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## **ERISA Successor and Affiliate Liability**

Navigating Controlled Group and Successor Liability Rules for Defined Benefit Pension Plans

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1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

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Today's faculty features:

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# ERISA Successor and Affiliate Liability

## Navigating Controlled Group and Successor Liability Rules

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Michael J. Prame, Principal, Groom Law Group

Lars C. Golumbic, Principal, Groom Law Group

# Overview

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- **Controlled Group Liability**
  - Identifying Group Members
  - Analyzing Potential Liability of Controlled Group
  - Analyzing Potential Liability of Controlled Group – Private Equity Funds
- **Successor Liability**
  - Asset Sales
  - Mergers and Other Changes in Corporate Form
  - Sham Transactions
- **Alter Ego Liability**

# Controlled Group Liability – Identifying Group Members

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- Certain employee benefit liabilities are an obligation of the plan sponsor or contributing employer and each member of its “controlled group.”
- For this purpose, a controlled group is a group of trades or businesses that is treated as a single employer under Code § 414(b) or (c).

# Controlled Group Liability – Identifying Group Members

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- Members of a controlled group may be persons organized as a corporation, partnership, proprietorship, trust or estate.
- A limited liability company (LLC) may elect to be treated either as a corporation or a partnership for federal tax purposes.

# Controlled Group Liability – Analyzing Potential Liability of Controlled Group

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- Controlled group of corporations
  - Parent-subsidiary group –
    - One or more chains of corporations connected through at least 80% stock ownership, by vote or value, with a common parent corporation
  - Brother-sister group –
    - Five or fewer persons who are individuals, estates or trusts
    - Together own at least 80% of the total vote or value of stock of each corporation
    - And the sum of the overlapping stock ownerships is at least 50%
  - Combined group

# Controlled Group Liability – Analyzing Potential Liability of Controlled Group

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- Trades or Businesses under Common Control
  - Parent-subsidary group –
    - One or more chains of organizations conducting trades or businesses connected through a “controlling interest”
  - Controlling interest means –
    - For a trust, 80% actuarial interest (assumes maximum exercise of discretion in favor of beneficiary)
    - For a partnership, 80% capital or profits interest
    - For a sole proprietorship, ownership
  - Combined group

# Controlled Group Liability –

## Analyzing Potential Liability of Controlled Group – Private Equity Funds

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- Trade or business is not defined in the Internal Revenue Code
  - Engaged in the activity for the primary purpose of income or profit and with continuity and regularity. Commissioner of Internal Revenue v. Groetzinger, 480 U.S. 23 (1987).
  - Some courts have treated ownership of property used by another operating company as a trade or business. PBGC v. Center City Motors, 609 F. Supp. 409 (S.D. Cal. 1984).
  - Others have held that mere ownership of land is not a trade or business. Textile Workers Pension Fund v. Oltremare, 764 F. Supp. 287 (S.D.N.Y. 1989).

# Controlled Group Liability –

## Analyzing Potential Liability of Controlled Group –

### Private Equity Funds

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- PBGC has taken the position that a private equity fund is a trade or business.
  - PBGC Appeals Board Letter dated Sept. 26, 2007
  - Sheet Metal Workers National Pension Fund v. Palladium Equity Partners, LLC, 722 F. Supp. 2d 854 (E.D. Mich. 2010) (citing with approval PBGC Appeals Board Letter)
- Some courts have found that a personal enterprise, such as renting a vacation home, is a trade or business.

# Controlled Group Liability –

## Analyzing Potential Liability of Controlled Group

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- Generally, the controlled group for purposes of liability is determined as of a snapshot date.
  - Date of plan termination for a single employer pension plan
  - Date of withdrawal for withdrawal liability
    - Trucking Employees of NJ Welfare Fund v. Bellezza Co., 57 Fed. Appx. 972, 2003 WL 262505 (3d Cir. Feb. 6, 2003).



# Controlled Group Liability –

## Analyzing Potential Liability of Controlled Group

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- Controlled group membership is mechanical, generally determined without regard to member's intent or knowledge
- Applies to liability for minimum funding contributions
- Can apply to COBRA obligations

# Successor Liability –

## Asset Sales

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- Asset purchaser may have successor liability for delinquent multiemployer plan contributions or withdrawal liability.
- Upholsterers' Int'l Union Pension Fund v. Artistic Furniture of Pontiac, 920 F.3d 1323 (7<sup>th</sup> Cir. 1990)
  - Seventh Circuit ruling that liability could be imposed after an asset sale where there was sufficient continuity of operations and the successor had notice of the liability.
  - Seventh Circuit's ruling derived from federal labor law test for determining whether a successor employer is liable to correct a predecessor's unfair labor practices.

