

# Employee Benefits in Mergers and Acquisitions

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# Structure of Presentation

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- **Objectives/Responsibilities**
  - **Identify and Quantify Liabilities**
  - **Structure Post-Close Benefits for Transferring Employees**
  - **Negotiate Purchase/Sale Agreement**
- **Structure of Transaction**
  - **Stock acquisition**
  - **Asset acquisition**
- **Typical (and not so typical) Benefit Liabilities**
- **Post-Closing Benefits Options and Issues**
- **Purchase/Sale Agreement: Issues and Options**



# Structure of the Transaction

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## ■ **Stock Acquisition**

- Target's benefit plans transfer by operation of law
  - ❖ Parties can negotiate different result
  - ❖ Target employees may participate in plans of parent or other affiliate
- Buyer acquires compliance risks

## ■ **Asset Acquisition**

- Less typical for benefit plans to transfer to buyer
- Buyer needs to offer alternative benefits
- Parties can negotiate transfer of particular plans, or portions of plans

# Benefit Liabilities: Generally

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## ■ Sample checklist items:

- Employee census information:
  - ❖ Name/SSN/DOB/DOH
  - ❖ Comp and benefits details
- Employment contracts, written or otherwise
- Plan documents and all amendments
- Summary Plan Descriptions and Summaries of Material Modification
- Insurance and group annuity contracts
- Most recent IRS Determination or Exemption Letters
- Trust documents and trust statements
- Collective bargaining agreements
- Funding and other financial information, including but not limited to valuation reports, withdrawal liability for any applicable plans
- Details of all EPCRS and other corrective actions for operational or form defects

# Benefit Liabilities: Generally (continued)

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- Sample Checklist Items (continued)
  - Forms 5500, with all schedules, audits and actuarial reports
  - Vendor contracts
    - ❖ HIPAA business associate agreements
  - All claims and appeals files
  - Enrollment materials: communications and sample forms
  - COBRA, HIPAA and all other legally required notices and certificates
  - Detailed records of COBRA qualified beneficiaries and status
  - Other employee communications
  - Employee manual or handbook
  - All policies for vacation/PTO/leave
  - Severance pay plans, policies, individual agreements and unwritten practices
  - Committee minutes, 408(b)(2) efforts, other governance matters



# Benefit Liabilities: Tax Qualified Retirement Plans

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- Defined Benefit Plans
  - Underfunded? Liability for plans of other members of target's controlled group?
  - Union multiemployer plan withdrawal liability
  - PBGC premium and reporting obligations
- Plan document timely updates and IRS approvals

# Benefit Liabilities: Tax Qualified Retirement Plans (Continued)

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- Plan Operations
  - ❖ Follow plan terms
  - ❖ For 401(k) plans: Timeliness of remittance of employee contributions
  - ❖ Testing
  - ❖ Compliance with legal operational requirements – e.g. loans or distributions
  - ❖ Self-audit and EPCRS activity v. IRS audits or CAP penalties
- Governance and fiduciary performance
  - Prohibited transactions or fiduciary breaches
  - Plan fees
  - Reporting and disclosure obligations



# Benefit Liabilities: Health, Welfare and Fringe Plans

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- Plan Operations
  - ERISA claims and other requirements and compliance with plan terms
  - Health care reform requirements
  - Required notices and communications
- Nondiscrimination Testing
  - Medical, cafeteria, group life, dependent care FSAs and adoption assistance plans
- Retiree Medical Plans
  - Ability to amend or terminate
- PTO/Vacation/Sick Leave Policies
  - Financial liabilities
  - Paid out or transferred to Seller
- Severance Plans, Individual Agreements and Other Commitments
  - Will transaction trigger liabilities?
  - Is Buyer or Seller responsible?





## **Benefit Liabilities: Nonqualified Equity and Like Plans**

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- SERPs/Excess Plans/Individual Arrangements
- Compliance with 409A
  - IRS self-correction program/activity
  - Commitments to gross up participants?
- Top Hat Plans
  - Realistic case for top hat status?
  - One time top hat filing completed?
- Funding status – Rabbi Trusts? Insurance?



# Benefit Liabilities: Other

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- For All Plans: identify liabilities created by planned acquisition
  - Change of control or like provisions:
    - ❖ Springing accruals /benefits
    - ❖ Automatic or accelerated vesting
    - ❖ Springing funding obligations
  - Employment agreement commitments

# Post-Close Benefits Structure: Generally

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- Buyer Needs to Consider
  - Whether to assume particular plans
  - How to deliver benefits to acquired employees if it doesn't assume plans
  - Big factors include
    - ❖ Costs/degree of funding
    - ❖ Compliance/taint
    - ❖ Whether plans fit into Buyer's existing benefits culture
    - ❖ Testing implications
  - Whether to require termination of plans pre-closing
  - Required transition efforts
- Seller needs to consider
  - Buyer's above requests
  - Seller requests to protect transferred employees
  - For plans that aren't transferred – terminate/amend?



