



ADMINISTRATIVE INITIATIVE

**STATE OF HAWAII
DEPARTMENT OF LABOR & INDUSTRIAL RELATIONS
“EMPLOYEE” VS. “INDEPENDENT CONTRACTOR” ANALYSIS**

**TITLE: GUIDELINES TO DETERMINE
WHETHER AN EMPLOYMENT
RELATIONSHIP EXISTS UNDER
VARIOUS STATUTORY CHAPTERS
ADMINISTERED BY THE DLIR**

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**DIVISION(S)/AGENCY(S): WAGE STANDARDS, DISABILITY
COMPENSATION, UNEMPLOYMENT
INSURANCE, HAWAII OCCUPATIONAL
SAFETY & HEALTH**

APPROVED BY:

NELSON B. BEFITEL

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A. Purpose

The purpose of this Administrative Initiative is to provide guidelines on the analytical framework used by the Department of Labor and Industrial Relations (DLIR) in determining whether a person’s legal status is an “Employee” or “Independent Contractor” under the following Chapters of the Hawaii Revised Statutes (“HRS”): Chapter 383 (Hawaii Employment Security Law); Chapter 386 (Workers’ Compensation Law); Chapter 387 (Wage and Hour Law); Chapter 392 (Temporary Disability Insurance); Chapter 393 (Prepaid Health Care Act); and Chapter 396 (Occupational Safety and Health).

B. Analytical Framework

In determining whether one is an “Employee” or “Independent Contractor”, one must comply with the following analysis:

- (a) Is employment presumed or does employment appear to exist based on an applicable statute or rule including, for example, definitions like those for “employee”, “employer”, and “employment”?
- (b) If so, is the type of service performed, nevertheless, excluded from the definition of “employment” under an applicable statute or rule?
- (c) If employment is presumed or appears to exist, which of the following tests must be used to determine whether the person is an employee under the applicable statutory Chapter: (1) Control, (2) Relative Nature of the Work, (3) Economic Reality, and/or (4) ABC?

The statutory Chapter in question and its interpretive Administrative Rules determine which test applies. For example, if the ABC Test applies, analysis outline under number 4 below should be followed.

The ABC Test applies to cases under Chapter 383 (Employment Security Law) based on HRS §383-6, and Chapter 393 (Prepaid Health Care Act) based on Hawaii Administrative Rule (“HAR”) §12-12-1. The Control and Relative Nature of the Work Tests apply to cases under HRS Chapter 386 (Workers’ Compensation Law) based on HRS §386-73.5, and Chapter 392 (Temporary Disability Insurance) based on HRS §392-21.5.¹

The Economic Reality Test is used as a guide in cases under Chapter 387 (Wage and Hour Law) based on the Wage Standards Division’s historical use of this Test.

HRS Chapter 396 (Occupational Safety and Health) does not require the use of a specific test, but has broad definitions of “employee”, “employer”, and “employment”, which should be used to assess whether employment exists or not. Whether a worker is an employee or independent contractor, however, is rarely, if ever, an issue under Chapter 396.

- (d) If the ABC Test applies, have all three conditions under the ABC Test been met? If all three conditions are not met, employment exists.

¹ HAR §12-11-1, an Administrative Rule relating to Chapter 392, uses the ABC Test to define “employment.” It, however, appears the ABC Test under HAR §12-11-1 no longer applies given the passage of HRS §392-21.5, which requires use of the Control and Relative Nature of the Work Tests.

- (e) For all other Tests (other than the ABC Test), including the Control, Relative Nature of the Work, and Economic Reality Tests, the existence and/or absence of relevant factors and a weighing of these factors, is required to assess whether employment exists.
- (f) The various Tests mentioned above are described below.

An analysis of a hypothetical case under the Economic Reality and ABC Tests has also been included in section B below for illustrative purposes. The analysis is aimed at showing the ABC Test may yield different results although the factors it assesses are quite similar to those assessed under other tests discussed. The analysis was designed to present a plausible, not conclusive, assessment of how different results might be reached under the two different Tests. In short, the point was to show the ABC Test, unlike the others, requires the existence of three specific conditions. If any condition is not met, employment is presumed.

