D&O Insurance and Employment Strategies in Response to the Automotive Industry in Crisis

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D&O Insurance and Employment Strategies in Response to the Automotive Industry in Crisis

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D&O Insurance Issues In Bankruptcy

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When Bankruptcy Is A Possibility

- D&O insurance is more important than ever
  - Risk of claims against officers and directors increases
  - Likelihood of indemnification by the company decreases

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When Bankruptcy Is A Possibility

- Key questions to ask about your D&O coverage:
  - Is the amount of coverage adequate?
  - Do you have good coverage terms?

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When Bankruptcy Is A Possibility

- Key coverage terms:
  - Bankruptcy-related provisions
    - Carve-outs from insured vs. insured exclusion
    - Waiver of automatic stay
  - Presumptive indemnification
  - Language of crime/fraud exclusion
  - Severability language
  - Fiduciary liability coverage
  - A-Side-Only coverage

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When Bankruptcy Is A Possibility

- How can you tell whether you have the right coverage?
  - D&O insurance audit

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When Bankruptcy Is A Reality

- Bankruptcy filing does not terminate or change the coverage
  - As long as premiums are paid

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When Bankruptcy Is A Reality

- But bankruptcy can restrict access to coverage
  - Are the policy proceeds part of the bankrupt estate?
  - Impact of entity coverage
  - The right coverage terms can mitigate these problems
  - Officers and directors may need separate counsel to pursue coverage

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When Bankruptcy Is A Reality

- Runoff triggers
  - Sale of controlling interest
  - Sale of assets
  - May need long term tail or new policy

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Issues Relating to Cutting Costs and Reductions in the Work Force

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Labor Considerations

- Cost-Cutting, Including RIFs
  - Union v. Non-Union
    - Union – NLRA Obligations
      - Decision to Close Plant or Relocate Work or Conduct Mass Layoff
        - » Does decision turn on labor costs or other factors that are amenable to collective bargaining? OR
        - » Does the decision lie "at the core of entrepreneurial control?"
        - » Management decisions having indirect impact on employment (e.g., mass layoffs in order to regain profitability) involve balancing between the benefit to labor-management relations versus burden on the conduct of the business
      - Decisional Bargaining

Labor Considerations

- Cost-Cutting, Including RIFs
  - Union – NLRA Obligations (cont'd)
    - Bargaining Over Effects and to Impasse
      - Duty May Apply in Absence of Decisional Bargaining
        - » Most often includes request for voluminous confidential information regarding the RIF and cost-benefit analyses
      - Agreement Need Not Be Reached
        - » Meaningful notice and opportunity to respond required
        - » Post-implementation offer to bargain is generally viewed as "fait accompli" and unlawful failure to bargain in good faith
        - » Union may be found to have waived right to demand effects bargaining

Labor Considerations

- Cost-Cutting, Including RIFs
  - NLRA Obligations – Remedies For Refusal To Bargain
    - Decision
      - Reinstatement of the Status Quo
        - » Re-open closed plant
        - » Reinstatement of all impacted employees
        - » Back pay for all impacted employees
        - » Other injunctive relief
    - Effects
      - Limited Back Pay
      - Bargaining Order

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Labor Considerations

- Cost-Cutting, Including RIFs
- The WARN Act
  - Companies planning a RIF must consider potential WARN Act obligations
  - The WARN Act requires all employers with 100 or more employees to provide at least 60 days' prior written notice of any covered plant closing or mass layoff

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Labor Considerations

- RIFs & The WARN Act
  - Triggers For Notice: Plant Closing
    - An employer must give notice of plant closing if it results in 50 or more employees suffering an "employment loss" at the site during any 30-day period. A plant closing is the permanent or temporary shutdown of a single site of employment, or one or more facilities or operating units within a single site of employment

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Labor Considerations

- RIFs & The WARN Act
  - Triggers For Notice: Mass Layoff
    - Any reduction in force which, within a 30-day period, results in employment loss at a single site of either (1) a third or more of the site's active employees, but at least 50 employees or (2) at least 500 employees

