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Employer Update

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Update: Legal Risks for Employers Who Use Social Networking Websites

By Jeffrey S. Klein, Nicholas J. Pappas, Jason E. Pruzansky and Andrea Y. Loh

A study suggests that more than 80% of U.S. adults who go online use social media at least once a month, and that half of those participate in social networks such as Facebook. We continue to be more surprised, however, by the other conclusion contained in the study: "ample resources and polls suggest that companies are not addressing potential implications to their business."[1] In our Fall 2009 newsletter, we addressed a variety of legal and business risks facing employers who use social networking websites to facilitate their employment decisions. The active dialogue since that time has prompted us to revisit and expand on some of the thoughts discussed there.[2]

While social networking sites provide innovative, informal and immediate ways for employers and employees to communicate, the use of such websites also may prompt individuals to overlook norms for appropriate workplace conduct that have developed before the recent increase in online networking. This phenomenon may be caused by a variety of factors, including the instantaneous nature of electronic communications and the ability of individuals to interact without physically seeing or speaking to each other. An employer or employee's migration away from well-established guidelines and policies addressing professional behavior naturally poses risks for employers. In this article, we focus on a number of issues in addition to those we addressed in our previous article. As with our previous article, we also identify areas where employers should consider updating their policies to account for the risks posed by the use of social media in order to ensure that their guidelines for professional conduct fully reflect the modern-day workplace.

Requests for Recommendations

One form of social networking that has become increasingly popular is the use of sites such as LinkedIn for professional networking. LinkedIn permits members to create a profile highlighting their current position, former places of employment, professional accomplishments and career interests. LinkedIn also provides members the opportunity to request performance-related feedback from current or former employers, including managers and superiors, who also are LinkedIn members. Understandably, supervisors who receive such solicitations may feel obligated to respond favorably in order to avoid possible embarrassment for the employee or themselves in a public setting; however, before responding to such requests, supervisors should understand that a decision whether or not to provide this type of positive feedback could have negative consequences in the employment setting.

For example, a manager who comments favorably regarding a subordinate's work on LinkedIn may be accused of contradicting possibly less favorable reviews of the subordinate's performance made in a confidential evaluation completed at work. If the employer subsequently were to take an adverse employment action against the employee, the employee could point to the arguably inconsistent statements as circumstantial evidence that the adverse action was not supported by a legitimate business reason, but rather was taken because of unlawful discrimination or in retaliation for protected activity. While the employer certainly could correct any misimpression caused by the favorable comment, the employee certainly will argue that any inconsistency between the LinkedIn comment and the performance evaluation creates an issue of fact precluding summary disposition of the employee's claims. To avoid this risk, employers may wish to consider adopting policies which preclude managers from providing recommendations for current or former employees on social networking websites such as LinkedIn.

Modifying the employer's social networking policy would create consistency with more traditional human resources policies that frequently preclude managers from responding directly to requests for letters of recommendation from former employees. Traditional policies typically provide that all requests for letters of recommendation must be forwarded to the company's human resources department, which, in turn, responds with information limited to the employee's dates of employment, positions held and final salary. Thus, prohibiting direct responses by supervisors on LinkedIn would make the employer's social networking policy consistent with longstanding approaches to requests from former employees for letters of recommendation.

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Harassment Claims

Employers should be aware that employees' use of social networking sites may increase an employer's risk of being subjected to harassment claims. Because communications through social networking sites allow for impersonal, "non-face-to-face" interaction, individuals may not perceive that their electronic communications are subject to the usual guidelines governing appropriate professional conduct. Employees also may become emboldened by their pseudo-anonymity to act in ways they otherwise would not – in essence taking on a new personality.[3] Likewise, a lack of established guidelines governing the new methods for communication provided by social networking sites also may contribute to an increased risk of inappropriate employee behavior. For example, a Facebook "poke" causes an alert to be sent to the recipient notifying them they have been "poked" along with the identity of the sender. The inherent ambiguity in a Facebook "poke" may actually foster its impermissible overuse. In 2009, a Tennessee woman was arrested and jailed after violating an order of protection – which prohibited communications with another woman – after she used Facebook to "poke" the protected individual.[4]

Although courts have yet to address this issue in the employment context, employers should be aware that communications occurring through social networking sites can, under certain circumstances, rise to the level of harassment. Employees will almost certainly argue that unwanted contact by supervisors or co-workers may satisfy the elements of a hostile work environment claim, requiring that the workplace be "permeated with discriminatory intimidation, ridicule, and insult . . . that is sufficiently severe or pervasive to alter the conditions of the victim's employment."[5] Courts have recognized that "even a single episode of harassment, if severe enough, can establish a hostile work environment."[6] Employers may argue that they were not on notice of such events, or that co-workers were engaged in private, off-work activity when they communicated on social networking websites. However, circumstances conceivably could arise where such conduct could spill into the workplace. Imagine the reaction of an employee if a co-worker posts exceedingly graphic pictures and/or comments about a fellow employee on a social networking website. After an employee complains to the employer about such conduct by a co-worker, the employer may have no choice but to react, whether or not the conduct rises to the level of unlawful sexual harassment.

Motivated by similar concerns, a number of states have introduced legislation that provide penalties for sexually offensive or harassing

communications perpetrated through social networking sites. *See, e.g.*, Social Networking Safety Act, H.R. 3757, 213th Leg. (N.J. 2009); Online Harassment, TEX. PENAL § 33.07 (2009); H.R. 1427, 95th Leg. (Miss. 2010). Given the legislative concern regarding harassment perpetrated through social networking sites, employers may assume that similar issues arise in the workplace and should consider revising their harassment policies accordingly.

Recruitment Practices

As we noted in our article in the Fall 2009 newsletter, a huge number of employers are using social networking websites to screen job candidates. We emphasized the need for employers who use social networking websites in this manner to take care to avoid applying varying selection criteria based on sex. Since our last column, commentators have identified additional risks from using social networking websites arising solely from variation in the use of social networking sites by individuals in different demographic categories. For example, a recent study shows that both Caucasians and Asians are overrepresented on Facebook and LinkedIn relative to the Civilian Labor Force, as defined by the U.S. Census, while Hispanics are disproportionately underrepresented on both sites, and African Americans are underrepresented on LinkedIn.[7] Additionally, individuals between the ages of 18-34 are overrepresented on Facebook but underrepresented on LinkedIn, while individuals over age 50 are underrepresented on Facebook and overrepresented on LinkedIn. Finally, women have been shown to be overrepresented on Facebook while men are conversely underrepresented on Facebook relative to the Civilian Labor Force. While employers could argue that a comparison between the demographics of the Civilian Labor Force and the usage of social networking websites is inappropriate for particular occupations, certainly any such discrepancies may influence employers to consider carefully the extent to which they will use social networking websites for screening potential job applicants.

