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STATE OF ALASKA  
DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT  
BEFORE THE DIVISION OF INSURANCE

In the Matter of )  
)  
**Arthur's Trucking/Royal Contractors, Inc.,** )  
Applicant/Appellant. )  
)  
)  
)

Case No. **H97-01**

**Order**

The Director of the Division of Insurance, having reviewed the Proposed Decision of the Hearing Officer in Case No. H97-01 in the matter of Arthur's Trucking and Royal Contractors Inc., hereby adopts the following as the decision of the Director:

**Findings of Fact and Conclusions of the Director**

This case is a consolidated appeal under AS 21.39.090 and 21.39.100 by two insureds challenging a workers compensation insurance rating code classification applied to them. The insureds are Arthur's Trucking (Arthur's), a sole proprietorship owned and operated by Tony Arthur, and Royal Contractors, Inc. (Royal), a corporation wholly owned and operated by Brett King. They appeal a decision of the National Council on Compensation

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1 Insurance, Inc. (NCCI) to classify Arthur's and Royal as code 7219 (Trucking  
2 NOC) rather than code 4000 (Sand or Gravel Digging and Drivers).

3 A public hearing was held in Anchorage on November 5, 1997.  
4 NCCI was represented by Attorney Clay Young. Broker Gordon Depue  
5 represented the Appellants. At the hearing, testimony was taken from Mr.  
6 Arthur, Mr. King, Mr. Depue, and Tim Hughes with NCCI. The record  
7 includes exhibits submitted at and after the hearing. A proposed decision  
8 was submitted to the director by hearing officer David Stebing on December 4,  
9 1997.  
10

11 Issues

- 12 1. Did NCCI correctly classify the Appellants as Code 7219?  
13  
14 2. Does the reclassification procedure used in these cases violate  
15 provisions of AS 21.39?

16 Findings of Fact

17 There are no material factual disputes in this case. The  
18 undisputed facts on which this decision is based are:

- 19 1. Arthur's and Royal sought workers compensation insurance in 1996  
20 through their broker Gordon Depue.  
21  
22 2. Arthur's is a sole proprietorship trucking business owned and  
23 operated by Tony Arthur and primarily engaged in the hauling of sand and  
24 gravel. Mr. Arthur has owned and operated a gravel pit since 1995 from  
25 which he occasionally extracted and hauled sand and gravel on his own  
26

1 property using his truck. Nearly all of his business involves hauling sand and  
2 gravel from pits owned by someone else to building sites or private road jobs.  
3 Usually, Mr. Arthur is told where to get the sand and gravel, and all he has to  
4 do is haul it. Sometimes as part of his business, Mr. Arthur has participated  
5 in operating gravel pits owned by others by using equipment necessary to load  
6 his trucks. (Exhibit E, pp. 6-7, 13, 15-19, 22, 30-33).

7  
8 3. At various times in the past, Arthur's was classified with code 4000  
9 for workers compensation insurance. (Exhibit E, pp. 24-26).

10 4. Brett King is 100 percent owner and operator of Royal, a trucking  
11 business incorporated in 1993 that uses leased trucks and that primarily hauls  
12 coal, sand and gravel. Royal owns sand and gravel pits. Most of its contracts  
13 involve hauling sand and gravel for private construction jobs and for highway  
14 work under bid. Royal uses its own pits as well as pits owned by others for  
15 its hauling contracts. (Exhibit D, pp. 6-8, 10-11, 13-17).

16  
17 5. At various times in the past, Royal's sand and gravel activities were  
18 classified with code 4000 for workers compensation insurance. (Exhibit D, pp.  
19 28, 32, 36).

20  
21 6. NCCI's Basic Manual provides that "it is the business of the  
22 employer within a state that is classified, not the separate employments,  
23 occupations, or operations within the business." (Exhibit B, p. R9).

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7. The R & A committee recommended that both businesses be classified as code 7219 (Trucking NOC) as opposed to code 4000 (Sand or Gravel Digging and Drivers). Both businesses appealed the decision.

8. By letter dated May 20, 1997, NCCI issued its determination advising Arthur's and Royal through their broker Gordon Depue that their sand and gravel hauling activities were classified with code 7219. (Exhibit 21). Both businesses sought a hearing through an appeal to the Director.