1. The “Control” Test

The Control Test has been discussed by the Hawaii Appellate Courts in: (1) unemployment insurance (“UI”) cases under HRS Chapter 383; and (2) workers’ compensation (“WC”) cases under HRS Chapter 386. UI cases typically require a lower degree of control than that required in WC cases.

UI cases only require a showing of “general control” exercisable, directly or indirectly, over the physical activities and time surrendered by the worker. See Homes Consultant Co., Inc. v. Aagsalud, 2 Haw. App. 421, 426, 633 P.2d 564, 567 (Ct. App. 1981) (quoting Bailey’s Bakery v. Tax Comm’r, 38 Haw. 16, 50 (1948)). In other words, a showing of general control is enough to show a worker is an employee, not an independent contractor.

For example, in Homes Consultant, the Court held that a business that sold and installed steel and fiberglass siding exercised sufficient control over its salespersons for UI purposes where the business: (1) had final approval on acceptance or rejection of proposed sales contracts; (2) kept records on the whereabouts of its sale literature and sales kits although it did not keep records on its salespersons; and (3) although its salespersons had substantial leeway in setting contract prices, these were subject to review by a sales manager before the company approved the contract. Id., 2 Haw. App. at 426, 633 P.2d at 568. Based on this level of general control, the Court found the salespersons were employees, not independent contractors, under Hawaii’s UI law.

In contrast to the type of general control sufficient in UI cases, WC cases require a higher degree of control to show an employment relationship exists. Instead, an ability to control how the work is done must exist. In other words, there must be an ability to “dictate the means and methods by which the work is to be accomplished.” See Locations, Inc. v. Hawaii Dept. Of Labor and Indus. Relations, 79 Haw. 208, 211, 900 P.2d 784, 787 (Haw. 1995) (quoting Tomondong v. Ikezaki, 32 Haw. 373, 380 (1932)).

An employer’s ability to control how the work is done has been contrasted with the following description of an independent contractor:

One who contracts with another to do a specific piece of work for him, and who furnishes and has the absolute control of his assistants, and who executes the work entirely in accord with his own ideas, or with a plan previously given him by the person for whom the work is done, without being subject to the latter's orders in respect of the details of the work, with absolute control thereof, is not a servant of the employer, but is an independent contractor.

Tomondong, 32 Haw. at 378. In such instances, where a worker does not relinquish control over details of the work or how the work is done, the worker will likely be an independent contractor, not an employee.

2. *The “Relative Nature of the Work” Test*

The Relative Nature of the Work Test “involves a balancing of factors regarding the general relationships which the employee has with regard to the work performed for each of his [or her] employers.” Locations, 79 Haw. at 212, 900 P.2d at 788. Factors to consider are: “whether the work done is an integral part of the employer’s regular business; and whether the worker, in relation to the employer’s business, is in a business or profession of his own.” Id.

Other factors to consider include the following: “the character of the claimant’s work or business - how skilled it is, how much of a separate calling or enterprise it is, to what extent it may be expected to carry its own accident burden and so on – and its relation to the employer’s business, that is, how much it is a regular part of the employer’s regular work, whether it is continuous or intermittent, and whether the duration is sufficient to amount to the hiring of continuing services as distinguished from contracting for the completion of a particular job.” See 3 Larson, Larson’s Workers’ Compensation Law, §60.05[2] at 60-11 (2004).

The Relative Nature of the Work Test is required for cases under HRS Chapter 386 (Workers’ Compensation Law) and HRS Chapter 392 (Temporary Disability Insurance). See HRS §386-73.5 and HRS §392-21.5.

3. *The “Economic Reality” Test*

The economic reality test originates from cases involving the U.S. Fair Labor Standards Act and involves consideration of various factors. Based on decisions by the U.S. Supreme Court, the Department of Labor considers the following factors significant:

- (a) The extent to which services rendered are an integral part of the principal’s business;
- (b) The permanency of the relationship;
- (c) The amount of alleged contractor’s investment in facilities and equipment;
- (d) The nature and degree of control by the principal;
- (e) The alleged contractor’s opportunities for profit and loss;

- (f) The amount of initiative, judgment, or foresight in open market competition with others required for success of the alleged independent contractor; and
- (g) The degree of independent business organization and structure.

