

**TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
TWENTY-EIGHTH LEGISLATURE, 2016**

ON THE FOLLOWING MEASURE:

S.B. NO. 2694, RELATING TO EMPLOYMENT SECURITY.

BEFORE THE:

SENATE COMMITTEE ON JUDICIARY AND LABOR

DATE: Tuesday, February 16, 2016 **TIME:** 9:00 a.m.

LOCATION: State Capitol, Room 016

TESTIFIER(S): Douglas S. Chin, Attorney General, or
Robyn M. Kuwabe, Deputy Attorney General

Chair Keith-Agaran and Members of the Committee:

The Department of the Attorney General provides comments about this bill.

The purpose of this bill is to clarify Hawaii's employment security law, regarding the tests to be used in determining whether an individual is an independent contractor.

This bill preserves what is commonly referred to as the "ABC Test," found in section 383-6, Hawaii Revised Statutes, and adds a revamped version of the common-law twenty factor test, which is already found in the Department of Labor and Industrial Relations' administrative rules, section 12-5-2(b), Hawaii Administrative Rules. Because the two tests are already in the statute and administrative rules, this bill may not be necessary.

In addition, this bill also includes a definition of "independent contractor," which creates an internal conflict because the definition is not consistent with the ABC and the common-law tests provided in the bill for determining if an individual is an independent contractor.

Due to the fact that the ABC test and the 20-point test are already found in the statute and administrative rules, and because the proposed definition of independent contractor is internally inconsistent with the section, the Department respectfully asks that the bill be held.

DAVID Y. IGE
GOVERNOR

SHAN S. TSUTSUI
LIEUTENANT GOVERNOR



LINDA CHU TAKAYAMA
DIRECTOR

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**STATE OF HAWAII
DEPARTMENT OF LABOR AND INDUSTRIAL RELATIONS**

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February 15, 2016

To: The Honorable Gilbert S.C. Keith-Agaran, Chair,
The Honorable Maile S.L. Shimabukuro, Vice Chair, and
Members of the Senate Committee on Judiciary and Labor

Date: Tuesday, February 16, 2016

Time: 9:00 a.m.

Place: Conference Room 016, State Capitol

From: Linda Chu Takayama, Director
Department of Labor and Industrial Relations (DLIR)

Re: S.B. No. 2694 Relating to Employment Security

I. OVERVIEW OF PROPOSED LEGISLATION

SB 2694 amends section 383-6, Hawaii Revised Statutes (HRS), by adding a second criterion that must be met to determine the existence of an employee-employer relationship. A new subsection codifies the Internal Revenue Service (IRS) twenty common-law factors and requires that both a preponderance of these elements and the ABC test must be considered in the adjudication of independent contractor status.

Section 12-5-2, Hawaii Administrative Rules (HAR), currently identifies 20 factors to be used as a guide in deciding whether sufficient control or direction is present to establish employment. However, SB 2694 includes an alternative version of the 20 elements and adds definitions of "client and "independent contractor," ostensibly to simplify and facilitate the self-employment determination process.

DLIR opposes the measure and suggests amendments if the Committee chooses to move the measure.

II. CURRENT LAW

Act 219, Session Laws of Hawaii (SLH, 1939) created the Unemployment Insurance Program in Hawaii in response to federal action taken under the Social Security Act of 1935. The provisions amended in the proposal were incorporated

into Hawaii's law via Act 219 (SLH,1939):

The IRS applies the common-law standard for Federal Unemployment Tax Act (FUTA) purposes and developed the twenty point criteria to weigh facts relevant to an employer's right to control and direct an individual who performs services, whether that right is exercised or not. Whereas only part "A" of the ABC test must be passed to meet federal unemployment conformity requirements, section 383-6, HRS, requires that all three prongs be satisfied to render an independent contractor ruling under state law.

Section 383-6, HRS, provides that, "Services performed by an individual for wages or under any contract of hire shall be deemed to be employment subject to subject to this chapter irrespective of whether the common law relationship of master and servant exists unless and until it is shown to the satisfaction of the department of labor and industrial relations that:

1. The individual has been and will continue to be free from control or direction over the performance of such service, both under the individual's contract of hire and in fact; **and**
2. The service is either outside the usual course of the business for which the service performed or that the service is performed outside all the places of business of the enterprise for which the service is performed; **and**
3. The individual is customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the contract of service."

