

1948

# The State Insurance Fund v. Thomas L. Dykes, The Industrial Commission of Utah, and Intermountain Service Bureau, Inc. : Brief of Defendant

Utah Supreme Court

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Grover A. Giles; Attorney General; C. N. Ottosen; Assistant Attorney General;

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# IN THE SUPREME COURT OF THE STATE OF UTAH

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THE STATE INSURANCE FUND,  
administered by the Commission of  
Finance of Utah,

*Plaintiff,*

vs.

THOMAS L. DYKES, THE INDUS-  
TRIAL COMMISSION OF UTAH,  
and INTERMOUNTAIN SERV-  
ICE BUREAU, INC., doing busi-  
ness as Merchants Police,

*Defendants.*

Case No.

7196

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## Defendant's Brief

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**FILED** GROVER A. GILES,  
Attorney General

NOV 9 - 1948

C. N. OTTOSEN,

*Assistant Attorney General*

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CLERK, SUPREME COURT, UTAH

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## Defendant's Brief

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### STATEMENT OF FACTS

The Defendants accept the statement of facts as given in the Plaintiff's Brief on file herein, as correct but deem it advisable to amplify said statement as follows in order to make it complete.

The policy of insurance, involved herein, was issued by the Plaintiff to J. Martin Stock, dba "Merchants Police" effective August 20, 1946 and continuing until June 30, 1947 (Tr. 63, 64). Mr. Stock changed the title of his business establishment from a privately owned concern to a corporation about July 1, 1947 (Tr.

80) but Mr. Stock still remained an active participant, was president of the new company and everything remained the same except the fact of incorporation, even the name of "Merchants Police" continued to be used (Tr. 55, 80, 81). The employment of the applicant, T. L. Dykes, by the new company, known as the Intermountain Service Bureau, Inc., was in all material respects by the same people and for the same purposes as though he had been employed by J. Martin Stock personally. The only major change in the new company was the change of name. In actual contacts and in actual business, the name of "Merchants Police" was not changed but was continued in use. The Utah State Insurance Fund, the insurance carrier in this case, insured J. Martin Stock, operating as "Merchants Police" and when this policy lapsed they made no effort to advise the Industrial Commission of such lapsation. The Utah Insurance Fund received an order which was issued by the Industrial Commission to all insurance carriers, demanding that a notice be given to the Industrial Commission of policy cancellations, based on failure to pay premiums; but in spite of this order, the State Insurance Fund officers elected to ignore the Industrial Commission's order (Tr. 70 to 73).

## QUESTIONS INVOLVED

1. Was the Utah State Insurance Fund policy of workmen's compensation cancelled when the employer incorporated and changed its name?

2. Was the order or motion of the Utah State Industrial Commission binding on the Utah State Insurance Fund so as to continue the Funds Liability over the period of time necessary to compensate applicant Dykes for his injuries and losses?

## ARGUMENTS

### ARGUMENT ON QUESTION NO. 1

As far as technical legal entities are concerned, it is apparent that the only insurance policy involved in this case was written on J. Martin Stock dba "Merchants Police." At the time the policy was written, Mr. Stock was no doubt the sole owner and operator of said concern. It is also apparent that the technical employer of applicant Dykes was the corporation, namely the Intermountain Service Bureau, Inc. Therefore, a serious question arises as to whether or not the difference in these two legal entities is sufficient or should be allowed to exclude applicant Dykes from any recovery because of injuries or damage; whether or not this situation should permit these persons or any persons or combination of persons in like situations to accomplish such a change of ownership or a change of name so as to be able to avoid, whether intentionally performed or not, their obligations under the Workmen's Compensation Act. Even though a separate concern was organized in this case, it is still important to determine who the real employer was and whether the mere change of name or the creation of a new entity,

with the same ownership and management, would of itself relieve the real employer of liability (*Melhus vs. Johnson and Sons*, (Minn.) 247 N. W. 2). In the case now before the court, Mr. Stock was the real owner and employer of all help in the original company. He continued as the president and was undoubtedly a prominent factor, if not the full owner and manager of the new company. There is no evidence in the record to show the respective interests of any stockholders in the new company. Much was made of the fact that one Earl Lowry was General Manager of the new company and hired the applicant Dykes (Tr. 57, 58) but Mr. Lowry's interest, whether as owner or mere employee in the new company, is not revealed nor was it shown at any time in the record that the new corporation had any assets. It was disclosed at the hearing, however, that the new company continued with the same type of business, continued under the same name (*Merchants Police*) with no change in address, telephone number or telephone listing and with little or no change in letter heads or in methods of operation. In fact, it was specifically admitted that the only difference between the old and the new company was the fact that certain types of investigations had been added in the operations of the new company (Tr. 55, 80, 81).

