New West Manufacturing

COVERAGE AND EXCLUSIONS

Corporate officers (RCW 51.12.020(a) (1979); RCW 51.12.020(8) (1987)(1992))

Corporate officers, elected and empowered by the articles of incorporation or by-laws, who are also directors and shareholders, are excluded from the mandatory coverage of the Act pursuant to RCW 51.12.020(9) (1979), provided that they have voluntarily assented to such status. The statute imposes no limitation on the number of corporate officers who can be so excluded; the statute does not require any minimum stock ownership; and the statute does not require that officers who are excluded from mandatory coverage exercise substantial control over the business operation. ***….In re New West Manufacturing,* BIIA Dec., 88 3634 (1989)** [dissent] [*Editor's Note:* See later statutory amendments to RCW 51.52.020(8), Laws of 1991, ch. 246, § 4 (effective January 1, 1992) and *In re Amos Hammer Cutting*, BIIA Dec., 05 14484 (2006).]

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BEFORE THE BOARD OF INDUSTRIAL INSURANCE APPEALS
STATE OF WASHINGTON

IN RE: NEW WEST MANUFACTURING, INC.	**)**	**DOCKET NO. 88 3634**
	)	
FIRM NO. 515,636	**)**	**DECISION AND ORDER**

APPEARANCES:

Firm/Petitioner, New West Manufacturing, Inc., by
Daniel J. Tighe

Department of Labor and Industries, by
The Attorney General, per
Art DeBusschere, Assistant, and William R. Bayness, Legal Examiner

This is an appeal filed by the firm on September 12, 1988 from an order of the Department of Labor and Industries dated September 2, 1988 which affirmed the Notice and Order of Assessment of Industrial Insurance Taxes No. 59188 dated March 7, 1988. The order assessed industrial insurance taxes and penalties in the sum of $25,554.76 for the period January 1, 1987 through June 30, 1987. **REVERSED AND REMANDED**.

DECISION

Pursuant to RCW 51.52.104 and RCW 51.52.106, this matter is before the Board for review and decision on a timely Petition for Review filed by the employer to a Proposed Decision and Order issued on June 1, 1989 in which the order of the Department dated September 2, 1988 was affirmed.

The Board has reviewed the evidentiary rulings in the record of proceedings and finds that no prejudicial error was committed and said rulings are hereby affirmed.

The issue in this appeal is whether the corporate officer/director/shareholder exclusion of RCW 51.52.020(9) (1979) prohibits the Department from assessing industrial insurance taxes for certain employees of New West Manufacturing, Inc. (New West).

New West is a shake and shingle manufacturing business. The firm was incorporated on March 9, 1987 with the filing of the articles of incorporation with the Secretary of State. The articles of incorporation signed by Dale B. Henson, Jr. on March 6, 1987, named 16 initial directors of the corporation. Prior to incorporation, Dale Henson, Jr., and the other 15 individuals who formed the corporation were a partnership.

The articles of incorporation required the directors to adopt bylaws of the corporation and gave the directors the power to amend and replace the bylaws from time to time, but reserved to the shareholders the power to make or alter bylaws which specify the number of directors. The bylaws

were adopted by the directors on March 5, 1987, four days prior to the filing of the articles of incorporation with the Secretary of State. In addition to a president and secretary/treasurer, the corporation elected 14 vice presidents.

Most employees of the corporation were also shareholders, owning one share of stock. One notable exception was Dale Henson, Jr., the President, who purchased 500 shares. Each share had a par value of, and was purchased for, $1.00. During the audit period January 1, 1987 through June 30, 1987 most individuals who worked for the corporation were shareholders, corporate officers, and directors of the corporation.

Between March 23, 1987 and August 18, 1988 the corporation held ten special meetings and one annual meeting. At these meetings additional officers and directors were elected and allowed to purchase stock. Additionally, officers and directors were allowed to resign their office and sell their stock back to the corporation.

Ostensibly the Department is challenging the validity of New West's corporate form, by arguing the company has failed to meet certain formal requirements. In reality, the Department is concerned about "the purchase price of the stock and the number of vice- presidents and the fact that all of the individuals who worked for the firm were corporate officers". 3/29/89 Tr. at 33. The Department apparently argues that RCW 51.12.020(9) (1979) requires active involvement in the management of a corporation and substantial ownership of stock before the exemption for corporate officers/directors/shareholders can apply.

Our Industrial Appeals Judge determined that during the audit period January 1, 1987 through June 30, 1987 three individuals, David Hendrickson, Dan Desrosiers, and D. Yaples, received payments for their labor, but were neither officers, directors or shareholders. There is no evidence to establish that these three individuals were officers, directors, and shareholders of the corporation during the audit period and no exception has been taken to the judge's finding of fact. We therefore agree with the Industrial Appeals Judge that these three employees are subject to the mandatory coverage provisions of the Industrial Insurance Act.

The Industrial Appeals Judge also determined that approximately 27 millworkers who were officers, and also directors and shareholders of the corporation, were subject to the mandatory provisions of the Industrial Insurance Act. We disagree. We believe an incorrect analysis was used in the Proposed Decision and Order in determining that the Department has authority to assess

industrial insurance taxes for corporate officers who are also directors and shareholders, absent the corporation's election of coverage pursuant to former RCW 51.12.020(9) and 51.12.110.

We initially note that the Industrial Appeals Judge, as well as the parties, have assumed that the issues in this appeal are controlled by RCW 51.12.020(8) in its present form. However, that section as amended by Laws of 1987, ch. 316, § 2, p. 315 (SHB 677), took effect on July 26, 1987. The audit period for this case covers the period January 1, 1987 through June 30, 1987, a period which is entirely before the effective date of the current amended statute. We must therefore look to the provisions of former RCW 51.12.020(9) which was in effect during the audit period at issue.

