Although multiemployer pension plan mergers are heavily regulated by the Employee Retirement Income Security Act (ERISA) and are the subject of many articles and much discussion, there is almost no ERISA regulation of multiemployer health and welfare fund mergers. This article focuses on the principal legal and practical issues that should be considered by trustees and plan professionals in connection with mergers between multiemployer health and welfare plans.

Merging Multiemployer Health and Welfare Funds: A Practical Guide

by Mitchel D. Whitehead, Carrie J. Grove and Nicholas J. Waddles

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There is no shortage of rules and regulations that apply to mergers among multiemployer pension plans: from the funding, notice and procedural rules contained in ERISA;[1] to the requirement that such mergers be submitted to the Pension Benefit Guaranty Corporation (PBGC) in advance for approval; to the numerous books, articles and other publications written by benefits practitioners on the subject.

Conversely, mergers between multiemployer health and welfare plans are subject to almost no federal regulation, require no advance approval by federal agencies and are the subject of very little published guidance. The purpose of this article is to give plan trustees and administrators a practical guide to the merger of two or more multiemployer health and welfare funds. The authors also provide an Internet link to a general form of merger agreement that illustrates many of the issues that should be addressed in any merger transaction. The authors begin, however, with a very brief summary of the principal legal requirements involved.

ERISA Considerations and Other Legal Requirements

As noted above—and somewhat incredibly—there are no substantive ERISA requirements for mergers involving multi-

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employer health and welfare funds. Moreover, there are very few reported cases that involve health fund mergers; and none of these cases deal meaningfully with the due diligence, procedural or other requirements of accomplishing a merger (although there is some authority on the related issue of whether participants who withdraw from a welfare plan and move to another plan are entitled to a transfer of a ratable portion of reserves from the original plan).[2]

Settlor Function vs. Fiduciary Decisions

The merger of two or more multiemployer health funds can be divided into two separate and distinct stages: (1) the initial decision to merge the funds, and (2) the process of implementing that decision. The decision to merge multiemployer health funds is most commonly made by the bargaining parties and is reflected in a collective bargaining agreement that instructs the trustees of the funds to be merged and to take all necessary steps to implement the merger.

The 2007 decision in *Beck v. Pace,* by the U.S. Supreme Court, recognized that an employer's decision refusing to merge its pension plan into a multiemployer pension plan was a settlor function immune from the fiduciary considerations of ERISA.[3] However, there is no doubt that once a decision to merge has been made, trustees must implement that decision in compliance with ERISA's general fiduciary duties to act prudently, for the exclusive benefit of participants and in accordance with the plan documents.

Despite possible application of the settlor function rule to the merger decision, trustees would be well advised to be prepared to defend independently both the rationale for the merger (as benefiting plan participants over time) and the due diligence supporting the "economics" of the transaction (that no material funding problem will result).[4] This usually does not present a serious problem in the multiemployer context, since (a) the bargaining parties and the trustees are often the same people; and (b) the plan sponsors (the employers and the unions) generally work with consultants and advisors in advance to assess the workability, financial impact and other implications of a potential merger well before negotiating the terms and including them in a bargaining agreement. In other words, the due diligence is generally done by the bargaining parties well before the trustees are instructed to act. Regardless of who does the due diligence on the merger decision, and when, it should at a minimum address (a) whether the transaction will cause a material funding problem for either of the plans, and (b) whether the merger will cause any material disadvantage to plan participants over time.

If, however, due diligence has not been done to the trustees' satisfaction, or the trustees determine that the merger is not workable or perhaps cannot be justified from a fiduciary standpoint, the trustees will then need to confront the very difficult question of whether they have the authority to disregard a directive in the collective bargaining agreement and refuse to merge the funds. This question will ultimately depend on exactly what rights and responsibilities are granted to the trustees versus the bargaining parties in the trust agreement and the collective bargaining agreements establishing the relevant funds.[5]

Fiduciary Duties—Do the Deal Right

Quite apart from the decision of whether to merge (usually made by the bargaining parties), the trustees must ensure that their actions and decisions during the second stage of the merger (i.e., the implementation stage) are fully consistent with the general fiduciary requirements of prudence, exclusive benefit and adherence to the plan documents.

