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NOV 19 2007

Department of Insurance
State of Idaho

BEFORE THE DIRECTOR OF THE DEPARTMENT OF INSURANCE

STATE OF IDAHO

In the Matter of

DOCKET NO. 2350

DIAMOND Z MANUFACTURING and
RULE STEEL TANKS, INC.

FINDINGS OF FACT, CONCLUSIONS OF
LAW, DECISION AND PRELIMINARY
ORDER

A.

Procedural Status of the Case

On February 12, 2003, the National Council on Compensation Insurance, Incorporated (NCCI), issued to Liberty Northwest, the surety for Diamond Z Manufacturing and Rule Steel Tank (hereinafter Rule Steel or Diamond Z/Rule Steel), a decision in which NCCI determined that Weld Tech, Inc., underwent a change in ownership and therefore Weld Tech, Inc.'s adverse experience rating should be combined with and therefore become the rating of Diamond Z/Rule Steel.

This followed correspondence from Liberty Northwest, requesting the change, dated January 20, 2003, in response to a document signed by Greg Burkhart, an officer of Rule Steel Tanks. Mr. Burkhart provided information to Liberty on or about January 11, 2003, indicating

among other things, that Daniel Rule owned 100% of both Rule Steel Tanks, Inc., and Rule Pacific Corporation, dba Weld Tech.

On April 6, 2005, Mr. Burkhart wrote to Tari Harding of Liberty Northwest, contesting the way in which Liberty Northwest presented to NCCI Rule Steel's relationship with Weld Tech, Inc. Mr. Burkhart's April 6, 2005, correspondence was contained on letterhead of Rule Steel. The April 6, 2005, correspondence to Liberty Northwest challenges whether it was proper to combine the experience of Weld Tech, Inc. with the rest of the operations of Rule Steel Tanks, from activities prior to Rule Steel's asset acquisition as of January 12, 2002,.

Another letter dated April 6, 2005, was addressed to NCCI from Mr. Burkhart, also challenging the combination and imputing the Weld Tech, Inc., experience rating to Rule Steel Tanks, and its combined business with Diamond Z Manufacturing.¹

On May 17, 2005, on behalf of Diamond Z/Rule Steel, Work Care Northwest, Inc., another worker's compensation insurer, wrote to Kristina Nelson at NCCI, also challenging the experience rating combination of Weld Tech, Inc. with that of Diamond Z/Rule Steel. Work Care Northwest's Vice President, Cindy Copple, stated, "The sale was of physical assets only," but the "operation, employees, etc., of Weld Tech, Inc. did not get sold or conveyed to Rule Steel Tanks."

In response, on May 18, 2005, NCCI replied to Ms. Copple at Work Care Northwest stating that the contract of sale of the Weld Tech, Inc., assets to Rule Steel included not only personal property but also "goodwill" of Weld Tech, Inc. Further, because Weld Tech, Inc., did not continue as an ongoing entity, and because "Rule Steel continued operating essentially the

¹ The manner in which Diamond Z and Rule Steel came to be affiliated is not apparent from the record, but also appears to be irrelevant.

same type of business, they [apparently meaning Rule Steel] acquire the previous experience for Weld Tech.”

On November 8, 2005, Diamond Z/Rule Steel, through its counsel, Michael Christian, completed a worker’s compensation Appeal request form addressed to NCCI. This document appears in NCCI Exhibit 1, at Pages 6, 7, and 8.

On November 21, 2005, in a ruling authored by Tim Hughes, the NCCI’s regulatory services manager, NCCI stated, in relevant part, “the sale of physical assets to a business that continues its operation constitutes an ownership change for purposes of experience rating. With the sale of both the physical assets as well as the goodwill accumulated by Weld Tech, it is NCCI’s position that a transfer of the business occurred.”

NCCI went on to state, “It is noted that the operations prior to the sale were classified to Code 3040, and that the buyer continued Code 3040 type operations. For these reasons, it is NCCI’s position that the transfer of experience is in keeping with the above rule.” The November 21, 2005, ruling also provided for further appeal to the Idaho Worker’s Compensation Classification Review Committee (Review Committee). The parties do not dispute that Diamond Z/Rule Steel appealed this November 21, 2005, ruling.²

The Review Committee apparently met on June 22, 2006, to review Diamond Z/Rule Steel’s Appeal.