It is a well accepted principle of law that the corporate entity of an organization will be disregarded by the courts when justice requires it (See 13 Am. Juris. pg. 160, sec. 7; *Fletcher on Corporations*, vol. 1, sections 41, 44 and 45; *Whipple vs. Industrial Commission*



(Ariz.) 121 Pac. (2) 876; Horovitz on Workmen's Compensation Law, pg. 229). No corporation should be allowed to cover the true substance of an existing situation so as to render an undue advantage to one of the parties and permit loss and damage to another, especially if the damaged party is without fault. Certainly applicant Dykes, in this case, had a right to rely on the fact that compensation insurance was being supplied and there is no fault on his part that any question has arisen as to whether or not he was properly covered and protected by workmen's compensation insurance. The Defendants concede that in an ordinary case, no fire, automobile or liability policy is assignable or transferable to another owner because of our rules that such policies are personal. The Defendants do not dispute the cases quoted by the Plaintiff on this rule and further concede that if the case before the court is a true, and in all respects a case of an assignment of a liability policy from one owner to another, without the approval of the insured, then the Intermountain Service Bureau, Inc., as the new owner of the Merchants Police business, would not be covered under the original policy as originally issued. The Defendants submit, however, that in reality there was no transfer of the business nor was there a change of "ownership or operation"; that the mere change of entity should not be allowed as a means of working an injustice in this case; and that the case before the court is not a true case of assignment of a policy and a transfer of a business, insured by said policy. Our problem is really a question as to whether

or not the "ownership and operation" of the Merchants Police remained the same to such an extent that the policy of workmen's compensation, written herein, was not automatically cancelled as a result of the cancellation clause contained in the insurance fund policy. We call the court's attention to the said cancellation clause in the State Insurance Fund policy, which reads as follows:

"If the employer shall *transfer* his or its *ownership or operation* of the business insured by this policy, this policy shall automatically become cancelled." (Italics ours)

A true assignment of a policy involves the actual placing of a new assignee in the position of the former insured. It involves the actual switching of one person for another and a changing of the personalities involved. It is substantially the act of transferring all of some valuable interest or property to another person (Johnson vs. Brewer, Ga. 68 S. W. 590, 591; Ormond vs. Connecticut Mutual Life Insurance Co., N. C. 58 S. E. 997, 998), or as may be more graphically explained, relative to fire insurance policies, there must be a parting from the property interest so that the former owner, after the transfer, has no further interest or control (Couch Encyclopedia of Insurance Law, vol. 6, section 1450d, pgs. 5139 and 5142). In other words, the rule against an assignment because of the personal element being involved, serves no purpose whatsoever where there is no change of personalities or where the identity of the original insured remains the same in the new company.

This is because the issuance of any policy depends upon the character of the insured employer as to his integrity, prudence, caution and ability in the management and operation of his business and in the selection of his employees. This emphasizes the Defendants' position that there is in reality no transfer of business and no assignment of the policy involved in this case. In the original Merchants Police under Mr. Stock as private owner, it was his interest that was the subject of the insurance and the insurance policy did not automatically cancel on the incorporation of the new company because it was still this identical interest and still Mr. Stock's interest that remained predominant and which interest the policy continued to protect because of Mr. Stock's continued relationship in the new company. In order for the insurance fund policy to cancel itself, in accordance with its own terms, as quoted above, the insured employer had to "transfer", "ownership or operation" of his business. The Defendants submit that there is not a single word of evidence in the record revealing the least intent or actual accomplishment of any part of the "transfer" of any "ownership or operation." On the contrary the evidence introduced does reveal that outside the mere change in name, everything remained the same including the "ownership and the operation" and that there was no suggestion of any "transfer," as required in the quoted cancellation clause before it could become operative.

The Defendants have been unable to locate any cases exactly in point where a change occurred from an

independently owned private business to a corporation but the Defendants have located several cases where changes were made in partnerships. These cases involve changes in personnel and changes of name, similar to the case before the court. The courts held that these slight changes involved no "assignment to strangers" but involved a retention of substantially the originally insured parties and that insurance policy clauses voiding policies where real assignments are involved were not operating in such cases. (See Couch on Encyclopedia of Insurance Law, vol. 6, section 1450p and cases cited thereunder; also Wilson vs. Genesee Mutual Insurance Co., N. Y. 16 Bart. 511, 512). As a first premise, the Defendants maintain that the Plaintiff's policy did not automatically cancel itself when the corporation was formed in July of 1947; that the clause quoted above, and as worded, does not apply to the facts in this case for the reason that the clause in question applies only where an actual transfer of the business and property to an actual third party or stranger results and where there is an actual change in ownership or operation. Such a transfer did not occur for the reason that the business continued with no changes as has been set out above. Even though the incorporation of an organization does technically create a new entity, the Defendants feel that their position is further justified in the fact that the law says no such move should be permitted to work injustices upon others. Such a move, if supported by the courts would permit the hiring of new men under a new company name, without protection to