See, e.g., U.S. Dept. of Labor (“DOL”), Fact Sheet #13: Employment Relationship Under the Fair Labor Standards Act (FLSA), www.dol.gov/esa/regs/compliance/whd/whdcomp.htm.

Generally, these factors are used to distinguish employees from independent contractors. The presence of any one factor, however, is not dispositive. Instead, circumstances of the whole activity must be examined and weighed. See, e.g., Real v. Driscoll Strawberry Associates, Inc., 603 F.2d 748, 754-55 (9th Cir. 1979) (“Economic realities, not contractual labels, determine employment status”).

According to the U.S. Department of Labor, factors not material to the analysis include the following: where the work is performed²; the absence of a formal employment agreement; whether the alleged independent contractor has a State/local government license; and the time or mode of pay. See DOL Fact Sheet #13, www.dol.gov/esa/regs/compliance/whd/whdcomp.htm.

4. The “ABC” Test

The “ABC Test,” one defined and made applicable by Hawaii’s statutes and/or rules, requires an assessment of three conditions. The name of the test originates from three conditions, previously labeled “ABC”, instead of “1-3”, as they now are.

The ABC Test establishes a presumption of employment unless it is shown that the three conditions it lists exist. All three conditions are necessary to defeat the presumption.

The following language of HRS §383-6 sets forth the ABC Test:

Services performed by an individual for wages or under any contract of hire shall be deemed to be employment 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:

- (a) 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
- (b) The service is either outside the usual course of the business for which the service is performed or that the service is performed outside of all the places of business of the enterprise for which the service is performed; and
- (c) 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.

² Under the ABC Test, however, this factor is relevant to determine whether the second condition is met.

HRS §383-6.

Unless and until all three conditions are met, employment is presumed. Id.; see also Homes Consultant, 2 Haw. App. at 424, 633 P.2d at 567. Moreover, the type of control required by the first condition only refers to “general control”, not control over all details of the work performed. Id., 2 Haw. App. at 425-26, 633 P.2d at 568-69.

5. Definitional Provisions Under HRS Chapter 396 Occupational Safety and Health

Hawaii’s Occupational Safety and Health Law, HRS Chapter 396, does not require the use of any specific test to determine whether a person is an employee. Chapter 396, however, uses the following definitions of “employment”, “employee”, and “employer” which can be used to address the issue:

“Employee” means every natural person who is required or directed or permitted or suffered by any employer to engage in any employment, or to go to work or be at any time in any place of employment.

“Employer” means:

- (a) The State and every state agency;
- (b) Each county and all public and quasi-public corporations and public agencies therein;
- (c) Every person which has any natural person in service;
- (d) The legal representative of any deceased employer;
- (e) Every person having direction, management, control, or custody of any employment, place of employment, or any employee.

“Employment” includes the carrying on of any trade, business, occupation, or work, including all excavation, demolition, and construction work, or any process or operation in any way related thereto, in which a person is engaged to work for hire, except domestic service in or about a private home.

HRS § 396-1.

C. Hypothetical Case

Company XYZ manufactures surfboards, which must be shaped and sanded as part of the board-making process. XYZ has a shop it uses to make the boards. Worker sands surfboards for XYZ under a written contract, which requires XYZ to pay Worker \$20.00 per surfboard, plus an additional charge for longer boards. Worker negotiated these rates and terms with XYZ. Under their agreement, XYZ may reject boards completed by Workers if they are not sanded properly. XYZ, however, has never had a problem with Worker submitting sub-standard boards, and Worker has never had a board

rejected.

It generally takes Worker 45 minutes to an hour to finish a board. Worker decides how many boards he wants to complete in a day and is not required to finish any minimum number. XYZ does not require Worker to keep a regular schedule. Worker is free to decide the days and times he will work. Worker, however, generally works from Monday to Friday from 6:30 a.m. to 5:00 p.m.

XYZ always has a rack of boards needing shaping and sanding. Each board has a serial number, which Worker uses to track the boards he sands. After he completes a board, Worker places them on a separate rack in XYZ's shop reserved for finished boards. For payment, Worker prepares an invoice referencing the serial numbers of boards he has completed.