In correspondence dated July 7, 2006, addressed to Diamond Z/Rule Steel’s lawyers, Tim Hughes, on behalf of the Committee, stated that the Review Committee determined “that the ownership ruling applied to Rule Steel Tanks is affirmed. The Appeal to remove the prior loss

² The record does not contain the document that appealed the November 21, 2005, ruling, but because the Review Committee acted on the matter, the hearing officer deems this omission from the record irrelevant.

experience of Weld Tech is denied.” Another thirty days’ appeal rights were also described in this July 7, 2006, correspondence.

On July 12, 2006, through counsel, Rule Steel Tanks petitioned the Department for Appeal of the Review Committee’s Decision.

On July 17, 2006, the matter was referred to the undersigned.

The parties conducted a telephonic prehearing conference with the Hearing Officer on September 1, 2006, at 10:00 A.M.

As a result of that telephonic conference, the Hearing Officer issued a Scheduling Order on September 29, 2006, providing that the parties would submit, as agreed during the conference, all of the matters in writing and consider it submitted on receipt of the last reply from Appellant Diamond Z. That reply was received by the Hearing Officer on November 7, 2006.

The matter has been submitted and is therefore ready for decision.

B.

Statement of the issues

The primary issue in this case involves the question of whether or not the sale of assets from Weld Tech, Inc. to Diamond Z/Rule Steel/Rule Pacific constitutes a change in ownership, and if so, whether a change in ownership should require combining the Weld Tech, Inc.’s higher experience rating with that of the acquiring entity, Diamond Z/Rule Steel.

In this case, Weld Tech, Inc. which was previously owned by individuals unrelated to owners of Diamond Z and Rule Steel Tanks, apparently acquired a significant loss and therefore also had a significantly high, adverse experience rating. Diamond Z/Rule Steel has, at least from some time in 2003, contested whether or not their experience ratings should be adversely

affected by the high experience rating of Weld Tech, Inc.'s prior owners. As noted above, NCCI and the Review Committee affirmed the initial analysis which was to treat Weld Tech Inc.'s experience as being transferred to Diamond Z/Rule Steel and the various Daniel Rule entities as a consequence of Rule Steel's or Diamond Z's acquisitions or mergers.

C.

Background and summary of evidence

In addition to those matters of evidence that are summarized above in the statement of procedure, the Hearing Officer notes that NCCI and the Idaho Review Committee have used the following grounds for supporting use of Weld Tech's experience in calculating the experience rating of Diamond Z and Rule Steel Tanks. First, NCCI and the Committee both relied on Diamond Z/Rule Steel's acquisition of not only personal property but also "subject to goodwill," in determining that, in addition to the acquisition of personal property physical assets, Rule Steel Tank also "takes over the operations" of Weld Tech.

The deliberations of the Idaho Review Committee on June 22, 2006, also contain the following. The "Members determined that the purchase of goodwill indicates that Rule Steel Tanks was interested in continuing relationships with the same customers and vendors of the prior business [Weld Tech, Inc.]. In addition, the "members also stated that the process and hazards, both before and after the sale, remained similar."

In the evidence presented to the Review Committee, NCCI stated that because the sale between Weld Tech, Inc., and Rule Steel included Weld Tech's physical assets and goodwill, "This sale constitutes an ownership change, requiring the transfer of the seller's experience to the buyer."

