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STRATEGIC PERSPECTIVES—A troubling expansion of successor liability

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Under the Employee Retirement Income Security Act (ERISA), as amended by the Multiemployer Pension Plan Amendments Act (MPPAA), an employer that has assumed an obligation to contribute to and subsequently withdraws from a collectively bargained and jointly administered defined benefit pension plan (a "multiemployer plan") is liable for its allocable share of any underfunding. This "withdrawal liability" has become a significant issue since 2008, due to the economic and investment impact of the recession, historically low interest rates, declining plan participation, and an increase in the number of retirees, among other things.

Two recent opinions from the U.S. Courts of Appeals forecast a troubling expansion of the imposition of withdrawal liability of non-signatory entities under the successor liability doctrine. While the imposition of such liability is not new, recent case law extends the doctrine beyond the reach of the Seventh Circuit federal appeals court (located in Chicago, and covering Illinois, Indiana and Wisconsin) to which it had previously been confined, and appears to ease the requirements for a claim against a putative successor. These cases also illustrate the effect of successor liability on the "building and construction industry exception" to withdrawal liability. The exception is a set of special rules that apply to certain multiemployer plans and employers in the building and construction industry.

Withdrawal liability generally

Withdrawal liability is triggered when a contributing employer withdraws from a multiemployer plan. This generally occurs when: (i) the employer permanently ceases to have an

obligation to contribute to the multiemployer plan; or (ii) the employer permanently ceases all covered operations under the plan.[1] As discussed below, this rule is modified for certain multiemployer plans and employers in the building and construction industry.

Under a "sale of assets" exception, a withdrawal does not occur solely as a result of a sale of assets, provided that certain requirements are met at the time of the transaction. One of these requirements is that the buyer assumes an obligation to contribute to the multiemployer plan.[2]

An employer incurring a complete withdrawal from a multiemployer pension plan is liable for its allocable share of the plan's unfunded vested benefits, determined using one of several statutory formulas. The gross amount so allocated is then payable by the employer in annual or more frequent payments; absent a default, a plan cannot require payment in a lump sum or other accelerated basis. Each annual payment is determined with reference to the employer's contributions in the 10 years preceding the withdrawal.[3] An employer's withdrawal liability is payable for a maximum of 20 years.[4] This "20-year cap" does not apply in the event of a "mass withdrawal."[5]

Disputes over an employer's withdrawal liability are subject to mandatory arbitration.[6] Failure to timely initiate arbitration results in the amount of withdrawal liability demanded becoming due, payable, and thereafter not subject to challenge.[7]

Building and Construction Industry Exception

Special rules apply when both of the following conditions are met:

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[1] ERISA § 4203. The statute also has a concept of "partial withdrawal" (ERISA § 4205), a discussion of which is beyond the scope of this article.
[2] ERISA § 4204(a)(1).
[3] ERISA § 4219(c)(1)(C)(i).
[4] ERISA § 4219(c)(1)(B).
[5] ERISA § 4219(c)(1)(D). A mass withdrawal may occur when substantially all employers withdraw by arrangement or agreement or when the plan is terminated due to the withdrawal of all employers.
[6] ERISA § 4221(a)(1).
[7] *See, e.g., Nat'l Fund Pension Plan of the UNITE HERE Workers Pension Fund v. Westchester Lace & Textiles, Inc*., 2006 U.S. Dist. LEXIS 49845 at*14 (S.D.N.Y. 2006).

