Mergers & Acquisitions: The Importance of Thoughtful and Timely Communications

By: William B. Payne

While any change in employers is stressful, sale of a division or subsidiary probably creates more anxiety than the sale of the entirety of a company. By selling a division an employer has broken its implicit bond with its employees. Usually it is underperforming businesses that are sold, implying that workers have genuine reason to be concerned about continued employment. Thoughtful action by the buyer is required to win over employees at all levels of the business being sold.

The Sale Process

During the sale process, sellers typically do what they can to minimize the concern of employees, often by shielding them from what is going on. Buyers are denied contact with employees, and even walk-around due diligence is minimized to avoid speculation.

Secretly, however, is difficult to maintain. Buyers inevitably break confidentiality, and the spider-web of talk makes it back to employees. Targets themselves are never careful enough; Internet chatrooms buzz with the latest speculation (often true) and internal rumors grow rife. The seeds of employee unrest may thus be planted before negotiations even begin. Sellers can never be too careful in the steps they take to avoid premature concern.

Legal Background

Sellers that are public corporations are required by stock exchange rules and securities laws to disclose “material developments.” Negotiations toward sale of a significant division sometimes fall under that heading. Once a definitive agreement is signed, it is usually followed by a
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press release announcing the sale. In certain circumstances, the Securities and Exchange Commission may require that various communications, even to internal employees, be filed with it and become publicly available under Regulation M-A.

Buyers and sellers, even those that are privately held, usually feel a need to let their employees know what is going on. It is not possible to approach this unilaterally, because disclosure to employees usually becomes public knowledge.

The Gap Between Signing and Closing

Various third-party events typically need to occur prior to the actual purchase of a company, just as when purchasing a house there is a lapse between signing a purchase agreement and closing. However, the reasons are different. Most home buyers need to arrange financing and sell their existing houses. When a company is changing hands, there are usually various consents and approvals that must be obtained; e.g., governmental approvals.

In all but the smallest transactions, governmental approvals will include antitrust clearances. In regulated industries, such as banking and utilities, various other approvals may be required at federal and state levels. Based on the way the contract is written, it may be necessary to seek consents and waivers under other contracts to which the target is a party, if they are material.

Therefore, while on occasion a deal is signed and closed simultaneously, there is often a gap as these consents and approvals are obtained. While antitrust clearances may be received in less than a month, other regulatory approvals can take years.

Meanwhile, the required public announcement of the deal has undoubtedly caused grave concern for all constituencies — employees, customers, vendors, and the community. Because the closing has not occurred, the buyer cannot directly assume management of the target’s business. In fact, until antitrust clearances are obtained, that would be a violation of law. While the parties always promise to cooperate, it is not the same as managing the process (and some forms of cooperation may even constitute an illegal combination of the businesses). Furthermore, most companies do not want to surrender management to a third party.

Successful buyers (and targets that want a successful integration) go through extensive planning in order to avoid adverse perceptions during this period. This involves capturing the hearts and minds of all constituencies. Although it is a matter of common sense, how well this is done varies considerably. The steps to be taken also vary tremendously, depending upon the industry, corporate cultures, size and other factors.

Initial Communications to Employees

To belabor the obvious, all changes beget uncertainty and anxiety. In the context of an acquisition, the result is at best a distracted workforce that can damage the business being purchased before the buyer has closed the deal. At worst, the company may experience a wholesale defection of employees, particularly the most talented. Whether from general malaise or defections, there may be a loss of customers, a downturn in productivity and a hiatus in activities essential to the future of the business.

If a public announcement is inevitable, most buyers and sellers will want to coordinate an announcement to employees to avoid surprises and to provide essential details that may not be included in the public announcement. Too often this announcement is done poorly for two principal reasons: ineffective communication and failure to plan.

Ineffective Communication. While CEOs, HR and PR professionals — even lawyers — intuitively understand the need to communicate with employees of the business being sold, the quality of these communications varies significantly. Perhaps the worst scenario is the buyer that leaves it to the seller to simply issue an announcement to its employees. Employees will generally perceive that they have just been sold down the river and that the new employer is making no promises.

Vague assurances delivered from a distance in bureaucratese do little to assuage employee concerns. Most CEOs know that being up close and personal is the most effective form of communication. The best solution for welcoming new employees, bringing them into the fold and sharing a vision is the multi-location CEO tour. But there must also, of course, be some substance to communicate.

There is never a guarantee that any communication program, even the best designed, will succeed. Employees may be cynical about management promises, particularly from buyers who have a slash-and-burn reputation. Third-party responses, such as criticism of the deal from the street, may also affect employee confidence and acceptance. Regulatory delays imply uncertainty that is difficult for management to counteract.

Failure to Plan. Good news should be communicated as soon as possible. If there will be no layoffs, what could be better news to employees? If the new employer offers superior benefits, why not communicate that to affected employees?

Too often, however, rather than doing integration planning as part of due diligence, buyers begin it after the deal is signed (or worse, after the deal is closed). In that case, it is often impossible to provide any news, because the buyer has preserved all of its options — even in situations where it is known that there will be no adverse changes for

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employees (such as when the buyer always continues to operate its acquisitions as independent businesses). The failure to say anything will encourage the worst inferences.

Generally, decision-making is not enhanced by the passing of time, and the result of postponed decisions can be significant attrition in the workforce. CEOs should be as decisive on the front end of the integration process as they are on the buy decision.

**Special Retention Devices**

“Stay bonuses” and similar devices are sometimes used to help ensure that an employee base will be retained upon the sale of a business. They may have both bonus and retention components, with varying time periods required to vest the retention component. These are occasionally seller-initiated incentives, such as when a small group of employees are involved in the sale process and are necessary to its successful culmination. Sellers attempt to entice the employee to continue working through conclusion of the sale and (to assure the buyer of a smooth transition) for a period of time after the closing. Buyers often seek the comfort such devices provide in industries where employee migration is commonplace, such as with broker-dealers.

To work, these incentives need to be part of the initial announcement to employees, even when details are to come later. While typically not individual agreements with employees, negotiated arrangements with key employees may be an essential complement.

**Putting Together the Communications Program**

While the initial communication is crucial, periodic updates while the deal remains pending are also essential. Such communications should deal with details and developments. Often employees do not understand why a transaction is not announced and closed simultaneously, and the often vague public announcement about “regulatory approvals” may not be understood by the rank-and-file. Delays in closing, in particular, need to be dealt with.

All of the following elements may be important in an effective communication program:

- As much detail as possible (but do not overpromise)
- As much personal involvement as possible
- Clear statements about the vision of the combined organization
- Timely and regular follow-up

**Barriers to Overcome**

HR professionals will need to overcome internal and external barriers. The seller will insist on control over communications to its employees. While the seller must in fact contemplate the possibility that the deal won’t close, its interest is not nearly as great as that of the buyer. Often the internal processes are more difficult for the buyer — from the distracted CEO to the just-get-it-done communications professional.

Effective early communication has the best chance of winning the hearts and minds of a new group of employees. Once rumor and innuendo have tarnished the image of the buyer, it will be significantly more difficult to garner favor with the new employees. Communicating early and often is also the best way to avoid disruptions in the business, whether through the loss of employees and customers or general employee angst.

There is no general formula for effective communication in the M&A context. What is important is active and thoughtful leadership that recognizes the importance of timely and meaningful communication to the workforce.

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Composition of the Workforce

The first step is understanding what is there. Basic questions about the number and cost of hourly and salaried employees should be answered before a deal is struck. If the business is overstaffed, the buyer can avoid the complications of a reduction in force by simply taking on less than all of the existing workforce. Conversely, a division that is understaffed may require the buyer to plan for more overtime and recruiting costs in the short run.

A prudent buyer also will confirm that the workforce will be adequate to run the business immediately after the closing. There may be, for example, key personnel with institutional knowledge who are critical to running the business. Does that IS technician — the only one who understands the systems — plan on taking your job offer? In other cases, the division or subsidiary being purchased may rely on the parent company to provide corporate functions such as accounting, payroll, legal and tax. Some buyers will be in a position to provide these services from day one. For other buyers, it will be critical to make alternative arrangements, possibly by negotiating a transitional services agreement.

Understanding Economic and Legal Relationships with Employees

When purchasing a division or subsidiary, the buyer often has an opportunity for a fresh start with the employees. This does not mean, however, that a buyer can afford to ignore the old relationships. A buyer risks antagonizing employees if the new economic relationship is dramatically different than the old. In addition, some of the old legal relationships may raise issues for the business in its new form.

Buyers should understand the economic as well as cultural relationship in the broadest sense. In addition to salary and wages, what benefits and perks do employees receive? Do they enjoy generous health and retirement plans? Is the vacation policy liberal? Are employees used to getting a free lunch at the company cafeteria? Before making the buy decision, a buyer should consider whether it is prepared to match the existing economic package, and the consequences if it is not.

Most employees do not sign an employment agreement. To understand the legal relationship they have with their employer, a buyer needs to examine other sources such as the standard offer letter, the employment handbook and other employment policies. Unearthing the policies often is the first step since they may be contained in unexpected places such as memos or the company intranet site. How these materials are assessed depends in large part on the structure of the proposed transaction. If a buyer is purchasing the stock of a subsidiary, then the legal entity and its employment policies will stay intact until they are specifically amended. In such a case, the focus should be on which changes will need to be implemented immediately after the closing.

Under normal circumstances, the targets are key employees who will be party to an employment contract. Like agreements related to the target’s other key assets, these should be carefully reviewed and thoroughly understood by the buyer. In contrast to most of the target’s other agreements, however, rarely will it suffice to simply have the employment agreement assigned to the buyer. More likely, contracts with key employees will be terminated in favor of new agreements.

HR Issues in Buying a Division or Subsidiary

Buyers expect that the full capabilities of the target’s workforce will be available to it after closing. Preexisting relationships can dramatically interfere with this expectation. However, the common pitfalls can usually be avoided so long as they are identified and addressed before an agreement is reached.

Of particular concern to a careful buyer are non-competition agreements. Potential problems with these agreements can take several forms. The most obvious is where a buyer of a division or subsidiary does not negotiate a termination of non-competition provisions that run in favor of the selling parent company. Another problem can occur where the contract containing the non-competition provision is terminated, but the parties fail to address the fact that the non-competition provision, by its terms, survives termination of the contract for some period of time.

