Sun Capital Won This One, But Pension Plan Withdrawal Liability Still Presents a "Risky Gambit" to Private Equity Funds

Nov 18, 2020

Categories:

Private Equity Industry Blog
Tax Law Defined™ Blog

Authors:

Michael T. Bindner

A federal district court recently called investments in private companies that participate in a multiemployer pension plan (MPP) a "risky gambit" because of the potential for exposing the MMP's investors to withdrawal liability[1]. This type of liability is sometimes referred to as a "hidden liability" because, in some situations, investors may have exposure for the liability even if they did not affirmatively assume the liability under a purchase agreement.

As a part of the collective bargaining process, employers with union workforces oftentimes agree to contribute to an MPP, to which other union employers also contribute. If an MPP is underfunded when the employer stops contributing to the MPP (e.g., sells or liquidates its business, exits the union, etc.), federal pension law imposes an exit penalty, referred to as "withdrawal liability," by allocating a portion of the unfunded vested benefits in the MPP to the withdrawing employer. If the withdrawing employer cannot pay the withdrawal liability, the liability will be assessed to any commonly owned businesses of the employer, which can include an investor in a private company if the investor is determined to be a "trade or business." For this purpose, commonly owned businesses are businesses in a controlled group with or under common control with the contributing employer. A controlled group could include two entities, one of which owns 80% or more of the other.

In the ***Sun Capital Partners*** cases, federal courts determined that two Sun Capital funds were not merely "passive investors," but "trades or businesses" because they operated and managed the operating entity and were provided a direct economic benefit that an ordinary passive investor would not derive. The courts applied what is referred to as the "investment plus" test (i.e., the owner is more than just a passive investor) in making the determination that the Sun Capital funds were "trades or businesses." Fortunately for

2026 FBT Gibbons LLP. All rights reserved. ADVERTISING MATERIAL.

the funds, the U.S. First Circuit Court of Appeals in a decision issued in 2019 held that because (1) neither Sun Capital fund owned at least 80% of the operating entity and (2) the two funds were determined not to be in an implied partnership with each other, the two funds were not considered in common control with the operating entity and thus not responsible for the operating entity's withdrawal liability. In 2020, the U.S. Supreme Court refused to review the Circuit Court of Appeal's decision. As a result, the decision remains the controlling law on these issues in the jurisdiction of the First Circuit which covers Maine, Massachusetts, New Hampshire, Rhode Island and Puerto Rico and the decision may be followed by federal courts in other jurisdictions in the future. Even though Sun Capital eventually prevailed, they presumably spent significant sums on attorneys' fees fighting the Pension Plan on this issue. [2]

The Sun Capital precedent still poses a threat to investors because of the "trade or business" finding. Private equity firms should perform significant due diligence to ascertain the risk and exposure to withdrawal liability. Further, care should be taken to properly structure deals.

Read "Surprise! You may be Liable for Union Pension Plan Withdrawal Liability" for a full explanation of risks to individuals and entities, other than the employer, when the participating employer becomes insolvent and can't pay the withdrawal liability. Also, read "17 Ways to Avoid or Reduce Multiemployer Pension Plan Withdrawal Liability."

---

[1] SUN CAPITAL PARTNERS, III, LP, SUN CAPITAL PARTNERS III QP, LP, and SUN CAPITAL PARTNERS IV, LP v. NEW ENGLAND TEAMSTERS AND TRUCKING INDUSTRY PENSION FUND, 329 F.R.D. 102 (D. Mass 2018).

[2] SUN CAPITAL PARTNERS, III, LP, SUN CAPITAL PARTNERS III QP, LP, and SUN CAPITAL PARTNERS IV, LP v. NEW ENGLAND TEAMSTERS AND TRUCKING INDUSTRY PENSION FUND, 943 F.3d 49 (First Cir. 2019).

© 2026 FBT Gibbons LLP. May be considered attorney advertising in some jurisdictions.

2026 FBT Gibbons LLP. All rights reserved. ADVERTISING MATERIAL.

FBT Gibbons