Worker does all of his board sanding work at XYZ's shop using his own tools and equipment. Other people - working under similar arrangements as Worker - also use XYZ's shop to shape and sand surfboards. XYZ allows Worker to use its shop at no cost and without restrictions.

Worker is also free to use XYZ's shop to make boards for other people. Such work involves requests for custom-made boards, which do not belong to XYZ. Worker sets the price for his custom-made boards, which he makes fairly regularly at XYZ's shop. Generally, however, Worker works on XYZ's boards.

Worker advertises his work on custom-made boards using business cards and flyers. The address listed on Worker's business cards and flyers is XYZ's shop.

1. Under the Economic Reality Test Worker May Be An Independent Contractor

As noted above, the Economic Reality Test does not depend on isolated factors. Instead, it examines the circumstances of the whole activity, not just one or two factors.

In the case discussed above, the circumstances of Worker's entire relationship with XYZ suggest Worker may be an independent contractor, not an employee.

XYZ generally lacks control over Worker, who may determine his own hours and days of work. XYZ does not set Worker's hours, monitor or supervise his work, or require him to complete a set number of boards. Worker chooses when he will work and how many boards he will finish.

XYZ does not monitor Worker but merely pays him for the number of boards he completes based on invoices Worker submits. Worker has and uses his own tools and equipment to finish the boards.

Although Worker exclusively works at XYZ's shop, he is free to work on boards belonging to XYZ or customers seeking his custom-made boards. Worker advertises his custom-made boards using business cards and flyers and regularly makes such boards for other people. Worker independently sets the price for his custom-made boards. Worker also negotiated his \$20.00 charge per board with XYZ.

Viewing these facts as a whole, particularly XYZ's lack of control over Worker who freely determines his own hours and the manner in which he performs his services, Worker may likely be an independent contractor under the Economic Reality Test.

2. Under the ABC Test Worker May Be An "Employee"

Unlike the Economic Reality Test - which examines working circumstances as whole, not just a single factor - the ABC Test requires the fulfillment of three specific conditions. If any condition is not met, employment is presumed. In other words, the ABC Test is stricter than the Economic Reality Test.

Based on the hypothetical case above, it appears Worker cannot meet all three conditions under the ABC Test. Very generally, the three conditions are as follows: (1) Worker must be free from XYZ's control and direction; (2) the service Worker provides must be outside XYZ's usual course of business or outside its usual place of business; and (3) Worker must customarily be engaged in an independently established trade, occupation, profession, or business, like the one he performs for XYZ. As discussed below, the second condition appears to be missing.

The first condition appears to be met because Worker is generally free from XYZ's direction and control. Worker sets his own hours, days of work, and number of boards he sands and finishes. XYZ does not monitor or supervise Worker, but simply pays him based on the number of boards he completes. Worker can work on custom-ordered boards or on boards belonging to XYZ. Worker has the freedom to choose which boards he will work on. Thus, XYZ does not have control over Worker.

The third condition also appears to be met because Worker customarily engages in an independent business of his own. Worker regularly receives orders for his custom boards, which he advertises using business cards and flyers. Worker decides how much to charge for his custom-made boards, which he is free to work on in lieu of XYZ's boards. Worker is not required to complete a set number of XYZ's boards and regularly works on orders for his custom-made boards. When Worker works on XYZ's boards, he receives \$20.00 per board based on a fee agreement he negotiated with XYZ. Given these facts, it appears Worker customarily engages in an independent business of his own.

Despite the above, it appears the second condition, which requires Worker to perform services outside XYZ's usual course of business or all of its places of business, cannot be met. XYZ is in the business of making surfboards. Workers' board sanding services are an integral part of XYZ's surfboard making business. Moreover, Worker does all his sanding services exclusively at XYZ's place of business. Worker does not have his own shop and conducts his board sanding services solely at XYZ's shop. In this regard, the second condition under the ABC Test cannot be met and Worker is, accordingly, presumed to be an employee, not an independent contractor.

This Administrative Initiative is intended for use as a guide for interpretation and application of relevant statutes, regulations, and policies. It does not replace applicable Hawaii Revised Statutes or Hawaii Administrative Rules. If you have any questions, or, need further clarification, please contact the appropriate division or agency.

