

policy period. The parties have stipulated that the this issue should be resolved by the provisions of the Basic Manual for Workers' Compensation and Employers' Liability Insurance, published by the National Council on Compensation Insurance ("NCCI Manual").² As set forth below, the NCCI Manual requires Hartford to refund all excess premiums resulting from its use of incorrect classifications, back to the date of the inception of the policy. Accordingly, the decision of the Workers' Compensation Appeals Board is hereby **AFFIRMED**.

II. FINDINGS OF FACT

Valley Mechanical

1.

Valley Mechanical has been in business since 1982. Its business primarily involves two activities – heavy-plate fabrication and installation of equipment. Valley Mechanical employs an average of ninety employees, although the number fluctuates from year to year. According to David Stutz, the Chief Executive Officer and owner of Valley Mechanical, the company has not changed the nature of its business since it first purchased a workers' compensation and employers' liability insurance policy through Hartford. *Testimony of David Stutz.*

The Hartford Policy

2.

Hartford first issued workers' compensation insurance policy number 20WEPH7313 to Valley Mechanical ("Hartford Policy"), effective April 1, 2006, for the 2005-2006 policy year. The terms of the Hartford Policy have remained unchanged in pertinent part since the first policy year. Hartford policies are effective for one-year terms, running from April of one year to April

² In the *Joint Status Report* filed by the parties, the parties agreed that the NCCI Manual was controlling. Although Valley Mechanical asserted that other legal and equitable principles support its request for relief, this Court finds the NCCI Manual provision to be determinative, and it is therefore unnecessary to address Valley Mechanical's alternative bases for recovery.

of the next year, and are renewed annually. The Hartford Policy was the continuation of a pre-existing workers' compensation policy that Valley Mechanical had acquired through BB&T Insurance Services, Inc. At the time Hartford began insuring Valley Mechanical, Hartford's Executive Underwriter, EllenSue Jahn, reviewed the workers' compensation classifications already in place, but decided that it was not necessary to have a Hartford field underwriter collect independent data on Valley Mechanical's operations in order to confirm that the existing classifications were correct.³ *Testimony of EllenSue Jahn.*

NCCI Manual

3.

The Department of Insurance has contracted with the NCCI, which sets insurance industry standards in 33 states, to promulgate Georgia's workers' compensation insurance rules. *Testimony of Derrick Wirtz.* Accordingly, the NCCI is the authoritative body on workers' compensation classifications in Georgia and has "the final say" on which classifications apply. *Testimony of EllenSue Jahn.* Hartford's witnesses agreed that the NCCI Manual is incorporated into all workers' compensation and employers' liability insurance policies entered into in the state of Georgia, including the Hartford Policy. *Testimony of Andrew Golden; Testimony of EllenSue Jahn.* Specifically, the Hartford Policy states that "[a]ll premiums for this policy will be determined by our manuals of rules, rates, rating plans and classifications."⁴ *Exhibit R-1, -2.*

³ Jahn testified that the process for underwriting a workers' compensation policy differs depending on whether the policy is pre-existing or new. For example, for a new policy for a start-up company, information for determining the correct premium classifications would be collected by a field underwriter during an on-site visit. For a pre-existing policy, however, Jahn testified that it was not uncommon to rely on the prior classifications. *Testimony of EllenSue Jahn.*

⁴ Hartford's counsel cited the case *Home Insurance Co. v. Sunrise Carpet Industries, Inc.*, to support the conclusion that the NCCI Manual is incorporated into all workers' compensation

Development of Premium Rates

4.

Premiums are developed using thirteen different elements, only a few of which are relevant in this case. A foundational element is the baseline rate, called a “lost cost,” which is established by the NCCI to reflect the expected loss for every \$100 of payroll for any particular classification. There are approximately 598 NCCI codes that classify employees based on their job and the product produced. Each classification is intended to reflect the risk exposure associated with that particular job. The classification codes are nuanced so that they can clearly capture the work done by a company’s employees. *Testimony of Derrick Wirtz.* Insurance companies must assign the correct classification to an insured’s employees so that their wages will be assessed at the correct rate. *Testimony of Derrick Wirtz; Testimony of Dennis Sullivan.*

5.

