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Vazquez v. Jan-Pro Franchising Int'l, Inc.: *More Than Just Retroactive*

By George Abele & Laura Zabele

On May 2, 2019, the Ninth Circuit ruled that the California Supreme Court's recent decision in *Dynamex Operations West v. Superior Court*, 4 Cal. 5th 903 (2018) ("*Dynamex*") applies retroactively. *Vazquez v. Jan-Pro Franchising Int'l, Inc.*, 2019 U.S. App. LEXIS 13237 (9th Cir. May 2, 2019) ("*Vazquez*"). But the court did not stop there; it "provided guidance" to the district court on how to apply *Dynamex*'s ABC test in light of the record developed thus far. The Ninth Circuit's ruling reminds businesses in California to closely analyze how they have engaged independent contractors—even before the *Dynamex* decision—and to consider steps to minimize the risk of wage-and-hour litigation under the ABC test.

Background

Vazquez is a decade-old class action that originated in the District of Massachusetts. Plaintiffs were janitor-franchisees of defendant, Jan-Pro Franchising International, Inc. ("Jan-Pro"), an international janitorial cleaning business. Plaintiffs alleged that, through a "three-tier franchising model," Jan-Pro had misclassified them as independent contractors.[1]

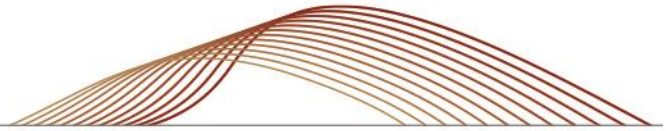
Over Jan-Pro's objections, the District of Massachusetts severed the California plaintiffs' claims and sent them to the Northern District of California, where those plaintiffs resided. Then, in mid-2017, the district court granted summary judgment in favor of Jan-Pro, concluding that the individuals performing the cleaning services were independent contractors. The district court's analysis relied on the three definitions of "to employ" set forth in *Martinez v. Combs*, 49 Cal. 4th 35 (2010), and concluded that none of them had been met.

But then came *Dynamex*, in which the California Supreme Court adopted the "ABC" test for determining whether workers are independent contractors under California wage orders. As a quick reminder, the three inquiries for the ABC test are as follows:

1. Is the worker free from the control and direction of the hiring entity?

2. Is the worker performing work that is outside the usual course of the hiring entity's business?

3. Is the worker customarily engaged in an independently established trade, occupation, or business?



Each factor is dispositive and, notably, the burden of proof is on the hiring entity to establish all three factors to prove independent contractor status. Thus, the ABC test presumes an employment relationship.

When the California Supreme Court decided *Dynamex*, *Vazquez* already was on appeal. The Ninth Circuit ordered the parties to brief the effect of *Dynamex* on the merits of the case. Of critical importance was whether *Dynamex* applied retroactively.

Opinion

Part 1: Dynamex Applies Retroactively

The Ninth Circuit concluded that *Dynamex did* apply retroactively. As a result, it vacated the district court's grant of summary judgment to Jan-Pro and remanded for further proceedings.

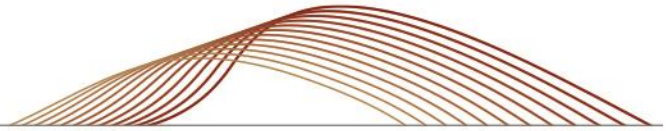
In explaining its decision, the court cited California's "general tradition that judicial pronouncements have retroactive effect," as well as "the emphasis in *Dynamex* on its holding as a clarification rather than as a departure from established law." *Vazquez*, 2019 U.S. App. LEXIS 13237, at *26-28. Moreover, although Jan-Pro and an amicus raised due process concerns,[2] the court reasoned that applying *Dynamex* retroactively would be "neither arbitrary nor irrational," since the wage orders at issue were remedial in nature and meant to be "liberally construed in a manner that services [their] remedial purpose." *Id*. at *29-30. The court also cited policy concerns identified in the *Dynamex* decision and concluded that, "[b]y applying *Dynamex* retroactively, we ensure that the California Supreme Court's concerns are respected." *Id.* at *30.

Part 2: A Discussion of the ABC Test

The *Vazquez* opinion does not end there, however. In what could be called an advisory opinion, the court went on to provide its "observations and guidance" for how the district court should apply *Dynamex* on remand—particularly focusing on Part B of the ABC test, which it noted "may be the most susceptible to summary judgment on the record already developed." *Id*. at *48. First, the court observed that "[other] courts have framed the [Part] B inquiry in several ways," including (i) whether the work of the employee is necessary to or merely incidental to that of the hiring entity; (ii) whether the work of the employee is continuously performed for the hiring entity; and (iii) what business the hiring entity proclaims to be in. *Id*. at *49. Advising that "[a]ll of these formulations should be considered," *id.*, the court considered each mini-part in turn.

With respect to Part B(i), the Ninth Circuit described this inquiry as either a "common-sense observation" of the nature of the business (e.g., floor measurers are necessary to the business of a carpet retailer) or a consideration of "economic terms," such as whether the business's revenues were derived from or affected by the worker's earnings. *Id.* at *49-51. The court noted that Jan-Pro received a percentage of revenue generated by the workers; thus, Jan-Pro was "actively and continuously profiting from the performance of those cleaning services as they are being performed," and its business "ultimately depends on someone performing the cleaning." *Id*. at *51-52. The court contrasted these facts with a case involving taxicab operators who paid a flat fee to lease taxicab medallions. *Id*. at *50-51. Because the medallion lessor's revenues were not affected by how much the taxicab drivers worked, the drivers were considered incidental to the operations of the lessors. *Id*.

