Agenda

• Deal Drivers – The Big Picture
  – Stock Deals
  – Asset Deals
• Employment Liabilities – Overview
• Due Diligence
• Union Issues
• Integrations, Terminations, and Restructurings
• 10 Biggest Employment Mistakes
• Concluding Remarks
Employment and Labor Issues

• Companies are increasingly focusing on potential employment liabilities in M&A transactions

• This focus is largely due to the increased risk of employment liability, including:

  – Rise in wage and hour claims and class actions

  – Expanded damages caps in discrimination

  – Recent revisions to the FMLA and the ADA
Deal Drivers — The Big Picture

- Employment Law for Deal-Makers . . .
  - Don’t *buy problems* you don’t want
  - Avoid *unwanted costs* for seller
  - Increase *deal value* for buyer and seller
  - Avoid *deal risk* for buyer and seller
  - Prevent *conventional employment* liability (reduction-in-force (RIF) discrimination claims, Worker Adjustment and Retraining Notification Act (WARN), etc.)

- Cornerstone: business objectives should drive employment issues
- You won’t get everything you want, so know the key business drivers

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Stock Deals – General

- Buyer gets everything, good and bad
- Employee relationships remain intact
- Employment and labor contracts remain intact
- Union relationships remain intact
- Restructuring costs attach to business unless . . .
  - restructuring costs are reflected in purchase price, OR
  - some “seller-predecessor” continues to exist AND it agrees to pay restructuring costs
Stock Deals – Strategies for the Buyer

- Due diligence, due diligence, due diligence
- Representations and warranties by seller
  - No benefits violations or litigation except . . .
  - No legal violations or litigation except . . .
- Schedules supplied by seller
  - Pending lawsuits
  - Labor contracts
  - Executive employment contracts
  - Benefits plans
  - Severance and release agreement history – a hidden gem
- Indemnification by seller for . . .
  - Matters predating purchase
  - Violations of representations/warranties
Asset Deals – The Good News

• Potential flexibility concerning employment and other contracts

• Seller’s employment liabilities more likely stay with seller

• Seller’s restructuring costs more likely stay with seller

• Potential flexibility concerning union agreements and relationships

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Asset Deals – The Bad News

• Successorship – what employment obligations does buyer inherit?
  – among the most complicated issues in labor law
• What is test for “successor” status? (more bad news)
  – different types of duties/claims:
    – liability for seller’s discrimination or other unlawful conduct
    – duty to remedy seller’s unlawful conduct
    – duty to bargain with seller’s union
    – duty to arbitrate grievances under seller’s labor contract
    – duty to adopt seller’s labor contract
• Buyer can accidentally assume seller’s problems and liabilities
  – transaction documents are *not controlling* (assumed/excluded liabilities)
Asset Deals – Successor Liability

• Successor liability applies if a court determines it is “fair and necessary” to do so:
  – Concern is that failure to hold successor liable for unlawful employment practices of predecessor would leave the alleged “victim” without a remedy and encourage evasion of statutory obligations through ownership transfers

• Courts often focus on two main factors:
  – Continuity in operations and workforce
  – Ability of the predecessor to provide relief to the alleged victims
Asset Deals – Successor Liability

- **Title VII**: Focus is generally on continuity in operations and workforce, notice to successor of predecessor’s legal obligations, and ability of predecessor to provide relief directly to aggrieved individual (i.e., alleged victim)

- **FLSA**: Special focus on predecessor’s ability to provide relief

- **FMLA (slightly different focus)**:
  - Courts often do *not* consider whether successor had notice of a claim
  - Focus is on whether there is substantial continuity in business operations; use of same work facility; similarity of jobs, working conditions, and supervisory personnel; similarity in machinery, equipment, and production methods; similarity in products and services; and ability of the successor to provide relief

- Regardless of specific factors, courts will generally review the **totality of the circumstances** to determine if successor liability should apply
To mitigate successor liability exposure, buyer should:

- Use the diligence process to determine whether such liabilities exist and, if so, the level of potential exposure
- Incorporate reps and warranties that such liabilities, if any, are the sole responsibility of seller
- Consider adding an escrow, special indemnity, or other mechanism to recover any potential successor liability costs
- Quickly integrate seller’s employees into its organization to avoid absorbing any flaws in seller’s practices
Asset Deals – Strategies for the Buyer

• Due diligence
• Seller’s representations/warranties
• Seller’s schedules
• Seller’s indemnifications
• PLUS . . .
  – deal structure and business changes can potentially alter what buyer gets
  – more potential leverage in renegotiating contracts with seller’s executives
  – more potential leverage in renegotiating union labor agreements
Employment Liabilities: Overview

