



Third Circuit Addresses Issue of First Impression

In re Marcal Paper Mills, Inc., 2011 WL 2410740 (3d Cir. June 16, 2011)

In *Marcal*, the Third Circuit addressed an issue of first impression under the Employee Retirement Income Security Act (ERISA) as amended by the Multiemployer Pension Plan Amendments Act (MPPAA): Can the portion of withdrawal liability attributable to post-petition services qualify as an administrative expense of the debtor's estate? The Bankruptcy Court said no, the district court said yes, and the Third Circuit affirmed the district court's decision.

Marcal Paper Mills, Inc. (Marcal, Inc.) filed for protection under Chapter 11 in November 2006. From and after its petition date through May 30, 2008, Marcal, Inc., continued to employ unionized workers and make pension-related contributions for such workers as required under the terms of applicable collective-bargaining agreements. As of May 30, 2008, Marcal, Inc.'s assets were sold, Marcal, Inc., ceased to employ such workers, and Marcal, Inc.'s obligation to make pension-related contributions ended. The purchaser of Marcal, Inc.'s assets—Marcal Paper Mills, LLC (Marcal, LLC)—did not employ the unionized workers and did not assume liability for any pension-related contributions from and after the date of the purchase of Marcal, Inc.'s assets. Marcal, LLC, did, however, assume liability for Marcal, Inc.'s pre-closing related pension obligations.

The Trucking Employees of North Jersey Welfare/Pension Fund (TENJ) determined that Marcal, Inc., had made a complete withdrawal from its pension fund as a result of Marcal, Inc.'s sale of assets and failure to continue to employ union workers. TENJ assessed Marcal, Inc., with total withdrawal liability in the amount of \$5,890,128 and moved the Bankruptcy Court to treat the withdrawal liability related to the union workers' post-petition services as an administrative expense of Marcal, Inc.'s estate.

The Bankruptcy Court denied TENJ's motion and classified the entirety of its claim as a general unsecured claim. The district court reversed and remanded with direction to the Bankruptcy Court to accord administrative expense status to the post-petition portion of Marcal, Inc.'s withdrawal liability. The Third Circuit reviewed *de novo* the question of whether withdrawal liability can qualify as an administrative expense under the Bankruptcy Code.

The Third Circuit began its analysis with Section 503(b)(1)(A). Under that section, an administrative expense includes the actual, necessary costs of preserving the estate, including wages, salaries, and commissions for services rendered after the petition date.



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To qualify as an administrative expense, the expense must arise from a post-petition transaction and be beneficial to the debtor in the operation of its business.

With these standards in mind, the Third Circuit described its understanding of Marcal, Inc.'s pension-related obligation. According to the Third Circuit, Marcal, Inc., was party to a defined-benefit plan. In a defined-benefit plan, the employer commits to a particular pension benefit as determined by the plan trustee based on the expected resources of the plan. Expected resources of the plan include expected future contributions, and, therefore, at the time of its withdrawal from the plan, a withdrawing employer may not have made sufficient contributions to fund its share of vested pension benefits. MPPAA was enacted to impose liability for unfunded vested benefits on the employer that is withdrawing from a defined-benefit plan and provide a framework for the calculation of the withdrawing employer's unfunded pension liability.

Under the facts at issue, the Third Circuit first determined that Marcal, Inc., received a benefit from the employees' provision of post-petition services. Therefore, the court agreed with the district court that withdrawal liability associated with such employees' post-petition services qualified for administrative expense treatment.

The court rejected Marcal, LLC's argument that the amorphous nature of the calculation of withdrawal liability and the variety of factors considered in such calculation—including factors unrelated to Marcal, Inc.'s particular employees or their specific post-petition work on behalf of Marcal, Inc.—weighed against a finding of benefit to the estate necessary for administrative expense status. Instead, the Third Circuit noted that the conditions of such calculations were known to Marcal, Inc., prior to its decision to use the services of covered employees from and after its petition date. While Marcal, LLC, “paints the amount of withdrawal liability it owes as wholly subject to the whims of the market and actuarial assumptions, it ignores the fact that pursuant to Marcal [Inc.]’s agreement to provide a defined benefit, it assumed those risks with open eyes.” The court further noted its view that it was “simply unseemly for [Marcal, LLC] to disclaim responsibility for the vested benefits Marcal[, Inc.,] created by choosing to use covered employees to perform post-petition work.”

The Third Circuit also rejected Marcal, LLC's argument that withdrawal liability, by its nature, was intended to benefit employees other than Marcal, Inc.'s employees, or entities other than Marcal, Inc., that might incur liability for Marcal, Inc.'s unfunded benefit obligations. As Marcal, LLC, admitted that withdrawal liability, in part, would benefit Marcal, Inc.'s employees, the court found that “the simple fact is that the plan exists for the benefit of the employees. . . . [and] [b]ecause withdrawal liability ensures that there are enough plan assets to provide promised benefits, it is provided in consideration for the employees' willingness to continue to work.”



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The Third Circuit noted that in finding “the post-petition portion [of the withdrawal liability] can be classified as an administrative expense, we harmonize the purposes of the Bankruptcy Code and ERISA, as amended by MPPAA.” The court further noted that “by limiting what constitutes an administrative expense to only that portion of the withdrawal liability which can be fairly allocated to the post-petition period, we help preserve the estate and prevent it from being devoured by the entire withdrawal liability claim.”

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