Legacy Liabilities: Dealing with Environmental, Pension, Union and Similar Types of Claims

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April 5, 2013

Introduction

- **Types of Liabilities**
  - **Environmental**:
    - Obligations to stop or contain ongoing pollution
    - Obligations to remediate contaminated sites
    - Obligations to reimburse other parties for remediation costs
    - Obligations to pay fines and penalties.
  - **Pension**:
    - Multi-employer plans:
      - Withdrawal liability
      - Partial withdrawal liability
    - Single-employer plans
      - Minimum funding contribution liability
      - Unpaid insurance premium liability
      - Underfunded liability
      - Termination Premiums

Introduction (continued)

- **Statutory Schemes Under Which Liabilities Arise**
  - **Environmental**:
    - Comprehensive Environmental Response Compensation and Liability Act of 1980 (“CERCLA”)
    - Resource Conservation and Recovery Act (“RCRA”)
    - Clean Air Act
    - Clean Water Act
    - Other federal and state laws
  - **Pension**:
    - Employee Retirement Income Security Act of 1974 (“ERISA”)

Introduction (continued)

- **Key Players**
  - **Environmental**:
    - Environmental Protection Agency (“EPA”) and other federal agencies
    - Department of Justice
    - Various state, municipal, local, and tribal authorities
    - Other indirect environmental claimant constituencies
  - **Pension**:
    - Pension Benefit Guaranty Corporation (“PBGC”)
    - Unions
    - Union pension plans
    - Multi-employer pension plans

Environmental Liabilities and Chapter 11

Environmental Considerations in Bankruptcy Proceedings – Introduction

- Environmental liabilities require special consideration in the bankruptcy context because the goals of environmental laws are at odds with the Bankruptcy Code's fresh start provisions.
  - Environmental laws are designed to prevent an entity from escaping responsibility for cleanup of contaminated sites.
  - Bankruptcy laws are designed to provide a Debtor with a fresh start by discharging prepetition liabilities.
- Environmental liabilities must be understood in any business transaction undertaken in the bankruptcy context.

Environmental Considerations in Bankruptcy Proceedings – Relevant Environmental Regulatory Programs

- Costs of Cleanup of Past Releases of Hazardous Substances.
  - Passage of CERCLA in 1980.
    - Present owner or operator; owner or operator at the time of release of hazardous substances; arranger; and transporter are jointly and severally liable for cleanup costs.
    - Retroactive liability and a retroactive focus to the law.
    - Strict liability.
    - Other federal, state and foreign statutes have adopted the same approach.
    - Natural resources damages.
    - Successor liability.
  - Federal and state governments may perform cleanup and sue for recovery of costs, or use injunctions to require cleanup by responsible parties.

Environmental Considerations in Bankruptcy Proceedings – Relevant Environmental Regulatory Programs (continued)

- Costs of Installing and Maintaining Operating Systems to Meet Environmental Regulatory Standards.
  - Clean Air Act.
  - Clean Water Act.
  - RCRA (hazardous waste, solid waste, underground storage tanks).
  - Other state and federal laws relating to toxic materials, asbestos, above ground storage tanks, wastewater discharges, etc.
  - Penalties for non-compliance.
- Personal Injury/Property Damage Actions as a Result of Releases of Contaminants.
  - Mass tort actions (asbestos, particulates, manganese, mercury, etc.).
  - Public nuisance actions.

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

- When is an environmental liability a Claim under the Bankruptcy Code?
  - Resolution of the conflict between bankruptcy and environmental laws often turns on the question of whether a particular cleanup obligation is a "claim" as defined by the Bankruptcy Code.
  - If the obligation is a claim, it is capable of being discharged; if it is not, the bankruptcy has no effect on it, and the debtor cannot escape responsibility for the cleanup.
  - Section 101(5) provides that a claim is "(A) [a] right to payment. . . , matured, unmatured, disputed, undisputed legal, equitable. . .; or (B) [a] right to an equitable remedy for breach of performance if such breach gives rise to a right to payment . . ."

