# New Homeland Security Memo Poses Problems for M & A Deals

## By Angelo A. Paparelli and Ted J. Chiappari

The latest spate of merger deals is another promising harbinger of better economic times.[1] They may also illustrate economist Joseph Schumpeter's principle of "creative destruction" in action.[2] A well-intentioned immigration agency's recent effort to modernize its views on the immigration consequences of business combinations may end up leading to its own form of destruction, although of questionable creativity, by posing new and unexpected obstacles for acquirers and M & A lawyers in the years ahead.

On August 6, 2009 USCIS amended its instructions to Immigration Service Officers (ISOs) on how to decide whether foreign workers sponsored by the acquired entity in a merger, acquisition or other form of business restructuring may keep their place in the immigrant visa queue.[3] If these foreign workers are required to begin again at the end of the line with a new request for employment-based green-card sponsorship by the acquiring enterprise, it could delay the green card by years, especially distressing in those cases where they may have already waited years to become permanent residents (and thereby move ahead on the path to U.S. citizenship).

Successor-in-interest eligibility (as this *genre* of immigration decisions is dubbed) is important not only to the foreign workers and their families, but also to the acquiring company. Frequently, these transactions make sense not only for the hard assets acquired but also because of the likely economic value of present and prospective intellectual property rights flowing from the minds of the acquired entity's employees (American and foreign-born) who collaborate as teams. Without key team members (the foreign employees seeking green cards), potential acquirers may worry that the team may not function as well and, as a result, the deal may not be as attractive or even worth pursuing.

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[1] "Big Merger Deals Signal Restored Confidence," *New York Times*, Sept. 28, 2009, accessible at http://www.nytimes.com/2009/09/29/business/29sorkin.html (all links last accessed on Oct. 4, 2009), and "A Drumbeat of Deals," *Business Week*, Oct. 12, 2009, p.4.

[2] In *Capitalism, Socialism and Democracy* (New York: Harper, 1975) [orig. pub. 1942], pp. 82 *et seq*., Schumpeter described his concept of creative destruction:

> The opening up of new markets, foreign or domestic, and the organizational development from the craft shop and factory to such concerns as U.S. Steel illustrate the same process of industrial mutation–if I may use that biological term–that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one. This process of Creative Destruction is the essential fact about capitalism. It is what capitalism consists in and what every capitalist concern has got to live in. . . .

[3] Memorandum of Donald Neufeld, Acting Associate Director, Domestic Operations, USCIS, "Successor-in-Interest Determinations in Adjudication of Form I-140 Petitions; Adjudicators Field Manual (AFM) Update to Chapter 22.2(b)(5) (AD09-37)," HQ 70.6.2, Aug. 6, 2009, accessible at: http://tinyurl.com/yaej97k.

The recent USCIS policy instruction originates with the 1986 acquisition of a small firm engaged in auto-collision repair. In the precedent decision, *Matter of Dial Auto Repair Shop, Inc.*, 19 I & N Dec. 481 (Comm'r 1986) (*Dial Auto*), the legacy agency, Immigration and Naturalization Service (INS), announced very strict successor-in-interest requirements. These successor-in-interest rules, fitfully honored in the observance and the breach over the next quarter century of ISO decisions, cast a cloud of uncertainty over M & A deals.

*Dial Auto* essentially required that if green-card eligibility is to continue without starting over, an acquiring company had to assume all assets and all liabilities of the target business. (Apparently unknown to the INS Commissioner at the time, 100% asset and liability acquisitions rarely happened in 1986, except in stock deals; indeed, the very purpose of engaging in an asset deal is and always has been to exclude virtually all liabilities.[4])