• Employment liabilities must be considered in light of the type of transaction and the task at hand:
  – Marking up the deal agreement (SPA, APA, JVA, JCA, etc.)
  – Building and reviewing disclosure schedules
  – Advising the client on liability and risk assessment
  – Integration and related matters

• Relates to all sides of the transaction (buy, sell, contributor, etc.)
• **Standard stuff**
  - Employee lawsuits pending
  - Benefit plans and SPDs
  - Employment agreements
  - Confidentiality, noncompetes, nonsolicitations
  - Employee handbooks
  - Arbitration Agreements
  - What unions and where?
  - Labor contracts

• **What you also really want (current and past)**
  - Charge/litigation history
  - Internal complaints/issues
  - Government audits, investigations, and citations
  - Exempt/nonexempt classifications/independent contractor reviews
  - Benefit claim appeals
  - Workers’ comp claims and expenses
  - Workplace accidents, other OSHA information
  - Employment applications, offer letters, turnover data, absenteeism, exit interview results
  - Separation or Severance Agreements
  - EEO-1 forms and affirmative action plans
  - Immigration I-9 forms for current employees
  - Visa overview
  - Prior handbooks, benefit plans, SPDs, etc.
  - Union-organizing attempts (past and pending)
  - All union memos of understanding, side letters, ratification summaries, etc.
  - Grievance, arbitration, NLRB charge history
  - Strike and work stoppage history
Large Exposure Issues

• The following have potential for large exposure to a buyer:
  – Termination and Change-in-control Obligations
  – Misclassification of Service Providers
  – Misclassification of Employees
  – Labor Organizations and Representation
  – OSHA

• Sellers should also pay attention to these issues:
  – Where sellers can resolve or limit these issues prior to the transaction, the sellers may increase their bargaining power and limit the need for heavy negotiation over potential liability
  – Do you have restrictive agreements? Have you made sure they cover what you need?
Misclassification Liability

• Misclassification of service providers
  – A key area in nearly every transaction

  – Like each key area of liability, this impacts both buyer and seller and has implications in integration

  – In acquire-hire transactions, will you be missing what you need?

• Two main types of misclassification:
  – Misclassification of independent contractors

  – Misclassification of employees for overtime purposes
    ➢ Red flag – none or very few nonexempt employees
Misclassification: Independent Contractors

• The key focus is whether an individual was properly classified as a contractor, consultant, or advisor rather than as an employee.

• Potential repercussions for contractor misclassification:
  – Misclassified contractors could be entitled to retroactive participation in employee benefits.
  – Payment of employment taxes and amounts that should have been withheld, including interest and penalties.
  – Unpaid overtime or other wage-based claims (if the employee should have been classified as non-exempt).
  – State law major risk driver.

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Diligence of Independent Contractors

- **Independent contractor classification diligence:**
  
  - Buyer should request information such as lists of contractors with summaries of any services provided and service history
  
  - Buyer should also request copies of individual contractor agreements and related statements of work
  
  - As with overtime, consider requesting any self audits of classifications as well as any recent agency audits
Misclassification: Overtime Exemptions

• The key focus is whether an employee was properly classified as exempt or nonexempt for overtime purposes (FLSA/state law)

• Potential repercussions for misclassification:
  – Potential liability for all unpaid overtime (may run back as far as three years in cases of willful violations)
  – Potential liability for withholding wages
  – Fines and penalties
  – Attorney fees exposure
  – Recordkeeping liability (e.g., where seller has failed to properly record employees’ hours worked)
Overtime exemption classification diligence:

– Request information on employees’ salaries, classifications and job titles, classification policies, and similar documents

– Inquire as to classification methods and practices

– Request internal and external self-audits of classifications as well as any recent DOL (or similar state agency) audits
Mile-High Summary of International Issues

• Assemble your team of knowledgeable lawyers in relevant jurisdictions
• Organize tasks and documents by country as well as by other aspects of the deal
• Press for diligence from relevant foreign entities
• Pay attention to time tables for pre- and postclosing tasks
• Much more extensive government regulation of individual employment relationships in many non-US jurisdictions
• Much more extensive government and legally required union and works council approvals required in many non-US jurisdictions
• Be aware of TUPE (Transfer of Undertakings (Protection of Employment)) and TUPE-like obligations and/or need for Three Party Agreements
• Watch for issues with multijurisdictional employees

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Union Issues

• If employees are represented by a labor organization, buyer must understand scope of representation, including obligations under existing agreements

• Such agreements may include information and requirements relating to such areas as:
  – Employee benefits and compensation
  – Promotions and demotions
  – Hiring and separation from employment
  – Grievances and related matters
Union Issues