Employers who are contemplating whether to use social networking sites as a sole basis for recruiting may wish to analyze whether they may be excluding qualified individuals who do not have access to or who elect not to use social networking technology. Employers may avoid such risks by using multiple recruitment methods in addition to recruitment through social networking sites.

Negligent Hiring

An employer's use of an employee's information posted on a social networking website could establish a basis for persons injured by the employee in the course of employment to argue that the employer is liable for negligent hiring and/or retention. "A cause of action for negligent hiring or retention requires allegations that the employer 'knew or should have known of the employee's propensity to commit injury,' or the employer failed to investigate a prospective employee notwithstanding knowledge of 'facts that would lead a reasonably prudent person to investigate that prospective employee.'"[8] Accordingly, if an employer read information on a job candidate's social networking site that could subsequently constitute evidence of a "propensity to commit injury," and the candidate subsequently injures another person, the injured person may seek to hold the employer liable for negligent hiring or retention.

Among the challenging issues that arise from this hypothetical fact pattern is the question of exactly how employers can identify information that demonstrates a "propensity to commit injury." For example, one can imagine that employers could be faced with having to decide whether the questionable remarks were said truthfully or in jest–and more importantly, how a court would view such information. One possible way to avoid this issue is for employers to define precisely the nature of the information recruiters or other human resources personnel will seek to obtain from an employee's social networking website, and affirmatively state that no other information will be sought or considered. Another prophylactic measure is for employers to separate those who will actually access the employee's social networking website from those responsible for making potentially adverse employment decisions regarding the employee. In that way, those making decisions should not be charged with knowledge of any potentially questionable information.

Practice Pointers

As we noted in our article in the Fall 2009 newsletter, growing numbers of employers are visiting prospective and current employees' social networking websites in connection with employment. However, as employers weigh the pros and cons of using social networking websites for this purpose, some employers might opt to refrain completely from visiting such websites. Other employers who choose to visit candidates' social networking sites or otherwise use such sites for recruiting purposes should, at the very least, educate themselves about the risks discussed above and in our previous article, and consider taking prophylactic measures to mitigate any such risks.

In addition to the guidelines we provided in our Fall 2009 *Employer Update* article, employers also may consider adopting policies:

- prohibiting supervisors from evaluating, recommending or otherwise commenting on subordinates' job performance on social networking sites such as LinkedIn;
- cautioning employees that they may be subject to discipline up to and including discharge for harassing, intimidating or demeaning co-workers or customers on social networking websites;
- directing human resources staff not to rely exclusively on social or professional networking sites to recruit candidates, and, if such sites are used, to do so in conjunction with a variety of other recruitment methods that encompass a broad range of sources;
- setting up a procedure that will define what personnel are authorized to access a job candidate's or an employee's social networking website for employment purposes, and defining precisely the categories of information the employer will seek to obtain from the social networking website; and
- directing that when managers do refer to employees' social networking websites for employment purposes, they comply with all employment policies and practices of the employer, including the duty to report to management any information about an employee that may reflect a propensity by the employee to injure others.

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1 Recruiting Trends, *Social Media Program for Human Resources*, http://www.recruitingtrends.com/social-media-program-for-human-resources (November 2, 2009).

2 Jeffrey S. Klein & Nicholas J. Pappas, *Legal Issues Arising out of Employees' Use of Social Network Websites*, N.Y.L.J., October 5, 2009, P. 3, Col. 1 (reprinted in the *Employer Update*, Fall 2009, P.2, Col 1).

3 *See* Helen Johnstone, *Who's That Hiding Behind the Screen?: Some People Undergo a Real Change When They Logon*, The Independent, August 28, 1995, available at http://www.independent.co.uk/life-style/whos-that-hiding-behind-the-screen-1598407.html.

4 Ki Mae Heussner, *Tennessee Woman Arrested for Facebook 'Poke,'* ABC News, October 12, 2009, available at http://abcnews.go.com/Technology/AheadoftheCurve/tennessee-woman-arrested-facebook-poke/story?id=8807685.

5 *Harris v. Forklift Sys. Inc.*, 510 U.S. 17, 21 (1993) (citation and internal quotations omitted).

6 Jeffrey S. Klein & Nicholas J. Pappas, *'Jones v. Clinton': An Emerging Trend in Title VII Law*, N.Y.L.J., June 1, 1998, P. 3, Col. 1 (quoting *Torres v. Pisano*, 116 F.3d 625, 630-31 (2d Cir. 1997)).

7 Stephanie R. Thomas, *Using Social Media for Recruiting? Beware Disparate Impact Claims*, February 9, 2010. Specifically, Hispanics comprise 13% of the Civilian Labor Force but only 5% of Facebook users and 2% of LinkedIn users. Individuals aged 50 and above amount to 29% of the Civilian Labor Force but only 13% of Facebook users and 33% of LinkedIn users. Women comprise 46% of the Civilian Labor Force but represent 55% of Facebook users.

8 *Sheila C. ex rel. Doe v. Povich*, 768 N.Y.S.2d 571, 580 (N.Y. App. Div. 2003).

Independent Contractor Classification: Two Strategies for Handling Increased Enforcement by the DOL and IRS

By Patricia Wencelblat

The United States Department of Labor ("DOL") and the Internal Revenue Service ("IRS") have recently begun a well-publicized crackdown on businesses that misclassify employees as independent contractors. President Obama's federal budget for the upcoming fiscal year includes $117 billion for the DOL, and expressly sets aside $25 million to help combat employee misclassification. This increased funding will be used to hire investigators and enforcement staff. Additionally, the IRS has begun auditing 6,000 companies to determine whether they are in compliance with laws regarding worker classification. President Obama's 2010 budget estimates that this increased enforcement will net at least $7 billion over 10 years.

The consequences for employers of worker misclassification can be significant, as damages may include overtime and minimum wage back pay with interest, liquidated damages, benefits, worker's compensation premiums and taxes that were never withheld or paid.

In light of this increased focus on worker classification, there are two distinct strategies employers may and should pursue to defend their independent contractor classifications: (1) focus on the traditional analyses utilized by the DOL and the IRS to ensure that working relationships with independent contractors fall outside of these parameters; or (2) attempt to shift the analytic paradigm either through litigation or negotiation with the DOL and/or IRS, a strategy that has proven to be effective to date for FedEx Home Delivery ("FedEx"). A business's failure to fit independent contractor positions into either one of these two strategies, or to otherwise come into compliance, could lead to significant liability either from the DOL, IRS or a private lawsuit.

