

The nature and extent of employment issues that will exist in connection with an M&A transaction will depend on (1) the deal structure and (2) the buyer's business objectives for the transaction. In this issue of *M&A Primer*, we provide an overview of employment issues from both perspectives.

The Deal Structure

As noted in our prior newsletter on "Deal Structure," all of a target company's assets and liabilities transfer in a merger and in the purchase of a target company's stock. Unless the target company terminates employees prior to the closing of the transaction, or the buyer is able to enter into agreements with the target company's employees that will take effect upon the closing, all of the target company's employees, and its rights and obligations with respect to those employees, remain "as is" and continue after the closing. This is the case whether the target company's employees become employed by a different entity upon the closing (as with a merger transaction), or remain employed by the same entity (as with a stock purchase transaction).

By contrast, the general rule for asset purchase transactions is that the buyer has the flexibility to pick and choose the assets and liabilities it wishes to acquire from the target company, leaving behind those it does not want. However, in order to avoid substantial injustice, courts may invoke the legal doctrine of *de facto merger* to find an automatic transfer of liabilities as a matter of law depending on the overall facts of the transaction and how the assets are used in the conduct of business after the closing.

For these reasons, a buyer in a merger or stock purchase transaction will want to enter into new employment agreements with target company employees, to become effective upon the closing, or distribute communications to target company employees on or immediately after the closing establishing new terms and conditions of employment. Such agreements or communications should be in writing and clearly set out the new terms and conditions of employment. A buyer in an asset purchase transaction will want to enter into new agreements with the target company employees, to become effective upon the closing, for new terms and conditions of employment with the buyer. Such agreements and communications not only serve important legal functions, but can also help target company employees feel welcome and provide them with important information, as well as relieve fears and anxieties they may have about their employment after the closing.

Business Objectives

In all three available deal structures, it is important for the buyer to define its business objectives for the transaction vis-à-vis acquisition of human resources. Many times, a business enterprise is of less value without key managers and employees who run the business—unless, of course, the objective of the transaction is solely to acquire tangible assets.

If the primary business goal of a transaction is to acquire the technology of a target company, the importance of acquiring the employees who have been key to developing that technology, and are needed to continue working with that technology,

cannot be overlooked. Even if the primary business objective of a transaction is to acquire an additional facility, to develop a presence in a new geographic area, to gain access to a new market, to acquire needed equipment, or to acquire a going business concern, a buyer cannot overlook the value of being able to acquire and retain key and other employees who know the facility and equipment, and have experience doing business within that area or market.

For these reasons, regardless of the deal structure, it is important for the buyer to separately define its human resources objectives for the transaction and to plan, with the aid of its own key human resources professionals, how to best attract, integrate, and retain needed target company employees. A buyer can avoid and successfully navigate many employment issues by involving its own human resources professionals and employment lawyers in transaction discussions, due diligence, and negotiations early in the transaction process. Relying on their separate areas of expertise, the buyer's human resources professionals and employment lawyers together can help the buyer understand the answers to the following questions:

- What are the existing employment-related rights and expectations of the target company's employees prior to and upon the closing?
 - Which rights and expectations need to be legally extinguished upon the closing, and what is the best method to do so, consistent with the deal structure, the buyer's company culture, and the administrative burdens that would be involved?
 - What will the buyer need to provide by way of compensation, benefits, severance, and other opportunities in order to retain key target company employees and other knowledgeable and skilled employees of the target company?
- What is the nature and organization of the target company's workforce, and are there opportunities for the buyer to do business better and/or more efficiently with a different staffing model or organizational structure?
- Which of the target company's employees are "key" and otherwise important to the buyer being able to profit from the transaction, and how long will the buyer need to retain "key" and other knowledgeable and skilled target company employees?
- What will the target company do during the one year following the closing to help target company employees become adapted to the buyer's company culture, become integrated into the buyer's business, and get to know key buyer company employees, and to reduce the possibility of the buyer's employees and target company employees developing an "us versus them" mentality?
- In the case of a merger, how will target company employees be integrated into the buyer's workforce by way of being transitioned onto the buyer's benefit and compensation plans, job title and compensation levels, operating systems (such as telephone, IT), and payroll schedule?

If you have any questions, please feel free to contact us.

In Tokyo:

Gregory Salathé
gsalathe@morganlewis.com

Lisa Yano
lyano@morganlewis.com

In San Francisco:

Karen Peteros
kpeteros@morganlewis.com