

District of Columbia Circuit Halts NLRB's Expansion of "Perfectly Clear" Successor Rule and Strengthens Successor Employers' Rights to Set and Implement New Initial Terms

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S&F Market Street Healthcare LLC, d/b/a Windsor Convalescent Center of North Long Beach v. National Labor Relations Board, Case No. 07-1439, 2009 BL 140584 (DC Cir. June 30, 2009)

On June 30, 2009, the federal Circuit Court of Appeals for the District of Columbia issued a decision with significant legal and practical implications for employers who acquire unionized operations from other employers. In the decision, *S&F Market Street Healthcare LLC, d/b/a Windsor Convalescent Center of North Long Beach v. National Labor Relations Board*, the Court declined to enforce a decision of the National Labor Relations Board (the "NLRB" or "Board") which had resulted from the Board's expansive reading of the so-called "perfectly clear" exception to the normal rule allowing "successor" employers to set their own initial terms and conditions of employment. The Court also rejected the Board's very exacting view of the detail with which a successor employer needs to explain its initial terms and conditions of employment in offers of employment to employees of an acquired unionized operation.

The Burns Decision and the Creation of the "Perfectly Clear" Successor Exception

S&F Market Street Healthcare is the most recent step in the evolution of NLRB and federal judicial precedent concerning the rights and obligations of employers who acquire unionized operations from other employers under the National Labor Relations Act ("NLRA"), the principal federal labor law. It is firmly established that when an employer acquires some or all of the unionized operations of another employer, it may be deemed a "successor" under the NLRA. An employer is considered a "successor" and obligated to recognize and bargain with the union that represented the employees of a predecessor employer if a majority of a "substantial and representative complement" of employees hired by the purchaser were previously employed by the acquired entity, the employees constitute an appropriate bargaining unit, and there is "substantial continuity" between the predecessor's and purchaser's operations. Particularly when an employer acquires a running operation (such as a factory, plant, or other facility) intact, and hires the staff in addition to purchasing property, plant and equipment, it will often be deemed a successor.

Prior to 1970, the NLRB's rule had been that a successor employer was required to bargain with an incumbent union before changing any of the terms and conditions of employment that prevailed under a predecessor regime, although it was not required to adopt the predecessor's collective bargaining agreement. In 1972, however, the Board tried to take this rule a step further and to require not only that a successor bargain with an incumbent union, but actually adopt the predecessor's collective bargaining agreement. The issue eventually reached the United States Supreme Court in a case titled *NLRB v. Burns International Security Services, Inc.*, 406 U.S. 272 (1972). In *Burns*, the Supreme Court rejected the Board's new rule and established the one that prevails today: in an asset purchase, even if a successor, a purchaser can set its own initial terms and conditions of employment upon which it will hire employees of the purchased entity after

assuming control of the entity's operations, although it must bargain with the incumbent union over any subsequent changes to those initial terms once it is deemed a successor.

The *Burns* decision, however, contained a caveat to the general rule. In a footnote, the Supreme Court observed that "there will be instances in which it is perfectly clear that the new employer plans to retain all of the employees in the unit." In such cases, the Court found, a successor would be obligated to bargain even over initial terms. This became known as the "perfectly clear" exception.

The NLRB Expands the Perfectly Clear Successor Exception

Although the perfectly clear successor exception began its existence as a narrow exception to the general rule of *Burns*, in the years after *Burns*, the NLRB began to expand the scope of the exception in its own decisions interpreting *Burns*. This process began with a Board decision called *Spruce Up Corporation*, 209 NLRB 194 (1974), in which the Board found that the perfectly clear successor exception would apply when a successor employer "failed to clearly announce its intent to establish a new set of conditions prior to inviting former employees to accept employment." Subsequent Board decisions followed, elaborated on, and incrementally expanded this gloss on the *Burns* exception.

Over the years, and by the time of *S&F Market Street Healthcare*, the Board had effectively transformed a narrow exception ensnaring only those successors who affirmatively made perfectly clear their intent to retain all existing employees into something quite different - a much broader exception that could ensnare employers who simply failed to do something, i.e., make sufficiently clear - in the Board's judgment - an intent to establish new terms of employment. In the *S&F Market Street Healthcare* case, the Board would take its interpretation of the perfectly clear successor rule farther than it ever had before.

S&F Market Street Healthcare – Factual Background

S&F Market Street Healthcare involved an employer known as Windsor, which operated skilled nursing and other healthcare facilities in California. Windsor agreed to acquire a nursing facility in Long Beach, California known as Candlewood. Candlewood's employees were represented by a union. Before taking control, Windsor decided that it would need to make significant changes to how the facility was run, including changes to its staff and their terms and conditions of employment. However, because Windsor needed to maintain continuous health care operations, it also needed the takeover to be seamless. Patient care had to continue as Windsor took control.