Ensure Compliance Using Traditional Analyses

The DOL and the IRS use different tests for determining worker classi-

fication, but there is much overlap between the two analyses. The DOL test is commonly referred to as the "Economic Realities Test" and seeks to determine whether the workers are economically dependent on the putative employer, or whether the contractors are truly in business for themselves. The Economic Realities Test looks at numerous factors as a whole, and no one factor is dispositive. The factors considered to be significant under the Economic Realities Test are:

1. The extent to which the services rendered are an integral part of the principal's business.
2. The permanency of the relationship.
3. The amount of the alleged contractor's investment in facilities and equipment.
4. The nature and degree of control by the principal.
5. The alleged contractor's opportunities for profit and loss.
6. The amount of initiative, judgment or foresight in open market competition with others required for the success of the claimed independent contractor.
7. The degree of independent business organization and operation.

The IRS test is commonly referred to as the "Right-To-Control Test," because each factor is designed to evaluate who controls how work is performed. The more control a company exercises over how, when, where and by whom work is performed, the more likely the IRS would find that the workers are employees, not independent contractors. IRS Revenue Ruling 87-41 contains factors, referred to as the twenty common law factors, that assess whether or not a business has the right to direct and control the actions of the worker. Although this revenue ruling remains valid today, more recently, the IRS has grouped the factors into three main categories of evidence that show whether a worker is an employee or an independent contractor:

1. Behavioral control;
2. Financial control; and
3. The relationship of the parties.

The Behavioral Control element examines the degree of control the business has over the worker. The key issues for behavioral control are instructions and training; if the worker controls the method by which a project gets done, the relationship looks more like that of an independent contractor. In evaluating this factor, the IRS also looks to (1) the degree of instruction, as more detailed instruction is indicative of an employer/employee relationship; (2) whether the workers are subject to an evaluation system, however, if an evaluation system just measures the end result, rather than the details of how work is performed, this is not indicative of an employment relationship; and (3) whether the business provides the worker with training on how to do the job. The most important factor of the behavioral element is whether the business retains the right to control the worker and the details of how the services are performed, regardless of whether the business actually exercises that right.

The Financial Control element refers to whether or not the business has the right to direct and control the financial aspects of the worker's job, and examines whether the worker has the ability to make additional profit if the worker can control expenses and other efficiencies. The key indicia of financial control include (1) whether the worker has made a significant financial investment in equipment; (2) whether the worker is reimbursed for expenses; (3) whether the worker has the opportunity to increase profits or suffer a loss; (4) whether the worker's services are available to the market; and (5) the business's method of payment to the worker, *i.e.*, flat fee or hourly.

Finally, the Relationship element examines whether certain elements are present in the type of relationship between the two parties. For example, whether there is a written contract, whether benefits are provided, the permanency of the relationship and whether the services provided are a key activity of the business.

Businesses should be particularly attune to situations where independent contractors are indistinguishable from employees.

With both the DOL and the IRS analyses, there is no one factor that takes precedence over the others. Rather, both agencies look at the whole relationship to determine the proper classification of the workers at issue. Given these analyses, businesses should focus on the "duck test" to determine a worker's status: if it looks like a duck, walks like a duck and sounds like a duck, it's a duck. Likewise, if it looks like an employee, walks like an employee and sounds like an employee, it's probably an employee. Businesses should be particularly attune to situations where independent contractors are indistinguishable from employees. For example, when independent contractors perform the same tasks or work in the same office with the same equipment as employees.

Businesses may want to carefully assess their working relationships with independent contractors using the factors highlighted above. If workers fall within the DOL or IRS definitions of "employees," employers may reclassify the workers as employees going forward and make sure to withhold all necessary taxes, comply minimum wage and overtime regulations and include the employees in all relevant benefit plans. Alternatively, employers may restructure the working relationship, for example by limiting the control exerted over the workers, to reduce the likelihood that either agency would consider the worker to be an employee. Businesses should also pay particular attention to the duration of their relationship with independent contractors. A long-term independent contractor who works solely for one business is likely to be viewed as an employee, whereas a long-term contractor who provides services to many business on the open market is more likely to be classified as an independent contractor. Should a business not be able to defend the independent contractor status of workers, and not be amenable to hiring these workers as employees, such businesses may want to consider hiring workers through an agency and insuring that the agency pays all required taxes and wages.

Shifting The Analytical Paradigm

Alternatively, for those employers whose business models rely on independent contractors, and who may not be able to restructure their working relationships with the independent contractors to fall comfortably within the traditional classification analyses, it may be worthwhile to litigate or otherwise persuade the DOL and/or IRS that the workers are properly classified as independent contractors by attempting to shift the analyses used by the DOL and/or IRS. Such a strategy has been successful to date for FedEx. In late 2007, the IRS issued a $319 million assessment against FedEx for back taxes and penalties for misclassification of its drivers in 2002. However, FedEx appealed this decision, and in 2009, the IRS reversed the 2007 decision and determined that FedEx did not owe any penalties for 2002. The IRS also later determined that FedEx did not owe any taxes or penalties for 2004-2006, and FedEx does not anticipate any additional audits from the IRS.

The "Entrepreneurial Opportunity" test provides another way for businesses to structure relationships with individuals to justify the independent contractor classification.

Additionally, in a recent decision, the D.C. Circuit accepted FedEx's argument, and issued a decision that can be interpreted as abandoning the "Right to Control" test in favor of an "Entrepreneurial Opportunity" analysis. *See FedEx Home Delivery v. National Labor Relations Board*, 563 F.3d 492 (D.C. Cir. 2009). It should be noted that although the litigation before the D.C. Circuit addressed the classification of workers for the purpose of determining their right to bargain as a union with FedEx, the common-law agency test utilized by the Court is similar to the factors used by the DOL and the IRS to determine the employment classification of a worker.

Significantly, the D.C. Circuit focused on the degree to which the FedEx delivery driver position "presents the opportunities and risks inherent in entrepreneurialism," instead of the traditional focus on the right to exercise control over the workers. Id. at 497. The Court noted that the drivers sign an independent contractor agreement, which states that FedEx may not prescribe the hours worked, whether or when the drivers take breaks, what routes they follow or other details of performance. *Id*. at 498. Additionally, the drivers had to provide their own vehicles, were responsible for the costs associated with maintaining those vehicles and could use the vehicles for other commercial or personal uses. *Id*. at 498-99. Drivers could also independently incorporate, negotiate with FedEx for higher fees, contract to serve multiple routes or hire their own employees for their single routes and could assign their contractual rights to their routes without FedEx's permission. *Id*. at 499.