them, which is exactly what has happened in this case. There is no evidence in the record of the financial standing of this new company, and where corporations have no assets and are excused by the mere change of name from liability on policies of workmen's compensation, the final results to the employee are obvious. We maintain the employee needs better protection, that the law grants it to him and he is protected under the rules as given herein. If the creation of a corporate entity is all that is needed to avoid responsibilities and to work injustices, a great field of fraud and disregard of human rights would have legal sanction. Our courts, however, have long been exercising the right to look beyond the entity of a corporation to see that those evils mentioned are not accomplished. Our authorities in support of these arguments have been quoted above. Again, in conclusion on argument No. 1, we call attention to the fact that the liability policy in question should not be declared cancelled as of the time of the incorporation of the new company.

## ARGUMENT ON QUESTION NO. 2

The Defendants first premise, as indicated above, is to the effect that the liability policy did not automatically cancel and we now hope to support the argument that because of the failure of the Insurance Fund officials to comply with the law and the duly adopted orders of the Industrial Commission of Utah, the coverage of the insurance policy in question, continued over to and included the time necessary to protect applicant

Dykes and to make the Plaintiff liable for Mr. Dykes' injuries and losses in accordance with its policy and therefore, also liable in accordance with the decision of the Industrial Commission of Utah, which decision is the basis of this appeal.

Up until May 13, 1947, sections 43-3-36 and 43-3-37, U.C.A., 1943 had been in force and effect but by a mere inadvertence, said sections were left out of the new insurance code passed by the 1947 legislature (Chap. 63 Laws of Utah, 1947) and were thereby repealed. Section 43-3-36, being the important section in this case, is herewith quoted and reads as follows:

“Every insurance company authorized to transact the business of workmen's compensation insurance and occupational disease insurance must write and carry all risks or insurance for which application is made to it, which are not prohibited by the provisions of Section 43-3-22, and any such insurance company assuming such a risk shall carry it to the conclusion of the policy period unless canceled, either by agreement between the industrial commission and the employer or in case of nonpayment of premium by thirty days' notice by such insurance company to the industrial commission and the employer.”

Through the above entitled section, before its repeal, the Industrial Commission of Utah was able to compel all insurance carriers to let the commission know when a policy of insurance lapsed for nonpayment of premium or when a cancellation was desired or accomplished. By this law and this system the Industrial Com-



mission performed a very worthy function and a great service to the working man by standing as a watchman and protecting the employees on their liability coverage to which they are entitled by law.

With the repeal of this section, which in the history of the Legislature was actually left out inadvertently and for no other purpose whatsoever, the Utah Industrial Commission was left without the direct authority sufficient to continue to perform that particular service and to know when liability coverage lapsed and employees were not being protected. Very shortly after the repeal, events occurred showing that a lot of serious losses to employees were actually resulting and would continue to result if some steps were not taken to replace said law through some form of authorized action. As a result of the Industrial Commission's effort to perform the service referred to, to perform their obligations relative to keeping all employees insured and to perpetuating, as far as was legal, the benefits of this repealed section, an order or rule was duly adopted by the State Industrial Commission on October 14, 1947 and copies thereof were sent to the Plaintiff and to all other insurance carriers in the state of Utah, again requiring that the provisions of these sections be followed and making it necessary, particularly, that notice be sent to the State Industrial Commission of any policies being cancelled for nonpayment of premium. For reasons of time and space, said order is not quoted herewith but is hereby incorporated by reference and is to be found in the transcript of record

on page 89. A copy of this order or motion was sent to and was received by the Plaintiff and no objections were ever raised by said Plaintiff relative to the requirements of said order until the hearing on this case (Tr. 70 to 73).

