



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

830 PUNCHBOWL STREET, ROOM 321  
HONOLULU, HAWAII 96813  
[www.hawaii.gov/labor](http://www.hawaii.gov/labor)  
Phone: (808) 586-8842 / Fax: (808) 586-9099  
Email: [dlir.director@hawaii.gov](mailto:dlir.director@hawaii.gov)

January 23, 2008

To: The Honorable Alex Sonson, Chair  
and Members of the House Committee on Labor and Public Employment

Date: January 25, 2008

Time: 8:15 a.m.

Place: Conference Room 309, State Capitol

From: Darwin L.D. Ching, Director  
Department of Labor and Industrial Relations

**Testimony in SUPPORT  
of  
H.B. 1969 – Relating to Workers’ Compensation**

**I. OVERVIEW OF CURRENT PROPOSED LEGISLATION**

House Bill 1969 proposes to amend the definition of “employment” within Section 386-1, Hawaii Revised Statutes (“HRS”). This bill will allow small business owners to forgo the purchase of workers’ compensation coverage if they meet one of the three proposed exclusions:

1. Services performed by a member of a limited liability company, if the member is an individual with distributional interest as defined in section 428-501, HRS, of at least fifty percent in the company;
2. Services performed by a partner of a partnership, within the meaning of section 425-101, HRS;
3. Service performed by a partner of a limited liability partnership, if the partner is an individual and has a transferable interest, within the meaning of section 425-127, HRS, in the partnership of at least 50 percent; and
4. Services performed by a sole proprietorship.

H.B 1969 also ensures that no employee will be required to become a member or partner as a condition of employment.

## II. CURRENT LAW

Currently, members of a limited liability company, partners in a partnership and partners in a limited liability partnership who provide services to the company are considered employees and are required to obtain workers' compensation coverage for themselves.

However, section 386-1, HRS, specifies if an individual owns at least 50% of a corporation, they are excluded from workers' compensation coverage.

## III. HOUSE BILL

The Department of Labor and Industrial Relations ("Department") strongly supports H.B. 1969 for the following reasons:

1. Hawaii's current workers' compensation law currently provides similar exclusions for corporation stockholders.

Limited Liability Company ("LLC"), Partners of a Partnership, and Limited Liability Partnership ("LLP") are a new type of business organization, owners and/or partners of a small business – regardless of the type of business entity – should be allowed to be exempt from purchasing workers' compensation coverage for themselves.

2. Employers/business entities would still be required to obtain workers' compensation coverage for their employees.
3. It is uncommon for an employer to sue himself, or file for workers' compensation.
4. The intent of workers' compensation is to protect employees from medical costs and lost wages, it should not necessarily be mandated upon employers or partners who do not wish to be covered.
5. This bill will clarify existing practice that sole proprietors are excluded from obtaining workers' compensation insurance for themselves.
6. Hawaii small businesses organized as an LLC, Partner of a Partnership, and LLP will see immediate cost savings on workers' compensation insurance premium costs.

**Testimony to the House Labor & Public Employment  
Friday, January 25, 2008; 8:15 a.m.  
Conference Room 309**

**RE: HOUSE BILL NO. 1969 RELATING TO WORKERS' COMPENSATION**

Chair Sonson, Vice Chair Nakasone and Members of the Committee:

My name is Jim Tollefson and I am the President and CEO of The Chamber of Commerce of Hawaii ("The Chamber"). I am here to state The Chamber's strong support to House Bill No. 1969, relating to Workers' Compensation.

The Chamber is the largest business organization in Hawaii, representing over 1100 businesses. Approximately 80% of our members are small businesses with less than 20 employees. 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.

This measure excludes services for a limited liability company or limited liability partnership from the definition of "employment" if the person performing services has a fifty per cent or higher transferable interest in the limited liability company or limited liability partnership.

Workers' compensation provides medical insurance and wage loss for work related injuries for employees while protecting employers from civil liability resulting from such injuries. The Chamber believes that this measure is consistent with the intent of protecting employees while helping employers reduce overhead costs by enabling businesses to save on workers' compensation premiums.

