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NO. A12-1654

State of Minnesota  
In Court of Appeals

In the Matter of Continental Hydraulics, Inc.

Continental Hydraulics, Inc.,

*Relator,*

v.

Minnesota Department of Employment  
and Economic Development,

*Respondent.*

RELATOR'S BRIEF AND APPENDIX

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The appendix to this brief is not available for online viewing as specified in the *Minnesota Rules of Public Access to the Records of the Judicial Branch*, Rule 8, Subd. 2(e)(2).

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## STATEMENT OF THE CASE

This appeal presents a very narrow and atypical appeal of an unemployment insurance (“UI”) decision. It is not an appeal about whether an employee deserves unemployment benefits, but about how a company’s UI tax rate is determined. Generally speaking, an existing employer’s UI tax rate is a product of its “experience rating history” and a base tax rate. Minn. Stat. § 268.051, subd. 2. For new companies, tax rates are calculated under a different provision that generally result in lower tax rates. *See id.*, subd. 5. The issue in this case is how the UI tax rates should be calculated for a new company, Continental Hydraulics, Inc. (“Cont. Hydraulics”), when it acquired a portion of an existing company’s business, namely the hydraulics business of Continental Machines, Inc. (“CMI”).

Minnesota, like most other states, have long had state statutes that call for transfer, full or partial, of experience rating when an employer acquires all or a part of another employer’s business and “there is 25 percent or more common ownership.” *See* Minn. Stat. § 268.051, subd. 4(b) (“Subdivision 4(b)”). These provisions calling for experience transfer are designed to prevent “SUTA dumping”<sup>1</sup> and have long been required by the federal social security laws. 42 U.S.C. § 503(k).

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<sup>1</sup> Depending on circumstances, “SUTA” may stand for the federal law that created the UI program, the State Unemployment Tax Act, or “State Unemployment Tax Avoidance”. *See* U.S. Dep’t of Labor Program-Letter No. 30-04, *SUTA Dumping-Amendments to Federal Law affecting the Federal-State Unemployment Compensation* (often referred to as “Program Letter 30-04”) Sec. 3 (August 13, 2004), available at [www.ows.doleta.gov/dmstree/uipl/uipl2k4/uipl\\_3004.htm](http://www.ows.doleta.gov/dmstree/uipl/uipl2k4/uipl_3004.htm), Appellant’s Appendix 1. “SUTA dumping” generally refers to UI tax evasion schemes where shell companies are formed and creatively manipulated to obtain low UI tax rates. *Id.* When a low rate is obtained by the shell company, payroll from another entity with a high UI tax rate is

But the specific issue in this case is a phrase that was added to Subdivision 4(b) in 2005 in order to comply with a federal mandate. Specifically, in 2004 the United States Congress recognized a large loophole in the existing anti-SUTA dumping laws. At the time, state and federal law called for a transfer of UI experience rating history from a predecessor company to a successor company if “there is 25% or more common ownership.” *See* Minn. Stat. § 268.051, subd. 4(b) (2004); *see also* 2005 Minn. Law c. 112 art. 1 sec. 7 (amending same). This language failed to address a form of SUTA dumping in which parties were creating a new company with new ownership in name only (*i.e.* new ownership was a related party such as a spouse or child) and then transferring all or a part of the assets of the existing company to the shell company while in all reality operating and controlling both entities. To address this ill, the federal SUTA Dumping Prevention Act of 2004 (“SUTA Act”) required states to add language requiring a transfer of experience rating where “substantially common management and control” remained after the asset transfer. Pub. L. No. 108-295, § 2, 118 Stat. 1090, 1090; *see also* Program Letter 30-04, attachment 1 (Answer to Question 4).

In 2005, Minnesota added the phrase “or there is substantially common management or control” to Subdivision 4(b).<sup>2</sup> *See* 2005 Minn. Laws ch. 112, art. 1, sec. 7. Since that time, Subdivision 4(b), and for this case clause 4(b)(2), provides that a portion of the experience rating history of a predecessor employer is transferred to the

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shifted to the shell company with the lower rate. The entity with the higher rate is then “dumped.”

successor employer when the successor acquires a portion of the predecessor and “there is 25 percent of more common ownership or there is substantially common management or control between the predecessor and successor . . .” Minn. Stat. § 268.051, subd. 4(b)(2) (2012) (emphasis added).

Here, the issue arose when CMI, which is primarily a tooling manufacturing business, decided to sell its hydraulics business on the open market in order to raise capital, a process that garnered multiple proposals and multiple bidders. Ultimately, an Italian company, Duplomatic Oleodinamica (“Duplomatic”), won the right to purchase the hydraulics business. At the time, Duplomatic was an operating hydraulics company that was marketing in Europe and Asia, but looking to expand into the US market. Duplomatic then formed Cont. Hydraulics to acquire certain assets of CMI (*i.e.* its hydraulics business) and would then look to take advantage of the Continental name. To be clear, Cont. Hydraulics was and always has been wholly owned by Duplomatic and, controlled and managed by people who report to and are directed by Duplomatic, and Duplomatic alone.

Despite the fact that Cont. Hydraulics was created to fulfill a legitimate asset acquisition and is wholly independent of CMI, the Department of Employment and Economic Development (“DEED”): 1) concluded that the experience rating history of CMI should transfer to Cont. Hydraulics under the theory that there is substantially common management and control between the two employers (it is uncontested that there

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<sup>2</sup> As stated in the 2005 session law, the language was added to comply with the federal SUTA Act. *See* 2005 Minn. Law c. 112 art. 1 (introduction).

is no common ownership); 2) recalculated Cont. Hydraulics' UI tax rate using CMI's experience rating history; and 3) imposed a penalty on Cont. Hydraulics for allegedly not providing information required when there is common management or control between two companies.