The Defendants' first observation in relation to said order and the provisions of the sections in question before they were repealed is to the effect that these sections were in force and still effective up to and including May 13, 1947 (see Chap. 63, Laws of Utah, 1947). It is further to be noted that the policy of insurance issued by the Plaintiff to J. Martin Stock dba Merchants Police was effective beginning 12:01 A.M., August 20, 1946 (Tr. 63). This means that the provisions of sections 43-3-36 and 43-3-37 were automatically included and were part of the policy of the Plaintiff which was issued to, and covered the Merchants Police and that from this standpoint, alone, the Plaintiffs' own policy, during all times herein, has made the Plaintiff responsible for the giving of a 30 days notice to the Industrial Commission of any intent to cancel this policy or any other policy for nonpayment of premium. It is a well established principle that the statutes of a state, applicable to any contract of insurance in force at the time of the making of a contract, forms and becomes a part thereof and must be read in construing the policy and said statute controls in case of conflict (see 44 C.J.S. on Insurance, section 302; also 29 Am. Juris. on Insurance, section 108). This principle of law, alone, makes the Plaintiff liable to the applicant Dykes under



the terms of its own policy. The Plaintiff makes a point of the fact that the Utah State Insurance Fund is not a company, that the law and the commissioners' order specifies insurance companies as those required to give notice and, of course, Plaintiff maintains that the insurance fund is not a company and is, therefore, not required to give said notice. Insurance carriers go by various names, such as companies, associations, underwriters, reciprocals and also by the name of insurance and assurance and other names so that the use of such a distinction to avoid obligations under such provisions as are here involved has never been supported by the law and should not be supported. In order to give purpose to the law there can be no doubt but that the term "insurance company" as in the sections above quoted, applies to all insurance carriers. The Utah Insurance Fund is no doubt properly classified as a state institution, but the law is further emphatic about the fact that state institutions must also abide by the law. State institutions should set examples to the public and certainly it must be said that neither the purpose of such a law nor the good that results nor the harm that can be done by either observing or failing to observe such a law is lessened or changed merely because a state institution is involved. The Defendant submits that the Plaintiff is and should also be among those required by the law or the order to observe its provisions.

Even if the Defendants should be left to their rights, if any, under the order or motion of October 14, 1947, we desire to point out the following. The Indus-

trial Commission has no powers to legislate but they do have the power necessary to accomplish the objects of the State Workmen's compensation Act and to accomplish all the objects which are incidental to the powers already granted to them (Utah Copper Co. vs. Industrial Commission, 57 Utah 118). Further, the 1947 Legislature, effective as of May 13, 1947, enacted section 43-19-13 of Chap. 63, Laws of Utah, 1947, which section reads as follows:

“All insurance companies writing workmen's compensation insurance and occupational disease insurance in this state, and the Commission of Finance in connection with its administration of the State Insurance Fund, shall be subject to the rules and regulations of the Industrial Commission. Said Commission may provide the methods to be used by them in the payment of compensation and benefits. The Industrial Commission may provide uniform rates to be charged by such companies but such rates need not be uniform with the rates fixed for the State Insurance Fund.”

This section clearly puts the Plaintiff subject to the rules, regulations and orders of the Industrial Commission so long as the Industrial Commission stays within the limitations set out by our Supreme Court in the Utah Copper case, *supra*, and the Defendants submit that certainly the purposes of the order is within the purposes of the Utah Workmen's Compensation Act. The practice of notifying the Industrial Commission or comparable commissions in other states, of an inten-

tion to cancel a liability policy is well accepted by most, if not all states and courts. This practice has shown itself to be a very essential factor to the more complete performance of the Industrial Commission's function in the supervising of workmen's compensation laws.

On page 10 of the Plaintiff's Brief, one Schneider on Workmen's Compensation is quoted out of his Vol. 2, of said works, Section 468, page 1588. The Plaintiff did not complete that author's quotation and the Defendants submit the balance, which reads as follows:

“The provision of an insurance policy for cancellation by sending to an employer at his last known residence, a notice by registered mail 10 days prior to the time such cancellation takes effect, and at the same time giving notice of cancellation to the compensation commission, as well as the New York statutory provisions for cancellation are met, where a registered letter has been sent and has arrived at its proper destination 10 days prior to the date of cancellation, although the name of the employer and the name of the town are misspelled, and although the employer does not actually receive the notice, where he has ignored notices that a registered letter is ready for delivery, and it is returned to the company nearly three weeks later; and where the commission was likewise notified of the cancellation at the same time.”

See also 107 A.L.R., 1519.

## CONCLUSION

In conclusion Defendants submit that there was no automatic cancellation of the employer's policy in this case for the reasons given herein, that the plaintiff gave the new company until Nov. 12, 1947 (one day after applicant Dykes' first injury) to pay the premium and before the policy would lapse. Further, the failure of the Plaintiff to abide by the order of the Industrial Commission makes said Plaintiff liable for applicant Dykes' losses in accordance with the decision and award of the Industrial Commission. That the Plaintiff is liable under the law and the order of the Commission because they are subject to the Commission's orders and also because the law in question was in force when said policy was issued. Defendants request that the award and decision of the Industrial Commission be sustained.

Respectfully submitted,

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