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Proactive Employment Compliance

Enhancing the Value of Growing Private Equity Platform Companies via Proactive Compliance Initiatives

October 16, 2018

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Attorney Advertising

Presented by

Peter Steinmeyer
Member of the Firm
psteinmeyer@ebglaw.com
312-499-1417

Denise Dadika
Member of the Firm
ddadika@ebglaw.com
973-639-8294

Paul DeCamp
Member of the Firm
PDeCamp@ebglaw.com
202-861-1819

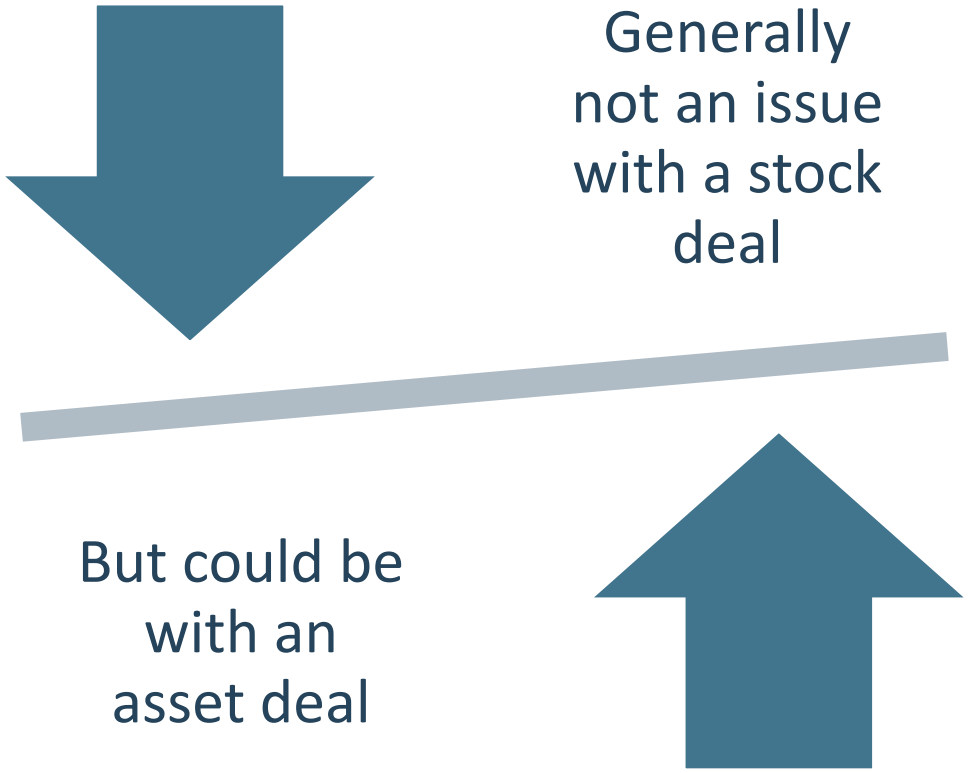
Agenda

1) Potential employment law issues associated with a corporate transaction, including issues with executive employment agreements, restrictive covenants, severance obligations, and unique issues associated with unionized workforces
2) Due diligence and ongoing compliance in the #MeToo era
3) Pay equity
4) Potential wage and hour issues

Potential issues with executive employment agreements

- Will transaction constitute a “change in control”?
- If so, will that provide “good cause” for executive to voluntarily terminate?

Are existing restrictive covenants assignable?



Even if assignable, will existing restrictive covenants be enforceable?

Will new restrictive covenants be needed to protect the business?