**Background**

- Declining union density
  - Private sector union membership: now 6.6 percent

- Union frustrations with conventional organizing
  - Unsuccessful EFCA battle

- The National Labor Relations Board (NLRB or Board) and US Department of Labor (DOL) – labor law reform “in the trenches”
  - Efforts to assist unions with organizing
  - Efforts to make the National Labor Relations Act (NLRA) more relevant in nonunion workplaces
Union Issues

For sellers (and buyers in a stock deal)

- Labor contract obligations
  - Successors/assigns language
  - Limitations on sales, relocations, plant closings, and layoffs
  - Maintenance-of-benefits clauses and required participation in multiemployer pension plans (withdrawal liability)
  - Neutrality or card-check provisions

- Bargaining obligations
  - Decision-bargaining
  - Effects-bargaining
  - Closing-turned-into-something-else
  - Expiration of existing labor agreements

- Potential “runaway shop” claims (antiunion discrimination)

- Risks:
  - Status quo injunctions
  - Buy-it-back, put-it-back plus $$$$
Union Issues

For buyer (in an asset deal)

- Union “successorship” – what seller obligations does buyer inherit?
  - “Workforce majority” is controlling in many cases
    - measured against whom?
    - discrimination in hiring is illegal
  - Business continuity component is also relevant
  - “Perfectly clear successor” loses ability to unilaterally set new initial terms and conditions
  - REMEMBER: different “successor” test for each type of potential obligation

- Protect against “material changes” with deal pending
  - Seller’s labor contracts being renegotiated (check contract termination dates)
  - Significant grievance arbitration cases, other union litigation, and settlements
  - Ad hoc “side agreements” or “memos of understanding”
  - Seller management’s “mixed loyalties” problem
Integration Issues: Initial Questions

• Buyer needs to consider how to integrate service providers into postsigning organization, including:
  – Will they become employees of buyer or a sub upon closing? If so, where in the organization?
  – If acquired company continues to exist as a wholly owned sub of buyer, will they continue to be employed by the surviving entity?
  – Will buyer continue any of seller’s existing benefit plans?
  – How will buyer handle accrued but unused benefits (e.g., vacation)?
    ➢ Offer credit for any prior service with seller?
Termination-Related Liabilities

• Contractual severance or similar benefits
  – Individual employment agreements
  – Severance plans
  – CIC agreements

• Statutory termination payments
  – Includes WARN and similar state law (e.g., NY and CA)
  – Can arise in the context of existing liabilities (e.g., seller conducted recent layoffs or plant closings but failed to comply with WARN)
  – Can also arise where buyer needs to reduce target’s workforce
WARN in General

• WARN – Worker Adjustment and Retraining Notification Act
  – 60 days written notice before . . .
  – any “plant closing” or “mass layoff”

• WARN problems:
  – Forget common sense
  – Notices must be written, with specific dates
  – Watch postponed separations/transactions
  – Exceptions are not true exceptions (exceptions, exemptions, and exclusions!!)
  – Many states have separate and different WARN-type notice laws


**WARN Notice Issues**

**Sale Situations**

- Stock deal may not involve employee “terminations” at all
- Technical terminations don’t count if . . .
  - There is a “sale” (all or part of the business), and
  - Seller’s employees are hired by buyer as of the effective date (time) of sale
- Buyer/seller allocation of WARN duties:
  - Statute is incomprehensible
  - Watch 90 days before and after the deal
- Deal-related WARN short list . . .
  - Address buyer/seller allocation of WARN obligations
  - Use representations/warranties to address separations before/after sale
  - Address buyer’s plans about seller employees
  - Err on the side of issuing WARN notices
  - WATCH for “technical terminations” occurring before or after sale effective date
Termination-Related Liability

- Statutory and common law severance for non-US employees:
  - Concept of “at-will” employment is largely nonexistent outside the United States
  - Local laws may require termination payments or lengthy notice periods (e.g., UK, Germany, The Netherlands)
  - These statutory (or otherwise mandated) termination obligations could be material and local counsel should advise regarding scope and implications of such obligations
Contracts

Contractual Upside

• People you need . . .
  – New employment contracts
  – Adoption of seller’s employee contracts
  – Retention or signing/transition bonuses (whether paid by seller or buyer)
  – Consulting agreements (key seller employees, short-term buyer need)
  – Immigration issues, H-1B visa problems, intercompany transfers, etc.
    (especially with multinational companies)

• Protection you need . . .
  – Confidentiality agreements
  – Assignment of inventions
  – Nonsolicitation/hiring restrictions
  – Noncompete agreements
  – Special-need consulting agreements (e.g., cooperation by seller’s employees is essential to ongoing litigation, transitional training)
  – Immigration assistance concerning all visa and work authorization issues
Contracts