# Successor Liability –

## Asset Sales

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- Einhorn v. M.L. Ruberton Constr. Co.  
(3d Cir. 2011)
  - Followed reasoning in *Artistic Furniture* to find availability of successor liability to multiemployer plan contributions in context of asset sales.
  - Adopted *Artistic Furniture* factors:  
(1) continuity of operations; (2) notice of the liability.

# Successor Liability –

## Asset Sales

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- Successor liability has been asserted successfully even in the context of bankruptcy.
- Chicago Truck Drivers, Helpers & Warehouse Workers Union (Ind.) Pension Fund v. Tasemkin, Inc., 59 F.3d 48 (7<sup>th</sup> Cir. 1995)
  - 7th Circuit found no reason to accord a purchaser of a formally bankrupt entity any “special measure of insulation from liability” because the sale took place in the context of a bankruptcy proceeding.

# Successor Liability – Mergers and Other Changes in Corporate Form

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- Successor liability also has been applied in the context of a merger.
- Teamsters Pension Trust Fund of Phila. & Vicinity v. Littlejohn, 155 F.3d 206 (3d Cir. 1998)
  - Third Circuit permitted imposition of successor liability in context of a merger, even where successor did not have notice of the liability.
  - Third Circuit reasoned that, contrary to context of merger, a successor in asset sale would have a financial incentive to inquire about seller's previous liabilities to negotiate for lower purchase price.

# Successor Liability – Mergers and Other Changes in Corporate Form

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- Section 4218 of ERISA provides that a withdrawal will not occur under ERISA solely because an employer ceases to exist as a result in change in corporate structure.
- CenTra Inc. v. Central States Se. and Sw. Areas Pension Fund, 578 F.3d 592 (7<sup>th</sup> Cir. 2009)
  - Seventh Circuit found that a reorganized corporation properly “inherited” the contribution histories of its old subsidiaries for purposes of determining withdrawal liability.

# Successor Liability – Sham Transactions

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- In single employer context, if principal purpose of any entity in entering transaction is to evade liability, and transaction becomes effective 5 years before a plan's termination, entity and its controlled group can be liable as if entity were contributing employer. ERISA § 4069(a).
- In PBGC v. White Consolidated Indus., 215 F.3d 407 (3d Cir. 2000), company was found to have engaged in an evasion transaction by transferring underfunded plans in a highly-leveraged buyout.

# Successor Liability – Sham Transactions

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- In multiemployer plan context, if a principal purpose of any transaction is to evade or avoid liability, then plan is to determine and collect liability regardless of the transaction. ERISA § 4212(c).
- Santa Fe Pacific Corp. v. Central States, Se. & Sw. Areas Pension Fund, 22 F.3d 725 (7<sup>th</sup> Cir. 1994)
  - Seventh Circuit held that sale of stock was a sham transaction where the employer chose to sell the stock of the company to avoid withdrawal liability.



# Alter Ego Liability

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- Developed in the context of federal labor law.
- Core purpose is to prevent employer from evading obligations through sham transaction or technical change in operations.
- Factors may include degree of overlap in management, business purpose, operation, equipment, customers, supervision, and ownership.

# Alter Ego Liability

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- Retirement Plan of the UNITE HERE Nat'l Retirement Fund v. Kombassan Holding A.S., 629 F.3d 282 (2d Cir. 2010)
  - Second Circuit found sufficient facts to show commonality of control and business purpose between corporation and other contributing employer to pension plan.
- Resilient Floor Covering Pen. Fund v. M&M Install., 630 F.3d 848 (9<sup>th</sup> Cir. 2010)
  - Ninth Circuit suggested that district court consider on remand whether "evade or avoid" provision under section 4212(c) of ERISA is intended to be sole route of redress.

# Alter Ego Liability

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- At least one court has rejected extension of alter ego theory to apply to a trade or business under common control with a contributing employer.
  - Government Dev. Bank for Puerto Rico v. Holt Marine Terminal, No. 02-7825, 2011 WL 1135944 (E.D. Pa. Mar. 24, 2011)

# Alter Ego Liability

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- PBGC has asserted “alter ego” doctrine as a basis for recovery against controlled group members outside of United States.
- PBGC takes the position that controlled group liability is extra-territorial. PBGC Opinion Letter 97-1 (May 5, 1997).
- U.S. court jurisdiction over non-U.S. company presents a practical problem.
  - Rejection of claim if minimum contacts do not exist in the U.S. – GCIU-Employer Ret. Fund v. Goldfarb Corp., 565 F.3d 1019 (7<sup>th</sup> Cir. 2009)
  - PBGC v. Asahi Tec Corp., No. 10-cv-01936 (D.D.C., filed Nov. 12, 2010)

# Alter Ego Liability

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- PBGC has obtained leverage to negotiate additional recoveries based on non-U.S. controlled group members by filing a notice of federal lien with the Recorder of Deeds of the District of Columbia, following the procedure for filing a tax lien on personal property of a taxpayer outside the U.S. IRC § 6323(f).

# Questions?

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