Former RCW 51.12.020 (Laws of 1979, ch. 128, § 1, p. 488) provided in part:

> The following are the only employments which shall not be included within the mandatory coverage of this title:
>
> . . . (9) Any executive officer elected and empowered in accordance with the articles of incorporation or bylaws of a corporation who at all times during the period involved is also a director and shareholder of the corporation. Any officer who was considered by the Department to be covered on or after June 30, 1977, shall continue to be covered until such time as the officer voluntarily elects to withdraw from coverage in the manner provided by RCW 51.12.110. However, any corporation may elect to cover such officers who are in fact employees of the corporation in the manner provided by RCW 51.12.110.

To determine the scope of this exclusionary section, we have reviewed the history and development of the industrial insurance laws relating to coverage for corporate officers.

Prior to 1971, the Industrial Insurance Act covered only those employments specifically classified as extrahazardous. All employments were excluded unless specifically included. Laws of 1961, ch. 23, RCW 51.12.010. In 1971 the Legislature completely reversed this theory of coverage and declared that all employments were mandatorily included within the coverage of the Act except those specifically excluded. Laws of 1971, 1st Ex.Sess., ch. 289,] 2, p. 1543 (codified as amended at RCW 51.12.010) and] 3, p. 1544 (codified as amended at RCW 51.12.020.)

Between 1971 and 1979, corporate officers were not specifically excluded from mandatory coverage under RCW 51.12.020. However, RCW 51.32.030, as it read prior to July, 1977, provided:

> Any individual employer or any member or officer of any corporate employer who is carried upon the payroll at a salary or wage not less than the average salary or wage named in such payroll and who shall be injured, shall be entitled to the benefit of this title, as and under the same circumstances and subject to the same obligations as a workman: PROVIDED, that no such employer or the beneficiaries of such employer

> shall be entitled to benefits under this title unless the director, prior to the date of the injury, has received notice in writing of the fact that such employer is being carried upon the payroll prior to the date of the injury as the result of which claims for a [sic] compensation are made.

The Department interpreted RCW 51.32.030 to require written notification of an intent or election to be covered as a prerequisite to coverage for corporate officers.

In December, 1977, the Washington Supreme Court decided Jepson v. Dept. of Labor & Indus., 89 Wn.2d 394, 573 P.2d 10 (1977). Mr. Jepson was a vice president of a corporation. In addition to his administrative responsibilities, Mr. Jepson supervised construction work at jobsites. While supervising work, he was severely injured. He filed a timely claim for benefits which the Department rejected based on its interpretation of RCW 51.32.030, and the fact that Mr. Jepson had not notified the Department of any election to be covered. The court disagreed with the Department's analysis, and concluded that Mr. Jepson was mandatorily covered because there was no specific exclusion for corporate officers contained in RCW 51.12.020. Jepson, at 399.

Only a few months prior to the decision in Jepson, the Legislature had amended RCW 51.32.030 and struck any reference to corporate officers, thereby eliminating the requirement of electing coverage by providing written notification. Laws of 1977, 1st Ex. Sess., ch. 323, § 14, p. 1239 (effective date, July 1, 1977). This action by the Legislature, in combination with the decision in Jepson, clearly established that corporate officers were subject to mandatory coverage under the Act and could not withdraw from coverage.

In the 1979 legislative session, several bills were considered to exclude certain corporate employees from mandatory industrial insurance coverage--SB 2072, HB 92, SHB 92.

The original HB 92 provided:

> A member or officer of a corporate employer may file notice in writing with the director and with the corporate employer stating the member's or officer's desire to withdraw from coverage under this title. No member or officer of a corporate employer may be unduly pressured to withdraw from coverage nor may sanction be taken if the member or officer elects not to withdraw. The withdrawal shall become effective thirty days after the filing of the notice or on the date of the termination of the security for payment of compensation, whichever last occurs. Withdrawal of acceptance of this title does not affect the liability of the department or self-insurer for compensation for any injury occurring during the period of acceptance.
>
> A corporate member or officer who has withdrawn from coverage under this title may at a later date, by filing written notice with the director and

> corporate employer, elect to reinstate coverage under this title. Reinstatement shall be subject to a physical examination conducted by a medical doctor, the purpose of which is to determine the existence or nonexistence of any condition which may have resulted from injury prior to reinstatement.

Rather than stating an exclusion from mandatory coverage under RCW 51.12.020, this bill would have permitted members or officers of corporate employers to withdraw from mandatory coverage.

The bill analysis prepared for the House of Representatives on the original HB 92, which used the term "member or officer of a corporate employer", suggested "that the provision be limited to those with equity in the corporation and not extended to those made an honorary officer of the corporation while serving as an actual employee." Bill Analysis, K. Wiitala, House of Representatives, Labor Committee, at 1 (January 16, 1979.)

The Legislature thus considered the possibility that an individual might be an officer of a corporation in name only and not have any real equity or proprietarial interest in the corporation. Apparently to guard against the possibility that such individuals could be excluded from mandatory coverage, the Legislature added the requirement that the officer must also be a shareholder and director. This language was contained in SHB 92, which also changed the mechanism from an option to withdraw from mandatory coverage which was originally contemplated by HB 92, to an outright exclusion from coverage within RCW 51.12.020, with the option to elect coverage.

However, SHB 92, which was the final version enacted by the Legislature, imposed no requirement that the corporate officer own a majority or even a substantial percentage of corporate stock in order to qualify for the exclusion. The legislative history reveals that the House Labor Committee was provided with synopses of the Alaska, Connecticut, Tennessee, Oregon, California, Idaho, Maine, Minnesota, and North Dakota statutes. B. Longman, Office of Program Research, House of Representatives, Memorandum to House Labor Committee (April 4, 1978).

The most pertinent statutes were those from Oregon, Idaho, Maine, and North Dakota. The Idaho statute required a corporate officer to own not less than 10% of "all the issued and outstanding voting stock of the corporation" and to also be a director in order to be excluded from coverage. Idaho Code, § 72-212. Maine allowed any person who was a "bona fide owner of at least 20%" of the outstanding voting stock of the corporation by which that person was employed to waive coverage. Maine Rev.Stat., Title 39, § 2. North Dakota exempted "the president, vice presidents, secretary, or treasurer of a business corporation whose duties [were] solely those of such executive office." An

officer performing non-executive functions was not exempt. N.D.Code, § 65-01- 02. Oregon at that time exempted "officers of corporations" from coverage. Ore.Rev.Stat., § 656.027. Yet, even though the Washington Legislature was aware of various methods by which other states had restricted the corporate officer exclusion, it chose not to apply any of these requirements to further limit the scope of the Washington exclusion.

