

Northwest Wall & Ceiling Contractors Association

RETROSPECTIVE RATINGS

Relief from retrospective rating assessment

The Department is under no duty to investigate or inform a retrospective rating group of possible consequences related to the group's plan, membership, or other decisions. The Department is not a guarantor of automatic refunds to a retrospective rating group. The participation in the retro group is voluntary and involves risk.***In re Northwest Wall & Ceiling Contractors Ass'n, BIA Dec., 09 14561 (2010)*** [Editor's Note: The Board's decision was appealed to superior court under Thurston County Cause No. 08-2-00959-6.]

Scroll down for order.

1 Our industrial appeals judge has summarized the evidence relevant to this appeal in the
2 Proposed Decision and Order. We expand on that summary only to the extent necessary to explain
3 our decision.

4 As this Board has observed, retrospective ratings groups are authorized and governed by
5 the provisions of Chapter 51.18 RCW and by the provisions of Chapter 296-17 WAC, beginning
6 with WAC 296-17-90401. In general, retrospective rating is an incentive program, voluntarily joined
7 by individual qualified employers and qualified groups of employers. Retrospective rating groups
8 must be made up of employer members engaged in substantially similar business operations,
9 considering the nature of the services or work activities performed. Retrospective rating groups
10 select options with varying caps on the amount of risk they are willing and able to take. The terms
11 of the relationship among the participants within a retrospective rating group are determined by the
12 rating group, not the Department.

13 Retrospective rating involves a process wherein the Department of Labor and Industries
14 retrospectively examines premiums paid by the participating employer or employer group for three
15 past rating years at issue, comparing premiums paid with losses incurred and anticipated due to
16 industrial injury and occupational disease claims arising and assigned to participating employer
17 accounts in the rating years at issue. Liability for a given fiscal year is not fully determined until the
18 third and final adjustment relative to and following the year in which the industrial injury occurred or
19 in which the occupational disease was diagnosed. Based on formulas applied, a premium rebate
20 (refund) may be provided, or an additional assessment (penalty) may be assessed. Whether a
21 retrospective rated employer or group receives a rebate or incurs an additional assessment
22 depends substantially upon the premium:loss ratio for the three rating years in question.
23 Retrospective rating groups thus assume a significant level of risk, up to the plan cap, or stop loss
24 level, which reflects the level of risk that the group is willing to accept.

25 The premium side of a retrospective rating group's ratio is comprised by the group
26 membership in terms of the totality of premiums paid by the group's employer members for hours in
27 the respective risk/rate job classifications. To reduce losses, a retrospective rating group can
28 promote safety, monitor and intervene in claims at the Department, and promote early return to
29 work and other programs that minimize claim costs.

30 In the early 1990s, the drywall industry in Washington was in a state of turmoil with respect
31 to ever-increasing industrial insurance premiums. The turmoil was widely believed to be due to the
32 failure of many drywall contractors to accurately report the number of hours being worked by

1 employees, a failure that allowed dishonest contractors to pay less in premiums than honest
2 contractors and for the dishonest contractors to have a considerable competitive advantage in
3 bidding new jobs. Although some hyperbole may have been involved, anecdotal reports suggested
4 that one-half to two-thirds of all drywall work was either under-reported or not reported at all.
5 Honest contractors, who were indirectly paying the claim costs for dishonest contractors, demanded
6 change.

7 In response, the Department of Labor and Industries met with industry representatives in a
8 program that came to be known as The Drywall Initiative. NWCCA was represented in the Drywall
9 Initiative by the Drywall Technical Advisory Committee. After much discussion and a lengthy
10 comment period, new rules were adopted that abandoned the hourly basis for reporting industrial
11 insurance premiums, focusing instead on the number of square feet of drywall that went into a
12 given job. Essentially, the more drywall that was installed on a job, the greater the total industrial
13 insurance premium that would be owed by the contractor, regardless of how many employee hours
14 were allegedly involved with the installation. One advantage to using the square foot method was
15 that drywall suppliers were a fairly reliable source as to how much drywall was being installed, the
16 implication being that suppliers prepared an invoice or similar documentation as to how much
17 drywall was delivered to a particular job for a particular contractor. The change in rules went into
18 effect on January 1, 1997.