Insurance companies also look at another element to determine the appropriate workers’ compensation premium—a “loss cost multiplier.” The loss cost multiplier is based on an insurance company’s own operating expenses and profit margin. The insurance company determines its loss cost multiplier and then files it with the Department of Insurance. In order to determine the premium it will charge to insure a particular business, the insurance company will multiply NCCI’s lost cost baseline rate by its own lost cost multiplier to determine the overall rate per \$100 of payroll to charge as premium. *Testimony of Derrick Wirtz.*

insurance policies in Georgia. 229 Ga. App. 268, 268-69 (1997). The court in that case cited language in the policy, analogous to the language in the Hartford Policy, that “[t]he premiums for this policy will be determined by our manuals of rules, classifications, rates and rating plan”—language the court presumably relied on when, later in its decision, it stated that the NCCI Manual was incorporated by reference into the policy. *Id.*

6.

A third element is the “experience modifier,” which reflects the business’s history of workers’ compensation claims (that is, claims filed when an employee is injured on the job). The NCCI predicts that the insured will have a certain amount in losses based on the assigned classifications. An experience modifier will impact the premium in the following way: if the company does better than its anticipated loss, it receives a credit against its premium; if it does worse than its anticipated loss, it receives a debit against its premium. *Testimony of Derrick Wirtz.*

Annual Audits

7.

The Hartford Policy specifies the terms under which an audit of insurance premiums may occur. At the outset of a policy term, the premium charged is only an estimate based on the insured’s projected payroll for the coming twelve-month period. *Exhibit R-1, -2; Testimony of John Hewgley.* After the conclusion of a policy term, an audit is used to determine the final premium “by using the actual, not the estimated, premium basis and the proper classifications and rates that lawfully apply to the business and work covered by [the] policy.” *Exhibit R-1* (emphasis added). *Exhibit R-1.* Thus, audits of payroll must occur after the completion of a policy term to determine how much money was actually paid out. *Testimony of John Hewgley.* Audits systematically occur after the end of a policy period and, per the terms of the policy, can be initiated by Hartford or an insurance rate service organization for “three years after the policy period ends.” *Exhibit R-1.* While audits are generally for one-year periods, insurance companies can and do conduct multiple year audits. A multi-year audit is rare, but generally occurs when the insurance company has a financial incentive, such as when it has identified a mistake in

classifications that would result in an increased premium. *Testimony of John Hewgley.*

8.

Audits frequently result in an adjustment in the premium amount. *Testimony of Anthony Stangel.* Where an audit results in an adjustment, the Hartford Policy requires the insurance company to refund the balance if the audit results in a lower premium than estimated, and requires the insured to pay the balance if the audit results in a higher premium than estimated. *Exhibit R-1.* The Hartford Policy does not contain a time restriction or deadline for such payments.

9.

The NCCI Manual, on the other hand, does address time restrictions in relation to premium over- and undercharges that are the result of incorrect classifications (as opposed to fluctuations in payroll). NCCI Rule 1(F)(2) and NCCI Rule 1(F)(3), respectively, address decreased premiums, which result in refunds to the insured, and increased premiums, which obligate the insured to pay additional moneys. NCCI Rule 1(F)(2) provides that “[c]orrections in classifications that result in a decrease in premium, whether determined during the policy period or at audit, must be applied retroactive to the inception of the policy.” By contrast, Rule 1(F)(3) states:

Corrections in classification that result in an increase in premium must be applied as follows:

- If the correction in classification is effective during the first 120 days of the policy term, then the correction is applied retroactively to the inception of the policy.
- After the first 120 days of the policy term, but before the final 90 days, then the correction is applied as of the date the company discovers the cause for that correction.
- If the correction in classification is effective during the last 90 days of the policy term, then the correction is applied only to a renewal policy, if any.

Exhibit R-8.

10.

As expected, following the completion of every policy year, Hartford conducted an audit of Valley Mechanical's payroll. *Exhibit R-3; Testimony of David Stutz; Testimony of Anthony Stangel.* Each audit for the policy years 2005-2006 through 2010-2011 resulted in an increased premium. *Exhibit R-3; Testimony of David Stutz.* Audits were conducted at Valley Mechanical's corporate headquarters in Georgia. Anthony Stangel, who conducted the audit every policy year following the 2007-2008 policy year, did not physically inspect Valley Mechanical's operations but instead inquired about operations changes. Overall, while Stangel observed that payrolls increased and decreased based on demand for Valley Mechanical's services, he reported no operational changes in the business. *Testimony of Anthony Stangel.*

11.