The Legislature also declined to provide any definition of what is meant by the term "executive officer elected and empowered in accordance with the articles of incorporation or bylaws of a corporation who at all times during the period involved is also a director and shareholder of the corporation." The decision not to include a definition was reached after the House Labor Committee considered a proposed substitute to HB 92 which would have defined a corporate officer as "a shareholder who is an active and direct participant in the management and policy-making functions of the corporation." Like the original version of HB 92, this proposed substitute would have provided a withdrawal mechanism rather than a straight exemption from mandatory coverage. Bill Analysis, K. Wiitala, House of Representatives Labor Committee (January 30, 1979). The Legislature chose not to adopt this proposed definition.

In addition, the Legislature also considered keeping all corporate officers, directors, and shareholders within mandatory coverage and simply allowing them to withdraw if they so elected and if certain criteria, such as the absence of undue pressure, were met. HB 92. This option as well was rejected.

Indeed the Legislature took the opposite tack. Not only were corporate officers/directors/shareholders excluded from mandatory coverage, but the final sentence of SHB 92 leaves no doubt about the Legislature's intention that corporate officers/directors/shareholders who essentially contribute their personal labor to the corporation are excluded from mandatory coverage, but may be given elective coverage if the corporation itself so elects. The critical language reads: "However, any corporation may elect to cover such officers who are in fact employees of the corporation in the manner provided by RCW 51.12.110." (Emphasis added)

In sum, after extensive debate and consideration of a variety of diverse options, the Legislature excluded from mandatory coverage "executive" officers who are "elected and empowered in accordance with the articles of incorporation or bylaws" and who are also directors and shareholders. Laws of 1979, ch. 128, § 1(9) p. 488. The language which the Department would now have us read

into the statute in order to narrow the exclusion from coverage was specifically considered and rejected by the Legislature.

The word "executive" is not defined in the statute and was deleted in 1987 by SHB 677 as a "technical" change requested by the Department of Labor and Industries. House Bill Report, Commerce and Labor Committee (February 9, 1987); See also Senate Bill Report, Commerce and Labor Committee (March 30, 1987). Larson defines the word "executive" to include such work as "policy making, hiring and firing, and negotiation of important contracts. .." 1C A. Larson, Workmen's Compensation Law, § 54.21(d) at 9-232 (1988). There is, of course, no statutory requirement that this executive authority actually be exercised. Indeed, as noted above, the Legislature rejected a proposed definition which would have required active involvement in the management of the corporation. However, apparently the Legislature did contemplate that the officer be "empowered" to perform executive functions, whether or not that power was actually utilized. Whether the "technical" deletion of "executive" at the Department's request in 1987 removed even this requirement is not entirely clear. Since the 1987 amendment is not currently before us, we need not address that question here.

In the final analysis, our review of the legislative history of former RCW 51.12.020(9) leads to the clear conclusion that the Legislature intended to exclude from mandatory coverage any and all corporate officers who are elected and empowered by the articles of incorporation or bylaws and who are also directors and shareholders of the corporation. We can find no other limitation imposed or intended by the Legislature. We therefore conclude that the Legislature intended what the plain reading of the statute reveals. Dennis v. Dept. of Labor & Indus., 109 Wn.2d 467, 479-80, 745 P.2d 1295 (1987).

Like the statute itself, Washington case law does not specifically interpret the term "executive officer elected and empowered in accordance with the articles of incorporation or bylaws of a corporation who. . . is also a director and shareholder of the corporation." Koreski v. Seattle Hardware Co., 17 Wn.2d 421, 135 P.2d860 (1943) provides some guidance. Koreski involved the question of whether a corporate officer who had not elected coverage under the Act could sue a third party employer who was covered under the Act. We discuss this case in detail infra with respect to our analysis of RCW 51.04.060. For our purposes here, Koreski contains some language concerning how corporate officer status is conferred, though that was not, of course, the issue before the court.

In Koreski the Supreme Court stated:

> We do not find any language within the workmen's compensation act from which it may be reasonably inferred that an officer of a corporate employer may not also have the position or status of a "workman." His status is determined, as aptly observed by counsel for appellant, by what he does and not by the office he holds; otherwise, a corporate employer could give an official title to each of its employees, fail to report its payroll or neglect to pay into the workmen's compensation fund, and thereby deprive a third person, employer or workman, of immunity guaranteed to such person by the statute.

Koreski, at 435. This language suggests two things -- that a corporate officer can also be a worker, which is obvious from the final sentence of RCW 51.12.020(9) (1979), and that a worker cannot be excluded from mandatory coverage by an employer who simply decides to call that worker a corporate officer, even though the worker does not in fact serve in that capacity.

Our research has also disclosed several Oregon cases of interest, though none is dispositive here, given the differences in our statutory schemes. Carson v. State Industrial Accident Commission, 152 Or. 455, 54 P.2d 109 (1936); Allen v. State Industrial Accident Commission, 200 Or. 521, 265 P.2d 1086 (1954); and Erzen v. State Accident Insurance Fund, 40 Or.App. 771, 596 P.2d 1004 (1979). The Oregon statute at issue in Carson and Allen read in pertinent part as follows:

> Any person who is . . . an officer of a corporation . . . may make written application to the commission to become entitled as a workman to the compensation benefits thereof, ... An officer of a corporation shall not be deemed a workman of such corporation and entitled to the benefits of this Act unless he complies with this section.

Carson, at 458-459 (§ 49-1816b, Ore.Code Supp.1935 (§ 3, ch. 116, Ore.Laws 1933)); Allen, at 525-526 (OCLA § 102-1732 (ORS 656.128) as amended by Ore.Laws 1947, ch. 8).