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

(continued)

- Whether Non-Monetary Environmental Obligations Are Claims
  - **Supreme Court**
    - In *Ohio* v. *Kovacs*, 469 U.S. 274 (1985), the Supreme Court held that an injunction to cleanup a hazardous waste site gave rise to a “right to payment” against the former individual site owner, and thus was a dischargeable claim, where a receiver had been appointed pre-petition to take control of the individual’s assets, thereby dispossessing the owner of any ability to comply with the injunction, and where the State of Ohio was found to have converted its claim to one for money.
    - Application to traditional chapter 11 cases limited because the *Kovacs* ruling turned on the pre-petition appointment of a receiver.
  - **Lower Courts**
    - Many lower courts have limited *Kovacs* to its unusual facts and found injunctive remedies under various circumstances <u>not</u> to be dischargeable claims. *See, e.g., United States v. Apex Oil Co.*, 579 F.3d 734 (7th Cir. 2009); *In re Torwico Electronics, Inc.*, 8 F.3d 146 (3d Cir. 1993); *In re Chateaugay Corp.*, 944 F.2d 997 (2d Cir. 1991); *In re Mark IV Indus., Inc.*, 438 B.R. 460 (Bankr. S.D.N.Y. 2010), *aff’d*, 459 B.R. 173 (S.D.N.Y. 2011); *but cf. United States v. Whizco,* 841 F.2d 147 (6th Cir. 1988).

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

(continued)

- Aside from whether an environmental liability is a “claim,” other issues will arise on the question of dischargeability.

- Among other things, the claim must have arisen prior to confirmation in a Chapter 11 proceeding, *see* 11 U.S.C. § 1141(d), or pre-petition in a Chapter 7 proceeding, *see id*. § 727(b). The circuits have established different standards for determining when an environmental claim arises. *Compare In re Crystal Oil Co.*, 158 F.3d 291 (5th Cir. 1998), with *In re Chateaugay Corp.*, 944 F.2d 997 (2d Cir. 1991).

- Even if environmental liability would otherwise be a dischargeable claim, continued ownership or operation of property after reorganization may give rise to a new CERCLA claim, notwithstanding the prior discharge. *See In re CMC Heartland Partners*, 966 F.2d 1143 (7th Cir. 1992).

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

(continued)

- When are Post-Petition Expenditures for Debtor's Environmental Liabilities Administrative Expenses?
  - Pursuant to Section 503(b)(1)(A) "actual, necessary costs and expenses" are administrative expenses of the estate.
  - Several courts have held that costs incurred by the United States pursuant to CERCLA with respect to property of the bankruptcy estate during the Chapter 11 process are entitled to administrative priority. *See, e.g., In re H.L.S. Energy Co.*, 151 F.3d 434 (5th Cir. 1998); *Chateaugay Corp*., 944 F.2d 997 (2d Cir. 1991); *In re Wall Tube & Metal Prods. Co*., 831 F.2d 118, 123-24 (6th Cir. 1987); *In re Smith-Douglass, Inc*., 856 F.2d 12, 17 (4th Cir. 1988); *In re American Coastal Energy Inc.*, 399 B.R. 805 (Bankr. S.D. Tex. 2009).
  - Response costs paid during administration of the estate with respect to prepetition releases are necessary to preserve the estate in that the expenditures enable the estate to maintain itself in compliance with applicable environmental laws.

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

(continued)

- Exceptions From the Automatic Stay.
  - Actions or proceedings by governmental units to enforce police or regulatory power are exceptions to the automatic stay. 11 U.S.C. § 362(b)(4)
  - Matters within this automatic stay exception include:
    - Actions or proceedings for injunctive relief. *See Penn Terra Ltd. v. Dep't of Envtl. Res.,* 733 F.2d 267 (3d Cir. 1986).
    - Actions or proceedings seeking to reduce CERCLA liability to a monetary judgment (although the judgment itself may only be enforced in the bankruptcy case). *See City of N.Y. v. Exxon Corp.*, 932 F.2d 1020 (2d Cir. 1991).
    - Actions or proceedings to fix the amount of fines or penalties (although again the resulting money judgment may only be enforced in the bankruptcy case). *See In re Commerce Oil Co.*, 847 F.2d 291 (6th Cir. 1988)

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

(continued)

- Abandonment of Property.
  - The Bankruptcy Code permits the trustee to abandon property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate. 11 U.S.C. § 554.
  - However, in *Midlantic Nat'l Bank* v. *NJ Department of Environmental Protection*, 474 U.S. 494 (1985), the Court held that "a [bankruptcy] trustee may not abandon property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards." *Id.* at 507.
    - The Court also stated that "The Bankruptcy Court does not have the power to authorize an abandonment without formulating conditions that will adequately protect the public's health and safety." *Id.*
    - Although state environmental law was at issue in *Midlantic*, its holding applies equally to federal environmental law.
  - Subsequent cases have varied in their interpretation of the breadth of the restriction that *Midlantic's* holding places on abandonment.