Diamond Z/Rule Steel, during the June 22, 2006, Review Committee Proceeding, noted that Diamond Z/Rule Steel purchased only the physical assets of Weld Tech, Inc., and that it did not take over Weld Tech Inc.'s operations. Rule Steel did not request or receive a noncompetition clause, raising the inference or establishing the fact that Rule Steel Tanks had no intention of assuming Weld Tech, Inc.'s business operations. Further, Rule Steel stated that it did not take over Weld Tech's physical location, only a few former employees of Weld Tech were subsequently employed by Rule Steel Tanks, and after the asset purchase, the former owners of Weld Tech each started separate businesses. Rule Steel also noted that Weld Tech, Inc., did not cease to exist, as it was the payee of a note payable by Rule Steel nearly a year after the asset transfer. Finally, Rule Steel Tanks argues that because it had no control over the losses incurred by Weld Tech, Inc. it should not be held responsible for the experience rating caused by Weld Tech Inc.'s loss.

Diamond Z/Rule Steel Tanks provided the following documentary evidence in support of the instant Appeal.

Exhibit A. Contract of Sale of Personal Property between Weld Tech and Rule Steel.

Exhibit B. Idaho Workers Compensation Rating and Classification Review

Committee Agenda Summary Sheet (apparently the documentary summary of the parties' position for the June 22, 2006, Review Committee Hearing).

Exhibit C. Articles of Incorporation of KB Welding, Inc.

Exhibit D. Corporation Reinstatement Certificate for Pacific Metal Works.

Exhibit E. Promissory Note payable from Rule Steel Tanks to Weld Tech, Inc., dated December 28, 2001.

Exhibit F. Resignations of Kelly and Shawna Bartlett from Weld Tech, Inc., and

Statement of Change of Registered Agent for Weld Tech, Inc., showing the new registered agents as Shannon Taylor and Brent Taylor.

Exhibit G. Worker's compensation experience rating for Rule Pacific Corporation doing business as Weld Tech.

Exhibit H. Articles of Incorporation of Rule Pacific Corporation.

Exhibit I. Rule Steel Tanks Workers Compensation Insurance Proposal proposed by WorkCare Northwest, Inc., and McDonald InsurServ.

NCCI's documentary evidence in the current Appeal consisted of a 64-page Exhibit 1.

The Hearing Officer also treats as matters of record the July 7, 2005 and November 21, 2005, letter rulings from NCCI that were attached to the July 12, 2006, correspondence that initiated the instant Appeal.

These matters constitute the factual record in this Appeal and are all deemed admitted by stipulation or by failure to object.

The parties have not challenged whether the Experience Rating Plan Manual, cited below, does or does not apply to the issues in this Appeal, and therefore the Hearing Officer deems that, since both parties have quoted these Rules, both parties agree to be bound by the Experience Rating Plan Manual.

D.

Applicable laws and regulations

The rating plan manual rule which appears to have been in effect at the time of the transfer of the assets of Weld Tech, Inc., to one or more of the Rule Steel entities is as follows:

Experience Rating Plan Manual
Part 3, section B – Ownership Changes:

For purposes of this Plan a change in ownership includes any of the following:

- a. Sale, transfer, or conveyance of all or a portion of an entity's ownership interest.
- b. Sale, transfer, or conveyance of an entity's physical assets to another entity that takes over its operations.
- c. Merger or consolidation of two or more entities.
- d. Formation of a new entity subsequent to the dissolution or nonoperative capacity of an entity.
- e. Voluntary or Court-mandated establishment of a trustee or receiver, excluding a debtor in possession, a trustee under irrevocable trust or a franchisor.

1. Continuation of Experience

Unless excluded under Rule 2, the experience for any entity undergoing a change in ownership shall be transferred to the experience ratings of the acquiring, surviving or new entity.

As noted by Diamond Z/Rule Steel, the numbering of these rules changed sometime between 2005 and 2006. Therefore, for the purposes of this decision, the hearing officer notes and will cite the following additional, current, citations to the NCCI rating rules:

Rule 3.C.1 – Types of Ownership Changes.

- a. For purposes of this Plan a change in ownership includes any of the following:

- (2) Sale, transfer or conveyance of an entity's physical assets to another entity that takes over its operations.

Rule 3.E.1 – Transfer of Experience.

The experience for any entity undergoing a change in ownership will be retained or transferred to other experience ratings of the acquiring, surviving or new entity unless specifically excluded by this Plan.

Rule 3.E.2 – Exclusion of Experience.