- The plan primarily covers employees in the building and construction industry; and
- Substantially all of the employees for whom the employer is obligated to contribute to the plan perform work in the building and construction industry.[8]

Under the "Building and Construction Industry Exception," a Building and Construction Industry Employer that ceases to have an obligation to contribute to a Building and Construction Industry Plan will not incur a complete withdrawal from such plan unless the employer:

- Continues to perform work in the jurisdiction of the collective bargaining agreement of the type for which contributions were previously required; or
- Resumes such work within five years of the date on which the obligation to contribute under the plan ceases, and does not renew the obligation at the time of the resumption.[9]

Contrary to the general rule (*i.e.,* the cessation of the contribution obligation alone triggers a withdrawal), withdrawal liability is imposed on an employer under the Building and Construction Industry Exception only when the employer's "obligation to the fund ceased," but the employer "continued doing covered work."[10]

Successor liability for ERISA obligations

The common law rule is that an asset purchaser does not assume an asset seller's liabilities, including ERISA obligations.[11] Beginning with the U.S. Supreme Court's *Golden State Bottling Co. v. NLRB,*[12] however, federal courts have formulated a successor liability exception for certain labor- and employment-related liabilities, founded on a judicial

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[8] ERISA § 4203(b)(1). A covered plan is generally referred to as a "Building and Construction Industry Plan," while a covered employer is generally referred to as a "Building and Construction Industry Employer".
[9] ERISA § 4203(b)(2)(B).
[10] *Elliott v. Carpenters Pension Trust Fund for N. Cal.*, 859 F.2d 808, 811 (9th Cir. 1988).
[11] *Travis v. Harris Corp*., 565 F.2d 443, 446 (7th Cir. 1977).
[12] 414 U.S. 168 (1973).

determination that certain policies based on federal labor relations law prevail over the competing interest of fluidity of corporate assets reflected in the common law rule.[13]

Federal district courts first applied the successor liability doctrine to impose liability for delinquent fund contributions upon a successor[14] and subsequently extended the doctrine to withdrawal liability.[15] Until recently, the Seventh Circuit was the only federal circuit to impose withdrawal liability on a successor.[16]

Test for successorship

Courts recognizing the successor liability doctrine have almost universally adopted a two-pronged test. To hold a successor liable, a court must find both: (1) "sufficient indicia of continuity between the two companies" (generally called *substantial continuity*); and (2) "the successor had *notice* of its predecessor's liability."[17]

- *Substantial continuity:* Courts have looked to a variety of factors, including, among others, the continuity of the workforce, management, equipment, and location; completion of work orders begun by the predecessor; and constancy of customers.[18]

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[13] In *Upholsterers Int'l Union Pension Fund v. Artistic Furniture*, 920 F.2d 1323, 1329 (7th Cir. 1990), the Seventh Circuit noted that successor liability is appropriate "in those cases where the vindication of an important federal statutory policy has necessitated the creation of an exception to the common law rule, where the successor has had prior notice of the liability in question, and where there has existed sufficient evidence of continuity of operations between the predecessor and successor."

[14] *See Artistic Furniture, supra*; *Einhorn v. M.L. Ruberton Construction*, 632 F.3d 89 (3d Cir. 2011); *Mass. Carpenters Cent. Collection Agency v. Belmont Concrete Corp*., 139 F.3d 304, 308 (1st Cir. 1998); *Stotter Div. of Graduate Plastics Co., Inc. v. Dist. 65, United Auto Workers*, 991 F.2d 997, 1002 (2d Cir. 1993); *Haw. Carpenters Trust Funds v. Waiola Carpenter Shop, Inc*., 823 F.2d 289 (9th Cir. 1987).

[15] *See, e.g., Automotive Industries Pension Trust Fund v. South City Ford*, 2012 WL 1232109 (N.D. Cal. 2012); *RP Baking LLC v. Bakery Drivers and Salesmen Local 194 Industry Pension Fund,* 52 EBC 1628 (D. N.J. 2011); *Trustees of the Utah Carpenters & Cement Masons Pension Trust v. Daw, Inc.,* 2009 WL 77856, at *3 (D. Utah 2009); *Central Pennsylvania Teamsters Pension Fund v. Bear Distrib. Co.*, 2009 U.S. Dist. LEXIS 26481 (E.D. Pa. 2009); *Central States Pension Fund v. Hayes*, 789 F. Supp. 1430 (N.D. Ill. 1992).

