OCHDL PUBLIC SERVICE

One of the benefits of working at O'Neil Cannon is the firm's strong commitment to public service. The Firm encourages its attorneys to give back to our community. I am honored to serve on the Board of The Wisconsin Law Foundation. The Wisconsin Law Foundation is the charitable arm of the State Bar of Wisconsin. The mission statement for the organization notes that "the Wisconsin Law Foundation is a charitable and educational organization that serves to promote public understanding of the law, improvement of the administration of justice and other law-related public service through funding of innovative and creative programs that improve the vision of the American justice system." The Wisconsin Law Foundation accomplishes this mission through its numerous programs.

Two of the programs supported by the Wisconsin Law Foundation are the Wisconsin State High School Mock Trial Tournament and the Belle Case LaFollette Awards. The mock trial program teaches high school students about the court system and develops students' public speaking and research skills. The Belle Case LaFollette Award recognizes three recent law school graduates who represent under-served populations such as those of modest means and those who live in rural areas. These awards support the Wisconsin Law Foundation's mission of law-related public service. You can visit the State Bar of Wisconsin website to learn more about the many programs supported by the Wisconsin Law Foundation.

OCHDL IS PLEASED TO ANNOUNCE THAT ATTORNEY NICHOLAS G. CHMURSKI HAS JOINED THE FIRM

Attorney Nicholas G. Chmurski, a graduate of Marquette University, has recently joined the Milwaukee law firm O'Neil Cannon Nick is a member of the Business Law and Real Estate and Construction Groups. His business background and clerkship experience make Nick a valuable resource, as he is able to contribute across practice groups to help solve a wide range of legal issues.

O'Neil Cannon, founded in Milwaukee in 1973, is a full-service legal practice that primarily focuses on providing business law and civil litigation services to closely-held businesses and their owners. The firm represents corporations, institutions, and partnerships at all stages of the business life cycle, helping them start, grow and transition from one generation to the next. We also assist business owners with their personal legal needs including tax and estate planning, family law and litigation—including personal injury litigation.

AVOIDING PITFALLS WHEN ADDING SWEAT EQUITY MEMBERS IN AN LLC

Many owners and businesses desire to reward employees with ownership interests for services rendered. This can be a valuable incentive that recognizes past accomplishments and improves employee engagement and retention by allowing them to share in the success of the business without requiring a capital investment. While bonuses, raises, or phantom equity can often accomplish similar goals with fewer structural considerations, the allure of being a true owner is sometimes hard to match. More likely than not, the flexibility and reduced formality of an LLC were factors in making it the entity of choice. However, because LLC ownership is unique, there are several key issues to consider when adding this sweat equity member to make sure all parties understand the consequences.

First, how is the LLC managed? If it is a member-managed LLC (default in Wisconsin), the new employee-member could have full agency power and could enter into contracts or agreements on behalf of the LLC. While the employee might already have significant authority according to his or her job title or responsibilities, this member agency authority extends to issues outside of the ordinary course of business, such as taking out a loan or purchasing real estate. On the other hand, a member of a manager-managed LLC is viewed more akin to a passive, limited partner, with no actual agency power. Therefore, before adding the employee as a member, the current members should review the ownership structure and possibly amend the LLC's articles of organization to align their goals.

Second, does the LLC have an operating agreement? Outside of being an essential tool to structure and manage the business, an operating agreement can modify default provisions of the Wisconsin statutes that govern LLCs (Wisconsin Statutes Chapter 183). For example, unless modified in an operating agreement, Wisconsin law provides that voting in member-managed LLCs is based on members' capital contributions, and not on members' ownership interests. An employee receiving a member's interest for services will have voting rights based on the value of his or her services as recognized on the LLC's capital account, regardless of the actual member's interest received. To remedy this situation, the LLC should document all members' capital contributions (including the value for services) and draft (or amend) an operating agreement that clearly defines voting rights for all members. There are many ways to accomplish this goal (unitizing the members' interest, etc.), but it is important to make sure all parties understand their respective rights and roles in the LLC.

