COLLECTIVE BARGAINING OVER ASSET RESTRUCTURING

Edward B. Rock & Michael L. Wachter†

In both the union and nonunion sectors, firms restructure their assets and production, deciding continuously whether to make or buy an input (the subcontracting decision), as well as whether to continue or to exit a product line. The principal difference in the legal requirements applicable to restructuring in the union sector lies in the National Labor Relations Act's (NLRA) obligation to bargain over the "terms and conditions of employment." This obligation raises the legal question of when, in an asset restructuring, there is a duty to bargain with the union. The question has significance for asset restructuring in both the union and nonunion sectors because the regime of explicit contracting encouraged by the NLRA provides our clearest window into the less easily identified patterns of implicit contracting that prevail in the substantially larger nonunion sector. In this Article, we use labor economics to elucidate the nature of the question, the competing concerns, and, finally, to provide a positive theory of the law.¹

In Part I, we describe the problems raised by the restructuring of production through subcontracting and asset sales, and describe, in highly stylized form, the principal types of cases that arise. In Part II, we summarize the current state of the law as it applies to these common types of cases. Finally, in Part III, we analyze the economic logic of the legal

† Edward B. Rock is Professor of Law at the University of Pennsylvania. B.S. 1977, Yale University; B.A. 1980, University of Oxford; J.D. 1983, University of Pennsylvania.


An abbreviated version of this article was published in THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS (1987) under the title Asset Restructuring and Union Bargaining.

doctrines by summarizing the relevant economic analyses and applying them to the principal types of cases that arise.

I. TWO TYPES OF ASSET RESTRUCTURING: SUBCONTRACTING AND ASSET SALES

Firms restructure for a variety of reasons: declines in the product markets; shortages in the labor markets; changes in input markets; technological change rendering current production techniques obsolete; and so forth. In restructuring, management faces a choice between subcontracting production to a factor outside the firm (the "make versus buy" decision), or exiting the product line and disposing of the assets. The choice between subcontracting and exiting, and the choices posed within each, form basic and repeating asset restructuring fact patterns that raise characteristic issues under the NLRA's duty to bargain.

When a firm subcontracts, it moves operations (production or services) which had been carried out within the firm to factors outside the firm. In other words, the firm decides to stop making an input and to buy it instead. A prominent feature of this decision is that the firm continues in its product market, making adjustments in its input supply. Suppose that Computer Manufacturer, Inc., which, until now, has produced its own laptop cases, decides to "subcontract" laptop case production. There are three principal types of cases that arise, with a variety of cases falling in between these illustrative types:

SUBCONTRACTING A: Computer, without first bargaining to impasse, replaces the employees handling case making with lower-cost personnel supplied by an outside contractor. Employees perform the same work in the same place, under the same supervision, with no reduction in output or change in technology.

SUBCONTRACTING B: Computer hires Plastiforms, a national plastic fabricating company, which uses its own equipment and employees to make Computer's laptop cases along with other plastic products. The employees work under the tight control of Plastiforms, which uses its own scheduling and work requirements.

SUBCONTRACTING C: Computer offers its own employees the opportunity to serve as independent contractors for the firm. The case-making equipment is sold to those employees who accept the proposition. Computer buys the cases for a fixed price. However, it no longer supervises the case makers other than to demand that the cases be up to a particular quality standard.

Sometimes the firm decides not to subcontract the production of an
input to outsiders, but decides instead to exit the product line. Suppose, for example, that Computer decides to exit the laptop business. Note here, that in contrast to the subcontracting context, the firm no longer continues in its product market. Again, there are three types of cases that arise upon a decision to exit:

EXIT A: Computer sells the laptop division or subsidiary intact to Newco, which continues operations unchanged.

EXIT B: Computer terminates its laptop employees and sells its laptop-making equipment to a second-hand machinery dealer, which sells the machinery piecemeal, or, if the assets are sold as a package, to Newco, who uses the assets to make new products (e.g., disk drives), using new employees.

EXIT C: Computer sells all its laptop assets to Newco, which retains most of Computer's laptop employees and puts them to work making laptops the same way.

Subcontracting A, B, and C all raise the question of what obligations to bargain, if any, fall on an existing firm upon a decision to subcontract an input. In contrast, Exit A, B, and C all raise the question of what obligations to bargain, if any, fall on a firm which buys assets from a firm exiting a product line. The duties of the asset acquirer are known as "successorship liability" and arise under corporate law, labor law, and products liability law. In this Article, we look only at one corner of the question, namely, when an asset purchaser has a duty to bargain under the NLRA.