[16] *Chicago Truck Drivers, Helpers and Warehouse Workers Union Pension Fund v. Tasemkin, Inc*., 59 F.3d 48 (7th Cir. 1995).

[17] *Artistic Furniture*, *supra*, 920 F.3d at 1329.

[18] *See Einhorn*, *supra*, 632 F.3d at 99; *Fall River Dyeing & Finishing Corp. v. NLRB*, 482 U.S. 27, 43 (1987); *Artistic Furniture*, *supra*, 920 F.2d at 1329; *3750 Orange Place Ltd. P'ship v. Nat'l Labor Relations Bd*., 333 F.3d 646, 655 (6th Cir. 2003) (to determine whether there is a continuity of business identity, the Court must find the

- *Notice*: Courts have held that notice can be proven not only by actual knowledge, but also by evidence that allows the factfinder to infer constructive knowledge from the circumstances.[19] In the withdrawal liability context, courts have expressly rejected the argument that notice cannot exist because the obligation for withdrawal liability does not arise until assessed by the fund, which assessment cannot by definition occur until after the event causing the withdrawal, *i.e.,* the sale of assets.[20]

Tsareff v. ManWeb

In *Tsareff v. ManWeb Services, Inc.*,[21] the Seventh Circuit expanded upon its prior application of the successor liability doctrine in the withdrawal liability context[22] by holding that a buyer's notice of a seller's contingent withdrawal liability satisfied the notice requirement.

Tsareff involved the sale of assets by a unionized electrical contractor (Tiernan & Hoover) to a non-union engineering company (ManWeb). As a result of the transaction, Tiernan & Hoover (the asset seller) no longer had any unionized employees; the pension fund asserted that this resulted in a complete withdrawal and assessed withdrawal liability. Tiernan & Hoover failed to contest the fund's assessment by initiating arbitration; thereafter, the fund filed suit against both Tiernan & Hoover (as a withdrawing employer) and ManWeb (as a successor).

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following: (1) whether there has been a substantial continuity of the same business operation; (2) the new employer uses the same plant; (3) a majority of the new workforce is made up of the predecessor's employees; (4) the same jobs exist under the same working conditions; (5) the same supervisors are employed; (6) the same machinery, equipment and methods of production are used; and (7) the same products are manufactured or the same services are offered); *Bd. of Trustees of Unite Here Local 25 v. MR Watergate LLC*, 677 F. Supp.2d 229, 231 (D.D.C. 2010) (applying nine-part test to determine whether purchaser of assets is a successor, subject to successor liability analysis to determine withdrawal liability).

[19] *Artistic Furniture*, *supra*, 920 F.2d at 1329.

[20] *See Tsareff, infra; see also Automotive Industries Pension Fund, supra*, 2012 WL 1232109 at p.3 (denying motion to dismiss where fund's assessment for withdrawal liability occurred five years after sale and plaintiffs alleged actual and constructive knowledge of seller's unfunded pension liabilities).

[21] 794 F.3d 841 (7th Cir. July 27, 2015).

[22] *See Tasemkin, supra*.

The district court granted ManWeb's motion for summary judgment and dismissed all claims against them.[23] First, the court found the requisite notice was lacking because "Tiernan & Hoover did not withdraw or incur withdrawal liability until after the asset purchase," making it impossible for ManWeb "to have had notice of an existing liability in advance of the closing on the asset purchase."[24]

Then, considering the Building and Construction Industry Exception, the district court said:

> All of the parties agree that Tiernan & Hoover is an employer in the construction industry, [] and thus subject to [§ 4203(b)]. Further, all agree that Tiernan & Hoover ceased to have an obligation to contribute to the Plan when the asset sale occurred and once it ceased operations. However, the parties do not agree on the issue of whether a complete withdrawal occurred pursuant to [§ 4203(b)(2)(B)]. The Plan argues that ManWeb's continued performance of work of the type for which contributions were previously required of Tiernan & Hoover serves to impose withdrawal liability on Tiernan & Hoover. We disagree.[25]