Restrictions on the use of confidential information can present similar problems, but because these provisions are not as high profile as non-competes, they are more likely to get overlooked. The scope of what constitutes confidential information is often surprisingly broad and can cover seemingly routine employee functions. A related concern stems from the increasing popularity of invention assignment agreements. Under these agreements, all intellectual property conceived by an employee becomes the property of the employer. A buyer is unlikely to miss the fact that an important patent or trademark belongs to the parent company of the business being purchased; but subtler forms of intellectual property such as process and know-how can easily be overlooked.

As part of due diligence, the buyer should take the time to review the target’s personnel and human resources records, as well as its employment litigation and investigation history, looking for evidence of ongoing

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Mergers and Acquisitions: Benefits Issues

By: Michael Voves

Prior to the purchase of a division or subsidiary (the “target”), a buyer must determine whether it will continue to maintain separate benefit structures or integrate the target’s benefit plans with its own. While for most strategic buyers integration is more likely, there are some circumstances where separate plans may be preferable, such as when the target’s line of business differs substantially from the buyer’s. In either scenario, HR has the task of ensuring a seamless transition of employee benefits. This article highlights some of the employee benefit issues HR will face.

No Integration

In some cases, the buyer will continue to maintain separate compensation and benefit plans for the target after the acquisition. If the target is a stock acquisition of a subsidiary that maintains its own plans (as opposed to participating in those of the selling parent), HR’s principal task is to work with insurance carriers and administrative service providers in advance of closing to avoid a contract breach due to a change in control or assumption of the plans. This is particularly important in a forward triangular merger, where the surviving corporation is a newly-formed subsidiary set up solely for the purpose of acquiring the target. The surviving corporation assumes all liabilities, third-party contracts, etc., with respect to the target’s benefit plans. Insurance contracts that require consent to assignment may become void if the carrier is not notified in advance of the acquisition. If it fails to obtain consent, an employer that thinks it has an insured health plan or ample stop-loss insurance coverage may unexpectedly find that it is now a self-insurer of all claims for health benefits. Insurance carriers and service providers are by and large willing to give the necessary consent, provided they are notified in advance of closing.

The consent-to-assignment issue also surfaces in an asset acquisition where the buyer assumes contracts related to seller’s benefit plans. An insurance carrier or other service provider will want to know what the make-up of the acquired division will be post-acquisition before it will agree to an assignment. If the buyer hires only a select group of division employees that fits within its business strategy, an insurance carrier may want to renegotiate the terms of an existing agreement. HR needs to work with carriers and administrative service providers in advance of closing to avoid breaks in coverage. Of course, it is important to note that in an asset acquisition, the buyer is under no obligation to assume any liabilities or contracts related to the seller’s benefit plans. However, the alternative is to establish new plans and enter into new contracts with the same or different service providers, which typically requires more effort than a single assumption of plans.

If the target participates in the seller’s plan, and the buyer wants the target to stay in those plans, the acquisition becomes exceedingly complex. Most sellers will be reluctant to allow the target to participate in its plans after the closing since participation in a multiple employer welfare or pension plan can have undesirable side effects (e.g., multiple employer welfare plans are subject to potentially cumbersome state insurance laws). Therefore, sellers typically require that the buyer establish new plans for the target. These often simply mirror what was provided by the seller.

Maintaining plans separately will impose obligations on HR on an ongoing basis. HR will be required to prepare separate annual returns, plan amendments, summary plan descriptions, benefit statements and other communication materials for the target’s plans. With respect to pension and retirement plans, the buyer’s and target’s plan assets will be held in two separate trusts, each perhaps with its own trustee, custodian and recordkeeper and each requiring a separate annual plan audit.

Qualified pension and retirement plans (e.g., 401(k) plans, ESOPs, profit sharing plans and defined benefit pension plans) are required to provide broad-based coverage to employees and are therefore also subject to complicated discrimination testing requirements imposed by federal tax laws. HR will need to conduct these tests, which compare the participation percentages of highly paid and non-highly paid employees, for both the buyer’s and target’s qualified pension and retirement plans. When testing, HR must look at all employees in the buyer’s entire controlled group of corporations (control being determined by 80% ownership by value or voting rights). Therefore, the acquisition of a new subsidiary or division with its own qualified plan creates testing issues for all qualified plans in the buyer’s controlled group.

In certain instances, the buyer may be able to qualify a subsidiary or division as a separate line of business and thereby limit the scope of testing. Moreover, special grace periods apply before newly acquired subsidiaries or divisions must be aggregated with existing affiliates for purposes of testing. HR needs to remain aware of these rules, as well as all available testing alternatives, and monitor each plan’s discrimination testing carefully.

Integration

More often, the target’s employees will be moved into the buyer’s benefit plans. Integration has the beneficial effect of leaving HR with a single set of retirement and welfare plans to administer — a single audit, single annual return, single benefit statements, single summary plan description, concludes on page 6
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a single trust, a single plan amendment the next time Congress changes the law, etc. Given its administrative advantages, as well as the potential for maximizing economies of scale, integration is most desirable when this arrangement fits within the buyer’s overall business strategy. The disadvantage, from an HR perspective, is that the initial implementation requires more than a simple assumption of existing benefit arrangements.

If the target does in fact maintain its own plans, the buyer must decide how and when it should terminate those existing arrangements. Disposing of the target’s health and welfare plans may be relatively simple. Because most insurance contracts expire annually, buyers often let all existing health, life or disability plans run until the contracts expire. The same holds true for certain flexible spending reimbursement accounts, which hold pre-tax participant contributions aside to cover anticipated medical or dependent care costs incurred during the year. It is generally easier to maintain the existing accounts through the end of the year rather than transfer credits to the buyer’s plan. The delay gives HR extra time to prepare for integration and may also allow the target’s employees to be enrolled simultaneously with the buyer’s annual enrollment date.

If the target does not maintain its own plans, but rather participates in those of the selling parent, the buyer may be compelled to offer immediate enrollment in its plans to avoid a break in coverage. This scenario is most likely to arise where the target is a division of the seller, but is certainly possible where the target is a subsidiary as well. A concerned seller may ask the buyer to waive eligibility waiting periods and credit the target’s employees with deductibles incurred during the year of the acquisition. The buyer may also be asked to credit employees with their prior service for purposes of eligibility and vesting under the buyer’s retirement plans. How these issues are handled is a matter of negotiation, but they are items that HR will need to track going forward. HR for both the buyer and the seller also will have to work together to transition any flexible spending reimbursement accounts belonging to the target’s employees. If the target is a subsidiary, the buyer will require that the seller amend its plans prior to closing to remove the target as a participating employer in the seller’s benefit plans (to avoid the multiple employer plan issue discussed previously).

The transition of retirement plans warrants additional consideration. If the target maintains its own retirement plan, the buyer may choose to merge it into its own plan. In that case, ERISA and federal tax law require that the buyer preserve certain accrued or other protected benefits (such as vesting schedules or distribution rights) for the target’s employees under the buyer’s plan. This may require HR to maintain special accounts for the target’s employees, leaving the buyer in somewhat the same administrative position as if it had continued with two separate plans.

In some cases a merger may not be feasible, such as when the buyer maintains a different type of plan. In that case, the buyer may freeze the target’s retirement plan (i.e., stopping contributions without closing the plan or distributing assets). Freezing requires that employees become fully vested in their accrued benefits. In that scenario, the target’s employees are allowed to enroll in the buyer’s plan and accrue future benefits, while HR continues to administer their previously accrued benefits in the frozen plan. Alternatively, to avoid this burden, the buyer may simply terminate the target’s plan and distribute assets to employees, who may then be permitted to roll their distribution into the buyer’s plan or an IRA.

Unfortunately, in some cases it may not be possible to force employees to take a distribution (due to complicated federal tax laws). It is possible, for example, that some employees would not take a distribution following termination and HR would be left with some small portion of the plan to administer or merge into the buyer’s plan.

If the target does not maintain its own retirement plan but participates in one or more of the seller’s plans, an agreement may be reached to spin off a portion of the seller’s plan and transfer the respective assets and liabilities to the buyer. The buyer would then merge those assets and liabilities into its existing plan (or set up a frozen plan specifically to hold the accrued benefits, as discussed above). If the transferred liabilities are from a defined-benefit pension plan, the buyer needs to think very carefully about how the purchase agreement will define that liability, which in turn affects the amount of assets the seller must transfer to the buyer to cover the liability. There are several actuarial methods used to measure accrued liability in a defined-benefit pension plan. A buyer-friendly method might measure the liability by looking at projected benefits as if the plan were maintained indefinitely; a seller-friendly method might measure the accrued liability as if the plan were terminated at the time of closing. Once a method is chosen, HR will need to work closely with the buyer’s and seller’s actuaries to ensure that an accurate valuation of the liabilities is obtained, and that a plan is in place to accept the resulting transfer of assets.

Conclusion

The employee benefits issues which HR will face in an acquisition of a subsidiary or division depend principally on three factors: whether the transaction is an asset or stock acquisition; whether the target maintains its own plans or participates in the selling parent’s plans; and whether the target will continue to maintain its own plans or participate in the buyer’s plans after the acquisition. The preceding discussion illustrates the complexity of HR’s role in transitioning employee benefits.

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**Mergers and Acquisitions: WARN and the NLRA**

By: Erik Nelson

Many employment-related issues demand attention during the course of planning and implementing an M&A transaction, including several statutes that can complicate the transaction. Fortunately, the effects of these statutes can be easily managed with proper planning and foresight.

**Worker Adjustment and Retraining Notification Act**

A goal of many M&A transactions is to create synergies by combining operations and eliminating duplicated effort. Often, such restructuring results in personnel layoffs or plant closings, implicating the Worker Adjustment and Retraining Notification Act (WARN), which Congress enacted in the mid-1980s to require employers to provide advance warning of certain mass layoffs and plant closings. WARN requires any employer with more than 100 employees (excluding part-time employees — anyone employed, on average, for less than 20 hours per week or “for fewer than 6 of 12 months preceding the date on which notice is required”) to provide written notice to affected employees or their union representatives and to government officials at least 60 days prior to any “plant closing” or “mass layoff.” Only pursuant to a very few, narrow exceptions, such as a natural disaster or other unforeseen business circumstance, can employers avoid this obligation.

A plant closing is any “permanent or temporary shutdown of a single site of employment, or one or more facilities or operating units within a single site of employment,” which results in an employment loss during any 30-day period of 50 or more full-time employees. A mass layoff is defined as any reduction in force at a single work site which results in an employment loss, during any 30-day period, for: (1) at least 33% of the workforce and at least 50 full-time employees, or (2) at least 500 employees at the site. To constitute an “employment loss,” a layoff must exceed six months. If the layoff does last longer than six months and triggers WARN, then notice will have been due 60 days before the layoff originally began. This can result in significant after-the-fact liability.

