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Deal-Breaking M&A Issues Related to Employee Benefit Plans and Executive Compensation

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[Mark Poerio](#) specializes in executive compensation, employee benefits, and fiduciary matters, especially from a business, governance, tax, securities, and litigation perspective. He currently serves as President of the prestigious American College of Employee Benefits Counsel, and on the executive board of the American Benefits Council.

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The Wagner Law Group is a nationally recognized practice in the areas of ERISA and employee benefits, estate planning, employment, labor and human resources and investment management.

Employee benefit and executive compensation related issues have been known to unravel merger and acquisition transactions. These sometimes seriously disruptive issues can explode an otherwise viable deal when overlooked until the last minute. The list below is intended to facilitate the detection, negotiation, and resolution of possible employee benefit plan and executive compensation related problems. As a general matter, sellers may defuse risks and streamline negotiations through proactive pre-sale planning. On the other hand, buyers are able to maximize their deal-related protections (and their post-closing alternatives) by assuring early stage attention to the items listed below.

Note that the following list merely illustrates the range of benefit plan issues that may interfere with a change in corporate control (CIC) transaction. Disclosure schedules will often suggest other material issues, such as benefit plan defects and potential liabilities. Overall, sellers, targets, and buyers should always be represented in these matters by experienced M&A ERISA counsel.

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Employment-related Agreements

- Key employees who have the right to resign with full severance upon a CIC.
- Key employees who are not subject to post-employment restrictive covenants.
- Employment-related covenants and agreements that are not assignable to the buyer (or surviving entity).

Equity Award Plans

- Out-of-the-money stock options that the employer cannot unilaterally cancel.
- Stock options with a below-market exercise price on the grant date (or grants for which there is not a reasonable basis on which to show the exercise price was at or above fair market value).
- Uncertainty over how equity awards will be handled upon a CIC.
- Violation of federal and state registration or disclosure requirements.

Non-qualified Plans

- Questionable compliance with §409A.
- Whether plans with material benefits will terminate or continue following the CIC.
- Whether rabbi trusts will continue, or be formed to provide CIC protections for executives.

Parachute Payments

- 280G golden parachute penalties (or the failure to assess the golden parachute implications of both the CIC transaction and any associated terminations of employment).
- Lost accelerated vesting, severance, or other benefits due to 280G limits (or the need to replace them).
- The need for a shareholder cleansing vote, with associated disclosures and risks.

TAX-QUALIFIED PLANS

401(k) and other Defined Contribution Plans

- Litigation risks from excessive fees, poorly monitored investments, or employer stock investments.
- Compliance problems in need of correction (how to correct, and by whom), and their impact on a possible plan termination or

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merger.

- Positioning for plan termination (to avoid post-CIC "orphan plan" risks).

NOTE: target companies and sellers are often best served to terminate their retirement plans and to seek IRS determination letters asap after signing a merger or sale agreement.

Defined Benefit Plans

- Underfunding on a current or plan termination basis. Whether the plan will terminate or continue post-CIC.

ESOPs

- Questionable appraisals of employer stock, including the CIC value.
- Whether the ESOP will terminate or continue post-CIC.
- Whether an outstanding securities acquisition loan will be discharged or continued.
- Whether unallocated shares will be released solely to seller's employees.
- How, and by whom, ESOP shares will be voted in connection with the CIC.

Multiemployer (Union)

- Significant withdrawal liability for underfunded plans.
- Bonding and other ERISA 4204 issues related to an asset purchase.
- Whether plan contributions will continue or terminate post-CIC.

WELFARE PLANS

Group Health Plans

- Self-insured plans without adequate stop-loss coverage (or excessive exposure to uninsured claims).
- Whether buyer or seller will be responsible for material COBRA obligations.

Life Insurance (COLI)

- Whether significant corporate-owned life insurance will be continued, terminated, or transferred to the executive (and the

terms for transfer).

Retiree Medical

- Whether the plan is terminable at will, or provides lifetime benefits.
- Whether the plan will continue or terminate post-CIC.

Severance Plans

- Whether a plan is terminable at will, locked-in for some time post-CIC, or triggers significant severance liabilities.

Please contact Partner Mark Poerio via [email](#) or by phone (202-969-2248), if you have any questions.

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