19 The problem with converting to the square foot method of reporting is that there was no way
20 to precisely convert hours-worked to square-feet-of-drywall. Because of this problem, the
21 Department was necessarily forced to engage in a bit of educated guessing. The Department
22 estimated the amount of reportable drywall that had been sold in the state the previous year and
23 divided by the total premium amount the Department anticipated would be needed to cover claims,
24 yielding a premium/square-foot for the future year that was thought to be adequate. Given that the
25 Department was estimating, two related points deserve consideration. First, it was difficult for the
26 Department's estimate to be informed by its actuaries. Actuaries look back in time, using three to
27 five years of data to mathematically predict the future. Given that a new measuring standard had
28 been adopted, no such data was available. Second, the Department's estimate may have
29 influenced, however subtly, by industry representatives who were interested in seeing that
30 premiums were kept as low as reasonably possible. Ultimately, the Department decided to adopt a
31 conversion factor of 1-hour's-work = 125 sq. ft-of-installed-drywall.

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1 In addition to estimating future drywall premiums, the Department and industry
2 representatives made three assumptions that no one seemed to question. It was believed that the
3 newly adopted rules would result in dramatically increased industrial insurance reporting by drywall
4 contractors. Given the difficulty that a contractor would have in denying that a certain amount of
5 work had been performed, it was assumed that (1) there would be full compliance from drywall
6 employers; (2) the reporting would be accurate; and (3) a larger pool of premium dollars would be
7 collected.

8 Acting on the assumption that more premium dollars would be forthcoming, the Department
9 established a base rate paid by all contractors and went a step further, offering employers
10 discounts if they met new, more rigorous reporting requirements. It appeared that contractors who
11 had previously failed to report hours would finally be held accountable.

12 Unfortunately, the assumptions proved to be overly optimistic. Over a period of several
13 years, and with the benefit of experience, it was learned that reporting improved, but only
14 incrementally. Apparently, disreputable contractors found new ways to avoid premium obligations
15 and it gradually became apparent that there may not have been as many dishonest contractors as
16 first thought. Perhaps anecdotal reports of widespread abuse by non-compliant drywall employers
17 were overstated. Whatever the reason, the premium pool did not dramatically increase. At the
18 same time, claims costs continued to rise. The premiums paid by NWCCA members for the plan
19 years of 1998 and 2000 proved to be too low when compared with claim costs. Ultimately, this
20 imbalance gave rise to the retrospective assessments at issue here.

21 NWCCA alleges that the Department knew, or should have known, to charge higher
22 premiums in 1998 and 2000 such that retrospective assessments would not have been necessary.
23 Obviously, this allegation benefits from a decade of hindsight and ignores both the purpose of the
24 Drywall Initiative and the fact that employers impact claim costs positively and negatively by their
25 behavior. Employers who are lax with respect to monitoring workplace safety, efficient claims
26 administration, and early return to work opportunities can reasonably expect higher claims costs.
27 Similarly, it can be difficult for the Department to predict how vigorously drywall employers will
28 pursue safety and efficiency. As Robert Malooly, assistant director of insurance services for the
29 Department, testified, determining rate adequacy is like predicting the outcome of the Kentucky
30 Derby in advance.

31 NWCCA argues that the Department failed to warn drywall employers that participation in the
32 Drywall Initiative would make participation in a retrospective rating program more risky. This

1 assumes that the Department knew from inception that the Drywall Initiative was ill-considered.
2 There is no evidence to that effect. To the contrary, the Drywall Initiative appears to have been a
3 reasonable and prudent response to industry complaints of significant non-compliance by many
4 drywall employers.

5 NWCCA's suggests liability for the assessment lies with the Department and that NWCCA
6 had no responsibility for reasoning through its decision to participate in a retrospective rating plan.
7 This is largely unpersuasive. The Department was not and is not a guarantor of automatic annual
8 refunds to a retrospective rating group. Participation in a retrospective rating program is voluntary.
9 RCW 51.18.010(1)(a). It involves risk. Participating employers choose the amount of risk they are
10 willing to assume. More to the point, an employer may protect itself from liability by declining to join
11 a retrospective rating group altogether, thereby placing the risk for industrial insurance losses in the
12 hands of the Department of Labor and Industries.

13 Nothing in the evidence before us convinces us that the change in the basic reporting unit
14 (from hourly to square foot) was unknown or unexpected by NWCCA and its constituent members.
15 Had NWCCA applied sufficient interest and resources, it could have predicted the impact upon the
16 group and its members. Collectively, NWCCA members contributed millions of dollars in premiums
17 during the years in question and contemplated hundreds of thousands of dollars in potential refunds
18 or assessments. Through its own efforts, it could have forecast the consequences of the change
19 for its members and the group's success or liability.