# Post-Close Benefits Structure: Tax-Qualified Retirement Plans

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- General Concerns
  - Funded status
  - Taint/compliance status
  - Testing status post-closing
  - 411(d)(6) protections
- Defined Benefit Plans
  - Seller retains plan
  - Seller transfers plan or portion of plan



## Post-Close Benefits Structure: Tax-Qualified Retirement Plans (Continued)

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- Defined Contribution Plans (e.g. 401(k) Plan)
  - Seller retains plan
    - ❖ Rollover
    - ❖ Loans
  - Seller transfers plan or portion of plan
  - Seller terminates plan



## **Post-Close Benefits Structure: Health, Welfare and Fringe Plans**

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- **Stock acquisition**
  - **Target's plans typically continued for short term**
  - **Buyer can assimilate employees into Buyer's benefits culture over time**
- **Asset acquisition**
  - **Clone plans**
    - ❖ **Continuation of comparable or same benefits for employees**
    - ❖ **Significant stand up effort**
    - ❖ **Legally new plans of buyer based on terms of Seller's plans**
  - **Force employees into Buyer's plans**
- **FSAs**
  - **Short year**
  - **IRS sanctioned alternatives**
- **MEWAs**



# Post-Close COBRA Obligations

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- **COBRA in Stock Acquisition**
- **COBRA in Asset Acquisition**
  - Seller maintains any plan = Seller
  - Seller does not maintain plan = Buyer if successor employer
  - Parties can contract differently but liability if other fails to perform

## Post-Close Benefits Structure: Nonqualified Plans

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- Distributions Triggered?
  - Stock deal = no separation
  - Asset deal = separation unless parties agree otherwise
- Change in Control
  - = 50% stock, 40% of assets or majority of Board
  - If CiC, plan terms may require payout
  - If CiC but plan terms do not require payout, sponsor of plan post-close can terminate plan and payout benefits to affected employees
- Assign Plan
  - If plan survives closing, parties can assign responsibility to Buyer or Seller
  - If Seller retains plan, Seller needs Buyer to communicate future separations
- Release/Waiver of Seller by Employees





## Purchase/Sale Agreement: Benefits Provisions Generally

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- **Seller representations**
- **Seller pre-closing covenants**
- **Closing covenants**
- **Transition Services Agreement**

# Purchase/Sale Agreement: Seller Reps

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## ■ Seller Reps

- Employees
- Plans
- Documents, communications, filings, Etc.
- Various compliance representations – ERISA, Code, PTs, Funding, Reporting, Etc.
- Absence of audits, investigations, examinations, legal actions

## ■ Negotiation Issues

- Seller discloses all plans or only material plans?
- Seller commits to comprehensive disclosure of everything or only requested items?
- Material or absolute compliance?
- Disclosure of all problems or only known problems?
- Representations cover only Target plans or all Seller plans?
- Catch-All representations

# Purchase/Sale Agreement: Seller Pre-Closing Covenants

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- Seller Covenants re Period Prior to Closing
- Affirmative Acts
  - Spin-off or create new plans that can be assumed by Buyer
  - Separate vendor or insurance arrangements so that Buyer can assume contract
- Commitments to Refrain from Certain Acts
  - No change in plans, benefits, compensation
  - No creation of new benefit plans or compensation arrangements
  - No movement of employees from one plan to another
  - Carve outs?
    - ❖ Changes already contracted
    - ❖ Changes already announced
    - ❖ Changes required by law
    - ❖ Changes in accordance with ordinary course of business

# Purchase/Sale Agreement: Buyer and Seller Covenants

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- Buyer and Seller Closing Commitments
  - Specify which party takes which ongoing plans and liabilities
    - ❖ Plan by plan
  - Specify whether all of a plan's assets and liabilities move:
    - ❖ Who takes retirees and deferred vested former employees?
  - Specify who satisfies severance obligations
    - ❖ Seller covers severance costs triggered by sale?
    - ❖ Buyer assumes future severance obligations?



## Purchase/Sale Agreement: Buyer and Seller Covenants (continued)

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- Special Circumstances
  - Special FSA accommodations?
  - Commit that there won't be a separation from service for NQDC plan purposes?
- Post-Close Buyer Commitments
  - Commitment to maintain benefits for period of time
  - Commitment to give service credit for time with Seller



## Purchase/Sale Agreement: Transition Services Agreement

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- Buyer needs Seller to expressly commit to provide all needed transition services
  - Payroll services
  - Administrative or recordkeeping services
  - Assign contracts or relationships or negotiate commitments from vendors
- Seller should avoid inadvertently stepping into benefits outsourcing business
  - Should expressly avoid any fiduciary role/function for Buyer's plan
  - Should cap liability and acquire indemnity protection from Buyer
  - Obtain termination right if Buyer fails to maintain plans as clones of Seller's plans



**Questions?**

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## Section 230 Disclaimer

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