

# Client Alert

A report  
for clients  
and friends  
of the firm. May 2001

## Prudential's Plan to Demutualize May Have Fiduciary Impact on Employee Benefit Plans and their Sponsors

The impending conversion of Prudential Insurance Company of America from a mutual company to a publicly traded corporation raises important considerations for employee benefit plans and plan sponsors. Pursuant to Prudential's plan of demutualization, certain eligible policyholders will receive compensation in the form of shares of Prudential stock, cash or policy credits (i.e., enhancements to policy value). If an eligible policyholder is an employee benefit plan governed by the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), various decisions regarding the demutualization should be made by plan sponsors and/or plan fiduciaries and, in certain instances, these decisions may be subject to ERISA's fiduciary requirements (e.g., plan assets must be held for the exclusive benefit of plan participants and fiduciaries must follow the terms of the plan documents, act prudently and diversify plan assets).

Some of the decisions regarding the demutualization include:

### **Whether to Vote in Favor of or Against Prudential's Demutualization.**

This is often the first decision with respect to a demutualization and will likely be subject to ERISA's fiduciary requirements. This decision should be handled like any other vote or tender of securities held by an employee benefit plan.

### **How to Allocate Compensation from the Demutualization.**

This is probably the most difficult decision arising in connection with a demutualization. A decision must be made regarding whether a portion of the compensation from the demutualization is considered owned by the employee benefit plan and, therefore, "plan assets." Even where the employer is the policyholder, the employee benefit plan may be entitled to receive part or all of the demutualization compensation - particularly if participants paid any portion of the premiums under the plan. In addition, if compensation from the demutualization is attributable to different insurance policies and/or different employee benefit plans, a decision must be made whether the compensation should be allocated among those employee benefit plans and how that can be accomplished. To the extent that compensation from the demutualization is determined not to be plan assets, there is some authority to allow an employer to retain that portion for itself. This often entails careful review of the insurance policies and the history of who has paid premiums - the employer or the participants.

### **Whether to Elect to Receive Shares of Prudential Stock, Cash or Policy Credits from the Demutualization.**

To the extent that compensation from the demutualization is a plan asset, the decision to receive shares of Prudential stock, cash or policy credits is an investment decision that should be handled like any other investment decision made by plan fiduciaries. Similarly, if an election is made for an employee benefit plan to receive shares of Prudential's stock, the decision regarding how long to hold the shares and when to sell it will be subject to the fiduciary requirements.

### **How Stock or Cash Received from the Demutualization should be held to Comply with ERISA's Trust Requirements.**

ERISA requires that all assets of an employee benefit plan must be held in trust, under insurance contracts or policies issued by an insurance company or by an insurance company. Accordingly, to the extent that compensation from the demutualization is plan assets,

it must be held in compliance with ERISA's trust requirements. The U.S. Department of Labor recently stated that, in the case of employee benefit plans that are not otherwise required to maintain a trust under ERISA, it would not assert a violation in any enforcement proceeding solely because of a failure to hold compensation from Prudential's demutualization that are plan assets in trust if (i) such assets consist solely of proceeds from the demutualization, (ii) such assets and earning thereon are placed in the name of the plan in an interest-bearing account or custodial account as soon as reasonably possible but no later than 12-months following receipt and (iii) the assets are subject to the control of a designated plan fiduciary that maintains such documents and records necessary under ERISA.

### How the Compensation from the Demutualization should be Used by a Plan.

This generally depends on the type of employee benefit plan and the terms of its governing documents. In certain instances, employers may need to amend their plans prior to receiving the proceeds from the demutualization in order to document how the proceeds will be used (e.g., whether proceeds will be used to increase benefits or provide a contribution holiday for the employer and/or the participants).

To prepare for Prudential's demutualization, all plan documents should be reviewed to determine how these questions and others arising out of Prudential's demutualization should be decided. In addition, with respect to welfare plans, a review of the history of premium payments to Prudential may need to be undertaken to determine whether, and to what extent, participants have paid for the insurance coverage through the years.

Proskauer Rose has assisted a number of clients in addressing the issues arising out of the demutualization of insurance companies, including the demutualization of MetLife Insurance Company last year. In addition, we have worked with benefit consultants and actuaries who have assisted in determining the equitable allocation of compensation from demutualizations among plans and plan sponsors as well as among various plans.

### Has your Address Changed?

Please let us know if your mailing address needs to be updated. Contact Deborah Chernoff with the correct information, either via email: [dchernoff@proskauer.com](mailto:dchernoff@proskauer.com), or fax: 212.969.2900.

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### Client Alert

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