If so:

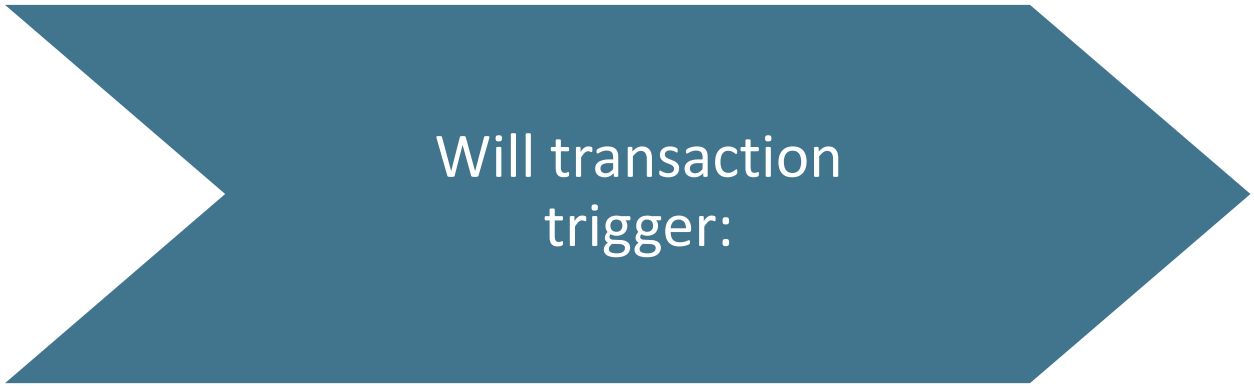
What will be the consideration?

What state's law shall govern?

Are new terms and conditions needed to lock in key employees?

- Adequacy of compensation and benefits?
- Incentive compensation?
- Confidentiality?
- Term of employment
- Garden leave/mandatory notice?
- Binding arbitration?

Potential benefits issues with executive employment agreements



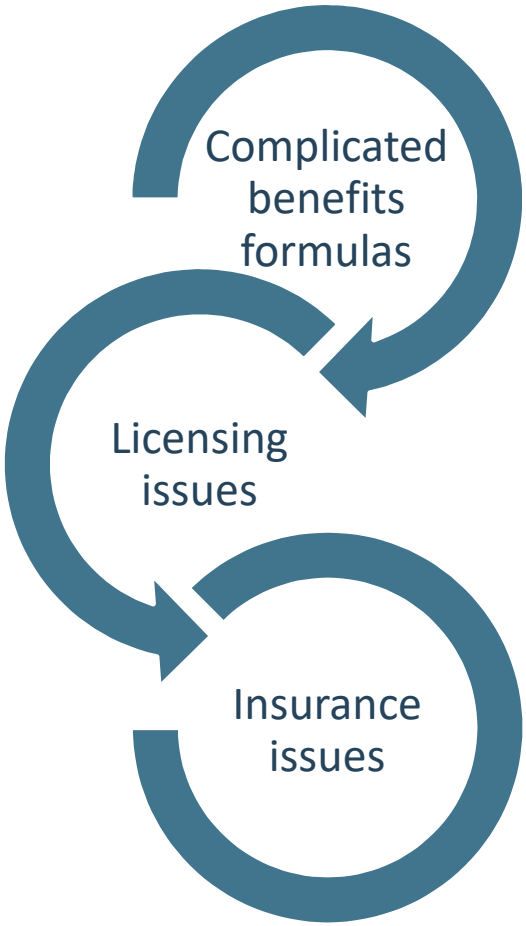
- Severance entitlement?
- Accelerated vesting of equity awards?

Is the workforce unionized?

If so:

- Potential withdrawal liability issues from changes in contributions to multi-employer pension plans
- Potential issues under collective bargaining agreements
- Potential issues regarding bargaining units
- Duty to bargain over terms and conditions

Unique issues with physician employment agreements



Due Diligence in the #MeToo Era

- The price of sexual-misconduct accusations has never been higher
- Understand potential exposure through more robust due diligence

Review:

