Bloomberg BNA

Pension & Benefits Daily ™

Withdrawal Liability—A Concealed but Potentially Devastating Assessment

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During the past several years a hidden liability has been lurking in the shadows. This hidden threat is known as withdrawal liability and is a critical issue that any employer with a unionized workforce needs to be cognizant of and potentially confront to mitigate the serious consequences associated with a withdrawal liability assessment. Withdrawal liability is a hazard that has the ability to completely undermine the financial stability of a business.

The purpose of this article is to summarize the significance of withdrawal liability, highlight warning signs that may alert you of the possible existence of a withdrawal liability problem, and suggest some best practices to address withdrawal liability issues to safeguard your business going forward.

Withdrawal liability is a creation of Congress designed to address funding issues that arise related to union defined benefit multiemployer pension plans, and does not apply to defined contribution plans, such as 401(k) plans, medical benefit plans or other types of welfare arrangements. At its core, withdrawal liability is a statutorily prescribed exit fee that can be triggered when an employer completely stops contributing to the multiemployer pension plan or when an employer reduces its contributions beyond certain percentages over time.

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The amount of the withdrawal liability assessment can be significant, even when an employer has only been making pension contributions with respect to a handful of union employees. Indeed, withdrawal liability assessments can run into the hundreds of thousand dollars and often exceed one million dollars. Therefore, ignoring the potential liability is done at great risk and may result in a very costly mistake.

Hidden Trap for Unwary

What makes withdrawal liability a hidden trap for many employers is their unawareness regarding the many circumstances that can trigger such liability. For example, ordinary transactions, such as closing a facility, selling a business, or laying off employees, can trigger the assessment of withdrawal liability.

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In addition, withdrawal liability assessments can also be triggered upon the occurrence of a ''mass withdrawal.'' A mass withdrawal occurs when substantially all of the contributing employers to a multiemployer pension plan withdraw at the same time. Until recently, mass withdrawals were extremely rare. However, as a result of historically low interest rates and market declines experienced during the past few years, many union multiemployer plans are now in severe financial trouble and this has exponentially increased the number of such plans that have or will likely experience a mass withdrawal.

Another hidden and misunderstood pitfall related to withdrawal liability involves the extremely broad reach of such liability. It is extremely important to note that a withdrawal liability assessment is not limited to just the employer that hires the union employees and contributes to a multiemployer pension plan, but encompasses the employer's so called ''control group.'' Therefore, under the structure established by Congress, each trade or business in the control group with an employer contributing to a multiemployer plan is jointly and severally liable, along with that employer, for the employer's withdrawal liability.

For purposes of withdrawal liability it is irrelevant that the trades and businesses are unrelated; as long as there is common ownership, they are part of the control group. This rule applies to the following:

- stock ownership with a common parent, known as parent-subsidiary corporations;
- corporations owned by five or less stockholders, known as brother-sister corporations; and
- combined groups of corporations that are members of a parent-subsidiary or brother-sister controlled group.

It should also be noted that even entities that are under common ownership, though not corporations (such as partnerships and limited liability companies), can also be subject to control group liability and held jointly and severally liable for the decision by an employer to withdraw from a multiemployer pension plan.

Piercing Corporate Veil. It is also possible that individual stockholders or officers of a corporation may also be considered part of a control group, subjecting them to personal liability under the concept of ''piercing the corporate veil.'' Further, besides the piercing the corporate veil theory, business owners should also be careful that an individual enterprise or activity, such as a commercial rental property business, does not unintentionally create personal liability for the withdrawal liability. For example, in a decision rendered last year by the U.S. Court of Appeals for the Seventh Circuit, a husband and wife who were the principal owners of a trucking company were held personally liable for a withdrawal liability obligation of almost $3.1 million as assessed by a multiemployer defined benefit pension fund against their trucking company.

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In the case of *Central States Southeast and Southwest Areas Pension Fund v Messina Products, LLC*, 706 F.3d 874, 2013 BL 35790, 55 EBC 2196, (7th Cir., 2013)(28 PBD, 2/11/13; 40 BPR 376, 2/12/13), the Seventh Circuit held that Stephen and Florence Messina, the landlords of the property rented to Messina Trucking LLC, were jointly and severally liable, in their personal capacity, for the withdrawal liability as incurred by their closely related trucking operation. It is important to note that in this case the federal court did not determine that the husband and wife were personally liable for the withdrawal liability under a piercing the corporate veil theory, but on the basis that they owned and leased the property from which the trucking company (a closely held corporation) operated.

