractors under the bill's proposed exclusion. This reclassification would shift responsibility for a number of business related expenses from businesses to the workers. An increase of qualified business expenses to the workers would likely result, decreasing their tax liability. At the same time, the decrease in expenses to businesses would likely increase their tax liability. FTB notes that the net effect of these changes would depend on (1) the marginal tax rates of the businesses and workers involved, and (2) any adjustment that may take place in compensation levels or related business expenses, and that net effect of all these changes on aggregate tax liability is not known.

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