Lastly, what are the tax consequences? If the LLC is taxed as a partnership (default), the employee receives a regular capital interest in the LLC, that member's interest would be considered compensation in exchange for services that will likely be taxed as ordinary income. Depending on the value of those services, the employee could have a significant tax burden in the year he or she receives the capital interest without any guarantee of receiving cash distributions from the LLC to help cover that tax. Think winning a car on *The Price is Right*, only to discover a several thousand dollar tax bill waiting off-stage. The LLC can address this by offering the employee an interest consisting of the future profits/losses of the business. A profits interest still allows the employee to have similar rights as a member in the LLC, but because there is no initial value assigned to the profits interest (and thus no liquidation value), the employee has no immediate tax obligation. The employee-member would then owe tax only on his or her allocation of future company profits. While taxes are inevitable, proper planning can avoid surprises and headaches for the employee and company, alike.

In conclusion, while LLCs provide flexibility for adding sweat equity members, careful design and implementation is required to avoid any potential surprises.

EMPLOYMENT LAWSCENE ALERT: COURT INVALIDATES EXPANDED OVERTIME RULE

On Thursday, a federal court in Texas issued summary judgment invalidating the Obama administration's updated overtime regulations, which raised the minimum salary level for exempt employees from $455 to $913 per week. The Court determined that the "significant increase" was outside of the scope of Department of Labor's (DOL) authority, as was the provision that the minimum salary threshold would automatically update every three years.

The Court looked to Congress's intent under the Fair Labor Standards Act and found that the determining factor for whether an employee should be considered exempt is the duties the employee performs and whether those duties are executive, administrative, or professional in nature. By more than doubling the minimum salary level and excluding an estimated 4.2 million employees who were previously classified as exempt from exempt status, the Court found that the DOL had gone too far and essentially rendered the duties test meaningless. Because the emphasis should be on duties, not salary, the Court invalidated the updated overtime rules.

However, the Court did not go as far as to rule that the DOL has no authority to establish a minimum salary level. The Court found that the current minimum salary level is a permissible “floor” to screen out “obviously nonexempt” employees. Although the Fifth Circuit Court of Appeals is currently considering an appeal of the preliminary injunction the Texas federal court issued last November, the DOL under the Trump administration only continued the appeal for the purpose of establishing that it had the authority to establish a minimum salary level, which has now been done by the Texas court. The DOL is currently seeking public feedback on revisions to the overtime rule and may issue its own revised rule in the future. We will keep you updated on any further changes.

BEST LAWYERS® HONORS 18 ATTORNEYS IN 2018

O’Neil, Cannon, Hollman, DeJong and Laing S.C. is pleased to announce that 18 lawyers have been named to the 2018 Edition of *Best Lawyers*, the oldest and most respected peer-review publication in the legal profession.

Best Lawyers has published their list for over three decades, earning the respect of the profession, the media, and the public as the most reliable, unbiased source of legal referrals. Its first international list was published in 2006 and since then has grown to provide lists in over 75 countries.

“For more than a third of the century,” says CEO Steven Naifeh, “Best Lawyers has been the gold standard of excellence in the legal profession.” President Phil Greer adds, “We are extremely proud of that record and equally proud to acknowledge the accomplishments of these exceptional legal professionals.”

Lawyers on *The Best Lawyers in America* list are divided by geographic region and practice areas. They are reviewed by their peers on the basis of professional expertise, and undergo an authentication process to make sure they are in current practice and in good standing.