Cont. Hydraulics filed an administrative appeal of all three determinations because there is not, and never has been, a single point in time of, commonality in ownership, management, or control between Cont. Hydraulics and CMI. The administrative appeal was eventually heard by Unemployment Law Judge Scott Mismash ("ULJ"). On February 17, 2012, the ULJ issued his Finding of Fact and Decision ("Decision").

Although the evidence conclusively demonstrated that Cont. Hydraulics was a company formed and wholly owned by the operating, Italian hydraulics company, Duplomatic, with no shared management or control, the ULJ concluded there was substantially common management or control between CMI and Cont. Hydraulics based on the following reasoning:

[I]t appears the final decision making authority changed. However, despite Wilkie's "hands on" activities in CMI, he is physically located in Chicago and received input from his local managerial staff. Of those people, Horihan is now the CEO of CHI and Heist is the CFO. They report to Maddalon, who is not situated locally. Furthermore, Horihan's direct reports were also employed at CMI. While there has been change at the very top and key people have been shuffled, the preponderance of the evidence is that the ultimate decision makers [sic] for CMI (hydraulics division)<sup>3</sup> and [Cont.

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<sup>3</sup> It should be noted, while the assets acquired have often been referred to as CMI's "hydraulics division," CMI operated as one company that made and sold machine tooling and hydraulic equipment. T. 19. So while there was internal distinctions and separate employees that dealt

Hydraulics] receive/received their input on business decisions from essentially the same people.

Appellant's Appendix ("AA") 21–22.

The Decision does not: 1) address the fact that Cont. Hydraulics' acquisition of CMI's hydraulics business was a market transaction that resulted in two wholly independent and unrelated companies; 2) include any statutory analysis of Subdivision 4(b); or 3) find that a single person was ever simultaneously employed by, had management of, or control over both Cont. Hydraulics and CMI for so much as a single instant.

Having erroneously concluded that there is substantially common management or control between CMI and Cont. Hydraulics, the ULJ confirmed DEED's tax rate determination for Cont. Hydraulics. The ULJ also concluded that because there is substantially common management or control, Cont. Hydraulics was required to provide information to DEED and, because it had not, DEED had been properly assessed a penalty.

Cont. Hydraulics filed a request for reconsideration of the Decision. On September 17, 2012, the ULJ issued its final order confirming the Decision. This appeal followed.

### **STATEMENT OF THE FACTS**

CMI began as a machine tool production company in the late 1920s and continues its machine tooling business today. Hearing Exhibit ("Ex.") 9; Hearing Transcript ("T.")

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with hydraulics versus machine tooling, CMI operated as a single entity and single employer.

19. At all relevant times, Mike Wilkie and his sister owned 100% of CMI.<sup>4</sup> T. 12.

Wilkie is CMI's CEO and chairman. T. 20, 32. He exercised active control over CMI and had to approve "[a]ny major issue regarding major purchases, hiring, [and] layoffs."

T. 20. In all senses of the word, Wilkie controlled and controls CMI T. 20. In addition to Wilkie, management over CMI was exercised by company president Michael Johnson.

T. 32. Although there were other "managers," the only other executive level position was vice president and treasurer Gary Heist. T. 14. The "management structure" of CMI consisted of "the president and CEO which was Mr. Johnson and Mr. Wilkie." T. 20.

As the evidence shows, in 2009, CMI needed to raise capital for its core business and began the process to identify saleable assets. T. 22. Since the hydraulics business was not related to the core business, it was identified as an asset with value on the open market and a broker was hired to market the sale. *See* T. 22; Exs. 2 and 9. The broker was able to identify three potential suitors. T. 22. Eventually, Cont. Hydraulics' parent company, Duplomatic, was the successful bidder for CMI's hydraulics division. T. 22. Cont. Hydraulics was then created and completed the acquisition of CMI's hydraulics business.

From Cont. Hydraulics creation in April 2011 to the present day, Duplomatic has always been the sole owner of Cont. Hydraulics; no other person or entity owns any

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T. 19.

<sup>4</sup> The ULJ claimed to be in possession of information that Heist owned 33 percent of CMI. T. 12. It is unclear what information the ULJ had to support this claim, but Heist testified he was not an owner. It now appears that neither DEED nor the ULJ assert that Heist has any ownership in CMI.

shares in Cont. Hydraulics. T. 13. Duplomatic is and was an operating hydraulics company whose majority shareholder is European based AXA Private Equity. T. 13. Prior to the asset purchase, Duplomatic manufactured and sold hydraulic valves throughout Europe and Asia, and has joint ventures in China and Brazil. T. 18. Duplomatic created Cont. Hydraulics and purchased the hydraulics business from CMI in order to expand its existing hydraulics business into the United States. T. 18. The transaction was an arm's length, negotiated transaction that involved M&A advisor Fineruop Soditic, the law firm Dewey & Leboef, the CPA firm Studio Legale e Tributario, and KPMG Transaction Services. Ex. 9. An international press release announced the acquisition of CMI's hydraulics business and Duplomatic's plans to enter the US market. Ex. 9.