The Chamber supports this measure for the following reasons: The Chamber finds that owners who do not work at the business would more than likely not suffer a work-related injury; therefore they do not benefit from workers' compensation. Additionally, owners would not gain any benefit from suing his or her own company for any injury, even for one that was suffered and was related to the business. Similarly, owners who work at the business would also have little incentive to file a workers' compensation claim. Essentially, owners would have nothing to gain from suing themselves because such action would result in increased premium costs, and potentially affect the viability of their business.

Accordingly, it makes sense for owners to opt out of the mandatory workers' compensation coverage. Mandatory coverage imposes additional costs on businesses, especially on sole proprietors; therefore, the proposed exclusion will alleviate some of the high costs of doing business. At least 41 states have some statutory provision that make workers' compensation coverage elective for sole proprietors and at least 31 states have some statutory provision that makes workers' compensation coverage elective for LLC members.

For these reasons, the Chamber urges your Committee to pass this measure.

Thank you very much for the opportunity to testify.



## **Before the House Labor Committee**

DATE: January 22, 2008  
TIME: 8:30 a.m.  
PLACE: Conference Room 309

### **Re: HB 1969 Relating to Workers' Compensation Testimony of Melissa Pavlicek for NFIB Hawaii**

Thank you for the opportunity to testify. On behalf of the thousands of business owners who make up the membership of the National Federation of Independent Businesses in Hawaii, we ask that you pass HB 1969. NFIB supports this measure in its current form.

The National Federation of Independent Business is the largest advocacy organization representing small and independent businesses in Washington, D.C., and all 50 state capitals. In Hawaii, NFIB represents more than 1,000 members. NFIB's purpose is to impact public policy at the state and federal level and be a key business resource for small and independent business in America. NFIB also provides timely information designed to help small businesses succeed.

We strongly support this measure and believe that it a major step toward supporting small business in Hawaii.

**Ronald I. Heller**  
700 Bishop Street, Suite 1500  
Honolulu, Hawaii 96813

phone 808 523 6000 fax 808 523 6001  
rheller@torkildson.com

**TESTIMONY BEFORE HOUSE COMMITTEE  
ON LABOR & PUBLIC EMPLOYMENT**

**Re: House Bill 1969**

**Tuesday, January 22, 2008 at 8:30 am  
State Capitol – Conference Room 309**

Chair Sonson, Vice-Chair Nakasone, and Members of the Committee:

My name is Ronald Heller. I am an attorney, and my clients include many small businesses in Hawaii. I support House Bill 1969.

The Workers' Compensation law in Hawaii allows owner-employees, in certain circumstances, to decide not to buy Workers' Compensation insurance coverage for themselves. The current law, however, is irrational and unfair.

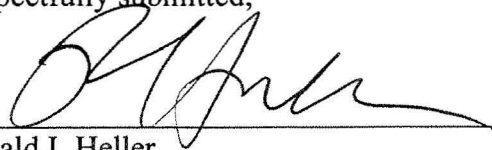
Under current law, the rules for Limited Liability Companies ("LLCs") are different from the rules for corporations. For corporations, current law provides that an owner-employee holding at least 50% of the stock is exempt from the requirement of Workers' Compensation coverage. (The owner-employee *may* choose to buy coverage on himself or herself, but it's not required.) If a business is organized as an LLC, however, then there is no exemption at all, regardless of the percentage owned. This is totally irrational – if a business is incorporated, a 50% owner is not required to have Workers' Comp coverage, but if that same business is an LLC, then even an 80% or 90% owner has to be covered.

There are also inconsistent rules for partnerships. The DLIR has taken the position that the requirement of Workers' Comp coverage does not apply to a partnership when the only workers are the partners themselves. However, the DLIR says that a Limited Liability

Partnership (“LLP”) must have Workers’ Compensation coverage even if there are no workers other than the partners. Since an LLP *is* a partnership under state law, it doesn’t make sense to treat it differently from any other partnership.

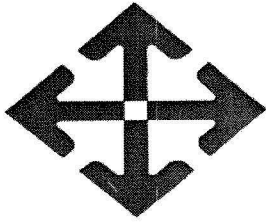
The obvious answer is to scrap all of the artificial distinctions based on whether a business is a corporation, a partnership, an LLC or an LLP. We should have a simple rule that sets an ownership threshold – I suggest 25% – and allows anyone with more than the specified percentage to opt out of Workers’ Comp coverage for themselves. In my view, the 50% threshold proposed in HB 1969 is unnecessarily high, but this bill, as proposed, is certainly a much-needed step in the right direction.

