



**TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
TWENTY-FIFTH LEGISLATURE, 2010**

ON THE FOLLOWING MEASURE:

S.B. NO. 2849, S.D. 2, RELATING TO THE HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND.

BEFORE THE:

HOUSE COMMITTEE ON FINANCE

LATE TESTIMONY

DATE: Monday, March 29, 2010 **TIME:** 5:00 p.m.

LOCATION: State Capitol, Room 308

TESTIFIER(S): Mark J. Bennett, Attorney General, or
Brian Aburano, Deputy Attorney General

Chair Oshiro and Members of the Committee:

The Department of the Attorney General opposes this bill in its current form.

The bill amends chapter 87A, Hawaii Revised Statutes (HRS), to: (1) allow the Hawaii Employer-Union Health Benefits Trust Fund (EUTF) to procure carriers, administrators, consultants, actuaries and auditors exempt from HRS chapter 103D; (2) imposes duties, restrictions, and liabilities on fiduciaries of the trust; (3) permits the EUTF to employ or retain a private attorney; (4) changes the number of trustees on the EUTF board, how they are appointed, their terms of office, and quorum and voting requirements; (5) provides for sub-boards to administer exclusive bargaining unit contributions and benefits; and (6) requires the EUTF to provide health and other benefit plans within certain contributions and appropriations.

FIDUCIARIES

The bill provides that a fiduciary of the trust shall comply, with respect to a plan, with all fiduciary duties imposed on fiduciaries under title 29 U.S.C. sections 1101-1191c, as amended, and related regulations. See page 1, lines 9-13. Title 29 U.S.C. sections 1101-1191c are part of the

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federal statutes commonly known as the Employee Retirement and Income Security Act (ERISA). As a governmental plan, the EUTF is exempt from the requirements of ERISA pertaining to fiduciaries. See 29 U.S.C. §§ 1002(32) (definition of "governmental plan") and 1003(b)(1) (ERISA provisions not applicable to governmental plans).

First, the bill does not define who is a "fiduciary" of the trust. The lack of a definition may create litigation issues in the future. Also, the EUTF statutes use the term "fund" not "trust" but it is unclear that fiduciaries should be limited to those who are fiduciaries of the fund. Other parts of this bill create trustees who might not be fiduciaries of the EUTF fund but would appear to be fiduciaries of the EUTF plan, i.e., sub-boards of trustees. See page 11, lines 10-19. To define the fiduciaries who are to comply with section 1 of the bill, the following sentence should be added to section 87A-B(a) at page 1, line 13:

For purposes of this section, a fiduciary shall mean the trustees appointed under section 87A-5(a) and the trustees of any sub-board appointed under section 87A-5(b).

Second, while the bill provides that a fiduciary of the trust shall comply with all fiduciary duties imposed under ERISA, it goes on to state some but not all fiduciary provisions of ERISA. See page 1, line 14, to page 4, line 14. This might create an ambiguity as to whether ERISA provisions not stated in the bill apply or do not apply. For example, page 3, line 14, to page 4, line 2, track the prohibited transactions language of 29 U.S.C. section 1106, but the bill does not include the language in 29 U.S.C. section 1108 that provides exemptions for what would otherwise be prohibited transactions. To clarify

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this matter, the current language from page 1, line 9, to page 4, line 14, of the bill should be replaced with the following:

§87A-B Fiduciary duties; prohibited transactions. A fiduciary shall comply, with respect to the fund, with all fiduciary duties imposed on fiduciaries under Title 29 United States Code Sections 1101-1191c, as amended, and related regulations. For purposes of this section, a fiduciary shall mean the trustees appointed under section 87A-5(a) and the trustees of any sub-board appointed under section 87A-5(b).

Third, the bill makes fiduciaries personally liable for breaches of fiduciary duty, including making good to the "plan" any losses to the plan from each breach. See page 4, line 15, to page 5, line 2. The EUTF statutes do not have a definition for "plan" so this may create an ambiguity. More importantly, under current law, the EUTF trustees have a general exemption from personal liability under HRS section 26-35.5(b). See Awakuni v. Awana, 115 Haw. 126, 136-140 (2007). If the bill means to do away with this exemption, it may become difficult to get persons to serve as trustees of the EUTF and/or the premium costs for insuring EUTF trustees may rise to account for the greater potential risk. See HRS § 87A-25(4) (EUTF board required to procure fiduciary liability insurance).