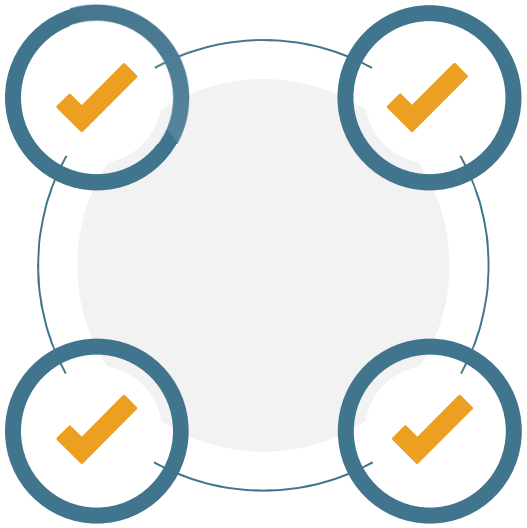
- Pending Litigation
- Threatened Litigation
- Internal Complaints
- Settlement/Severance Agreements

Due Diligence in the #MeToo Era

Review:

Exit Interviews

Recruitment & Turnover Data



Non-Harassment & Complaint Procedure Policies

Employment Agreements

Due Diligence in the #MeToo Era

Safeguards:

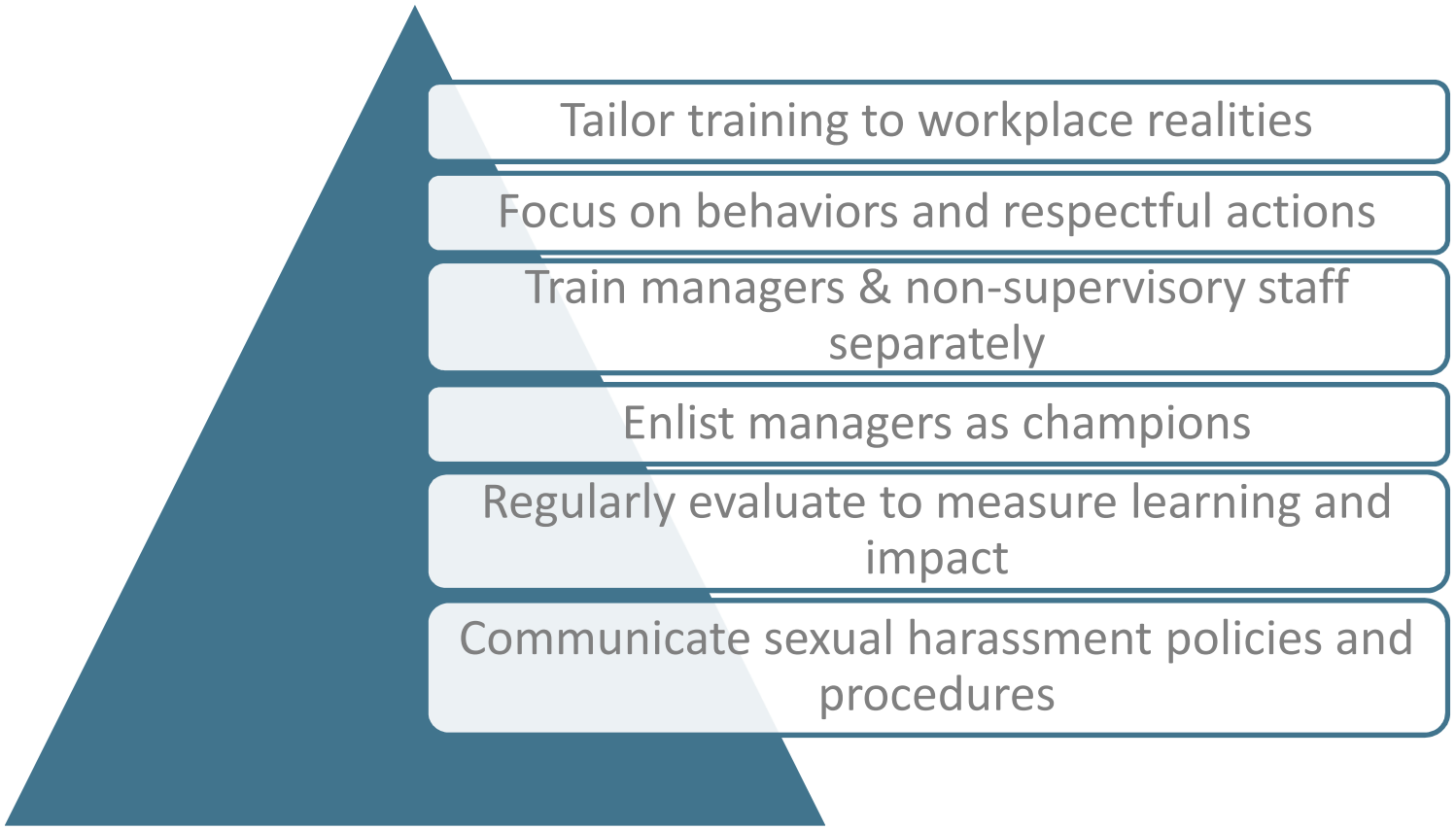
- #MeToo Rep aka “Weinstein Clause”
- Indemnification Provisions

