***Employee Benefits and Executive Compensation Considerations in Mergers and Acquisitions* Series: Multiemployer Pension Plans in Mergers and Acquisitions**
Speakers: Paul Porretta and Chris Stock
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Paul Porretta:

Hello, and thank you for joining us for a discussion on multiemployer pension plans in mergers and acquisitions. I'm Paul Porretta, a partner in the New York office of Troutman Pepper Hamilton Sanders LLP. I'm joined by my colleague, Christopher Stock, who's an associate in our Richmond, Virginia office. To start us off, Chris, tell us what a multi-employer pension plan is?

Chris Stock:

Thanks, Paul. Let's start with the basics. Yeah, and multiemployer plan is a defined benefit, defined contribution, or welfare benefit plan, where more than one employer is required to contribute and maintain pursuant to one or more collective bargaining agreements or CPAs, between one or more unions, and more than one employer. Today, we'll be focusing on multiemployer pension plans, as Paul mentioned.

These plans were established under the Labor Management Relations Act of 1947, also known as the Taft-Hartley Act. The legislative environment surrounding these plans has been changing and evolving ever since, including changes to further strengthen the protection of these plans under the Multiemployer Pension Plan Amendment Act or MPPAA, the Pension Protection Act of 2006, and The American Rescue Plan act of 2021, as well as additional guidance from the IRS, Department of Labor, and the Pension Benefit Guaranty Corporation.

Currently, there are approximately 1,400 multiemployer defined benefit pension plans in the US, holding an impressive $627 billion in assets. These plans cover about 10 million participants. While they only represent 3% of all defined benefit plans, they cover nearly 29% of all participants in pension plans. A significant portion of these participants are employed by small companies in industries such as building, and construction, retail, trade, manufacturing, mining, trucking, transportation entertainment. This highlights the broad reach and impact of these plans.

Contrary to popular belief, these plans are not sponsored and maintained by the union. Instead, they're managed by a joint board of trustees, which includes equal representation from both the union and management. This board is responsible for the operation and administration of the plan. The benefits and contributions provided under these plans are typically set in the Collective Bargaining Agreements or CBAs, which is negotiated between the contributing employer and the union. Many of these plans are unit benefit plans that offer a specified dollar amount per month, multiplied by years of credit service.

Another common misconception is that employers are participating employers in the plan. However, they're only contributing employers and their only contractual connection to the plan is the CBA, which outlines their contribution obligations. Paul, in a transaction where a target company is a contributing employer, or a member of controlling group containing a contributing employer to a multiemployer pension plan, what are some key issues that the buyer should consider?

Paul Porretta:

Thanks, Chris. Let's start off by talking about the general diligence and representations that we would see in a purchase agreement, and how that might be different or distinguished with a target company that is obligated to contribute to multiemployer plan. As Chris explain, if an employer doesn't actually sponsor or maintain a multiemployer pension plan, the seller in a transaction will not be in a position to make certain representations that we would typically expect from a seller in connection with a single-employer plan.

For example, the seller would not be able to represent that the multiemployer plan is qualifying as [inaudible], or free from operational failures. Further, these particular matters may not be relevant to the buyer, since there should not be any liability on qualification or operational failures that would attach to either the seller or the buyer. Of course, diligence on the sellers collective bargaining agreements will be of interest to the buyer, as it should indicate the multiemployer plans that seller is currently obligated to contribute to. And there will be other diligence specific to multiemployer pension plans that will be important to the buyer. Diligence that generally is not applicable to single employer plans. We'll cover multiemployer pension plan diligence in a few minutes. But first, Chris, the primary multiemployer pension plan issue in mergers and acquisitions is withdrawal liability, and withdrawal liability exposure. Could you explain what this is all about?

Chris Stock:

Yes. The rules surrounding these plans underwent a significant change in the 1980s with the introduction of the MPPAA. Before this, an employer could stop contributing to a plan and walkway without any further liability. However, the MPPAA change this by imposing withdrawal liability on employers that leave multiemployer plan. Withdrawal exposure is merely a contingent liability until an employer ceases contributing to or withdraws from the multiemployer plan. Once triggered, the employer is liable for the employer's allocable share of the unfunded vested benefits.