Many people find the mass layoff provision confusing because it is not clear whether the threshold is 33% of the employees or 50 employees. In fact, the threshold is both — at least 33% of the workforce at the site must be laid off, and the actual number must be 50 or more. The simple way to remember the WARN thresholds is to think of 50 as the magic number. If less than 50 employees lose their jobs at a single site of employment, it is not a mass layoff or plant closing within the meaning of WARN.

If WARN notice is required, the employer must give it to the union representatives of affected employees or, if there is no union, to each affected employee. Notice also must be given to the applicable State Dislocated Worker Unit and to “the chief elected official of the unit of local government within which such closing or layoff is to occur.” The U.S. Department of Labor currently maintains a list of all State Dislocated Worker Units on its website, (http://www.doleta.gov/layoff/e_sdwuc.cfm).

Any plant closing or mass layoff occurring as part of or contemporaneously with a business sale must be preceded by WARN notice. The seller is responsible for providing such notice up to and including the effective date of the sale. Accordingly, if a seller is aware that a threshold number of employees will be terminated at the time of the sale, it must provide timely, appropriate WARN notice. After the effective date of the sale, the purchaser is responsible for providing required notice. Further, any employee of the seller is considered an employee of the purchaser immediately after the effective date of the sale.

Thus, any terminations or layoffs contemplated as part of an M&A transaction should be discussed carefully during negotiations. The parties must determine whether the WARN notice requirements will be triggered by the transaction and, if so, when the notice will be given and by whom. Depending on the timing of the planned workforce reduction, notice may be required well in advance of the closing date. Further, if it intends not to hire some or all of the seller’s employees, the buyer should ensure that the seller terminates the employees (with appropriate notice, if required) prior to the effective date of the sale. Given the statutory presumption that the seller’s employees automatically become the buyer’s employees, it behooves the buyer to communicate its intentions to the seller and to the seller’s employees in a timely way to avoid any unpleasant surprises.

Many states have their own WARN-like laws that may differ in some respects. Minnesota, for example, merely requires an employer giving notice under WARN to also report the names, addresses and occupations of the employees who will be or have been terminated to the Commissioner of Economic Security. Wisconsin, however, imposes WARN-like notification requirements but with reduced thresholds — 25 affected employees rather than 50.

**Successorship Under the National Labor Relations Act (NLRA)**

For many years courts, arbitrators and the National Labor Relations Board (the “Board”) have struggled to define the respective rights and obligations of buyers and sellers of businesses that have unionized workers. In many circumstances, the buyer must take on the obligations of the seller with respect to an organized workforce; sellers nearly always must bargain with union representatives regarding the effects of a proposed deal. Consequently,

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in any transaction involving unionized employees, it is imperative that buyers and sellers understand their rights and obligations and act accordingly.

Upon the request of a union representative, a seller must bargain regarding the effects of any decision to terminate part or all of its operations. As a part of this obligation, the seller may be required to provide the union with information relevant to the sale. In addition, the union has a right to seek benefits for its members, including favorable terms in the M&A agreement and severance benefits in the event of terminations. Indeed, many collective agreements already provide severance benefits in the event of a sale or merger. Buyers always should review such agreements during due diligence.

While a seller always must bargain with its unions, a buyer may not be obligated to recognize the existing union and/or assume the obligations of existing collective agreements. Buyers must assume some or all of the union-related obligations of the seller in the following three situations:

- Where the buyer and seller are "alter egos"
- Where the transaction is a merger or stock purchase
- Where the buyer in an asset purchase is a "successor employer"

**Alter Ego Employers**

When the "old" and the "new" employer are, in reality, the same or substantially identical, the two generally will be considered "alter egos," and no change in the employment relationship will be deemed to have occurred. In determining whether entities are alter egos, the Board considers (1) whether common ownership exists, and (2) whether the same or substantially identical management, business purpose, operations, equipment, customers and/or supervision will be in place after the transaction. Generally, common ownership alone will not result in alter ego status. If substantially identical management or other elements of the second factor are found, however, the existence or non-existence of common ownership may be irrelevant. Examples of an alter ego relationship include ostensibly separate businesses that, in fact, are operated as one, and new employers that are merely the old employer, or its agents, in another guise. In such a case, all existing union-related obligations are imposed upon the new employer. The obligation to recognize and bargain with the union and abide by the terms of the collective agreement continues as though no change occurred.

**Mergers and Stock Purchase Transactions**

Union-related obligations also typically survive the transfer of ownership following a merger or stock purchase, with the surviving firm standing in the place of the original employer. Where there is a sale or transfer of stock and substantial continuity of operations and employment, there is no effective change in employers. Similarly, the surviving corporation in a merger generally is liable for the obligations of the disappearing firm. Consequently, it will be obligated to recognize and bargain with the union and abide by the terms of the collective agreement as though no change occurred.

**Asset Purchase Transactions and Successor Employers**

Asset sales generally produce greater change than alter ego relationships, mergers and stock purchases. Thus, the notion of successorship becomes an issue. When a change in ownership occurs as a result of an asset sale, the buyer will assume some of the seller's union-related obligations if the buyer becomes a "successor employer." Generally, a successor employer will not be required to assume any existing collective agreement but will, in most circumstances, have a duty to recognize and bargain with the union.

Successorship is based upon the totality of the circumstances surrounding the ownership change, including continuity in the work force and the enterprise. The Supreme Court has stated that if "the new employer makes a conscious decision to maintain generally the same business and to hire a majority of its employees from the predecessor, then the bargaining obligation [remains]." Fall River Dyeing & Finishing Corp. v. N.L.R.B., 482 U.S. 27, 46 n. 12 (1987). The Board generally will not find successorship, based upon continuity in the work force, unless the new employer has a "substantial and representative complement" of employees, the majority of whom were hired from the predecessor. See, e.g., Fall River, 482 U.S. at 47-52. A new employer will be deemed to have hired a substantial and representative complement of employees based on the following factors:

- Whether the job classifications designated for the operation are substantially filled
- Whether the operation is at substantially normal production
- The size of the complement of employees on the date of normal production
- The length of time before a substantially larger work force may be required
- The likelihood of an expansion to a significantly larger work force.

A union demand for bargaining made prior to establishment of a "substantial and representative complement" continues in effect until the buyer reaches that status. While a buyer has no duty to hire the seller's employees (unless otherwise agreed), it cannot refuse to hire the seller's employees based upon their union status.

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In determining whether there is substantial continuity in the business enterprise, the following factors are considered:

- Is the work force the same or substantially the same?
- Is there substantial continuity of the business operation?
- Is the work being performed in the same plant?
- Do the jobs exist under similar working conditions?
- Does the new employer utilize the same supervisors, machinery, equipment and methods of production?
- Does the new employer manufacture the same products or offer the same services?

A new employer generally may set the initial terms and conditions of employment for all of its new workers, including those that are unionized. To protect this right, the new employer must make it clear that it will offer employment only on its own terms and conditions. After establishing these initial terms, and upon becoming a successor employer, the new employer likely will be obligated to bargain with the union over ongoing employment issues.

In some situations, the buyer may want to approach an incumbent union to discuss its plans or to obtain concessions. The buyer must be careful that such an approach not be viewed as recognition of the union and an agreement to bargain. To avoid this, the buyer must disclaim any intent to recognize the union or assume the collective agreement. The buyer also can meet with the seller’s employees prior to the sale to inform them of initial terms and conditions of employment, so long as the purpose is related to their continued employment.

The existence of a successors and assigns clause in an existing collective agreement (dictating that the agreement will be binding upon any buyer) also may create issues for buyer and seller. Although such a clause is not, in fact, binding on the buyer, it may have a significant impact upon the seller, including the potential assessment of damages or even injunctive relief blocking the sale.

**Various Employment Laws**

Setting aside consequent terminations, most M&A transactions do not implicate non-discrimination and other employee-protection statutes. These laws can, however, have an impact upon the value of the deal. For example, a buyer may be obligated to remedy a predecessor’s unfair labor practices, or may be held liable for its statutory violations. If the culture of the target has allowed inappropriate conduct to go unchecked and unpunished, the liability for conduct occurring after the effective date of the sale may inure to the buyer. These risks can be managed (although not eliminated) by careful due diligence.

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Mergers & Acquisitions: 
Post-Employment Restrictive 
Covenants In the Acquisition Context

By: Roy A. Ginsburg

Your company is about to acquire a considerably smaller firm. 
You have completed your due diligence and have concluded that 
there is a compelling product fit between the two organizations, 
a sound geographic mix, and some potential synergies between 
the talents and skills of your management team and several of 
the key managers in the company you are acquiring. 
You had your Vice President of Human Resources review the 
employment agreements of these key individuals and were advised 
that they have standard non-competition, non-solicitation, and confidentiality agreements 
with their existing employer. Your VP of HR advised that the 
post-employment restrictive covenants are enforceable.

Shortly after the acquisition has been completed, four of the 
most promising employees of the acquired company resign. 
Worse yet, you now learn that they have joined your principal competitor. Do you have any recourse? 
Will the post-employment restrictive covenants these employees had with the firm you acquired provide your company adequate protection?

Although the hypothetical above provides a number of important facts that will influence the outcome of these questions, additional information is required to answer them with confidence. 
Moreover, as explained further below, the inquiries being posed retrospectively should have been explored in advance, before the acquisition closed.

First and foremost, you need to know whether the post-employment restrictive covenants contained an assignment clause. In other words, did the employees, when they executed the non-competition agreements and other post-employment restrictive covenants, agree that the agreements would be enforceable by a successor corporation? Is the assignment clause a part of the restrictive covenants and is it written in clear and understandable language? If these questions cannot be answered affirmatively, you may have no recourse whatsoever.

Courts around the country have been examining the issue of the assignability of post-employment restrictive covenants for some time. Although the results are not unanimous, and depend on the state law where the dispute arose, there is a growing body of case law holding that unless there is a specific assignment clause, the agreement is not enforceable by the acquiring firm.

This outcome appears to be driven by several rationales. Many courts begin with the general proposition that personal services contracts (such as employment agreements) are not enforceable. Thus, as these courts have concluded, the subsequent employer can neither force the employee to continue working for it nor prevent the employee from working for other firms. For example, the Ohio Court of Appeals observed in late 2002, “the employment relationship is a personal matter between an employee and the company who hired him and for whom he chose to work. Unless an employee explicitly agreed to an assignability provision, an employer may not treat him as some chattel to be conveyed, like a filing cabinet, to a successor firm.” 

