

Human Resources

Court Creates New Independent Contractor Test

THE CALIFORNIA Supreme Court has handed down a decision that rewrites the state's independent contractor law by adopting a more stringent test for determining whether or not someone is an employee for wage order cases.

The new law will affect any California business that uses independent contractors and it makes it more difficult to classify someone as an independent contractor.

In its decision in *Dynamex Operations West, Inc. vs. Superior Court*, the court rejected a test that's been used for more than a decade in favor of a more rigid three-factor approach, often called the "ABC" test.

The big change

The prong that changes the most is the B prong under the ruling (see box on right). Prior to

this decision, a hiring entity could show that a worker is an independent contractor by either demonstrating that they work outside the course of the company's usual business or outside all of the places of business of the hiring company.

The decision essentially deletes the second clause about outside all of the places of business of the hiring company.

In other words, the only way to be an independent contractor is if the work falls outside the scope of the usual course of business of the hiring entity. So, if you have employees doing the same work as an independent contractor, there could be a problem.

While this shouldn't interfere with your business if you hire a contractor to come in and work on building repairs, companies that have been using the independent contractor model to conduct their business may run into problems.

THE NEW 'ABC' TEST

Under this new test, a person would be considered an independent contractor only if the hiring entity can prove:

- A.** That the worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact.
- 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 the work performed (in other words, that the worker is in business for themselves).

It should be noted that this case only concerns wage orders issued by the Industrial Welfare Commission, and does not apply to other wage and hour laws.

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Commissioner Approves 10.3% Benchmark Rate Cut

THANKS TO the reforms enacted in 2014, California Insurance Commissioner Dave Jones has ordered a 10.3% average mid-year decrease to the state's benchmark workers' comp rates.

The new benchmark rate, which insurers use as a guidepost to price their policies, will take effect on July 1.

The benchmark is essentially the base rates that cover expected costs of claims and claims-adjusting expenses across all worker class codes.

Insurers can price their policies as they wish, so there is no guarantee that any particular employers will see rate cuts. When pricing your policy, your insurer will take into account your claims history, your industry and your geographic location, among other factors.

Why are rates falling?

The benchmark rate is falling due to the effects of SB 863, which took effect in 2014. The Workers' Compensation Insurance Rating Bureau said in its rate filing that besides increasing permanent and temporary disability payments to injured workers, the law has reduced claims costs by:

- Significantly reducing the number of spinal surgeries.
- Reducing bureaucratic tie-ups, leading to increases in claim settlement rates. At the 48-month mark, 77.1% of claims had been settled in 2017, up from 71.1% in 2011. The Rating Bureau says the law has accelerated the rate in which claims have settled as a result of

quicker medical-treatment resolution through the use of independent medical review, reduction in the volume of liens and the drop in spinal surgeries. The higher claims settlement rates have also decreased the cost of adjusting claims.

- Setting requirements for lien filings and simplifying the lien system. Before new rules on liens took effect, in 2016 the Workers' Compensation Appeals Board was receiving 25,500 liens a month. After the rules took effect, lien filings had fallen 40% to a monthly average of 15,500 as of March 2017.

Also, a new Medical Treatment Utilization Schedule drug formulary, which took effect Jan. 1, 2018, is expected to reduce costs as well.

The black marks

The one area of concern is cumulative injury claims, which continue to grow in numbers mostly in the Los Angeles area and San Diego. The ratio of cumulative injury claims in the LA area had grown to 15.5 claims per 100 indemnity claims in 2016, up from 8.7 in 2011.

In San Diego, they accounted for 11.2 claims per 100 indemnity claims in 2016, up from 6.6 claims in 2011.

In addition, the average cost of medical treatment is also on the way up, but at a relatively low rate of 3% a year. ❖

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Workers are Employees if Job Is in 'Usual Course' of Operations

That means for other cases not concerning wage orders, an earlier decision known as the "Borello" decision still stands in terms of the independent contractor test.

In Borello, the Supreme Court held that the "right to control" the means and manner in which work is performed is the most key factor when evaluating a classification analysis. Other factors include:

- Ownership of equipment
- Opportunity for profit and loss, and
- The belief of the parties.

This test is more flexible because it balances the different factors

to arrive at a classification based on individual circumstances of each case.

Prior to Dynamex, many referred to the multi-factor Borello test as the traditional "common law" classification analysis.

The takeaway

The court has abandoned the existing test for deciding a worker's employee status, which included factors like whether a person could be fired without cause and amount of supervision.

Now, workers are considered employees if their job is considered to be the "usual course" of the business operations. ❖

Protecting Your Important Data When Employees Leave

WHEN IS a business most susceptible to losing data, intellectual property and important records? No, not during a cyber attack or a break-in, but during lay-offs.

