



ABC Test Breaks Biden's \$400k Tax Pledge

Background on ABC Test

Assembly Bill 5 (AB5) is a California law established in 2019. AB5 contains a stringent three-stage worker classification test designed to determine whether a worker is an independent contractor or an employee. AB5's work restriction is known as the "ABC" test and goes far beyond federal guidelines on independent contractor classifications.

Under the three-step ABC test, businesses must prove that a contractor is doing duties "outside the usual course of work of the hiring entity" and that "the worker customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed." This significantly limits the ability of businesses to retain contractors who may operate within the scope of work sometimes performed by employees in similar circumstances. It is an unnecessary distinction that prevents most businesses from working with independent contractors.

Meanwhile, Democrats are attempting to enact a nationwide version of the ABC test in the "Protecting the Right to Organize" (PRO) Act, a laundry list of giveaways to Big Labor. The PRO Act has passed the House, and Senate Democrats are attempting to implement pieces of the PRO Act in the left's \$3.5 trillion tax-and-spend reconciliation spending blowout.

As part of this effort to backdoor the PRO Act, Democrats are attempting to include the "Unemployment Insurance Modernization Act" in reconciliation, [sponsored by](#) Sen. Ron Wyden (D-Ore.). Sec. 212 of the bill mandates that all 50 states must use the ABC test to determine if a worker is an employee or an independent contract for the purpose of receiving unemployment benefits.

Currently, there are two types of unemployment taxes businesses pay today on each employee:

- A federal unemployment tax (FUTA) which is 6% on each employee's first \$7,000 of earnings less 5.4% federal tax credit (Net—0.6%).
- A state unemployment tax (SUTA) which is up to 5.4% tax on at least the first \$7,000 in earnings per employee.

Unemployment Tax Today:

- States determine who is liable for their state unemployment tax.
 - Only California uses the strict ABC test for unemployment and has nearly 50 exemptions to it.
- Most states do not use any form of the ABC worker classification test.

Unemployment Tax under Senator Wyden's ABC Test:

- States **adopt** strict California ABC test without exemptions, then SUTA increases for employers who must reclassify independent contractors to be employees for unemployment insurance tax purposes.

OR

- States reject California ABC test in favor of their own test, then FUTA increases by 5.4% per employee due to loss of FUTA credit.

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Bottom Line: this would impose a tax hike on small businesses in states that do not adopt the restrictive California style "ABC test" for purposes of determining eligibility for unemployment insurance benefits.

The ABC Test Is A Violation of President Biden's \$400k Tax Pledge

The ABC Test is a tax hike on independent contractors:

According to the tax code, independent contractors can deduct legitimate business expenses like travel, home office setups, meals, vehicle use, rent, and health insurance premiums among many others. These deductions reduce the costs that independent contractors have to shoulder for being their own boss.

Employees cannot deduct business expenses. Given that the ABC test's stringent requirements would force the mass reclassification of independent contractors to employees, the approximately 59 million Americans that engage in some form of freelance work could lose access to these business deductions. This is a clear tax hike on millions of American workers.

The ABC Test is a tax hike on small business owners:

Regardless of structure, most small businesses pass revenue directly to individual owners who pays individual tax on Form 1040. For an individual small business owner that utilizes independent contractors, the ABC Test would make them subject to new unemployment insurance taxes as "employees". This would require more revenue to cover added payroll tax liability and results in less net income.

The ABC Test Clearly Violates the President's \$400,000 Tax Pledge:

President Joe Biden and Vice President Kamala Harris pledged to not raise taxes on Americans that make less than \$400,000 per year.

Given that tens of millions of American freelancers make less than \$400,000, any form of the ABC test that makes it into law would violate the Biden pledge.