The D.C. Circuit described its analysis as retaining the common-law test, but with a shift in emphasis towards entrepreneurialism. *Id*. at 503. And under this shift, the Court placed significant weight on the drivers' ability to own and transfer the proprietary interest in their routes. *Id*. The Court found the indicia of control emphasized by the NLRB, such as requiring drivers to wear a uniform and display a FedEx logo, to be unpersuasive because of the specific type of service FedEx provided. *Id*. at 500-01. The drivers at issue in the litigation delivered small packages to residential customers, and the control FedEx exercised was intended to satisfy customers' concerns regarding safety, not as a means of controlling the drivers, and that such constraints do not determine the employment relationship. *Id*. at 501. The Court looked at the working relationship as a whole, and because of the entrepreneurial nature of the position, concluded that the drivers were correctly classified as independent contractors.

While it is not clear if courts will follow the D.C. Circuit's line of reasoning, the "Entrepreneurial Opportunity" test provides another way for businesses to structure relationships with individuals to justify the independent contractor classification. Businesses interested in following this route (no pun intended) should focus on providing their workers with legitimate and real opportunities for profit and loss, even if this results in some loss of control over the workers or the performance of the services. For example, businesses should allow for some form of entrepreneurialism and the contractor's ability to increase profit, as the D.C. Circuit focused on the FedEx drivers' ability to sell their contractual rights without any approval. Such entrepreneurialism may take many different forms while still providing business with the ability to argue that such workers are correctly classified as independent contractors. For example, business may require the workers invest significantly in equipment necessary to perform the work, and allow those workers to use that equipment for other purposes, or allow independent contractors to hire their own staff or sub-contractors to complete projects for a business.

Conclusion

The increased enforcement efforts of the DOL and the IRS with regard to the misclassification of workers as independent contractors raise significant risks for businesses that retain independent contractors. However, the recent decision by the D.C. Circuit may provide an alternative argument, in additional to the traditional analyses, to justify the classification of workers as independent contractors. Finally, should a business find that its relationship with an independent contractor cannot satisfy either the traditional test or the entrepreneurial alternative analysis, the business should consider hiring such workers as employees or utilizing an agency to ensure compliance with all requisite laws and regulations.

Individual Managers and Supervisors May Be Subject to Personal Liability Under the FMLA

by Philip F. Repash

In *Narodetsky v. Cardone Industries Inc.*,[1] a Pennsylvania federal district court recently ruled that a plaintiff could proceed with his claim under the Family and Medical Leave Act of 1993 ("FMLA" or the "Act") against a former employer and several individually named managers and supervisors, based on allegations that each participated in a scheme to terminate plaintiff's employment after learning that he had requested medical leave. The FMLA generally requires employers to allow eligible employees to take up to 12 weeks of unpaid leave for certain family and/or medical reasons. The recent *Narodetsky* case is significant because it highlights a growing split in authority among the federal district courts as to whether the FMLA imposes personal liability upon individual managers and supervisors, including those who are not corporate officers. No federal court of appeals has yet directly considered this question, and the federal district courts that have addressed the issue, as discussed below, have reached sharply conflicting results.

Factual Background

Plaintiff Narodetsky worked as a tool designer for twelve years for Cardone Industries in Philadelphia, Pennsylvania. In August 2009, Narodetsky learned that he needed leg surgery. Narodetsky and his wife allegedly contacted Cardone's human resources department to schedule FMLA medical leave and to request that Narodetsky be placed on short-term disability during the leave period.

Narodetsky alleges that, shortly after communicating his leave requests, company managers conducted a forensic search of his work computer in an effort to find pretextual grounds to terminate his employment, thereby obviating the need to grant him FMLA leave. On September 9, 2009, prior to commencing his medical leave, Narodetsky was called into a meeting by certain of the defendants and confronted with a pornographic email that was allegedly forwarded by him from his work computer to a co-worker about a year earlier. Narodetsky was then summarily fired.

In response, Narodetsky filed suit in the United States District Court for the Eastern District of Pennsylvania against the company and five individually named managers and supervisors. In his complaint, Narodetsky alleged that each of the defendants played some role in orchestrating and carrying out a plan to terminate his employment in violation of the FMLA. The five individually named defendants included the CEO and president of the company, a human resources representative, a benefits manager, an acting director of human resources

and the plant manager. Only the CEO and president was alleged to be a corporate officer. The individually named defendants moved to be dismissed from the case on the ground that Narodetsky failed to plead sufficient facts in his complaint to establish that any of them was the "employer," as that term is defined under the FMLA.

Individual Liability Under the FMLA

The FMLA makes it "unlawful for any employer to interfere with, restrain, or deny the exercise of or the attempt to exercise, any right provided for" in the Act. 29 U.S.C. section 2615(a)(1). The FMLA defines "employer" as "any person who acts, directly or indirectly, in the interest of an employer to any of the employees of such employer." 29 U.S.C. section 2611(4)(A)(ii)(I). The FMLA's implementing regulations explain that "individuals such as *corporate officers* 'acting in the interest of an employer' are individually liable for any violations of the requirements of FMLA." 29 C.F.R. § 825.104(d) (emphasis added).

The federal district courts have expressed conflicting views over whether individual managers and supervisors are subject to personal liability under the FMLA. Several courts, including in Utah, Kansas and Maine, have held that individual liability under the Act may extend to individuals such as corporate officers, but not to lower-level managers or supervisors.[2] Other federal district courts, including in New York, Illinois and New Jersey, have ruled that *all* individuals, regardless of their status within a corporate hierarchy, may be subject to personal liability under the Act if they controlled, in whole or in part, the ability of an employee to exercise protected rights under the Act.[3] Finally, at least one federal district court has held that the FMLA does not provide for individual liability at all, construing the Act in accordance with other federal employment statutes such as Title VII.[4]

Managers and supervisors should understand that interference with and/or retaliation against an employee for exercising his or her FMLA rights could result in potential liability not only for the company but also for themselves, individually as managers and supervisors.

In concluding that the individual managers and supervisors could face personal liability under the FMLA, the *Narodetsky court* stated that, in construing the allegations in the light most favorable to plaintiff, the complaint adequately alleged that each of the individual defendants had exerted some control over Narodetsky's FMLA rights, including the ability to fire him and to deny his request for medical leave. The court added that, while mere conclusory allegations of such control in a complaint do not state a claim, Narodetsky had alleged sufficient facts to justify the individual defendants' continued inclusion in this case. Addressing the conflicting federal court decisions holding that individual liability can extend only to individuals such as corporate officers (or that individual liability is not provided for by the FMLA), the court acknowledged that the Third Circuit Court of Appeals had not yet ruled on the issue, but summarily rejected those conflicting authorities as not being "in accordance with the case law in this circuit," citing several past Pennsylvania and New Jersey district court decisions.