The description of Valley Mechanical's operations in the "physical audit" from each policy year, dating from the 2005-2006 policy year through the 2011-2012 policy year, was as follows:

The insured is a light gauge metal fabrication shop. Custom parts and accessories are made for industrial equipment. The main customers are in the food services industry. The shop operations consist of welding, cutting, and assembly. The machine shop is a separate operation. This shop is a precision machine shop with work done at very close tolerances. The parts machined are for industrial equipment. Some of the products made are air handlers, platforms and rails, and other job shop projects. The insured also installs the products made in the shop. Also, the insured offers installation of production line equipment at the plant locations of the customers. This represents less than 10% of the installation work done by the insured. The same workers in the shop may perform the installation work. I did not see the need to add code 3724 Millwright at this time.

Exhibit R-3. During this time frame, Valley Mechanical's employees were classified as follows:

- Precision Machined Parts MFG, NOC, classification code 3629, rate 1.65;
- Sheet Metal Work NOC and Drivers, classification code 5538, rate 8.92;
- Salespersons – outside, classification code 8742, rate .43; and
- Clerical office employees NOC, classification code 8810, rate .23

The description of operations remained unchanged from the policy year beginning April 1, 2006, through the policy year ending April 1, 2012, until it was retroactively changed following the NCCI audit, discussed below. *Exhibit R-3; Testimony of Anthony Stangel.*

NCCI Audit

12.

The NCCI conducted an audit of Valley Mechanical in 2012 at the company's own request. Valley Mechanical had taken the step of requesting an independent audit at the suggestion of Derrick Wirtz, an insurance agent employed by First Volunteer Insurance, specializing in workers' compensation insurance for machine shops and millwrights. Wirtz had visited the company's plant, viewed its operations, and spoken with managers about what work they were actually doing. Based on his observations and expertise in the field, he believed that Valley Mechanical's workers had been misclassified. *Testimony of Derrick Wirtz.*

13.

Following the audit, NCCI released a report in June of 2012 that determined, based upon the actual work performed by Valley Mechanical employees, that the classifications Hartford had applied to Valley Mechanical's operations were incorrect, with two exceptions. *Exhibit R-7.* The two classifications retained as correct were codes 8810 (Clerical Office Employees) and 8742 (Salespersons or Collectors — Outside), with rates of .23 and .43 per \$100 of payroll, respectively. *Exhibit R-7.* Otherwise, the audit eliminated classification codes 3629 (Precision Machined Parts) and 5535 (Sheet Metal Work), with the respective rates of 2.28 and 14.65. It replaced these classification codes with codes 3620 (Tank building), 3632 (Machine Shop), and 3742 (Millwright Work), with the respective rates of 6.43, 5.90, and 8.31. *Exhibits R-3, R-7.* The overall result of the audit was a determination that Hartford had substantially overcharged

Valley Mechanical during each of the preceding policy years, going back to 2005-2006.

Testimony of David Stutz.

14.

Hartford formally accepted⁵ the results of the NCCI audit and reduced Valley Mechanical's insurance premiums based on the new classification codes for two policy years: the policy year beginning April 1, 2011, and the policy year beginning April 1, 2012. *Testimony of Andrew Golden.* The total premium refunded amounted to approximately \$76,000, 94% of which was due to the misclassifications and 6% of which was due to a lower-than-projected payroll. *Testimony of Dennis Sullivan.* Hartford argues that it was only required to implement the change in classifications during the then-current policy year (i.e., 2012, the policy year in which the error was discovered). *Testimony of Andrew Golden.* Nevertheless, Hartford implemented the change for the prior policy year. It is Hartford's position that this was a voluntary decision, made out of consideration of the fact that Valley Mechanical had requested the audit during the prior policy year. *Testimony of Andrew Golden; Testimony of EllenSue Jahn.* Arguing to the contrary, Valley Mechanical insists that Hartford is required to implement the correct classifications for every policy year in which the incorrect classifications were imposed, back to the 2005-2006 policy year. Both rely on the language of the NCCI Manual to support their respective positions.

