

No. 08-2-00959-6

42018-0

**IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION II**

NORTHWEST WALL & CEILING
CONTRACTORS ASSOCIATION,

Plaintiff/Appellant,

v.

DEPARTMENT OF LABOR & INDUSTRIES,

Defendant/Respondent.

REPLY BRIEF OF APPELLANT

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I. Argument in Reply

Retro participants like NWCCA account for approximately one half of all the standard industrial insurance premiums paid to the Department of Labor and Industries.¹ Even so, the Department simply forgot about Retro when implementing the Drywall Initiative. The Department's mistake resulted in NWCCA being assessed and paying \$610,834 in net penalties for the first time in its retro history.

The Department implemented changes that fundamentally altered the nature of Retro for drywall employers but simply did not think about its impact on Retro groups. The change blindsided drywall employers who participated in Retro because, for the past 17 years, the Department had used actuarially sound data to ensure adequate rates. The Drywall Initiative took this reliable insurance program and converted it into a highly speculative endeavor – a gamble.

Gambling is not insurance.² Even so, the Board acknowledged that the Department's confidence in the rates implemented with the Drywall Initiative was akin to "predicting the

¹ Exhibit 7 (Requests for Admission) at RFA #18.

² RP (11/16) at 24 (Romero: "Retro is a risk, but it's not a gamble L&I changed that agreement from being an agreement where there's an acceptance of some risk to a pure gamble.")

outcome of the Kentucky Derby in advance.”³ Meanwhile, NWCCA members had to rely on the adequacy of the drywall rates to set the costs for bidding their contracts. If those rates were not a reliable estimate, then the drywall bids likewise would be seriously flawed.

It was improper for the Department to turn an insurance program into a pure gamble for the drywall employers. In Washington, there is a “quasi-fiduciary relationship” between an insurer and an insured. *Van Noy v. State Farm Mut. Auto. Ins. Co.*, 142 Wn.2d 784, 793, 16 P.3d 574 (2001). An insurer must “deal fairly with an insured, giving equal consideration in all matters to the insured’s interests as well as its own.” *Id.* Such an insurer, public or private, fails in this duty when it converts an insurance program into a pure gamble without warning.

The Department admitted at trial that recognized insurance principles required it to inform NWCCA “of major changes in the potential costs of coverage.”⁴ The Department admitted that, with the Drywall Initiative, it “intentionally set rates for some of the new drywall classes substantially below where the data from the old drywall classes suggested the rates should be[.]”⁵ The Department

³ BR at 3-4.

⁴ Exhibit 7 at RFA #21.

⁵ Exhibit 8 at Interrogatory #11.

admitted that no warning went out to drywall employers because, mistakenly, “no one thought about Retro.”⁶

Importantly, the Department also admitted it could not reasonably expect its Retro participants to discover the rate inadequacy of the Drywall Initiative without a warning from the Department.⁷ As the Department’s lawyer put it below, Retro participation is “tricky business.”⁸ As the Retro Program Manager testified: “I would not expect the man or woman on the street to be interested or able to” determine rate adequacy.⁹

Recognized insurance principles required the Department to provide a warning to Retro participants about the newly speculative nature of Retro after the Drywall Initiative. Such a warning, if given, might have looked something like this:

Beginning in January 1997, the Department is implementing the “Drywall Initiative” program. We believe this program will ultimately benefit drywall employers by making it more difficult to cheat the system. Therefore, the Department expects to collect more in premium dollars, which will ultimately allow the Department to lower drywall rates and offer a discount to good employers.

⁶ RP (11/17) at 173.

⁷ RP (11/17/09) at 119-120 (Doherty). Doherty followed that statement by testifying that the Department does “consider Retro employers normal human beings.” *Id.*

⁸ RP (11/17) at 14; *see id.* at 17 (“really complicated”).

⁹ RP (11/17/09) at 119-120 (Doherty). Doherty followed that statement by testifying that the Department does “consider Retro employers normal human beings.” *Id.*

However, the Drywall Initiative also requires us to switch to a new unit of exposure. We have attempted to convert our old hourly data to square foot data by using the assumption that one hour of work equals 125 feet of drywall installed. This number may not be an accurate measure for many drywall employers, as these rates differ based on the type of project and efficiency of the employee. Moreover, we are creating new classes for reporting by drywall employers (ten total) and implementing an owner exemption, each of which may significantly increase the danger of rate inadequacy. This means that, for the first 3-5 years of the Drywall Initiative, we will no longer have sufficient data to determine the "credibility" of our rates. There is now a significant chance that the rates we use for drywall will be significantly inadequate.