An employer that withdraws is required to pay its liability in annual amounts based on its contributions during the preceding 10 years. The plan must limit the payment schedule for partial withdrawal or complete withdrawal to a maximum of 20 years. It's imposed on the employer along with members of its controlled group, which includes all entities under common control with the employer. It is not uncommon for employers to be unaware of the real risk or have an up-to-date estimate of the financial exposure of a withdrawal.

For example, small employer making annual contributions of 200,000 may face millions of dollars in a complete withdrawal liability, especially if the plan is severely underfunded. An employer can incur withdrawal, liability voluntarily or inadvertently upon a partial withdrawal, complete withdrawal, or mass withdrawal. Each of these types of withdrawals has specific conditions that trigger them, and understanding these conditions is crucial for the parties to a transaction to manage their potential liabilities.

First, we'll cover partial withdrawal. In a partial withdrawal, an employer generally experiences a partial withdrawal from a multiemployer pension plan on either a 70% decline in their contributions in each year of a three-year consecutive testing period, or when a player permanently ceases to have an obligation to contribute at one. but not all facilities covered by the plan if the employer continues to perform the same type of work at that facility. Alternatively, a partial withdrawal occurs when an employer permanently ceases to have an obligation to contribute under one or more, but not all CPAs will continue to perform the same type of work in the union's jurisdiction or transferring the work to another location.

An employer experiences complete withdrawal from a multiemployer plan upon the earlier of permanently ceasing to have an obligation to contribute to the plan. For example, an employer renegotiates its CBA, such that it ceases contributing to the multiemployer plan, and for example, replaces it with an obligation to contribute to a multiemployer 401(k) plan. Another event that could trigger complete withdrawal is permanently ceasing all covered operations in connection with its obligation to contribute to the plans. For example, the employer sells the assets and operations of his business, and terminates the employment of all employees covered by the collective bargaining agreement.

Lastly, a multiemployer pension plan experiences a mass withdrawal upon either the complete withdrawal of every employer obligated to contribute, the cessation of the obligation of all employers to contribute, or the withdrawal of substantially all employers pursuant to an agreement or an arrangement to withdraw. In a transaction that involves a party in the construction, trucking. entertainment, or retail food industry, special withdrawal liability rules may apply. These rules can alter the circumstances which a business is deemed to have withdrawal liability.

On the seller side, they should be aware that ERISA prohibits parties from evading withdrawal liability. The main purpose of the transaction is to avoid liability for required contributions to the plan. Paul, in a transaction where multiplayer plan is involved, what types of questions and information to request to get a better understanding these plans? What reps would you expect to see in a purchase agreement?

Paul Porretta:

Yes. Thanks, Chris, for setting the stage on the specter of withdrawal liability and its potential significance in mergers and acquisitions. Now, let's go back and talk about the diligence and representations that will be specific on these matters. Starting with diligence, the seller should be prepared for full disclosure on the multiemployer pension plans they're currently obligated to contribute to as well as plans that they may have ceased contributing to, and plans that their control group members contribute to, or contributed to in the past.

For each of these plans, the seller should gather contribution records going back at least five years. They should also provide any yellow zone or red zone notices that were received from the plans, and documentation on any applicable withdrawal liability exemptions. Such as the ones that Chris mentioned on the building and construction industry. The multiemployer plans Form 5500s will also be a focal point for diligence review, since they contain key funding information.

Perhaps, most importantly, the seller should obtain the most recently available estimate of its withdrawal liability from the multiemployer plan, which the plan is required under ERISA to provide upon request, although the plan may charge a reasonable fee for doing so. But due to the complexity of withdrawal liability estimates, it typically takes at least three weeks to prepare often longer. A seller should request withdrawal liability estimate early on in the transaction process. Since it could be important and sure enough, the buyer should be requesting a copy of.

The buyer's diligence process often includes engaging their own actuary for an analysis of the target's withdrawal liability exposure. This is often advisable, particularly if the sellers multiemployer pension plan obligations are substantial. Since an actuary is needed to decipher the funding and liability assumptions. Further, the buyers out actuary would want to calculate their own estimate of withdrawal liability, as well as review any estimate that was prepared by the plan.