Discussion

In alleging that NCCI has improperly classified his clients, Mr. Depue made the following arguments:

1. Who owns the dirt (sand and gravel) should not be the sole criterion for classification.
2. NCCI is engaged in discrimination and harassment of small businesses through classifying businesses as code 7219 as opposed to code 4000.
3. Credibility of rates is impaired through NCCI essentially taking the "cream" of the code 4000 risks, with excellent claim experience, and transferring them to code 7219.
4. Small businesses like his clients cannot operate in the environment NCCI has created where there is uncertainty that the classification code will not be changed after the contracts have been bid and work performed, resulting in a higher insurance rate and significantly increased costs.

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5. NCCI should be directed to cease and desist from making rate classification decisions based upon who owns the dirt, and NCCI should be enjoined from continuing harassment of small businesses through repetitive classification inspections.

Mr. Arthur also testified, making the following arguments: A small businessman should be able to know what the insurance rate is "going in." NCCI should not be able to change the classification after it is initially chosen, resulting in the insured business losing money. The audit should be conducted "up front." Small businessmen cannot live with this re-classification system. An audit resulting in a reclassification after a contract has been performed "can break a guy" and "can be the difference between your profit and your loss." (Hearing tape 1, side B; Exhibit E, pp. 28, 35-36).

The director has considered these arguments. As recommended by the hearing officer, the director concludes that classification 7219 is correct, based on the description of the category in the Scopes Manual, and that the reclassification procedure does not violate AS 21.39. These conclusions are discussed in more detail below. The director also adopts the hearing officer's conclusion that the classification is not based on ownership of the dirt, and that there is no evidence in the record of harassment of small businessmen by the NCCI.

1. The Classification as Code 7219 Is Supported by the Nature of the Businesses.

1 The Basic Manual allows classification of risk based upon "the  
2 business of the employer." (Exhibit B, p. R9). Mr. Depue acknowledged at the  
3 hearing that the main business of the company generates the class code.  
4 (Exhibit F, p. 45).

5 In this case, trucking-related businesses are being classified. The  
6 Scopes Manual describes the two classifications at issue. Pertinent provisions  
7 are stated below:

9 **4000 PHRASEOLOGY SAND OR GRAVEL DIGGING & DRIVERS.**  
10 Includes construction, repair or maintenance of all buildings, structures  
11 or equipment and the installation of machinery. No canal, sewer or cellar  
12 excavation or underground mining. . . .

13 **SCOPE** Code 4000 is applied to risks engaged in digging or  
14 dredging of sand or gravel. The material is excavated from surface pits  
15 with mechanical equipment such as power shovels, drag lines, clamshell  
16 diggers or cranes, or obtained from non-navigable waters by means of  
17 hydraulic dredges, clamshell dredges, etc. The sand is then conveyed  
18 from the bank, pit or dredge to hoppers, by trucks, belt conveyors, narrow  
19 gauge railroads, or pipelines. It is then washed, graded, screened and  
20 stored in bins, hoppers or piles for delivery by truck or rail to customers.

21 **7219 PHRASEOLOGY TRUCKING: NOC -- ALL EMPLOYEES AND  
22 DRIVERS.**

23 Storage warehouse employees to be separately rated. . . .

24 **SCOPE** Code 7219 is applied to insureds engaged in the hauling of  
25 general merchandise under contract for one or more individuals or  
26 concerns provided such operations are not otherwise classified in the  
manual. . . .

Trucking concerns usually maintain terminals, central  
loading platforms or a temporary storage depot where merchandise is  
stored for a short period pending transfer to another destination.  
Platform persons engaged in loading or unloading merchandise as well as  
miscellaneous employees such as terminal employees, garage employees  
and repairers are considered to be an integral part of trucking operations  
and are assigned to Code 7219. . . .



1 p. 33). Therefore, it was not error for the R & A committee and NCCI to  
2 classify the subject businesses with code 7219 as opposed to code 4000.

3 2. The Reclassification Procedure Does Not Violate the Law.

4 There is no dispute that both Arthur's and Royal have been  
5 classified with code 4000 at various times in the past. (Hearing tape 1, side B;  
6 Exhibits 2, 6). Arthur's and Royal argued that reclassification could cause a  
7 hardship for business operators who plan for known expenses in bidding on a  
8 contract, and then are faced with a significant increase in insurance premiums  
9 later, possibly even at the end of the contract. The appellants argued that  
10 increased premiums can virtually wipe out the profits. (Exhibit D, pp. 11, 36-  
11 38; Exhibit F, p. 27).