Normally, Retro employers are protected from inadequate rates by the "performance adjustment factor." However, the performance adjustment factor corrects only for general rate inadequacies across all classifications; it does not correct for a rate inadequacy in specific risk classifications. The Department is thus unable to act with the normal assurance that the Drywall rates it has set are actuarially adequate. This means there is a significantly greater risk, for all Retro participants, of potentially receiving retrospective assessments (penalties) than in prior years.

The Department admits it had "ready means available for communicating, to all drywall Retro participants, the potential inadequacy of the discounted rates implemented by the Drywall Initiative."¹⁰ Even so, no warning went out. As a result, NWCCA lost the opportunity to make a fully informed decision about Retro participation for the 1998-2000 plan years. Unaware, they stayed

¹⁰ Exhibit 7 at RFA #10.

in Retro, and the Department collected an extra \$610,834 as a result. Like Judge Grant, this Court should order the Department to refund that money and reverse the decision of the Board.

II. Reply to Department's Factual Summary

A close review of the record below reveals no actual factual disputes or credibility determinations. Though the parties differ on the proper characterization and legal consequence of several facts, there is no dispute as to what actually happened in this case. In fact, the Board of Industrial Insurance Appeals fully incorporated the factual summary of Industrial Appeals Judge Grant, who ordered the Department to refund NWCCA's money.¹¹ That undisputed evidence significantly undermines the Department's explanation of its actions in this case.

A. The new drywall rates were not actuarially determined.

The Department admits that Frank Romero "came up with the size of the discount," but then asserts that its own actuaries "approved" and "blessed" the new drywall rates.¹² They assert that their actuaries "found the level of discount reasonable in light of the

¹¹ BR at 3 ("Our industrial appeals judge has summarized the evidence relevant to this appeal. We expand on that summary only to the extent necessary to explain our decision.").

¹² Brief of Respondent at 16.

reforestation experience.”¹³ But the Department admitted below that “the discount the Department implemented as part of the Drywall Initiative was not an actuarially derived number.”¹⁴ The Department also admitted below that it “did not attempt to determine the adequacy of the discounted rate implemented as part of the Drywall Initiative before it implemented the Drywall Initiative.”¹⁵ The Department cannot now suggest that its actuaries engaged in actuarial analysis of the rates. Its admissions, which the Board and Superior Court failed to acknowledge, are binding.

Having made these admissions, the Department now asserts that it is no violation of the recognized insurance principles applicable to a *retrospective* insurance program to set rates that (1) are not actuarially derived and (2) have not been analyzed for adequacy. That argument fails because, as the Department must concede, Retro Program Manager Diane Doherty testified to the contrary. The Department attempts to distance itself from this all-too-candid testimony by deriding Ms. Doherty as being “neither an actuary nor an expert on rate setting.”¹⁶ But Ms. Doherty was the

¹³ Brief of Respondent at 16.

¹⁴ Exhibit 7 at RFA #4.

¹⁵ Exhibit 7 at RFA #7.

¹⁶ Brief of Respondent at 35.

person that the Department put in charge of deciding this appeal, based upon recognized principles of insurance.¹⁷ Presumably the Department put her in that position because she has an understanding of the recognized insurance principles applicable to a retroactive insurance program.

Regardless, Ms. Doherty's testimony shows that the Department knew it was reasonable for a Retro participant to expect that the Department's rates would be actuarially derived and analyzed for adequacy. The Department's failure to live up to those expectations, without any warning to its insureds, violated recognized insurance principles.

