

# BWC's New Method for Determining Successorship



## What is successorship?

"Successorship" or "successors in interest" are terms that describe the takeover of one employer's business by another, generally resulting from a change in ownership due to a purchase, acquisition or merger. For workers' compensation purposes, it requires the continuation or transfer of experience and liability from the predecessor (seller) to the successor (buyer). If BWC determines the relationship between the predecessor and successor is a continuation of the business or operations, BWC combines the predecessor policy into the successor policy.

## The significance of determining successorship

Continuation of experience from the predecessor policy to the successor policy is an essential element in developing the appropriate premium rate for the successor policy. The prior experience of the predecessor is a valid indicator or predictor of the expected future performance of the successor. Although there may be a change in ownership, if the operation of the predecessor remains relatively the same with the same or similar degree of hazard, it is appropriate to transfer the experience to the new owner and successor policy.

## BWC's historical practice for determining successorship

Historically, BWC has used several factors when determining if a successorship exists for workers' compensation purposes. Such factors include but are not limited to:

- Retention of employees;
- Same or similar pursuit of industry;
- Same location of the predecessor;
- Goodwill of the predecessor;
- Retention of client or customer base and servicing of warranties.

All play a vital role in the determination process. However, some factors may weigh more heavily than others depending on the particular circumstances of the purchase. There are no set-in-stone criteria or checklists that BWC used in the determination process. This lack of a definitive, objective process had triggered complaints from BWC's customers, interested parties and other stakeholders. Complaints largely concerned uncertainty, inconsistency and disputes regarding the appropriateness of the successorship determination and the ensuing transfer of experience and liability to the purchasing entity.

## What is new?

Beginning Jan. 1, 2016, BWC implemented a new process, using the successor methodology developed by the National Council on Compensation Insurance (NCCI). The primary intent of the new method for determining successorship is to provide an unambiguous and predictable means for determining the continued use of experience and transfer of liability whenever an entity undergoes any type of ownership change. Stated simply, the NCCI approach is that in the case of purchases, acquisitions and mergers, experience will transfer from the predecessor policy into the successor policy the vast majority of the time, unless three specific conditions have been met. Those three conditions require: (1) a material change in ownership and the new owner must change the business so substantially that (2) the governing classification and (3) the process and hazard of the operation change.

BWC will also consider a fourth condition in determining whether an exception to the NCCI practice is considered. The additional condition concerns the time between the predecessor ceasing operations and the purchase effective date. When that time period is significant, BWC believes that past experience is not necessarily a useful indicator of future performance, even for businesses that would not otherwise be excepted from an experience transfer under the NCCI criteria. In summary, BWC will use four factors listed in the following four items to determine if a successorship does not exist. BWC may grant the exception if the conditions of paragraph 1 are met. The standard NCCI criteria for establishing an exception to successorship are listed in paragraphs 2 through 4.

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- 1.** The time (days/months) between the predecessors ceasing all operations and ceasing as an active entity, and the effective date of the purchase. The predecessor must prove closure date.
    - a.** If the period is greater than six months, a successorship does not exist. BWC will not transfer experience or liability from the predecessor to the successor policy.
    - b.** If the period is less than six months, BWC considers the relationship between the seller and buyer a successorship unless the buyer satisfies the conditions in item 2 through 4.
    - c.** If there is a family relationship or other connection between the predecessor and successor, BWC may apply coverage initiation regardless of the timeframe between closing of the business and the date of the sale.
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- 2.** Is there a material change in ownership? To meet the material change in ownership requirement, there must be an outright sale (no association between seller and buyer).
    - a.** In the case of a continuation in ownership, such as a change in partnership, the owner's interest must have been less than 1/3 ownership before the change or less than 1/2 ownership after the change to meet this requirement.
    - b.** If there is a family relationship or other connection between the predecessor and successor, BWC does not consider the sale of the entity to be a material change in ownership.
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- 3.** Is there a change in governing classification? To meet the change in governing classification, there must be a change in operations significant enough to require a reclassification of the governing class code.
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- 4.** Is there a change in process and hazard? To meet the change in process and hazard requirement, there must be a total change in operations or industrial pursuit – or a totally new way of performing the work, providing the service, handling the material, etc. – that dramatically changes the degree of hazard under the successor policy. This may require an evaluation by BWC's underwriting department, a site visit by BWC's audit department or a consultation with BWC's Division of Safety & Hygiene.
    - a.** It is possible to meet the "change in governing classification" requirement and not meet the change in process and hazard. This could occur if BWC applies a new manual classification to the predecessor's operations due to changes implemented by the successor (see No. 3 above). However, if the successor uses the same processes, machinery, equipment, tools, etc., then basically the same degree of hazard exists.
    - b.** The successor must provide documentation to support a substantial modification in process and hazard.

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## How will this apply to bankruptcy and receivership?

### Bankruptcy

1. When an employer enters into bankruptcy to reorganize and continues to operate, BWC will issue a new policy with the status debtor in possession (DIP).
  - a) The experience from the original policy will transfer to the DIP policy to develop their rate. However, the liabilities will remain with the original policy.
  - b) If the employer emerges from the bankruptcy and continues in business, BWC will update the policy to remove the DIP status; the employer retains the experience.
2. When an employer enters into bankruptcy and sells the business, there is no transfer of experience or liabilities to the buyer.

### Receivership

When a receiver is responsible to liquidate the assets of the entity, court appointed or not, BWC considers this a third-party intermediary; no liabilities or experience transfers to the succeeding employer, unless that employer is the same as, a family member of or is connected to the owner whose assets were liquidated by receiver

### Implementation date

BWC's underwriting department will use this new method for determining successorship for all purchases, mergers and acquisitions it reviews on or after Jan. 1, 2016.

### Notification to the employer

Upon notification or discovery of a potential successorship, BWC's policy underwriting unit will research the relationship and all factors associated with the potential successorship. Once the unit makes the decision to process the combining of policies (successorship) or consider it not to be a successor relationship, BWC will send a letter to the buyer.

### Obtaining employer and policy information on a potential seller

The NCCI criteria make it clear there is a strong possibility that the experience and liability of the predecessor will transfer to the successor when a purchase, acquisition or merger occurs. To facilitate a buyer's awareness, BWC developed the *Request for Business Transfer Information (AC-4)* to allow potential buyers to obtain employer-related data associated with the seller's policy. The potential seller must sign the AC-4, granting BWC the right to release employer-related policy data to the potential buyer. BWC strongly encourages any entity that is considering the purchase of another entity to use this form to help discover any issues with the seller's policy prior to purchase.