12  
13 The director acknowledges that a hardship could possibly occur  
14 under such circumstances, but the facts set out by the hearing officer in this  
15 case do not show whether Arthur's or Royal in fact suffered such a hardship  
16 from the reclassification. The Director concludes that the reclassification  
17 procedure provided for in the NCCI Manual does not violate AS 21.39. The  
18 reclassification provision reasonably balances the interests of insurers and  
19 insureds, recognizes that changes in operations may occur and therefore  
20 promotes rates that are appropriate and adequate, but not excessive.

21  
22 The Basic Manual's provision for reclassification is as follows:  
23 **Rule IV(G). Changes or Corrections in Classifications**

24 **1. Changes in Classifications**

25 Changes in classifications due to changes in insured's  
26 operations will be applied pro rata as of the date of change in insured's  
operations.

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**2. Corrections in Classifications**

Corrections in classifications that result in a decrease in premium, whether determined during the life of the policy or upon audit, shall be applied retroactive to the inception of the policy. Corrections in classifications that result in an increase in premium shall be applied as follows:

The effective date of a change for purposes of the time periods in a., b., and c. below is the date a carrier determines that it is necessary to effect a classification(s) change.

a. During the first 120 days of the coverage term, retroactively to the inception of the coverage.

b. After the first 120 days of the coverage term, but before the final 90 days, pro rata as of the date the company discovers the cause for such change.

c. During the last 90 days of the coverage, corrections in classifications will not be effected except upon a renewal policy, if any.

**3. Misrepresentations or Omissions**

Notwithstanding anything above to the contrary, any correction in classifications arising from discovery of a misrepresentation or omission by the insured, its agent, employees, officers or directors, shall be applied pro rata from the date upon which it would have applied had such misrepresentation or omission not been made.

See Exhibit B, Rule IV(G), p. R18 (emphasis added).

It is axiomatic that, if an insured obtains insurance at a lower rate than that to which it is entitled, the fundamental insurance principle of risk sharing has failed because other insureds then bear a disproportionate expense. The practical need expressed by Mr. Arthur "to establish one rate, going in, stick with it, all the way through" (Hearing tape 1, side B) must be balanced against the need of the insurer to receive adequate rates for the risk insured against. Businesses are not always accurate, whether accidentally or intentionally, in the way they describe their activities when applying for insurance. Further, businesses may change operations in response to market conditions or business opportunities that may arise during the policy period.

1 For these reasons, there is a need for mechanisms to verify that an insured is  
2 correctly classified. Payroll audits after the commencement of insurance  
3 coverage are a customary practice with workers compensation insurance  
4 because premium charges are made against payroll, which is unknown until  
5 after the year is complete. See Larson, infra, § 92.65. Audits protect the  
6 public interest by allowing for correction of the classification of a business as  
7 well as for correction of inaccurate payroll projections.

8  
9 The Basic Manual provision set out above promotes accurate  
10 rates by permitting corrections to the classification of a business if it is  
11 discovered to be inaccurate or not reflective of actual operations. Rule IV(G)(b)  
12 covers corrections that do not result from omissions or misrepresentations by  
13 the insured. Where the result of a correction in category is to decrease the  
14 applicable premium, the insured is entitled to a full refund because the correct  
15 rate is applied retroactively from the beginning of the coverage. Where the  
16 result is an increase in premium, the hardship to the insured is tempered by  
17 the allocation provisions in this Rule, so that, if an insured is locked into a bid  
18 price on a lengthy contract, the higher rates will not apply for the full period.  
19 This provision does not fully avoid, but somewhat mitigates, any hardship  
20 from reclassification. To the extent an insured remains liable for higher  
21 premiums after reclassification, this should be a factor motivating an insured  
22 to provide fully accurate information to assure correct classification in the first  
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1 place and to keep the insurer informed of any changes in projected payroll  
2 and/or operations.

3 Appellants argue that NCCI should follow the practice in other  
4 states and create a new classification code for "short haul trucking." The  
5 NCCI has an opportunity to consider this argument, along with appropriate  
6 data and actuarial expertise as it updates the Scopes Manual twice a year.  
7 (Exhibit C, preface). However, in this proceeding, on this record, the Director  
8 will not require such a change.  
9

10 **Conclusion**

11 For the reasons set out herein, the Director affirms the final  
12 decision of the NCCI that appellants Arthur's Trucking and Royal Contractors,  
13 Inc. should be classified as code 7219.  
14

15  
16 Dated: January 28, 1998

  
Marianne K. Burke, Director  
Division of Insurance