At all times since its creation, Cont. Hydraulics has operated and conducted itself as a wholly independent business with a sole shareholder, Duplomatic. Since its inception, Cont. Hydraulics has been controlled by president and chairman Maddalon,<sup>5</sup> who in turn answers to the chairman of Duplomatic. T. 17. There has been no suggestion that Maddalon or any officer of Duplomatic has ever had any involvement with CMI. *See* T. 18. Cont. Hydraulics prepared its own handbooks and policies. T. 22. Neither Duplomatic, Cont. Hydraulics, nor any of Duplomatic's shareholders has ever held any ownership interest in CMI. T. 12. Likewise, CMI's owners, Mr. Wilkie and his sister, have no ownership stake in Cont. Hydraulics or Duplomatic. T. 12. Neither CEO

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<sup>5</sup> Maddalon's titles follow the European model. T. 17, 31 In American parlance, his duties are more consistent with CEO.

Wilkie, company president Johnson, CMI's board of directors, nor any other "decision maker" at CMI has ever had any involvement with Cont. Hydraulics. T. 23.

In short, Cont. Hydraulics is not a shell company of CMI, but was formed and is operated by a pre-existing European hydraulics company as a way to provide the European company with a presence in the lucrative United States market. Ex. 9. In the words of Maddalon:

As a result of this acquisition, [Diplomatic] has entered the US market – the biggest in the world – through a very well known brand in the sector and a firm established network of distributors. The integration strategy between the two companies aims to expand the hydraulic component division's catalogue, by adding [Diplomatic] products, and to launch joint sales initiatives aimed at maximizing the potential synergies arising from the combination.

Ex. 9.

With the sale of the hydraulics business, CMI terminated employment of all 81 employees that worked in the hydraulics business. T. 20. That included one, and only one, member of CMI's executive group, vice president and treasurer Heist, who is now CFO of Cont. Hydraulics. T. 15. All 81 of CMI's former employees then accepted offers of employment from Cont. Hydraulics. T. 20. Even when Heist and other current employees of Cont. Hydraulics were employed by CMI, their involvement in decision making was limited: they could offer input to Wilkie and Johnson. T. 20 But Wilkie and Johnson made all final management and control decisions. T. 20. Of course, having been terminated from CMI, none of the 81 former employees has had input of any kind into the operation, management or control of CMI since termination. T. 20.

The persons with management and control of Cont. Hydraulics, namely Maddalon and CEO Dale Horihan, have no existing relationship with CMI and never had management or control of CMI. Duplomatic's chief executive officer, Roberto Maddalon, is the chairman and president of Cont. Hydraulics. T. 17. He continues to hold all titles and reports to Duplomatic's president. T. 18. Maddalon was the existing CEO of Duplomatic at the time of the acquisition. T. 18. He is not simply a figurehead for Cont. Hydraulics, but has been actively involved in shaping Cont. Hydraulics. T. 18. On the other hand, when it comes to CMI, Maddalon has had "no decision making management control or otherwise." T. 27.

The second in charge at Cont. Hydraulics is Horihan. He has full day-to-day, or "local," management of Cont. Hydraulics. T. 15. Horihan had "no role in major decisions making for [CMI]." T. 27. Rather, his function with CMI was marketing and sales of hydraulics products. T. 15. The only other executive level employee at Cont. Hydraulics is CFO Heist. T. 16.

As is the case with any company, Cont. Hydraulics has other "managerial staff," but the "management"<sup>6</sup> of Cont. Hydraulics was Maddalon, Horihan and Heist. T. 16. Maddalon has never been employed by CMI; Horihan and Heist were both terminated from CMI before beginning their respective roles with Cont. Hydraulics. T. 19–20.

Within a week after Cont. Hydraulics completed the acquisition of CMI's hydraulics business (late April 2011), it completed DEED's online forms. T. 21. On

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<sup>6</sup> As discussed below under Heading II, "management" of a corporation refers to executive officers who are responsible for its operation.

August 5, 2011, DEED sent Cont. Hydraulics a letter requesting additional information. Ex. 5. After receipt of the letter, CFO Heist called DEED and asked what information DEED was looking for. T. 22, 24. Heist confirmed that Cont. Hydraulics was not part of another company, but was a brand new company. T. 22. He again went to DEED's online website and added "everything that [he] could." T. 24.

On November 10, 2011, DEED appears to have sent a letter to Cont. Hydraulics requesting additional information. Ex. 4. But no one at Cont. Hydraulics can recall seeing the letter. T. 24. The November 10th letter begins, "A review of your Minnesota Unemployment Tax account indicates that you are reporting wages for employees previously reported by [CMI]." Ex. 4. The letter goes on to state, "It is the intention of [DEED] that the tax experience rating history of [CMI] be transferred to [Cont. Hydraulics] as of 4-21-2011." *Id.* The letter ends with a request that Cont. Hydraulics provide acquisition information. *Id.* It is uncontested that Cont. Hydraulics did not provide additional information in response to the November 11, 2011 letter. Ex. 8(1) (stating that as of December 20, 2011 DEED had "received no response to our letter").

On December 20, 2011, DEED issued its Determination of Succession concluding that Cont. Hydraulics was "a successor to [CMI] effective 04/21/2011" and that it would "receive a partial transfer of experience rating history from [CMI]." Ex. 1. DEED recalculated Cont. Hydraulics' 2011 UI Tax Rate at 8.34% by transferring an experience rating of 7.84% from CMI.<sup>7</sup> Ex. 1.

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<sup>7</sup> As discussed below in Section III, without the experience transfer, Cont. Hydraulics' tax rate as a new employer would be approximately 3%. Under either case, there would also

It should be noted that CMI's 7.84% experience history rating for 2011 is attributable, in large part, to the Great recession. By statute, the 2011 experience history rating would have been set on or before December 15, 2010 and been based on a "wage detail reports for the 12 calendar months ending the prior June 30." Minn. Stat. § 268.051, subd. 3. In other words, CMI's 2011 experience history rating would be based on wage detail reports from June 2009 through June 2010. During this time, CMI's experience rating history would also have been effected by its inclusion in DEED's "Shared Work Program," which was designed as an alternative to employee layoffs for a temporary downturn in business. See Minn. Stat. § 268.136. Under the program, partial UI benefits are paid in exchange for keeping the employee working, but at reduced hours. *Id.*, subd. 4. Any UI benefits paid, however, will be reflected in an employer's UI experience rating history.