Cary Corp. v. Linder, No. 80589, 2002 WL 31667316 (Ohio Ct. App. November 27, 2002). See also, Hess v. Gebhard & Co., 808 A.2d 912 (Pa. 2002) (covenant not to compete contained in an employment agreement is not assignable to the purchasing business entity in the absence of specific assignability provision); 
Reynolds & Reynolds v. Hardee, 932 F. Supp. 149 (E.D. Va. 1996) (employment agreement is based on mutual trust and confidence; non-compete is not assignable).

Even in jurisdictions where courts are unwilling to proclaim unequivocally that post-employment restrictive covenants are unenforceable by a successor firm, there often is increased skepticism about the validity of restrictive covenants when the acquiring company is seeking to enforce them. Courts generally recognize that such covenants are anti-competitive, constitute a restraint of trade and inhibit employee mobility. Judges often are looking for ways in which to limit the enforceability of restrictive covenants, and the absence of an assignability clause in the agreement may provide that justification.

Even where these initial hurdles can be overcome, many courts find it inequitable to enforce post-employment restrictive covenants against an employee who did not bargain for it with the successor corporation. Courts have recognized that an employer is well situated to re-negotiate a new agreement with the employee at the time the acquisition occurs. For example, the Pennsylvania Superior Court emphasized,

“Strong policy considerations underlie the conclusion that restrictive covenants are not assignable. Given that restrictive covenants have been held to impose a restraint on an employee’s right to earn a livelihood, they should be construed narrowly; and absent an explicit assignability provision, courts should be hesitant to read one into the contract. Moreover, the employer, as drafter of the employment contract, is already in the best position to include an assignment clause . . . Similarly, a successor employer is free to negotiate new employment contracts with the employees . . . or secure the employee’s consent to have the prior employment contract remain in effect.”


continues on page 11
Post-Employment Restrictive Covenants  from page 10

Thus, in addition to concerns about the equities of allowing a successor corporation to enforce an agreement to which it had never been a party, several courts have adopted the All-Pak court’s analysis, finding that enforceability of restrictive covenants following the acquisition is precisely one of the issues that should have been addressed before the acquisition closed. These courts have concluded that having foregone the opportunity to address this issue at a time when the parties could have bargained openly and in good faith, it would be unfair to allow the successor corporation to enforce the pre-existing restrictive covenants.

Minnesota Law

In Minnesota, courts are somewhat more tolerant of restrictive covenants than in some other jurisdictions (e.g., California, Colorado or North Dakota). Even here, however, many judges have been quick to point to the anti-competitive, restraint of trade, reduction in employee mobility concerns that have lead courts in other jurisdictions to repudiate restrictive covenants altogether. If, however, the post-employment restrictive covenants are fundamentally sound, with reasonable geographic, temporal and substantive restrictions, and if the agreement contains an explicit assignment provision, it may be enforceable by a successor corporation.

For example, in Saliterman v. Finney, 361 N.W.2d 175 (Minn. Ct. App. 1985), the Minnesota Court of Appeals evaluated a case involving the acquisition of a small dental office. After the business was purchased, one of the dentists who worked there resigned and opened a competing practice nearby. That dentist, however, had a post-employment restrictive covenant, which included an explicit assignment clause. The Court of Appeals found the limited restrictive covenant (a several-mile radius) was enforceable by the successor corporation. The Saliterman decision hinged on the nature of the business (a dental practice) where patient good will was deemed critical and the geographic restriction was extremely limited. Moreover, the court did not have to evaluate whether to enforce the non-compete in the absence of an assignment provision. It is unclear, therefore, whether the Saliterman decision has any applicability beyond its narrow facts, especially given Minnesota courts’ skepticism about the enforceability of post-employment restrictive covenants.

A very recent case from the United States District Court for the District of Minnesota concluded that Saliterman should be construed narrowly. In Inter-Tel, Inc. v. CA Communications, Inc., et al., Civ. File No. 02-1864 (D. Minn. December 29, 2003), Judge Magnuson found that Saliterman was limited to the context where there was an explicit assignment provision in the post-employment restrictive covenant. The Court held that “in Minnesota . . . a finding of assignability likely depends on the language of the contract.” The Court went on to observe that “Minnesota courts are historically reluctant to enforce covenants not to compete, because such covenants decrease competition and restrict the employee’s ability to earn a living.” Judge Magnuson, therefore, concluded that where the contract does not provide for assignment, a Minnesota court “would likely construe the language of the contract against the employer and find the assignment void.” As with some of the judicial analyses described above, the Court also noted that the successor corporation could have negotiated this issue at the time of the acquisition. Judge Magnuson held that “Inter-Tel’s failure to ensure that the restrictive covenants were assignable is fatal to its claims seeking to enforce those covenants.”

In sum, although Minnesota law on this issue is not crystal clear, the better judicial analyses require an assignment provision for the post-employment restrictive covenants to be enforceable by a successor corporation. Certainly, the prudent attorney will address this issue at the time of the acquisition, not in a post-acquisition dispute designed to remedy an unanticipated and undesired result.

Other Issues

Even if a post-employment restrictive covenant contains an appropriate assignability clause, the due diligence inquiries should not end there. There are other potential pitfalls that may adversely affect the enforceability of such restrictive covenants. Briefly summarized, these issues include the following:

First, you should examine whether there was adequate consideration for the restrictive covenant. If the underlying agreement would not have been enforceable by the company that was acquired, it will not be enforceable by the successor corporation.

Second, you need to explore whether the acquired corporation uniformly used restrictive covenants. To the extent that the acquired company was inconsistent with respect to obtaining restrictive covenants, this too may undermine their enforceability. Again, if they would not have been enforceable by the acquired company, there is little likelihood that they could be enforced by the successor entity.

Third, you should evaluate whether the restrictive covenants were enforced. If the company you are acquiring routinely obtained but rarely enforced its non-competes or other restrictive covenants, you may have a tough argument ahead.

Fourth, you need to consider thoughtfully the equities of the situation. For example, if the company you acquired concludes on page 12
operated in a limited geographic area (perhaps limited to one state), and if your company is a nationwide enterprise, the geographic restriction that the employee may have considered reasonable when signing the document could have far different implications post-acquisition. Similarly, if the substantive restriction of the original agreement had limited scope, reflecting the limited product line of the acquired company, there may be fundamental inequities in enforcing the substantive limitations of that agreement with respect to a more expansive product line.

Fifth, since the enforceability of restrictive covenants are dependent on state law, you need to examine carefully the laws of the relevant states. Where was the acquired company doing business? Where was the original agreement executed? Where did the employee whose post-employment activities you hope to restrict actually work? Where is the acquiring company located? Where will the affected employee work post-acquisition? These are but a few of the questions that should be explored when trying to assess whether the post-employment restrictive covenants are enforceable.

In sum, care should be given to evaluating whether post-employment restrictive covenants will be enforceable after an acquisition. At a minimum, this evaluation should encompass the issue of whether the restrictive covenant has an assignment clause, and the five other key questions listed above. If there is any doubt about the enforceability of the restrictive covenant, and if certain employees of the company being acquired are deemed critical to the acquisition, this issue should be addressed before the transaction is closed. There are a variety of ways that the acquiring company can protect itself against the risk that key employees might be lost following the acquisition, not the least of which is negotiating a new agreement. If the key employees refuse to execute new agreements, that may be a telling indication of their plans (firm or tentative) following the acquisition. This factor then can be given appropriate weight when determining whether to proceed with the acquisition and if so, at what price.

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We all know the purposes of the attorney-client privilege, the ethics doctrine of confidentiality and the opinion work product doctrine: to encourage clients to make full disclosures to their lawyers, so that the lawyers can give clients fully-informed advice; to assure clients that their lawyers will not make harmful or embarrassing disclosures even of non-privileged information; and to keep an attorney’s work and opinions from litigation opponents.

For these purposes to be served, lawyers must keep themselves and their organizational clients informed of changes to these confidentiality doctrines. This is crucial because confidentiality protection is most often lost inadvertently, through inattention or through misunderstanding of the law of privilege or work product. Maintaining a working knowledge of these doctrines has, however, become more difficult because of the increasing volume and nuance of relevant case law.

This article will spotlight several attorney confidentiality law developments in Minnesota, the Eighth Circuit and the U.S. Supreme Court: cases which have widened the organizational “circle of confidentiality;” exceptions to privilege rules, like the “joint defense,” “communicating agent” and “crime-fraud” doctrines; and waiver issues, like inadvertent production and work product waiver. First, however, let us recall the essentials of the confidentiality doctrines of attorney-client privilege, work product and the ethics duty of confidentiality.

Privilege, Work Product and Confidentiality: The Basics

The attorney-client privilege may be asserted against attempts to compel testimony which would reveal confidential communications seeking or giving legal advice. The privilege is created by state statute and federal common law. The ethics duty of confidentiality, created by Rule 1.6, Rules of Professional Conduct, requires attorneys to keep confidential (subject to certain exceptions) both privileged communications and other confidential information whose disclosure is apt to be detrimental to the client. Work product is recognized by Rule 26, Rules of Civil Procedure, and by common law. It applies to trial preparation material and attorney opinions.

Broadening the Circle of Confidentiality

The “circle of privilege,” that is the persons within (or even outside of) an organization who may be privy to confidential communications without losing protection, has widened in recent years. Knowing who is within the circle is crucial, because the presence of any person outside the circle can destroy the privilege. Thus, if a client’s friend or relative is present for attorney-client communications, the communications are not privileged. State v. Rhodes, 627 N.W.2d 74 (Minn. 2001). Several cases show the trend to broaden the circle of privilege.

Although Upjohn Co. v. U.S., 449 U.S. 383 (1981) and Diversified Industries, Inc. v. Meredith, 572 F.2d 596 (8th Cir. 1977), are not recent, they continue to be essential in identifying the corporate persons who are within the protected circle of confidentiality. These cases recognized that corporate counsel may obtain information from even low-level employees for the purpose of advising the corporation, and that information may be protected by privilege and work product. In Upjohn the IRS was unable to obtain completed questionnaires that had been sent by counsel to Upjohn employees who might have had knowledge of improper payments to foreign officials. So long as the purpose of the questionnaires was to facilitate legal advice, and so long as confidentiality and restricted access to the questionnaires were maintained, the documents were protected. In re Bieter Company, 16 F.3d 929 (8th Cir. 1994), recognized that even non-employee outside consultants could be within the circle of privilege, so long as they were regularly involved in assisting the company in important decision-making, including acting on the advice of counsel.