These six fact patterns represent the major types of subcontracting and successorship cases and raise all the fundamental issues that arise in the multitude of cases that fall in between. The issues raised by these cases are closely related to a variety of other changes of scope and direction of the firm. In particular, the analysis that we use here can be used to analyze the duty to bargain in other contexts in which it arises, namely, work relocation and reassignment.

These cases raise several concerns. In any asset restructuring, the employer can be assumed to be trying to increase profits while retaining managerial flexibility. This goal can be accomplished in a variety of ways, including buying inputs from an outside supplier who can produce them more cheaply; replacing expensive unionized employees with inexpensive nonunionized employees supplied by an outside subcontractor; selling the assets to a firm that can operate them more efficiently because of new technology or technique; or selling the assets to a firm that will maintain operations but pay employees less. For their part, the employees worry about maintaining their jobs, as well as about subcontracting or asset sales being used as a mechanism to reduce wage rates, either by replacing...
employees or by paying existing employees less.

As we will show below, the current legal regulation can be understood as a reasonably successful attempt to facilitate the efficient restructuring of enterprises while protecting each side against ex post attempts to grab a greater share of the joint surplus from the relationship. By protecting the parties against ex post opportunism, the law encourages the parties to invest optimally, ex ante, in match specific assets.

II. THE LEGAL ANALYSIS OF SUBCONTRACTING AND SUCCESSORSHIP: THE DUTY TO BARGAIN

A. The Duty to Bargain

The duty to bargain plays a central role in the NLRA system. Under sections 8(a)(5) and 8(b)(3) of the NLRA, it is an unfair labor practice for an employer or a union "to refuse to bargain collectively."\(^2\) Section 8(d) defines collective bargaining as "the performance of the mutual obligation of the employer and the representative of the employees to meet at reasonable times and confer in good faith with respect to wages, hours, and other terms and conditions of employment."\(^3\) While the parties have an obligation to meet and confer in good faith, that obligation "does not compel either party to agree to a proposal or require the making of a concession."\(^4\)

These vague but critical mandates have given rise to an extensive and complex jurisprudence.\(^5\) On the one hand, the National Labor Relations Board (NLRB) and the courts have elaborated on the duty to meet, confer, and negotiate, as well as on the obligation to deal in good faith. On the other hand, they have limited the applicability of the duty to bargain to so-called "mandatory topics," specifically—drawing on the language of section 8(d)—"wages, hours, and other terms and conditions of employment." For most other topics, bargaining is permissive, not mandatory.\(^6\)

The duty to bargain is critical for three reasons in the restructuring context. First, when the duty to bargain applies, the employer must

---

4. Id.
bargain with the union over mandatory topics, risking an economic strike if an agreement cannot be reached. Moreover, the employer will be unable to institute changes in mandatory topics unilaterally without first bargaining to impasse. Second, the duty to bargain maintains, establishes, or reestablishes a bargaining relationship between the employer and the union. Without it, the union must engage in an organizing drive, which is typically very costly and has an uncertain outcome. Third, the duty to bargain forces the parties to disclose information in certain defined contexts.\(^7\) The duty to bargain thus provides the union with a low transaction cost mechanism for reestablishing with the new employer the employee protections that it had achieved with the old employer.

While serving these goals, however, the duty to bargain creates its own opportunities for strategic behavior. Because the employer may not make unilateral changes, even during a strike, before negotiations reach an impasse, the duty to bargain provides a mechanism that skillful negotiators may use for delay. By stringing out negotiations with sequential minor concessions, anecdotal evidence suggests that a party may delay impasse, and thereby preserve the status quo, for as long as two years.

The issues relating to the duty to bargain that are central to this Article are the identification of circumstances in which the existing employer must bargain with the union before subcontracting the supply of an input (the subcontracting cases) and circumstances in which an asset purchaser takes on a duty to bargain with the union which previously represented the workers (the successorship cases).