In a follow-up letter on December 21, 2011, DEED stated the basis for its experience rating transfer: "[b]ased on the wage transfer, it appears that . . . you share common ownership, management or control [with CMI]." Ex. 8(2). In that same December 21, 2011 letter, DEED assessed a penalty of \$18,201.00 for Cont. Hydraulics' alleged failure to provide information about the acquisition of CMI's hydraulics business. *Id.* Cont. Hydraulics then timely filed an appeal for the following reasons:

[Cont. Hydraulics] is a new company that was purchased by a new ownership group that has no relationship with [CMI] except for a landlord/lessee contract. The 2 companies are in

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be additional statutory assessments for the Federal Loan Interest Assessment and Workforce Development Fee. Ex. 1.

totally different business segments and have no business connections. [Cont. Hydraulics] hired the employees in question upon termination by CMI. We were not required to do so by terms of the purchase agreement. [Cont. Hydraulics] has hired additional employees and have utilized numerous employment agencies since the purchase date of April 13, 2011 to support its planned growth. The ownership group has already invested in excess of \$1 million in asset purchases and improvements and have budgeted another \$1.2 million for 2012 to insure long term growth and viability for the current employees employed. It is in our opinion that we are not a part of [CMI] in that we DO NOT share common ownership, management and control. As stated above the only relationship we currently have with CMI is that we rent a portion of their facilities under a 5 year lease agreement. 100% of our stock is owned by Duplomatic Oleodinamica, SpA.

Ex. 2.

Following a hearing, the ULJ issued the Decision, affirming DEED's: 1) decision to partially transfer CMI's UI experience rating history to Cont. Hydraulics; 2) calculation of 2011 and 2012 tax rates based on the transferred experience history; and 3) assessment of the \$18,201.00 penalty. AA 20–25. Cont. Hydraulics submitted a timely request for reconsideration to the ULJ, who affirmed the Decision. AA 26–36 and AA 47–50.

## ARGUMENT

### I. STANDARD OF REVIEW.

The court of appeals may reverse or modify the ULJ's decision if it is affected by an error of law and may reverse or modify the ULJ's findings or inferences if they are "unsupported by substantial evidence in view of the entire record as submitted." Minn. Stat. § 268.105, subd. 7(d); *Peterson v. Nw. Airlines, Inc.*, 753 N.W.2d 771, 774 (Minn.

Ct. App. 2008), *review denied* (Minn. Oct. 1, 2008). In reviewing whether the ULJ committed an error of law, statutory construction is a legal issue that is reviewed de novo. *Vasseei v. Schmitt & Sons Sch. Buses, Inc.*, 793 N.W.2d 747, 750 (Minn. Ct. App. 2010).

**II. THE ULJ ERRED AS A MATTER OF LAW IN ITS APPLICATION OF SUBDIVISION 4(B)(2).<sup>8</sup>**

At issue in this appeal is DEED's decision to transfer the UI experience rating from CMI to Cont. Hydraulics pursuant to Subdivision 4(b), which provides:

A portion of the experience rating history of the predecessor employer is transferred to the successor employer when:

(1) a taxpaying employer acquires a portion, but less than all, of the organization, trade or business, or workforce of another taxpaying employer; and

(2) there is 25 percent or more common ownership or there is substantially common management or control between the predecessor and successor, the successor employer acquires, as of the date of acquisition, the experience rating history attributable to the portion it acquired, and the predecessor employer retains the experience rating history attributable to the portion that it has retained.

Minn. Stat. § 268.051, subd. 4(b) (emphasis added). The underlined language was added to Subdivision 4(b) in 2005 to comply with the SUTA Act. *See* 2005 Minn. Laws ch. 112 (stating the law was “[a]n act relating to unemployment insurance; conforming various provisions to federal requirements”). The “federal law” referred to was the SUTA Act that, in 2004, amended 42 U.S.C. § 503(k)(1) to add the following:

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<sup>8</sup> Since the ULJ offered no analysis of how it interpreted Subdivision 4(b) in either the Decision or in denying the request for reconsideration, it is unclear what the ULJ believed was the proper interpretation.

For purposes of subsection (a), the unemployment compensation law of a State must provide--

(A) that if an employer transfers its business to another employer, and both employers are (at the time of transfer) under substantially common ownership, management, or control, then the unemployment experience attributable to the transferred business shall also be transferred to (and combined with the unemployment experience attributable to) the employer to whom such business is so transferred,

(B) that unemployment experience shall not, by virtue of the transfer of a business, be transferred to the person acquiring such business if--

(i) such person is not otherwise an employer at the time of such acquisition, and

(ii) the State agency finds that such person acquired the business solely or primarily for the purpose of obtaining a lower rate of contributions[.]

SUTA Dumping Prevention Act of 2004, Pub. L. No. 108-295, § 2, 118 Stat. 1090, 1090.

- A. As a provision mandated by the federal SUTA Act, Subdivision 4 should be interpreted according to its plain language and consistent with the general, federal purpose in requiring states to add “substantially common management or control.”**

It is axiomatic that this court’s duty with respect to a state statute is to effectuate the legislature’s intent. Minn. Stat. § 645.16. Interpretation of state statutes begins with an inquiry into whether the law is ambiguous or unambiguous. *Harrison ex rel. Harrison v. Harrison*, 733 N.W.2d 451, 453 (Minn. 2007). A statute is ambiguous if there is more than one reasonable interpretation of the statutory language. *Am. Family Ins. Grp. v. Schroedl*, 616 N.W.2d 273, 277 (Minn. 2000). A reasonable interpretation must apply rules of grammar and give words and phrases “their common and approved usage.”