Certainly, if the seller, or one of its control group members has already triggered a complete withdrawal or partial withdrawal, the seller should provide the buyer with copies of the notice of withdrawal liability that was received from the multiemployer plan, along with any requests for redo that were submitted, the payment schedule, and the payment status. Finally, the buyer's diligence review should keep an eye out for any downward trend in multiemployer plan contributions. Since it may signal a partial withdrawal that that may be on the horizon, as well as any significant withdrawals by other employers contributing to the plan. Since this could be a sign of a possible mass withdrawal at some point in the foreseeable future.

Turning to key representations, it's reasonable for a buyer to receive seller representations and disclosure schedules on the following. First, a complete list of multiemployer plans that the seller or its control group members are obligated to contribute to, or to which they have or may have liability. This would include multiemployer plans they've already withdrawn from, and are making withdrawal liability payments to, or within a reasonable period for which a multiemployer plan may assess withdrawal liability.

Second, representations should be specific as to whether the seller or any of its control group members have ever been assessed withdrawal liability for a complete withdrawal or a partial withdrawal. And whether any event has occurred or circumstances exist, such that, upon providing notice to the multiemployer plan could reasonably be expected to result in complete or partial withdrawal liability.

Third, there should be a representation that all contributions due and payable to the multiemployer plans for periods through the closing date had been paid. Forth, a representation that the seller is not subject to any contingent liability pursuant to an arrangement under Section 4204 of ERISA, which we'll talk more about in a few minutes, and has not engaged in a transaction to evade or avoid withdrawal liability. There are other reasonable representations, but these are perhaps most important ones. Now, Chris, can you tell us how all of this works in a stock transaction?

Chris Stock:

Thanks, Paul. If the transaction is structured as a stock deal or merger, the buyer steps into the shoes of the seller and assumes the seller's role as a contributing employer to the multiemployer plan, and generally will not trigger withdrawal liability. However, the change in business form must not cause any interruption in the employer contributions or the obligation to contribute to the plan. Although, withdrawal liability will not necessarily be triggered automatically by the stock sale, the buyer should have a detailed understanding of the seller's obligations to the plan. Because after the closing, the buyer is responsible for the seller's funding obligations under the collective bargaining agreement. Succeeds to the entire contribution history of the seller and is subject to withdrawal liability based on the whole contribution history if the buyer has a complete or partial withdrawal after the closing.

Typically, the buyer will want to negotiate and adjustment to the purchase price taking into account the probability, and liability that would arise if there is a complete withdrawal from the multiemployer plan. Now that we've covered stock transactions, what are the risks to the parties in asset transaction, Paul? Will this type of transaction trigger withdrawal liability?

Paul Porretta:

Thanks, Chris. Yes. the implications of multiemployer plan contribution obligations are different in an asset transaction. Because by operation of a sale of substantially all of the employer's assets, there will be a complete withdrawal because the employer will thereby cease covered operations and terminate the employees who are covered by the collective bargaining agreement. The buyer will want assurances that the seller has disclosed the sale to the multiemployer plan, and that the seller has the ability to pay the withdrawal liability that will result. The buyer should have these concerns, in particular, because if the seller defaults on its withdrawal liability, the plan may be able to enforce liability against the buyer as a successor employer for a finding of successor employer liability.

A bad set of facts for the buyer would be an asset purchase agreement that's totally silent on the multiemployer plan and the withdrawal liability. Also, such facts could support a claim by the plan against the buyer and the seller that the transaction was structured for the purpose of evading or avoiding withdrawal liability. And that the buyer knew or should have known about the withdrawal liability.

But aside from this, a seller of assets may avoid incurring a complete withdrawal. If the buyer expressly assumes the seller's contribution history to the multiemployer plan, as well as its contribution obligations for periods going forward in an arrangement that satisfies the requirements of Section 4204 of ERISA, which we previously mentioned briefly. The requirements for an ERISA 4204 arrangement include the following. First, the buyer becomes obligated to contribute with respect to the covered operations under the collective bargaining agreement. Substantially, the same number of contribution base units that the seller was obligated to contribute prior to the transaction.

Second, the buyer provides the plan with a bond or Escrow for a period of five years after the closing, in an amount equal to the greater road. The seller's average contribution base units for the three preceding years to three years preceding the sale, or the seller's contribution for the immediately preceding year. Third, the asset purchase agreement must provide that the seller is secondarily liable to the plan in the event of any partial withdrawal, or a complete withdrawal by the buyer during the first five years after the asset sale.