Section 12-5-2, HAR, defines terms used in the ABC test and includes the 20 factors intended to be used as a guide in determining whether an individual is an employee under common law rules. The rule clearly enunciates that the degree of importance of each factor varies depending on the occupation and the factual context in which the services are performed, without requiring a "preponderance of factors."

III. COMMENTS ON THE SENATE BILL

The measure as written creates conflicts in statutory interpretation that would delay decision-making and likely encourage more appeals of coverage determinations.

The Department raises the following concerns regarding SB 2694:

1. Subsection (b) effectively replaces the 20 factors contained in the HAR, and assumes that these factors "shall be guidelines for determining whether an individual could be deemed an independent contractor." This reasoning, in conjunction with the definition of "independent contractor" in subsection (c)

which limits its focus to prong C, neither includes the conjunctive ABC and “preponderance of factors” tests, nor fully addresses all aspects of the ABC test.

2. Subsection (c) includes new “client” and “independent contractor” definitions that have no other references in chapter 383, HRS. The rationale of restricting these terms to section 383-6, when their applicability should be integrated and compatible with established definitions of “employer” or “employing unit” is unclear.
3. Additionally, “independent contractor” is defined by circular reasoning, which undercuts the basic premise of the Hawaii Employment Security Law that a determination of independent contractor is conditioned on satisfying the three prongs of the ABC test, irrespective of whether the common law relationship of master and servant exists.

The stated intent of this measure is to provide greater clarity and detail for the determination of coverage under the law i.e. employee vs. independent contractor. However, as drafted, the measure would be more burdensome for businesses because they would have to apply the ABC test and find a preponderance of the twenty factors of the common-law test to determine independent contractor status.

The department recommends that the 20 factors in section 12-5-2, HAR, be codified in lieu of the statutory amendments proposed in this bill. Further, the department recommends deletion of 1) the presumption that an individual may be an independent contractor based on the preponderance of the twenty factors test and 2) the definitions of “client and “independent contractor” due to the concerns discussed above.



**Testimony to the Senate Committee on Judiciary and Labor
Tuesday, February 16, 2016 at 9:00 A.M.
Conference Room 016, State Capitol**

RE: SENATE BILL 2694 RELATING TO EMPLOYMENT SECURITY

Chair Keith-Agaran, Vice Chair Shimabukuro, and Members of the Committee:

The Chamber of Commerce Hawaii ("The Chamber") **supports the intent** of SB 2694, which clarifies Hawaii's employment security law for independent contractors and includes twenty factors to be used as guidelines when determining whether an individual could be an independent contractor. Also retains the ability of the department of labor and industrial relations to determine if an individual is an independent contractor and requires the director of labor and industrial relations to report to the legislature prior to the regular session of 2017 regarding guidelines developed by the unemployment insurance coverage committee.

The Chamber is Hawaii's leading statewide business advocacy organization, representing about 1,000 businesses. Approximately 80% of our members are small businesses with less than 20 employees. As the "Voice of Business" in Hawaii, the organization works on behalf of members and the entire business community to improve the state's economic climate and to foster positive action on issues of common concern.

The Chamber believes independent contractors are an important part of Hawaii's business community and economy. We have seen too much of a broad interpretation in the current law as to who qualifies as an independent contractor vs. an employee of a company. As more independent contracts are emerging in the ever-changing economic environment, clarification of who qualifies as an independent contractor would offer proper protection to legitimate independent contractors and the business that they contract with.

Thank you for the opportunity to testify.



HEARING BEFORE THE
SENATE COMMITTEE ON JUDICIARY & LABOR
February 16, 2016
State Capitol, Room 016
9 AM

TESTIMONY IN STRONG SUPPORT OF SB2694 RELATING TO EMPLOYMENT SECURITY

Aloha Chair Keith-Agaran, Vice Chair Shimabukuro, and Members of the Committee:

I am writing share our **strong support of SB2694** which clarifies Hawaii's employment security law for independent contractors; includes twenty factors to be used as guidelines when determining whether an individual could be an independent contractor, retains the ability of the department of labor and industrial relations to determine if an individual is an independent contractor; requires the Director of Labor and Industrial Relations to report to the legislature prior to the regular session of 2017 regarding guidelines developed by the unemployment insurance coverage committee; and requires an annual report to the legislature regarding covered employment determinations. This bill goes a long way toward protecting legitimate independent contractors and those that hire them from erroneous rulings by the Department of Labor and Industrial Relations (DLIR), where legitimate independent contractors have been determined to be employees.