Respectfully submitted,



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Ronald I. Heller



# The Hawaii Business League

820 Mililani St., Ste. 810 Honolulu, Hawaii 96813-2938

Phone: (808) 533-6819 ♦ Facsimile: (808) 533-2739

January 22, 2008

Testimony To: House Committee on Labor and Public Employment  
Representative Alex M. Sonson, Chair

Presented By: Tim Lyons  
Executive Vice President

Subject: H.B. 1969 - RELATING TO WORKERS' COMPENSATION

Chair Sonson and Members of the Committee:

I am Tim Lyons, Executive Vice President of the Hawaii Business League, a small business service organization. We support this bill.

A few years ago the legislature provided for owner's of corporations who own 50% or more of their company to exempt out of worker's compensation. This was based on the fact that owners may have other income or they may be able to get some type of alternate disability insurance plan at a cheaper rate than they could for worker's compensation insurance coverage. Then, the concept of Limited Liability Corporation was born and there was some confusion as to whether these owners of 50% or more should be exempt since the LLC law refers to them as "members". Under corporate law the president of a corporation is considered an employee even though he may own 100% of the corporation. Based on fairness and in an effort for our

laws to stay up to date with current legal practices (the utilization of LLP's and LLC's) we support this bill.

Thank you for this opportunity to testify.



HOUSE OF REPRESENTATIVES  
THE TWENTY-FOURTH LEGISLATURE  
REGULAR SESSION OF 2008

COMMITTEE ON LABOR & PUBLIC EMPLOYMENT

Rep. Alex M. Sonson, Chair  
Rep. Bob Nakasone, Vice Chair

Date: Friday, January 25, 2008  
Time: 8:15 a.m.  
Place: Conference Room 309, State Capitol

TESTIMONY FRED GALDONES/ILWU LOCAL 142

RE: HB 1969, RELATING TO WORKERS' COMPENSATION

Thank you for the opportunity to present testimony regarding HB 1969. We oppose this myopic bill.

H.B. 1969 proposes to amend Hawaii's worker's compensation statute by removing four categories of individuals from the definition of "employment". These categories are: 1) services performed by a partner for a partnership; 2) services performed by a partner of a limited liability partnership who possesses a 50% transferable interest; 3) services performed by a member of a limited liability company if the individual has a distributional interest of 50% or more in the limited liability company; and 4) services performed by a sole proprietor for the sole proprietorship. In short, all four of these categories of individuals will be made exempt from workers' compensation coverage.

We believe this bill is short-sighted because by creating gaps in what was intended to be virtually universal coverage afforded by Chapter 386 HRS it will cause an even greater proliferation of exceptions from coverage making an already questionable market even less attractive to insurers. In recent decades, the legislature has already allowed innumerable exclusions from coverage, exempting domestics, real estate agents, corporate officers who are 25% stock holders; and 50% business owners from coverage. However, allowing further exclusions erodes the population of insured employees necessary to sustain reasonably affordable workers' compensation coverage, and in that fashion works to the detriment of other employers and all employees, while allowing a privileged few to opt out of this fundamental and necessary program of social insurance. If unchecked, granting more and more exceptions will reduce this population to the point where insurers will be compelled to increase premiums to maintain their operations and to provide coverage to an ever-diminishing number of employees.

Ultimately, H.B. 1969 is a symptom of the burgeoning economic inequality that afflicts this country and threatens to undermine the fundamental social safety net Hawaii has established for all of its workers. While it is common to hear criticism of the rising cost of workers' compensation insurance and to cast blame for such costs upon the injured worker, in reality, the exclusionary practices of those seeking to avoid their common obligation to protect

their fellow workers through a comprehensive scheme of insurance coverage are at fault in contributing to unnecessary costs. If business enterprises and the legislature are truly committed to cost control in workers' compensation premiums, they should join ILWU Local 142 in rejecting this spurious proposal and defeating H.B. 1969.

