

A Bill for an Act Relating to Prepaid Legal Services.

Be It Enacted by the Legislature of the State of Hawaii:

SECTION 1. The Hawaii Revised Statutes is amended by adding a new chapter to be appropriately designated and to read as follows:

“CHAPTER PREPAID LEGAL SERVICES

Sec. -1 Definitions. As used in this chapter:

- (1) “Department” means the department of regulatory agencies.
- (2) “Plan administrator” means those persons who have discretionary authority for the management of the plan or for the collection, management, or disbursement of plan moneys.
- (3) “Prepaid legal service plan” (“Plan”) means a group legal service plan in which the cost of the services are prepaid by the group member or by some other person or organization in the member’s behalf. A group legal service plan is a plan by which legal services are rendered to individual members of a group identifiable in terms of some common interest. A plan shall provide:
 - (A) That individual members shall be afforded freedom of choice in the selection of their own attorney or attorneys to provide legal services under such plan.
 - (B) For the payment of equal amounts for the cost of services rendered without regard to the identity of the attorney or attorneys selected by the plan member or members. No plan shall otherwise discriminate on the basis of such selection.

Sec. -2 Applicability; other statutes, rules of court.

- (a) This chapter shall apply to all plans in the State other than:
 - (1) Plans in which either the group or the plan administrator is otherwise subject to regulation under chapter 431 or 433.
 - (2) Plans in which any party to the plan is the federal government or any agency thereof.
 - (3) Any employer-employee plan which is subject to the federal Employee Retirement Income Security Act of 1974, Public Law 93-406.
- (b) The operation of all plans subject to this chapter shall also be subject to chapters 480, 481, part I, 481A, and 481B, and other provisions of law which may be applicable. Chapters 431, 433, and 434 shall not apply to any plans or the operations thereof which are subject to this chapter, except as provided in sections -5 and -6.
- (c) No plan subject to this chapter shall contravene Rules of Court adopted by the Hawaii supreme court.

Sec. -3 Filing and other requirements. Sixty days prior to the implementation of any plan and the accumulation or payment of money thereunder, all

plan documents shall be submitted in writing to the department. Such documentation shall contain in writing the following:

- (1) A brief statement of the plan's financial structure, including a statement of the amount of prepayment, and other charges or dues to be paid by plan members and the manner in which such amount is to be paid.
- (2) A statement of the amount of benefits, legal services, or reimbursement for legal services to be furnished each member of a plan, and the period during which it will be furnished; and, if there are exceptions, reductions, exclusions, limitations, or restrictions of such benefits, legal services, or reimbursements, a detailed statement of such exceptions, reductions, exclusions, limitations, or restrictions.
- (3) A statement of the terms and conditions upon which the plan may be canceled or otherwise terminated by the group, the plan administrator, the persons furnishing legal services, or the member; provided that for any such cancellation or termination, other than by a member, there shall be provision made for the disposition of funds accumulated under the plan.
- (4) A statement describing the applicability or nonapplicability of the benefits of the plan to the family dependents of the member.
- (5) A statement of the period of grace which will be allowed the member or his group for making any payment due under the plan.
- (6) A statement describing a procedure for settling disputes between or among the group, the plan administrator, the persons furnishing legal services, and the member.
- (7) A statement that the plan includes the endorsements thereon and attached papers, if any, and contains the entire contract or contracts to be used between all parties to a plan.

Any amendments or changes to the documents filed under paragraphs (1) to (7) shall be filed with the department sixty days before they take effect. All documents filed under this section shall be public documents.

Sec. -4 Accumulated funds, protection, violation. Any plan which accumulates funds prior to the payment of such funds to the persons providing legal services shall meet the requirements of this section.

The plan administrator shall obtain a bond in an amount and form approved by the department which shall be executed by the plan administrator and a surety company authorized to do business in the State as a surety. The bond shall be to the benefit of the members of the plan and shall be filed with the department. In lieu of the bond required by this section, the department shall accept letters of credit, certificates of deposits, or other evidences of security in form and amounts deemed appropriate by the department.

In administering this chapter and this section in particular, it is the intention of the legislature to encourage the formation and operation of prepaid legal service plans. Therefore, all efforts shall be made by the department in determining the amount or type of security required to meet such legislative intent to encourage the formation of prepaid legal service plans.

Sec. -5 Annual exhibits; examination by director. Each plan shall file with the director of regulatory agencies within thirty days after the end of its fiscal year a statement under oath in such form as the director prescribes containing:

- (1) A statement setting forth the total amount of gross receipts and expenditures of the plan during its fiscal year;
- (2) The assets and liabilities of the plan at the close of its fiscal year; and
- (3) The profit and loss of the plan during its fiscal year.