Carson was the first case raising the issue of the interpretation of the Oregon corporate officer exclusion. Briefly, the facts in Carson were that Mr. Carson had been employed as a common laborer for eleven years by one L.E. Miesen. Mr. Miesen decided to incorporate. Based on representations that it would neither cost him anything nor benefit him in any way, Mr. Carson agreed to the use of his name. One share was issued to him but it was never paid for nor was it delivered to him. Mr. Carson exercised no control over the business. He was elected as the secretary and as a director of the corporation, but no meetings of stockholders or directors were ever held. Mr. Carson continued working as a laborer and, about one year after the incorporation, was killed as a result of an industrial injury.

On these facts, the court held:

> [W]e believe it was never intended that an employee, being an officer of a corporation in name only and having no voice in determining the policy of the company, should be precluded from receiving benefits under the act. An officer of a corporation, within the meaning of the act, should at least have some financial interest in the company and have a voice in its management.

Carson, at 459-460. Mr. Carson's widow's pension claim was allowed.

The next Oregon case to raise the question of whether the corporate officer exclusion applied involved the president of a corporation who owned half of its stock and was hired, by vote of the directors and stockholders, to perform a variety of duties for the corporation, including some manual labor. The corporation had elected coverage generally and had even paid premiums based on Mr. Allen's work, but no specific notification of an election of coverage had been made for Mr. Allen.

Like Mr. Carson, Mr. Allen also died as a result of an industrial injury. The court held that since he was a "bona fide" corporate officer, his failure to specifically elect coverage was fatal to his widow's claim.

The third Oregon case we have reviewed is Erzen, which involved a claimant who owned 22% of the corporate stock, had been elected president by the board of directors at the only meeting the corporation had ever held, and was designated manager of the business. In addition to managing the business, Mr. Erzen also worked filling in as a security patrolman and was injured in that capacity. Since the decision in Allen and Carson, the Oregon statute had been twice amended. The version applicable in Erzen read as follows:

> All workers are subject to ORS 656.001 to 656.794 except those nonsubject workers described in the following subsections: . . . . (7) . . . officers of corporations.

ORS 656.027 (1965). Nonsubject corporate officers were still allowed to elect coverage.

The court concluded that the claimant was a "bona fide" officer of a corporation under the Carson test, but that since he was injured while performing duties associated with an ordinary employee, he was entitled to coverage despite his failure to elect such coverage. The court reached this conclusion in light of the Oregon Workers' Compensation Board's prior order interpreting ORS 656.027(7) to mean that whenever a corporate officer is engaged in performing the duties of an ordinary worker, he is subject to the Act, and that the exclusion applies only to corporate officers when they are performing official duties. Erzen, at 776. This latter interpretation, of course, is directly

contrary to the plain language of the last sentence of RCW 51.12.020(9) (1979) and therefore has no application in Washington. This judicial interpretation would also seem to have been overruled by subsequent legislative action in Oregon. Since the decision in Erzen, ORS 656.027 has been further amended and currently reads:

> All workers are subject to ORS 656.001 to 656.794 except those nonsubject workers described in the following subsections: .. (9) a corporate officer who is also a director of the corporation and has a substantial ownership interest in the corporation, regardless of the nature of the work performed by such officer.

All of these court cases arose in the context of whether an individual could sue for damages or receive workers' compensation benefits as a result of an injury. The question of premium assessment which we have before us was not at issue. The evidence in a case in which the Department is trying to collect premiums, as opposed to a case where an individual is trying to collect benefits, may well be developed in a different fashion.

Be that as it may, Koreski and the Oregon cases do provide some guidance. In effect, the Oregon courts, through case law, imposed a requirement that a "bona fide" corporate officer must also be a director and shareholder. That is essentially what is meant by the "bona fide corporate officer" test imposed by Carson. This is basically the statutory requirement in Washington in a nutshell. The Oregon Legislature also appears to have moved in this direction since the decision in Erzen.

The Oregon cases and Koreski also suggest that if a person is a corporate officer, director, and shareholder in name only he is not exempt from coverage. In addition, if an individual has not voluntarily agreed to become a corporate officer, shareholder and director, he does not attain that status. Since Mr. Carson obviously was given the misimpression that becoming a corporate officer and director would not affect him in any way, the court clearly felt he did not truly agree to that status. And someone who, like Mr. Carson, has not actually paid for and received stock is not really a shareholder.

But this does not mean that one can say, as the Proposed Decision and Order in effect said here, that simply because a person is really a worker and contributing personal labor to the corporation, that person is not excluded from mandatory coverage as a corporate officer, director, and shareholder. Our statutory scheme, particularly the final sentence of subsection (9), simply does not permit that result. As the Oregon court said in Allen, in each case it is a question of fact whether an individual is a "bona fide" corporate officer. We will look therefore to whether, under Washington

corporate law, a person is in fact a corporate officer, director, and shareholder. We will also look to whether a person is in fact "empowered," and whether the individual voluntarily entered into this business relationship and agreed to the status of corporate officer/director/shareholder.

This is the same type of inquiry we have undertaken in the past when we have reviewed employment and contractual relationships in order to determine if the mandatory provisions of the Industrial Insurance Act apply. We have evaluated contractual relationships, in detail, to determine whether the "essence of the contract" is the personal service of the worker and thus subject to the mandatory provisions of the Industrial Insurance Act, under the statutory definition of "worker." James D. Shanley & Wife, dba Northwestern Mutual Life Ins. Co., BIIA Dec., 87 0485 (1988); In re Traditions Unlimited, BIIA Dec., 87 0600 (1989). We have also examined a purported partnership agreement to determine if the substance of the relationship was truly one of employer-employee. In re K E W Construction, BIIA Dec., 87 0152 (1988). We have consistently looked to the substance of each relationship in order to determine coverage under the Act. We have done so by applying established rules of law. In KEW Construction we looked to the well-established rules on partnership law as determined by the Washington Supreme Court. (citing State v. Bartley, 18 Wn.2d 477 (1943)). We felt bound by the definition of partnership and the rules for determining the existence of a partnership as set forth in RCW 25.04.060 and RCW 25.04.070.