The experience for any entity undergoing a change in ownership shall be excluded from future experience ratings only if each of the following conditions A, B, and C are met.

- a. The change must be a material change such that:
 - (I) The entire ownership interest after the change had no ownership interest before the change, or
 - (II) The collective ownership of all those having an interest in an entity both before the change and after the change amounts to either less than 1/3 ownership before the change or less than 1/2 ownership after the change.
- b. The material change in ownership is accompanied by a change in operations sufficient to result in reclassification of the governing classification.
- c. The material change in ownership is accompanied by a change in the process and hazard of the operations.

* * *

Class Code 3040 – Iron or Steel: Fabrication: Ironworks Shop – ornamental.

Code 3040 operations usually consist of the laying out of the various type stock size angles, bars, rods or sheets; the marking out of the pieces; and the cutting, sawing, drilling, punching, riveting, bolting or welding of the pieces into the desired nonstructural product.

* * *

Class Code 3066 – Sheet Metal Work – Shop.

Code 3066 is assigned to insureds engaged in operating a sheet metal shop wherein various products are manufactured from galvanized sheet metal or aluminum stock. The manufacturing is performed with such equipment as circular and square shears, breaks, rolls (both smooth and corrugating), punches, riveters, flangers, and perhaps some welding machines, both spot and continuous.

Former Rule 3.B.b. is now found in Rule 3.C.1.a(2). Former Rules 3.B.1 (Transfer of Experience rating) and 3.B.2 (Exclusion of Experience) now appear at Rule 3.E.1 and 3.E.2, respectively.

E.

Arguments of the parties and discussion

Diamond Z/Rule Steel argues that NCCI and the Review Committee failed in the initial application of Rule 3.C.1.a(2), in that there is no evidence that Diamond Z/Rule Steel took over

the seller's operations. Diamond Z/Rule Steel does not challenge that the contract of sale of personal property resulted in the sale, transfer, or conveyance of Weld Tech, Inc.'s, assets to Diamond Z/Rule Steel (or Rule Pacific Corporation, an entity owned and related through common ownership interest of Daniel Rule). However, Diamond Z/Rule Steel strenuously argues that Diamond Z/Rule Steel/Rule Pacific did not take over the operations of Weld Tech, Inc.

NCCI and the Review Committee rely on three factors in determining that Diamond Z/Rule Steel/Rule Pacific took over the operations of Weld Tech, Inc. These were, first, that Diamond Z purchased Weld Tech's goodwill; second, that Diamond Z "continued Code 3040 type operation" (November 21, 2005, Decision from NCCI); and third, that "the process and hazards, both before the sale and after the sale remain similar" (Committee Decision memorialized on July 7, 2006).

The Hearing Officer turns first to the question of whether purchase of goodwill allows for an inference that Diamond Z/Rule Steel carried on Weld Tech, Inc.'s operations. The Hearing Officer finds that there are no facts in this record that establish that the acquisition of goodwill, even with customer lists, demonstrates whether or not the prior asset owner's "operations" were carried on by the acquiring entity.

The Hearing Officer notes that goodwill is no more and no less than an expectation, as argued by Diamond Z/Rule Steel. This expectation does not demonstrate what the actual nature of the operations were, either before or after the effective date of the Contract of Sale of Personal Property in this matter. Accordingly, the Hearing Officer concludes that the inclusion of goodwill in the Contract of Sale of Personal Property between Weld Tech and Rule Steel does not constitute evidence that Diamond Z/Rule Steel constituted "another entity that takes over the

operations” of the selling entity. The Hearing Officer also agrees that absence of a non-competition clause in the purchase agreement negates the inference that sale of goodwill shows Diamond Z/Rule Steel’s continuation of operations of Weld Tech., Inc.

The references to “similar processes and hazards” and “continued Code 3040 type operations” apparently refer to whatever similarity may be found between Class Code 3040 and Class Code 3066.

In its argument, NCCI states, “Both Code 3040 and Code 3066 apply to metal working operations. Both classifications share common processes and hazards, such as the cutting, sawing, drilling, punching, riveting, bolting or welding of metal products.” However, the Hearing Officer notes that this is not, in fact, an accurate statement.