O’Neil, Cannon, Hollman, DeJong and Laing S.C. would like to congratulate the following attorneys named to the 2018 *Best Lawyers in America* list:

- Douglas P. Dehler – Litigation-Insurance
- James G. DeJong – Corporate Law, Mergers and Acquisitions Law, Securities/Capital Markets Law
- Seth E. Dizard – Bankruptcy and Creditor Debtor Rights/Insolvency and Reorganization Law, Litigation-Bankruptcy
- Peter J. Faust – Corporate Law, Mergers and Acquisitions Law
- Robert R. Gagan – Municipal Law

- John G. Gehringer – Commercial Litigation, Construction Law, Corporate Law, Real Estate Law
- Joseph E. Gumina – Litigation-Labor and Employment
- Dennis W. Hollman – Corporate Law, Trusts and Estates
- Grant C. Killoran – Litigation-Health Care
- Dean P. Laing – Commercial Litigation, Personal Injury Litigation-Plaintiffs, Product Liability Litigation-Defendants
- Gregory W. Lyons – Commercial Litigation, Litigation-Insurance
- Gregory S. Mager – Family Law
- Patrick G. McBride – Commercial Litigation
- Thomas A. Merkle – Family Law
- Steven J. Slawinski – Construction Law

Since it was first published in 1983, *Best Lawyers* has become universally regarded as the definitive guide to legal excellence. *Best Lawyers* is based on an exhaustive peer-review survey. Over 54,000 leading attorneys cast more than 7.3 million votes on the legal abilities of other lawyers in their practice areas. Lawyers are not required or allowed to pay a fee to be listed; therefore inclusion in *Best Lawyers* is considered a singular honor. *Corporate Counsel* magazine has called *Best Lawyers* "the most respected referral list of attorneys in practice."

401(K) PLAN ERRORS COST SELLERS OF COMPANY NEARLY $200,000

A recent Court of Appeals decision provides a tangible example of the costs of ignoring employee benefit compliance requirements. In *Tatum v. SFN Group, Inc.* (No. 16-11966, 6/23/17), the 11th Circuit affirmed that the purchase price paid for a CFO-outsourcing firm was properly reduced in light of compliance errors in the operation of the company's 401(k) Plan.

In February 2010, Tatum, LLC (Seller) and staffing company SFN Group (Buyer), entered into a merger agreement (Agreement) under which the Buyer agreed to acquire Seller's company for payment of several million dollars, which included payments in cash and stock, as well as the assumption of debt and liabilities. The Seller's 401(k) plan was assumed by the Buyer. Under the terms of the Agreement, part of the purchase price was held back for eighteen months after the closing in the form of an indemnification holdback fund. The purpose of the holdback fund was to compensate the Buyer in the event it incurred certain defined damages, including damages resulting from the Seller's breach of any representation or warranty contained in the Agreement.

After the closing, but just before the end of the eighteen-month holdback period, the Buyer notified the Seller of its discovery that the Agreement had misrepresented the Seller's 401(k) plan. Specifically, the Seller had represented and warranted in the Agreement that its 401(k) plan was operated in compliance with applicable law. The Buyer had learned, however, that the 401(k) plan was not in compliance, and was therefore subject to potential tax-disqualification by the IRS.

The 401(k) plan's significant compliance errors were ultimately resolved through the IRS's Voluntary Correction Program (VCP), under which a 401(k) plan sponsor may self-report a compliance issue to the IRS and receive approval for its proposed solution, thereby avoiding tax-disqualification. By the time the compliance errors were rectified, the total 401(k)-related legal expenses and VCP fees incurred by the Buyer totaled $192,000. As a result, the indemnification holdback fund, minus the $192,000 amount, was disbursed to the Seller.

While the Seller asserted claims including breach of contract and conversion in an attempt to recover the withheld funds, the Court found that the Seller had breached its duties to the Buyer under the Agreement and that the Buyer was entitled to withhold the amount at issue.

Had the 401(k) plan errors been previously resolved by the Seller, or discovered by the Buyer before the transaction closing, the costs to the Seller (and burdensome correction process by the Buyer) may have been reduced or avoided. The ruling serves as a reminder of the importance of adherence to compliance with benefits requirements, as well as the need for performing careful due diligence and strategically drafting the purchase agreement in merger and acquisition transactions.