A key element in complying with these requirements in the merger context is the trustees' performance of the appropriate "transactional" due diligence (i.e., making sure the deal is done right). This phase of the merger process is very important, both in terms of implementing the deal prudently and in clearly documenting what steps were taken. Trustees should not hesitate to insist that plan professionals provide their input as to exactly what due diligence steps are required and/or recommended. The due diligence process should involve all key plan professionals, including the administrative staff, attorneys, consultants and accountants. Due diligence also requires a thorough review of all relevant plan documents, including the trust agreement, plan document, plan

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rules, regulations and procedures, applicable collective bargaining agreements, summary plan description, financial statements, Form 5500 filings, fiduciary liability insurance (including any pending claims against the policy), fidelity bond, and all service provider agreements and reports (such as HMOs, PPOs and other insured arrangements). The trustees and plan professionals should review all existing investments and analyze the impact of the merger on these investments. In addition, it should be determined how administrative and other costs will be affected by the merger.

One useful tool to help manage this process is a due diligence checklist prepared by plan professionals showing all steps required to complete the merger, along with a time line showing when each step will be completed. There is no more effective way for trustees to get the "big picture" on the transaction and to fully appreciate the time frames involved. In the authors' experience, mergers generally take more time and effort to finalize than originally expected.

ERISA requires fiduciaries to act in accordance with the documents that govern a plan as long as they are consistent with ERISA. Therefore, in reviewing all of the trust agreements, bargaining agreements and other plan documents as part of the due diligence process, the trustees will need to determine whether there are any contractually required conditions, notices, filings or other steps that must be satisfied before the merger can be completed. The review also should serve to ensure that each employer's obligation to make contributions will pass to, and be enforceable by, the surviving fund.[6]

Another important reason for due diligence review is to ensure that the trust agreements specifically address the trustees' ability to authorize a merger of the funds, and/or to implement a merger that has been authorized by the bargaining parties. Although the trustees of multiemployer health funds may have the power to authorize and implement a merger under the general powers provided to them in most trust agreements, if the power to authorize or implement a merger is not specifically mentioned, the trustees should consider adopting amendments to the trust agreements that specifically grant the trustees these powers.

Prohibited Transactions

The prohibited transaction rules of ERISA must also be considered in a merger transaction. The rules will be implicated if any of the plans involved are "parties in interest" with regard to each other (since ERISA prohibits certain transactions between plans and parties in interest), or the plans have common trustees (since ERISA's fiduciary self-dealing rules prohibit trustees from acting on both sides of a transaction).

It is not always easy to determine whether the funds involved in the merger are considered parties in interest since it is not unusual for the merging funds to be closely related with common trustees, the same administrator, or the same sponsoring employers or unions, or to be part of the same industry.

These relationships alone would not automatically cause the funds to be parties in interest with respect to each other. The funds would likely be parties in interest only if one of the funds provided services to the other (e.g., administrative services, leasing office space, etc.), or if they provide coverage to each other's administrative employees.

Because it may be difficult to determine whether a fund is a party in interest to a closely related fund, the trustees should request that plan counsel review the current relationship between the funds and any anticipated transactions with other parties in connection with the merger to determine whether any transactions involve parties in interest and violate the prohibited transaction rules.

Similarly, ERISA's self-dealing rules could pose a problem for a merger, particularly with regard to any common trustees.[7] Although Congress created an exception to the prohibited transaction rules for pension fund mergers involving common trustees, the exception does not explicitly extend to mergers of health and welfare funds.[8] There are a number of strategies for dealing with this problem, including having the common trustees abstain from all relevant discussions and votes. This is another issue on which it is essential to have the advice of legal counsel.

Notice Requirements

While there is no statutory requirement to provide advance notice of the merger of multiemployer health funds, certain notices should be provided both before and after the merger becomes effective.

Advance Notice to Affected Parties

Merger transactions are often accompanied by elaborate communication campaigns designed to inform participants and minimize anxieties about the deal. Communication can reduce enrollment, eligibility, benefit change and other transition problems.