Conclusion

In light of the *Narodetsky* decision, and unsettled state of the law on this question generally, employers should ensure that all supervisors and managers obtain adequate FMLA training. Managers and supervisors should understand that interference with and/or retaliation against an employee for exercising his or her FMLA rights could result in potential liability not only for the company but also for themselves, individually as managers and supervisors. Employers also should review their insurance agreements to determine whether individual managers' and supervisors' legal expenses and liabilities are covered in the event they are named, along with the company, in an FMLA lawsuit.

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1 No. 09-4734, 2010 U.S. Dist. LEXIS 16133 (E.D. Pa., Feb. 24, 2010).

2 *See Stuart v. Regis Corp*., No. 05-0016, 2006 U.S. Dist. LEXIS 46719, at *20 (D. Utah July 10, 2006) ("Individuals who have no corporate role beyond a managerial position are not employers under the FMLA."); *Williamson v. Deluxe Fin. Servs*., 2005 U.S. Dist. LEXIS 15293, No. 03-2358-KHV, 2005 WL 1593603, at *9 (D. Kan. July 6, 2005) (both supervisor and human resources manager did not have sufficient responsibility or stature within company to warrant imposition of personal liability under FMLA); *Brunelle v. Cytec Plastics, Inc*., 225 F. Supp. 2d 67, 82 (D. Me. 2002) (holding that "even though [individual front-line supervisor] arguably had personal responsibility for making decisions that contributed to the alleged denial of leave . . . he simply was not a prominent enough player in [company's] operations to be considered an 'employer' for purposes of the FMLA"); *Keene v. Rinaldi, 127* F. Supp. 2d 770, 777 n.3 (M.D.N.C. 2000) ("FMLA [not] intended to impose liability on mere supervisory employees as opposed to owners, officers, etc.") (citation omitted).

3 *See Freemon v. Foley*, 911 F. Supp. 326, 331 (N.D. Ill. 1995) (holding that "the FMLA extends to all those who controlled 'in whole or in part' [the plaintiff's] ability to take a leave of absence and return to her position"); *see also Richardson v. CVS Corp*., 207 F. Supp. 2d 733, 744 (E.D. Tenn. 2001) (finding plaintiff presented sufficient evidence to deny defendant's summary judgment motion on claim for individual liability of district manager); *Mercer v. Borden*, 11 F. Supp. 2d 1190, 1191 (C.D. Cal. 1998) (holding plaintiff's complaint stated a valid claim for individual liability against lower level managers who allegedly violated the FMLA); *Bryant v. Delbar Products, Inc*., 18 F. Supp. 2d 799, 808 (M.D. Tenn. 1998) (holding that manufacturing manager may be

individually liable because he acted "directly or indirectly" in the corporation's interest and had the authority to grant plaintiff leave); *Holt v. Welch Allyn, Inc.*, No 95-1135, 1997 WL 210420, at *2 (N.D.N.Y. Apr. 15, 1997) (same); *Johnson v. A.P. Products, Ltd.*, 934 F. Supp. 625, 628 (S.D.N.Y. 1996) (same, but granting defendant's motion to dismiss where complaint did not allege that human resources manager "exercised any control over [plaintiff's] ability to take a leave of absence or her termination").

4 *See, e.g., Carter v. Uniform Rental Serv. Of Culpepper, Inc.*, 977 F. Supp. 753, 759 (W.D. Va. 1997) (FMLA intended to track Title VII and other similar federal employment statutes and not allow for liability against individuals); *Frizzell v. Southwest Motor Freight, Inc.*, 906 F. Supp. 441 (E.D. Tenn. 1995) (same); *but see Holt v. Welch Allyn, Inc.*, 95-CV-1135, 1997 U.S. Dist. LEXIS 5896, at **7-8 (N.D.N.Y. Apr. 15, 1997) ("The definition of employer in the FMLA is unlike the definition of employer in Title VII but tracks the definition of employer in the [Fair Labor Standards Act ("FLSA")]. . . . Under the FLSA, the term employer has been 'interpreted to include individuals with substantial control over the aspect of employment alleged to have been violated.' . . . Therefore, applying this same definition to the FMLA results in liability being extended 'to all those who controlled in whole or in part [plaintiffs'] ability to take . . . leaves of absence and return to [their] positions.'").

Applying New York's Faithless Servant Doctrine, Massachusetts High Court Orders Former Employee to Repay $6.8 Million

By Daniel J. Venditti

Under New York law, a century-old legal rule permits employers to recover compensation paid to (or to withhold compensation from) employees who have engaged in certain types of misconduct during their employment. Drawing on traditional principles of agency and fiduciary responsibility, New York courts have held that so-called "faithless servants"–those who have acted disloyally or dishonestly–must forfeit their compensation earned during the entire period of their misconduct. For the faithless employee, application of this rule can be harsh, as demonstrated by a recent decision of the Supreme Judicial Court of Massachusetts. In *Astra USA, Inc. v. Bildman*, Massachusetts's highest court, applying New York law, ordered a former CEO of a pharmaceutical company to forfeit $6.8 million in salary and bonuses that he was paid during a six-year period of misbehavior.[1] This ruling should be a reminder to New York employers and employees of this potent remedy available against employees who betray their employer's trust.

New York's Faithless Servant Doctrine

Under New York law, all employees owe a duty of loyalty to their employer. This means employees must at all times act in their employer's best interest. Imposition of this duty protects employers from a host of employee misconduct to which the employer is vulnerable by placing its employees in a position of trust. For example, employees may not (1) privately profit from the activities they perform on behalf of their employer; (2) use their employer's confidential information for their own benefit or to the detriment of their employer; (3) divert corporate opportunities or income to themselves; or (4) compete with their employer. Under New York's faithless servant doctrine, an employee who breaches his duty of loyalty forfeits the right to any compensation for services during the period of misconduct.[2] Forfeiture may be appropriate even where the employer did not suffer any provable damages because of the employee's misbehavior.