20 NWCCA suggests that the Board should apply equitable principles used in the law of
21 contracts, including insurance contracts, in order to provide relief here, arguing that the Department
22 had superior ability to forecast the adequacy of premiums for plan years 1998 and 2000. Because
23 it did not advise NWCCA members of the potential of increased risk, the Department was negligent
24 in meeting its contractual obligations and the retrospective rating agreement should be reformed or
25 rescinded under equitable principles. It is questionable, however, whether contract law
26 appropriately applies in the manner suggested by NWCCA. As we noted in *In re Contractors'*
27 *Alliance*, Docket No. 05 22737 (September 26, 2007), the retrospective rating program is governed
28 by statute and by adopted Washington Administrative Code provisions. Although it is true that an
29 agreement is made by the retrospective rating group to do certain things as a condition of
30 retrospective program participation, the terms of the program are governed by the statute and code
31 provisions. This Board declines to invalidate those provisions. In light of the fact that the code
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1 provisions, when applied to the facts of this case, direct the retrospective rating results, NWCCA
2 has failed to show how the Board may provide relief without invalidating the code provisions.

3 Finally, NWCCA argues that the Department of Labor and Industries failed to follow
4 recognized insurance principles as mandated by RCW 51.18.010(2), claiming the Department failed
5 to set rates based on the best data available at the time it set those rates. In making this argument,
6 however, NWCCA ignores the point that actuarial data requires a period of at least three years of
7 experience, and preferably five, to be sufficiently mature to be reliable. Had there been no change
8 in the basic reporting unit, NWCCA's argument would have considerable weight, but that is not the
9 case. It also bears mentioning that liability for a given plan year is not fully determined until the
10 third and final adjustment following the year in which the industrial injury occurred or in which the
11 occupational disease was diagnosed.

12 In sum, NWCCA has not identified, in statutory or regulatory law, any Department duty to
13 investigate and inform NWCCA or its members of the possible consequences of properly adopted
14 rules relative to NWCCA's plan choices, membership choices, or other NWCCA decisions. It has
15 not shown how the Department's action, or lack of action, rose to the level of breaching any duty.
16 In short, it has not shown why NWCCA members should be relieved of retrospective assessments
17 that are otherwise authorized by law. The Department order under appeal is affirmed.

18 **FINDINGS OF FACT**

- 19 1. The Department of Labor and Industries issued a rate notice to the
20 Retrospective Rating Group, Northwest Wall and Ceiling Contractors
21 Association (NWCCA). On February 27, 2006, NWCCA protested the
22 Department's rate notice and requested relief from the Department's
23 final adjustment for the Retrospective Rating Program plan years
24 beginning on July 1, 1998; July 1, 1999; and July 1, 2000.

25 On June 13, 2006, the Department issued an order in which it
26 determined that it could not reconsider plan years beginning on July 1,
27 1998, 1999, and 2000 because a protest was not received within the
28 30-day time limitation, and therefore those determinations regarding the
29 Retrospective Rating Program plan years were final and binding. On
30 July 14, 2006, NWCCA appealed the Department's June 13, 2006 order.
31 On July 26, 2006, the Board granted NWCCA's appeal and assigned it
32 Docket No. 06 17036.

Following a formal hearing, a Proposed Decision and Order was issued
on March 22, 2007, in which the industrial appeals judge determined
that NWCCA's protest was not timely filed. On January 8, 2008, the
Proposed Decision and Order was reissued to NWCCA upon the
Retrospective Rating Group's showing that it did not receive the Board's
March 22, 2007 Proposed Decision and Order. On April 1, 2008, the

1 Board issued a Decision and Order in which it determined that
2 NWCCA's protest was not timely filed. On April 23, 2008, NWCCA
3 appealed the Board's April 1, 2008 Decision and Order in Thurston
4 County Superior Court. On November 21, 2008, the Superior Court
5 issued an order in which it reversed the Board's April 1, 2008 Decision
6 and Order and remanded the matter to the Department for consideration
7 on the merits.

8 On March 4, 2009, the Department issued an order in which it denied
9 NWCCA's request for relief on the basis that the plan for years
10 beginning on July 1, 1998, 1999, and 2000, the Retrospective Rating
11 Group's members paid standard premium rates set in accordance with
12 Department rules. The Department used base rates set by rule, and for
13 calendar years 1998 through 2001, the Department set base rates using
14 the best information available at the time. On March 5, 2009, the
15 Department issued an order that was identical to its order dated
16 March 4, 2009.

17 On March 25, 2009, NWCCA protested the Department's March 4, 2009
18 order. On April 9, 2009, the Department issued an order in which it
19 affirmed its March 4, 2009 order. On May 4, 2009, NWCCA appealed
20 the Department's April 9, 2009 order. On June 2, 2009, the Board
21 granted NWCCA's appeal under Docket No. 09 14561.