Ongoing Compliance in the #MeToo Era

Review Policies and Practices

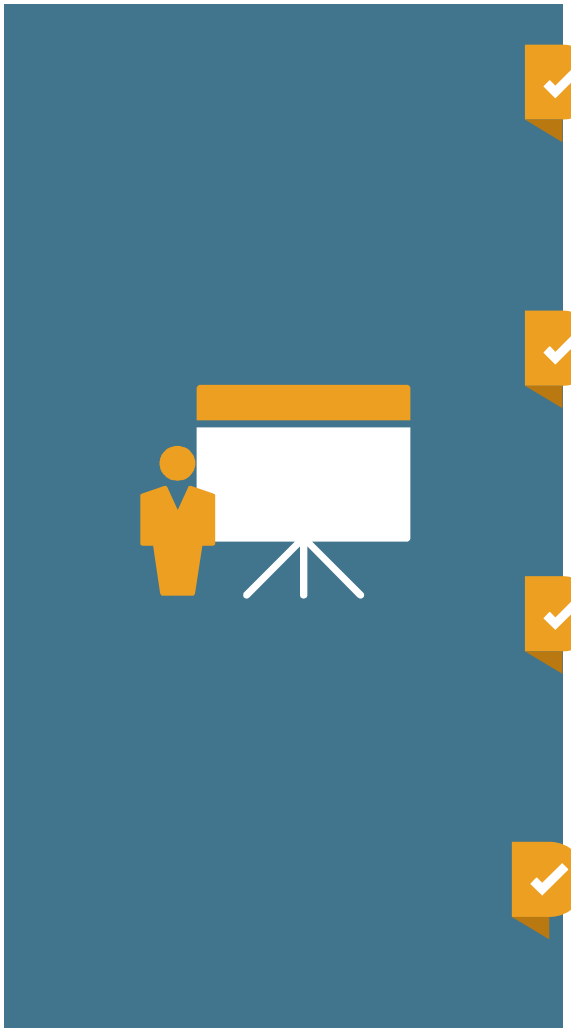
Ongoing Compliance in the #MeToo Era

Training & Communication



Ongoing Compliance in the #MeToo Era

Building and Sustaining a Holistic Harassment Prevention Program



- Leaders model respectful behaviors and establish a culture of respect in which harassment is not tolerated;
- Promote social accountability for managers and front-line supervisors to prevent and respond to harassment;
- Create internal task force or committee empowered to identify specific problems and remedies;
- Create pathways to diversify leadership and core jobs.

Pay Equity: A Brief History

- The Equal Pay Act of 1963: "Equal Pay for Equal Work"
  - Bans wage discrimination where jobs require equal skill, effort, and responsibility, and are performed under similar working conditions
- "Comparable Worth" / "Comparable Work"
  - Concept that jobs which require comparable abilities, knowledge, and skills, should be paid the same wage rate, regardless of the sex of the worker
- The Lilly Ledbetter Fair Pay Act of 2009
  - Each paycheck that contains discriminatory compensation is a separate, new violation of the law