Related to the foregoing, the bill does not make it clear that the personal liability of EUTF trustees is limited as the personal liability of ERISA fiduciaries is limited. For example, liability for breach of fiduciary duty under ERISA allows recovery of monetary damages only for the plan itself, not for individuals. See Cline v. Industrial Maintenance Eng. & Contracting, 200 F.3d 1223, 1229 (9th Cir. 2000), citing Cinelli v. Security Pacific Corp., 61 F.3d 1437, 1445 (9th Cir. 1995).

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Similarly, under ERISA, there can be no breach of fiduciary duty liability regarding the design, amendment or termination of health benefits and other welfare benefits plans. See Curtiss-Wright Corp. v. Schoonejongen, 514 U.S. 73, 78 (1995) citing Adams v. Avondale Industries, Inc., 905 F.2d 943, 947 (6th Cir. 1990); Lockheed Corp. v. Spink, 517 U.S. 882, 889-91 (1996). To remedy the concerns raised in this and the preceding paragraph, the current language from page 4, line 15, to page 5, line 21, of the bill should be replaced with the following:

§87A-C Liability for breach of fiduciary duty. (a)

Any person who is a fiduciary of the fund and who breaches any of the responsibilities, obligations, or duties imposed on fiduciaries under section 87A-B shall be personally liable to reimburse any losses to the fund resulting from each breach and to restore to the fund any profits of the fiduciary that have been made through the use of assets of the fund by the fiduciary, and may be subject to any other equitable and remedial relief as the court may deem appropriate, including removal of the fiduciary; provided that the liability created by this section is only to the fund and not to individual participants or beneficiaries of the fund and does not apply to the design, amendment, or termination of health or other benefit plans established by the board.

(b) No attorneys' fees or costs incurred in bringing a claim arising under this section, including under a private attorney general doctrine, may be recovered from the fund, the State, or any county.

(c) Any provision in any agreement or instrument that purports to relieve a fiduciary of responsibility or liability for any responsibility, obligation, or duty under

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section 87A-B shall be void as against public policy.

However, nothing in this section shall preclude:

- (1) A fiduciary from claiming immunity under section 26-35.5(b);
- (2) The fund from purchasing insurance for its fiduciaries or for itself to cover liability or losses occurring by reason of the act or omission of a fiduciary in the case of a breach of a fiduciary obligation by the fiduciary, if the insurance permits recourse by the insurer against the fiduciary in the case of a breach of fiduciary obligation by the fiduciary; or
- (3) A fiduciary from purchasing insurance to cover the fiduciary's own liability for breach of a fiduciary duty.

Fourth, the bill provides that any provision in any agreement or instrument that purports to relieve a fiduciary of responsibility or liability for any duty shall be void as against public policy. See page 5, lines 3-6. Again, it is unclear as to whether this means to do away with the current exemption from liability for EUTF trustees under section 26-35.5(b). This can be addressed by amending the bill as stated above.

Finally, if the bill means to do away with the exemption from liability for EUTF trustees under section 26-35.5(b) and to have the EUTF board represented and advised by private attorneys rather than the Attorney General, the bill must be amended to make it clear that the State and counties shall have no liability whatsoever for any breach of fiduciary duty by the EUTF board or any EUTF trustee and shall have no obligation to defend or indemnify the EUTF board or any EUTF trustee. This is

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necessary to avoid the State and counties incurring major liability due to the bill waiving EUTF trustee immunity and delegating legal oversight of the EUTF board to private counsel. Further, the bill must be amended to limit the liability for breach of fiduciary duty to the amount of the EUTF board's insurance coverage available for such liability. This could be accomplished by adding the following language to the end of the proposed section 87A-C:

(d) If the fund purchases insurance for its fiduciaries or itself, the fund's and the fiduciaries' liability for any and all money damages, losses, costs, and expenses caused by any and all fiduciary breaches of the responsibilities, obligations, or duties imposed under section 87A-B shall be strictly limited to the extent of such insurance.

(e) In no event shall the State or any county be liable for any money damages, losses, costs or expenses caused by a fiduciary's breach of any of the responsibilities, obligations, or duties imposed on fiduciaries under section 87A-B. Neither the State nor any county shall be obligated to defend or indemnify any fiduciary against a claim arising under this section.

PRIVATE ATTORNEY

The bill permits the EUTF to employ or retain a private attorney who is independent of the Attorney General without going through the Attorney General. The private counsel would be permitted to represent the EUTF, an agency of the State, in any litigation, render legal counsel and advice, and draft documents. See page 6, line 1, to page 8, line 15, and page 14, lines 5-14.