Campaigns often involve one or more meetings with participants to answer questions and to assist in any required enrollments, applications and so on. At a minimum, the trustees of funds involved in the merger should provide participants, beneficiaries, contributing employers, affected unions and any other interested parties with advance written notice of the merger. Ideally, the notice should describe the impending transaction; set forth the closing date; describe the benefit changes that become effective after the closing; explain any required enrollment, elections and eligibility steps; and provide the parties with appropriate contact information in order to address any issues that arise during the transition period. The notice to contributing employers must also specify where contribution checks are to be sent after the merger.

Of the information to be provided in the notice, it is particularly important to give participants and beneficiaries detailed information regarding timing, enrollment deadlines and elections, and how the benefits will change once the funds are merged. Because it is unlikely that any two funds will have the same benefit structure, the trustees or bargaining parties of the funds to be merged will need to decide what benefits will be offered under the merged plan. The trustees should inform the participants and beneficiaries of these changes as soon as possible after the benefit structure is finalized, and well in advance of the implementation of the new benefit changes. The authors recommend that the funds provide the notice of the merger (including all benefit changes) to the affected parties an absolute minimum of 30 to 60 days in advance of the anticipated merger effective date.

Summary of Material Modifications

The trustees of each fund to be merged

are legally required to provide a summary of material modifications (SMM) to all of the fund participants and their beneficiaries explaining the merger and the new terms of the merged fund. Where practical, the advance notice to the participants and beneficiaries described previously should be designed to meet the SMM content requirements; otherwise a separate SMM will still need to be provided. The relevant Department of Labor (DOL) regulations require that an SMM be provided to participants and beneficiaries receiving benefits under a health plan within **60 days after an adoption or modification of benefits occurs** if any of the modifications or changes to the plan are considered a material reduction in benefits. In the merger context, this requirement applies to all plans to be merged. If none of the changes to the plans are considered material reductions, then the SMM is due within 210 days after the end of the plan year in which the changes are effective.

Notice to Affected Vendors

All vendors should be notified of the merger at the earliest possible date and asked to confirm that they will continue to provide services, if requested, to the surviving fund. To the extent that an agreement with a particular vendor or service provider will be terminated or assigned to another fund as a result of the merger, the agreement should be reviewed to determine the form and timing of any required notice to the provider. Fund counsel should be involved as early in this process as possible to allow adequate time to evaluate each agreement and notify the provider accordingly.

Practical Issues

Apart from the legal considerations, there are a number of practical and operational issues that will need to be addressed prior to the merger closing date and, where appropriate, covered by an express provision in the merger agreement. This phase of the merger implementation process usually requires a substantial commitment of time and resources on behalf of the plan professionals and administrative staff. In the authors' experience, funds should allow from three to six months to complete this part of the process. The following is a preliminary listing of the most relevant practical issues funds will face when implementing a merger.

Prepare Merger Agreement

The parties will need to prepare and sign a written merger agreement. Given the requirement that fiduciaries follow the terms of the plan's governing documents, the merger agreement can serve as an amendment to the plans involved in the transaction. The agreement should contain all of the material terms of the merger, such as the merger effective date, the merger closing date, the amount of assets to be transferred, any representations and warranties made between the funds, and a summary of the new benefit structure.

In addition, the agreement should incorporate other relevant items, including the procedure for appointing trustees to the new merged fund, an indemnification provision whereby the surviving fund in-

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demnifies the trustees of the other fund, and a description of how fiduciary liability insurance coverage will be handled for the surviving fund and the fund (or funds) that do not survive. The agreement should also address the administrative and transition issues discussed below. Once drafted, the agreement should be reviewed by each fund's trustees, counsel and consultants to ensure that all issues are accurately addressed and reflected in the agreement.

A merger of multiemployer health and welfare funds is also a merger of administrative, claims processing, information technology (IT), trustee and operational cultures.

A sample merger agreement can be found at www.seyfarth.com/dir_docs/publications/SampleMerger.pdf. This sample is provided solely for the purpose of illustrating the types of issues that might be addressed in a typical merger transaction. An agreement will need to be tailored by fund counsel for each separate merger transaction.

