Why a Protected Benefits Analysis Is Necessary When Merging Retirement Plans

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When employers merge retirement plans in connection with a business transaction or otherwise, they should be wary of ERISA's anti-cutback rule, which prohibits the reduction of accrued participant benefits under a qualified plan. Additionally, plan merger rules require that a merged plan must provide participants with a benefit equal to or greater than what they would have received before the merger and must otherwise preserve certain protected benefits. In order to mitigate the risk of violating these rules, plan sponsors should conduct a protected benefits analysis to compare plan provisions under the old plan to the benefits provided under the new merged plan. In addition to protected benefits, elections for nondiscrimination testing purposes must be consistent across all retirement plans within a plan sponsor's controlled group.

Below is a non-exhaustive list of plan provisions and benefits that should be considered as part of the protected benefits analysis when merging from the old plan into the new merged plan:

- Top paid group election for highly compensated employees: For purposes of determining which participants are highly compensated employees ("***HCEs***") for nondiscrimination testing purposes, a plan sponsor may elect to classify only the highest paid 20% of an employer's workforce as HCEs (in addition to any 5% owners). Without such an election, all employees that have earned more than $160,000 in 2025 (indexed for inflation in subsequent years) would alternatively be considered HCEs under the plan. Since all plans within a controlled group must either apply the top paid group election or not, this election must be considered when merging plans, and also if there is more than one plan sponsored by employers within a controlled group.
- Vesting schedules: In the event that the new merged plan has a less favorable vesting schedule, the more favorable vesting schedule from the old plan must be preserved for any already accrued benefits.
- Distribution events: Specific distribution events that are permitted under the old plan must be preserved under the new merged plan. For example, if the old plan allows for in-service distributions at age 59½ and the new merged plan does not, participants with accrued benefits must retain the right to make in-service distributions with respect to such benefits.
- Optional forms of benefit: Although a plan is not required to provide certain early retirement benefit provisions, specific distribution forms of payment, waivers of allocation conditions for the purpose of receiving employer contributions, and other optional forms of benefits, if such plan provisions were provided to participants under the old plan, they generally must be preserved under the new merged plan for such participants. Notwithstanding the foregoing, under an exception to the anti-cutback rules, 401(k) plans can generally be amended to remove optional forms of distributions (such as installments and annuities) provided that the plan offers a single-sum distribution option that is "otherwise identical" to the optional form of benefit being eliminated. Defined benefit plans can also be amended to eliminate certain optional forms of benefit (such as redundant benefits) if an exception to the general rule is satisfied.

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When merging retirement plans, the ERISA anti-cutback rule provides protection for retirement plan participants. As we discussed in this article, in order to limit potential issues in connection with a plan merger, including with respect to any required plan design elections, plan sponsors should coordinate with their benefits counsel and outside service providers to ensure that the new merged plan provides for a smooth transition of benefits under the plan.

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