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First, under existing law, the EUTF may and has used private counsel with the approval of the Attorney General and Governor. See HRS §§ 28-8 and 28-8.3. Such counsel may be approved where there is a direct conflict or additional expertise is needed.

Second, the EUTF is a state agency and part of the Executive Branch. It is critical that the legal advice given to the EUTF be consistent with the advice given to other state agencies and with the interests of the Executive Branch. Otherwise, the EUTF could be given inconsistent advice that is unnecessarily damaging to the EUTF, the State, or the Executive Branch, or much time and effort will be unnecessarily spent resolving avoidable differences between the EUTF and the Governor or other state agencies. It is only through the Department that consistent advice can be given to the EUTF.

Third, the Department provides a broad range of experience and expertise to the EUTF that would not be available through a small group of contract hires, in-house lawyers or counsel with ERISA "employee benefits experience." See page 14, lines 11-14. While the Attorney General can hire private counsel for the EUTF to advise it on specific employee benefits matters (as noted above, the EUTF is exempt from ERISA), no such counsel is likely to have expertise on the variety of unique government laws that are applicable to the EUTF, i.e., open records laws, open meetings act, privacy and confidentiality laws, budget laws, legislative process, etc.

Fourth, state agencies have generally only been allowed to procure their own counsel independent of the Attorney General where there is a conflict or a need for specialized expertise not available in the Department. See Standing Committee Report No. 1044-96, 1995 House Journal, p. 1441 (Ombudsman should be

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allowed to hire counsel in those matters where the Attorney General would be in conflict by representing the agency affected); Standing Committee Report No. 2825, 2000 Senate Journal, p. 1169 (Kahoolawe Island Reserve Commission allowed to utilize attorneys with specialized, highly technical, legal expertise beyond what the Attorney General may be able to provide to ensure that cleanup proceeds on schedule). Conflicts rarely arise in the Department's representation of the EUTF and where they arise the Attorney General can authorize the EUTF to procure independent counsel. Since the EUTF is exempt from ERISA, there is no need for the EUTF to employ private counsel with expertise in ERISA law. It should be noted that the EUTF has always been advised by a benefits consulting firm that has broad experience and expertise in employee benefits matters, and that the EUTF's request for proposals have indicated that any such firm should have in-house or outside legal counsel with expertise in employee benefits.

BOARD OF TRUSTEES; SUB-BOARDS

The bill replaces the ten trustees on the EUTF board with twelve trustees: (a) six trustees representing employee-beneficiaries, each being nominated by a specific bargaining unit or units; (b) five trustees representing public employers, one being appointed by the Governor to represent the State administration, one nominated by the UH Board of Regents, one nominated by the Board of Education, two nominated by the mayors of four counties; and (c) one trustee appointed by the Governor to represent retirees. See page 8, line 16, to page 11, line 9. All appointees serve at the pleasure of the appointing authorities. See page 11, lines 8-9, and page 13, lines 18-19. Four trustees representing employee-beneficiaries and four trustees representing public employers must be present to

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constitute a quorum, and a vote of four trustees on each side is necessary to carry any measure. See page 14, line 15, to page 15, line 20.

First, while there is no Hawaii case law on the subject and case law from other jurisdictions is not uniform, there is an issue as to whether the power to appoint public officers can be constitutionally delegated to private organizations (in this case, to the exclusive bargaining representatives for bargaining units). Courts in several states have held that the power to appoint a public officer is a sovereign power of government granted by the people to elected officers and that delegating that power to a private organization accountable to no one but their own membership is unconstitutional. James v. Schorr, 65 A.2d 810 (Del. 1948); Rudman v. Rini, 356 N.E.2d 4 (Ill. 1976); Gamel v. Veterans Memorial Auditorium Commission, 272 N.W.2d 472 (Iowa 1978); Sediak v. Dick, 887 P.2d 1119 (Kan. 1995); Opinion of the Justices, 150 N.E.2d 693 (Mass. 1958); and Hetherington v. McHale, 329 A.2d 250 (Pa. 1974); cf. Jones v. Chiles, 638 So. 2d 48 (Fla. 1994) (statute violated separation of powers by depriving governor of power to appoint executive officer). While this bill provides for the Governor to appoint each trustee nominated by the bargaining unit or units, since the Governor is given only one nominee to choose from, the procedure really amounts to a delegation of the power of appointment to the bargaining unit or units.