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Labor Considerations

- RIFs & The WARN Act
  - Triggers For Notice: Aggregation Of Losses
    - If 2 or more groups suffer employment losses at a single site of employment during a 90-day period, and each group is less than the minimum number required to trigger WARN notice, the groups will be aggregated, unless the employer demonstrates that the losses resulted from separate and distinct employment actions, and not from an attempt to evade WARN requirements
  - Content of Notice & Procedure

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Labor Considerations

- RIFs & The WARN Act
  - Relevant Exceptions To 60-Day Notice Requirement
    - The following circumstances may relieve the employer from the full 60 day notice requirement:
      - Faltering Company
        - » Applies to plant closings, where giving notice would ruin opportunity to get new capital or business
      - Unforeseeable business circumstances

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Labor Considerations

- RIFs & The WARN Act
  - Penalties
    - Liability to each aggrieved employee for back pay and benefits for the period of violation, up to 60 days
      - The employer's liability may be reduced by items such as wages paid to the employee during the period of violation
    - Aggrieved employees may sue the employer in U.S. District courts
    - Failure to notify the local government unit subjects the employer to a civil fine of up to $500 for each day of the violation

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Labor Considerations

- RIFs & The WARN Act
  - Beware of "BABY WARN" acts
    - In addition to the WARN act, at least 15 states have their own specific plant closing or plant relocation requirements

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Labor Considerations

- RIF Selection Criteria
  - First, decide how many employees/what percentage need to be reduced as part of RIF
  - Next, decide what type of RIF you will implement
    - Voluntary?
    - Involuntary?
    - Voluntary followed by involuntary if necessary?
  - Then, decide on the selection criteria

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Labor Considerations

- RIFs – Building Defenses into the Process
  - Defenses can be built into the RIF process that will help if litigation follows a RIF
  - Companies should take time to carefully plan the RIF process, conduct careful analyses of the decisions, and draft appropriate releases in advance of the RIF
  - Companies should then stick to the plans!
  - Human resources and legal can play an important role in building defenses

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Labor Considerations

- RIFs – Building Defenses into the Process
  - Decision-maker should complete all of the forms provided and company (HR) must ensure that the selection decision was:
    - (1) Thoroughly considered and based on legitimate factors consistent with the company's processes;
    - (2) Thoroughly documented, and
    - (3) In compliance with employment laws, including those prohibiting discrimination

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Labor Considerations

RIFs – Building Defenses into the Process

- **Documentation is key**

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Labor Considerations

- RIFs – Building Defenses into the Process
  - Individualized decision-making is important
  - Class actions stemming from RIFs are based on the existence of a common policy or practice that makes the class members similarly situated

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Labor Considerations

- RIFs – Building Defenses into the Process
  - Make sure to involve a legal review in the process
  - Legal should conduct a disparate impact analysis
  - All information provided to Legal and any discussions with Legal are confidential and privileged and should not be disclosed to others outside of Legal or the HR department
  - ***** Do not forward e-mails containing legal advice *****
  - Post-RIF steps

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Labor Considerations

- RIFs – Releases/Severance Agreements

Benefits to Employers

- Protect Reputation in the Community
- Satisfy bona fide desire to "do the right thing"
- Obtain confidentiality, non-compete, non-disparagement, and/or non-solicitation agreements

and . . .

- OBTAIN EMPLOYEE WAIVER OR RELEASE OF FUTURE CLAIMS

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Labor Considerations

RIFs – Releases/Severance Agreements

Factors Affecting Validity of Severance Agreement

1. Requirement of consideration
2. Individual State Law
3. Individual Employee Circumstances
4. Older Workers Benefit Protection Act (OWBPA)
   - Time consideration & "Attachment A" issues

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Labor Considerations

- RIFs – Releases/Severance Agreements

Releases – OWBPA

When the waiver is sought in connection with a RIF involving 2 or more people, additional requirements apply:

1. Each employee must be given 45 days to consider the offer; and
2. At the start of the 45-day period, each employee must be given a clearly understandable list of any covered class, unit or group of individuals, any eligibility factors for an exit incentive program, and any applicable time limits of the program ["Attachment A"]