Knowing what is protected material is just as important as identifying who is a protected person. Two recent cases will help organizations protect types of documents that are regularly used by house counsel and outside counsel.

Kobluk v. Univ. of Minnesota, 574 N.W.2d 436 (Minn. 1998), recognized that the privilege protects a typical contemporary mode of attorney-client communications: the exchange of drafts of a letter to a third party. The court rejected the argument that because the author of each draft intended that it be final and that it be sent to a third party, the intent of confidentiality required for the privilege was lacking. Instead, the court found a “presumption of confidentiality” for attorney-client communications generally and found that the exchange of drafts was simply a modern mode of communication.

In re Spalding Sports Worldwide Inc., 203 F.3d 800 (Fed. Cir. 2000), held that the client’s communications with patent counsel, including technical information, were for the purpose of seeking legal advice and were protected by privilege — notwithstanding the client’s intent that counsel use the materials transmitted for the purpose of making public filings to obtain a patent. The holdings of the Federal Circuit regarding substantive patent law, including privilege issues directly related to patent law, are binding on all federal district and circuit courts. Spalding makes indisputable the proposition that patent attorneys provide counsel as other attorneys do, and are not mere scribes or conduits.

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PROFILE: Dorsey’s M&A Group

Dorsey’s M&A Group is a national leader in mergers and acquisitions. Dorsey completed more M&A deals than any other law firm in the country during the 10 years ended December 31, 2003. Members represent corporate clients, individuals, investment banks, management buyout groups and others in transactions involving the purchase or sale of businesses and related financing — acquisitions, divestitures, leveraged buyouts, mergers, tender offers and more. Transaction range in size from small to billions of dollars, and include the purchase and sale of both public and private companies.

Deals are led by experienced M&A practitioners supported by a breadth of experience. Approximately 200 lawyers from Dorsey’s 20 national and international offices devote substantial amounts of time to M&A transactions.

• **Breadth** — Most M&A deals touch on many areas of law, such as tax, employee benefits, employment, intellectual property, litigation, environmental, real estate and corporate. Being able to consult with experts is imperative. Dorsey is one of the largest law firms in the United States. Legal specialties in Asia, Europe and several U.S. cities provide unique resources when needed.

• **Depth** — Each legal specialty is represented by a number of lawyers, not by an “expert” wearing many hats. Timing is always crucial in M&A transactions and Dorsey is able to put teams of experts together on the spot.

• **Capabilities** — Lawyers staffing M&A teams have honed their skills in their representation of business clients within their respective specialties.

• **Training and backup** — Marking up documents from a prior deal to meet your unique needs is costly, produces imperfect documents and is fraught with risk (e.g., the specially negotiated term from the prior deal that gets left in the document). That’s not Dorsey’s approach. The M&A Group has created idealized form documents so that every first draft starts with your perspective in mind (buyer or seller). For most law firms, training is on the job. While nothing can substitute for experience, Dorsey provides formal training to both partners and associates so that current topics and persistent problems are discussed on a continuing basis.

• **Efficiency** — Carefulness and concern should not be sacrificed for expediency when an important deal is in progress. On the other hand, there’s no need for waste. Dorsey’s M&A Group has invested significant time in the development of forms and the training to understand the use of those forms. Dorsey’s M&A lawyers know what to do because of their collective experiences.

• **Timeliness** — Deadlines are always tight. Unlike other areas of law, where court calendars dictate timing, M&A deals are driven by the respective interests of the parties involved. Timely action is the best way to assure certainty. Because of the experience and the depth of the firm’s internal resources, Dorsey lawyers can jump in when needed to prepare the necessary documentation, assist in due diligence and conduct necessary negotiations.

• **External resources** — Through computerized data bases and other external resources, Dorsey’s M&A Group can, within hours, locate useful precedent for particular situations that may lead to advanced problem solving.

• **Internal resources** — Dorsey’s networked computer technology is easy to use, reliable, and affords the firm an ability to share experiences unequalled by any other law firm. In addition, Dorsey’s internet-based document management system permits client access to deal documents from virtually anywhere in the world.

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**Corporate Finance**

#1 in Mergers & Acquisitions

In the last 10 years Dorsey has done more M&A deals in the U.S. than any other law firm.

— Thomson Financial Securities Data

Total Deals: 1647

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<td>Deals</td>
<td>58</td>
<td>85</td>
<td>99</td>
<td>153</td>
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<td>223</td>
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Dorsey's National Ranking:

1994: #2
1995: #2
1996: #1
1997: #1
1998: #1
1999: #1
2000: #2
2001: #1
2002: #2
2003: #3
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<tr>
<th>Date Closed</th>
<th>Client Name</th>
<th>Target</th>
<th>Deal Description</th>
<th>Entity Sold</th>
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<tr>
<td>January 2003</td>
<td>Bankruptcy Services, LLC</td>
<td>Bankruptcy Services, LLC</td>
<td>Sale to EPIQ Systems, Inc.</td>
<td>National leader in Chapter 11 case management services</td>
</tr>
<tr>
<td>January 2003</td>
<td>IAMGold Corporation</td>
<td>Repadre Capital</td>
<td>Share for share acquisition</td>
<td>Gold mining company</td>
</tr>
<tr>
<td>January 2003</td>
<td>Patina Oil &amp; Gas Corporation</td>
<td>Elysium Energy, L.L.C.</td>
<td>Acquisition of the remaining 50% interest of Elysium Energy, L.L.C.</td>
<td>Oil and gas energy company</td>
</tr>
<tr>
<td>March 2003</td>
<td>Patina Oil &amp; Gas Corporation</td>
<td>Le Norman Partners</td>
<td>Acquisition of the remainder of Le Norman Partners</td>
<td>Oil company</td>
</tr>
<tr>
<td>April 2003</td>
<td>American Lock Company</td>
<td>American Lock Company</td>
<td>Sale to Master Lock Company, a subsidiary of Fortune Brands, Inc.</td>
<td>Manufacturer of locks, padlocks and combinations locks</td>
</tr>
<tr>
<td>April 2003</td>
<td>Caswell International Corporation</td>
<td>Caswell International Corporation</td>
<td>Sale to Meggitt PLC</td>
<td>Leading provider of live fire training equipment for US law enforcement agencies and ground target for military customers worldwide</td>
</tr>
<tr>
<td>April 2003</td>
<td>The Schwan Food Company</td>
<td>Mrs. Smith's Bakers' frozen dessert business</td>
<td>Purchase of Mrs. Smith's Bakers' frozen dessert business from Flowers Foods</td>
<td>Frozen dessert business</td>
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<tr>
<td>June 2003</td>
<td>Conseco Finance Corp.</td>
<td>Conseco Finance Corp.</td>
<td>Sale of all of its assets and operations, out of bankruptcy to CFN Investments Holdings LLC and Investor Group</td>
<td>Finance Company</td>
</tr>
<tr>
<td>June 2003</td>
<td>Geomaque Explorations Ltd.</td>
<td>Midas Gold plc</td>
<td>Acquisition of Midas Gold plc</td>
<td>International gold mining, mine development and exploration company</td>
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<td>June 2003</td>
<td>Orphan Medical, Inc.</td>
<td>Orphan Medicalis BusulfexÆ (busulfan) Injection business</td>
<td>Sale of its BusulfexÆ (busulfan) Injection business to ESP Pharma, Inc.</td>
<td>Conditioning regimen prior to hematopoietic progenitor cell transplantation</td>
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<td>July 2003</td>
<td>EM.TV &amp; Merchandising AG</td>
<td>The Jim Henson Company, Inc.</td>
<td>Sale of The Jim Henson Company, Inc. to JHC Holding Company, LLC for cash and assumed debt</td>
<td>Leading producer and marketer of pre-school, kids and family entertainment</td>
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<td>November 2003</td>
<td>eFunds Corporation</td>
<td>Oasis Technology, Ltd.</td>
<td>Purchase of the assets of Oasis Technology, Ltd.</td>
<td>Private payment software company</td>
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<tr>
<td>November 2003</td>
<td>UnitedHealth Group</td>
<td>Golden Rule Financial Corp.</td>
<td>Acquisition of Golden Rule Financial Corp.</td>
<td>Offers financial services, life insurance, health insurance and medical savings accounts</td>
</tr>
<tr>
<td>December 2003</td>
<td>Hickory Tech Corporation</td>
<td>Hickory Tech Corporation Wireless business</td>
<td>Sale of its wireless business to Western Wireless Corporation</td>
<td>Communications company</td>
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The circle of privilege also has been broadened by two exceptions (communicating agents and joint defense) and narrowed by a third (crime-fraud). The first two provide continued privilege protection notwithstanding disclosure of privileged information to a person other than the attorney or client normally. In the third, perverse purposes destroy otherwise privileged communications.

Communicating Agents. Agents of the lawyer or client may be privy to lawyer-client communications without the privilege being lost so long as the involvement of the agent facilitates the rendering of legal advice. Translators, accountants or other experts can all be communicating agents within the circle of privilege, but only if their true purpose is to facilitate legal advice. The fact that the attorney hires the agent will not by itself guarantee protection if the true purpose is to render, say, accounting or other technical advice. The presence of a public relations expert in an attorney-client litigation planning meeting can destroy the privilege if, as will often be the case, the expert’s presence is not to facilitate legal advice.

Joint Defense. The joint defense doctrine, like the communicating agent doctrine, allows a person other than attorney and client into the circle of privilege. Before discussing this doctrine, however, two confusions must be dispelled. First, joint defense differs from “joint clients” in that the former requires separate counsel and the latter involves just one lawyer. Second, joint defense is more properly called “common interest” because it is not restricted to defendants — although some courts have restricted the doctrine to litigation contexts. In any event, the joint defense doctrine to apply, the parties must share substantial common interests, they must be separately represented and they must agree not to disclose to others their privileged information. In such circumstances they may share privileged information without waiving the privilege. Most courts would recognize the doctrine if, say, in a corporate acquisition context, buyer’s counsel, doing due diligence, asked the seller to share its counsel’s evaluation of certain claims or litigation against the seller.

For this doctrine to apply, the parties must truly share common interests. In re Grand Jury Subpoena Duces Tecum, 112 F.3d 910 (8th Cir. 1997), recognized the doctrine, but rejected Hillary Clinton’s claim to its benefits. The court reasoned that the matter at stake in the grand jury proceedings — whether Mrs. Clinton went to prison — was not a cognizable interest of the White House, with whose counsel Mrs. Clinton’s counsel had shared otherwise privileged information.