Pay Equity: Federal Equal Pay Act of 1963

Exceptions to "Equal Pay for Equal Work" Mandate

- Pay differential may be justified where it is based on:
  - A seniority system
  - A merit system
  - A system which measures earnings by quantity or quality of production
  - Any other factor other than sex

Pay Equity: States/Cities Broaden Their Equal Pay Laws

Since 2016: Equal Pay/Anti-Discrimination Laws Amended in CA, MA, MD, NJ, NY, OR, WA & PR

What They Do (some or all of the following):

- Expand reach, e.g., MA – all employers covered
- Broaden categories protected against wage discrimination, e.g., NJ – 20+ protected statuses!
- Loosen the "equal pay for equal work" standard, e.g., "comparable work," "substantially similar work"
- Expand which facilities/offices can be compared
- Impose stiffer penalties, e.g., NJ – Treble damages; up to 6 years of back pay

*** Not all the laws contain all these provisions**

Pay Equity: Salary History Inquiry Bans

Enacted

- CA
- CT
- DE
- MA
- OR
- VT
- NYC
- Albany & Westchester Counties
- NY
- SF Phil.*
- PR

Illinois

- Governor veto
- "Bring me something more akin to the MA law"

Also vetoed in:

ME

NJ

Who's next?

NY?

MD?

Pay Equity: Due Diligence

Review

- Employee census, which should include each employee's job title, department, salary, salary history, gender and race
- Job descriptions
- Compensation policies
- Applications/Recruiting Practices
- Internal pay equity audits
- Litigation, complaints, or demand letters, alleging unequal pay practices

Pay Equity: Ongoing Compliance

- Ensure Compliance with All Pay Equity Laws
  - E.g., may be broader than just gender-based; is there a local law banning salary history inquiries?
- Review Hiring Practices
  - Revise applications; train interviewers
  - Recruitment: Consider wider applicant pool
  - Evaluate outside recruiter's practices
- Create/Review salary bands
- Consider Pay Audits
  - Evaluate pros and cons
  - If you find problems, fix them!

Salary history question on a job application? Illegal!

Employee or Independent Contractor?

An important threshold issue that often arises in health care transactions is whether to classify providers as independent contractors or employees. The answer to that question affects coverage under a variety of laws, including wage and hour, tax, unemployment and workers' compensation insurance, and more.

Sometimes the correct classification is straightforward, as is often the case with hospitals and other skilled care facilities.

Other times, the situation is more complicated, as with networks of geographically dispersed providers.

In some instances, acquisitions can jeopardize otherwise safe classifications, such as when a company that classifies certain providers as independent contractors buys another entity that treats that same type of provider as employees.

FLSA "Economic Realities" Test

- The standards used to determine whether an employment relationship exists, and thus whether a given law applies to that relationship, vary from law to law.
- Under the Fair Labor Standards Act, the federal law that provides for minimum wage and overtime—subject to certain exemptions—for employees, courts and the Department of Labor apply an "economic realities" test that considers:
  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.

FLSA "Economic Realities" Test (cont'd)

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.

—U.S. Department of Labor, Wage and Hour Division, Fact Sheet 13 (July 2008), https://www.dol.gov/whd/regs/compliance/whdfs13.htm

IRS "Control" Test

- For purposes of federal tax law, the Internal Revenue Service follows a "general rule . . . that an individual is an independent contractor if the payer has the right to control only the result of the work, not what will be done and how it will be done."
- The IRS used to have a 20-factor test to differentiate independent contractors from employees.
- The IRS recently moved away from the former test and has adopted a three-factor test, with each factor having several sub-factors. Taken together, the new test does not appear to be all that different from the former test, but it is important to be aware of the new standard.

IRS "Control" Test (cont'd)

- The IRS now looks to three main areas of control:

  1. Behavioral Control: A worker is an employee when the business has the right to direct and control the work performed by the worker, even if that right is not exercised. (With four categories of behavioral control.)

  2. Financial Control: Does the business have a right to direct or control the financial and business aspects of the worker's job? (With five categories of financial control.)