Contractual Downside

• Sources of Potential Contract Liability
  – Individual employment contracts
  – Employee handbooks
  – Oral contracts (real or alleged)
  – Collective bargaining agreements, side letters, memos of understanding, etc.
  – Implied and quasi-contracts

• Watch . . .
  – Family businesses
  – Retiree medical insurance or other retiree obligations
  – Culture clash (turnover, litigation, or both)
Restructuring

The Legal Framework

• Selected Labor Statutes:
  – NLRA, including possible successor liability
  – Labor Management Relations Act (LMRA), addressing breaches of labor contracts
    – WATCH: the “federal court injunctions can block deals” problem

• Selected Employment Statutes:
  – Title VII of the Civil Rights Act of 1964 (Title VII)
  – Age Discrimination in Employment Act (ADEA)
  – Americans with Disabilities Act (ADA)
  – Family and Medical Leave Act (FMLA)
  – Fair Labor Standards Act (FLSA)
  – Worker Adjustment & Retraining Notification Act (WARN)
  – Occupational Health & Safety Act (OSHA) and other health/safety/environmental laws
  – Employee Retirement Income Security Act (ERISA)
  – Immigration & Nationality Act (INA) and related statutes
  – State and local employment laws

Unions, Bargaining, etc.

Discrimination/Harassment

Overtime/Wage and Hour

Closing/Layoff Notice

Pensions/Benefits

Breach of Contract, Fraud, etc.
Restructuring

Severance Pay and Waivers/Releases

- Read the severance plan (guidelines etc.)
- Amend the plan if necessary *before* workforce reduction
- Read all handbooks and individual contracts
- Consider an “ERISA-compliant” severance plan
- Watch “technical” sale-related terminations as severance triggers
- Preexisting severance plan – no WARN “credit”
- Releases (OWBPA):
  - 45-day review period required if “group” terminations (21 days otherwise)
  - 7-day revocation period
  - “group” terminations: need to disclose positions/age/eligibility factors list
  - other content requirements (advise employee in writing to consult attorney, etc.)
Restructuring

Who Does the Restructuring?

• Restructuring or RIFs by Seller . . .
  – May be done voluntarily by seller presale to attract buyer(s)
  – May be done voluntarily by seller to improve deal valuation
  – Buyers frequently force seller to do restructure or conduct an RIF because it . . .
    – avoids or reduces potential buyer liability to sellers employees or union(s)
    – reduces risk that buyer will “overpay” for inflated business
    – avoids buyer severance and other RIF costs

• Restructuring or RIFs by Buyer . . .
  – Seller refuses to restructure
  – Buyer does not believe restructuring by seller will be done right
  – Restructuring or RIFs too complicated to do predeal

• Related Options
  – Party not restructuring pays all or some costs (valuation adjustment, etc.)
  – Structure deal so that buyer only takes particular facilities (de facto restructuring)
  – Buyer effectively implements RIF by selective hiring (i.e., seller terminates all employees, and buyer only hires some of seller’s former employees)
Noncompetes

- Legitimate business interests
- Duration
- Geographic scope
- Is payment required for duration of restriction?
- Variations by jurisdiction
- Sale of business vs. employment
- Laws developed on similar themes – generally, but the devil is in the domestic details, e.g., California
10 BIGGEST EMPLOYMENT MISTAKES
Potential Consequences

Deal-Related Employment Mistakes

1. Deal inertia, vendor mayhem, no strategy/objective
2. Deal people and operations people don’t talk (the “how do you run this business” problem and “due diligence wasted” problem)
3. No litigation plan
4. Communications are bad, implementation too slow
5. Union issues: leverage works, shortcuts don’t (and never pay money to union officials)
6. False, misleading, inflated promises
7. Benefits surprises (“The plan says that?”)
8. Smoking gun reduction/RIF problems
9. “WARN what?”
10. “Soft-side” breakdown, culture clash

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Employment Issues Summary

- Business objectives should drive employment strategy
- Use employment counsel (separate from benefits and deal counsel)
- Structure “due diligence” around operating plans (and get “due diligence” to buyer’s operations people)
- Realistically plan for and address union issues
- Coordinate buyer’s and seller’s announcements (communications are especially important to manage employee hiring, retention issues, union issues, and deal-related employment litigation risks)
- Timing considerations
  - 45 days – required for employee review of releases (group terminations)
  - 30 – 60 days or more – seller and/or buyer bargaining with any unions
  - 60 days – WARN notice period (if WARN notices are required)
Lisa Stephanian Burton defends employers in litigation and counsels on labor and employment issues that include wage and hour, discrimination, leaves of absence, and other US state and federal laws and regulations. Lisa also advises employers on business immigration matters. She works frequently with employers in the life sciences, healthcare, technology, retail, and financial services industries. Lisa is the leader of the labor and employment practice in the Boston office.
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