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Labor Considerations

- Other Cost-Cutting Measures
  - Overtime reduction
  - Shortened work-week
  - Pay cuts
  - Temporary layoffs

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Labor Considerations

- Bankruptcy & Section 1113
  - Section 1113 (11 U.S.C. § 1113) is the only authority under which a debtor in a Chapter 11 case may reject a prepetition collective bargaining agreement

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Labor Considerations

- Bankruptcy & Section 1113
  - A debtor seeking to alter or terminate a collective bargaining agreement under Section 1113 must:
    - Comply with the procedural requirements of Section 1113; and
    - Receive court approval of the alteration or termination

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Labor Considerations

- Bankruptcy & Section 1113
  - Procedural Requirements
    - Proposed modifications must be forwarded to the union
      - Must be done before applying to the court for approval of rejection of the collective bargaining agreement

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Labor Considerations

- Bankruptcy & Section 1113
  - Procedural Requirements
    - Modifications must be based on best available information
    - Modifications must be "necessary" to the reorganization
      - Courts differ over definition of "necessary"
    - Modifications must be fair to all interested parties

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Labor Considerations

- Bankruptcy & Section 1113
  - Procedural Requirements
    - Union must be provided with information that is necessary to evaluate the proposed modifications
      - Company may need to seek protective order for sensitive information
    - Debtor must confer with the union in good faith before the bankruptcy court hearing on the application to reject the collective bargaining agreement

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Labor Considerations

- Bankruptcy & Section 1113
  - Bankruptcy Court Hearing
    - Hearing must be held within 14 days after filing of application
      - Court may extend by up to 7 days if circumstances and interests of justice so require
    - Notice must be provided to all interested parties at least 10 days prior to hearing
    - Court must decide whether to reject the collective bargaining agreement within 30 days of the start of hearing
      - If court fails to decide within 30 days, debtor may terminate or modify on its own until the court rules

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Labor Considerations

- Bankruptcy & Section 1113
  - Court will approve rejection of the collective bargaining agreement if:
    - The debtor has followed all foregoing procedural requirements
    - The union has refused to accept the proposal without good cause
    - The balance of equities clearly favors rejection of the CBA

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Labor Considerations

- Bankruptcy & Section 1113
  - With court approval, the employer can implement its "final" offer to the union, but the union can still strike
    - There is not a contract in place, and there is not a "no-strike" provision in place
  - Thus, in order for Section 1113 to be an effective remedy, the employer must either believe employees will not strike, or that company can withstand a potential strike

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Labor Considerations

- Section 1113 – Interim Relief
  - Debtor may obtain temporary, emergency alterations to a CBA if necessary to the continuation of its business, or to avoid irreparable damage to the debtor's estate
  - If interim relief is granted, must still negotiate with union towards permanent modification or rejection of the CBA

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Labor Considerations

- Section 1113 – Interim Relief
  - Must be notice and hearing before interim relief can be granted
  - A debtor may seek interim relief at any time – not required to have first filed an application for rejection
  - However, must still file application and follow procedural requirements in order to obtain permanent rejection

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Employee Benefits: How to Reduce and Eliminate Costs

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Three Important Takeaways

1. There may be legal restrictions/ limitations that apply
2. Don't shirk process.
3. Remember your fiduciary duties.

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Defined Benefit Pension Plans

- Can freeze or cutback benefit accruals with 45 days advance notice to participants; this will not save a lot of immediate cash
- Pension Protection Act of 2006 provides for some automatic cutbacks:
  - If plan less than 80% funded, cannot pay full lump sum benefits
  - If plan less than 60% funded, benefit accruals automatically freeze and payments of "unpredictable contingent event benefits" (such as plant shutdown benefits) not permitted

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Defined Benefit Pension Plans - Termination