Over time, however, in a series of nonbinding letters sent by INS officials to inquiring immigration lawyers, the agency gradually recognized that an acquiring business could purchase less than all of the seller's assets and all liabilities and still preserve the benefits of immigration successorship. At first, these letters acknowledged that even if the buyer only acquired substantially all of the assets and liabilities of the seller, successor-in-interest eligibility would survive for immigration purposes. Later, the INS missives recognized that green-card eligibility could be preserved in a deal where the buyer merely assumed substantially all liabilities and assets in the spinoff of a business division rather than only through the acquisition of an entire company. In the past few years, ISOs, perhaps prompted by a recent spate of more lenient USCIS informal letters, tended to approve most deals where the transaction merely entailed the assumption of immigration-related assets and liabilities.[5]

In its August 6, 2009 policy memorandum, the USCIS provided its rationale for taking a fresh look at its interpretation of successor-in-interest immigration standards:

> USCIS recognizes that business practices change over time, particularly in the areas of acquisitions, mergers, and transfers of assets and liabilities between entities. . . . [Business] entities do not always wholly assume the assets and liabilities of entities they acquire or merge with and that businesses may choose not to assume certain assets or liabilities in connection with a perfectly legitimate transaction. This guidance is intended to allow flexibility for the adjudication of I-140 [employment-based immigrant visa]

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[4] David W. Pollak, "Successor Liability In Asset Acquisitions," Practising Law Institute Course Handbook, Acquiring or Selling the Privately Held Company (2002, Vol. Two, B0-01AH).

[5] For a discussion of the gradual relaxation of eligibility requirements for a successorship in interest, see Angelo A. Paparelli, "Assuage Therapy – Enticing M& A Lawyers to Help with Immigration Successorship," (June, 2008) accessible at: www.seyfarth.com/dir_docs/publications/AttorneyPubs/Assuage%20Therapy.pdf , Angelo A. Paparelli, Alan Tafapolsky, Ted Chiappari, Susan Cohen, & Stephen Yale-Loehr, "It Ain't Over Till It's Over: Immigration Strategies in Mergers, Acquisitions and Other Corporate Changes," Bender's Immigration Bulletin (Oct. 1, 2000 and Oct. 15, 2000); Alan Tafapolsky, Angelo A. Paparelli, A. James Vazquez-Azpiri and Susan K. Wehrer, "Thriving on Change: How to Solve Immigration Problems in Merger & Acquisition Deals," New Rules for the New Millennium (AILA 2001), Angelo Paparelli, Daryl Buffenstein & Robert Banta: "Evading 'the Slings and Arrows of Outrageous Fortune': The Immigration Consequences of Mergers, Acquisitions and Other Business Changes," 93-11 Immigr. Briefings (Nov. 1993).

> petitions that present novel yet substantiated and legitimate successor in interest scenarios.

The USCIS memorandum then acknowledged and distinguished *Dial Auto*:

> [This case] did not state that a valid successor relationship could *only* be established through the assumption of *all* of a predecessor entity's rights, duties, and obligations. [Underlining and italics in original.]

**Successor-in-Interest Factors**

Apparently because *Dial Auto* involved the transfer of immigration benefits derived through a labor-market recruitment test known as labor certification, the August 6 memorandum focused most of its attention on employment-based immigrant visa categories that require a labor certification.[6] The USCIS memorandum announced three successor-in-interest factors, each of which must now be established (through the submission of new or amended employment-based immigrant visa petitions) in order for pipeline green-card benefits secured by a target entity to be retained by foreign employees of the surviving firm:

1. The job opportunity offered by the successor must be the same as the job opportunity originally offered on the labor certification.

The first requirement means that job duties, location and requirements must be identical, although the rate of pay may be increased as a result of the passage of time. Moreover, as the memorandum noted, "[a] successor in interest claim will fail if the successor is requesting that USCIS accept any changes to the items specified on the labor certification that related to the labor market test." This is not as inflexible as it may seem at first glance. Elsewhere in the memorandum, USCIS stated that increases in the rate of pay and changes of location within normal commuting distance are not considered material, and the memorandum is silent as to changes in title.