Second, one of the employee-beneficiary trustees is to be appointed by the exclusive bargaining representative for bargaining unit 5. See page 9, lines 21-22. All bargaining unit 5 members are now in VEBA health benefits plans under chapter 87D and do not participate in the EUTF. Unless bargaining unit 5 members are to be transferred back to the

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EUTF, it would not make sense to permit bargaining unit 5 to appoint a trustee to administer the EUTF. For similar reasons, it may be questioned why the bill provides for the Board of Education to nominate one of the employer trustees.

Third, by providing for more employee-beneficiary trustees than public employer trustees, the bill strays from the equal representation on the EUTF board that was originally mandated by Act 88, Session Laws of Hawaii 2001. See Stand. Comm. Rep. No. 880, 2001 Senate Journal, page 1275, and Stand. Comm. Rep. No. 1097, 2001 House Journal, page 1548. In this respect, Act 88 was apparently based on provisions of the Labor-Management Relations Act (LMRA), specifically 29 U.S.C. section 186(c), which permits an employer (or employers) to make payments to a trust fund established for the sole and exclusive benefit of the employees of such employer (or employers) if such payments are held in trust and the employees and employer(s) are "equally represented in the administration of such fund."

Fourth, by increasing the quorum to four trustees on each side, the bill makes it more likely that the EUTF board will not be able to meet and take actions necessary for the efficient and continued operation of the EUTF health and other benefits plans. In the past, the EUTF has had problems getting a quorum of three trustees on each side to meet.

Fifth, the bill does nothing to solve a recurrent problem of the EUTF board, which is the lack of an effective tie-breaking mechanism. As with the current law, the bill provides that both employee-beneficiary trustees and public employer trustees must agree on any matter that must be voted upon. While the LRMA is not directly applicable to the EUTF, it should be noted that under the LMRA where there is equal employee and employer representation on a trust fund board and no neutral

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person(s) empowered to break a deadlock, there is to be an agreement that provides for an impartial umpire to decide the dispute. See 29 U.S.C. § 186. The current EUTF statutes and rules do not provide for neutral persons or an impartial umpire to resolve board deadlocks.

Sixth, the provision for the appointment of sub-boards to design benefits and administer particular bargaining unit contributions and benefits appears to resurrect the union health plans that were done away with under Act 88. Having a single health benefits system, rather than multiple union plans, was seen as a cost-saving feature of Act 88. See Conf. Comm. Rep. No. 124, 2001 House Journal, pages 1097-1098; and Actuarial Audit and Operational Audit of the Public Employees Health Fund, Auditor's Report No. 99-21 (May 1999). In addition, the statute does not make it clear how or what employer(s) will appoint trustees to a sub-board, how such sub-boards will operate, whether the sub-boards would have control of their own funds, where such funds would be deposited and held, whether fiduciary duties will apply to trustees of sub-boards, and what responsibility the EUTF board would have for such sub-boards, if any.

HEALTH AND OTHER BENEFITS PLANS

The bill provides that the EUTF board is to provide health and other benefits plans: (a) for collective bargaining units, based on collectively bargained contributions; (b) for retirees, within the appropriation adopted by the State and counties; and (c) for all others, based on the contributions from both the employers and employees. See page 16, lines 1-12.

With respect to (a), this would require the collective bargaining parties to agree to employer and employee contributions well before the EUTF board must design the health

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and other benefits plans, procure carriers to provide or third-party administrators to administer the plans, and conduct an open-enrollment and informational campaign so that employees can select their plans. Historically, the collective bargaining parties have not agreed on contributions before the EUTF must design and procure its plans; they have only negotiated contributions after the EUTF plans have been designed and procured. If this bill were to pass and the collective bargaining parties continue their past practice, the EUTF board will be left in a difficult position and EUTF employee-participants may suffer as a result.

With respect to (b), this will require the State Legislature and counties to appropriate moneys well in advance of the EUTF design and procurement of retiree health and other benefits plans. Historically, such appropriations have followed, not been in advance of, EUTF design and procurement of retiree plans. Again, if this bill were to pass and the State Legislature and counties do not make appropriations in a timely manner, the EUTF board will be left in a difficult position and EUTF retiree-participants may suffer as a result.

We suggest that a section be added before section 10 of the bill to provide for the designation of the new sections added to chapter 87A, Hawaii Revised Statutes, to state, "In codifying the new sections added to chapter 87A, Hawaii Revised Statutes, by section 1 of this Act, the revisor of statutes shall substitute appropriate section numbers for the letters used in the designations of, and references to, those new sections in this Act."