Minn. Stat. § 645.08(1); *see also Larson v. State*, 790 N.W.2d 700, 703 (Minn. 2010). Of

course, “technical words and phrases . . . are construed according to [their] special meaning or their definition.” Minn. Stat. § 645.08(1).

This case, however, provides an additional layer of complexity because the language at issue is not simply a state statute, but mandatory language that had to be enacted nationwide to comply with the federal SUTA Act. Minnesota law provides, “Laws uniform with those of other states shall be interpreted and construed to effect their general purpose to make uniform the laws of those states which enact them.” Minn. Stat. § 645.22. In interpreting statutory language that has been uniformly enacted, other states’ interpretations are given considerable weight. *Johnson v. Murray*, 648 N.W.2d 664, 670 (Minn. 2002).

**B. The plain language of Subdivision 4(b)(2) requires there to be an existing state in time where persons with management and control were shared by both the predecessor and the successor.**

First, the relevant language of Subdivision 4(b)(2) at issue in this case provides “there is substantially common management or control.” Minn. Stat. § 268.051, subd. 4(b)(2) (emphasis added). As a matter of common grammar, the verb “is” is the present tense of the verb “be.” *The American Heritage Dictionary* 693 (2d College ed. 1985). As such, it refers to the subject’s “present state; as it stands.” *Id.* Applying this common grammar and meaning, for Subdivision 4(b)(2) to be applicable, the present state of “management or control” of the predecessor must be “common” to the successor. The relevant definition of “common” is “[b]elonging equally to two or more; shared by all alike; joint.” *Id.* at 268. Thus, under the common language of Subdivision 4(b)(2), for the provision to apply, the present state of “management or control” must be shared by

both the predecessor company and the successor. In other words, “there is substantially common management and control” only when the same persons are managing or control both the predecessor and the successor at the same time.

In the context of corporations, the words “control” and “management” have technical meanings. “Control” is defined by corporation statutes as:

the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise. A person's beneficial ownership of ten percent or more of the voting power of a corporation's outstanding shares entitled to vote in the election of directors creates a presumption that the person has control of the corporation. Notwithstanding the foregoing, a person is not considered to have control of a corporation if the person holds voting power, in good faith and not for the purpose of avoiding section 302A.673, as an agent, bank, broker, nominee, custodian, or trustee for one or more beneficial owners who do not individually or as a group have control of the corporation.

Minn. Stat. § 302A.011, subd. 48 (emphasis added). As this definition provides, “control” of a corporation is placed in the hands of the board of directors or an owner with sufficient voting shares to dictate who will be on the board of directors. *See Transamerica Ins. Co. v. FDIC*, 489 N.W.2d 224, 228–29 (Minn. Ct. App. 1992) (discussing power of board is to control company).

The “management” of a corporation, is not mid-level managers, but the persons who are responsible for the operation of the company, such as the chief executive officer or other executive level officers. *See Black's Law Dictionary*, 971 (7th ed. 1999) (defining “management” as, “The people in a company who are responsible for its

management”); *see also Benda v. Girard*, 592 N.W.2d 452, 453–54 (Minn. 1999) (“managerial and executive services” for tax code purposes include “quality review, strategic planning, monitoring regional operational performance, attending board of directors’ meetings, and attending corporate social functions and award ceremonies”).

Applying basic grammar and plain meaning of the words in Subdivision 4(b)(2), “there is substantially common management or control” when a substantial percentage of the predecessor’s executive officers or its board of directors not only continues to make major decision for the predecessor but concurrently has the same responsibility for making the major decisions of the successor company. This is not only the one interpretation that is consistent with basic grammar and common understanding of the words in question, it is the same meaning that other states have expressly adopted.

For example, some state statutes or codes provide that “substantially common management or control” exists if the predecessor continues to:

1. own or manage the organization that conducts the organization, trade, or business.
2. own or manage the assets necessary to conduct the organization, trade, or business.
3. control through security or lease arrangement the assets necessary to conduct the organization, trade, or business.
4. direct the internal affairs or conduct of the organization, trade, or business.

*See, e.g.*, Tex. Lab. Code Ann. § 204.081(2); Mo. Code Regs. Ann. tit. 8, § 10-4.190(1)(B). And Florida’s administrative code provides that “common management”

occurs when a “person concurrently occupies management positions in two or more businesses.” Fla. Admin. Code Ann. r. 60BB-2.031(3)(d) (emphasis added).

Further, this interpretation is consistent with the guidance issued from the U.S. Department of Labor on what states must do to comply with the SUTA Act in Program Letter 30-04. Specifically, that letter includes as “Attachment I” a “Detailed Explanation of Section 330(k) SSA – Questions and Answers. AA 4-12. Question 4 ask for an example of when an experience rating transfer must occur under the new substantially common management or control amendment. *Id.* at 5. The U.S. Department provides the following example:

Answer: Corporation A is assigned the state’s maximum UC contribution rate of 5.4%. It establishes a shell corporation that is treated as a separate employer for UC purposes. The shell eventually qualifies for the state’s minimum UC contribution rate of .5%. . . . Corporation A then transfers all or some of its workforce to that shell. The result, absent the amendments, would be that, even though Corporation A controls the shell and its operations, it escapes a rate of 5.4% on the transferred workforce and instead pays at a rate of .5%.