- 22 2. NWCCA was an organization comprised of drywall contractors and was
23 an active participant in the Department's retrospective rating program for
24 several years, including plan years 1998, 1999, and 2000.
- 25 3. NWCCA's retrospective rating plan years began July 1 of each year and
26 ended on June 30 of the following year.
- 27 4. From 1993 to 1997, industrial insurance premiums for drywall employers
28 in Washington State increased significantly, due in part to non-compliant
29 drywall contractors failing to report worker hours and pay industrial
30 insurance premiums related to those hours.
- 31 5. By failing to report hours, non-compliant contractors obtained a
32 significant competitive advantage over compliant contractors who
correctly reported.
6. During the mid-1990s, the Department and drywall industry
representatives worked to address the problem of non-compliant
employers. The program that followed became known as the Drywall
Initiative.
7. During the mid-1990s, NWCCA was represented on the Drywall
Technical Advisory Committee by Richard Mettler.
8. Prior to January 1, 1997, industrial insurance premiums for drywall
contractors were based on the number of hours worked by employees.
9. The Drywall Technical Advisory Committee recommended to the
Department that it change its rate structure from one that was based on
hours worked to one based on square feet of drywall material installed.

- 1 10. Pursuant to its statutory rule-making authority, the Department
2 conducted public hearings to discuss the Drywall Initiative and the
3 proposal to change to square foot reporting.
- 4 11. On January 1, 1997, the Department implemented the provisions of the
5 Drywall Initiative, changing the method of calculating drywall premiums
6 from one unit of measurement (hours worked) to another unit of
7 measurement (square feet of drywall). The Drywall Initiative introduced
8 discounts for compliant contractors who completed new, more stringent
9 documentation requirements.
- 10 12. Contemporaneous with the change in the unit of measurement, the
11 Department adopted 1 hour of work as being the equivalent of
12 125 square feet of drywall (1 hour = 125 square feet).
- 13 13. Following the change in the reporting unit of measurement, the
14 Department began to develop new actuarial data.
- 15 14. The Department requires three to five years of accumulated data to
16 make statistically reliable predictions.
- 17 15. Industrial insurance claims may remain open for several years. Liability
18 for a given plan year is not fully determined until the third and final
19 adjustment following the year in which an industrial injury occurred or in
20 which an occupational disease was diagnosed.
- 21 16. The employer, not the Department, controls work place safety, the work
22 environment, and the activities of workers at a given job site.
- 23 17. Retrospective rating group employers can minimize claim costs by
24 promoting workplace safety, monitoring claims at the Department, and
25 providing early return-to-work opportunities for injured workers, among
26 other things. By minimizing claim costs, retrospective rating group
27 employers can earn refunds.
- 28 18. Retrospective rating group employers that fail to promote work place
29 safety, monitor claims, and provide return-to-work opportunities may
30 incur higher claim costs and be assessed additional premiums.
- 31 19. NWCCA's participation in the retrospective rating program was
32 voluntary.
20. NWCCA was aware that the retrospective rating program involved risk.
21. For plan years 1998, 1999, and 2000, NWCCA and its constituent
members selected the amount of risk they were willing to undertake.
22. For plan years 1998, 1999, and 2000, NWCCA members paid standard
premium rates set in accordance with Department rules. The
Department used base rates set by rule, and used the best information
available at the time.
23. With respect to plan year 1998, NWCCA's claims costs exceeded
premiums, resulting in a retrospective **assessment** against NWCCA in
the amount of \$735,149.

- 1 24. With respect to plan year 1999, NWCCA's claims costs were less than
2 premiums, resulting in a **refund** of premium to NWCCA in the amount of
3 \$433,843.
4 25. With respect to plan year 2000, NWCCA's claim costs exceeded
5 premiums, resulting in a retrospective **assessment** against NWCCA in
6 the amount of \$309,528.

7 **CONCLUSIONS OF LAW**

- 8 1. The Board of Industrial Insurance Appeals has jurisdiction over the
9 parties and subject matter of this appeal.
10 2. For the plan years beginning July 1, 1998; July 1, 1999; and July 1,
11 2000, NWCCA members paid standard premiums at rates set in
12 accordance with Department rules. The Department used base rates
13 set by rules in accordance with RCW 51.18.010.
14 3. For the plan years at issue, the Department set base rates using the
15 best information available at the time in keeping with RCW 51.18.010.
16 4. The order of the Department of Labor and Industries dated April 9, 2009,
17 is correct and is **AFFIRMED**.

18 Dated: June 16, 2010.

19 BOARD OF INDUSTRIAL INSURANCE APPEALS

20 /s/ _____
21 DAVID E. THREEEDY Chairperson

22 /s/ _____
23 FRANK E. FENNERTY, JR. Member

24 /s/ _____
25 LARRY DITTMAN Member