If those requirements are satisfied, an employer will not incur a partial withdrawal or a complete withdrawal by ceasing covered operations or ceasing to have an obligation to contribute as a result of a sale of assets. This of course, is going to need to be fully disclosed and acceptable to the multiemployer plan. A Section 4204 arrangement can be valuable to both the seller and the buyer in an asset sale, and could be a material term of their transaction. Here's why. If the buyer intends and expects to continue the operations covered by the collective bargaining agreement for at least five years after the asset sale, and in fact, does so.

Then, entering into the Section 4204 arrangement ultimately puts the buyer in no worse position economically in terms of withdrawal liability exposure after that five-year point. But from the seller side, if there's no withdrawal liability at the time of the transaction, due to the Section 4204 arrangement, and there's no withdrawal by the buyer during this five-year period, then the seller avoids the expensive withdrawal liability that they would have otherwise incurred. Or, any secondary liability if the buyer had withdrawn during that five-year period.

But just as an observation, this is typically the subject of negotiation between the parties. Because if everything is lined up in this way, and it's reasonably expected to turn out that there's no withdrawal during the five-year period after the asset sale. Then, the buyer might reasonably bargain for a lower purchase price in consideration for the fact that the seller will not trigger withdrawal liability, as well as the risk that the buyer is taking on by assuming the seller's contribution history.

With that said, we've touched briefly on the implications of multiemployer pension plans with respect to control group members, control group members of the seller. Let's go a little bit deeper into that. Pursuant to ERISA, all trades or businesses under common control are generally treated as a single employer in connection with employee benefit plans. This group of traits or businesses under common control is referred to as the control group.

In the event of an employer's withdrawal from a multiemployer pension plan, whether it's a partial withdrawal, complete withdrawal. or a mass withdrawal, the members of the employers control group may be subject to liability. The exposure of control group members to withdrawal liability payment applications will arise if the employer defaults on withdrawal liability payments. In which case, multiemployer plans in furtherance of their ERISA fiduciary duties will seek payment from the control group members.

For the control group members, this is often an unknown liability. A control group member may not even be aware that it's part of the control group, or that another member of the control group contributes to a multiemployer plan. Further, some courts have looked to expand the meaning of "trades or businesses under common control", and thereby expand the reach of control group liability. This is something we saw in the Sun Capital cases in the First Circuit about a decade ago. As a result, diligence will want to confirm whether there's any hidden withdrawal liability exposure with respect to targets control group members. Chris, I know there's some other important aspects to this that you would like to add.

Chris Stock:

Yes. Thanks, Paul. Most purchases expect when they purchase the assets of another business, as opposed to purchasing the shares of a corporation. They're shielded from most, if not all of the selling businesses existing liabilities. However, in recent years, multiemployer plans have been actively pursuing unpaid withdrawal liability claims against the buyers of a withdrawing employer's assets even when the traditional successor liability criteria isn't met. The Supreme

Court has recognized that a successor company may be deemed to have assumed the liabilities of its predecessor company if the successor had notice of the predecessor's liability. And there's a substantial continuity of identity in the business enterprise.

Some courts have even concluded that having notice of the contingent withdrawal liability was sufficient to meet the notice requirement for successor liability. Further, buyers who are purchasing assets from a company that has or had an obligation to make contributions to a multiemployer plan should carefully consider the extent to which the post sale operations might be viewed as substantially continuous of the seller's business. Historically, there have been numerous factors examined by the courts to determine if continuity of enterprise existed. Including whether the new employer used the same plan, employer used substantially the same workforce under the same working conditions, used the same machinery, and equipment, and manufacture the same product as the previous company.

In conclusion, understanding the intricacies of multiemployer pension plans and their potential liabilities is crucial for businesses involved in mergers and acquisitions. A buyer of a business that contributes to a multiemployer pension plan face a series of unique considerations, including balancing the economics of continued participation, or withdrawal, as well as evaluating the risks of changes to the legislative environment. These plans have far-reaching impacts and navigating their complexities requires careful planning, because the risk and potential liabilities are substantial. Thank you for joining us, and please make sure to check out future podcasts in this series. Thanks.