In K E W Construction, relied on by the Industrial Appeals Judge in support of his decision, we did not undertake to create new principles in the law of partnership which would give this Board the power to disregard a partnership relationship for the sole purpose of allowing the assessment of industrial insurance taxes. On the contrary, in KEW Construction we applied existing partnership law to determine if a partnership relationship truly existed. Having reached the conclusion that no partnership existed, and finding the relationship to be an employer-employee relationship, we were inextricably led to the conclusion that the partnership exclusion of RCW 51.12.020(5) was inapplicable and, therefore, that the workers involved were subject to the mandatory provisions of the Industrial Insurance Act.

The logical construct set forth in K E W Construction does apply to the analysis in the present case involving New West, but the rationale of K E W Construction is that this Board will apply the principles of existing law to determine if a business is excluded by the provisions of RCW 51.12.020.

Our analysis in K E W Construction does not support the analysis of the Proposed Decision and Order in this matter. If on the facts in K E W Construction we had found a partnership, our inquiry

would have ended. The provisions of RCW 51.12.020(5) would then have applied to exclude the partnership from the mandatory coverage of the Act.

The Industrial Appeals Judge in the Proposed Decision and Order focused on RCW 51.04.060 which provides:

> No employer or worker shall exempt himself or herself from the burden or waive the benefits of this title by any contract, agreement, rule or regulation, and any such contract, agreement, rule or regulation shall be pro tanto void.

The most recent judicial interpretations of that statute involve an employer's indemnification of a third party tortfeasor and are not particularly relevant here, except to the extent they permit such indemnification, despite the employer immunity bestowed by the Act. The courts have determined that this is not a waiver of the benefits of the Act which would be precluded by RCW 51.04.060. See, e.g., Redford v. Seattle, 24 Wn.App. 484 (1979) aff'd 94 Wn.2d 198 (1980).

Three older cases are somewhat more relevant to our discussion. Koreski v. Seattle Hardware Co., 17 Wn.2 421, 135 P.2d 860 (1943) involved a prior statute which provided:

> That no action may be brought against any employer or any workman under this act as a third person if at the time of the accident such employer or such workman was in the course of any extra-hazardous employment under this act .... Rem.Rev.Stat. (Sup.), § 7675.

Koreski, at 429. The question before the court was whether a corporate officer/worker who had not elected coverage under the Act could sue another employer who was engaged in extrahazardous employment under the Act and therefore was entitled to immunity from civil suit. Mr. Koreski argued that since he was a corporate officer and had not elected coverage under the Workers' Compensation Act, he was not bound by the exclusive remedy provisions of the Act. He therefore contended that he was free to sue another employer, even though that employer was covered under the Act.

Citing Lunday v. Dept. of Labor & Indus., 200 Wash. 620, 94 P.2d 744 (1939), the court stated: "Under the act, no employer or workman may exempt himself from the burdens or waive the benefits of the act." Koreski, at 436. The court concluded that Mr. Koreski could not refuse the remedy offered under the Act and thereby make a third party employer who was engaged in extrahazardous employment, and had complied with the provisions of the Act, liable in a civil suit. However, the precedential value of Koreski was seriously undermined by the later en banc Supreme Court decisions in Latimer v. Western Machinery Exchange, 40 Wn.2d 155, 241 P.2d 923 (1952) rev'd on rehearing,

42 Wn.2d 756, 259 P.2d 623 (1953) and Pink v. Rayonier Inc., 40 Wn.2d 188, 242 P.2d 174 rev'd on rehearing, 42 Wn.2d 768, 259 P.2d 629 (1953). See Comment, 1 Digest of Washington Cases on Workers' Compensation Law at 65-66.

The Lunday case cited in Koreski involved the question of whether the deceased was a worker at the time of his death. The court concluded that since the delivery trip during which Mr. Lunday was killed involved transporting both groceries (not extrahazardous employment) and meat (extrahazardous employment), he was engaged in extrahazardous employment when he died. His widow was therefore entitled to a worker's compensation pension. The Department had denied coverage because the employer was merely leasing space from a meat market, the market fixtures had been sold to another, and the employer was not itself involved in extrahazardous employment. The court determined the effect of the lease and bill of sale on the widow's right to benefits by referring to the "declared public policy of the act -- particularly as manifested by Rem.Rev.Stat., § 7685 [P.C. § 3479] . . .", the predecessor to RCW 51.04.060. However, despite this reference to the no-waiver provision, the real basis for the court's decision was that the employer had agreed in the lease to make meat deliveries. For that reason, i.e., because the employer was in fact engaged in extrahazardous employment, the widow was entitled to a workers' compensation pension.

One further case which interpreted RCW 51.04.060 is Lindbloom v. Dept. of Labor & Indus., 199 Wash. 487, 91 P.2d 1001 (1939). The facts there involved a widow's claim for pension based on her husband's death during the course of extrahazardous employment. The dispositive issue was whether the deceased was an employee or an independent contractor. The facts clearly showed that he was an independent contractor. Citing the predecessor to RCW 51.04.060, the widow argued that the contract was a "mere subterfuge to avoid paying industrial insurance premiums upon the men doing the work . . . ." Lindbloom, at 489. The court responded:

> There is no substantial evidence to sustain this contention. The law does not prevent the owner of timber land from entering into an independent contract to have it logged or to have a portion of the logging operation performed under such an agreement. Such contracts have been repeatedly sustained."

Lindbloom, at 489-490. The denial of the widow's pension was therefore upheld.

As with the cases interpreting the term "corporate officer", the cases involving RCW 51.04.060 arise in the context of whether someone should receive benefits under the Act or be permitted to sue a third party. We have found no cases interpreting RCW 51.04.060 which involve the question before

us, i.e., whether a corporate employer may be assessed premiums on hours worked by corporate officers/directors/shareholders.

In addition, none of those cases arose after the dramatic shift in 1971 to mandatory coverage, with listed exclusions. And obviously all were decided prior to the enactment of the specific corporate officer/director/shareholder exclusion at issue here.

