# STATE OF CALIFORNIA
# DEPARTMENT OF INSURANCE
## S A N  F R A N C I S C O

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| In the Matter of the Appeal of<br><br>DIAMONDBACK ENTERPRISES, INC., et al,<br><br>Appellant.<br><br>From a Decision of<br>THE WORKERS' COMPENSATION INSURANCE RATING BUREAU OF CALIFORNIA,<br><br>Respondent. | DECISION<br><br>File No. SF 6960-R-82 |

FACTS

1. The Appellants were fully insured for their workers' compensation liability during all times pertinent to this appeal.

2. Respondent, the Workers' Compensation Insurance Rating Bureau of California ("Bureau") is a rating organization licensed pursuant to the provisions of California Insurance Code Section 11750, et seq.

3. In December 1983, employees of Automated Farm Systems ("AFS") formed CHOP, a holding company, to purchase the outstanding shares of AFS.

4. By July 1985, CHOP was owned 50% by Ron Poulton, and 50% by Larry Ostrom.

5. AFS, a CHOP subsidiary, merged with Donald Wilson Irrigation Systems ("DWIS") with the latter the survivor, which remained a subsidiary of CHOP.

6. In September 1986, Poulton redeemed his stock, leaving Ostrom the sole shareholder of CHOP.

7. In July 1985, Ostrom and Poulton formed Diamondback Enterprises, which purchased certain operations (assets and liabilities) of CHOP.

8. In March 1987, Ostrom became 100% shareholder of Diamondback.

9. In July 1987, CHOP and DWIS filed for Chapter 11 Bankruptcy, with CHOP being subsequently dismissed from the proceedings as superfluous.

10. The Bureau used the combined experience of CHOP and DWIS in computing the experience rating for Diamondback for the policy years 1986 and 1987.

11. Diamondback appealed the Bureau staff Decision to the Classification and Rating Committee of the Bureau, which sustained the staff decision. Subsequently, Appellants took an appeal to Insurance Commissioner pursuant to Insurance Code Section 11753.1.

Appellant contends the Bureau should not combine DWIS and CHOP for experience purposes as they are separate and distinct enterprises. Among other things, the DWIS was continually managed by a Mr. Kemble, a former owner, until illness forced Mr. Ostrom to assume the management. Further, Appellant argues the Bureau cannot pierce the corporate veil to find the persons who own the stock in order to determine if entities are combineable for experience rating purposes. Also, Appellant argues that the Chapter 11 proceedings prevent the Bureau from combining the experience since DWIS, one of the entities whose experience is being used, is also in bankruptcy.

The Bureau does look behind to the corporate veil to see who is actually running these entities. Essentially, its position is that "people, not corporate entities" make the decisions. The Bureau argues that the bankruptcy proceeding is not a factor, since Chapter 11 is a debtor in possession proceeding and thus the experience of such a bankrupt may be combined with other operations of the debtor.

The oral arguments, and the briefs presented by both sides, discuss at length corporate, bankruptcy, and even partnership law. The basic issue here is the assessment of workers' compensation insurance premiums. Page 5 of "Appellant's Reply to the Bureau's Response to Appellant's Brief in Advance of Hearing" recognizes that there really is a workers' compensation insurance issue, stating "The policy behind these Rules should be the protection and preservation of workers' compensation benefits for workers employed in the State of California." This is an important consideration. However, the complete system of workers' compensation encompasses more than a system for delivery of benefits to injured workers. A basic tenet of the workers' compensation law is to make employers responsible for the injuries to the workers, without regard to fault. Work injuries are to be considered a part of the cost of doing business, just as repairing broken machinery would be. Further, a responsibility is placed on employers to maintain a safe work environment.

Insured employers are expected to sustain some losses under their workers compensation policies. The California Experience Rating Plan ("Plan"), Title 10, California Code of Regulations Section 2353, furthers the basic principals of the workers' compensation system by (1) rewarding employers whose losses are less than expected, and (2) exacting additional premium from those employers whose losses are greater than would be expected. The problem sometimes is; who is the employer responsible for these losses?

Management plays an important role in work place safety. The Plan recognizes this. At the time pertinent to this appeal, the Plan considered management to be vested in ownership. Section III, Rule (8). Thus, ownership must be determined in order to assess experience under the Plan.

Section III, Rule (9) provides that the experience of separate entities shall be combined for rating purposes when the same person or persons own a majority interest in each of the entities so combined. Subsequent to July 1985, CHOP was owned 50% by Ostrom and 50% by Poulton. DWIS was a subsidiary of CHOP. Ostrom and Poulton formed Diamondback in 1985, the ownership being 50% each. DWIS, a subsidiary of CHOP, was owned 50/50 by Ostrom and Poulton. The newly-formed Diamondback was 50/50 Ostrom and Poulton. Thus, Ostrom and Poulton controlled CHOP through stock ownership, DWIS as it was a subsidiary of CHOP, and the newly-formed Diamondback.

DWIS and CHOP filed for Chapter 11 Bankruptcy protection in June 1987 (CHOP was subsequently dismissed). Chapter 11 is a debtor in possession bankruptcy. Rule (9) of the Plan provides that the operations of a debtor in possession shall be combined for experience rating purposes with any other operations of the debtor. At the Classification and Rating Committee Hearing, the Appellant stated that an injunction might be sought from the Backruptcy Court if the combination of experience stood. We have not heard anything from the Court in this matter.

There could be, or perhaps have already been, certain stock transfers subsequent to October 1987 because of the bankruptcy. This aspect of the case is still apparently under review by the Bureau staff. Hopefully, some agreement will be achieved among the parties concerning this issue after October 1987 so to preclude it from also going through the appeals process as a separate matter.

## CONCLUSION and ORDER

The Bureau Decision to combine the experience of DWIS and CHOP to determine the experience rate of Diamondback for 1986 and 1987 is not an unreasonable decision. As shown, Ostrom and Poulton effectively controlled all three of these enterprises. Proper assignment of workplace injuries and the subsequent promulgation of an experience rate based on these injuries necessitated looking through the corporate veil to determine the individuals involved. Therefore, it is ORDERED that the Decision of the Classification and Rating Committee, that the experience of CHOP, Inc. and Donald Wilson Irrigation Systems be combined to determine the experience modification for Diamondback Enterprieses, Inc. be sustained.

DATED:

April 4, 1991

Joseph P. Powers

JOSEPH P. POWERS
Hearing Officer

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