

Defined Benefit Plan Lift-Outs Fiduciary Standards

May 14, 2024

PRACTICES Employee Benefits and Executive Compensation

Recently, several plaintiff law firms, on behalf of former plan participants, have challenged decisions by defined benefit plan sponsors to transfer their plan liabilities to insurance companies. A defined benefit plan “lift-out,” which is permitted under ERISA, transfers risk and certain liabilities (usually for retirees or beneficiaries in pay status) to an annuity provider outside of the plan. The complaints generally allege that the plan sponsor breached its fiduciary duties by selecting an annuity provider backed by a private equity firm rather than a traditional annuity provider.

As a reminder, and as we previously reported [here](#), the plan’s purchase of annuities is a fiduciary decision and must comply with the requirements of DOL Interpretative Bulletin 95-1 (available [here](#)) for the purpose of obtaining the safest annuity available for defined benefit plans. While lift-outs may be the right approach for plan sponsors and committees in the current interest rate environment as compared to other defined benefit plan de-risking strategies, including terminating the plan, plan fiduciaries must ensure they are selecting an annuity provider in accordance with DOL guidance.

Under the DOL’s current guidance, a plan fiduciary that is considering a defined benefit plan “lift-out” must take steps calculated to obtain the safest annuity available, unless under the circumstances it would be in the best interests of participants and beneficiaries to do otherwise. In connection with this requirement, the DOL provides the following types of factors that a plan fiduciary should consider, among other things, when selecting an annuity provider:

- The quality and diversification of the annuity provider’s investment portfolio;
- The size of the insurer relative to the proposed contract;
- The level of the insurer’s capital and surplus;
- The lines of business of the annuity provider and other indications of an insurer’s exposure to liability;
- The structure of the annuity contract and guarantees supporting the annuities, such as the use of separate accounts; and
- The availability of additional protection through state guaranty associations and the extent of their guarantees.

With respect to the above requirements, pursuant to the SECURE 2.0 Act of 2022, Congress directed the DOL to review these fiduciary standards and provide a report in order to determine whether amendments are warranted, including assessing any risk to participants. The DOL indicated that it expects to submit this report to Congress shortly. In light of these recent litigation and regulatory developments, engaging legal counsel and an outside consultant to navigate the process is extremely important once the plan sponsor begins to consider a defined benefit plan lift-out.