It is therefore not entirely clear where RCW 51.04.060 fits into the analysis of whether an individual qualifies for the statutory exclusion. Certainly the no-waiver provision of RCW 51.04.060 cannot preclude employers from actually utilizing the exclusion established by the Legislature under RCW 51.12.020(9) (1979). The Legislature could not have intended to provide an exclusion from mandatory coverage and, at the same time, prohibit its use. What RCW 51.04.060 seems to permit, and require, is an inquiry to determine whether a person truly is a corporate officer, director, and shareholder, applying the factors outlined above and Washington corporate law.

We turn then to the question before us in this appeal: Whether each of the individuals for whom industrial insurance taxes are sought is an officer, elected and empowered by the articles of incorporation or bylaws, and also a director and shareholder of the corporation.

RCW 23A.12.040 provides a fixed rule for determining the existence of a corporation. Upon filing the articles of incorporation the corporate existence begins. In the present case the record indicates that New West is a duly formed corporation under the laws of the State of Washington.

In order to qualify for the exclusion provided in former RCW 51.12.020(9), the corporation must also show that the individuals sought to be excluded are officers, directors and shareholders of the corporation. On the facts before us, New West has met this requirement. The officers are excluded from the Industrial Insurance Act unless the corporation has elected coverage. There is no evidence to show that it has so elected.

The Department, in briefs filed with this Board, argues variously that the corporation did not strictly adhere to certain requirements set forth in its bylaws, and that since the initial designation of the directors was done prior to the filing of the articles of incorporation, the designation of the directors is void.

The Department points out that the corporation came into existence on March 9, 1987 when the articles of incorporation were filed with the Secretary of State. The Department also notes that the board of directors signed the "Consent to the action of the board of directors in lieu of organizational meeting of Directors" (Exhibit No. 43) on March 5, 1987. We also note that the shares of stock were

issued by the corporation to the initial shareholders on March 6, 1987. The Department believes that such action by the shareholders and directors prior to the filing of the articles of incorporation voids the selection of the directors and officers. The Department cites no authority which would cause this sequence of events to negate the election of the directors and officers of the corporation. We believe that, although the corporation acted prior to its formal existence in naming directors, officers, and issuing shares of stock, those acts of the corporation were clearly subsequently ratified by the shareholders and directors. 2 W. Fletcher, Private Corporations § 397 (PermEd 1982).

The Department also argues that the initial designation of the officers in the "Consent to action of board of directors in lieu of organizational meeting of Directors" merely designates the officers and does not reflect that the officers were elected. The Department concluded that those officers therefore are not elected officers of the corporation. Article III of the bylaws does require that the officers shall be elected at the first meeting (Exhibit 3). Yet in subsequent meetings there is a consistent reference to the election of the officers. We can only conclude by the subsequent acts of the corporation in electing various vice presidents that the initial officers were also elected as required by the bylaws.

It is important to note that the officers and directors of this corporation are the shareholders. Thus, any criticism of the action of the officers or directors is not well-founded since the acts of the officers and the directors constitutes the acts of the corporation through its shareholders. Where the directors are the shareholders, they are the corporation. Steeple v. Max Krumer Company, 121 Wash. 47, 208 Pac. 444 (1922); 2 W. Fletcher, Private Corporations § 395 (Perm. Ed. 1982).

The Department also argues that because improper notice was given to the shareholders, officers, and directors regarding the subsequent meetings, that the election of the officers at those meetings is void. However, our review of the corporate law of this state indicates that the validity of election of officers of corporations can be effectively questioned only by the corporation or its shareholders. Baggot v. Turner, 21 Wash. 339, 58 Pac. 212 (1899) 2 W. Fletcher, Private Corporations § 365 (PermEd 1982). Again, the officers and directors are also the shareholders. Hence, the election of all of these officers and directors was accomplished by a vote of a majority of the shareholders.

The Department also argues that the increase in the number of directors and officers was not allowed by the bylaws. However, Article 5 of the articles of incorporation sets forth that there shall not be less than three directors and that the shareholders shall from time to time determine the number of directors (Exhibit No. 2). Although there is no explicit record of an increase in the number of directors

or officers of the corporation, the only logical conclusion that can be drawn from the acts of the shareholders is that the number of directors and officers was increased at the various shareholder meetings since, in fact, the shareholders voted for additional directors and officers. A corporation may alter, amend or repeal bylaws, and may waive bylaws expressly or impliedly. Bay City Lumber Company v. Anderson, 8 Wn. 2d 191, 111 P.2d 771 (1941). That appears to have been the case with respect to designating the number of directors or officers of New West.

Finally, the Department argues that because the corporation allowed one-person one-vote in its election of the directors and officers, when the bylaws call for votes based on the ownership of the shares of stock in the corporation, that the election of the officers and directors is void. However, again, the only conclusion that can be drawn from the acts of the shareholders of this corporation is that the bylaws were expressly or impliedly altered at the meetings where the shareholders, in fact, elected additional officers and directors by the use of one-person, one-vote. There is no indication that any shareholder has complained about any irregularity in the election of the officers or directors. Further, while as a general rule informality in the operation of a corporation is not allowed, an exception is noted for small, closely held corporations. Block v. Olympic Health Spa, Inc., 24 Wn.App. 938, 604 P.2d 1317 (1979); 2 W. Fletcher, Private Corporations § 394.1 and 397 (Perm.Ed.1982).

Although the Department seeks to question the acts of this corporation in the selection of its officers and directors, we are aware of no grant of authority to the Department to question the internal management of the corporation. The objections raised by the Department relating to this corporation's failure to follow, to the letter, the internal procedures of its bylaws and articles regarding notice and voting requirements fails to consider the fact that the shareholders are the directors and, hence, the corporation. While these objections, if lodged by directors, officers, or shareholders of this corporation may be valid concerns, we do not believe, nor has any authority been cited, that the Department has the power to raise these issues in opposition to the desires of the shareholders of the corporation.

We have also reviewed the doctrine of corporate disregard set forth by the Washington Supreme Court in Morgan v. Burks, 93 Wn.2d 580, 611 P.2d 751 (1980). That doctrine, which is intended to protect third parties from harm when dealing with corporate entities, does not appear applicable to the issues raised in this appeal. We have found no case authority which would allow the Department to disregard the corporate existence simply to assess industrial insurance taxes. The Department has not offered any authority in support of the application of the doctrine to the facts of this

case, nor has it even suggested the doctrine is applicable. See generally Harris, Washington's Doctrine of Corporate Disregard, 56 Wash.Law Rev. 253 (1981).

