

**A Word for the Wise:**  
**Planning your Sale of Business Transaction with**  
**Employees in Mind**

You've probably heard the HR mantra, "employees are our biggest asset". Although such platitudes contain a kernel of truth, employees are not considered assets in the strict legal sense, and this fact is an essential one to grasp for anyone planning a business transaction that will affect employees.

Much has been written in recent times about the poor success rate of mergers and acquisitions from the perspective of how human resources issues are handled, such as how employees of an acquired company transfer and are integrated into the new organization. This is where the kernel of truth comes into play: employees do matter because a business transaction may actually fail if people issues either don't hit the radar screen at the right juncture, or are mishandled from the perspective of the design of the transaction, documentation and employee communications.

Organizations need to incorporate human resources considerations into the design and execution of a business transaction, whether a divestiture, acquisition, outsourcing or joint venture. Failure to do so is not only reckless from the perspective of potential exposure to employment liabilities that can destroy a business case, in some instances it may even make the objectives of a transaction unrealizable.

For example, a manufacturer in Ontario determines that its labour costs are too high, so it looks for a suitor willing to acquire the manufacturing assets, supply manufactured product back, and take on the employees. A potential purchaser is identified and is attractive because it has a lower labour rate that should translate into lower manufacturing costs - and, theoretically, savings that Seller will realize. This is where obtaining employment law advice is critical: testing the theory.

All employees in Canada have a contract of employment, and absent an express provision permitting the employer to assign the contract to another entity, contracts of employment are not assignable. Yes, surprisingly, slavery is dead: you can't buy and sell employees.

It follows that, in almost all situations, the acquiring organization must present an offer of employment to employees of the seller, a contract offer that can be accepted or rejected. In other words, the transfer of employees to the purchaser's organization at closing is not a certainty: if the Purchaser does not table a compelling offer, it may be rejected and such a result has practical and legal implications.

A practical implication is that the Purchaser may not succeed in attracting a sufficient number of employees of Seller to deliver the post-closing manufacturing capability it has contracted to provide back to Seller. The legal implication is that the employment of the employee who does not become employed by the Purchaser will be considered terminated by the Seller at closing.

Unless Purchaser has expressly (in a definitive agreement) assumed responsibility for such liabilities, Seller will be on the hook (in respect of each such employee) for notice of termination (or termination pay) and severance pay pursuant to the (Ontario)

Employment Standards Act (“ESA”). The liabilities are greater if a mass termination is triggered (i.e. for employers subject to the ESA, that means more than fifty employees are terminated within an establishment in a four week period, which in our example would mean that fifty or more employees have rejected).

Purchaser’s job offer and do not become employed by Purchaser). Seller will also have common law liability if the Purchaser’s employment offer is substantially inferior when compared to the employee’s terms and conditions of employment under their contract of employment with the Seller.

Turning back to the facts, recall that Seller was attracted to Purchaser because Purchaser had lower labour costs. So how is Purchaser to succeed in enticing Seller’s employees to become employed by Purchaser if Purchaser’s employment offer is on terms and conditions that, in aggregate, are substantially lower in value than employees currently enjoy as employees of Seller? Good question! Another good question is whether or not Seller built into its business case for the transaction employment termination costs under the ESA and at common law. And, what happens if Purchaser doesn’t have a sufficient number of employees, post-closing, to supply manufactured goods back to Seller? It sounds like a deal that’s been poorly designed.

The foregoing example is based on the premise that Purchaser needs Seller’s employees to transfer in order for the deal to work. Putting aside the situation where the employees of the business that Seller is divesting are subject to a collective agreement (in which case, the Purchaser is usually declared a successor employer that is bound to the collective agreement and is required to continue to employ the employees on the terms and conditions in that contract), it is open to Buyer and Seller in an asset sale to design their transaction to not involve a transfer of Seller’s employees. In that scenario, unless Seller is able to redeploy the employees in its remaining operations, Seller will be responsible for terminating the employees.

The foregoing example describes a landmine that may find the foot of an unwary entrepreneur who fails to understand the intricacies of labour and employment law in the context of a sale of business that involves a potential transfer of employees. The lesson is clear: determine at an early stage whether or not employees are key to the success of a deal, and receive expert labour and employment law advice to better understand liabilities and to develop an appropriate strategy.

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