Over the years we have seen numerous rulings where the DLIR has made determinations against employers, classifying people as employees for unemployment benefits through discretionary calls and misapplication of the 3-way test and the subsequent testing built into the rules. We have worked to address this issue with and on behalf of our members for years, but many businesses, particularly small businesses, do not have the time or money to take on the state, so they simply chose not to fight it and many poor rulings stand.

Two years ago one of our members, Envisions Entertainment, received a determination from the DLIR that a musician and sole proprietor they hired twice in 18 months to perform music for two events was considered by the DLIR to be employee, not an independent contractor, even though this individual had a full-time position elsewhere, said he was an independent contractor who occasionally provided services to Envisions Entertainment and others, had a registered business in our state, had a general excise tax license, and signed an independent contractor agreement. The DLIR determination was made before interviewing the company and doing any fact finding. Further, it is important to note that the DLIR's ruling against Envisions Entertainment did not provide any additional benefits to the musician and not garner the state any more in taxes. The determination merely shifted some of the unemployment benefits burden from the man's full-time employer to Envisions Entertainment. Therefore, the company made the decision to fight the ruling as they regularly need to hire independent contractors in their course of business and the ruling could devastate their company.

Many who read the department's determination, including several lawyers, called it "ridiculous" and we had to agree. So, we spoke with legislators two years about this and were encouraged to first work through the Administration and Department, which we and Envisions Entertainment did.

We met with and helped educate the Lt. Governor and department on the issue in the hopes of garnering an administrative fix to avoid a costly legal battle on both sides. However, the former DLIR Director stood by the department's incorrect ruling and said they do sometimes rule in favor of employers and that he would send us 20 redacted copies of rulings as proof. After several months, working through the Lt. Governor's office who worked with DLIR to obtain those copies, they could not send us even 1 ruling, which further illustrates the prevalence of this problem.

Envisions Entertainment had to and did take their case to court. It was an expensive battle (over \$70,000), but the company won! Not only did they win, but the judge's ruling showcased how inappropriate the department's behavior was and created a new precedent. And, while that is helpful, there is still too much leeway for "interpretation" in the law and DLIR has a history of broad and poor interpretations against employers. This is not just an Envisions Entertainment issue or a Maui issue, this is a state issue that affects individuals, businesses and industries who hire independent contractors to perform specific services.

Given the good intentions of the current law, we felt a better route was to simply clarify who qualifies as an independent contractor as more and more entrepreneurs are doing business as independent contractors in this changing economic environment. Two bills were introduced last legislative session HB1213 and SB1219. They sought to make it clear as to who qualifies as an independent contractor to remove ambiguity and incorrect determinations against independent contractors and companies that hire them. This clarification in no way affected employees. Instead, it recognizes that more and more people are operating as independent contractors in a new economy and clarifies in state statutes who is an independent contractor under the law.

Both bills went through the legislative process. HB1213 died earlier on, but SB1219 made it to conference committee. Through this process, many Senators and Representatives well understood the issue and had stories of their own of people who had been negatively impacted by erroneous rulings.

Further, the state may find that they have unfairly and unlawfully collected taxes on those Independent Contractor who were later deemed to be employees by DLIR as they paid GET as an Independent Contractor. When the state was asked if the GET paid was returned in those cases, there was no answer from the DLIR or the Tax Department.

So, today, in an effort to continue the dialog, be clear that this is not an employee issue, and obtain better protections for independent contractors and those that hire them, **we are here to encourage strong support SB2694** as this bill:

- Recognizes that more individuals are doing business as independent contractors and that they may still have other jobs outside of their business;
- Provides greater clarity in Hawaii's employment security law for those who choose to be independent contractors;
- Provides better guidelines for determinations; and
- Requires reporting and more transparency from the DLIR.