The powers, authorities, and duties relating to examinations vested in and imposed upon the insurance commissioner under chapter 431 are extended to and imposed upon the director in respect to examinations of the plans; provided that no examination shall attempt to obtain or inspect written or oral information or documents in violation of the attorney-client privilege as it is contained in the Code of Professional Responsibility adopted by the supreme court.

Sec. -6 Investments of certain plans. No plan promising or offering to pay for legal services in an amount equal to or in excess of \$25 a year shall invest any of its assets other than as authorized and provided for in respect to domestic insurance companies and societies under chapter 431, which provisions are hereby extended to and made applicable to prepaid legal service plans.

Sec. -7 Failure to comply; penalty. Any plan which neglects or refuses to comply with this chapter shall be notified in writing by the director of regulatory agencies of the neglect or refusal and to take corrective action; if the neglect or refusal continues for seven days after notification, the plan, group, or plan administrator may be fined not more than \$1,000. Every day's neglect or refusal after the expiration of seven days shall be a separate offense."

SECTION 2. Section 431-3, Hawaii Revised Statutes, is amended by amending subsection (b) to read as follows:

"(b) The following contracts are not considered to be insurance for the purposes of this chapter:

- (1) A title insurance contract;
- (2) A bond with respect to which no premium is charged or paid;
- (3) A bond or contract or undertaking in the performance of which the surety has an interest other than that of surety;
- (4) A plan or agreement between an employer and any employee or his representative, individually or collectively, by the terms of which the employer or the parties to the plan or agreement agree to contribute to the cost of nonoccupational disability benefits, medical attention, treatment, or hospitalization for the employee or members of his family unless such plan is underwritten by an insurer as defined in this chapter;
- (5) A prepaid legal service plan as defined in chapter other than plans in which either the group offering the plan or the person administering the plan is otherwise subject to this chapter."

SECTION 3. Section 433-1, Hawaii Revised Statutes, is amended to read as follows:

"**Sec. 433-1 Definition; exemption.** Any corporation, unincorporated association, society, or entity

- (1) Organized and carried on for the primary benefit of its members and their beneficiaries and not for profit, and making provision for the payment of benefits in case of sickness, disability, or death to its members or disability or death of its members' wives or children, or making provision for the payment of any other benefits to or for its members, whether or not the amount of the benefits is fixed or rests in the discretion of the society, its officers, or any other person or persons, the fund from which the payment of the benefits shall be made and the fund from which the expenses of the society shall be defrayed being derived from assessments or dues collected from its members, and the payment of death benefits being made to the families, heirs, blood relatives, or persons named by its members as their beneficiaries; or
- (2) Organized and carried on for any purpose, which regularly requires money to be paid to it by its members, whether the money be in the form of dues, subscriptions, receipts, contributions, assessments, or otherwise, and which provides for the payment of any benefit or benefits or the payment of any money or the delivery of anything of value to its members or their relatives, or to any person or persons named by its members as their beneficiaries, or to any class of persons which includes or may include its members, whether or not the amount or value of the benefit, benefits, money, or thing of value is fixed, or rests in the discretion of the society, its officers, or any other person or persons; or
- (3) Organized and carried on for any purpose, whose requirements and provisions although not identical with are determined by the insurance commissioner to be substantially similar to those enumerated in (1) and (2) above,

is, for the purpose hereof, a mutual benefit society; provided that participating in a prepaid legal service plan subject to chapter shall not in itself make a corporation, unincorporated association, society, or entity a mutual benefit society and subject to this chapter. It shall be deemed to be a fiduciary company within the meaning of section 402-1 and shall, in all respects, unless otherwise specifically provided, be subject to part I of chapter 402, relating to fiduciary companies. Such society shall be exempt from the insurance laws of the State, except as hereinafter provided."

SECTION 4. Section 434-1, Hawaii Revised Statutes, is amended to read as follows:

"Sec. 434-1 Scope of chapter. This chapter relates only to fraternal benefit societies as hereinafter defined which desire to be authorized to pay benefits in accordance with this chapter after July 10, 1961. It shall not be deemed to apply to mutual benefit societies existing or exempted under chapter 433, and any mutual benefit society existing and authorized to pay benefits pursuant to chapter 433 on July 9, 1961, may continue to be so authorized and shall continue to be regulated or exempted by chapter 433. It shall not apply to prepaid legal service plans subject to chapter even though the plan may be offered by a fraternal benefit society."

SECTION 5. Section 235-1, Hawaii Revised Statutes, is amended by adding a new definition to be appropriately inserted and to read as follows:

“Prepaid legal service plan” (“Plan”) means a group legal service plan in which the cost of the services are prepaid by the group member or by some other person or organization in the member’s behalf. A group legal service plan is a plan by which legal services are rendered to individual members of a group identifiable in terms of some common interest. A plan shall provide:

- (A) That individual members shall be afforded freedom of choice in the selection of their own attorney or attorneys to provide legal services under such plan.
- (B) For the payment of equal amounts for the cost of services rendered without regard to the identity of the attorney or attorneys selected by the plan member or members. No plan shall otherwise discriminate on the basis of such selection.”

