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TO THE  
HOUSE COMMITTEE ON  
CONSUMER PROTECTION AND COMMERCE  
THE TWENTY-EIGHTH STATE LEGISLATURE  
REGULAR SESSION OF 2015

Wednesday, February 11, 2015  
2:30 p.m.

TESTIMONY ON H.B. NO. 1097

RELATING TO THE SECURE AND FAIR ENFORCEMENT  
FOR MORTGAGE LICENSING ACT

THE HONORABLE ANGUS L.K. MCKELVEY, CHAIR,  
AND MEMBERS OF THE COMMITTEE:

My name is Iris Ikeda, Commissioner of Financial Institutions ("Commissioner"),  
testifying on behalf of the Department of and Consumer Affairs ("Department") on  
House Bill No. 1097. The Department offers the following comments.

House Bill No. 1097 (1) amends the description of "sole proprietorship" in the  
Secure and Fair Enforcement for Mortgage Licensing Act (Chapter 454F, HRS).

Section 454-1, HRS, defines "sole proprietorship":

"Sole proprietorship" means a mortgage loan originator business that is solely  
and personally owned and operated by an individual mortgage loan originator,

and where there is no legal distinction between the individual business owner and the business.

This definition makes it clear that the “sole proprietorship” category of mortgage loan originator (“MLO”) fees in section 454F-22(b), HRS, applies only to an MLO business that is solely and personally owned and operated by an individual mortgage loan originator, and where there is no legal distinction between the individual business owner and the business. The definition was added to Section 454F-1, HRS, by the 2014 legislature to clarify the collection of fees as DFI was able to obtain a license type called “sole proprietor” in NMLS for Hawaii.

A sole proprietor is distinguished from a one-person LLC through the assets and liabilities of the entity. A sole proprietor is a single person who receives all the income and is responsible for all the liabilities. A one-person LLC is a corporate entity where the corporation receives all the income and is responsible for all the liability; the individual is shielded from all income and can invest the income back into the business. The bill proposal would amend the definition by removing the phrase, “where there is no legal distinction between the individual business owner and the business”. However, that phrase was a purposeful part of the sole proprietorship definition to make it clear that a single owner/operator legal entity such as a corporation or LLC, is not eligible for the “sole proprietorship” category of MLO fees. Removing language from the definition as the bill proposes would cause confusion.

“Sole proprietorship” licensing application and renewals are simpler and less time consuming for DFI staff to review and process than non-sole proprietorship MLO applications and renewals. This is in part because non-sole proprietorship MLO

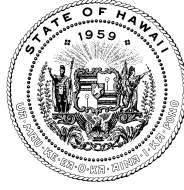
applications involve a review of the records required of the legal entity to maintain its legal entity status, such as an LLC or corporation. Consequently, a different fee schedule was established for sole proprietorships and non-sole proprietorships.

The current definition of “sole proprietorship” is consistent with definitions used by government agencies such as the IRS and the SBA. The IRS.gov website explains: “A sole proprietor is someone who owns an unincorporated business by himself or herself. However, if you are the sole member of a domestic limited liability company (LLC), you are not a sole proprietor if you elect to treat the LLC as a corporation.” Similarly, SBA.gov provides this definition: “A sole proprietorship is the simplest and most common structure chosen to start a business. It is an unincorporated business owned and run by one individual with no distinction between the business and you, the owner. You are entitled to all profits and are responsible for all your business’s debts, losses and liabilities.”

DFI respectfully submits that amending the definition of “sole proprietorship” as this bill proposes, will cause unnecessary ambiguity and confusion in the interpretation of Chapter 454F, HRS. DFI submits concerns about the bill proposal’s amendment to the definition of “sole proprietorship”.

DFI has concerns about this bill, House Bill No. 1097, and the unintended consequences that may ensue.

Thank you for the opportunity to testify. I would be pleased to respond to any questions you may have.



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TO THE SENATE COMMITTEE ON CONSUMER PROTECTION & COMMERCE  
THE TWENTY-EIGHTH LEGISLATURE  
REGULAR SESSION OF 2015

Date: Wednesday, February 11, 2015  
Time: 2:30 p.m.  
Conference Room: 325

**TESTIMONY ON HOUSE BILL NO. 1097**  
**RELATING TO THE SECURE AND FAIR ENFORCEMENT FOR MORTGAGE**  
**LICENSING ACT**

TO THE HONORABLE ANGUS L.K. MCKELVEY, CHAIR, AND MEMBERS OF THE COMMITTEE:

Thank you for the opportunity to testify. My name is Tung Chan, Commissioner of Securities and head of the Business Registration Division of the Department of Commerce and Consumer Affairs. We offer technical comments relating to business registration law and take no position beyond our area of expertise.

We strongly do not recommend the proposed amendment to the definition of "Sole proprietorship" that deletes the phrase "there is no legal distinction between the individual business owner and the business". "Sole proprietorship" is a very well-established legal term of art and its primary key feature is that "there is no legal distinction between the individual business owner and the business," as compared to other entities like for example, an LLC which is expressly defined as "a legal entity distinct from its members." HRS §428-201.

To modify the key feature of a sole proprietorship, especially when it creates ambiguity between it and other well-established business entities like LLCs, seems ill-advised since it may undermine the settled legal, business and tax distinctions that have accrued to sole proprietorships in the law and through the courts. In fact, the Hawaii Intermediate Court of Appeals noted the importance of this particular feature of sole proprietorships in Credit Associates of Maui, Ltd. v. Carlbom, 98 Haw. 462, 465-66, 50 P.3d 431, 434-35 (Ct. App. 2002) where it wrote, “a sole proprietorship has no legal identity apart from its owner.” The court then took efforts to re-emphasize this critical point. To delete this fundamental feature of a sole proprietorship creates a high probability of unintended consequences in any future court interpretations.

For these reasons, we do not recommend the proposed change to this fundamental understanding of a sole proprietorship and we recommend great caution. If the bill’s main goal is not to alter this very well-established term of art, we respectfully ask the Committee to explore an alternate drafting solution and we offer our services to assist. Thank you for the opportunity to testify. I would be happy to answer any questions the Committee may have.

**LATE**



February 11, 2015

TO: COMMITTEE ON COMMERCE PROTECTION & COMMERCE  
Angus L. K. McKelvey, Chair  
Justin H. Woodson, Vice Chair

FR: Cathy Lee, President  
Hawaii Association of Mortgage Brokers

RE: H.B. 1097 Relating to the Secure and Fair Enforcement for Mortgage Licensing Act.  
**Position: Support, but open to deferral**

Dear Chair Angus McKelvey, Vice Chair Justin Woodson and Members,

The Hawaii Association of Mortgage Brokers (HAMB) supports House Bill 1097.

HAMB believes that definition of "sole proprietorship" under chapter 454F, Hawaii Revised Statutes, does not adequately reflect the structure of some businesses regulated by this chapter. Some licensees under chapter 454F, Hawaii Revised Statutes, may in fact operate in other allowed business organizations, such as a limited liability company, but only have one licensed individual working for that organization.

However, we have been in discussions with the Department of Commerce and Consumer Affairs, Division of Financial Institutions (DFI) and understand its concerns. HAMB hopes to continue further discussions in the interim on this issue. As such, we are amenable should the Committee decide to defer this measure. We appreciate the introducer for putting this measure forward and we thank you for the opportunity to testify.