The faithless servant doctrine applies only to pervasive misconduct that is related to the material aspects of the employee's employment. A one-time disloyal act, routine on-the-job performance failures and even criminal or tortious behavior (if unrelated to the employee's core responsibilities) usually will not suffice. These types of misconduct might properly result in discharge, civil damages or criminal fines or penalties, but in most cases will not result in forfeiture of compensation under the faithless servant doctrine.[3] As stated by a New York court in the early 20th century:

> While the failure to devote his entire time to the business or to use his best endeavors in the prosecution of the business or occasional acts of disloyalty might constitute breaches of his contract of employment sufficient to justify a discharge they would constitute no defense to an action for compensation if the plaintiff performed the essential part of his contract. . . . [But where] the employer alleges facts sufficient to show dishonesty and disloyalty on the part of his employee which permeates the employee's service in its most material and substantial part, the employee cannot recover the agreed compensation; for he has failed essentially to give the stipulated consideration for the agreed compensation, and is asking for pay for his own wrongdoing.[4]

Accordingly, courts have imposed a forfeiture against employees who engaged in competition with their employer while still employed, diverted corporate opportunities, stole clients and misappropriated royalty

checks.[5] On the other hand, courts have refused to impose a forfeiture under the faithless servant doctrine in connection with conduct unrelated to the performance of the employee's responsibilities, such as "routine" terminations for harassment or credit card fraud.[6]

Astra USA, Inc. v. Bildman

In *Astra v. Bildman,* the Massachusetts Supreme Judicial Court considered New York's faithless servant doctrine as it applied to a former executive who engaged in an egregious campaign of misconduct during his tenure with a Massachusetts-based pharmaceutical company. Bildman became president and CEO of Astra in 1981. In 1996, Bildman was suspended pending an investigation of allegations that he had sexually harassed female Astra employees. The investigation revealed widespread abuse of Bildman's authority and company resources, including (1) sexual harassment of several female Astra employees; (2) threatening employees who cooperated with the investigation; (3) removal and destruction of company documents and records; (4) use of company funds to pay for various personal expenses, including contracting and landscaping work on multiple homes, chartered yacht excursions, female escort services and $16,000 in legal fees he incurred fighting a $60 speeding ticket; and (5) use of Astra employees, on company time, to provide private tennis lessons to his family and service his antique car collection.[7]

In June 1996, Astra terminated Bildman's employment for cause, and the company later entered into a consent decree with the EEOC that established a $9,850,000 fund to compensate Bildman's victims of sexual harassment. Astra then sued Bildman. After a trial, a jury found Bildman liable under various theories of recovery, including fraud, conversion and breach of fiduciary duty based on Bildman's improper use of funds and certain statements he made (or failed to make) to Astra's board in connection with the allegations of harassment against him. The jury awarded Astra more than $1,000,000 in damages on these claims. The jury also made separate findings that Bildman sexually harassed Astra's female employees and retaliated against those who complained about it, although no additional damages were awarded based on these separate findings.

New York's faithless servant doctrine is unique in its requirement for complete forfeiture of all compensation during the period of disloyalty.

In a post-trial motion, the court considered Astra's request for forfeiture of all of Bildman's compensation based on New York's faithless servant doctrine. Astra sought the return of Bildman's salary and bonus payments from 1991 to 1996. Purporting to apply New York's faithless servant doctrine, the trial court held that Bildman had been faithless, but *did not* direct him to forfeit his pay because the court found that Astra failed to establish that the compensation it paid to Bildman exceeded the value of the benefit of his legitimate services.[8] Under Massachusetts law, this would have been proper. Like New York, Massachusetts recognizes a forfeiture rule. However, under Massachusetts's law, the court must consider the value of the employee's services, and can impose a forfeiture only to the extent that the compensation received exceeded the value of those services. This error by the trial court led to a reversal. Under New York law, having found Bildman to be a faithless servant, the trial court's only course was to order a *complete* forfeiture of the compensation Bildman received during the six-year period of his disloyalty. The court ordered Bildman to repay $5,599,097 in salary and $1,180,000 in bonuses.

Astra v. Bildman is noteworthy because it demonstrates how powerful a tool the doctrine can be for an employer in remedying the misconduct of a faithless servant. In addition to the $1,000,000 civil verdict against him, Bildman was required to pay back approximately $6,800,000 in salary and bonuses he collected over a six-year period. The case also raises interesting questions about whether and to what extent the faithless servant doctrine can be applied based on an employee's sexual harassment or other acts of employment discrimination. The difficulty for an employer seeking a forfeiture under those circumstances would be establishing that engaging in harassment or discrimination was a betrayal in connection with the "most material and substantial part" of the employee's service. An employer also would need to overcome the fact that, although New York courts have not defined the outer boundaries of the faithless servant doctrine, most applications involve some sort of economic self-dealing.[9] Moreover, as discussed above, a federal court in New York has stated that "routine" sexual harassment does not support a faithless servant claim.

But what constitutes "routine" harassment? Is it routine if, as the court in *Astra* found, a top executive

uses the company "as his sexual fiefdom, in the process driving away employees, creating a corrosive corporate atmosphere" and leading to months of bad publicity?[10] The *Astra* case does not provide a clear answer to the question of whether employment harassment or discrimination would be a sufficient basis upon which to impose a forfeiture. Although Bildman did engage in sexual harassment, there was substantial evidence that Bildman diverted corporate assets for his own personal use, which clearly falls within the core of a traditional breach of a fiduciary's duties. Even though Bildman engaged in severe harassment, it is not clear whether or how much of the forfeiture was attributed, if any, to that harassment as opposed to Bildman's financial transgressions against his employer.

Choice of Law Issues

New York is not the only state to recognize a forfeiture remedy based on an employee's misconduct. New York's faithless servant doctrine is, however, unique in its requirement for complete forfeiture of all compensation during the period of disloyalty. As interpreted by the Second Circuit Court of Appeals, there is no restriction in New York that the forfeiture be limited to compensation that was earned in connection with the misconduct, nor any requirement for a court to consider the nature or severity of the employee's breach. Other states that recognize a forfeiture remedy take a more restrictive approach. For example, as discussed above, Massachusetts rejects the "extreme remedy" of complete forfeiture. Under Massachusetts law, a disloyal employee may be required to forfeit only that compensation which exceeds the value of his services to his employer.[11]

Because of the variation among state laws, employers should remain mindful of the choice-of-law rules in the jurisdictions in which they do business. Absent an express agreement providing otherwise, the decision of which forfeiture rule to apply will be made based on local choice-of-law rules. In *Astra v. Bildman*, New York law applied because, when considering the "internal corporate affairs" of a corporation, Massachusetts will apply the law of the state where the business was incorporated, which, in that case, was New York.[12] Employers, therefore, may wish to include a choice of law provision in their employment contracts and employee handbooks that explicitly invokes the application of New York law to the employment relationship.