*Id.* This guidance simply confirms what the plain language of the SUTA Act and Subdivision 4(b) provide. The phrase “there is substantially common management and control” is not meant to apply to an arm’s length, marketed asset purchase where a wholly unrelated company purchases a segment of an existing company for legitimate business purposes.

**C. The ULJ's apparent interpretation of Subdivision 4(b) is not reasonable.**

Unfortunately, the ULJ did not engage in any written explanation of what he believed to be the meaning of the phrase “there is substantially common management or control.” Instead, the Decision begins by conceding that “Wilkie had final say in all significant investment and strategic decisions,” while Maddalon “has the final in such decision[s]” for Cont. Hydraulics. There is no suggestion, nor would the evidence support any claim, that Maddalon has ever had any involvement in any decision of CMI or that Wilkie has ever had any involvement in Cont. Hydraulics. As such, it is legally impossible to conclude that there is “common control” let alone “substantially common control” between CMI and Cont. Hydraulics.

The Decision is completely devoid of analysis of the respective “management” of the two companies. Instead, the ULJ focused on the fact that “managers” of CMI’s hydraulics business were hired by Cont. Hydraulics for positions, in most cases, with greater authority. Again, there are no findings or evidence to support a finding that these “managers” fall with the definition of a corporation’s “management” or that even a single person was contemporaneously employed by, or even involved with, both companies.

Instead of analyzing the meaning of “management” and whether any members of CMI’s “management” are or ever were, contemporaneously part of Cont. Hydraulics’ “management,” the ULJ focused on the fact that “managers” of CMI’s hydraulics business, which the ULJ himself would later refer to as “managerial staff” were hired by Cont. Hydraulics for positions, in most cases, with greater authority. Of course, the

indisputable evidence also shows that all 81 persons hired by Cont. Hydraulics were first terminated by CMI. The Decision also finds that Wilkie lived in Chicago and “received input from the managers reporting to Johnson,” while Maddalon “has little experience in the U.S. markets and those who report to him were employees of CMI.”

From these findings, the ULJ began his conclusion stating, “It is true the heads of the companies are different. And with that it appears the final decision making authority changed.” These statements are not only correct, the statements are dispositive. There cannot be “substantially common management or control” under a proper interpretation of that language when the final decision making resides in different hands.

But instead of recognizing this reality, the ULJ went on to conclude:

While there has been change at the very top and key people have been shuffled, the preponderance of the evidence is that the ultimate decision makers for CMI (hydraulic division) and CHI receive/received their input on business decisions from essentially the same people. Furthermore, those are the people managing operations locally.

As discussed below, these claims are not supported by the evidence, but more importantly, even accepting the statement as true it does not support a conclusion that there is substantially common or control between CMI and Cont. Hydraulics.

First, the plain language of Subdivision 4(b) does not permit an analysis of the decision maker of a segment of CMI. Rather, the statute plainly refers to “predecessor employer” and “successor employer.” An “employer” is in turn defined as “any person that has had one or more employees during the current or the prior calendar year including any person that has elected, under section 268.042, to be subject to the

Minnesota Unemployment Insurance Law and a joint venture composed of one or more employers.” Minn. Stat. § 268.035, subd. 14. A “person” is in turn defined as “an individual or any type of organization or entity . . . .” *Id.*, subd. 21. These definitions do not support a parsing out of CMI by internal division. Rather, a “predecessor employer” is the entity that hired the employees. Here, the entity is CMI, which was but a single company that included 165 employees, more than half of whom worked and continue to work in the machine tooling.

Second, there is nothing in Subdivision 4(b) that supports a transfer of experience rating because the persons providing “input” to admittedly different management groups are similar. To provide an transfer under Subdivision 4(b) on these grounds would require reading language into the statute that does not exist. It is well recognized that courts may not read language into a statute that does not exist. *Rohmiller v. Hart*, 811 N.W.2d 585, 590 (Minn. 2012).

Finally, the interpretation that the ULJ seems to have applied to this case would lead to an absurd distinction. Specifically, if Duplomatic had acquired the assets from CMI directly, rather than creating a distinct, wholly owned subsidiary, it would be uncontested that a portion of CMI’s UI experience rating history would not transfer to Duplomatic. Of course, there are a plethora of business considerations that weigh into the decision why a company in Duplomatic’s position would chose to create a distinct legal entity to receive the newly acquired assets, including the fact that Duplomatic is a European company. But under the ULJ’s interpretation, whether there is a transfer of

rating history will ultimately turn on a corporate planning decision of whether to create a wholly owned subsidiary or whether to simply absorb the acquired assets.

**D. Cont. Hydraulics is not a shell company of CMI, was not formed for SUTA dumping, and has no commonality in management or control with CMI.**

There has never been so much as a suggestion that Duplomatic's decision to acquire CMI's hydraulics business, and creation of Cont. Hydraulics to fulfill that acquisition, was anything other than a legitimate market transaction driven by one company's need to raise capital and another's desire to enter the U.S. market through an established brand. *See Ex. 9.* Nor was any evidence presented suggesting that the acquisition was in anyway driven by a desire to avoid UI experience rating (aka SUTA dumping). Rather, the evidence confirms Cont. Hydraulics' acquisition of CMI's hydraulics business was a market transaction in which a wholly independent entity, created and owned by an unrelated European company, purchased a segment of CMI for legitimate business purposes that had nothing to do with SUTA dumping. *See Ex. 9.* This quite simply is not even a close case. It is a market transaction where a new legal entity was created by an unrelated company to facilitate the market-based asset purchase and, as the evidence confirms, there has never been a point when there is any common management or control between Cont. Hydraulics and CMI, let alone substantially common management or control.

