

Independent Contractor vs. Employee: Navigating California’s Stricter Classification Rules with Federal FLSA Standards in 2026, by Kartikey A. Pradhan, Esq. and John Deagon, Esq., 4-14-2026

As worker classification laws continue to evolve, employers face new challenges in determining who qualifies as an “employee” versus an “independent contractor.” Federal agencies, state legislatures, and courts—particularly in California— apply different and sometimes overlapping standards, leaving businesses to navigate a complex compliance landscape. In jurisdictions like California, where the default presumption is employee status, misclassification is not a technical compliance issue but a significant driver of litigation exposure.

The Core Problem: Divergent Standards Creating Inconsistent Risk

At the federal level, worker classification under the Fair Labor Standards Act (FLSA) is currently governed by the U.S. Department of Labor’s multi-factor ‘economic realities’ framework, which examines the totality of the circumstances to determine whether a worker is economically dependent on the employer or instead in business for themselves. That framework, however, remains subject to ongoing regulatory change, as the DOL proposed revisions in February 2026.

California, however, applies a far more stringent ABC test, originally codified in Labor Code § 2750.3 and now located in §§ 2775–2787, with related provisions in those sections addressing exceptions and occupational carve-outs. Under this framework, a worker is presumed to be an employee unless the hiring entity establishes all three of the following:

- (A) The worker is free from the hiring entity’s control and direction in performing the work.
- (B) The work is performed outside the usual course of the hiring entity’s business.
- (C) The worker is customarily engaged in an independently established trade, occupation, or business.

Prong B tends to be the most difficult to satisfy—especially where contractors perform work integral to a company’s core operations.

It is important to note, however, that California’s ABC test is subject to numerous statutory exceptions and industry-specific carve-outs, including those set forth in California Labor Code §§ 2775–2787. In addition, certain worker classifications—most notably app-based drivers—are governed by separate frameworks, such as Proposition 22, which establish alternative criteria distinct from the traditional ABC analysis. As a result, classification determinations in California often require a threshold assessment of whether an exception applies before applying the ABC test itself.

Why Divergent Standards Matter

Because federal and state tests differ so sharply, national employers risk inconsistent results when using uniform classification models. Common consequences include:

- False sense of compliance. A classification model that satisfies federal standards may fail under California’s ABC test.
- Inconsistent workforce structures. Workers classified as independent contractors in one jurisdiction may require employee status in another.

- Increased litigation exposure. Plaintiffs’ attorneys often target multi-state companies, platform-based providers, and professional services models.

In practice, many employers rely on classification models that may satisfy federal standards but fail under California’s framework, creating systemic exposure across entire categories of workers.

Misclassification as a Gateway Claim

In California, a finding of misclassification frequently gives rise to additional claims, such as:

- Minimum wage and overtime violations (Lab. Code §§ 510, 1194)
- Meal and rest break violations (Lab. Code §§ 226.7, 512)
- Wage statement violations (Lab. Code § 226)
- Waiting time penalties (Lab. Code § 203)

These claims often proceed as class actions or Private Attorneys General Act (PAGA) representative actions, greatly amplifying potential liability. As a result, a single misclassification decision can cascade into multiple wage-and-hour violations across an entire category of workers.

From a litigation perspective, misclassification claims rarely stand alone and are typically leveraged to support broader wage-and-hour and PAGA exposure.

High-Risk Business Models in 2026

These models are frequently targeted in enforcement actions and litigation because they present structural difficulty in satisfying the ABC test.

Industries that may face heightened misclassification exposure include:

1. Gig economy and platform-based services. Core service providers often fail Prong B.
2. Professional services and consulting. Long-term contractors integrated into daily operations appear indistinguishable from employees.
3. Staffing and subcontracting models. Multi-layered relationships can conceal—but not eliminate—control and dependence.

Enforcement Trends and Litigation Focus

Regulators and plaintiffs’ counsel increasingly look beyond contracts to examine day-to-day realities:

- Substance over form. Written “independent contractor” labels carry limited weight where inconsistent with actual practices.
- Uniform policies and procedures. Standardized training, supervision, and operational controls may indicate employee status.

- Data-driven discovery Electronic communications, time records, and system access logs are frequently used to demonstrate integration and dependence.

Many lawsuits now frame misclassification as a systemic failure—inviting class and PAGA litigation. As a result, these cases are increasingly framed as enterprise-wide compliance failures, positioning them for class or PAGA treatment at the outset.

Practical Strategies for Employers

To mitigate risk, employers should consider:

1. Conducting classification audits that evaluate both federal (economic realities) and applicable state standards based on actual work practices;
2. Assessing Prong B exposure for roles tied to the organization's core business functions;
3. Restructuring roles where appropriate, including converting workers to employee status or narrowing the scope of contractor engagements;
4. Reinforcing indicia of independence, such as limiting control, reducing operational integration, and engaging bona fide independent businesses; and
5. Documenting classification decisions and periodically revisiting them to support good-faith compliance efforts.

Key Takeaways

- California is among the most stringent jurisdictions, with a broad ABC test and an active enforcement and litigation environment;
- Misclassification can lead to cascading liability through derivative wage-and-hour claims; and
- Proactive review, documentation, and jurisdiction-specific analysis are essential to mitigating risk.

Conclusion

Worker classification in 2026 remains a moving target shaped by evolving and, at times, conflicting federal and state frameworks. Employers that assume that compliance under one standard will automatically satisfy another may face significant exposure—particularly in jurisdictions like California, where the ABC test continues to be applied rigorously. Regular audits, thoughtful structuring of work relationships, and ongoing compliance review remain the most effective tools for managing risk in this complex and dynamic area.

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