⁵ See *Joint Status Report*. While Hartford has chosen not to contest NCCI's factual findings and choice of classification codes, Hartford Executive Underwriter EllenSue Jahn and Hartford auditor Anthony Stangel maintained at the hearing that NCCI's method for allocating classification codes was incorrect. Stangel insisted that NCCI should have classified the business and not the employees. Jahn speculated that because NCCI's audit was merely a snapshot in time, the nature of Valley Mechanical's work may have changed overtime, as it is dependent on the types of jobs it receives. Nevertheless, they both agreed that Hartford is bound to accept NCCI's classifications as the ultimate authority on the matter.

III. CONCLUSIONS OF LAW

1.

By agreement of the Parties, Respondent Valley Mechanical bears the burden of proof. *Joint Status Report*. The standard of proof is a preponderance of the evidence. Ga. Comp. R. & Regs. 616-1-2-.21.

Contract interpretation principles

2.

“Insurance in Georgia is a matter of contract.” *Cole v. Life Ins. Co.*, 236 Ga. App. 229 (1999) (citing *Richards v. Hanover Ins. Co.*, 250 Ga. 613 (1983)). As is generally true in contract law, insurance policies (contracts) using language that is “plain, unambiguous, and capable of only one reasonable interpretation” cannot be construed by the court. *Cincinnati Ins. Co. v. Davis*, 153 Ga. App. 291, 294 (1980). Of course, “the contract as a whole must be looked to in arriving at the construction of any part.” *Nationwide Mut. Fire Ins. Co. v. Collins*, 136 Ga. App. 671, 675 (1975) (citing *Sovereign Camp, W. O. W. v. Heflin*, 188 Ga. 234, 235 (1939)). If there are conflicting terms, the one “most favorable to the insured” applies. *W. Pac. Mut. Ins. Co. v. Davies*, 267 Ga. App. 675, 679 (2004) (citing *Home Ins. Co. v. Sunrise Carpet Indus.*, 229 Ga. App. 268, 271 (1997)). Furthermore, [i]n construing an insurance policy, the test is not what the insurer intended its words to mean, but what a reasonable person in the position of the insured would understand them to mean. The policy should be read as a layman would read it and not as it might be analyzed by an insurance expert or an attorney.” *Cincinnati Ins. Co.*, 153 Ga. App. at 295 (citing *Nationwide*, 136 Ga. App. at 675).

Ambiguity favors the insured

3.

If the insurance contract contains ambiguities that can be read in a manner urged by the insured, the language must be “strictly construed against the insurer as drafter of the document,” *Home Ins. Co.*, 229 Ga. App. at 271 (citing *Hulsey v. Interstate Life &c. Co.*, 207 Ga. 167 (1950)), and interpreted “liberally in favor of the contention of the insured.” *Cincinnati Ins. Co.*, 153 Ga. App. at 294. Thus, “[w]hen the premium and method of premium calculation are ambiguous or contradictory, the method of calculation most favorable to the insured shall be applied.” *Home Ins. Co.*, 229 Ga. App. at 271 (citing *Davis v. United Am. Life Ins. Co.*, 215 Ga. 521 (1959)). The insurer also has a duty to act reasonably and in good faith in calculating retroactive premiums. *Home Ins. Co.*, 229 Ga. App. at 271-72. In addition, if there is an exclusion in an insurance policy, the insurer has “the burden of showing that the exclusion exists and that the facts come within it.” *Nationwide*, 136 Ga. App. 671, 676 (1975) (citing *Darby v. Interstate &c. Ins. Co.*, 107 Ga. App. 409 (1963) and *S. Guar. Ins. Co. v. Duncan*, 131 Ga. App. 761, 764 (1974)). In short, disputes regarding insurance contracts tend to favor the insured, especially where there is any ambiguity in the document.

NCCI Rule 1(F)(2)

4.

Here, both Parties agree that the interpretation of NCCI Rule 1(F)(2) is of central importance to resolving the present dispute and that reference to it alone⁶ can resolve the issue of whether premium overpayments discovered during an audit (1) date back to the beginning of the current policy year, or (2) date back to the inception of the policy. The language of NCCI Rule

⁶ Valley Mechanical asserted alternative theories of recovery, such as unjust enrichment. However, it is unnecessary to reach those theories in this case.

1(F)(2) is as follows: “Corrections in classifications that result in a decrease in premium, whether determined during the policy period or at audit, must be applied retroactive to the inception of the policy.” To interpret the meaning of “the inception of the policy,” the Court looks to the all relevant provisions in the NCCI Manual and the Hartford Policy. *See Nationwide*, 136 Ga. App. at 675 (interpret a part in light of the whole).