Cont. Hydraulics was created by the Italian hydraulics company, Duplomatic, because it wanted to move into the American market. To do so, Cont. Hydraulics

purchased the hydraulics business from CMI as a market transaction that was financed by AXA Private Equity.

It is equally indisputable that CMI decided to sell its hydraulics business because it needed to raise capital and the hydraulics business was not a core business function of CMI. Cont. Hydraulics paid fair value, which was financed by AXA Private Equity, for the purchase of the hydraulics business. As is typical with any such asset purchase, CMI terminated the employment of all 81 persons in the hydraulics business, whom were then hired by Cont. Hydraulics. After the asset purchase was complete, the 81 persons hired by Cont. Hydraulics had no involvement of any kind with CMI. While after the sale of its hydraulics business, CMI continues to employ 84 persons and operate its core business of machine tool production.

Not a single person that continues to be employed by CMI, including its president Johnson and its chairman and CEO Wilkie, has ever had any management or control of any kind in Cont. Hydraulics. From the moment Cont. Hydraulics was created through the asset purchase and through today, Duplomatic's CEO, Maddalon, has always been Cont. Hydraulics' chairman/president, which in European parlance means he has final decision making authority (i.e. "control"). Maddalon has never held any position with CMI. Rather, CMI is owned by Wilkie and he has final authority for all business decision at CMI as its CEO and chairman. The day-to-day operation of Cont. Hydraulics rests with CEO Horihan (i.e. "management"). The undisputed evidence is that while Horihan was employed by CMI, he had no authority for making business-operational

decisions. The day-to-day decision maker at CMI was and is fulfilled by its president Johnson.

In short, management and control at CMI is, and always has been, in the hands of Wilkie and Johnson. These are the individuals, along with CMI's board of directors, that are responsible for the management and control of CMI. Based on the plain meaning of Subdivision 4(b), these are the people that would also need to control and manage, or at least exert some power over, Cont. Hydraulics for a UI experience rating history transfer to be appropriate. The evidence, of course, is that neither individual has ever had an ounce of involvement with Cont. Hydraulics. Cont. Hydraulics is instead controlled and managed by Maddalon and Horihan, which the evidence just as clearly shows have never managed or controlled CMI. As such, the undisputed evidence conclusively demonstrates that there is not substantially common management and control between the two entities. Therefore, there cannot, as a matter of law, be a transfer of UI experience rating history under Subdivision 4(b).

### **III. CONT. HYDRAULICS' 2011 AND 2012 TAX RATE MUST BE RECALCULATED.**

An employer's UI tax rate is calculated pursuant to Minn. Stat. § 268.051. For employers that "qualif[y] for an experience rating" the tax rate is calculated by adding the employer's experience rating to the "base tax rate" along with certain other statutory assessments *Id.*, subd. 2(a). To qualify for an experience rating, an employer must have "been required to file wage detail reports for the 12 calendar months ending the prior June 30." *Id.*, subd. 3(a). But for a "new employer" (i.e. one that has not been in

business long enough to have 12 months of wage detail reports), the rate is calculated differently. *Id.*, subd. 5. For new employers not in a “high experience rating industry,” Section 268.051 states such employers “must be assigned, for a calendar year, a tax rate the higher of (1) one percent, or (2) the tax rate computed to the nearest 1/100 of a percent, by dividing the total amount of unemployment benefits paid all applicants during the 48 calendar months ending on June 30 of the prior calendar year by the total taxable wages of all taxpaying employers during the same period, plus the applicable base tax rate and any additional assessments under subdivision 2, paragraph (c).” *Id.*

Here, it is uncontested that were it not for DEED’s “succession decision” transferring a portion of CMI’s experience rating, Cont. Hydraulics’ tax rate would be calculated under the “new employer” provision as a company that did not exist before April 2011. Under the new employer provisions, Cont. Hydraulics’ tax rate would be approximately 3% for 2011 and 2012 (before statutory assessments). But based on DEED’s and the ULJ’s legally and factually incorrect conclusion that there is substantially common management or control between CMI and Cont. Hydraulics, the ULJ affirmed DEED’s decision to transfer 49.09% of CMI’s experience rating to Cont. Hydraulics. So instead of an approximately 3% UI tax rate, the 2011 tax rate was recalculated at 7.84% and calculated at 7.89% for 2012 (plus statutory assessments for both years). Since the decision to transfer CMI’s experience rating was legally and factually flawed, DEED’s determination of tax rates for 2011 and 2012 along with the ULJ’s affirmance of those decision are legally incorrect and must be set aside.

**IV. THE ULJ ERRED IN REAFFIRMING THE PENALTY AGAINST CONT. HYDRAULICS FOR NOT PROVIDING INFORMATION THAT WAS NOT REQUIRED AND THAT DID NOT EXIST.**

In the “other notes” section of the Decision, the ULJ concluded that Cont. Hydraulics violated Minn. Stat. § 268.051, subd. 4(d), which states, “Each successor employer that is subject to paragraph (a) or (b) must notify the commissioner of the acquisition by electronic transmission, in a format prescribed by the commissioner, within 30 calendar days of the date of acquisition.” *Id.* (emphasis added). Paragraph (a) or (b), addresses full or partial experience rating transfer with there is there is common ownership, management or control. An employer, subject to paragraphs (a) or (b), that does not provide the required notification “is subject to the penalties under section 268.184, subdivision 1a.” *Id.* In turn, that section provides:

If the commissioner finds that any employer or agent of an employer failed to meet the notification requirements of section 268.051, subdivision 4, the employer must be assessed a penalty of \$5,000 or two percent of the first full quarterly payroll acquired, whichever is higher. . . . The penalty under this paragraph must be canceled if the commissioner determines that the failure occurred because of ignorance or inadvertence.