***Astra v. Bildman* demonstrates how powerful a tool the doctrine can be for an employer in remedying the misconduct of a faithless servant.**

Retaliation

Because of the strict application of New York's faithless servant doctrine and the harshness of its remedy, employers may be tempted to respond to an employee's accusation of wrongdoing with a charge of faithlessness. As with any employer accusation against an employee, employers must take care to ensure their accusation of disloyalty is well-grounded in fact. Otherwise, the accusation may serve as the basis of a claim of retaliation, especially if the faithless servant claim arises for the first time as a counterclaim in litigation.[13]

Certainly, there are non-retaliatory reasons why an employer might raise a faithless servant claim only in response to an employee's lawsuit, and not sooner, but employer-versus-employee counterclaims by their nature may appear to be retaliatory. However, employers should consider, in appropriate cases, the offensive and defensive use of the faithless servant doctrine in disputes with current or former employees.

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1 455 Mass. 116 (2009).

2 *See, e.g., Phansalkar v. Andersen Weinroth & Co.*, 344 F.3d 184, 200 (2d Cir. 2003); *Feiger v. Iral Jewelry, Ltd.*, 41 N.Y.2d 928, 928 (1977) (citing Restatement (Second) of Agency (1958), § 469); *Wechsler v. Bowman*, 285 N.Y. 284, 292 (1941); *Lamdin v. Broadway Surface Adv. Corp.*, 272 N.Y. 133, 138 (1936).

3 Other financial remedies distinct from forfeiture of compensation–for example, disgorgement of profits–might be available to an employer against a disloyal employee. *See, e.g., Gomez v. Bicknell*, 302 A.D.2d 107 (N.Y. App. Div. 2002).

4 *Abramson v. Dry Goods Refolding Co.*, 166 N.Y.S. 771, 773 (N.Y. App. Term 1917).

5 *See Bon Temps Agency, Ltd. v. Greenfield*, 212 A.D.2d 427 (N.Y. App. Div. 1995) (disloyal placement manager for staffing agency placed two of Agency's own employees in different positions, and performed services for a competitor agency); *Maritime Fish Prods., Inc. v. World-Wide Fish Prods., Inc.*, 100 A.D.2d 81 (N.Y. Sup. Ct. 1984) (employee "surreptitiously organized a competing corporation, corrupted a fellow employee, and secretly pursued and profited from one or more opportunities properly belonging to his employer"); *Pictorial Films, Inc. v. Salzburg*, 106 N.Y.S.2d 626 (N.Y. Sup. Ct. 1951) (employees fraudulently removed employer's files and instructed client to send royalty checks to them instead of to the employer).

6 *See Torres v. Gristede's Operating Corp.*, 628 F. Supp. 2d 447, 470-71 (S.D.N.Y. 2008) ("Nor can it be, as [the employer] apparently supposes, that every routine termination for sexual harassment or credit card fraud necessarily raises faithless servant claims.").

7 *Astra USA, Inc. v. Bildman*, 455 Mass. 116, 124 n.13 (2009).

8 There was no intermediate level appellate decision in *Astra*. The Supreme Judicial Court transferred the case to itself from the appellate court on its own motion.

9 One notable exception is *Colliton v. Cravath, Swaine & Moore LLP*, No. 08 Civ. 0400, 2008 WL 4386764, at *6 (S.D.N.Y. Sept. 24, 2008) (holding that faithless servant doctrine would apply where attorney was convicted of statutory rape and patronizing a prostitute).

10 *Astra USA, Inc.*, 455 Mass. at 136 n.30.

11 *See id.* at 133-34.

12 *See id.* at 119 n.4.

13 *See Torres v. Gristede's Operating Corp.*, 628 F. Supp. 2d 447, 474 (S.D.N.Y. 2008) (granting summary judgment in plaintiffs' favor on retaliation claim (citing *Bill Johnson's Restaurants v. NLRB*, 461 U.S. 731, 740 (1983))).

German Law Provides for Statutory Participation Rights of Employee Representative Bodies in Share and Asset Deals

By Stephan Grauke and Mareike Pfeiffer

The right to participate in an employer's decisions allows employee representative bodies to safeguard the interests of individual or groups of employees. Besides the unions, the most powerful employee representative bodies are the works councils that are granted considerable participation rights in measures taken by the employer impacting individual employees (*e.g.,* employment, relocation or termination), groups of employees or the entire workforce (*e.g.,* execution of so-called "operational changes" (such as closure, splitting or relocation of operations) or the introduction of flexible working time schemes).

The scope of these participation rights is primarily determined by the German Works Council Constitution Act (*Betriebsverfassungsgesetz*). Under this Act, a works council may be elected by the employees within and for each operational unit headed by a uniform management (*einheitlicher Leitungsapparat*), provided that at least five employees work for such unit. In addition to the operational level, an additional works council (i) must be established at the company level by the local works councils, in case several of the latter exist within the company (joint works council (*Gesamtbetriebsrat*)), (ii) may be established at the group level (group works council (*Konzern betriebsrat*)), and (iii) may be established at the European level if the company (or the group) employs at least 1,000 individuals within the European Community and/or 150 individuals in at least two different Member States (European works council).

If a company regularly employs more than 100 individuals, the Works Council Constitution Act requires the establishment of an economic committee (*Wirtschaftsausschuss*) at the company level by the works council(s). The economic committee is exclusively responsible for consulting with the employer on so-called "economic affairs" of the company.

Participation Rights in Asset Deals

In case of a sale of all of the assets of a company or certain assets forming an independent operational unit for labor law purposes, the transfer of an independent operational unit results in the transfer of all employees attributable to the respective company or unit to the purchaser of such assets by operation of law (Section 613a German Civil Code). As a consequence, the seller or the purchaser must inform each affected employee, in writing, of the proposed transaction and the consequences for the individual employee. In addition to this information obligation to the individual employee, there are participation rights of the employee representative bodies, which are described below.

Isolated Asset Deals

In determining the participation rights of employee representative bodies in asset deals, it is decisive whether the transfer of the operational unit is accompanied by so-called "operational changes" (such as the termination of employment contracts or the split-off of the assets to be acquired, for details see below).

