MERGERS AND ACQUISITIONS

KEY CONSIDERATIONS ON A COMPANY 401(K) PLAN

WHERE TO START

It is helpful to determine your course of action before the company transaction is closed, as some alternatives may be eliminated once the closing has taken place. Whenever a plan sponsor is involved in a merger or acquisition, the sponsor should involve its legal and/or tax counsel and third-party administrator (TPA) at the earliest possible stage of the process to ensure that all issues and considerations are handled at the right time and in the proper manner. During the negotiation process, the seller and buyer will need to gather data and determine who will be responsible for the seller's retirement plan.

There are generally three alternative scenarios for acquiring companies:

- Merge an existing plan into the buyer's plan
- Terminate the seller's plan and have acquired employees take distribution
- Maintain two separate plans: the seller's and the buyer's plans

TYPE OF SALE

ASSET SALE

An asset sale is the acquisition of the business assets of another company (for example, equipment or a building). Typically the seller is responsible for terminating the plan and distributing plan assets. The employees who are hired by the purchaser of the assets are terminated with regard to the seller and the seller's plan, and are therefore entitled to distributions from the seller's plan. In many cases, the purchaser will assume the plan,in which case there would be no distributable event since the acquiring employer would be seen as maintaining the seller's plan.

STOCK SALE

A stock sale is the acquisition of the stock of another company. After the sale, the business is owned by the buyers and the stock is reissued in the name of the buyer. The purchaser continues the business and is responsible for the plan. If this is a stock acquisition or merger, the acquiring company is deemed automatically responsible for the plan assets and liabilities unless arrangements are made for the seller to terminate its plan prior to the acquisition or merger.

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If the acquiring employer does not want to keep the selling employer's 401(k) plan, the purchase agreement should be written to include a requirement that the seller terminate the plan before the business transaction occurs. At this time, the seller is responsible for terminating the plan and distributing plan assets.

If the acquiring company already has a 401(k) plan at the time of transaction, the successor plan rules prevent the acquirer from terminating the plan of the purchased company once the sale is complete. The successor plan rule was created to stop employers from terminating a plan and then starting a new one.

Once the stock sale is complete, the new owner can merge the two plans together within the IRS allowable transition period. The existing plan will be merged with the acquiring company's plan and there is no distributable event.

The Internal Revenue Code has a rule that permits an acquiring employer to operate both plans — its own and the seller's — separately during a transition period. The period ends on the last day of the year following the year of the acquisition.

BEFORE MAKING THE DECISION

Before making the decision, make sure you know everything that is involved with each option. Given the variety of circumstances that may affect your decision on how to best manage 401(k) plans during a merger or acquisition, we encourage you to contact us with any questions. Do not make the mistake of terminating the plan by simple processing distributions, as this may immediately disqualify your plan as all outgoing monies must be an approved IRS distributable event. In addition, you must make sure the plan document and all final compliance testing and tax filings are up to date.

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