Minn. Stat. § 268.184, subd. 1a(a).

**A. Because Cont. Hydraulics is not “subject to paragraphs (a) or (b)” of Subdivision 4, the ULJ erred in affirming the penalty assessment.**

DEED claims to have assessed the \$18,201 penalty for an alleged violation of Subdivision 4(d). That subdivision unambiguously applies only to “[a] successor employer that is subject to paragraph (a) or (b).” Minn. Stat. § 268.051, subd. 4(d).

As the Decision acknowledges, Cont. Hydraulics could only be required to provide information under Subdivision 4(d) if it is a successor under Subdivision 4(b). As discussed above, it is clearly not such a company. As such, there can be no penalty assessed.

In addition, there are factual errors in the discussion of the penalty in the Decision. First, Heist specifically testified that he provided information about Cont. Hydraulics' creation in April 2011. DEED confirmed as much in an August 5, 2011 letter when it wrote, "You recently registered a business entity with our Department indicating that you had either acquired all or part of a business or a had a change of legal entity." Ex. 5. Of course, Heist rightfully understood Cont. Hydraulics was a new company that did not share any ownership, management or control with CMI. Therefore, there was nothing more for Heist to provide.

**B. Even if Cont. Hydraulics had been "subject to paragraph (a) or (b)," the ULJ would have erred as a matter of law in not cancelling the penalty.**

Under the plain language of Section 268.051, subd. 4(d), a company that violates the reporting provisions is "subject to a penalty under section 268.184, subdivision 1a." Minn. Stat. § 268.051, subd. 4(d). The plain language of Section 268.184, subd. 1a(a) provides, "The penalty under this paragraph must be canceled if the commissioner determines that the failure occurred because of ignorance or inadvertence." *Id.* (emphasis added). Since "must" is a mandatory verb, it is legal error to impose a penalty where the failure to provide information is the result of "ignorance or inadvertence."

Here, while the ULJ found that “the failure to report the information was not due to inadvertence or ignorance” that finding is neither consistent with the plain meaning of those words nor supported by the evidence.

The common meaning of “ignorant” is “[u]naware or uninformed.” *The American Heritage Dictionary* 640 (2d College ed. 1985) (also defining “ignorance” as “[t]he condition of being ignorant”). The common meaning of “inadvertent” is “Accidental; unintentional.” *Id.* at 649. Alternatively stated, a penalty can only stand where the commissioner finds a company was aware that it had to provide the information and intentionally chose not to do so.

This interpretation is not the only reasonable interpretation of the plain language, it is also consistent with the federal SUTA Act, which provided:

(D) that meaningful civil and criminal penalties are imposed with respect to--

(i) persons that knowingly violate or attempt to violate those provisions of the State law which implement subparagraph (A) or (B) or regulations under subparagraph (C), and

(ii) persons that knowingly advise another person to violate those provisions of the State law which implement subparagraph (A) or (B) or regulations under subparagraph (C).

SUTA Dumping Prevention Act of 2004, Pub. L. No. 108-295, § 2, 118 Stat. 1090, 1090.

Here, the evidence conclusively establishes that if Cont. Hydraulics could have been subject to Subdivision 4(d), the failure to provide any information was the result of “ignorance or inadvertence.” Heist testified that after receiving the August 5, 2011 letter,

he contacted DEED by phone to find out what DEED was looking for. He testified that he again reviewed the online submission forms and confirmed everything he submitted was correct. At that point, he believed that everything was resolved. Heist testified that to the best of his knowledge, Cont. Hydraulics did not receive the subsequent requests from DEED on November 10, 2011, or that the letter was lost.

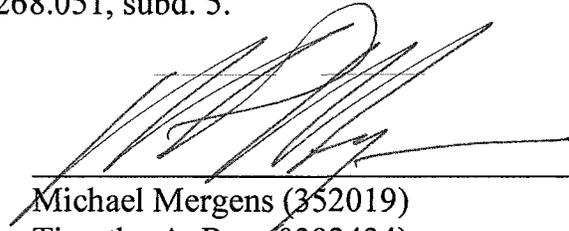
While it is uncontested that Cont. Hydraulics did not provide any additional information after Heist verified the submission in August 2011, it was because he believed in good faith that he had supplied all needed information and was not aware of the November 11, 2011 request. Even if Cont. Hydraulics had substantially common management and control with CMI, which it never has, it is not appropriate to impose a penalty on a party who rightfully and in good faith believes all required information had been provided. Indeed, the plain and unambiguous language of Minn. Stat. § 268.184, subd. 1a(a), demands that the penalty “must be canceled if the commissioner determines that the failure occurred because of ignorance or inadvertence.”

### **CONCLUSION**

The uncontested evidence shows that Cont. Hydraulics is a new company that was created and wholly owned by Diplomatic. While Cont. Hydraulics acquired the hydraulics business of CMI, it did so as a market transaction and never shared any ownership, management or control with CMI. As such, it is legal err to transfer CMI’s UI experience rating to Cont. Hydraulics. It is likewise legal err to impose a penalty of \$18,201 for not providing information when no such information was required. Finally, because Cont. Hydraulics is a new company without any experience rating, DEED has

committed legal err in its determination of Cont. Hydraulics' 2011 and 2012 tax rates. Therefore, Cont. Hydraulics requests this Court reverse the Decision, strike down the UI experience rating transfer and penalty, and remand the matter to DEED for recalculation of tax rates under Minn. Stat. § 268.051, subd. 5.

Dated: 11/30/12



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