B. The Department does, and necessarily must, analyze the sufficiency of insurance rates at the classification level.

The Department asserts that its actuaries need only consider rate adequacy "at the fund level, not at the classification level."¹⁸ The problem with that argument, of course, is that the only way to have rates adequate at the fund level is to have rates that are adequate in the various individual classifications. And because the

¹⁷ See BR at 185. See also RP (11/16) at 118-119 ("Q. And you weren't in charge of Retro then, so you weren't making decisions about what should be communicated to Retro employers, right? A. Correct. Q. But now you are in charge of Retro? A. Yes. Q. And so it sort of falls to you to decide whether or not NWCCA is going to get their money back, right? A. Yes.").

¹⁸ Brief of Respondent at 36.

Department is not allowed to unfairly discriminate between different classifications of employers, its job is to set each classification as closely as possible to the true cost of insurance.¹⁹ Thus, no matter what the Department calls its process, it must (and does) analyze rate adequacy at the classification level.

The Department's attorney emphasized that very fact below during his cross-examination of Bill White:

Q. And you explained how you make an adjustment for the overall rate change that needs to happen; correct?

A. Correct.

Q. And then you also make an adjustment to take into account data specific to the particular risk classification?

A. Correct.^[20]

The Department's Director of Insurance Services, Bob Malooly, agreed: "We try to set rates so that they [come] as close to break-even as we can"²¹ because doing so is "a recognized insurance principle."²² According to Malooly, the Department's actuaries "gather as much information as they can from the historical performance. . . . And our goal is to make sure that the rates are

¹⁹ RP (11/16) at 27 (Romero: "There's another basic insurance principle that the rate or rating system should not be unfairly discriminatory.")

²⁰ RP (11/16) at 151.

²¹ RP (11/16) at 116.

²² *Id.*

fair.”²³ The Department’s actuary, Bill Vasek, also conceded the point: “What we try to do on a class basis is we try to set rates so that the expected costs, the expected costs of the rates are equal in order to have fairness.”²⁴

Analysis of “expected costs” at the classification level is analysis of adequacy at the classification level. Accordingly, the Department admitted below that it “intentionally set rates for some of the new drywall classes substantially below where the data from the old drywall classes suggested the rates should be[.]”²⁵ That admission runs directly contrary to the Department’s assertion, in its appellate brief, that it “thought” the Drywall Initiative rates were adequate “at the time” they were implemented.²⁶ If the Department knew where the class rates “should be,” then it assessed rate adequacy at the classification level, and it had every reason to know that the new rates would set Retro participants up for failure.

C. The Department’s claim that it “refrains from giving advice” is contradicted by the undisputed testimony.

The Department also attempts to justify its failure to warn NWCCA about the new level of uncertainty in Retro by asserting

²³ RP (11/16) at 118.

²⁴ RP (11/20) at 83.

²⁵ Exhibit 8 at Interrogatory #11.

²⁶ Brief of Respondent at 40.

that “the Department refrains from giving advice” to Retro participants.²⁷ Although there is a difference between giving “advice” and “warning,” it is undisputed in this record that the Department does give advice to Retro participants when it suits the Department’s needs. The uncontradicted testimony of Mr. Mettler was that the Department’s attorney, Jim Johnson, recommended a change in NWCCA’s plan for the 1999-2000 plan year:

And I probably should have picked up on this, is that it was also suggested, recommended by Mr. Romero and Mr. Johnson that we might want to look at what plan we had selected for the current year we were in, which that be at the -- at that point that would be the '99 to 2000 year, and this was March and they hadn't -- you know, it was in progress in the year and they said, look it, we'll give you this one -- you know, if you want look at it again and you have to act fast, we will give you an opportunity to change your plan, which was kind of unusual because this -- we were into it many months.²⁸

Regardless, it is disingenuous for the Department to claim that it does not play any role in a firm’s decision to participate in Retro when it (1) “encourages” participation in Retro and (2) had set up a special Retrospective Rating Advisory Committee.

²⁷ Brief of Respondent at 10.

²⁸ RP (11/20) at 53-54.

D. This Court should reject the Department's suggestion that all Retro participants must engage in their own actuarial analyses before deciding to enroll in Retro.

The Department's primary defense of its failure to warn NWCCA of the Retro problems is that NWCCA should have realized the Department's mistakes even if the Department did not. The Department suggests a Retro employer can easily "estimate its break-even point" before enrolling in Retro "by plugging into the formula the basic premium ratio and loss conversion factor determined by its size group, and plan and maximum premium ratio choices."²⁹ The Department asserts that NWCCA "could have known," prior to enrolling in the 1998-1999 plan year, that the many changes associated with the Drywall Initiative would cause its premium to decline by "about 15 percent."³⁰

This is a significant oversimplification of the challenges a Retro group would face in such a "break-even point" analysis.