With employees maybe feeling disgruntled after being let go, it's common for some of them to pocket important company data – usually client lists, old e-mails, vendor contacts and even intellectual property that is essential to the company's competitive advantage.

During lay-offs or termination, you need to take steps to protect your data and intellectual property, but there are legal implications. Consider the following:

Non-disclosure agreements – These focus on company data that a competitor can use to harm the business.

These agreements spell out the employee's fiduciary obligations under the law by identifying protected company information. The agreement requires that the employee keep such information secret for a certain period of time.

Return and inventory all company property – Before your employee leaves the premises, make sure they have returned all of your property that may contain company data like:

- Laptops.
- Originals and copies of company documents the employee has made.
- Data on the worker's personal phone or home computing devices (this may be difficult to enforce, but you should make them aware that they are required to delete it).

Passwords and access – On their last day, remember to delete from your database and systems their user names and passwords and access codes. This could include:

- E-mail passwords
- Voicemail passwords
- Teleconference and intranet passwords
- VPN access and passwords
- Building or office coded lock-access codes.

Make sure to collect company ID cards. If you have concerns they may try to contact your customers or vendors for any reason that could be detrimental to your firm, you can notify them that the employee is no longer with you.

Conduct an exit interview – During this interview, you should go over why they were let go and the importance of not taking with them any physical or intellectual property.

Ask questions to determine what, if any, company data they may have been privy to or had access to. Also, if you have a non-disclosure agreement in place, use this time to reiterate the consequences for violating those agreements.

Get ahead of legal issues

Tread carefully when laying off staff, and in particular when trying to protect your important company data. Consult your lawyer before putting any policies in place. ❖



Directors of Small, Mid-sized Firms Increasingly Sued

JURY AWARDS and settlements against directors and officers of companies have increased dramatically, largely due to federal securities class-action lawsuits.

But while small and mid-sized business owners often believe they won't be targeted by those kinds of lawsuits, directors and officers of privately held companies can also be sued, leaving their personal assets at risk.

Unfortunately, many small and mid-sized business owners, while insuring their businesses, often overlook their directors' liability. This protection gap can be covered with directors and officers (D&O) liability insurance, which protects company leaders from litigious employees, competitors, investors, vendors – and even customers.

Directors and officers can be held personally liable for civil, criminal or regulatory proceedings should they fall short of their obligations, and their personal assets could all be at risk.

General liability or umbrella business insurance policies do not cover claims involving directors and officers.

For smaller firms, which typically have fewer resources to defend allegations or fund potential fines, penalties or awards for damages, D&O is becoming an increasingly important coverage.

One in eight owners of small businesses surveyed by Chubb Group reported having been sued in the previous five years. The average damage from the lawsuits was \$225,682 in losses. Some suits cost much more, with losses approaching \$5

million.

What D&O covers

One of the most important aspects of a D&O policy is that it's a protection against the costs of frivolous lawsuits.

D&O covers court costs and lawyers' fees if a business becomes the target of regulators, or even a criminal investigation. But the policy will not shield managers if they commit fraud or participate in crime.

That said, if one board member is convicted of fraud while the other board members are innocent, a policy could still cover the legal costs of those who did no wrong.

The typical action that would trigger a D&O policy would allege that management committed some wrongful acts.

Sometimes it's best to mix and match coverages based on your organization-specific risks. For some companies, a Side A will do.

Common claims for small firms

- Allowing misleading information in a company prospectus.
- Not complying with regulations and laws.
- Employee-driven lawsuits alleging management allowed harassment or discrimination despite knowing about it.
- Suits by investors about decisions concerning mergers and acquisitions.

Different 'sides' of D&O policies

There are varying deductibles for the different "sides" of the policy.

Side A – Known as the "personal protection" part of the policy, this indemnifies directors and officers if the company is unable to do so.

Side B – This part reimburses a company if it pays the legal bills of its directors and officers due to an action against them in their company capacity. Side B responds most commonly in the majority of claims brought against directors and officers.

Side C – Known as "entity coverage," this part covers a company if it is sued alongside any directors and officers.

We can evaluate and review the coverages and policy language associated with D&O insurance for you to find a policy that best suits your organization and board.

Cost of coverage

There are a number of low-cost D&O policies available for small firms. The cost of providing a director with \$1 million limit is more affordable than you may realize. Call us for details.

Sometimes you will have little choice to purchase a policy. For example, many directors and officers may refuse to take on a position without the coverage. And if your business wants to attract new funding, most institutional investors require the protection. ❖



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