We have also examined the doctrine of ultra vires as it exists pursuant to RCW 23A.08.040. We can find no grant of authority to the Department in that statute which would allow the Department to declare invalid the acts of the corporation in the selection of its officers and directors.

Indeed, we have been unable to find any grant of authority to the Department which would allow it to challenge the ability of the corporation to act in selecting its officers or directors, or which would allow it to otherwise declare such designations void, for the sole purpose of assessing industrial insurance taxes. We, of course, are not empowered to grant the Department that authority, and supplant the existing law in this state relating to corporations, in order to permit the assessment of industrial insurance taxes which are not otherwise due.

Once again we observe that no shareholder, officer or director has objected to the manner in which this closely held corporation has conducted its business. By choosing the corporate form of business, the corporation and its officers derive statutory benefits and incur statutory obligations. We are not prepared to substitute our judgment for the judgment of this or any other business corporation in conducting its internal affairs. While it is inevitable that certain partnerships and corporations may choose their business form at least in part to escape the benefits and burdens of our Industrial Insurance Act, we must assume that they do so with their eyes open. More importantly, they do so with the express consent of the Legislature.

We admit that we do find it odd that workers who would otherwise be subject to the Act can be excluded from coverage by virtue of the fact they are elected corporate officers and directors and retain a nominal, single share of stock in a corporation. The workers of New West who each hold a share of stock valued at $1.00 are certainly not "owners" of the corporation in any meaningful sense. However, it is not our function to question the wisdom or social utility of an exclusion from mandatory coverage which the Legislature has clearly seen fit to permit. If the Legislature is troubled by such a business relationship fitting within the corporate officer exclusion of RCW 51.12.020, it, unlike this Board, may take action to change the statute.

Businesses should be able to rely upon the plain meaning of the exclusionary language contained in RCW 51.12.020. A business which has elected a form which is excluded by the specific terms of the Act should not be required to somehow "justify" the selection of that form of business to the Department in order to avoid the mandatory provisions of the Industrial Insurance Act. To decide

otherwise would vest the Department with impermissible discretion in applying -- or refusing to apply -- the exclusions set forth in RCW 51.12.020.

The Department has exceeded its authority in attempting to void the acts of this corporation in selecting its directors and officers. While the Department attempts to use the formal requirements for corporations as a tool for attacking the corporate form here, the real quarrel the Department has with New West is clear from the testimony of Steve Benfield, the field auditor who performed the audit in this case. As Mr. Benfield acknowledged, what the Department was really concerned with here was "the purchase price of the stock and the number of vice- presidents and the fact that all of the individuals who worked for the firm were corporate officers." 3/29/89 Tr. at 33.

In essence what the Department is challenging is the number of vice-presidents, the fact that they are employees of the corporation, and the fact that each one owns only one share. Yet the Washington corporation statute does not restrict the number of vice-presidents a corporation may have. And RCW 51.12.020 does not restrict the exclusion to a certain number of officers or to officers who own a certain number of shares. Furthermore, RCW 51.12.020 affirmatively excludes from mandatory coverage corporate officers/directors/shareholders who are also employees, and they may be electively covered only by choice of the corporation.

The Department would have us read into the statute, language which the Legislature rejected during the debate surrounding HB 92 and SHB 92 in 1979. The Department wants us to interpret the statute to require active involvement in management of the corporation and substantial ownership of stock before the exclusion can apply. No such language appears in the statute. In fact, such language was specifically considered and rejected by the Legislature. The Department's arguments are best made in that forum. Unlike the Legislature, we do not make the law; like the Department, we can only interpret legislative enactments.

While there may well be situations where we will find that the requirements of the corporate officer/director/shareholder exclusion are not met, this is not one of them. In this case, the original 16 incorporators had previously been a partnership, and the Department's audit (Exhibit No. 47) shows that the Department determined they were entitled to the exclusion from mandatory coverage for partners under RCW 51.12.020(5). Only after this same group of 16 incorporated did the Department, for some reason, decide they were not entitled to the exclusion offered under RCW 51.12.020(9) (1979) for corporate officers/directors/shareholders. There is no evidence that anything much changed to justify this new scrutiny by the Department. If anything, the parties took on a more formal

organization -- they filed articles of incorporation, issued stock which the shareholders paid for, held meetings, elected directors, and appointed vice-presidents. The corporate officers, directors, and shareholders apparently consented to that status; certainly there is no evidence to the contrary. They are therefore entitled to the exclusion from mandatory coverage which the Legislature created in 1979 after substantial discourse. Public policy issues are best resolved before the Legislature, the policy-making body where diverse interests are represented and the issues can be thoroughly debated.

After consideration of the Proposed Decision and Order and the Petition for Review filed thereto, and a careful review of the entire record before us, we are persuaded that the Department's Notice and Order of Assessment which assessed industrial insurance taxes and penalties for the period January 1, 1987 through June 30, 1987, is incorrect as it pertains to the officers, who are also directors and shareholders of the corporation, and should be reversed. This matter is remanded to the Department with instructions to issue an order finding that the officers, who are also directors and shareholders of this corporation, have not had coverage elected by the corporation under the provisions of former RCW 51.12.020(9) and 51.12.110 and that no industrial insurance taxes are due for those officers, directors, and shareholders for the period January 1, 1987 through June 30, 1987, and to assess industrial insurance taxes and penalties only for those employees of the corporation that are covered under the mandatory provisions of the Industrial Insurance Act.

FINDINGS OF FACT

1. On March 7, 1988 the Department issued Notice and Order of Assessment No. 59188 which assessed industrial insurance taxes and penalties for the period January 1, 1987 through June 30, 1987 against New West Manufacturing, Inc. in the amount of $25,554.76. On March 9, 1988 the firm mailed a protest and request for reconsideration. On March 16, 1988 the Department issued an order holding Notice and Order of Assessment No. 59188 in abeyance. On September 2, 1988 the Department issued an order affirming the March 7, 1988 Notice and Order of Assessment. On September 12, 1988 the firm filed a notice of appeal with the Board of Industrial Insurance Appeals and on September 26, 1988 the Board issued an order granting the appeal and assigned it Docket No. 88 3634.