Of note, Code 3040 has to do with iron and steel fabrication for non-structural, ornamental purposes. Code 3066, on the other hand, is sheet metal shop work. The only items that share commonality in these two code classifications are punching, riveting, and welding of metal. Code 3066 does not mention cutting, sawing, drilling, or bolting, and does not include iron as a referenced metal. Thus, the Hearing Officer finds that, based on the evidence provided to the Hearing Officer, and also provided to NCCI and to the Review Committee, any so-called “similarity” of operations also fails to establish a basis for the transfer of Weld Tech, Inc.’s experience rating to Rule Pacific, Diamond Z, or Rule Steel Tanks. In short, the record supplied to both NCCI and the Committee (NCCI’s Exhibit 1 in this Appeal) fails to establish a similarity of operations between those carried on by Weld Tech, Inc., prior to the sale of its assets and those carried on by Diamond Z/Rule Steel after it acquired Weld Tech, Inc.’s assets.

The Hearing Officer does not find, as a matter of law or as a matter of fact, what the current nature of operations that Diamond Z/Rule Steel/Rule Pacific entities might be carrying

on as a consequence of their acquisition of the Weld Tech assets, simply because the record is devoid of such evidence. However, because the Hearing Officer cannot make such a determination, the Hearing Officer also must conclude that neither NCCI nor the Idaho Review Committee was in such a position, based on the record before them. In other words, there is simply a lack of *prima facie* or factual evidence, or evidence that would even allow for the drawing of an inference to suggest, that Weld Tech's operations were "taken over" by Diamond Z Manufacturing /Rule Steel Tanks/Rule Pacific. In the absence of both the asset acquisition and the "taking over of operations" of the asset seller, a "change in ownership" under Rule 3.C.1.a.(2) cannot be said to have occurred.

Accordingly, the Hearing Officer makes the following findings and enters the following conclusions.

F.

Findings of fact

1. The record before the NCCI and the Idaho Review Committee does not establish that Diamond Z/Rule Steel Tanks/Rule Pacific, constituted an "entity that takes over" the operations of another entity (Weld Tech, Inc.).

2. The evidence in the record in this Appeal is insufficient to establish that Diamond Z/Rule Steel/Rule Pacific's acquisition of goodwill of Weld Tech, Inc., demonstrates that Diamond Z took over Weld Tech, Inc.'s operations.

3. Rule 3.C.1.a.(2) requires, in order for NCCI or the Idaho Review Committee to establish a change in ownership, two things to occur: first, sale, transfer or conveyance of Weld Tech, Inc.'s physical assets, which everyone concedes occurred, and second, that another entity,

in this case Rule Steel Diamond Z, takes over its operations, as to which there is no evidence in the record.

4. As a consequence of the lack of evidence regarding whether or not Rule Steel/Diamond Z, the acquiring entity, took over Weld Tech's operations, the Hearing Officer finds, as a matter of fact that no "change in ownership" occurred as that term is defined under Rule 3.C.1.a.(2).

5. The Hearing Officer finds that, in the absence of facts establishing that a change in ownership occurred, it is not necessary to discuss Rule 3E1, transfer of experience, or Rule 3E2, exclusion of experience. For those Rules to come into effect, a change of ownership must occur, and as the Hearing Officer has previously found that "no change in ownership" occurred, the Hearing Officer also finds that no transfer of experience may be applied based on Weld Tech, Inc.'s, Inc. experience prior to the effective date of the Contract of Sale of Personal Property in December of 2001.

G.

Conclusions of law

1. No change in ownership occurred under Rating Plan Manual Rule 3.C.1.a.(2) occurred, because there is no evidence in the record that Diamond Z/Rule Steel was "another entity that takes over its [Weld Tech, Inc.'s] operations."

2. In the absence of any evidence to support a finding or conclusion that Diamond Z/Rule Steel took over the operations of Weld Tech, Inc., the Review Committee committed a clear error of law in finding that a change in ownership occurred, because a finding that taking over the operations of the asset seller is a necessary condition for concluding that a change in ownership occurred under Rating Plan Manual Rule 3.C.1.a.(2).