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles

(continued)

- Obligation to Manage and Operate Property In Accord With Applicable Law
  - 28 U.S.C § 959(b) provides that trustee (including debtor in possession) "shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which the property is located."
  - Courts have described the trustee's obligation as including compliance with both federal and state environmental law. *See, e.g., In re American Coastal Energy Inc.*, 399 B.R. 805 (Bankr. S.D. Tex. 2009); *U.S. v. Wheeling-Pittsburgh Steel Corp.*, 818 F.2d 1077 (3d Cir. 1987).

Environmental Considerations in Bankruptcy Proceedings – Intersection of Bankruptcy and Environmental Principles
(continued)

- Treatment of Claims of Joint Tortfeasors.
  - Section 502(e)(1)(B) provides that contingent contribution or reimbursement claims brought by parties that are co-liable with a debtor with respect to claims brought by a creditor shall be disallowed.
  - This provision applies to contingent claims of co-PRPs that are jointly liable to the government on an environmental claim.

Employee Benefits Liability and Chapter 11

Pension and Benefit Issues

- What is a Pension Plan?
- What is the nature of pension liability?
- How does an employer get out from under such liability?
- Can the employer end its obligation by terminating the Plan?

Defined Benefit Pension Plans and the PBGC – Overview

- Tax-qualified defined benefit pension benefits are provided to employees through company-sponsored plans and union-sponsored “multiemployer pension plans.”
- Company-sponsored tax-qualified pension plans may provide benefits for union employees as well as for non-union employees.
- Tax-qualified plans are subject to statutory minimum funding rules and are required to participate in the PBGC insurance system.

Defined Benefit Pension Plans and the PBGC – Overview (continued)

- Non-qualified pension plans do not require minimum statutory contributions and are not subject to PBGC insurance.
  - Commitments under these SERPS are generally analyzed as contract claims in the U.S.
  - These SERPS cannot be extended to the lower-paid work force, and must be limited to a select group of management and highly-compensated employees.

Pension Costs – Overview

- In a multiemployer plan, the employer is responsible for negotiated contributions pursuant to a collective bargaining agreement.
  - The employer may have to make contributions in excess of the negotiated rate if the plan is underfunded and the employer must make contributions under the statutory minimum funding requirements.
  - PBGC deals directly with multiemployer plan trustees and not with contributing employers.

Pension Costs – Overview (continued)

- For multiemployer plans, if the employer discontinues its participation, completely or in part, it can be assessed *withdrawal liability* or *partial withdrawal liability.*
  - Partial withdrawal liability events can include plant shutdowns, significant workforce reductions, etc.

Pension Costs – Overview (continued)

- For single-employer plans, an employer which terminates 20% or more of its active plan participants in connection with a facility closing may be required to place an amount representing a proportional share of the plan's unfunded liability in escrow or furnish the PBGC with a bond equal to 150% of that amount.
- If the plan does not terminate within 60 months of the withdrawal, the liability is abated and the escrow amount is refunded or the bond cancelled.

Pension Costs – Minimum Funding

- The costs of continuing a pension plan vary from year to year, principally based upon plan asset investment performance and the changing value of benefit promises: benefit liabilities fluctuate from year to year as interest rates rise and fall, new benefits are earned, old benefits are paid out, workers die, etc.
- Changes in pension funding rules enacted by Congress can also have significant impact on employer's funding requirements.

Pension Costs – Minimum Funding (continued)

- Under certain circumstances, companies may obtain ***funding waivers*** from the Internal Revenue Service which reduce the amount of the contributions required for the upcoming plan year.
- A funding waiver merely allows an employer to amortize payment of one year's required pension plan contribution over five years and does not extinguish the employer's contribution obligations. *See* Internal Revenue Code § 412(d); ERISA § 303.
- A plan is limited to three waivers in 15 years.

Pension Contributions – Minimum Funding

- ERISA requires employers to make annual contributions.
  - The pace is designed to quickly bring pension plans to a well-funded position and maintain funding at an adequate level. *See* IRC § 412; ERISA § 302.