2. On March 9, 1987 New West Manufacturing, Inc. became a corporation by filing articles of incorporation with the Secretary of State.

3. During the period January 1, 1987 through June 30, 1987, David Hendrickson, Dan Desrosiers, and D. Yaples were employees of the

corporation and were not officers, shareholders or directors of the corporation.

4. The various officers of the corporation, who were also directors and shareholders of the corporation, did not have coverage elected by the corporation under the Industrial Insurance Act pursuant to the provisions of former RCW 51.12.020(9) (1979) and 51.12.110.

CONCLUSIONS OF LAW

1. The Board of Industrial Insurance Appeals has jurisdiction over the subject matter and parties to this appeal.

2. The various officers who are also directors and shareholders of New West Manufacturing, Inc. are excluded from the mandatory provisions of the Industrial Insurance Act pursuant to former RCW 51.12.020(9) (1979), coverage under the Act not having been elected by the corporation pursuant to RCW 51.12.110.

3. New West Manufacturing, Inc. owes industrial insurance taxes, and penalties equal to 20% of the taxes owing, for the three employees not excluded from the mandatory provisions of the Act, listed in Finding of Fact No. 3.

4. The Department of Labor and Industries incorrectly assessed industrial insurance taxes and penalties for the employees who were officers and also directors and shareholders of the corporation.

5. The order of the Department of Labor and Industries dated September 2, 1988 which affirmed Notice and Order of Assessment No. 59188 which assessed industrial insurance taxes and penalties as due and owing in the amount of $25,554.76 for the period January 1, 1987 through June 30, 1987, is incorrect and is reversed and this matter is hereby remanded to the Department with instructions to issue an order finding that the officers, directors and shareholders of this corporation had not had coverage elected by the corporation under the provisions of former RCW 51.12.020(9) (1979) and RCW 51.12.110 and that no industrial insurance taxes are due for those officers who were also directors and shareholders for the period January 1, 1987 through June 30, 1987, and to further assess industrial insurance taxes, and penalties equal to 20% of the taxes owed, only for those employees of the corporation who were not officers and also directors and shareholders, i.e., David Hendrickson, Dan Desrosiers, and D. Yaples.

It is so ORDERED.

Dated this 6th day of December, 1989.

BOARD OF INDUSTRIAL INSURANCE APPEALS

/s/_____

SARA T. HARMON Chairperson

/s/_____

PHILLIP T. BORK Member

DISSENT

Because the majority's opinion legitimizes an obvious sham attempt to evade the provisions of our Industrial Insurance Act, I must dissent. The Industrial Insurance Act is remedial in nature and its intent is to provide protection for workers by providing sure and certain relief for those injured in their work. The Act is to be liberally construed with doubts resolved in favor of the worker. Dennis v. Dept. of Labor & Indus., 109 Wn.2d 467 (1987); Sacred Heart Med. Ctr. v. Carrado, 92 Wn.2d 631, 600 P.2d 1015 (1979). Because of the majority's opinion, the workers of New West Manufacturing, Inc., who are already exposed to the dangers of the workplace will now be deprived of the protection guaranteed by our Industrial Insurance Act. Should any of these workers be killed or injured in the workplace, their families run a substantial risk of being left destitute. I will have no part of a decision which will allow an employer to escape its burden under our Industrial Insurance Act and reap that economic reward, at the expense of the injured worker.

The majority believes that RCW 51.04.060 which provides that no employer or worker may attempt to exempt themselves from the provisions of the Industrial Insurance Act is inapplicable in this situation. I disagree. It is clear to me that the agreement between the workers and New West Manufacturing, Inc., wherein the workers become nominal officers, directors, and shareholders, is clearly an agreement with no other purpose than to evade the benefits and burdens of the Industrial Insurance Act. It therefore is void pursuant to RCW 51.04.060.

I also disagree with the majority's analysis of the legislative history of RCW 51.12.020(9). The legislative history reveals a concern by the Legislature to allow corporate officers, whose position with the firm is similar to that of sole proprietors and partners, to be exempt from coverage under the Industrial Insurance Act. The legislative history does not reveal an intent by the Legislature to allow sham arrangements whereby workers are made nominal officers, shareholders, and directors of a corporation in order to avoid the benefits and burdens of the Industrial Insurance Act.

While the majority opinion is reluctant to interpret the term "corporate officer" as it is used in 51.12.02(9) by reference to any other source besides corporate law, I believe such a narrow view is unsupported by case law. In Carson v. State Industrial Accident Commission, 152 Or. 455 (1936), the Oregon Supreme Court had no difficulty in interpreting the term "corporate officer" as defined in their Workers' Compensation Act. The court in Carson determined that only bona fide corporate officers, with a right to control the corporation and a financial interest in the corporation, were subject to the exclusionary language of their statute. It's interesting to note that the worker in that case, Mr. Carson,

actually owned one share of stock in the company for which he worked. That did not deter the Oregon court from determining that he lacked a financial interest in the corporation. Additionally in Carson, although Mr. Carson had signed various documents for the corporation as its secretary, the court had no difficulty in determining that his actual role in the corporation, in fact, excluded him from management and control. With the clear direction enunciated by the Oregon court in Carson v. State Industrial Accident Commission, I find it unreasonable for this Board to sit on its hands and refuse to liberally construe our Industrial Insurance Act and provide protection to the workers. The majority's opinion will only encourage further attempts by unscrupulous and immoral employers to erode the will of the Legislature in providing protection for workers and their families. By allowing these sham agreements to destroy the protection provided by the Industrial Insurance Act, this Board is allowing the enrichment of this employer at the expense of the lives and well being of the workers and their families. This I will not do.

For the reasons stated above, I would adopt the Proposed Decision and Order.

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FRANK E. FENNERTY, JR. Member