²⁹ Brief of Respondent at 10.

³⁰ Brief of Respondent at 19. The "about 15 percent" figure came originally as an unsupported estimate by the Department's lawyer offered, for the first time, in the Department's prehearing memorandum. See BR at 246 ("At the time NWCCA had to commit to sponsoring the group for 1998 ... NWCCA had available to it a year's worth of data showing the effect the discounting was having on its members' standard premiums. That history showed that the discount was reducing NWCCA's standard premiums by about 15 percent."). Apparently, that figure is based on comparing the amount of premium that NWCCA members reported in 1997-1998 to some unspecified set or average of NWCCA's members' reporting from prior years.

Each Retro year “stand[s] on its own.”³¹ The amount of work each employer does changes significantly from year to year, and the number and composition of employers in the NWCCA drywall group also changes.³² The only thing NWCCA could bank on from year to year was that its safety program meant they would perform, as a whole, better than the Department’s expectations for an average drywall employer. This is why, until the Drywall Initiative, they had 17 straight years of refunds.

In fact, it was the Department’s cross-examination of Bill White that pointed out how extraordinarily complicated it would have been for an association of (mostly) drywall employers to forecast its performance in Retro after the implementation of the Drywall Initiative. As the Department showed below, an association like NWCCA would have to have been able to know and apply the effects of several highly complicated factors beyond anything they had ever had to understand for Retro before:

³¹ RP (11/17) at 174.

³² RP (11/17) at 11; *see also* Exhibit 19. From 1998 to 1999, the number of employers in the group went from 20 to 10.

- the new (1997) division of the single drywall classification into ten different classifications: discounted and non-discounted classes for Installation, Taping, Priming/Texturing, Stocking, and Scrapping;³³
- the late-adopted “owner exemption,” for which no data was available because that information was not reported prior to 1997;³⁴
- the percentage of overall reporting by non-drywall employers within the NWCCA Retro group, i.e., NWCCA employers who were not subject to drywall initiative rate changes,³⁵ and
- the accuracy of the 125 square foot per hour estimate that the Department apparently used to convert its old numbers, which is not only dependent upon the specific worker and employer but also on the type of project (commercial versus residential).³⁶

Thus, the Department’s lawyer pointed out at the hearing that even attempting to estimate a “break even point” for a Retro association would have been “tricky business.”³⁷ The Department’s lawyer also went out of his way, below, to point out that this type of forecasting could not be expected of “[n]ormal human beings”:

Q. Certainly, people who like to play with numbers, like actuaries, might think of doing something like that?

A. Yes.

³³ Exhibit 6.

³⁴ RP (11/17) at 29.

³⁵ RP (11/17) at 11.

³⁶ RP (11/17) at 12.

³⁷ RP (11/17) at 14; *see id.* at 17 (“really complicated”).

Q. Normal human beings might not?

A. Correct.^{38]}

The relevant question is thus whether the Department knew that its Retro employers could not reasonably be expected to conduct high-level actuarial analysis, every year, before deciding whether to participate in Retro. The Department's current Retro Program Manager, Diane Doherty, answered that question at the hearing: "I would not expect the man or woman on the street to be interested or able to" determine rate adequacy.³⁹ Thus, Doherty confirmed, "it would be reasonable ... for an employer in Retro to believe that the Department was setting adequate rates."⁴⁰

Although the Department derides Ms. Doherty in other portions of its response,⁴¹ the Department does not dispute this fundamental premise that she articulated: Retro employers reasonably assume the Department is doing its job in setting adequate rates. For that reason, the question that employers focus on in deciding whether to participate in Retro is: "Are we better than

³⁸ RP (11 /17) at 13.

³⁹ RP (11/17) at 119-120 (Doherty). Doherty followed that statement by testifying that the Department does "consider Retro employers normal human beings." *Id.*

⁴⁰ *Id.* at 120. Dr. White was even more explicit: "But as I mentioned many times before, the Department -- and they should know this -- they're dealing with unsophisticated insurance buyers. These people are in associations where their job and the jobs of the people that are in it are trying to scratch out a living doing some drywall. It's not to do actuarial analysis." RP (11/17) at 72.

