Proskauer

newsletter

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in this issue

A monthly "best practices" alert for multinationals confronting the challenges of the global workplace.

This Month's Challenge

Transferring executives across national borders raises a question of integrating pension schemes (among other things). Without careful drafting, the company may be giving the employee an unexpected windfall.

Best Practices Tip of the Month

Multinational employers need to make sure their pension schemes and executive compensation plans take into account the various national laws that govern these arrangements.

Tip of the Month

Benefit Plans of Multinational Companies Must Take into Account the Employer's Multinational Status

It's not easy to be a multinational corporation, and one of the difficulties, it turns out, is remembering that the company has employees in many countries besides the U.S.. A multinational company acts at its peril when it forgets that its foreign affiliates are not governed by U.S. laws. That was the lesson delivered by the Seventh Circuit Court of Appeals last month to Eli Lilly and Company, the multinational pharmaceutical giant, in *Bandak v. Eli Lilly and Co. Retirement Plan*.

In 1995, Lilly transferred Stephen Bandak, who had been working in Lilly's UK affiliate for nearly seventeen years, to the U.S. To protect Bandak from a loss of pension benefits as a result of his transfer, Lilly told him that under the company's U.S. pension plan, the pension calculation would include his prior years of service in the UK. When Bandak retired in 2004, the company duly calculated his pension based on his full 26 years of service, yielding a monthly benefit of about $18,000 – then subtracted the $4,000 per month benefit he was receiving from the UK affiliate's pension plan to prevent double-counting of those years he spent in the UK. Even with the offset, calculating the pension in this manner resulted in a much larger pension for Bandak than he would have received if the UK years had not been included in calculating the U.S. portion of his pension benefit. Bandak objected, however, insisting he was entitled to receive both the pension under the UK plan for his years of service in the UK and the full benefit under the U.S. plan, for his combined years of service in the UK and the U.S., without offset.

The offset to prevent double-counting is standard fare in U.S. defined benefit pension plans, and the Lilly plan included a specific provision requiring the offset of the benefit payable to an employee "under a qualified defined benefit plan maintained by [a Lilly] affiliate . . . if such benefit accrued during a Benefit Year of Service credited under [the U.S. plan]." The court, however, sided with Bandak. The problem with Lilly's attempt to apply the offset provision in the U.S. plan is that the UK plan could not be considered a *"qualified"* defined benefit plan.

The plan itself did not contain a definition of a "qualified" plan. Judge Posner, writing for the court, held that this is a technical term that must have been used by the plan's authors in its technical sense: "Lilly is a sophisticated enterprise," Posner said, and "the plan document was undoubtedly drafted by lawyers specializing in ERISA, and those lawyers would, unless it were stated otherwise in the document, use technical legal terms in their technical legal sense." Technically, he concluded, a "qualified" defined benefit plan is a plan that qualifies for favorable tax treatment under the US Internal Revenue Code. The UK plan did not fit this definition.

It seems that Lilly, for all its sophistication and its array of lawyers steeped in ERISA, simply forgot, when drafting the offset provision in the US pension plan, that some employees would be transferring into the US plan with pension service under foreign plans that were not qualified under U.S. tax laws.

To make matters worse for Lilly, at least in this case, the U.S. plan was amended specifically to cure this defect. That amendment, however, was adopted two years after Bandak was transferred to the U.S., and by its terms only applied to employees coming under the U.S. plan after its adoption. The company's contention that the U.S. plan was always understood to mean that service could not be counted twice under an affiliate plan and the U.S. plan received short shrift from the Seventh Circuit, both because the plan document failed to include such an arrangement and because there was no evidence in the record that the offset had been applied in that fashion.

The lesson for multinational employers is clear: When drafting benefit plans (and other HR documents), remember that multinational employers have employees in countries where U.S. laws do not apply.

Proskauer Rose LLP's International Labor and Employment Law Practice Group counsels companies doing business globally in connection with the employment issues they face in their workplaces around the world.

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