SECTION 6. Section 235-7, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

“(a) There shall be excluded from gross income, adjusted gross income, and taxable income:

- (1) Income not subject to taxation by the State under the Constitution and laws of the United States;
- (2) Rights, benefits, and other income exempted from taxation by section 88-91, having to do with the state retirement system, and the rights, benefits, and other income, comparable to the rights, benefits, and other income exempted by section 88-91, under any other public retirement system;
- (3) Any compensation received in the form of a pension for past services, or paid as a weekly benefit for unemployment up to but not in excess of the amount provided by the employment security law (it being the intention of this provision to exempt that amount whether paid from a fund or account in the federal or state treasury or paid by an employer or by a trust or other means provided by an employer);
- (4) Compensation paid to a patient affected with leprosy employed by the State or the United States in any hospital, settlement, or place for the treatment of leprosy;
- (5) Except as otherwise expressly provided, payments made by the United States or this State, under an act of Congress or a law of this State, which by express provision or administrative regulation or interpretation are exempt from both the normal and surtaxes of the United States, even though not so exempted by the Internal Revenue Code itself;
- (6) All proceeds received by organizations enumerated under section 237-23(6) to (9), resulting from the sale of brooms which are manufactured by blind persons working at the adult blind broom shop;
- (7) Any income expressly exempted or excluded from the measure of the tax imposed by this chapter by any other law of the State, it being the intent of this chapter not to repeal or supersede any such express exemption or exclusion;

- (8) The \$500 received by each member of the reserve components of the army, navy, air force, marine corps, coast guard of the United States of America and the Hawaii national guard as compensation for performance of duty as such;
- (9) Income derived from the operation of ships or aircraft if such income is exempt under the Internal Revenue Code pursuant to the provisions of an income tax treaty or agreement entered into by and between the United States and a foreign country, provided, that the tax laws of the local governments of that country reciprocally exempt from the application of all of their net income taxes, the income derived from the operation of ships or aircraft which are documented or registered under the laws of the United States;
- (10) The value of legal services provided by a prepaid legal service plan to a taxpayer, his spouse, and his dependents;
- (11) Amounts paid, directly or indirectly, by a prepaid legal service plan to a taxpayer as payment or reimbursement for the provision of legal services to the taxpayer, his spouse, and his dependents;
- (12) Contributions by an employer to a prepaid legal service plan for compensation (through insurance or otherwise) to his employees for the costs of legal services incurred by his employees, their spouses, and their dependents.”

SECTION 7. Section 235-9, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

“(a) Except as provided in sections 235-61 to 235-67 relating to withholding and collection of tax at source, and section 235-10 relating to “unrelated business taxable income”, the following persons and organizations shall not be taxable under this chapter:

- (1) Banks, building and loan associations, and industrial loan companies taxable under chapter 241; and insurance companies and agricultural cooperative associations, exclusively taxable under other laws;
- (2) Corporations, companies, associations, or trusts conducted solely for charitable, religious, educational, prepaid legal services, or scientific purposes within the State, including fraternal beneficiary societies;
- (3) Corporations, companies, associations, or trusts organized for the establishment and conduct of cemeteries, no part of the net earnings of which inures to the financial benefit of any private shareholder or individual;
- (4) Business leagues, chambers of commerce, real estate boards, or boards of trade, not organized for profit, and no part of the net earnings of which inures to the benefit of any private shareholder or individual;
- (5) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare which shall include the operation of a prepaid legal service plan, or local associations of employees, the membership of which is limited to the employees of a designated person or persons, and the net earnings of which are devoted exclusively to charitable, educational, prepaid legal service, or

- recreational purposes within the State;
- (6) Labor organizations;
- (7) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofit purposes, no part of the net earnings of which inures to the benefit of any private shareholder;
- (8) A trust forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries, and which meets the requirements of the Internal Revenue Code for exemption from the tax thereby imposed.”

SECTION 8. Section 235-10, Hawaii Revised Statutes, is amended to read as follows:

“**Sec. 235-10 Unrelated business taxable income.** The persons and organizations exempted by section 235-9 shall, if subject to tax under the Internal Revenue Code upon their “unrelated business taxable income”, be taxed thereon under this chapter. For the purposes of this section the term “taxable income” as used in sections 235-58 and 235-71 shall be read as “unrelated business taxable income”.

“Unrelated business taxable income” means the same as in the Internal Revenue Code, except that in the computation thereof sections 235-3 to 235-5, and 235-7 (except subsection (c)), shall apply, and in the determination of the net operating loss deduction under section 235-7(d) there shall not be taken into account any amount of income or deduction which is excluded in computing the unrelated business taxable income. Unrelated business income shall not include any income from a prepaid legal service plan.”