Windsor required any existing Candlewood employees to complete employment applications. The applications stated that applicants would need to undergo background and drug tests, and that only those employees who met Windsor's operational needs would be hired. Candlewood applicants were also told that, if hired, they would be probationary or temporary employees, that they would be employed at will, and that their other terms of employment would be set forth in a new employee handbook. Windsor actually took control of the facility at midnight on July 1, 2004. However, with the press of business, certain aspects of the takeover, such as the dismantling of a particular bulletin board and the distribution of the new handbooks describing all the changes in detail, were not be accomplished until approximately one week after the takeover.

The NLRB's Decision

The NLRB's decision, issued on September 30, 2007, was the high point of the Board's attempted expansion of the perfectly clear successor exception, and threatened, in effect, to overrule *Burns sub silentio*. The Board held that, notwithstanding the various announcements of changed terms that Windsor had made, it had not preserved its right to set initial terms and was a perfectly clear successor because the changes it had announced did not implicate "core" terms of employment. The Board also stated that the changes announced by Windsor were too general to preserve its rights.

While the Board's holding dealt principally with the perfectly clear successor exception, the Board also included a footnote to its decision, which may have been a signal of the Board's next line of attack on the *Burns* rule. In the footnote, the Board noted that, even if Windsor were an ordinary successor with the right to set its own initial terms of employment, it would only have had the right to implement those terms that it had specifically announced before the takeover.

The DC Circuit Rejects the Board's Decision and Restores Burns

Windsor sought review of the Board's order by the DC Circuit, the federal court of appeals with primary responsibility for reviewing Board decisions. The Court denied enforcement to the Board's order. Considering the Board's finding that Windsor was a perfectly clear successor, the Court found that, given the evidence that Windsor had, in fact, announced various changes to terms of employment before taking control of the facility, the Board's finding that it was a perfectly clear successor was not supported by substantial evidence. More importantly, the Court emphatically rejected the Board's broad interpretation of the perfectly clear successor exception. The Court, noting the Board's expansion of the exception, noted that *Burns*

Started from the presumption that a successor employer may set its own terms and conditions of employment and reserved the "perfectly clear" exception for cases in which employees had been misled into believing their terms and conditions would continue unchanged. . . In this case, the Board presumed the predecessor's terms and conditions must remain in effect unless the successor employer specifically announces it will change "core" terms and conditions. Thus does the exception in *Burns* swallow the rule in *Burns*.

The Court confirmed that, in order preserve its right to set initial terms and avoid perfectly clear successor status, "the successor employer must simply convey its intention to set its own initial terms and conditions rather than adopt those of the previous employer." It also confirmed "that there is no requirement in *Burns* or *Spruce Up* that the intended change(s) involve "core" terms."

The Court also rejected the Board's suggestion that an ordinary successor may only implement initial terms if it specifically announced those terms before taking control of the operation in question. It held that, in stating this "novel rule" the Board "misapplied its own precedent and that of the Supreme Court." In this case, the Court noted, the employer did not accept the predecessor's terms, nor did it set its own initial terms, hire employees on those terms, and then change the announced terms. It concluded that "[b]ecause the employer did not change any terms it previously established but merely replaced its predecessors terms with its own" it was not required to bargain over the setting of initial terms, even though some of those terms (the dismantling of the bulletin board and distribution of handbooks) could only be implemented after the takeover. Indeed, the Court confirmed the Supreme Court's understanding in *Burns* that a

successor that implements initial terms is not changing any pre-existing term of employment because, prior to taking control, “it had no previous relationship whatsoever to the bargaining unit and . . . no outstanding terms and conditions of employment from which a change could be inferred.”

Probable Results

The DC Circuit’s ruling in *S&F Market Street Healthcare* signals the return of the perfectly clear successor rule to its original form as a narrow exception to the ordinary right of a successor to set its own initial employment terms, and a rejection of the NLRB’s much more expansive reading of the exception. It would seem to halt a progression of Board decisions drifting in the direction of restoring the Board’s pre-1972 rule requiring all successors to bargain before changing a predecessor’s existing terms. The decision also preserves ordinary successors’ ability to set their own panoply of initial terms, including those that were not specifically announced prior to takeover, provided that the successor avoids the now-narrowed perfectly clear successor exception. Nevertheless, it is important to note that the NLRB will not be bound by the DC Circuit’s decision in future cases. It is possible that the Board will continue to issue decisions under its own standard notwithstanding the DC Circuit’s opinion. However, in the event that the Board does continue to issue decisions in conflict with the principles stated in *S&F Market Street Healthcare*, impacted employers will now be able to seek review before the DC Circuit with a reasonable expectation of a favorable outcome.

Taken as a whole, *S&F Market Street Healthcare* should make it easier for employers to acquire the unionized operations of other employers and immediately restructure those operations without running afoul of the NLRA. Given the present time of economic uncertainty, it is understandable why an employer taking control of another’s operations might wish to move swiftly to effectuate changes. This decision should facilitate such efforts.

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