THE WILAW QUARTERLY NEWSLETTER

Newsletter Article Highlights:

- Don't Sell Yourself Short: Early Tax Planning to Maximize the Sale of Your Business
- Are You Ready to Comply with the Final Fiduciary Rule?
- Creating a Successful Succession Plan

Pleased to Announce:

- OCHDL included in the prestigious Chambers USA Directory
- Annual Charity Event raised over $14,000 for Milwaukee community

Click the image below to read more.

SEVENTH CIRCUIT UPHOLDS WISCONSIN RIGHT-TO-WORK

In March 2015, Wisconsin Governor Scott Walker signed Right-to-Work legislation into law, which allowed workers covered by union representation to not pay union dues if they do not wish to. Since its passage, the law has been under legal fire, including a failed bid for preliminary injunction to halt the law and a state circuit court ruling that found the law unconstitutional. However, in 2015, the federal district court sitting in the Eastern District of Wisconsin upheld the Right-to-Work law as constitutional, relying heavily on the Seventh Circuit's 2014 decision, *Sweeney v. Pence*, which upheld Indiana's right-to-work statute.

On Wednesday, the Seventh Circuit doubled down on its holding in *Sweeny* and upheld Wisconsin's Right-to-Work law as constitutional. The Court found that the plaintiff unions had failed to provide "any compelling reason" to overturn the *Sweeny* decision. The ruling stated that there have been no intervening developments in statutory, Supreme Court, or even intermediate appellate court law that would cause them to reevaluate their decision in *Sweeney* and that the strong dissent in *Sweeney* and a close vote to rehear the case en banc were not compelling reasons that would justify overturning a three-year old decision. The Court also rejected the unions' takings clause argument, whereby they claimed that members of the union who did not pay dues but benefitted from the unions' bargaining and political activities would be taking the unions' property without compensation. The Court found that, in the event that a taking occurred, state courts could "provide an adequate route for seeking just compensation." Although the union has stated that it is considering its next steps, it appears that Wisconsin's Right-to-Work law will continue to pass judicial scrutiny and be enforceable and constitutional.

CONGRESS CONTEMPLATES "COMP TIME" BILL

In May 2017, the House of Representatives passed the Working Families Flexibility Act, which would amend the Fair Labor Standards Act to allow nonexempt employees in the private sector to choose to receive compensatory time ("comp time") in lieu of overtime pay for hours worked in excess of 40 hours per week. Under current law, employers in the public sector must pay nonexempt employees a rate of at least one and one-half of their regular wage for each overtime hour worked. However, certain government employees can receive comp time in lieu of overtime pay.

The Working Families Flexibility Act would allow private sector employees who had worked at least 1,000 hours in a 12-month period to accrue up to 160 hours of compensatory time per year, at the rate of one and one-half hours of comp time for each overtime hour worked, which could be used upon reasonable notice by the employee as long as such use does not disrupt the employer's operations. The decision of whether to receive overtime pay or comp time would be up to the individual employee or a collective bargaining agreement covering a group of employees, and any compensatory time accrued by the employee but unused by the end of the year would need to be paid to the employee. Additionally, any employee could, with 30 days' notice, choose to cash out their unused comp time and return to traditional payment of overtime. Similarly, employers could, with 30 days' notice, discontinue offering comp time as an alternative option to overtime pay. The bill states that employers may not intimidate, threaten, or coerce employees to choose to take comp time instead of overtime pay or force them to use accrued comp time. If enacted, this provision is one of the most likely to lead to litigation between employees and employers.

The bill is currently pending before the Senate, which may not have enough support to pass the bill. Proponents of the law believe that the bill would add flexibility for workers, while opponents believe that it would undermine the payment of overtime. Similar bills have been proposed in Congress previously, including as recently as 2013. However, the current bill has the support of the Trump administration. We will keep you updated on any further developments and, if passed, on techniques for implementation.

IT'S (ALMOST) JUNE 9! ARE YOU READY TO COMPLY WITH THE FINAL FIDUCIARY RULE?