SECTION 9. Section 237-1, Hawaii Revised Statutes, is amended by adding a new definition to be appropriately inserted and to read as follows:

““Prepaid legal service plan” (“Plan”) means a group legal service plan in which the cost of the services are prepaid by the group member or by some other person or organization in the member’s behalf. A group legal service plan is a plan by which legal services are rendered to individual members of a group identifiable in terms of some common interest. A plan shall provide:

- (A) That individual members shall be afforded freedom of choice in the selection of their own attorney or attorneys to provide legal services under such plan.
- (B) For the payment of equal amounts for the cost of services rendered without regard to the identity of the attorney or attorneys selected by the plan member or members. No plan shall otherwise discriminate on the basis of such selection.”

SECTION 10. Section 237-23, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

“(a) This chapter shall not apply to the following persons:

- (1) Banks taxable under chapter 241;
- (2) Public service companies (as that term is defined in section 239-2), with respect to the gross income, either actual gross income or gross income estimated and adjusted, which is included in the measure of the tax

- imposed by chapter 239;
- (3) Public utilities owned and operated by the State or any county or other political subdivision thereof;
 - (4) Insurance companies which pay the State a tax upon their gross premiums under chapter 431;
 - (5) Fraternal benefit societies, orders, or associations, operating under the lodge system, or for the exclusive benefit of the members of the fraternity itself, operating under the lodge system, and providing for the payment of death, sick, accident, prepaid legal services, or other benefits to the members of such societies, orders, or associations, and to their dependents;
 - (6) Corporations, associations, or societies organized and operated exclusively for religious, charitable, scientific, or educational purposes, as well as that of operating senior citizens housing facilities qualifying for a loan under the laws of the United States as authorized by section 202 of the Housing Act of 1959, as amended by the Housing Act of 1961, the Senior Citizens Housing Act of 1962, the Housing Act of 1964, and the Housing and Urban Development Act of 1965 as well as that of operating a prepaid legal service plan;
 - (7) Business leagues, chambers of commerce, boards of trade, civic leagues, and organizations operated exclusively for the benefit of the community and for the promotion of social welfare which shall include the operation of a prepaid legal service plan, and from which no profit inures to the benefit of any private stockholder or individual;
 - (8) Hospitals, infirmaries, and sanitarium;
 - (9) Cooperative associations now or hereafter incorporated under and pursuant to chapter 421 or 422 and which fully meet the requirements of section 421-23 or section 422-33 (provided that the exemption shall apply only to the gross income derived from its activities authorized by chapter 421 or 422; and that the exemption shall not relieve any person who receives any proceeds of sale from the association of the duty of returning and paying the tax on the total gross proceeds of the sales on account of which the payment was made, in the same amount and at the same rate as would apply thereto had the sales been made directly by the person, and all such persons shall be so taxable);
 - (10) Building and loan associations taxable under chapter 241;
 - (11) Persons affected with leprosy and kokuas, with respect to business within the county of Kalawao;
 - (12) Corporations, companies, associations, or trust organized for the establishment and conduct of cemeteries no part of the net earnings of which inures to the financial benefit of any private stockholder or individual (provided, that the exemption shall apply only to the activities of such persons in the conduct of cemeteries and not to any activity the primary purpose of which is to produce income, even though the income is to be used for or in the furtherance of the exempt activities of such persons);
 - (13) Industrial loan companies taxable under chapter 241, provided that the

- exemption shall apply only to the income from the “engaging in the business of an industrial loan company” as defined in section 408-2;
- (14) Businesses which are organized for the purpose of broadcasting radio programs to areas outside of the State to promote the Hawaiian tourist industry and which are solely supported by State funds;
 - (15) Local development companies incorporated under the laws of the State and approved by the Small Business Administration as qualifying for loans under section 502 of the Small Business Investment Act of 1958, as amended, provided that the exemption shall apply only with respect to gross income derived as interest on loans made to borrowers from loan funds obtained from the Small Business Administration but only if the loans are made at the same rates of interest payable to the Small Business Administration by the local development corporation;
 - (16) Nonprofit shippers associations operating under part 296 of the Civil Aeronautics Board Economic Regulations.”

SECTION 11. Statutory material to be repealed is bracketed. New material is underscored. In printing this Act, the revisor of statutes need not include the brackets, the bracketed material, or the underscoring.*

SECTION 12. This Act shall take effect upon its approval; provided that sections 5, 6, 7, and 8 shall apply to calendar years beginning after December 31, 1975 and that sections 9 and 10 shall take effect on July 1, 1976.

(Approved May 27, 1976.)

*Edited accordingly.