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4 Crucial Employment Law Questions For Dealmakers

By **Braden Campbell**

Law360 (July 30, 2018, 8:45 PM EDT) -- From hidden legal liabilities to high-priced compensation pacts for soon-to-be redundant executives, there's a veritable minefield of employment-related issues capable of stalling otherwise promising mergers and acquisitions. Here, Law360 looks at four questions businesses should ask their attorneys to keep the nuances of employment law from getting in the way of deals.

Am I Buying a Lawsuit?

Because few things are as costly to a company as a lawsuit, potential legal liabilities top the list of employment-related issues businesses need to look out for when they're thinking of making a purchase, Alston & Bird LLP employment partner Grant Alexander told Law360.

"The No. 1 concern is what problems are they buying," said Alexander, who advises buyers and sellers on deals. "Companies need to be aware of what are the potential lawsuits out there."

Some threats, like existing lawsuits, are obvious. But businesses should also be careful of legal liabilities that may lurk under the surface, Alexander said. A demand letter or internal harassment report can easily become a lawsuit, as can complaints to state or federal agencies, he said.

Employers will want to be especially wary of mistakes in classifying workers as exempt from overtime or as independent contractors rather than employees, both of which can lead to costly class actions. These mistakes are among the first Fenwick & West LLP partner Sheeva Ghassemi-Vanni looks for when she's hired to audit a deal.

"If I'm representing a buyer, I'll come in and get a census of [the target company's] workers and then will go through and help [the buyer] assess potential misclassification risk," Ghassemi-Vanni said.

If this turns up zero or only a handful of nonexempt workers, this suggests the target employer may be illegally denying some of its workers overtime, Ghassemi-Vanni said. Similarly, she said a buyer will want its attorney to apply the relevant tests to figure out whether its would-be workers are employees or independent contractors, who don't get perks like overtime and unemployment.

Businesses should also negotiate an indemnification agreement working out who's on the hook should unforeseen complications, like misclassification suits, crop up.

"One way to address a lot of issues is that these M&A deals will routinely include very detailed

language on indemnification,” Alexander said. “Those indemnification clauses and that due diligence process [should be] done by experts who know what language to include.”

What Kind of Deal am I Making?

Mergers generally fit into one of two transaction structures, and the employment considerations can change depending on which form a deal takes, said Brian Pick, a transactional attorney with McDonald Carano.

There are stock sales, in which the acquiring business takes an ownership stake in the company it’s buying and absorbs it. And there are asset sales, in which the acquiring company buys some or all of the assets of the target company.

Because businesses essentially step into their target’s business in a stock sale, these deals require businesses to do due diligence “and understand exactly what potential liabilities are [and] what business operations look like,” Pick said.

“If there are existing workers’ compensation issues and unemployment issues ... you take them as buyers in a stock sale,” Pick said.

By contrast, because they’re buying assets rather than assuming the target, buyers in asset sales only inherit certain liabilities based on their state’s laws. In these deals, the big question facing buyers is how to integrate the target’s workers into their business, Pick said.

“You’re looking at ... how do you get employees out of one business and into the other,” Pick said. “It becomes more of an employee relations issue because you look at how do you terminate all these employees and then rehire all of them.”

If a business decides to bring on only some of the acquired company’s workers, this presents its own set of issues, Ghassemi-Vanni said. Depending on how many workers the business is letting go, the deal can implicate the federal WARN Act, which requires businesses to give workers a certain amount of notice before mass layoffs. It can also trigger a wave of benefits payouts, she said.

“Do you have to pay out any benefits, like vacation ... or is there an opportunity to transfer the vacation to the new company?” Ghassemi-Vanni asked. “Are you going to keep the old plan that people are under, or are you going to have them go onto new plans — vacation, sick time, et cetera?”

Whose Advice am I Taking?

Mergers are incredibly complicated and often involve high stakes, so businesses should think hard about bringing on outside attorneys to shepherd them through deals, attorneys say.

Though businesses may think they see the picture, whether they’re looking at a target or preparing themselves for sale, outside attorneys can point out things they miss, Alexander said.

“I think it’s fairly common for companies not to consult with counsel, to believe they have internal processes in place to identify all of their going concerns and liabilities,” he said. “Internal employees may be aware of 60 percent or 80 percent of the story, but not 100 percent. Outside counsel are aware of everything that’s going on.”

Bringing on outside counsel is especially important where the target operates in one or more

jurisdictions the buyer doesn't, Alexander said. If a California business wants to acquire a company across the border in Oregon, for example, it should bring on a local attorney for advice on local wage laws, he said.

"If you've got the entity being acquired with multiple facilities in multiple states, you've got multiple attorneys to consult with," he said.

What's on the Books?

Employers should also analyze the employment agreements and employee handbooks of the business they're buying to know what they're getting into, attorneys say.

It can pose issues for acquiring companies when their targets have looser intellectual property protections and confidentiality rules than they do, according to Alexander.

"They need to be aware of what could be damaging out there," he said. "If you have employees taking source code or the Coke formula home with them because before they didn't have any limitations, you're setting yourself up for potential exposure."

When one business buys another, it inherits the target's obligations to its workers. These obligations include employment contracts, and any severance provisions they contain may factor into whether the buyer keeps on the target's executives, Ghassemi-Vanni said. Other things to look at include handbook policies covering the target's workers and whether the workers are covered by restrictive covenants such as noncompete agreements, she said.

--Editing by Kelly Duncan and Aaron Pelc.

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