At 11:59 p.m. on Friday, June 9, 2017 (the Effective Date), the ERISA definition of a fiduciary will expand to include, for the first time, many financial firms and advisors that provide investment advice to certain employer-sponsored retirement plans and individual retirement accounts (IRAs). This is because part of the final Department of Labor (DOL) Fiduciary Rule (described in our prior post) takes effect at this time, and will apply to anyone receiving a fee for providing a "recommendation" regarding covered investment transactions. "Recommendation" is broadly defined to include communications that are likely to be considered a suggestion to take, or to refrain from taking, a particular course of action.

After the Effective Date, ERISA fiduciary duties will also extend to the provision of a recommendation regarding whether or not to take a rollover or distribution from an ERISA retirement plan or an IRA, even if the rollover or distribution recommendation is not accompanied by investment advice.

While the Fiduciary Rule most directly impacts investment advice providers, employer sponsors of ERISA retirement plans should also be aware of the new rules and of the ways in which plan service provider arrangements and internal human resources practices may be impacted by them.

Key requirements and recommendations for both investment advisors and employer retirement plan sponsors are briefly summarized, below.

Action Items for Advisors

Unless an exception or exemption applies, financial advisors who give investment advice to participants of covered plans and IRAs must now observe impartial conduct standards, and some portions of the DOL Best Interest Contract (BIC) exemption or Principal Transaction exemption (if applicable). This means that advisors must, as of the Effective Date:

- provide advice in participants' best interests;
- receive no more than reasonable compensation; and
- avoid misleading statements.

By January 1, 2018, the remainder of the BIC and Principal Transaction exemption rules apply and affected advisors must:

- maintain (and adhere to) written anti-conflict policies and procedures;
- make required disclosures to advice recipients; and
- enter into enforceable written contracts relating to the provision of investment advice services relating to covered employer retirement plans and IRAs.

Advisor Transition-Period

Under a temporary non-enforcement policy issued by the DOL on May 22, 2017, neither the DOL nor the IRS will enforce potential violations of the prohibited transaction rules, provided that the advisors are working diligently and in good faith to comply with the new rules. This temporary non-enforcement policy will end on January 1, 2018, which is also when the remaining parts of the Fiduciary Rule (and exemption) requirements take effect.

Taxes and Penalties for Violation

After January 1, 2018, an advice fiduciary that fails to comply with the new rules, and thereby engages in a prohibited transaction, may be required to refund all fees earned from the transaction and to pay an annual excise tax of 15% on such fees until repayment occurs. To the extent that such a prohibited transaction relates to an ERISA-subject retirement plan, a violation of the rules could potentially also result in legal claims by retirement plan sponsors or IRA investors, civil penalties, and personal liability for losses or improper profits.

Certain Assets Unaffected

The new rules do *not* affect any health, disability, term life, or other health-related arrangements or assets that do not contain an investment component. Personal brokerage accounts (not involving an employer-sponsored retirement plan or any IRA) are also unaffected by the changes.

Action Items for Employer Plan Sponsors

Employer retirement plan sponsors should consider taking the following steps:

- Review existing educational materials provided to participants to determine whether they remain non-fiduciary “investment education,” or whether they now constitute fiduciary “investment advice.”
- Review practices relating to rollovers into and out of the plan to determine whether they trigger fiduciary advice-related obligations.
- Confirm that in-house employees who provide advice to participants (if any) are not being separately compensated for such advice.
- Review contractual arrangements with advisers to determine which advisers are fiduciaries under the new rules. For those service provider serving as a fiduciary for the first time under the Fiduciary Rule, expect that agreements will be amended or replaced before January 1, 2018. Any resulting fee changes must be clearly disclosed.
- Expect to receive additional disclosures beginning in 2018 from investment advice fiduciaries that will rely on the BIC exemption to continue receiving certain types of compensation. Among other things, these disclosures must describe any of the advice fiduciary’s conflicts of interest, and the types of compensation paid in connection with plan investment recommendations.
- Carefully review all fee disclosures you receive to ensure that you understand what fees are being charged for plan services. Confirm that the fee structure and amounts of compensation received by advisers are reasonable, in light of the services performed.