Review Compliance Issues and Completion of Due Diligence

Prior to the closing date, the trustees should verify completion of all recommended due diligence items being performed by the plan professionals and the status of any items that are outstanding. Again, the trustees should ensure that the due diligence process is properly documented.

Verify Post-Merger Benefit Design

As discussed earlier, it is virtually assured that at least one (if not all) of the funds involved in the merger will be changing the benefits provided to its participants. Therefore, the trustees and plan professionals of the affected funds will need to work together to design the new post-merger benefit structure, which may be dictated by the bargaining parties. Also, the treatment of the participants under the merged fund should be specifically addressed in the merger agreement and should be communicated to the participants and beneficiaries well in advance of the merger effective date.

Resolve Administration and Transition Issues

A merger of multiemployer health and welfare funds is also a merger of administrative, claims processing, information technology (IT), trustee and operational cultures. Thus, there are a number of issues that should be resolved before, during and after the merger closing date. Following is a list of some of the more significant administrative and operational issues to be considered:

- Who will handle the administration and claims processing for all of the affected participants after the merger closing date, and where will the administrative operation be located?
- Will the existing administrative operation of the nonsurviving fund(s) (or specific individuals who work for that operation) be engaged to provide transitional or ongoing administrative services? Will offices be combined or relocated?
- If a third-party administrator (TPA) is used for one or more of the funds to be merged, will that TPA be terminated? Does it make sense from a practical and/or financial standpoint to self-administer the merged fund on a going-forward basis?
- How will the transfer of documents and records be accomplished (in order to comply with HIPAA privacy and other rules, as well as how the documents will physically be transferred), and where will those records be kept?
- What arrangements will be made for any noncollectively bargained administrative staff who participate in any of the affected funds?
- What will happen to any leases or other arrangements for office space currently being utilized in connection with the affected funds' administration?
- How will the existing policies, procedures and practices relating to benefit claims and calculations be communicated to any successor administrative operation (if the existing administrative operation and/or staff is not retained)?
- Is there any proprietary or licensed administrative or claims processing software or hardware that must be assigned or transferred to the resulting fund? Does existing software access allow for the merger and added lives, and does it allow for use at a different location or "site"?
- How will the arrangements be handled for the payment of employer contributions, and will they be payable at the same location, at the same time and using the same lockbox and remittance report, or will those procedures change?
- Will there be any impact on the methods currently used for allocating employer contributions between related funds?

In the authors' experience, a health and welfare fund merger requires intensive effort and numerous meetings between the plan professionals and the administrative staff of all funds involved in the merger to work through these issues. The administrative and practical issues generally take months to resolve and will undoubtedly impact the merger closing date.

Fiduciary Liability Insurance

The trustees of each affected fund (other than the surviving fund) should consider obtaining at least six years of "tail coverage" under their existing policy of fiduciary liability insurance. Such coverage is fairly standard and most likely can be purchased at a reasonable premium. This type of coverage, if purchased, should be addressed in the merger agreement. The trustees of the funds that will be merged into the surviving fund should also be added to the surviving fund's existing fiduciary liability insurance policy as additional insureds.

Request Indemnification

If the trust agreements of the funds to be merged contain an indemnification provision protecting the trustees in connection with their actions as trustees, the trustees of the funds that are being merged into the surviving fund should request that the surviving fund indemnify and hold

them harmless on the same basis as is currently provided under the nonsurviving fund's trust agreement. If this occurs, the surviving fund would assume the post-merger obligation of the nonsurviving funds to provide trustee indemnification. If given, this indemnity could cover any liability arising in connection with or resulting from the merger. In addition, the trustees of each fund to be merged may want to review their current indemnity provision to ensure that it provides "state-of-the-art" protection for the trustees, and for the advancing of expenses to the maximum extent permitted by law.

Provide for Continuation of the Fidelity Bond

Apart from fiduciary liability insurance, the trustees of the nonsurviving funds may want to make arrangements to continue the ERISA-mandated fidelity bond coverage for the nonsurviving funds for an appropriate period of time.

Determine Board Composition

Prior to the merger closing date, the trustees of all affected funds should clarify and have reduced to writing the number of initial trustees that are to serve on the board of the resulting fund and the procedure for selecting or appointing trustees thereto. These decisions should be included in the merger agreement.