Pension Contributions – Minimum Funding **(continued)**

- "Catch-up Payments": The funding rules require accelerated payments over seven years to reduce underfunding in defined benefit plans, and restrict benefit increases and certain distributions based on the funding level of a plan.

    See Title I of ERISA and the Internal Revenue Code (as amended by §§ 101-116 of the Pension Protection Act of 2006 (hereinafter referred to as the "PPA")).

Pension Contributions – Minimum Funding (continued)

- The rules are intended to cause plans to become better funded and, therefore, less likely to need termination or, if terminated, to have smaller shortfalls for the PBGC to absorb. (NB: PBGC liens extend to these payments).
- Missed contributions in excess of $1 million trigger liens against all controlled group members.
- PPA funding target is proving more difficult to meet in today's economy and interest rate environment.
  - MAP-21 legislation designed to reduce minimum contributions required
  - Proposed bill would grant relief: for those plans that fall below the set target funding for a particular year, these plans will be required to fund up to the specified funding percentage for that year, instead of 100%.

Pension & Benefits – Terminating an Underfunded Pension Plan

- ERISA prohibits an employer from terminating an underfunded tax-qualified pension plan unless specific requirements are met.
- An important exception allows an employer in Chapter 11 to voluntarily terminate its underfunded pension plan – a so-called “distress termination” – if the bankruptcy court approves the termination.
- There are three other distress termination tests that can be met but are outside of bankruptcy.

Pensions & Benefits – Distress Termination

- The bankruptcy court can approve the “distress” pension plan termination only if the court determines that, unless the plan is terminated, the debtor will be unable to pay all of its debts pursuant to a plan of reorganization and will be unable to continue in business outside the Chapter 11 reorganization process.
  - A review of the relevant case law suggests that the bankruptcy court can make this finding even before a plan of reorganization is proposed. ERISA § 4041(c).
- The PBGC is still required to make an independent finding that the plan(s) must be terminated in order for the sponsor to re-organize.

Pensions & Benefits – Distress Termination (continued)

- In Chapter 7 or a liquidating Chapter 11, the plan will be terminated because of the liquidation of the employer (unless there are solvent affiliates which can assume the plan).
  - In this case, the Chapter 7 trustee must take over not only the employer's estate, but also any of its obligations as a plan administrator. *See* 11 U.S.C. § 704.
- The PBGC must make an independent finding with respect to these terminations.

Pensions & Benefits – Termination Procedures

- PBGC regulations govern the process of terminating a pension plan in a distress termination. This process includes 60 days advance notice (a “Notice of Intent to Terminate”) to participants, beneficiaries, union and PBGC. PBGC Reg. § 4041.43.
- The PBGC is a federal agency which insures vested pension benefits up to a limit, in cases where an underfunded tax-qualified pension plan is terminated.

Pensions & Benefits – Termination Procedures (continued)

- The PBGC may itself seek to terminate an underfunded plan in some situations. Where the employer is in bankruptcy, the PBGC can generally terminate a plan only if it demonstrates to the bankruptcy court that the termination is needed to protect participants or to avoid any unreasonable deterioration of the financial condition of the fund or any unreasonable increase in its liabilities. ERISA § 4042.
- PBGC can make that determination outside of bankruptcy as well.

Pensions & Benefits – Effect on Worker Benefits

- On the termination date, workers stop earning new benefits.
- If pension liabilities exceed pension assets, PBGC insures benefits subject to certain limitations.
- Benefits at greatest risk for loss include:
  - age 65 benefits in excess of $56,000 per year (actuarially equivalent lower limits apply to early retirement benefits paid before age 65);
  - some portion of benefit increases in effect for fewer than 5 years. ERISA § 4022; and
  - supplemental benefits.

Pensions & Benefits – Effect on Worker Benefits (continued)

- In a plan sponsor's Chapter 11 case, the petition date is the plan termination date for purposes of determining the Title IV guarantee.
  - In all other cases the plan termination date is the date fixed for measurement of each participant's guaranteed benefit.
- Post-petition benefit accruals are therefore not guaranteed. ERISA § 4022(g) as amended by PPA § 404.

Pensions & Benefits – Effect on Worker Benefits (continued)

- Plans provided pursuant to a CBA can be modified or terminated only pursuant to Bankruptcy Code § 1113 unless the union agrees.