Crime-Fraud. The crime-fraud doctrine is an exception to the attorney-client privilege doctrine. Even though the formal requirements for the privilege are met, the law will not grant a privilege, because the communications are for perverse purposes — using the attorney to commit a crime or fraud. Two recent cases help explain how this doctrine will be applied.

The procedure for determining whether the crime-fraud exception applies often involves in camera judicial review of documents. But what is the threshold for the court undertaking that review? In Re BankAmerica Corp. Securities Litigation, 270 F. 3d 639 (8th Cir. 2001), provides a detailed analysis of when in camera review may be done and when the crime-fraud exception should be applied. This case emphasizes that the party seeking discovery must make “a specific showing that a particular document or communication was made in furtherance of the client’s alleged crime or fraud.” The attorney’s knowledge and intent are irrelevant, because “it is the client’s intent to further a crime or fraud that must be shown.” This case also makes clear that merely showing that a corporation consulted counsel at about the same time that it made allegedly fraudulent statements is not enough to apply the crime-fraud exception. Reversing a district court order that the documents in question be produced without in camera review, BankAmerica Corp. directed the lower court to consider whether a sufficient showing had been made for review and, if so, to undertake document-by-document review before determining whether the documents must be produced.

Another important crime-fraud issue is whether the exception applies to improprieties short of crime or fraud. Restatement Third, The Law Governing Lawyers, which has been cited in the Eighth Circuit and in Minnesota on other privilege issues, acknowledges a division of authorities but concludes, “[T]he prevailing view limits the exception to crimes and frauds.” However, Minnesota state courts appear to take a broader view. As State v. Philip Morris Inc., 606 N.W.2d 676, 691 (Minn. App. 2000), recently stated, “The critical inquiry is whether the attorney-client privilege has become unworthy of protection.” Similarly, Kahl v. Minnesota Wood Specialty, Inc., 277 N.W.2d 395, 399 (Minn. 1979), quoted with approval Wigmore’s comment that the privilege should not extend to protect any “deliberate plan to defy the law and oust another person of his rights...”

Waiver Issues

Inadvertent Production

Parties enjoying the privilege need to be careful about protecting the confidentiality of privileged information. Two factors are apt to cause mistaken transmittals of privileged information: the relative ease of communication by fax

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and e-mail; and the huge volume of documents that need to be reviewed and (except for privileged items) produced in response to litigation demands.

What should be done when such a mistake occurs? ABA Formal Opinion 92-368 (1992) gives one view of the obligations of the receiving lawyer:

A lawyer who receives materials that on their face appear to be subject to the attorney-client privilege or otherwise confidential, under circumstances where it is clear they were not intended for the receiving lawyer, should refrain from examining the materials, notify the sending lawyer and abide the instructions of the lawyer who sent them.

The ABA opinion is not, however, the law, although a few courts have treated it as such. The receiving lawyer’s client duty — at least when the “inadvertent production” has been sufficiently careless to raise a question of possible waiver — may be to ask the client whether it wishes to seek judicial determination that a waiver has occurred. In any event, the case law in the Eighth Circuit and in Minnesota indicates that courts will be reluctant to find waiver by inadvertent production, unless the disclosing party has been exceptionally careless in its disclosures or in failing to retrieve disclosed documents.

**Work Product Waiver and Protection Generally**

Work product protection is generally thought to be inferior to privilege protection — after all, ordinary work product protection can be overcome on a showing of substantial need and undue hardship. There are doctrines, however, that make work production harder than may be supposed, even harder than privilege protection in some ways.

First, for work product to be created, attorney involvement is not required. Rule 26 explicitly protects materials prepared “by or for another party or by or for that other party’s representative.”

Second, “[O]pinion work product enjoys a nearly absolute immunity and can be discovered only in very rare and extraordinary circumstances.” In re Murphy, 560 F.2d 326, 336 (8th Cir. 1977). Opinion work product may be found even in “an attorney’s personal recollections, notes, and memoranda summarizing his conversations with potential witnesses.” U.S. v. Bonnell, 483 F.Supp. 1070, 1078 (8th Cir. 1979). Similarly, an attorney’s interview notes are protected. Baker v. General Motors, 209 F.3d 1051 (8th Cir. 2000). House counsel’s mere knowledge that certain documents exist can be opinion work product, where the knowledge arises from selection from voluminous documents. Shelton v. American Motors Corp., 805 F.2d 1323 (8th Cir. 1986).

Third, work product protection is less easily waived than privilege protection. With few exceptions, such as those discussed above, privilege is waived by disclosure to any third person. In the organizational context, Upjohn indicates that to maintain its protected status, privileged information should be disseminated within an organization only on a need-to-know basis. Work product protection is not so easily waived: “[D]isclosure of a document to third persons does not waive the work-product immunity unless it has substantially increased the opportunities for potential adversaries to obtain the information. Most cases have so held and have found no waiver from disclosure.” 8 Wright & Miller, Federal Practice and Procedure: Civil 2d § 2024 at 368-69 (1994).

**Ethics Confidentiality Issues**

Lawyers Board proceedings and publications have recently considered two interesting confidentiality issues arising under Rule 1.6, Minnesota Rules of Professional Conduct (MRPC).

**Must Attorneys Regard Some Public Documents as “Secrets”?** Would you want your attorney to talk about information that is embarrassing or detrimental to you, on the justification, “I can tell you about this — it’s in the court file?” Rule 1.6 forbids attorneys to disclose either privileged information or other information (“secrets”) whose disclosure would be detrimental to the client or which the client has requested be “held inviolate.”

Can information that is publicly filed be a “secret”? Some authorities have argued that there is so much information that, although publicly filed, is for practical purposes unknown to the public, such that a lawyer should not make further disclosure of the information where it would harm or embarrass a client. The Lawyers Board took this position in a recent disbarment case, In re Fuller, 621 N.W.2d 460 (Minn. 2001). Fuller, for his own purposes, had disclosed his client’s criminal record. A Supreme Court referee rejected the charge, reasoning that because the record was available to the public, it was not a “secret.” The referee’s holding is in accord with the majority of recent cases.

**May a Lawyer-Witness Assert Rule 1.6 in Response to a Subpoena?** When lawyers receive subpoenas for documents or testimony regarding a prior representation, they will normally look to the client to determine whether they should assert the attorney-client privilege as to any questions or document demands. What if the client wishes the attorney to decline to provide the information sought and instead to assert the attorney’s confidentiality duty under Rule 1.6, even if privilege does not apply to some of the items? A Senior Assistant Director at the Lawyers Board recently wrote, “If subpoenaed to a deposition or a hearing, the attorney could assert the attorney-client privilege or the ethical obligation in response to all questions seeking such

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information (and recall that the professional responsibility obligation of confidentiality is more extensive than the privilege).” Martin Cole, “The Self-Defense Exception to Client Confidentiality,” Minnesota Lawyer, April 1, 2002. This position appears to be incorrect as to the ethics obligation of confidentiality. MRPC Rule 1.6(b)(2) provides that a lawyer may reveal secrets when required by law; Rule 26, R. Civ. Proc., requires an answer to relevant discovery unless there is a privilege; and MRPC Rule 3.4(c) requires a lawyer to obey court rules. Similarly, U.S. v. Sindel, 53 F.3d 874 (8th Cir. 1995), held that Rule 1.6 did not protect non-privileged material from an IRS summons.

Conclusion

Because litigation is, in some measure, “a search for the truth,” and privileges conceal otherwise relevant facts, the law has always construed privileges narrowly. Nonetheless, the courts have recognized the importance of confidentiality for rendering legal advice as well as recognized certain realities of modern communication and litigation. At least for those well-informed on the protections and exceptions of the three confidentiality doctrines — attorney-client privilege, work product and the ethics duty of confidentiality — the protections of these doctrines are available, in some ways more broadly than ever before.

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The Scope of Continuing Violations

By: Clifford S. Anderson

The Scope of Continuing Violations

Theory in Title VII

Current or former employees seeking to litigate discrimination claims must first file a charge of discrimination with the Equal Employment Opportunity Commission (EEOC) or similar state agency within 300 days (or, in some cases, 180 days) of the alleged discriminatory event. Subject to certain exceptions based on principles of equity, the failure to file a timely charge of discrimination will spell the doom of a discrimination lawsuit. This analysis can be complicated, however, when multiple acts of discrimination over a period of time are alleged. Plaintiffs who have filed a belated charge of discrimination will often contend that events outside the 300 or 180 day period relate to events within this period, invoking the “continuing violation” doctrine in an effort to avoid dismissal of all or a part of the alleged claims. The U.S. Supreme Court addressed the applicability and scope of the “continuing violations” doctrine in National Railroad Passenger Corp. v. Morgan, 112 S. Ct. 2061 (2002).

The Court’s first principal holding, decided by a 9-0 vote, was that 42 U.S.C. § 2000e-5(e)(1) “precludes recovery for discrete acts of discrimination or retaliation that occur outside the [relevant] statutory time period” for filing charges of discrimination. Morgan, 112 S. Ct. at 2068. (Justice O’Connor, joined by Chief Justice Rehnquist and Justice Breyer, wrote a separate concurrence emphasizing that they would have extended the Court’s holding in an even more pro-employer direction, such that “the charge-filing period precludes recovery based on discrete actions that occurred more than 180 or 300 days after the employee had, or should have had, notice of the discriminatory act.” Id. at 2078 (emphasis added)). The remaining six justices, however, concluded that Morgan was not the proper case to decide “whether the time begins to run when the injury occurs as opposed to when the injury reasonably should have been discovered.” Id. at 2073.

The Court’s second principal holding resulted in a 5-4 divided court, with the majority representing an unusual alignment of Justice Thomas and Justices Stevens, Souter, Ginsburg and Breyer. The Court held that “consideration of the entire scope of a hostile work environment claim, including behavior alleged outside the statutory time period [defined in 42 U.S.C. § 2000e-5(e)], is permissible for purposes of assessing liability, so long as any act contributing to that hostile environment takes place within the statutory time period.” Id. at 2068 (emphasis added).

Finally, the Court also held that the “application of equitable doctrines . . . may either limit or toll the time period within which an employee must file a charge.” Id.