  3. Relationship: The type of relationship depends upon how the worker and business perceive their interaction with one another. (With four categories of relationship considerations.)

  —U.S. Department of Treasury, Internal Revenue Service, Fact Sheet 2017-19 (July 20, 2017), https://www.irs.gov/newsroom/understanding-employee-vs-contractor-designation

State-Law "ABC" Test

- About half of the states use a standard known as the "ABC" test to differentiate independent contractors from employees.
- Most states use this test for purposes of their unemployment and workers' compensation programs. Some, including California, use it more broadly.
- Under most formulations of the ABC test, a worker is an employee unless:

  A. The worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact; *and*

  B. The worker performs work that is outside the usual course and scope of the hiring entity's business; *and*

  C. The worker is customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed.

What These Various Tests Mean

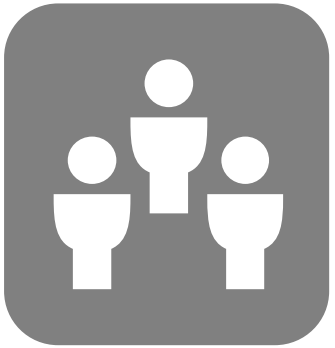
- You need to look at the laws of each state closely.
- The tests may point in different directions for different types of providers (e.g., MDs versus RNs versus LPNs).
- Don’t forget about restrictions on corporate practice of medicine, where applicable.
- Some companies end up incorporating different entities in different states to address some of these considerations, though that is not a risk-free approach.

Exempt or Non-Exempt?

Under federal law, licensed medical doctors engaged in the practice of medicine are exempt from overtime and minimum wage regardless of how you pay them.

In some states, however, there is a salary or fee-basis requirement for doctors.

For all providers who are not doctors, meaning physician assistants, nurse practitioners, RNs, and others, the normal rules apply regarding payment on a salary or fee basis in order to qualify for overtime exemption.



With many fee-for-service models, there is some risk that the services provided are not sufficiently unique or distinctive, as opposed to a repetition of essentially the same service for the same charge, to qualify as fee basis compensation.

Exempt or Non-Exempt? (cont'd)

- Some courts have interpreted the federal fee basis regulations as not allowing for other kinds of compensation, such as hourly pay. This can cause a problem if exempt employees receive fees for certain services and hourly or daily pay for other services (such as administrative time, meetings, or training).
- For providers of home health care, be aware of the Department of Labor's October 2013 regulations that significantly narrowed the scope of the FLSA's companionship services exemption by:
  1. Denying the exemption for providers employed by a third party rather than the patient or the patient's family.
  2. Limiting the amount of time a provider can spend on care services, as opposed to simply providing companionship, to 20% of the working time.

Considerations for Non-Exempt Employees

- Be sure to account properly for all working time. Areas of particular concern in the health care industry include:
  - Automatic deductions for meal periods, rather than having employees clock out at the start of a meal and then clock back in at the end.
  - Including travel time during the day, such as moving from one patient's home or location to another.
  - Paperwork and other activities that employees may perform (or allege after the fact that they performed) during unpaid meal breaks, after hours, or at home.
  - Most training programs, as well as meetings and other administrative time.
- Make sure to comply with any applicable meal and rest period laws.

Questions?

Peter Steinmeyer
Member of the Firm
psteinmeyer@ebglaw.com
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ddadika@ebglaw.com
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202-861-1819

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Upcoming Webinars

Proactive Compliance Initiatives for Private Equity Platform Companies Webinar Series

- **Proactive Health Care Regulatory Compliance** (Part 4)
  When: October 23, 2018 at 12:00pm – 12:45pm
  People: John Eriksen, Josh Freemire, Kevin Ryan

- **Employee Benefits and Executive Compensation Compliance and Planning** (Part 5)
  When: October 30, 2018 at 12:00pm – 12:45pm
  People: Christopher McMican, Kevin Ryan, Peter Steinmeyer

Registration is complimentary. For additional details, visit *www.ebglaw.com/events*.