Pensions & Benefits – PBGC Claims Against A Bankrupt Employer

- The PBGC may have the following claims against a bankrupt sponsor and all controlled group members:
  - Claim for unpaid minimum funding contributions;
  - Claim for unpaid premiums; and
  - Claim for unfunded liabilities.
    ERISA §§ 4007, 4042(d)(1)(B)(ii), 4062.

Pensions & Benefits – PBGC Claims Against A Bankrupt Employer (continued)

- These claims are joint and several against the employer and all of the members of its controlled group (*e.g.,* a parent corporation and its 80%-owned subsidiaries).

Pensions & Benefits – PBGC Claims Against A Bankrupt Employer (continued)

- In addition, there is a PBGC liability that is triggered when the plan sponsor (or controlled group members) exits from bankruptcy:
  - a termination premium in the amount of $1,250 per participant for each of three years is payable by the plan sponsor or controlled group members following termination of its underfunded plan.
  - For a plan terminated in bankruptcy, the first payment is not due until after the debtor's discharge from bankruptcy. ERISA § 4006(a)(7), as added by § 2201 of the Deficit Reduction Act of 2005.

Pensions & Benefits – Priority of PBGC Claims

- The PBGC's lien rights will not interfere with the priority of properly perfected liens securing obligations that predate the filing of notice of the PBGC's liens.
- There is also a grace period under ERISA § 6323(d) that extends until the earlier of (i) 45 days after the PBGC files notice of its lien or (ii) the date of "actual notice or knowledge" of the filing of such lien.

Pensions & Benefits – Employer Liability

- Plan termination results in a PBGC claim against a bankrupt employer's estate for 100% of the underfunding and unpaid contributions.
- The majority of the courts treat the shortfall as an unsecured, pre-petition general creditor obligation to the extent the shortfall arose pre-petition.
  - *See*, *e.g., In re Sunarhauserman, Inc.,* 126 F.3d 811 (6th Cir. 1997), involving a single-employer plan, in which the Court stated that it "view[s] the bankruptcy court's standard as focusing on whether the acts giving rise to a particular liability occurred pre- or post-petition . . ."

Pensions & Benefits – Employer Liability (continued)

- Certain outlier termination liability cases, such as *Columbia Packing Company* v. *PBGC,* 81 B.R. 205 (Dist. Ct. Mass. 1988), have held that even if the past service liability is calculated based on pre-petition labor, the entire amount is entitled to administrative priority so long as the payment accrued post-petition.

Pensions & Benefits – Employer Liability (continued)

- The PBGC's claim is for unfunded liabilities related to both PBGC guaranteed and non-guaranteed benefits.
- A portion of the assets recovered by the PBGC in its claim are used to provide additional benefits to participants.

Pensions & Benefits – Employer Liability (continued)

- Participants in an underfunded terminated plan will receive:
  - PBGC guaranteed benefits;
  - Non-guaranteed benefits paid out of the assets of the terminated plan – depending on the plan funding levels; and
  - PBGC paid non-guaranteed benefits paid out of the assets recovered by the PBGC's unfunded benefit liabilities claim – depending on the plan funding levels

Pensions & Benefits – Valuation

- In asserting its claim, the PBGC will value the pension underfunding using the PBGC actuarial factors (including the interest rate for determining the present value) as of the proposed date of termination.
- Some parties have characterized these assumptions as “very conservative”.
  - *Note*: a lower interest rate assumption produces a higher estimate of the present value of pension liabilities.
- Rates used in the valuation are based on market surveys of annuity providers.

Pensions & Benefits – Valuation (continued)

- In the *U.S. Airways* bankruptcy, the PBGC submitted proof of claim for $2,083,600,000 for unfunded benefit liabilities based on the 5.1% PBGC interest rate on the date of the plan termination.
    - *In re US Airways Group, Inc.*, 303 B.R. 784 (Bankr. E.D. Va. 2003).

Pensions & Benefits – Valuation (continued)

- Some bankrupt employers will object and request that the bankruptcy court value the unfunded benefit liabilities based on a "***prudent investor rate***"
  - In *U.S. Airways,* the employer unsuccessfully argued that the PBGC's claim "exceeds any reasonable calculation of the actual liability that PBGC will incur . . . because in calculating the value of benefit liabilities . . . PBGC used unrealistic actuarial assumptions that artificially inflate the value of the claim." (Debtor's Objection to the PBGC's Proof of Claim).