Facts and Procedural Background

On February 27, 1995, Abner J. Morgan, Jr., a black man, filed a charge of discrimination and retaliation with the EEOC and the California Department of Fair Employment and Housing (CDFEH) against the National Railroad Passenger Corporation (Amtrak). Morgan alleged that during the period he worked at Amtrak he was consistently harassed and disciplined more harshly than other employees on account of his race. Id. He alleged that the discrimination commenced when Amtrak hired him in August 1990, and subsequently included “termination for refusing to follow orders, Amtrak’s refusal to allow him to participate in an apprenticeship program, numerous ‘written counselings’ for absenteeism, as well as the use of racial epithets against him by his managers.” Id. at 2068 & n. 1.
The Supreme Court accepted the case to consider whether, and under what circumstances, a Title VII plaintiff may sue regarding events that fall outside the statutory period for filing a charge with the EEOC — either 180 or 300 days “after the unlawful employment practice occurred.” Id. at 2068 (citing 42 U.S.C. § 2000e-5(e)(1)). The Court examined two critical questions — (1) What constitutes an unlawful employment practice? and (2) When has that practice occurred? — in light of both discrete retaliatory or discriminatory acts (terminations, denials of promotion, etc.) and hostile work environment claims of discrimination. Id. at 2070.

Discrete Claims of Discrimination

The Court straightforwardly held that a “discrete retaliatory or discriminatory act ‘occurred’ on the date that it ‘happened.’” Id. A “party, therefore, must file a charge within either 180 or 300 days of the date of the act or lose the ability to recover for it.” Id. at 2071.

Morgan had argued that the statutory language of 42 U.S.C. § 2000e-5(e)(1) requires the filing of a charge within a specified number of days after an “unlawful employment practice,” and that “practice” describes “an ongoing violation that can endure or recur over a period of time.” Id. The Court rejected this argument based on a plain reading of the statute, noting that 42 U.S.C. § 2000e-2 sets out numerous discrete acts that constitute “unlawful employment practices,” including failing or refusing “to hire or to discharge any individual or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment because of such individual’s race, color, religion, sex, or national origin....” The Court easily concluded that there “is simply no indication that the term ‘practice’ converts related discrete acts into a single unlawful practice for the purposes of timely filing.” Id.

The Court cited several principles gleaned from the case law in support of its holding:

“[Discrete] [d]iscriminatory acts are not actionable if time barred, even when they are related to [other discrete] acts alleged in timely filed charges. Each discrete discriminatory act starts a new clock for filing charges alleging that act;” 42 U.S.C. § 2000e-5(e)(1) does not “bar an employee from using the prior acts as background evidence in support of a timely claim;” and

The “time period for filing a charge is subject to equitable doctrines such as tolling or estoppel.” Id. at 2072 (emphasis added).

Applying its holding to the facts of Morgan, the Court concluded that the Ninth Circuit erred when it applied “the continuing violations doctrine to what [the Ninth Circuit] termed ‘serial violations’” and held “that so long as one act falls within the charge filing period, discriminatory and retaliatory acts that are plausibly or sufficiently related to that act may also be considered for the purposes of liability.” Id. at 2073. Accordingly, the Court reversed that portion of the Ninth Circuit’s decision.

Hostile Work Environment Claims of Discrimination

The Court began its continuing violations theory analysis of hostile work environment claims by making four preliminary observations: (1) the very nature of such claims is that they involve “repeated conduct;” (2) therefore an unlawful employment practice involving such claims “cannot be said to occur on any particular day;” (3) rather, they occur “over a series of days or perhaps years;” and (4) “in direct contrast to discrete acts, a single act of harassment may not be actionable on its own.” Id.

Next, the Court noted that to determine whether an actionable hostile work environment claim even exists it is necessary to “look to ‘all the circumstances,’ including the ‘frequency of the discriminatory conduct; its severity; whether it is physically threatening or humiliating, or a mere offensive utterance; and whether it unreasonably interferes with an employee’s work performance.’” Id. at 2074 (citing Harris v. Forklift Systems, Inc., 510 U.S. 17, 23 (1993)). The Court then reasoned that a “hostile work

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environment claim is comprised of (sic) a series of separate acts that collectively constitute one ‘unlawful employment practice.’” Id. (citing 42 U.S.C. § 2000e-5(e)(1)). In sum, the majority held:

It does not matter, for purposes of the statute, that some of the component acts of the hostile work environment fall outside the statutory time period. Provided that an act contributing to the claim occurs within the filing period, the entire time period may be considered by a court for the purposes of determining liability.

Id. (emphasis added). Stated slightly differently, the Court re-emphasized its holding this way:

Given, therefore, that incidents comprising a hostile work environment are part of one unlawful employment practice, the employer may be liable for all acts that are part of this single claim. In order for the charge to be timely, the employee need only file a charge within 180 or 300 days of any act that is part of the hostile work environment.

Id. at 2075 (emphasis added).

The Court also clarified that an act falling within the statutory time period for filing “need not . . . be the last act.” Id. at 2074. Rather, as “long as the employer has engaged in enough activity to make out an actionable hostile environment claim, an unlawful employment practice has ‘occurred,’ even if it is still occurring.” Id.

By way of example, the Court explained that in a scenario where acts contributing to a hostile environment occur on days 1-100 and on day 401 — but not in between on days 101-400 — a charge filed in connection with the day 401 incident could, nevertheless, still pull in the acts that occurred on days 1-100 for liability purposes “so long as each act is part of the whole,” since a hostile work environment constitutes one “unlawful employment practice.”” Id. at 2075. On the other hand, the Court made clear that:

[If] an act on day 401 had no relation to the acts between days 1-100, or for some other reason, such as certain intervening action by the employer, was no longer part of the same hostile work environment claim, then the employee can not recover for the previous acts, at least not by reference to the day 401 act.

Id. (emphasis added).

Applying this analysis, the Court affirmed the Ninth Circuit’s reversal of the District Court’s dismissal of some aspects of Morgan’s hostile work environment claim. It did so because it found that Morgan’s allegations were related and at least some occurred within the 300-day charge filing period. Id. at 2076.

To avoid the prospect of hopelessly untimely claims, the Court also carved out certain equitable defenses when a “plaintiff unreasonably delays filing a charge.” Id. at 2076. First, the majority noted that “the filing period is not a jurisdictional prerequisite to filing a Title VII suit . . . [thus] . . . it is a requirement subject to waiver, estoppel, and equitable tolling ‘when equity so requires.’” Id. Second, the Court held an employer “may raise a laches defense, which bars a plaintiff from maintaining a suit if he unreasonably delays in filing a suit and as a result harms the defendant.” Id. This affirmative defense requires proof of two elements: (a) “lack of diligence by the party against whom the defense is asserted,” and (b) “prejudice to the party asserting the defense.” Id. The Court left for another day, however, “how — and how much — prejudice must be shown” and ‘what consequences follow if laches is established.” Id. (citation omitted).

Practice Pointers

Several practical tips for employers emerge from the Morgan decision:

• First, with regards to discrete claims of alleged discrimination (failure to hire, terminations, denial of promotion, compensation decisions, etc.), employers need to be diligent about conveying in writing, and documenting in their records, the precise date that the applicant or employee (and potential future Title VII plaintiff) received notice of an adverse employment decision. Such careful documentation will help ensure a factually indisputable date on which the filing period began, thus heightening the likelihood that a statute of limitations defense will succeed.

• In hostile work environment situations, employers should be thorough in documenting all internal harassment complaints by employees. The nature of the harassment, the identity of the alleged harasser(s), the dates, where it occurred and other pertinent facts should all be gathered. This will help generate a record that may later enable the employer to argue successfully that certain acts outside the time period for a timely charge “had no relation to the acts” for which the charge was timely.

• Finally, employers need to be cognizant of the equitable doctrines, including the affirmative defense of laches, that should be considered in the defense of any hostile work environment case where the plaintiff has unduly delayed commencing suit.

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The ADA and the “Direct Threat” Defense

By: Erik Nelson

The U.S. Supreme Court has, in recent years, paid increasing attention to and resolved several long-standing debates regarding the proper scope of federal employment laws. For example, the Supreme Court (never missing an opportunity to reverse the Ninth Circuit Court of Appeals) agreed to resolve a conflict among the circuits regarding whether the “direct threat” defense under the Americans with Disabilities Act (ADA) can apply where the employee poses a threat of harm only to himself. Like its other recent employment decisions, the Court’s decision in Chevron U.S.A. Inc. v. Echazabal, 122 S. Ct. 2045 (2002) likely will have a lasting and noticeable effect on federal discrimination litigation and continue to fuel a trend toward employer-friendly case law.

Mario Echazabal began working at a Chevron-owned oil refinery in 1972, employed by various maintenance contractors. Id. at 2047. Twice, in 1992 and 1995, Echazabal applied for employment directly with Chevron. Id. at 2047-48; Echazabal v. Chevron U.S.A., Inc., 226 F.3d 1063, 1065 (9th Cir. 2000). On both occasions he was hired conditionally, pending his passing a physical exam. On both occasions the offer of employment ultimately was withdrawn when the exams revealed liver abnormality and damage (later shown to be caused by hepatitis C) that would have been aggravated by continued exposure to liver-toxic chemicals at the refinery. 122 S. Ct. at 2047-48; 226 F.3d at 1065. It is not clear why Echazabal was allowed to continue working at the refinery after the first exam. Following the second, however, Chevron asked the contractor either to reassign Echazabal to duties away from exposure to liver-toxic chemicals or remove him from the refinery. 122 S. Ct. at 2048; 226 F.3d at 1065. Thereafter, the contractor laid Echazabal off. 122 S. Ct. at 2048.

Echazabal subsequently sued Chevron, claiming the company violated the ADA by refusing to hire him or even allow him to continue working in the refinery because of his liver condition. Id. Chevron defended the lawsuit on the grounds that Echazabal was not “otherwise qualified” for the job, because he was unable to tolerate the working environment, and on the grounds that he would pose a direct threat to his own health if he continued to work at the refinery. Id.; 226 F.3d at 1065-66, 1070-71. The district court granted summary judgment to Chevron, holding that “Echazabal raised no genuine issue of material fact as to whether the company acted reasonably in relying on its own doctors’ medical advice . . ..” 122 S. Ct. at 2048. Echazabal appealed to the Ninth Circuit, which asked for briefing on the question (not raised before the district court), of whether the direct threat defense can apply to a threat-to-self. Id.