Asset deals that are not accompanied by such operational changes are so-called isolated asset deals with respect to which the German Federal Labor Court ruled that an impending transfer triggers information and consultation obligations to the economic committee (if any), but no participation rights of the works council(s).[1] According to the ruling, the mere transfer of assets in an isolated asset deal without operational changes does not require the participation of the works council under the Works Council Constitution Act. In contrast to the economic committee, the works council is not assigned a general mandate for economic affairs by law. Thus, only the economic committee (if any) must be involved prior to execution of an asset deal. Such involvement must include (i) information consultation with the economic committee regarding the impending transfer of the company's assets/operational unit and (ii) consultation with the economic committee in this regard (*i.e.,* views must be exchanged), although the employer is not legally obligated to consider the proposals of the economic committee. The information provided to the economic committee must be correct, complete and comprehensive and must be submitted "in due time," which means that it has to be provided before the employer's "final" decision is made (*i.e.,* prior to the signing of a binding asset purchase agreement). In addition, relevant documents must be presented.

The violation of such participation rights may result in an administrative fine of up to EUR 10,000. However,

the economic committee cannot prevent execution of the intended asset deal.

Asset Deals Accompanied by Operational Changes

In practice, asset deals often involve "operational changes," such as:

- the splitting (*Spaltung*) or merger of operations to segregate the operational units to be purchased;
- the termination/mass lay-off of employees;
- the shutdown of an operational unit or material parts thereof;
- the relocation of operational units or material parts thereof;
- material changes of the organization, the purpose or the facilities of the operational unit; or
- the introduction of fundamentally new working methods or manufacturing processes.

If an asset deal is accompanied by such operational change, not only the economic committee must be involved, but also the responsible works council(s). Generally, the local works council(s) is responsible for negotiating a reconciliation of interest agreement and a social plan. In cases in which the employer maintains several operational units and the operational changes relate to at least two units, the joint works council is responsible. If the reorganization relates to operations of at least two different group companies, the group works council is responsible.

As mentioned above, the participation of the works council must include (i) provision of correct, complete and comprehensive information with respect to the operational change and the asset deal, (ii) consultations with the works council on the intended operational change and the asset deal, (iii) negotiation of a reconciliation of interest agreement with the works council (however, these negotiations must merely be conducted, a failure to reach agreement does not involve any consequences) and (iv) negotiation of a social plan.

A reconciliation of interest agreement sets forth the agreement with the works council as to the manner operational changes are to be implemented, whereas the social plan provides for financial compensation for the disadvantages an employee suffers as a consequence of the implementation of the operational changes. Compensation payments under social plans are generally calculated on the basis of the age of the individual employee, his/her period of service and his/her monthly salary. Additional payments are granted for employees with children, disabled employees and other hardships. The amount of such severance payments is not prescribed by law, but rather is subject to negotiation between the employer and the works council. Thus, the severance payments depend on local precedents, the negotiation power of the works council and past practice of the company and vary between industries and regions.

A violation of the participation rights of a works council may, according to rulings of certain labor courts, justify claims for a temporary injunction to stop implementation of the operational changes prior to the finalization of the negotiations of the reconciliation of interest agreement. Thus, the works council may delay (but not prevent) execution of the operational changes, which may also delay the asset deal. If an employer fails to negotiate a reconciliation of interest agreement with the works council, the employees are entitled to claim for statutory severance payments if their employment contracts are terminated due to execution of the operational changes or if they suffer any other economic disadvantages. The statutory severance payments are limited to an amount of 18 monthly salary payments, depending on the age of the employee and his/her period of service.

According to a judgment of the German Federal Labor Court in 2007,[2] reconciliation of interest agreements and social plans may also be negotiated with labor unions by way of a company-based tariff agreement (*Haustarifvertrag*) or a collective bargaining agreement concluded between the labor union and the relevant employers' association, provided that the employer is a member of the respective employers' association. According to the German Federal Labor Court, labor unions are generally in the position to enforce such agreements by measures like strikes. However, in practice, almost all reconciliation of interest agreements and social plans is negotiated with the works council(s) only.

In addition, an employer may be required to inform, hear and provide

The newly amended law now requires the participation of the works council in a share deal where control is acquired. It is notable that control is deemed to exist already upon the acquisition of at least 30% of the voting shares. The application and interpretation of the new law by German courts remain to be seen.

relevant documentation to the European works council (if any) if the intended operational changes relate to operations in more than one Member State of the European Union. The participation of the European Works Council, however, does not replace the obligations to the works council(s) established under the Works Council Constitution Act. The scope of the participation rights of the European works council is set forth in the local European Works Council Act of the country within the European Union where the controlling company of a group is located.

An asset deal requires participation rights of the works council only if such asset deal involves "operational changes." Such information and participation rights, however, do not result in the possibility of the works council to finally block the implementation of an asset deal.

Share Deals

In a share deal, shares in a company are transferred to a new shareholder without affecting the legal integrity of the company. For labor law purposes, this means that the company, in its capacity as employer, remains unchanged so that there is no transfer of the employees to a new employer. Consequently, until August 2008, the German Federal Labor Court considered a share deal not to require the participation of the works council, but only the so-called economic committee. To that extent, the German Federal Labor Court considered it sufficient if information about the sale of shares is furnished, if the name and address of the purchaser is identified and if it is confirmed that no understandings as to business policy and management exist.

In August 2008, new provisions were introduced to the German Works Council Constitution Act pursuant to which in a share deal resulting in the acquisition of control by the purchaser, it is now required that:

- the economic committee be informed timely and comprehensively and provided with the relevant documents (and generally is consulted); and
- the works council be informed timely and comprehensively and provided with the relevant documents (and generally is consulted), if the company regularly employs 100 individuals or less.

It is notable that pursuant to the legislation, a change of control already occurs if a purchaser acquires at least 30% of the voting rights of the company. This threshold is identical to the threshold triggering mandatory takeover offers for listed companies.

The new law expressly requires that the documents to be provided must include information on the potential purchaser and its intention regarding the future business activities of the company as well as the impact of the acquisition on the employees. If a bidding process takes place, information on all potential purchasers that submitted a binding offer must be provided to the economic committee or the works council.

In case the employer fails to comply with such information and consultation obligations, the legal consequences will generally be limited. As a rule, non-compliance is regarded as an administrative offense and could result in a fine of up to a maximum of EUR 10,000.

Several questions, *inter alia* whether (i) the share purchase agreement has to be submitted to the economic committee or the works council, and (ii) an indirect change of control (*i.e.,* the change of control in the upper tier structure) will trigger the described information and consultation obligations of the German employer are currently being discussed in legal literature. It remains to be seen how these provisions will be interpreted by the German labor courts.

1 German Federal Labor Court ruling dated March 17, 1987 in AP BetrVG 1972 § 111 No. 18; January 22, 1991 in AP BetrVG 1972 § 106 No. 9.

2 German Federal Labor Court ruling dated April 24, 2007 in NZA 2007, 987.

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