Conclusion

Despite the lack of any significant ERISA rules or regulations, the merger of multiemployer welfare funds can be a daunting, difficult and time-consuming task that demands careful attention from the trustees of the affected plans. Not only is it essential to exercise appropriate due diligence and prudence in implementing the transaction, but it is also important to document carefully what was done and that appropriate input and advice was obtained from the plan professionals. The negotiation and drafting of a comprehensive merger agreement is a key step in any merger transaction, and the above-referenced sample merger agreement should be a good starting place in determining what issues need to be addressed in any particular transaction. **B&C**

Endnotes

1. ERISA Section 4231 regulates mergers between multiemployer pension plans, and Section 4232 regulates mergers between multiemployer pension plans and single employer plans.

2. See, e.g., *Demisay v. Local 144 Nursing Home Pension Fund, 508 U.S. 581 (1993); Trapani v. Consolidated Edison Employees' Mutual Aid Society, Inc., 891 F.2d 48 (2nd Cir. 1989); Local 50, Bakery and Confectionery Workers Union, AFL-CIO, Health Benefits Fund v. Local 3, Bakery and Confectionery Workers Union, AFL-CIO, Welfare Fund,* 733 F.2d 229 (2nd Cir. 1984).

3. 127 S.Ct. 2310 (2007). It should be noted, however, that the application of the *Beck* decision in the multiemployer context is not completely settled, and there is some question about how a merger decision made by the trustees of a multiemployer plan (unlike the single employer plan in *Beck*) would be treated.

4. That is, regardless of what due diligence was done at the bargaining level, the trustees may want to consider independently validating the due diligence behind the decision to merge. This decision must be made, of course, in consultation with fund counsel.

5. A detailed discussion of this issue is beyond the scope of this article, but it is generally believed that trustees are compelled to implement the instructions of bargaining parties unless to do so would cause a violation of law or some other very serious harm to the plan. See, e.g., *United Mine Workers of America v. Robinson,* 455 U.S. 562 (1982); *Central Hardware Company v. Central States, Southeast and Southwest Areas Pension Fund,* 770 F.2d 106 (8th Cir. 1985); *Bachler v. Bayless,* 56 F.3d 70 (9th Cir. 1995).

6. In this regard, the plan will need to determine whether contributing employers should be required to sign a new participation agreement or other document that confirms their obligation to contribute to the surviving fund.

7. ERISA Section 406(b)(2) prohibits a fiduciary from acting "in any transaction involving the plan on behalf of a party . . . whose interests are adverse to the interests of the plan." In a merger context, the interests of each fund are technically adverse to all other funds to be merged, since they are on "opposite" sides of a merger transaction.

8. ERISA Sections 408(b)(11), 408(f) and 4231.

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Mitchel D. Whitehead, a partner in the Los Angeles office of Seyfarth Shaw, has over 25 years of experience advising clients with respect to ERISA and fiduciary issues. His practice is focused on the representation of large governmental retirement systems and multiemployer pension and health and welfare funds. Whitehead received his law degree from Loyola University School of Law and a bachelor's degree from the University of California at Riverside.

Carrie J. Grove, a senior associate in the Employee Benefits Group of Seyfarth Shaw in Los Angeles, has over ten years of experience as an ERISA attorney. Her practice focuses on multiemployer pension and benefit plans including the areas of fiduciary responsibility, benefit claims, prohibited transactions, agreements with third-party providers and withdrawal liability, and merger and spinoff issues. Grove received her law degree from the University of California Hastings College of the Law and a bachelor's degree from California State Polytechnic University, Pomona.

Nicholas J. Waddles is a senior associate in the Employee Benefits Practice Group in Seyfarth Shaw, LLP's Los Angeles office. He advises multiemployer pension and welfare benefit plan trustees, administrators, consultants and service providers on all aspects of employee benefits law including fiduciary responsibility, Internal Revenue Code (IRC) and ERISA qualification matters, mergers and acquisitions, and resolving compliance issues before DOL and IRS. Waddles received a J.D. degree from Washington University in St. Louis and a B.S. degree from Truman State University (Missouri).