In addition, the original job opportunity offered by the seller to the foreign worker in the labor certification application must remain "valid" without interruption. Thus, according to USCIS, the job opportunity is no longer valid (and successor-in-interest eligibility will be lost), if prior to the ownership transfer, "the original job opportunity ceases to exist," e.g., by the predecessor's full or partial cessation of business operations in such a way that the "beneficiary's services are no longer required." The same requirement of a continuously valid job opportunity applies equally to the post-closing actions of the acquiring entity.

This last requirement is open to challenge. By definition, a labor certification application is a *prospective* offer of employment that only becomes effective upon the date of approval of green card status. There is no interim requirement under law, regulation or judicial decision that the job or the sponsoring employer continue to make the job available before that date (as long as the legal existence of the entity continues,

[6] The categories generally requiring labor-market testing are the second and third employment-based preference categories, whereas the first preference visa category for "priority workers" accords a more generous annual allotment of the scarce immigrant visa numbers and an exemption from the labor certification requirement.

the entity continuously maintains its ability to pay the wage offered on the labor certification application and the proffered job is available on the green-card approval date).

2. The successor bears the burden of proof to establish eligibility in all respects, including the provision of required evidence from the predecessor entity, such as "evidence of the predecessor's ability to pay the proffered wage, as of the date of filing of the labor certification with [the U.S. Department of Labor]".

M & A lawyers representing buyers take note: Your due-diligence checklist must include steps to review and preserve all evidence relating to the eligibility of the target's sponsored foreign workers for the requested employment-based immigration benefit and the seller's documentation of its immigration compliance.

Especially important are financial records of the seller that establish its ability to pay the level of compensation offered to the foreign worker on the labor certification application. This will be problematic if shortages of revenue, profit or cash flow prompted the seller to seal the deal. If employment-based green card eligibility is to be preserved after the deal closes, the seller's "ability to pay" the wage offered in the labor certification application must be established throughout an unbroken time continuum (from the date the labor certification application is filed until the deal closes).[7] If the seller's continuous ability to pay is in doubt, the acquisition agreement should provide for indemnification or a lower price that accounts for the possible diminished value of the transaction to the seller by virtue of the potential loss of key workers (or added expense in starting the green card process over again) in case USCIS denies their requests for successor-in-interest recognition.

3. For a valid successor-in-interest relationship to exist between the successor and the predecessor that filed the labor certification, "the petitioner [the putative successor] must fully describe and document the transfer and assumption of the ownership of the predecessor by the successor."

USCIS suggests that the types of evidence to document the transfer and assumption of ownership "include but are not limited to" contracts of sale and acquisition, mortgage closing statements, an SEC Form 10-K, audited financial statements of predecessor and successor for the year of transfer, proof of the transfer of real estate title and business license, financial instruments used to "execute the transfer of ownership" and media reports announcing the deal.

**Where New Form Not Needed**

Fortunately, the memorandum clearly identifies the following situations in which a new or amended Form I-140 immigrant visa petition need not be filed:

- Where the only change involves (a) a new entity name or the adoption of a new fictitious business name ("so long as the ownership and legal business structure of the petitioning employer remains the

[7] After the transaction closes, the acquirer must establish its own continuous ability to pay the proffered wage from the date of closing until green-card status is granted.

same"), or (b) the job location changes but is still within the area of intended employment as the former location (defined as within normal commuting distance). This is a welcome clarification that eliminates what has been an unnecessary expense and hassle to employers who have had only insubstantial changes.

- If the job flexibility ("portability") provisions of § 106(c) of the American Competitiveness in the 21st Century Act apply.[8] Under the cited section, a foreign worker may preserve their eligibility for lawful permanent residence even if they change jobs or employers if the following conditions are satisfied: (a) more than 180 days have elapsed from the filing of the green-card (adjustment of status) application, (b) the I-140 petition is ultimately approved, (c) the adjustment application remains unadjudicated and (d) the new position is in the same or a similar "occupational classification" as the originally sponsored job. Thus, some successor-in-interest cases may be resolved without the submission of extensive evidence of ability to pay or deal documents, but merely by the successor's filing of a letter explaining the new job requirements and duties and demonstrating why the new position is in the same or a similar occupational classification. This too is a helpful clarification.