⁴¹ See *supra* at § II(A).

average at worker safety and keeping costs down?” If the employer believes their safety program is better than average at those issues, it makes sense to participate in Retro. NWCCA’s safety program provided a resounding “yes” to that question for the 17 years before the Drywall Initiative.

E. The 1999-2000 plan year refund was due, undisputedly, to abnormally low claims costs per unit of exposure.

Finally, the Department suggests that the rates were not inadequate because NWCCA got a refund in the 1999-2000 plan year.⁴² But it was settled long before the hearing that the 1999-2000 plan year was simply an aberration. In fact, the Department admitted as much in a Request for Admission: “[t]he refund NWCCA earned for plan year 1999-2000 was the result of abnormally low claims costs per unit of exposure.”⁴³ Retro Manager Doherty agreed at the hearing that NWCCA’s performance had been “phenomenally good.”⁴⁴ That NWCCA received a refund for the 1999-2000 plan year is irrelevant, except to the extent that the refund for that year must be set off against the

⁴² Brief of Respondent at 21.

⁴³ RFA #19.

⁴⁴ RP (11/17) at 135.

\$1,044,667⁴⁵ in Retro penalties for the 1998-1999 and 2000-2001 plan years.

III. Reply to Department's Legal Argument

A. The Department's waiver argument is a red herring.

The Department asserts that because NWCCA did not challenge the rates it set in the 1998-2000 plan years in the superior court, those rules are "valid and binding."⁴⁶ NWCCA does not challenge the validity of the rules implemented as part of the Drywall Initiative per se. If the rules were invalid, any employer would be able to challenge them, regardless of the employer's participation in Retro.

Rather, NWCCA was harmed by the Department's failure to run Retro consistent with recognized insurance principles. Specifically, as explained in NWCCA's opening brief, the Department was required by those principles to either (1) adopt adequate, actuarially derived rates or (2) make it clear to Retro participants that they were not doing so. This is not an argument that the rates are non-binding, but rather that the Department

⁴⁵ Exhibit 7 at RFA #13-14.

⁴⁶ The Department did not raise this issue before the first appeal to the Superior Court, where Judge Tabor specifically rejected any defenses based on timing of the appeal and ordered the merits of the claims to be addressed. BR at 81.

should not be allowed to retain retrospective assessments when it has failed in its statutory duty to run its retrospective insurance program consistent with recognized insurance principles. *See, e.g.*, RCW 51.08.010(2).

B. The Department did not follow recognized insurance principles in setting the Drywall Initiative rates.

The Department's primary defense of its conduct in this case has been, throughout the litigation, that it used the "best available information" in setting the Drywall Initiative rates for each relevant plan year. But the undisputed evidence below was that the Department deliberately ignored the *only available information* that could have showed the inadequacy of the Drywall Initiative rates.

The Department admits that it started receiving square foot data in January 1997.⁴⁷ NWCCA did not enroll for the 1998-1999 plan year until June 1998: 18 months later.⁴⁸ And NWCCA did not enroll for its final plan year until June 2000: 42 months later.⁴⁹ Even so, the Department takes the position that none of this data required it to do anything during the relevant plan years.

⁴⁷ Exhibit 7 at RFA #11 ("the first plan year the Department used data derived from square foot reporting was July 1, 1996 through June 30, 1997, when standard premiums were reported using square foot rates for the first and second quarters of 1997.").

⁴⁸ Exhibit 12 (timeline).

⁴⁹ Exhibit 12 (timeline).

Specifically, the Department asserts this data did not require it to either adjust the drywall rates or, more importantly, warn the drywall participants in Retro of the apparent inadequacy.

The Department asserts that its decision to use the "standard actuarial approach"⁵⁰ for this decidedly non-standard situation was an acceptable "judgment call," citing the testimony of Bill Vasek. But not even Vasek attempted to justify the failure of the Department to warn Retro participants about the difficult "judgment call" it had to make in setting the drywall rates for the 1998-2000 plan years. Nor did Vasek ever address Bill White's indictment of the Department's failure to warn:

Q. Okay. Now -- so you think it was -- do you think it was unreasonable of Bill Vasek in the fall of 1998 to decide to just let the drywall rates go where they go and follow the ordinary process?