For Part B(ii), the Ninth Circuit advised that the district court should consider "whether Jan-Pro's business model relies on unit franchisees continuously performing cleaning services." *Id*. at *53. As for Part B(iii), in determining the usual course of a hiring entity's business, the Ninth Circuit observed that



"courts [generally] consider how the business describes itself," such as through websites and advertisements. *Id*. For Jan-Pro, the court noted that its website described itself as a "commercial cleaning company." *Id*. Although Jan-Pro argued that it was in the business of "franchising," rather than cleaning, the Ninth Circuit expressed skepticism regarding that argument. *Id*. at *54.

Although the court did not similarly analyze Parts A and C of the ABC test, it observed that they were "most likely to trigger the need for further factual development, because the considerations relevant to those [parts] are the most factually oriented." *Id*. at *48. Overall, the Ninth Circuit concluded that the district court should "consider all three [parts] of the ABC test and, in doing so, may wish to consider authorities from other jurisdictions that apply the test."[3] *Id*. at *42.

Legal Takeaways

Jan-Pro likely will petition the Ninth Circuit to rehear the appeal *en banc*, and there currently are dueling proposals in the California legislature that would either codify the ABC test or restore the old test, which focuses primarily on the hiring entity's power to control the worker. In the meantime, below are considerations to keep in mind:

- *Vazquez* was not the first court to apply *Dynamex* retroactively. In *Johnson v. Vcg-Is*, for example, the Orange County Superior Court held that *Dynamex* applied retroactively to plaintiffs' Private Attorneys General Act ("PAGA") lawsuit based on wage order and Labor Code violations. 2019 Cal. Super. LEXIS 5 (Feb. 1, 2019).

- Applying *Dynamex* retroactively does not necessarily mean that the ABC test applies to all claims.

  - For example, in *Curry v. Equilon Enters., LLC*, 23 Cal. App. 5th 289 (2018), California's Fourth Appellate District concluded the ABC test did not apply in the joint employer context (although the court analyzed plaintiff's claims under the ABC test anyway, "out of an abundance of caution").[4] Similarly, in *Perkins v. Knox*, 2018 Cal. Wrk. Comp. P.D. LEXIS 490 (2018), the California Workers' Compensation Appeals Board declined to apply the ABC test to workers' compensation claims.

  - Likewise, not all wage-and-hour claims are necessarily affected by the *Dynamex* decision. In *Garcia v. Border Transp. Grp., LLC*, 28 Cal. App. 5th 558 (2018), for example, a California appellate court declined to apply the ABC test to "non-wage-order" claims, such as waiting time penalties under Labor Code § 203, and wrongful termination in violation of public policy.[5]

- Although no private right of action exists under Labor Code § 226.8 for willfully misclassifying individuals as independent contractors, *see, e.g., Noe v. Superior Court*, 237 Cal. App. 4th 316, 341 (2015), plaintiffs will seek penalties through PAGA for misclassification claims.

- Outside of California (and other states that apply the ABC test, such as Massachusetts), companies may be able to breathe a little easier. On April 29, 2019, the U.S. Department of Labor ("DOL") issued Opinion Letter FLSA2019-6, which concluded that workers who provide services to virtual marketplace companies (i.e., the gig economy) are independent contractors. It the Opinion Letter, the DOL applied the six-factor "economic realities" test under the Fair Labor Standards Act and found that all factors pointed to economic

independence, or independent contractor status. Although the letter is advisory and non-binding, it is nevertheless helpful to understand how the current DOL will analyze misclassification claims.

Many practical considerations also flow from the *Vazquez* decision. Please contact Paul Hastings to discuss your individual circumstances.

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If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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[1] Under the three-tier model, Jan-Pro contracted with intermediary "master owners" (regional, third-party entities) that in turn sold business plans to "unit franchisees," the entities or individuals who performed the cleaning services. The intermediary "master owners" were not named in the litigation.

[2] Jan-Pro and its amicus also raised policy arguments for why the ABC test should be applied differently in the franchise context. *Id.* at *42-45 (citing *Patterson v. Domino's Pizza, LLC*, 60 Cal. 4th 474 (2014)). The Ninth Circuit found these arguments to be "of limited persuasive value," in part because the case law cited by Jan-Pro and the amicus concerned vicarious liability in tort cases, which "have little to do with the rationale for wage orders," namely, "[to] creat[e] incentives for economic entities to internalize the costs of underpaying workers." *Id.* at *44. The court further noted that franchise-specific concerns "would apply just as much in Massachusetts, where courts have routinely applied the codified ABC test to franchises (and have routinely held against franchisors)." *Id.* at *45. The public policy implications of this ruling will likely continue to be the subject of future debate.

[3] Following its own advice, the Ninth Circuit cited case law from Connecticut, Illinois, Maine, Massachusetts, Michigan, Utah, and Vermont in its opinion. A number of those cases are somewhat dated. For example, in analyzing Part B(ii), the court cited a Michigan case from 1918 and two Utah cases from 1976 and 1985. In contrast, the California Supreme Court in *Dynamex* relied on more recent opinions from Massachusetts and New Jersey.

[4] *Vazquez* summarily dismissed the usefulness of *Curry*, without commenting that it arose in the joint employer context, rather than the independent contractor/employee context. *Vazquez*, 2019 U.S. App. LEXIS 13237, at *54-55.

[5] Note, however, that on May 3, 2019, the California Labor Commissioner released a letter stating that the ABC test from *Dynamex* applies to Labor Code *and* wage order claims—including claims such as reimbursement claims under § 2802 and waiting time penalties under § 203. The Labor Commissioner's letter is not binding on courts.