- Plan sponsor can terminate plan only if fully-funded
- Otherwise, must involve the PBGC to terminate a plan
  - Plan terminates during Chapter 7 bankruptcy proceeding
  - Continuing plan will prevent successful reorganization in Chapter 11
  - Plan sponsor will not be able to pay debts if it continues to fund the plan
  - Necessary to avoid unreasonably large pension increase due to decrease in plan participants
- If PBGC agrees to termination, plan is terminated and PBGC takes over assets and liabilities; plan sponsor (and controlled group members) still liable to PBGC for underfunded amount except in Chapter 11, in which case PBGC is generally given a general unsecured claim

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Defined Benefit Pension Plans – Funding

- Be especially mindful of minimum contributions required for pension plan
- Failure to timely pay could result in 10% excise tax, which could increase to 100% if the excise tax is not timely paid
- Can seek waiver of minimum contribution if you can convince the IRS that you need a temporary waiver ("temporary substantial business hardship") – See IRS Rev. Proc. 2004-15 for information on funding waivers
- Funding waiver application for calendar year plans is due by March 15 with respect to the prior year (i.e. March 15, 2009 with respect to minimum contributions for the 2008 plan

Defined Benefit Pension Plans – Impact of Early Retirement/Layoff

- If have excess pension assets, consider using defined benefit pension plans to fund early retirement windows (must be nondiscriminatory under IRC rules)
- If have underfunded pension, consider cost of layoffs/early retirement to pension plan – not only will more individuals start drawing a pension but an involuntary termination of 20% or more plan participants is considered a "partial plan termination" requiring full vesting

Defined Contribution Plans (401k)

- Most common approach is to "suspend" match; this results in immediate cash savings for the plan sponsor
- If using a "safe harbor" matching formula, requires 30-day advance notice of suspension; otherwise, no specific rule but good fiduciary practices would recommend a similar advance notice
- If using a "safe harbor" profit sharing formula, does not appear to be a way to suspend those contributions mid-year
- If you have a "money purchase" plan, need 45 day advance notice to cease contributions
- Keep plan termination rules in mind – permanent cessation of contributions requires full vesting; also a 20% or greater workforce reductions is considered a "partial plan termination" and must fully vest participants

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Welfare Benefits – Active Employees

- Most common approach is to increase cost-sharing in the form of increased employee premiums, co-pays and deductibles
- OK to make changes mid-year
- Cafeteria plan rules allow premiums to be automatically increased on a pre-tax basis, or if cost changes significant, may allow employees to drop coverage
- Be careful about benefits during layoffs or promised under severance packages – if fully-insured, has the insurance company agreed?

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Welfare Benefits – Retirees

- Consider terminating retiree medical/life insurance or increasing amounts retirees must pay
- Need careful review of plan documents and legal advice to do this – this is a highly litigated area
- Typically, plan must reserve right to amend or terminate plan – this includes looking back at plan documents in effect at the time the individual retired
- Any "promise" of lifetime benefits generally cannot be changed

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ERISA Do's and Don'ts

- DO follow the plan's amendment and termination processes – who has authority to amend or terminate? What does the plan or SPD say about what happens on amendment and termination?
- DO consider fiduciary duties. While decision to amend or terminate a plan is not a fiduciary function, implementation and communication of the amendment and termination is
- DON'T play fast and loose with plan assets. Make sure 401(k) and health insurance money is promptly remitted. This is one fiduciary breach that can result in criminal prosecution, including jail

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Executive Compensation

- Can reprice out-of-the-money options, subject to option plan terms and listing requirements if publicly-traded (typically, publicly-traded companies will need to shareholder approval to reprice options)
- Consider different types of equity awards to compensate for cash bonuses, such as restricted stock
- With regard to deferred compensation, be careful about 409A rules. Violation of the terms of the plan or 409A causes adverse tax consequences to the employee/director. There is also a general anti-abuse rule

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Employee Communications

- Don't try to hide the ball
- Don't delay communications
- Don't make promises (that cannot be kept) or misrepresentations. Remember – communication is a fiduciary function
- Consider whether you can offer a lower-cost benefit when eliminating or reducing a higher-cost benefit to soften the blow

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