The ADA proscribes “qualification standards, employment tests or other selection criteria that screen out or tend to screen out an individual with a disability . . . unless the standard, test or other selection criteria . . . is shown to be job-related for the position in question and is consistent with business necessity.” 42 U.S.C. § 12112(b)(6). The ADA specifically sets forth a defense, however, where the “qualification standards [have been] shown to be job-related and consistent with business necessity, and such performance cannot be accomplished by reasonable accommodation . . . .” Id. § 12113(a). “[Q]ualification standards’ may include a requirement that an individual shall not pose a direct threat to the health or safety of other individuals in the workplace.” Id. § 12113(b) (emphasis added).

The regulations issued by the Equal Employment Opportunity Commission (EEOC) implementing these provisions take them one step further. Specifically, the EEOC regulations provide that “[d]irect threat means a significant risk of substantial harm to the health or safety of the individual or others that cannot be eliminated or reduced by reasonable accommodation.” 29 C.F.R. § 1630.2(l) (emphasis added). Thus, the EEOC, through its implementing regulations, clearly establishes that the direct threat defense may be utilized even where the threat is to oneself.

The Ninth Circuit, over a sharp dissent, took a much different view. It held that the clear language of the statute unambiguously demonstrated the intent of Congress to allow employers to protect other persons in the workplace, but to forbid “paternalistic concerns regarding the [disabled] person’s health.” The court rejected the EEOC’s “contrary interpretation.” 226 F.3d at 1067-69.

The Supreme Court reversed, categorically rejecting most, if not all, of the Ninth Circuit’s reasoning and holding (unanimously) that the direct threat defense may be applied where the only threat of harm is to the disabled employee. The Court noted that the statute states only that a qualification standard “may include” a requirement that the employee not pose a direct threat of harm to others. 122 S. Ct. at 2049. “Far from supporting Echazabal’s position, the expansive phrasing of ‘may include’ points directly away from the sort of exclusive specification he claims.” Id. at 2050. The Supreme Court further observed that, taken to its logical extreme, the Ninth Circuit’s limited interpretation of the statute would lead to absurd results:

When Congress specified threats to others in the workplace, for example, could it possibly have meant that an employer could not defend a refusal to hire when a worker’s disability would threaten others outside the workplace? If Typhoid Mary had come under the ADA, would a meat packer have been defenseless if Mary had sued after being turned away?

Id. at 2051. concludes on page 22
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The Supreme Court also considered the impact of the Ninth Circuit's reasoning on state and federal worker safety laws, noting specifically that the Occupational Safety and Health Act obligates employers to furnish employees with a "place of employment . . . free from recognized hazards that are causing or are likely to cause death or serious physical harm." Id. at 2052, citing 29 U.S.C. § 654(a)(1).

The Court found that it simply could not reconcile the Ninth Circuit's decision to require employers to place employees in harm's way with legitimate policies protecting those same workers from the threat of harm. Ultimately, the Supreme Court decided that the EEOC regulation was a permissible and reasonable interpretation of the statute, reversed the Ninth Circuit's rejection of that regulation and remanded the case to the lower court "for proceedings consistent with this opinion." Id. at 2053. The Court left it to the Ninth Circuit to determine whether the direct threat defense was established by the facts in the case.

While this decision is important to further refining federal disability discrimination law, and reflects a welcome and continuing trend of decisions favorable to employers, it bears noting that the holding will have a somewhat limited effect. To date, the number of cases raising the defense of direct threat to self or others are relatively few; in part, perhaps, because of the uncertainty regarding whether the defense would apply to the disabled employee him/herself. It likely also is true that disabilities typically will only render an employee unable to perform certain essential functions of the job. Disabilities posing a threat of physical harm are, and likely will continue to be, somewhat rare. Further, Echazabal will not necessarily translate to state disability discrimination statutes. The direct threat defense is a creature born out of the specific language of the ADA and is not present in all state statutes.

For an employer assessing its disability discrimination policies and seeking to provide reasonable accommodations, Echazabal likely will require no dramatic change in policy or procedure (assuming, of course, that the employer's disability discrimination and reasonable accommodations policies were carefully and properly drafted in the first instance). As the Supreme Court notes, the EEOC regulations specifically require that the "determination that an individual poses a 'direct threat' shall be based on an individualized assessment of the individual's present ability to safely perform the essential functions of the job [which] shall be based on a reasonable medical judgment that relies on the most current medical knowledge and/or on the best available objective evidence." 29 C.F.R. § 1630.2(r).

As many employers are aware, all disability and reasonable accommodation assessments must be based upon an "individualized assessment" of: a) the employee's actual medical restrictions, using the best available medical date and information, and, b) the needs of the employer and the requirements of the job. Consequently, if an employer is utilizing an appropriately interactive process to identify and implement reasonable accommodations for potentially disabled employees, it already is engaging in exactly the sort of "individualized assessment" required to assert the direct threat defense. In fact, the only change that may be necessary for many employers is merely to establish the direct threat defense on the radar screen during reasonable accommodation assessment, by requesting, identifying (and keeping) medical documents and information that might establish a direct threat of harm posed by the alleged disability.

It will be interesting to see the ramifications of Echazabal for ADA enforcement in the coming years. Currently, the EEOC has been aggressively litigating against employers that, for example, try to identify employees or potential employees who are susceptible to carpal tunnel/repetitive motion injuries, in order to exclude them from repetitive motion positions. It seems to follow logically from Echazabal that an employee who cannot perform the essential functions of her position without credible risk of injury (whether that injury be to her liver or to her tendons) legitimately can be excluded from that position because she is a "direct threat" to her own health.

Also, the Supreme Court failed to address a key question which has split the circuits — whether an employee's threat of harm may render him not "qualified" under the prima facie prong of the disability discrimination case. The Ninth Circuit in Echazabal held that a direct threat must be analyzed as an affirmative defense, but other circuits have held that an employee is not "qualified" if he cannot perform the essential functions of the position without threat of harm to himself or others. See, e.g., Koshinski v. Decatur Foundry, Inc., 177 F.3d 599 (7th Cir. 1999).

Consequently, we likely can expect continued litigation concerning the scope of the Echazabal decision.

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Dorsey Expands Employment Law Practice in Southern California. Dorsey’s employment law expertise and capabilities in California received a significant boost in 2003, with the addition of Gabrielle Wirth and Kathlene Lowe to the firm’s Southern California office. Gabrielle brings 25 years of litigation experience to Dorsey, practicing in the area of complex employment litigation and class actions. Kathy joins Dorsey with more than 25 years experience as a trial lawyer. Dorsey also moved its Southern California office to 38 Technology Drive, Irvine, CA 92618-5310.

Victory for Cisco Systems. Dorsey obtained a complete summary judgment win for Cisco Systems, Inc. in a corporate raiding and misappropriation of trade secrets case involving $450 million in claimed damages. In September 25, 2003, opinion, Judge Joan Erickson (Minnesota Federal District Court) dismissed all claims against Cisco in Storage Technology Corporation v. Cisco Systems, Inc. The dismissal was the culmination of three years of highly contentious litigation, involving more than 90 depositions and the exchange of millions of documents. Cisco was represented by a team of Dorsey lawyers led by Roy Ginsburg and Joe Hammell. Storage Technology has filed an appeal with the Eighth Circuit.

Mall of America Shakeup. Management of the nation’s largest mall, the Mall of America, changed hands as a result of a major trial victory by Dorsey for Triple Five of Minnesota, Inc. and its principals, the Ghermezian family. Triple Five brought suit in 1999 against their partners in the Mall of America, the Simon Property Group and its individual and corporate affiliates, alleging breach of fiduciary duty stemming from the usurpation of a partnership opportunity to purchase 27.5% of the Mall. Following years of litigation and a two and one-half month trial, Judge Magnuson (Minnesota Federal District Court) issued an order directing the Simons to (1) sell the 27.5% interest in the Mall to Triple Five, (2) disgorge all net profits from their ownership interest in the Mall from the 1999 transaction to the present, (3) reimburse Triple Five for its reasonable costs and attorneys’ fees, and (4) transfer management of the Mall to Triple Five. The Dorsey team was led by Roger Magnuson and Chip Magid. The Simon Property Group has filed an appeal with the Eighth Circuit.

Asylum Class Action Victory. In a February 12, 2004, ruling, U.S. District Judge Richard Kyle granted summary judgment to the plaintiffs in a nationwide class action filed by Dorsey and others on behalf of more than 22,000 asylum holders whose requests for permanent resident status had been stalled by the INS for several years. Calling the government’s actions a “national embarrassment,” Judge Kyle directed the federal government to grant lawful permanent resident status to the thousands of men, women and children comprising the class. Jim Langdon and Kathy Moccio led the Dorsey team to this win.

Lawsuit Against Cirrus Grounded. A $40 million bet-the-company lawsuit against Cirrus Industries, an airplane manufacturer based in Duluth, was dismissed earlier this month by the Delaware Superior Court. The court granted summary judgment to Cirrus in an action brought by a jilted suitor whose offer to purchase the company was initially accepted but then rejected by the Cirrus Board after the suitor failed to completely fund a promised bridge loan. Minneapolis partners Carter and Chris Shaheen handled the case for Cirrus.

Not Just Any Fish Story. The Alaska Superior Court last week awarded more than $1,350,000 in attorneys’ fees and costs to Dorsey’s clients Nichirei Corporation of Japan and UniSea, Inc. of Redmond, Washington, following a trial victory last May in a $1 billion antitrust class action brought by 4,500 Bristol Bay Alaska fishermen. Nichirei and UniSea were represented by trial partners Dick Clinton and Bob Bundy from Dorsey’s Seattle and Anchorage offices, and Seattle trial associate Thuy Leeper.

M&A Leadership. Dorsey has been selected as lead outside transaction counsel on a deal for Cargill that, when consummated, will result in the creation of a new, publicly traded company with an initial market capitalization of $5.5 billion. Cargill, the world’s largest privately held company, will contribute its fertilizer business to the newly formed company, which will also merge with an existing, publicly held company. The Deal team from Dorsey is led by Minneapolis corporate partner Bob Rosenbaum and Bob Kuhns.

Pro Bono Award. Dorsey is the recipient of the National Law Journal’s Pro Bono Award for 2003. Dorsey earned special recognition among large law firms for its study of immigration reform on behalf of the American Bar Association. The ABA study involved more than 60 legal professionals in six offices, and the expenditure of more than 2500 hours over five months. The Dorsey team examined hundreds of immigration cases to gather valuable data on the effects of recent immigration reforms. Dorsey has met or exceeded the ABA’s “Pro Bono Challenge” by contributing at least 3% of its annual billable hours to pro bono work each year since 1992.
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