Pensions & Benefits – Valuation (continued)

- The employer may try to rely on the Sixth Circuit decision in *In re CSC Industries, Inc*., 232 F.3d 505 (6th Cir. 2000), in which the Court determined that "[w]hile validity of a claim is governed by nonbankruptcy law, bankruptcy courts have the statutory authority to determine the allowability and amount of the claim."

Pensions & Benefits – Valuation (continued)

- A relatively recent case that addressed the issue, *In re Sea Containers Ltd.,* 2008 WL 4296562 (Bankr. D. Del. 2008), agreed with and cited *U.S. Airways*: "[I]t is simply not a correct reading of [the Supreme Court's decision in] *Raleigh* [v. *Illinois Dep't of Revenue*] to say that nonbankruptcy law determines only the abstract validity of the claim" and that "Raleigh is very clear that a creditor's claim 'in the first instance' is a function of the nonbankruptcy law giving rise to the claim."

Pensions & Benefits – Valuation (continued)

- The PBGC continues to argue against the application of a “prudent investor rate.”
- Nevertheless, several jurisdictions have held that a pension termination underfunding claim should be measured using actuarial factors that are less conservative than those used by the PBGC (with the result that the liability claims would be smaller).

Pensions & Benefits – Valuation **(continued)**

– *See*, *e.g., In re CSC Industries, Inc.,* 232 F.3d 505 (6th Cir. 2000) (holding that the "prudent investor rate" is an appropriate valuation tool for a claim involving unfunded benefit liabilities in the bankruptcy context); *In re CF&I Fabricators of Utah, Inc.,* 150 F.3d 1293 (10th Cir. 1998) (affirming a lower court's use of the prudent-investor discount to present value an unfunded benefits liability claim).

Pensions & Benefits – Valuation (continued)

- In addition to disputes over the appropriate interest rate for the present value discounting of liabilities, the PBGC and the employer may argue over the appropriate mortality and retirement assumptions.
  - *E.g.*, in the *U.S. Airways* case, the employer objected to the PBGC's assumption regarding early retirement age.
- *PBGC disagrees with these assertions and has consistently litigated valuation issues unless a global settlement related to claims and recoveries is reached.*

Pensions & Benefits – Controlled Group Liability and Unfiled Foreign Affiliates

- Does plan liability extend to non-US entities?
- In a 1997 opinion letter the PBGC maintained that withdrawal liability extends to foreign entities within a controlled group upon the domestic entity's Chapter 11 filing despite the obvious jurisdictional issues.
- The PBGC has historically been unsuccessful in establishing liability against foreign entities in the face of jurisdictional challenges. *GCIU-Employer Retirement Fund v. Goldfarb Corp.*, 565 F.3d 1018 (7th Cir. 2009) (mere ownership of a majority of the equity interest in a U.S. Subsidiary and ERISA's broad definition of corporate affiliation as an element of liability insufficient to establish personal jurisdiction); *PBGC v. Satralloy, Inc.*, No. C-2-90-0630, 993 U.S. Dist. LEXIS 21422 (S.D. Ohio Aug. 6, 1993) (mere inclusion in the controlled group of, and ownership by, a U.S. entity were not contacts sufficient to subject a foreign entity to personal jurisdiction).

Pensions & Benefits – Controlled Group Liability and Unfiled Foreign Affiliates (continued)

- However, in *Pension Benefit Guaranty Corp. v. Asahi Tec Corp.*, Civil Action No. 10-1936 (ABJ), 2012 WL 843937 (D.D.C. Mar. 14, 2012), the District Court for the District of Columbia held that a Japanese parent corporation ("Asahi") with limited U.S. contacts was subject to the court's jurisdiction in a suit brought by the PBGC to collect unfunded pension liabilities of the parent's wholly-owned U.S. subsidiary which the parent had acquired in 2007.

- Denying Asahi's motion to dismiss for lack of personal jurisdiction, the District Court held that the PBGC had made a *prima facie* showing that Asahi was subject to the specific jurisdiction of the court, when Asahi had (i) purposefully directed activity towards the United States in connection with its acquisition of the subsidiary and (ii) knowingly assumed controlled group liability as a result of Asahi's diligence process in connection with the acquisition.

