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EU EMPLOYMENT ISSUES IN M&A TRANSACTIONS

By Hanno Timner, Caroline Stakim, and Jens Wollesen

Across industry sectors, there is one thing that all organizations have in common—people. Every organization needs a workforce to steer it in the right direction. This means that when it comes to M&A transactions, regardless of size, there will inevitably be employment law and human resources issues to deal with.

These issues can, and often do, affect not only the process and cost of a transaction, but can also impact how a company is able to manage its business going forward.

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Happily, there is some uniformity across the EU in employment law and practice, largely due to a number of employment-related EU-level Directives, each of which is implemented into the national laws of the 28 Member States. However, although this means that a common approach is taken in relation to particular issues, the details of how those laws apply in practice can vary widely from country to country

Share or asset deal?

At the very outset of a transaction, it is important to understand how it will be structured—whether it is a share or asset sale—as this will affect both the issues that could arise and the process involved.

One key difference between a share sale and an asset sale is that, in a share sale, the employing entity stays the same. All employment costs and liabilities remain with the target company. On the other hand, in an asset or business sale, the application of the EU Acquired Rights Directive (ARD), as implemented in all EU Member States (and often referred to as TUPE), means that the employment of assigned employees transfers to the purchaser automatically by operation of law. The transaction itself results in a change of employer, and the purchaser inherits all employees predominantly working in the business. There is no need for the purchaser to make an offer of employment, or for any offer to be accepted by the transferring employees. Their employment will transfer and the purchaser will essentially step into the seller's shoes in respect of the employment.

Along with the employees, purchaser also inherits all rights and obligations under the existing employment contracts (and under all benefit plans applicable to the transferred employees), even where that is not the intention of the parties. In some countries, such as the UK, this means that the purchaser becomes responsible for any employment costs and liabilities created in the pre-transfer period by seller. For example, if there are unpaid wages or bonus payments, or an act of the seller has resulted in a claim of discrimination, the seller would be responsible for those costs. In other countries, such as Germany, the previous employer is jointly and severally liable with the new employer for duties that arose prior to the date of transfer and are due before

UK: Employment Legislation Update – Fall 2015

By Caroline Stakim, MoFo London

This month we highlight the key legislative changes that employers in the UK should be aware have taken place.

From 1 October 2015, national minimum wage hourly rates increased to:

- £6.70 (from £6.50) for those aged 21 and over
- £5.30 (from £5.13) for those aged 18 to 20
- £3.87 (from £3.79) for those aged 16-17
- £3.30 (from £2.73) for apprentices aged under 19 or who are in their first year of apprenticeship.

Readers should note that from April 2016, the UK government intends to introduce a higher "national living wage" for workers aged 25 and over, starting at £7.20 per hour (i.e. 50p per hour more than the national minimum wage).

Also from 1 October 2015, the employment tribunals' power to make recommendations (such as a recommendation that the employer should provide equal opportunity training to managers) in successful discrimination cases was limited to recommendations that benefit the individual claimant (rather than recommendations that benefit the wider workforce). This means that recommendations for the benefit of the wider workforce can now only be made where the claimant remains in employment. In addition, the right of Sikh employees to wear a turban instead of a safety helmet was extended to almost all places of work (with certain exceptions relating to some military and emergency service roles).

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the end of one year after that date. For this reason, it is essential that the sale agreement appropriately allocates costs and liabilities between the parties.

Importance of due diligence (and data protection considerations)

In either case, due diligence exercises are important. The purchaser should fully understand what costs and liabilities it is inheriting: How many employees does the target business or company have and which ones are key to its success? What salaries and benefits are employees entitled to? To what extent have vacation or (often entirely unfunded) pension entitlements accrued? Are there existing trade unions or works councils? Is there any ongoing or threatened employment dispute or litigation, and will liability for these need to be assumed by the purchaser, even if such claims arose before the transaction?