Finding that the "plain language of the statute does not support the Plan's argument that ManWeb's continuation of certain work must or should be imputed to Tiernan & Hoover in determining whether Tiernan & Hoover effectuated a complete withdrawal,"[26] the court concluded "that Tiernan & Hoover did not effectuate a complete withdrawal pursuant to [§4203(b)] and thus, apart from its waiver of the defenses available to it, it would not be subject to withdrawal liability. Accordingly, prior to the transaction, ManWeb had no notice of Tiernan & Hoover's eventual failure to challenge the assessment or the resulting liability. There being no

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[23] *Haltom v. Tiernan & Hoover, et al.*, 976 F. Supp. 2d 1007 (S.D. Ind. 2013).
[24] 976 F. Supp. 2d at 1017.
[25] 976 F. Supp. 2d at 1018. As noted above, a finding of substantial continuity requires that a Building and Construction Industry Employer continue (or resume within five years) work that is within the scope of the collective bargaining agreement on a non-contributory basis in order to incur a complete withdrawal.
[26] *Id.*

genuine issue of material fact that ManWeb lacked notice of Tiernan & Hoover's withdrawal liability, it is not liable under the doctrine of successor liability."[27]

The Seventh Circuit reversed the lower court decision,[28] finding that notice of *contingent* withdrawal liability is sufficient for purposes of the successor liability doctrine. To find otherwise, the Seventh Circuit stated, would create a "liability loophole" whereby multiemployer plans "would be foreclosed in some situations (but not others) from seeking withdrawal liability from asset purchasers who would otherwise qualify as successors, and the plans would be left 'holding the bag.'"[29] The court then held that "ManWeb's notice of Tiernan & Hoover's contingent withdrawal liability can be both reasonably inferred and directly proven by evidence in the record," based on both testimony evidencing a general knowledge of the seller's withdrawal liability and provisions in the asset purchase agreement providing that ManWeb was not obligated to assume and did not agree to assume any liability or obligation "arising out of or related to union related activities, including without limitation pension obligations."[30]

The Seventh Circuit did not address the district court's holding that ManWeb's continuation of certain work should not be imputed to Tiernan & Hoover in determining whether Tiernan & Hoover effectuated a complete withdrawal under the Building and Construction Industry Exception, concluding that "[a]rbitration reigns supreme under the MPPAA" and that Tiernan & Hoover's failure to arbitrate "should have ended the inquiry."[31]

Lastly, with respect to the district court's finding that the imposition of successor liability on ManWeb would be inequitable, the Seventh Circuit found the district court committed reversible error "by ignoring the fact that ManWeb could and did protect itself against liability"

[27] *Id.* at 1019.
[28] 794 F.3d 841 (7th Cir. July 27, 2015).
[29] *Id.* at 846.
[30] *Id.* at 848.
[31] *Id.* at 850.

and, further, "could have required Tiernan & Hoover to obtain an estimate of their withdrawal liability…in order to negotiate a lower purchase price."[32]

Resilient v. Michael's Floor Covering

Shortly after the Seventh Circuit's ruling in *Tsareff*, the Ninth Circuit reached a similar result. In *Resilient Floor Covering Pension Trust Fund v. Michael's Floor Covering, Inc.*,[33] the Ninth Circuit imposed liability on an alleged successor to a Building and Construction Industry Employer. The Ninth Circuit has jurisdiction over Alaska, Arizona, California, Hawaii, Idaho, Montana, Nevada, Oregon, and Washington.

In *Resilient*, the owner (Michael) of the alleged successor (Michael's Floor Covering) was a former salesman of the predecessor (Studer's Floor Covering). Michael ultimately started his own floor covering business. There were several similarities between Michael's and Studer's: Michael's leased the same premises, obtained the same phone numbers, used similar signage, bought 30 percent of Studer's tools, equipment, and inventory at a public auction, and hired several of Studer's employees. Studer's did not sell, give, or otherwise assign its customer lists or any portion of its customer information to Michael's; indeed, the parties appeared to have no contractual relationship. Michael's, however, ended up retaining many of Studer's customers, in large part through the prior personal and business relationships developed by Michael while employed by Studer as a salesman.

