Can a Merger Save Your Pension Plan?

A merger may be a lifesaver for a financially troubled pension plan. The Multiemployer Pension Reform Act allows the Pension Benefit Guaranty Corporation to help plans with a merger.

by | **Lisa M. Schwantz**

benefits
MAGAZINE

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A defined benefit pension plan may be able to fix its financial problems or at least improve its financial situation by merging with a healthier or larger pension plan. However, one of the most challenging aspects of a merger is finding a suitable merger partner. This problem is compounded if a pension plan is in endangered or critical status.

There are many ways to accomplish a merger that comply with the Employee Retirement Income Security Act of 1974 (ERISA). And the Multiemployer Pension Reform Act of 2014 (MPRA), passed at the end of 2014, allows the Pension Benefit Guaranty Corporation (PBGC) to assist plans in merging.

Fiduciary Obligations

Trustees are required to act prudently when determining whether or not to merge their pension fund. The Department of Labor (DOL) requires that fiduciaries gather "all relevant facts and circumstances" when exploring a merger. DOL guidance provides that trustees must consider the funded status of the resulting merged plan, as well as the long-term financial viability of such plan. Fiduciaries are to take into account (1) the economic outlook of the industry, (2) demographics of the merged plan's participant population, (3) current and anticipated contribution rates and (4) administrative expenses.

There is some regulatory guidance that states that merging plans is a settlor function. *Settlor functions* are those activities that relate to the establishment, design and termination of plans. Settlor decisions are not subject to Title I of ERISA and therefore are not subject to the fiduciary standards. DOL *Field Assistance Bulletin 2002-2* states in part that when relevant documents (e.g., collective bargaining agreements, trust documents and plan documents) contemplate that the board of trustees of a multiemployer plan will act as fiduciaries in carrying out activities that would otherwise be settlor in nature, such activities would be governed by the fiduciary provisions of ERISA. It goes on to say that when the relevant plan documents are silent, then the activities of the board of trustees that are settlor in nature generally will be viewed as carried out by the board of trustees in a settlor capacity, and such activities would not be fiduciary activities subject to Title I of ERISA. Settlors cannot use plan assets for expenses for actions they take on behalf of a pension plan.

takeaways >>

- Pension plan trustees considering a merger must consider the resulting funded status and the longer term viability of a merged plan.
- Besides improving the funded status of one or both plans, mergers can result in administrative cost savings and more flexible investment options.
- Trustees considering a merger must complete extensive due diligence, studying plan documents and determining whether either plan is being investigated by the government.
- PBGC must determine whether a merger complies with the law.
- A plan, even though in critical or endangered status, may be able to merge if it passes one of two solvency tests.
- MPRA allows PBGC to provide financial assistance and other help with a merger.

There are many reasons for pension plans to merge. While the most obvious is to improve the funding position of one or both pension plans, mergers can produce administrative cost savings or greater flexibility with regard to investment options.

Due Diligence

To determine whether the merger will comply with legal requirements and achieve the trustees' goals, it is important for trustees to complete their due diligence. Many documents will be requested from each plan, including but not limited to (1) the plan document with all amendments, (2) the trust agreement with all amendments, (3) the summary plan description, (4) the latest Internal Revenue Service (IRS) determination letter, (5) Forms 5500 and audited financial statements for at least the preceding five years, (6) actuarial valuations for at least the preceding five years and (7) collective bargaining agreements to confirm they do not prevent the merger and what the expected contributions are.

Trustees should also determine whether either plan is under investigation by any government agency. It is during due diligence that benefit levels for the merged plan are evaluated and consideration is given to the future governing structure, such as the number of trustees or form of administration.