The property was directly leased by the husband and wife to the closely held trucking company in their individual capacity, which made the company an unincorporated enterprise. The husband and wife attempted to avoid the individual assessment of withdrawal liability on the grounds that the commercial rental activity was a passive investment activity and did not constitute the operation of a ''trade or business'' for purposes of the control group rules applicable to withdrawal liability assessments.

However, the federal court disagreed. It noted that the absence of a formal written lease, the lapse in rent payments for several years by the trucking company, and the failure to account properly for property maintenance by employees of the trucking company were each imputed to the owners.

The court held this level of activity as imputed on the owners exceeded the involvement typically associated with a passive investment. In the end, the federal court held that the commercial rental enterprise of the husband and wife constituted a trade or business, and therefore, they were jointly and severally liable for the withdrawal liability owed by Messina Trucking LLC to the Central States Southeast and Southwest Areas Pension Fund.

Strategies to Address Potential Liability

Obviously, the *Messina* case illustrates that the trustees of multiemployer pension funds are becoming much more aggressive and are willing to pursue any and all parties, including individual owners, in their efforts to collect outstanding withdrawal liability. Therefore, to shed some light into the shadowy world of withdrawal liability, there is a need to develop a comprehensive understanding of the company's possible exposure to such liability. If the possible existence of a withdrawal liability is uncovered, there will also be a need to develop a strategy to address such liability.

First, determine whether the company or any other company in the control group has union employees. If so, find out whether such company currently contributes to, or has at any time during the past six years contributed to, a multiemployer defined benefit plan on behalf of such union employees.

Second, know if the owners of the company have a business interest in a company that is contributing to, or has contributed to, a multiemployer plan or acquired the stock or assets of a company that contributed to a multiemployer plan.

Finally, the owners of a company need to make sure that none of their outside business activities could subject them to personal liability for any withdrawal liability that may potentially be owed by a closely held business.

Withdrawal Liability Exposure Checklist

The following summary checklist may be helpful in seeking to understand whether a company may face possible exposure to a withdrawal liability assessment:

1. Does the company currently contribute to a multiemployer defined benefit plan?

2. Has the company contributed to a multiemployer defined benefit plan at any time during the past six years?

3. Do any of the owners of the company also have an interest in a company that is contributing to, or has contributed to, a multiemployer defined benefit plan?

4. Do any of the owners of the company also have an interest in a company or have any business relationship to a company that is contributing to, or has contributed to, a multiemployer defined benefit plan?

5. Has the company acquired the stock or assets of a company that contributed to a multiemployer defined benefit plan?

6. Does the company have a close business relationship with a company that contributes to, or has contributed to, a multiemployer defined benefit plan?

If you answered ''yes'' to any of the questions above, you may have exposure to a withdrawal liability assessment, and it will then be extremely important to work with an expert to develop a strategy and action plan to minimize, or possibly eliminate, the company's risks of withdrawal liability. This is especially true in the current environment because the funding status of many union multiemployer defined benefit plans continues to deteriorate.

Request for Estimate

Consequently, the withdrawal liability amount that may be owed by the company or a member of the company's control group may be significantly increasing with each passing year. Thus, one of the first steps that any employer should take if it determines that a withdrawal liability problem may exist is to request a withdrawal liability estimate from the applicable multiemployer plan.

Under federal law, a multiemployer plan is required to provide such withdrawal liability estimates at least once a year upon written request from the employer (the plan is permitted to assess a reasonable charge to provide such estimate). However, it is important to note that any such estimate is just that—an estimate. The estimate will typically be based upon a withdrawal that occurs in the year before the request and not the current year.

Therefore, since the funding status of many plans is worsening, the actual withdrawal liability amount owed by an employer from year-to-year can change significantly. While an estimate will likely not provide a completely accurate picture of the withdrawal liability owed by an employer, it will at least provide an employer with some information about the extent of its withdrawal liability problem.

Conclusion

In the end, employers with unionized workforces need to be proactive and should not adopt a wait-and-see approach. Developing a short-term, mid-term and long-term strategy to address potential withdrawal liability may be critical in protecting the financial viability and long-term survival of the company. The key is to make sure that any strategy to avoid and/or mitigate withdrawal liability is also in line with the company's short, mid and long-term business objectives. With enough advanced planning, this can almost always be accomplished.