NCCI Manual treats increases in premiums differently from decreases in premiums

5.

The NCCI Manual treats undercharges in premium differently from overcharges. The court in *Home Insurance Co. v. Sunrise Carpet Industries, Inc.*, basing its decision on a reading of the NCCI Manual and a similarly-worded insurance policy, stated in dicta that a post-expiration policy audit could “change the classifications and decrease the premium” retroactively, although it could not increase a premium. 229 Ga. App. at 271-72. Under the NCCI Manual, corrections in classifications that result in retroactively-increased premiums are carefully circumscribed and depend on the policy day on which the classification error was discovered. In the case of increased premiums, no mention is made of classification errors that are discovered at an audit, because audits frequently occur after the conclusion of the policy term, and the NCCI rule does not contemplate retroactive increases in premiums due to classification errors after completion of the policy term. In fact, NCCI Manual Rule 1(F)(3) specifies that if “effective during the last 90 days of the policy term . . . the correction is applied only to a renewal policy,” i.e., going forward.

6.

By contrast, NCCI Manual Rule 1(F)(2) specifies that, where premium refunds are at stake, regardless of whether a classification is discovered at an audit or during the policy period,

the change in classification will go back to “the inception of the policy.” The dispute is over the meaning of the phrase “the policy”: whether it refers to only a currently-active policy or whether it refers to the policy containing the classification error. In context, it is unreasonable to interpret “the policy” in the former manner, because the sentence itself explicitly states that the classification error may have been discovered either during the policy period or an audit. As the Hartford Policy makes clear, audits often occur after the conclusion of a policy period. Hartford explicitly retains the power to audit the insured for up to three years, which would encompass three past policy periods. As there is no time limitation placed on audits initiated by either a rating organization or the insured (as contrasted with the three-year limit for the insurance company), the NCCI Manual provision establishes that whenever an audit reveals an overpayment due to a mistaken classification, a refund will be owed back to the inception of the policy, not just the current policy year. Furthermore, the Hartford Policy clearly states, without qualification or restriction, that it will refund any overcharges resulting from misclassifications.

7.

Hartford argues that because Rule 1(F)(3), dealing with corrections in classifications that result in an increase in premium, does not “envison actions outside of current applicable policy periods,” Rule 1(F)(2), dealing with corrections in classifications which result in a decrease in premium, must also be limited to current policy terms. *Post-Hearing Brief of Petitioner*, filed March 20, 2014. This reasoning is unpersuasive. By specifically limiting the recovery of additional payments to the current policy period in the case of increased premiums but not doing so in the case of decreased premiums, the rule demonstrates that no such limitation applies where the insured is owed a refund. *See Couch v. Red Roof Inns, Inc.*, 291 Ga. 359, 363 (2012) (can use the “principle of ‘*expressio unius est exclusio alterius*’—“the express mention of one thing

excludes all others” to interpret sequential provisions). This interpretation is in line with Georgia law favoring the insured. *See, e.g., Cincinnati Ins. Co.*, 153 Ga. App. at 294.

Ambiguity is resolved in favor of Valley Mechanical


8.

Although the NCCI Manual can only reasonably be read to require refunds dating back to policy’s inception, which was the 2005-2006 policy year, the law is clear that even if this Court found the language to be ambiguous, any ambiguities in the policy are to be “strictly construed against the insurer as the drafter of the document . . . and insurance contracts are to be read in accordance with the reasonable expectations of the insured where possible.” *Home Ins. Co.*, 229 Ga. App. at 271 (internal citations omitted). Here any ambiguity in the meaning of “the inception of the policy” is interpreted in favor of Valley Mechanical to mean the policy period in which there was an error in classification. In addition, based on the language in the Hartford Policy and the NCCI Manual, it would have been reasonable for Valley Mechanical, the insured, to expect that any overcharges based on misclassifications would result in a refund, regardless of when the error occurred.

IV. DECISION

In accordance with the foregoing Findings of Fact and Conclusions of Law, Hartford is required to apply the correct classification codes and refund any resulting overcharge back to inception of the 2005-2006 policy year. The decision of the Workers’ Compensation Appeals Board is hereby **AFFIRMED**.

SO ORDERED, this 7th day of May, 2014.



KIMBERLY W. SCHROER
Administrative Law Judge