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Requirements

PBGC is a federal agency created by ERISA to protect pension benefits for private sector defined benefit plans. PBGC is funded by annual premiums from those plans. If a multiemployer pension plan is no longer able to meet the benefit obligations that have previously been promised, then PBGC steps in to assist that plan to pay certain minimum benefit levels, which top out at less than $14,000 a year for 30-year participants. Before the passage of MPRA, pension benefits in pay status were subject to reduction or suspension only if a plan was about to become insolvent. (PBGC does not take over multiemployer plans; it provides financial assistance for plans to pay minimum PBGC guarantees.) Depending on the plan's benefit levels, these reductions can be significant, having a detrimental effect on participants and beneficiaries. Therefore, mergers have a definite appeal if such reductions can be avoided.

PBGC is responsible for determining whether pension plan mergers comply with applicable law. The following requirements must be met:

- No participant's or beneficiary's accrued benefit will be lower immediately after the effective date of the merger than the benefit immediately before that date.
- The benefits of participants and beneficiaries are not reasonably expected to be subject to suspension after the merger (reduced to PBGC minimums).
- An actuarial valuation of the assets and liabilities of each of the affected plans has been performed during the plan year preceding the effective date of the merger or transfer, based upon the most recent data available as of the day before the start of that plan year, or other valuation of such assets and liabilities.

- PBGC is notified of the merger at least 120 days prior to the merger's effective date.

The notice informs PBGC of the merger and asserts that the merger complies with the applicable law. Plan sponsors may also request a compliance determination from PBGC that the merger transaction indeed meets all legal requirements. PBGC may waive the 120-day advanced notice requirement if the plan sponsors demonstrate that failure to complete the merger within the applicable time period will harm the participants, PBGC determines that the merger complies with the ERISA requirements, or PBGC completes its review of the transaction. If the plan sponsors forgo the compliance determination by PBGC, then the timing of the notice decreases to 45 days prior to the effective date of the merger.

A plan being in the *red zone* (critical status) or *yellow zone* (endangered status) does not preclude it from merging with another plan. The merged plan just has to pass one of two solvency tests.[1] The first solvency test is that the merged plan's expected fair market value of plan assets immediately after the merger equals or exceeds five times the benefit payments for the last plan year ending before the proposed effective date of the merger or transfer. The other test is that in each of the first five plan years beginning on or after the proposed effective date of the merger, expected plan assets plus expected contributions and investment earnings equal or exceed expected expenses and benefit payments for the plan year. The actuary will be able to determine whether the merged plan meets either of these tests.

There is a special plan solvency rule for mergers that are considered *de minimis*.[2] The determination of whether a *de minimis* merger satisfies the plan solvency requirement may be made without regard to any other *de minimis* mergers or transfers that have occurred since the last actuarial valuation. A merger is *de minimis* if the present value of accrued benefits (whether or not vested) of one plan is less than 3% of the fair market value of the other plan's assets.

Generally, mergers are prohibited if there is an expectation of plan insolvency that would lead to a suspension of benefits under ERISA. Insolvent plans can receive assistance from PBGC and may be able to benefit from the new partition and suspension provisions adopted in MPRA.

Help From PBGC

Passage of MPRA opened the door for PBGC to provide additional assistance to plans seeking to merge. If PBGC determines that the merger is in the best interest of at least one plan and not reasonably adverse to the overall interests of the participants and beneficiaries of both plans, it can facilitate the merger. Facilitation includes training, technical assistance, mediation, communication with stakeholders and support-related requests to other government agencies.

The most significant tool granted to PBGC is the ability to offer financial assistance to facilitate mergers if:

- One or more of the plans is in critical and declining status
- PBGC reasonably expects that the financial assistance will reduce its expected long-term loss with respect to the plans involved
- PBGC reasonably expects that the assistance is necessary for the merged plan to become or remain solvent
- PBGC certifies that providing such assistance will not jeopardize its ability to assist other plans in the future
- The financial assistance is paid from PBGC's multiemployer benefit fund.

There is still hope for a plan that is in critical or endangered status. MPRA has broadened the tools available for both the trustees and PBGC to effectuate a merger that forestalls insolvency and provides sufficient retirement benefits to participants.

Endnotes

1. 29 C.F.R. §4231.6.
2. 29 C.F.R. §4231.7.

<< bio

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