The diligence process can also help the purchaser assess what, if any, steps it needs to take post-completion. In a share sale, any dismissals or changes to terms and conditions are generally subject to the same employment laws that would apply if taken outside the confines of an M&A transaction. In an asset deal, on the other hand, a significant difference is that the application of the ARD/local TUPE also places further restrictions on what an employer can and cannot do with its workforce, for example, in relation to the terms and conditions of employment or proposed dismissals.

This might be familiar territory to non-EU parties. While conducting due diligence in the EU, however, one important difference is the application of the EU Data Protection Directive which (amongst other things) restricts the processing and disclosure of so-called personal data (i.e., information relating to an identified or identifiable individual). Information concerning the employees who will transfer to the purchaser will inevitably constitute such personal data. The seller and the purchaser therefore need to safeguard such data and ensure that they take appropriate steps to ensure compliance during due diligence, for example, by disclosing or relying on only aggregate or anonymized employee data. The recent decision of the European Court of Justice

The Modern Slavery Act 2015 introduced a new obligation for commercial organizations with a global turnover of more than £36 million who carry out any part of their business in the UK. Those organizations will be required to publish an annual statement, accessible on their website, that sets out the steps taken to ensure that no slavery or human trafficking is taking place in the business or supply chains (or, that no steps have been taken, if that is the case). It is expected that the first statements will be required to be published in respect of financial years ending on or after 31 March 2016 and that affected organizations will have six months from the end of their financial year to comply. Statutory guidance on what should be included in the annual statement is also expected to be published shortly.

For queries relating to any of the above, or for advice on any other UK employment or HR issues, please contact Caroline Stakim, associate in London, at +44 (0)20 7920 4055 or cstakim@mofo.com.

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(EJC) denying protection by means of the existing safe-harbor arrangement among the EU and the United States underpins the importance of the observations of such provisions.

Obligations to inform (and potentially consult) and the employees' right to object to transfer

The ARD also triggers substantial information obligations which need to be taken into account when contemplating the structure and timing of a transaction. The seller and the purchaser are required to comprehensively inform each individual employee (or in some countries, the employee representatives) of the planned transaction and the effects it will have on the employment relationship. This includes information regarding the date of the transfer; the reasons for it; the legal, social and economic consequences; and the details of any measures that the purchaser contemplates taking in connection with or after the transfer. In a number of EU countries, including Germany, only the provision of comprehensive and correct information to the employees in writing will trigger the one-month period during which employees are entitled to object to being transferred to the buyer of the business. Consequently, the parties will need to take this information obligation seriously and make sure that they are able to prove when the information notices were served to the employees.

Both parties to an asset transaction and corresponding business transfer also need to consider the consequences of employees objecting to the transfer of their employment to the purchaser. While in some EU countries (such as the UK) an objection can lead to the automatic termination of the employment relationship (with the effect that employees hardly ever make use of their right to object), other local laws (such as German law) stipulate that objecting employees must remain employed by the seller of the business, who might in turn need to eventually dismiss these employees, taking local dismissal protection regulations into consideration.

As well as the obligation to provide information about the transfer to employees or their representatives, consultation obligations may be triggered. The ARD provides that employee representatives should be consulted where, in relation to a transfer, measures affecting employees are envisaged. In the UK, both the seller and the purchaser must consult with their own affected employees (and it should be remembered that this group could include employees who are not transferring but who are otherwise impacted by the transfer). This consultation must take place "in good time" and with a view to reaching agreement. In practice, this obliges the employer to enter into good faith negotiations long enough before the transfer to allow a meaningful consultation to take place. The period of time that will be required to do so will depend heavily on the number, and nature, of the measures proposed.

Comprehensive co-determination rights of works councils and timing

Asset transactions regularly lead to additional (non-ARD) consultation obligations vis-à-vis local works councils. In Germany, for example, works council rights to information and co-determination are triggered in cases of a so-called "operational change." This term encompasses all measures that affect the operational organization and identity, from a shutdown to relocation, change of business objectives or fundamental changes to production methods.