**Testimony of Thomas J. Smyth, CEcD**  
**Before the**  
**House Committee on Labor & Public Employment**  
**Friday, January 25, 2008**  
**8:15 am Room 309**  
**on**  
**HB1969 Relating to Worker's Compensation**

Chair Sonson, Vice Chair Nakasone, and Members of the Committee:

**I strongly support HB 1969 that excludes those with 50% interest in a Limited Liability Company or Limited Liability Partnership, individual partners and sole proprietors, from mandatory worker's compensation insurance coverage.**

I recently retired from the Department of Business, Economic Development & Tourism but my testimony today as an individual is based on over 20 years in direct support of small businesses, especially in the area of regulatory relief.

It took us two years to get legislation passed in 1993 to exclude 50% corporate owners. Eventually, support was obtained from all concerned when the provision that an employer would not require an employee to form a corporation to avoid insurance coverage was added. That same language is in each of the exclusion provisions in HB1969. Without being too facetious, may I note that if an employer really wanted to exclude an employee from coverage, the employer could require the employee to become a sole proprietor, certainly easier and less costly than other forms of a business. However, if those restrictions are necessary to ensure full support for this important bill, I certainly have no objection.

When LLC's were authorized in 1996, we did a quick survey with DCCA and DLIR to determine what changes were needed to the HRS to provide for this new and different form of business structure. Over several years, a variety of changes were made to ensure that those forming an LLC would not be penalized or otherwise left out of statutory requirements or benefits. It was initially felt that the corporate exclusions in Chapter 386 would apply to LLC's but a closer look led DLIR to conclude that a separate provision was needed since "ownership" and "stockholder" were terms not applicable to an LLC.

We drafted an administration bill just excluding LLC's several years ago after DBEDT and the Small Business Regulatory Review Board received many complaints from companies switching from corporate to LLC structure who were told that even 100% owners would need WC coverage. Those advocating for total employee coverage initially opposed the bill, but eventually even those objections were reconciled. However that bill, and others like it broadening the exclusion as in HB 1969, have not passed.

**This is a simple matter of fairness and equity.** Major owners should be able to voluntarily opt out of coverage and provide their own insurance. The “social compact” that for so long has tied immediate employer insurance for medical costs and lost wages to the restriction on suits against the employer for the cause of the injury, is not appropriate for major owners who certainly are not going to sue themselves.

**I urge you to pass this bill out. With this committee’s strong support this time it may make it through to enactment.**

Thank you for the opportunity to provide testimony.



**Hawaii Independent Insurance Agents Association**  
84 North King Street  
Honolulu, Hawaii 96817  
Phone (808) 531-3125 Fax (808) 531-9995  
Email: [hiia@hawaii.rr.com](mailto:hiia@hawaii.rr.com)

January 25, 2008

To: Representative Alex Sonson, Chair  
Committee on Labor and Public Employment

From: Hawaii Independent Insurance Agents Association

RE: HB 1969, Relating to Workers' Compensation Insurance – Employment Exclusion

The Hawaii Independent Insurance Agents Association (HIIA) would like to submit **supporting** comments regarding HB 1969, Relating to Workers' Compensation Insurance – Employment Exclusion. HIIA is a non profit trade association of independent insurance producers dedicated to assisting the insurance buying public with their insurance needs. We represent more than 700 licensed insurance professionals and staffs that provide services to a diverse client base comprised of various business, non-profit, and individual customers.

HIIA would like to voice our **support** of HB 1969. As you know, Section 386-1's definition of *employment* historically has allowed majority owners (at least 50%) of corporations and sole proprietors to be excluded from workers' compensation coverage. This same section did not specify how majority owners of limited liability companies and limited liability partnerships should be handled. This bill finally clarifies that majority owners of these forms of business organizations should also be excluded from workers' compensation coverage, just as their corporate counterparts have always been.

Because this exclusion has not been clearly stated in the past, the Department of Labor & Industrial Relations (DLIR) administratively took the conservative route and advised insurers that they must include these individuals for coverage and therefore charge premium for the coverage. Although this step was taken to address the different practices used by the various insurers, the DLIR took a stance that was contrary to the real intent of this section.

There will be no negative ramifications from the passage of HB 1969. The positive outcome of HB 1969 will include a comprehensive definition of *employment* and a clear list of exclusion that not only includes majority owners of corporations, but also includes majority owners of limited liability companies and limited liability partnerships. Lastly, these changes will also provide guidance to the DLIR, insurance companies and agencies, as well as the business consumer as it relates to who must be covered by workers' compensation insurance.

Thank you for the opportunity to testify.