A. I think -- I think there were some problems with that. Because at this point, if he knows the rates are inadequate and he knows that there is a retro program that is using those rates, he has a choice either to leave them inadequate or to forgive the retro program -- I mean either to correct the rates or to forgive the retro program, their enrollment in retro, or to at least warn them that "Hey, fellas, we're" -- "now we know we're giving you inadequate premiums to support your Retro programs." So there's a number of choices you

⁵⁰ Brief of Respondent at 39.

can make, but you can't just leave people hanging.^{51]}

To the extent the Department did not understand that the Drywall Initiative rates were inadequate by the 1998 plan year, its failure to analyze and monitor its new program violated recognized insurance principles. To the extent the Department did understand the adequacy problems by that time, its failure to warn of the inadequacy violated recognized insurance principles. Regardless, the Department cannot be said to have used the "best available data" when it intentionally ignored the only available data.

C. The Department at all points failed to explain to drywall employers that its Drywall Initiative could mean major changes in the potential costs of Retro participation.

The Department admitted below that it owed NWCCA a duty to warn about any "major changes in the potential costs of coverage."⁵² The Department contends it met this duty by reporting "the amount of work being reported under the new rules" to the Drywall Technical Advisory Committee.⁵³ But simply publishing raw data, without any explanation as to why that data is relevant to the

⁵¹ RP (11/17) at 66.

⁵² Exhibit 7 at RFA #21 ("Admit that it is a recognized principle of insurance that insurers have a duty to inform insureds of major changes in the potential costs of coverage. Response: Admitted.").

⁵³ Brief of Respondent at 14, 38.

decision to participate in Retro, does not constitute a warning about a major change in the potential costs of coverage.

The testimony at the hearing was that, at some time in 1998, a non-actuary⁵⁴ at the Department brought raw data to a Drywall Technical Advisory Committee meeting. No analysis of those numbers was provided at those meetings.⁵⁵ More importantly, the topic of Retro was never brought up at those meetings.⁵⁶ That failure is significant given that half of the standard premiums the Department received came from Retro participants at the time.⁵⁷ Retro was not some fringe program that could justifiably be off of the Department's radar.

Because Retro was such a significant program, the Department actually had a Retrospective Rating Advisory Committee.⁵⁸ No one from the Department made any report to the Retrospective Rating Advisory Committee about the possible effects of the Drywall Initiative on Retro participants.⁵⁹

⁵⁴ Gary Griesmeyer was an "actuary analyst," and not an actuary. RP (11/20) at 76. An actuary analyst is someone who "hadn't completed all their exams to become an actuary yet." *Id.*

⁵⁵ RP (11/24) at 20-21, 38-40.

⁵⁶ RP (11/17) at 124.

⁵⁷ Exhibit 7 (Requests for Admission) at RFA #18

⁵⁸ Exhibit 7 (Requests for Admission) at RFA #3.

⁵⁹ *Id.*

The reason these kinds of helpful reports were never made is that the Department, quite simply, forgot about Retro when it implemented the Drywall Initiative. The Department has admitted as much: "At the time the Department had not considered what impact discounting rates could have on the prospects of receiving a beneficial adjustment through retrospective rating."⁶⁰ Ms. Doherty, who searched the Department's archives for some evidence that anyone at the Department had thought about Retro during the implementation of the Drywall Initiative, found no such evidence:

Q. No red flag went up, right?

A. Not that I'm aware of.

Q. And that's because no one thought about Retro, right?

A. As far as we know, yes.^[61]

As Bill White explained, the Department failed to consider the impact of the Drywall Initiative on Retro because the various units of the Department were not organized to communicate with each other on these critical issues:

The trouble is we weren't really organized to serve our clients, and we didn't -- all the people who impacted what happened to them didn't necessarily stop to think about the outcome. There was -- On this case there was Frank Romero, who was handling the discount and the classifications and all that stuff;

⁶⁰ Exhibit 7 at RFA #47.