Consultation obligations can, depending on the countries involved and whether the transaction also has an effect on the structure of the business operations, extend from simple information obligations to the seller's duty to follow quite detailed consultation processes. Information and consultation requirements might even need to be initiated and completed prior to the signing of an asset deal so the works council is still able to provide its expertise and evaluate the "if", "when" and "how" of the anticipated change. The ultimate goal of this process is to avoid unnecessary disadvantages for employees. The conciliation procedure itself is mandatory and cannot be cut short. However, the works council cannot compel the employer to enter into a conciliation agreement.

While local EU laws do not normally enable the works councils to permanently hinder the transaction, works councils are able to delay the consultation

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processes (and, consequently, the transaction itself), considerably. Negotiations can take as long as six months (sometimes even longer), and the parties are well advised to take this factor into account when working on the transaction timeline.

Failure to comply with the required consultation processes can have severe consequences; some countries, such as Germany, allow works councils to obtain injunctive relief from the local labor court prohibiting the transaction from being carried out until the seller has complied with of its all consultation obligations. Furthermore, employees may be entitled to severance pay and the employer may incur penalties of up to €10,000. Other local laws, such as those in France and Finland, even impose criminal liability if consultation obligations vis-à-vis the works councils are disregarded.

Implementing post-close restructuring and redundancies

Further consultation obligations may also be triggered in respect of post-completion actions that the purchaser wants to take. Where the purchaser inherits employees as part of a transaction, it is quite common for it to harmonise or streamline its workforce post-transfer, and this can result in large scale redundancies. The EU Collective Redundancies Directive (CRD) may apply where such collective dismissals are being contemplated. The employer at this point is obligated to collectively consult with workers' representatives, as well as inform national authorities of their plans.

National laws of each Member State will define what a collective redundancy is. For example, in the UK, a collective redundancy is where 20 or more dismissals are contemplated within a 90 day period at one establishment. Where this is the case, the obligation to collectively consult is triggered. This means that the employer must consult with employee representatives on their proposals and, in particular, on ways in which the dismissals can be avoided or the impact of them reduced. Minimum periods of consultation apply. Where between 20 and 99 dismissals are contemplated, collective consultation must last for at least 30 days and, where 100 or more dismissals are contemplated, that period increases to 45 days. The collective consultation must end before notice of termination is given.

In the context of an M&A transaction, prior to 31 January 2014, collective consultation could not begin prior to the seller's employees transferring to the purchaser. This was particularly frustrating for purchasers who knew ahead of a deal closing that collective redundancies would be necessary. However, changes to the UK rules mean that the purchaser can now, with the permission of the seller, begin collective redundancy consultation pre-transfer, thereby saving costs and time with integration exercises. The seller may provide information or assistance to the buyer, but is not obligated to do so.

Labor authority and government approvals

In certain circumstances, it may be necessary to obtain the approval of the local labor authority or government regarding actions taken in relation to employees. In France, where part of a business is being sold, the labor authority must approve the transfer of any employee representative's employment. Failure to do so can result in the transfer being deemed to be void as well as a claim for compensation or reinstatement from the employee concerned.

In other countries, labor and government bodies don't need to approve the action but do need to be informed of certain proposals. In the UK, an employer who contemplates making collective dismissals must notify the UK Department for Business, Innovation and Skills (BIS) of that fact. This notification must be in writing, and must be provided either 30 or 45 days (depending on the number of contemplated dismissals) ahead of any termination notice being issued. Failure to comply with this notification is a criminal offence punishable by an unlimited fine. In Austria, the Federal Employment Office (Arbeitsmarktservice) must also be informed of any collective dismissals in writing at least 30 days before notice of termination is given. Failure to do so there will make the termination of employment null and void.

Conclusion

While transactions in EU countries may be shaped by national labor law, harmonization across the region has gone a long way. Companies should structure deals with close attention to the EU Acquired Rights Directive (ARD), which requires the purchaser in an asset deal to inherit all employees predominantly working in the business. Another significant topic to be considered early on in a transaction are works council's rights and labor authority and government approvals that may be necessary. In some countries, works councils are able to delay and even stop the transaction, if information and co-determination rights are not respected.

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