- **Implications:** Due to the procedural posture of the case, Asahi must litigate the merits of the PBGC's case before it is able to raise jurisdictional challenges on appeal. Until the appellate process runs its course, however, the decision could discourage foreign entities from investing in U.S. entities with significant unfunded pension liabilities.

Retiree Benefits – Section 1114 Overview

- Compliance with Section 1114 of the Bankruptcy Code is the exclusive means for a debtor to reject or modify retiree insurance benefits in bankruptcy.

Retiree Benefits – Modification

- A trustee (including the debtor in possession) shall pay and not modify any retiree benefits unless:
  - the court, on motion of the trustee or the authorized representative, orders modification; or
  - the trustee and the authorized representative agree to modification.

Retiree Benefits – Procedure for Modification/Rejection under § 1114

- If the debtor seeks to modify or not pay retiree benefits, upon motion by any party in interest, the court shall appoint a committee of retired employees to serve as the authorized representative of persons receiving retiree benefits.

Retiree Benefits – Procedure for Modification/Rejection under § 1114 (continued)

- Before filing an application for modification, the trustee must make a proposal to an authorized representative based on the most complete and reliable information available at the time of the proposal.
  - Proposal must provide for those necessary modifications to the retiree benefits that are necessary to permit the reorganization of the debtor and that assures all creditors, the debtor and all of the affected parties are treated fairly and equitably.
  - The trustee must provide authorized representative with such relevant information as is necessary to evaluate proposal.

Retiree Benefits – Procedure for Modification/Rejection under § 1114 (continued)

- Between proposal and hearing on motion to modify, the trustee must meet and negotiate in good faith with union representative in attempting to reach mutually satisfactory modifications of retiree benefits.

Retiree Benefits – Procedure for Modification/Rejection under § 1114 (continued)

- The bankruptcy court shall approve an application for modification of retiree benefits only if the court finds that:
  - The debtor has made a proposal that fulfills the requirements of Section 1114;
  - Authorized representative has refused to accept the proposal without good cause; and
  - Such modification is necessary to permit the reorganization of the debtor and assure all creditors, the debtor and all of the affected parties are treated fairly and equitably, and the balance of the equities clearly favors modification of the retiree benefits.

Retiree Benefits – Timing

- A hearing must be held within 14 days of filing an application for modification, on 10 days notice to all parties.
- The court must rule on the application within 90 days of hearing, unless trustee and authorized representative agree to an extension.

Retiree Benefits – Remedies for Non-payment

- The only remedy for non-payment under Section 1114 is to allow benefits to be paid as an administrative expense under Sections 503 and 507.
- One court has determined that payment of retiree benefits is required as soon as there are unencumbered assets available to make such payments. *In re GF Corp.*, 23 C.B.C.2d 267 (Bankr. N.D. Ohio), *vacated in part on reconsideration, 120 B.R. 421 (Bankr. N.D. Ohio 1990).*

Retiree Benefits – Reservation of Right to Terminate or Modify

- Most retiree medical plans will include explicit language reserving the employer’s right to terminate the retirees’ benefits.
- Prior to the enactment of Section 1114, the Sixth Circuit Court of Appeals upheld a bankruptcy court decision that an employer’s explicit reservation in a benefits summary provided the employer with the right to terminate or modify retiree insurance benefits. (*In re White Farm Equipment Co.,* 788 F.2d 1186, 7 Employee Benefits Cas. (BNA) 1411, Bankr. L. Rep. (CCH) P 71104 (6th Cir. 1986)).

Retiree Benefits – Reservation of Right to Terminate or Modify (continued)

- Following the enactment of Section 1114, some courts have questioned whether Section 1114 applies if the debtor, prior to filing for bankruptcy protection, had reserved the right to modify or terminate retiree benefits.
- These courts reason that Section 1114 serves no purpose when the employer has a reserved right to modify retiree benefits. *See, e.g., In re Doskocil Cos.,* 130 Bankr. 870 (Bankr. D. Kan. 1991).

Retiree Benefits – Reservation of Right to Terminate or Modify (continued)

- Other courts, have rejected the reserved rights argument. *See, e.g., Ames Department Stores, Inv.* v. *Employees' Committee,* 1992 WL 373492 (S.D.N.Y. Nov. 30, 1992).