The Ninth Circuit first stated that there were two discrete questions:

- Whether a successor employer, both generally and within the construction industry, can be subject to withdrawal liability?

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[32] *Id.* at 849.
[33] 801 F.3d 1079, 2015 U.S. App. LEXIS 16160 (9th Cir. Sept. 11, 2015).

- If so, what factors are most relevant to determining whether a construction industry employer is a successor for purposes of imposing withdrawal liability?[34]

With respect to the first question, the Ninth Circuit found "no reason why the successorship doctrine should not apply to MPPAA withdrawal liability" generally.[35] With respect to construction industry employers, the court found that "the narrow construction industry exception to MPPAA withdrawal liability is fully consistent with the generally applicable successorship doctrine."[36] Accordingly, the court concluded that "a bona fide successor can be liable for its predecessor's MPPAA withdrawal liability, both in general and with regard to the special building and construction trade provisions in particular, so long as the successor had notice of the liability."[37]

Much of *Resilient* is devoted to discussing the proper test for successorship in the MPPAA withdrawal liability context. The Ninth Circuit concluded that the district court had erred in this regard by failing "to weigh market share capture as a prime consideration, and therefore did not make any finding as to whether Michael's had retained a significant portion of Studer's business or body of customers."[38] The court remanded the case to the district court for the proper consideration of these factors.

Implications

Read together, *Tsareff* and *Resilient* present a troubling expansion of the successor liability doctrine in the withdrawal liability context. Several aspects merit mention:

- *Tsareff* establishes that a buyer's mere "general awareness" that a seller contributes to a multiemployer plan, coupled with other facts indicative of such awareness (such as

[34] 2015 U.S. App. LEXIS 16160 at *2-3.
[35] *Id.* at *27.
[36] *Id.* at *30.
[37] *Id.* at *32.
[38] *Id.* at *37.

standard exculpatory or indemnification provisions in an asset purchase agreement) can be sufficient notice.

- *Resilient* represents a significant expansion of the application of successorship law to withdrawal liability beyond the Seventh Circuit.
- The Ninth Circuit in *Resilient* seemingly gave no consideration to the lack of a contract between the parties or the fact that the customer list or other customer information was not sold or otherwise transferred (especially troubling given the significance the court ascribed to Michael's retention of Studer's customers). This represents a significant expansion of the context in which the successor doctrine had previously been applied.
- Both decisions resulted in liability imposed on a successor where none arguably would have been imposed on the predecessor under the Building and Construction Industry Exception. This seems particularly harsh (and troubling) where ERISA's mandatory arbitration regime could result (as it did in these cases) in the successor being foreclosed from contesting the existence of the liability based upon the predecessor's failure to do so.

The expansion of the successor liability doctrine in *Tsareff* and *Resilient* should concern employers who have purchased or are contemplating purchasing the assets of a unionized business. Given the potential exposure, those contemplating purchasing the assets or otherwise continuing the operations of a business that historically has contributed to a multiemployer plan should engage counsel experienced in withdrawal liability to review potential exposure and consider measures to protect against withdrawal liability successor claims. Such measures could include securitization of potential exposure as a successor by the use of indemnification or

escrow. The parties also may consider structuring a transaction to comply with the "sale of assets exception" in ERISA Section 4204, thus avoiding a withdrawal by the seller as a result of the asset sale. Finally, a buyer may insert a provision in the contract requiring the seller to take all actions needed to preserve their right to contest the existence of withdrawal liability. Each situation, however, is distinct, further highlighting the need for knowledgeable counsel in this regard.

As evidenced by *Tsareff* and *Resilient*, the law is evolving. Future cases may offer additional guidance on several open and unresolved issues, including the application of the Building and Construction Industry Exception to the imposition of withdrawal liability on alleged successors.

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