3. The Decision of the Review Committee, that Weld Tech, Inc.'s experience rating, arising out of activities prior to the date of the asset sale in December 2001, should become the experience rating for Diamond Z/Rule Steel, is REVERSED.

4. NCCI shall direct any insurer who relied on this erroneous and mistaken analysis of change in ownership to recalculate any and all premium that may have been based on said miscalculated and erroneous determination of change in ownership.

5. Pursuant to Rule 703 of the Attorney General's Rules of Administrative Procedure, the following statement must accompany this Preliminary Decision.

a. This is a preliminary order of the hearing officer. It can and will become final without further action of the agency unless any party petitions for reconsideration before the hearing officer issuing it or appeals to the hearing officer's superiors in the agency. Any party may file a motion for reconsideration of this preliminary order with the hearing officer issuing the order within fourteen (14) days of the service date of this order. The hearing officer issuing this order will dispose of the petition for reconsideration within twenty-one (21) days of its receipt, or the petition will be considered denied by operation of law. See Section 67-5243(3), Idaho Code.

b. Within fourteen (14) days after (a) the service date of this preliminary order, (b) the service date of the denial of a petition for reconsideration from this preliminary order, or (c) the failure within twenty-one (21) days to grant or deny a petition for reconsideration from this preliminary order, any party may in writing appeal or take exceptions to any part of the preliminary order and file briefs in support of the party's position on any issue in the proceeding to the agency head (or designee of the agency head). Otherwise, this preliminary order will become a final order of the agency.

c. If any party appeals or takes exceptions to this preliminary order, opposing parties shall have twenty-one (21) days to respond to any party's appeal within the agency. Written briefs in support of or taking exceptions to the preliminary order shall be filed with the agency head (or designee). The agency head (or designee) may review the preliminary order on its own motion.

d. If the agency head (or designee) grants a petition to review the preliminary order, the agency head (or designee) shall allow all parties an opportunity to file briefs in support of or taking exceptions to the preliminary order and may schedule oral argument in the matter before issuing a final order. The agency head (or designee) will issue a final order within fifty-six (56) days of receipt of the written briefs or oral argument, whichever is later, unless waived by the parties or for good cause shown. The agency head (or designee) may remand the matter for further evidentiary hearings if further factual development of the record is necessary before issuing a final order.

e. Pursuant to Sections 67-5270 and 67-5272, Idaho Code, if this preliminary order becomes final, any party aggrieved by the final order or orders previously issued in this case may appeal the final order and all previously issued orders in this case to district court by filing a petition in the district court of the county in which: (7-1-93)

i. A hearing was held,

ii. The final agency action was taken,

iii. The party seeking review of the order resides, or operates its principal place of business in Idaho, or

iv. The real property or personal property that was the subject of the agency action is located.


f. This appeal must be filed within twenty-eight (28) days of this preliminary order becoming final. See Section 67-5273, Idaho Code. The filing of an appeal to district court does not itself stay the effectiveness or enforcement of the order under appeal.

Any Petition to Review this Preliminary Order should be addressed to:

Department of Insurance
700 West State Street
P.O. Box 83720, Boise, ID 83720-0043
Phone: (208) 334-4210
FAX: (208) 334-4298

A request for reconsideration may be mailed or delivered, in writing, but not via facsimile, to the address of the Hearing officer noted on the front page of this Decision.

IT IS SO ORDERED: November 16, 2007.


STEPHEN J. LORD, Attorney at Law
Hearing Officer

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I forwarded by the method stated below a true and correct copy of the foregoing Findings of Fact, Conclusions of Law, Decision and Preliminary Order on November 16, 2007.

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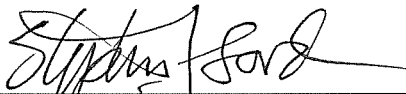
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And the original mailed on the same date to the Department to the attention of:

Assistant to the Director
Idaho Department of Insurance
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With a courtesy copy to:

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Stephen J. Lord