Mahalo nui loa for the opportunity to provide testimony. **We ask for your strong support of SB2694 to rectify this ongoing problem.**

Sincerely,



Pamela Tumpap
President



Randy Perreira
President

HAWAII STATE AFL-CIO

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The Twenty-Eighth Legislature, State of Hawaii
Hawaii State Senate
Committee on Judiciary and Labor

Testimony by
Hawaii State AFL-CIO
February 16, 2016

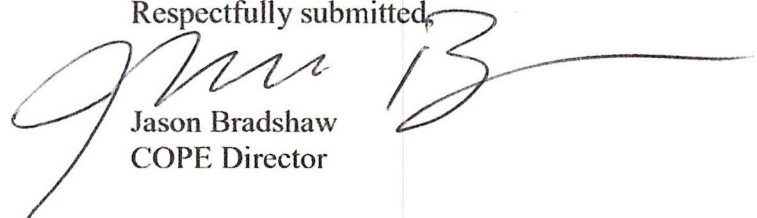
S.B. 2694 – RELATING TO
EMPLOYMENT SECURITY

The Hawaii State AFL-CIO opposes S.B. 2694 which clarifies Hawaii's employment security law for independent contractors and includes twenty factors to be used as guidelines when determining whether an individual could be an independent contractor and retains the ability of the Department of Labor and Industrial Relations to determine if an individual is an independent contractor.

The Hawaii State AFL-CIO is concerned changing the independent contractor law will be detrimental to a number of workers in the state of Hawaii. Independent contractors have several disadvantages such as not having the ability to collect unemployment insurance or claim workers' compensation. As a result, the Hawaii State AFL-CIO strongly urges the Committee on Judiciary and Labor to defer S.B. 2694 indefinitely.

Thank you for the opportunity to testify.

Respectfully submitted,



Jason Bradshaw
COPE Director



[COMMITTEE ON JUDICIARY AND LABOR](#)

Senator Gilbert S.C. Keith-Agaran, Chair

Senator Maile S.L. Shimabukuro, Vice Chair

Testimony in opposition to SB 2694

The Hawaii Bar Owners Association strongly opposes this bill.

How is clarity not clear?

When is a contractor a contractor? Simple question but never a simple answer here in Hawaii.

Here is a circumstance of how in Hawaii, a business entity (Maui Chamber of Commerce) could go to the legislature in 2015 and seek to pass a bill (SB1219) for simple clarity on when a person is an individual contractor as opposed to when they become an employee.

This should be clear upon the initiation of any work before any performance begins. Yet under the version SB2694 that now sits before the labor committee it has morphed into a pro-labor bill that only further clouds the matter and thus opens up the business to possible legal consequences over who is a contractor and who is an employee. It has confused the matter rather than clarify it. Who gains? The potential contractor loses the opportunity to perform and the business won't risk the potential for any possible liability to a labor department's possible determination for future unemployment compensation, social security, FICA, along with all other benefits owed, plus fines and defense fees after the fact of engagement.

The heading for this bill states:

“Clarifies Hawaii's employment security law for independent contractors”

In the current bill the labor department has these powers to make the contractual relationship unclear: (text of SB2694)

...Under Internal Revenue Service rules and common law, independent contractors control the manner and means by which contracted services, products, or results are achieved. The twenty factors set forth below **shall be guidelines** for determining whether an individual **could be deemed** an independent contractor. An individual **shall not have to meet all twenty factors** to qualify as an independent contractor. **The degree of importance of each factor may vary, depending on the occupation and the individual facts of each case as determined by the department. A preponderance** of the following twenty factors **may indicate** a worker is an independent contractor if the independent contractor:....

This empowers the labor department at their whim to determine a contractor is an employee after the fact.

Under these circumstances who could contract with anybody and know before engagement if they entered into a contractual relationship with an independent contractor or an employee? Is there any clarity here?

Would any of you enter into such a contract? Any wise businessman would not because there is No Clarity! This is not good for the business nor the contractor nor the business climate in our state!

Senators, We ask you to defer this action by opposing SB 2694.

Thank you,



Bill Comerford

Spokesman for the Hawaii Bar Owners Association

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