

IN THE WORKERS' COMPENSATION COURT OF THE STATE OF MONTANA

1999 MTWCC 55

WCC No. 9812-8106

SYNTHETIC TECHNOLOGIES CORPORATION
AND WEATHERGUARD CORPORATION

Appellants

vs.

EMPLOYMENT RELATIONS DIVISION
UNINSURED EMPLOYERS' FUND

Respondent.

DECISION ON APPEAL

Summary: After a DOL decision finding two appellant corporations were "uninsured employers," penalties were assessed against those corporations. On appeal to the WCC, the corporations argued that the workers in question were not employees within section 39-71-401, MCA (1995) because they owned 20% of the shares of stock of the corporation.

Held: The exemption invoked by appellants requires that the workers own 20% of the shares of the corporation's stock. A necessary incident of ownership is the right to use or dispose of the property in any lawful way which does not infringe on the rights of others. Here, the workers did not have the right to dispose of the stock where other stockholders could divest them of shares without compensation and where one individual collected "irrevocable proxies" from the would-be shareholder-workers.

Topics:

Constitutions, Statutes, Regulations and Rules: 39-71-401, MCA (1995). WCC affirmed DOL decision that corporations employing "shareholders" were uninsured and liable for penalties. Exemption under section 39-71-401, MCA (1995) for 20% shareholders did not apply because "shareholders" did not in fact own stock where they could be divested of ownership by others without compensation and one person had obtained "irrevocable proxy" for all shares.

Employment: Employee. WCC affirmed DOL decision that corporations employing "shareholders" were uninsured and liable for penalties. Exemption under section 39-71-401, MCA (1995) for 20% shareholders did not apply because "shareholders"

did not in fact own stock where they could be divested of ownership by others without compensation and one person had obtained "irrevocable proxy" for all shares.

Penalties: Uninsured Employers. WCC affirmed DOL decision that corporations employing "shareholders" were uninsured and liable for penalties. Exemption under section 39-71-401, MCA (1995) for 20% shareholders did not apply because "shareholders" did not in fact own stock where they could be divested of ownership by others without compensation and one person had obtained "irrevocable proxy" for all shares.

¶1 This is an appeal from a Department of Labor and Industry decision finding that the two appellant corporations were "uninsured employers." Penalties of \$40,145.56 were imposed upon appellant Weatherguard Corporation, and \$24,525.13 upon appellant Synthetic Technologies.

¶2 Weatherguard and Synthetic are both duly organized Montana corporations. Neither company carried workers' compensation insurance coverage even though they had workers. Both claim that all of their employees were shareholders each owning 20% of corporate stock and were therefore exempt from workers' compensation coverage requirements, § 39-71-401(2)(q)(iii), MCA. At the hearing below, the Department's hearing officer found that the employees did not in fact own shares. This appeal followed.

Issues on Appeal

¶3 The appellant corporations state the issue on appeal as follows:

Whether person [sic] working for Weatherguard Corporation or Synthetic Technologies Corporation are employees or officers of the corporation exempt from statutory and penalty premiums.

(Appellants' Brief at 2.) In their written appeal, they allege that the decision below was:

- in violation of Constitutional or Statutory Provisions;
- affected by other error of law;
- clearly erroneous in view of the reliable, probative and substantial evidence on the whole record; and/or
- arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of the Department's discretion.

Facts

¶4 The basic facts are not in dispute.

¶5 Van Smith, as sole proprietor, owns a business that sells insulated siding for buildings. Prior to December 1994, he employed "applicators" to install the siding for purchasers of the siding.

¶6 In 1994 and 1995, Smith and others formed the two appellate corporations. Smith was issued 20% of the stock in each corporation. The remaining 80% was issued to applicators who installed siding.

¶7 The shares of stock in both corporations were issued without any consideration other than promises to work for the corporations in the future.

¶8 The shareholder/applicators were paid by the hour. They received no dividends.

¶9 Several shareholder/applicators were summarily removed and their shares canceled without any remuneration, and new shareholder/applicators were issued shares without any financial consideration. Specific examples are listed in the decision below, a copy of which is attached.

¶10 As argued by the corporations' attorney during oral argument of this appeal, neither corporation ever had any assets and never expected to have assets.

¶11 Three shareholders in each of the corporations signed irrevocable stock proxies appointing Van Smith to vote their shares.

¶12 Shareholders of the corporations were limited to five so that no shareholder owned less than 20% of the corporate shares.

¶13 A field representative of the Department audited both corporations and determined that the shareholder/applicators did not in fact own stock because the stock had no value.

Discussion

¶14 At issue is the application of section 39-71-401, MCA (1995), which provides in relevant part:

39-71-401. Employments covered and employments exempted. (1) Except as provided in subsection (2), the Workers' Compensation Act applies to all employers, as defined in 39-71-117, and to all employees, as defined in 39-71-118. An employer who has any employee in service under any appointment or contract of hire, expressed or implied, oral or written, shall elect to be bound by the provisions of compensation plan No. 1, 2, or 3. Each employee whose employer is bound by the Workers' Compensation Act is subject to and bound by the compensation plan that has been elected by the employer.

(2) Unless the employer elects coverage for these employments under this chapter and an insurer allows an election, the Workers' Compensation Act does not apply to any of the following employments:

....

(q) an officer of a quasi-public or a private corporation or manager of a manager-managed limited liability company who qualifies under one or more of the following provisions:

....

(iii) the officer or manager owns 20% or more of the number of shares of stock in the corporation or owns 20% or more of the limited liability company;

....

¶15 Appellant corporations argue that they are duly organized Montana corporations, that the shareholder/applicators were issued 20% of the shares of the stock of the corporation, and that the applicators therefore owned the 20% shares of stock and were exempt from the coverage requirements of the Workers' Compensation Act.

¶16 Appellants are correct that the corporations existed. Whether their purported shareholders were in fact shareholders is another issue entirely.

¶17 The exemption invoked by appellants requires that the applicators **own** 20% of the shares of stock of the corporations. A necessary incident of "ownership" is "the right to use or dispose of it in any lawful way which does not infringe the rights of others." *Thompson v. Lincoln Nat. Life Ins. Co.*, 114 Mont. 521, 533, 138 P.2d 951, 957 (1943); *In re Hunter's Estate*, 125 Mont. 315, 324, 236 P.2d 94, 99, (1951) (quoting from *Thompson*). The facts of the present case show convincingly that the shareholder/applicators did not have the right to dispose of their shares of stock. By simple vote, other shareholders could divest them of their shares without compensation and without even an appraisal of the value of the shares. By fact of the irrevocable proxies, one individual - Van Smith - could eliminate any shareholder without compensation. The attorney for the corporations now argues that the proxies are legally invalid, however, the fact that they were gathered by Smith, along with exclusions of shareholders without compensation, shows that the applicators' stock ownership existed in form, not substance. The corporations were shams to evade workers' compensation insurance coverage requirements.

ORDER

¶18 1. The decision below is **affirmed**.

¶19 2. This decision is certified as final for purposes of appeal pursuant to ARM 24.5.348.

¶20 3. Any party to this dispute may have 20 days in which to request an amendment or reconsideration from this Decision on Appeal.

DATED in Helena, Montana, this 1st day of September, 1999.

(SEAL)

\s\ Mike McCarter

JUDGE

c: Mr. Gary S. Deschenes

Mr. Daniel B. McGregor

Attachment: Findings of Fact; Conclusions of Law; and Order

Date Submitted: June 7, 1999