- If the original petition was approved under the first preference "extraordinary ability" category or the second preference national-interest waiver procedure (other than for physicians in medically underserved areas). This is presumably because these categories allow for self-petitioning by the foreign worker. Since no U.S. employer is required, a change in an employer's corporate structure is not relevant to eligibility.

Also notable is the USCIS's eco-friendly recognition that – with the prior consent of the director of the Service Center where the job(s) is/are located to accept "consolidated evidence" – the successor need not include a complete set of supporting evidence relating to the terms of the deal. One set, in that situation, will do just fine, even if the successor-in-interest recognition request involves multiple foreign workers (as long as each worker's case is supported by a separate I-140 petition that includes evidence of the particular job opportunity).

**Certain Categories**

While USCIS is to be commended for attempting to modernize its interpretation of successor-in-interest eligibility, one disappointing aspect of its August 6 memorandum (offered without rationale) is its flat refusal to allow successor entities to secure pipeline green-card benefits to two of the first employment-based preference categories, i.e., those for EB1-2 Outstanding Professors and Researchers and EB1-3 Multinational Managers and Executives – both of which are exempt from the labor certification requirement. Depending on the circumstances, the burden on the acquiring entity of an organization employing outstanding professors or researchers of a new petition may not be greater than the burden of establishing that it is a successor-in-interest. For multinational managers and executives, however, a corporate reorganization can raise questions about the beneficiary's continued eligibility, and it may well be easier to establish that the acquiring entity is a successor-in-interest than it would be to establish *de novo* eligibility for the corporate transferees.

[8] Section 106(c), the portability provision of AC21, Pub. L. 106-313, is codified at Immigration and Nationality Act § 204(j); 8 U.S.C.§ 1154(j).

The agency's asserted purpose ("to allow flexibility for the adjudication of I-140 petitions that present novel yet substantiated and legitimate successor in interest scenarios") is not achieved by its blanket refusal to permit successor in interest benefits for these critically important categories. As one of the authors noted recently:

> The [USCIS] memorandum is not only arbitrary and unfair in granting special benefits when "stuff happens" to one group and denying them to similarly situated others. The memorandum flies in the face of 25 years of settled agency practice which (numerous immigration-lawyer colleagues can attest), has allowed successorship-in-interest to benefit these high-achieving denizens of academia and Wall Street.[9]

The absolute preclusion of high achievers is unjustified and unnecessary in light of longstanding agency practice.[10] The more serious problem, however, lies in the USCIS's failure to publish its interpretations as a proposed rule in the *Federal Register*, thereby allowing stakeholders to provide real-world commentary on this important area of employment-based immigration law. Given what is at stake here, USCIS should have incorporated the wisdom of dealmakers and experienced immigration lawyers on how today's deals are done, and how the relevant statutes, regulations and agency practices legitimately support an even more expansive and flexible interpretation of successor-in-interest eligibility.

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[9] Angelo A. Paparelli, blog posting, "USCIS Puts Silent Kibosh on Successorship in Interest for High-Achieving Immigrants," Sept. 10, 2009, accessible at: www.nationofimmigrators.com/?p=271.

[10] *See* Angelo A. Paparelli and Lenni B. Benson, "Life after Mergers and Acquisitions: The Immigration Impact on U.S. Employers and Alien Workers," published in New Waves for Foreign Investors in the 1990's, (AILA 1990), and The International Quarterly (Business Laws, Inc., Oct., 1990), Exhibits M and O, accessible at http://tinyurl.com/ycprdao, acknowledging that legacy INS accorded successor-in-interest treatment to immigrant visa applicants under the U.S. Department of Labor's Schedule A listing of jobs exempt from labor certification under precursor or closely comparable provisions that generally mirror the first preference Outstanding Professors and Researchers and Multinational Executives and Managers categories introduced by the Immigration Act of 1990.