⁶¹ RP (11/17) at 173.

there's myself, the actuary; and then there was the folks in Retro. . . . I don't exclude myself from criticism here.⁶²

Such communication within the Department would have led to an appropriate warning to NWCCA about the new risks of Retro:

Q. Mr. White, if somebody from Retro had come to you in '97 or even '96, late '96, when the drywall initiative was being prepared and certainly well publicized within the Department, and said, "You know what? We" -- "over here in Retro we have a drywall group. How is this going to impact them? Because the drywall initiative is clearly directed to drywall rates." What impact would that have had?

A. You're talking about somebody from Retro at L&I?

Q. Yes.

A. Well, I would definitely have cautioned them that this group definitely needs to be aware of what we're doing so they can make an intelligent decision about their participation. And, you know, they should very seriously consider sitting this one out because the dice are loaded, you might say.⁶³

D. **There is no material distinction between this case and *Woodworker's Supply*.**

The Department distinguishes its conduct from that of the private insurer in *Woodworker's Supply, Inc. v. Principal Mutual Life Ins. Co.*, 170 F.3d 985 (10th Cir. 1999) on the ground that "the trier

⁶² RP (11/17) at 99-100.

⁶³ RP (11/17) at 101.

of fact in this case rejected NWCCA's claim that the Department knew the drywall rates were inadequate."⁶⁴ The Department cites Findings of Fact 14 and 15 for that proposition, but those Findings of Fact make no such rejection.⁶⁵ Rather, the Department has admitted that it "intentionally set rates for some of the new drywall classes substantially below where the data from the old drywall classes suggested the rates should be[.]"⁶⁶

NWCCA does not suggest that any person in the Department acted with ill will or the intent to deceive them. But the Department's conduct, due to the failure of the Department to communicate internally, was the same: NWCCA was encouraged to participate in a program based on rates that the Department had intentionally understated. Nor does NWCCA need to show intentional misbehavior: a negligent violation of recognized insurance principles is still a violation of recognized insurance principles. The Board's conclusions to the contrary are unsupported by the undisputed facts.

⁶⁴ Brief of Respondent at 45.

⁶⁵ Finding of Fact 14 provides: "The Department requires three to five years of accumulated data to make statistically reliable predictions." Finding of Fact 15 provides: "Industrial Insurance Claims may remain open for several years. Liability for a given plan year is not fully determined until the third and final adjustment following the year in which the industrial injury occurred or in which an occupational disease was diagnosed."

⁶⁶ Exhibit 8 at Interrogatory #11 (emphasis added).

E. NWCCA is entitled to prejudgment interest and attorney fees.

The Department does not dispute that NWCCA, upon prevailing, will be entitled to prejudgment interest. The Department notes that attorney fees are not available to an employer, but only the employee, under RCW 51.52.130(1). But another statute does allow attorney fees for an employer in judicial review of administrative proceedings. See RCW 4.84.350.

IV. CONCLUSION

The undisputed facts show that the Department set its Retro customers up to fail. Its various divisions – those in Classification Services, those in Retro, and the actuaries – were not organized to communicate with each other during the implementation of the Drywall Initiative. “[N]o one thought about Retro,”⁶⁷ a program that supplied half of the standard premiums for the entire state. That failure violated recognized insurance principles applicable to retrospective insurance and caused NWCCA to pay \$610,834 in *extra* premiums. For these reasons, NWCCA respectfully asks this Court to reverse the Superior Court’s decision and refund

⁶⁷ RP (11/17) at 173.

NWCCA's money in the amount of \$610,834 together with interest and legal fees.

Respectfully submitted this 1st day of March, 2012.

STAFFORD FREY COOPER

By: 

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CERTIFICATE OF SERVICE

The undersigned certifies under the penalty of perjury according to the laws of the United States and the State of Washington that on this date I caused to be served in the manner noted below a copy of this document entitled REPLY BRIEF OF APPELLANT on the following individual:

Counsel for Respondent Department
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- VIA FACSIMILE
- Via First Class Mail
- Via Messenger
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RECEIVED
MARCH 13 2012
DEPARTMENT OF LABOR & INDUSTRIES
ATTORNEY GENERAL'S OFFICE

DATED this 2nd day of March, 2012, at Seattle, Washington.

Nori Skretta

Nori Skretta