B. Subcontracting in Labor Law

Two principal Supreme Court decisions frame the legal analysis of topics of bargaining: *Fibreboard Paper Products Corp. v. NLRB*\(^8\) and *First National Maintenance Corp. v. NLRB.*\(^9\) According to Justice Stewart's important concurring opinion in *Fibreboard*, the core conceptual distinction between mandatory and permissive topics of bargaining is whether the issue impacts "conditions of employment." Classic examples of non-mandatory issues include decisions such as investing in labor-saving machinery, liquidating assets, or deciding to go out of business.\(^10\)

---

7. When, for example, an employer claims that it is financially unable to meet the union's demands, it must corroborate such claims on request. See *NLRB v. Truitt Mfg. Co.*, 351 U.S. 149 (1956); *Sioux City Stockyards*, 293 N.L.R.B. 1 (1989); *Accurate Die Casting Co.*, 292 N.L.R.B. 284 (1989). Indeed, an employer's refusal to supply such information may convert an economic strike into an unfair labor practice strike. See *NLRB v. Jarm Enters., Inc.*, 785 F.2d 195 (7th Cir. 1986).


More generally, issues that "lie at the core of entrepreneurial control," those that involve the "commitment of investment capital and the basic scope of the enterprise," are not mandatory because they are "not in themselves primarily about conditions of employment." Similarly, topics such as the choice of "advertising and promotion, product type and design, and financing arrangements," are not mandatory because they have only an "attenuated impact on the employment relationship." We call these topics "category-1" decisions.

In contrast, mandatory topics are those decisions affecting wages, benefits, and "the various physical dimensions of [the] working environment." This includes factors such as hours, work performance, seniority, and retirement rights. In *First National Maintenance*, the explicit list of mandatory topics was expanded to include the order of succession of layoffs and recalls, production quotas, and work rules, topics "almost exclusively 'an aspect of the relationship' between employer and employee." We call these topics "category-2" decisions.

Finally, there is a third category ("category-3") of management decisions that are not clearly category-1 or category-2 decisions. These decisions, although perhaps involving the total employment level of the firm, are driven by other concerns:

[Decisions] that [have] a direct impact on employment, since jobs were inexorably eliminated by the termination, but had as its focus ... a concern ... wholly apart from the employment relationship. This decision, involving a change in the scope and direction of the enterprise, is akin to the decision whether to be in business at all.

Distinguishing between mandatory and permissive topics of bargaining within category-3 has proven difficult, controversial, and the subject of conflicting NLRB decisions. In *First National Maintenance*, the Supreme Court proposed a test in which it attempted to distinguish between topics that are primarily about labor cost issues, and are thus amenable to resolution through bargaining, and topics that are primarily about issues at the core of entrepreneurial control, as to which bargaining is likely to be futile and a burden to the employer due to the costs of delay.

In *Otis Elevator*, a plurality of the Board, in an attempt to apply the

11. *Id.*
12. *First Nat'l Maintenance*, 452 U.S. at 676-77 (expanding on Justice Stewart's opinion in *Fibreboard*).
14. See *id*.
16. *Id.*
Supreme Court's *First National Maintenance* analysis, proposed a test which, for a period of time, became the de facto standard.\(^\text{17}\) The plurality's test in *Otis II* proposed a "turns upon" standard that would mandate bargaining if the decision turned upon labor costs, but not when it turned upon the nature or direction of the business.\(^\text{18}\)

The various tests of *Otis II* were eventually rejected by the D.C. Circuit on several grounds, including inconsistency, vagueness and incompleteness.\(^\text{19}\) In response, the NLRB, rather than delineating the factors needed to implement the plurality test, offered yet another test.\(^\text{20}\) Although the new test contained important components of the plurality's test in *Otis II*, it was a distinct test. Moreover, the new test was to be applied only to decisions involving work relocation. The upshot is that the plurality's test, although applied unevenly, often with different terminology, and generally without reference, remains the prevailing standard used in implementing the Supreme Court's balancing test; however, its legal vitality remains open to question. In addition, several other tests have been developed to be applied to specific types of subcontracting.

These principles allow us to turn to the three illustrative types of subcontracting outlined above, and discuss their legal treatment.

In Subcontracting A, in which Computer replaces the employees making laptop cases with lower-cost personnel supplied by an outside contractor, employees perform the same work in the same place, doing the same jobs, under more or less the same supervision with no reduction in output or change in technology. This is the *Fibreboard* case itself. Here, as in *Fibreboard*, everything stays the same except that an outside firm provides lower-cost employees who perform the same work in the same place in the same way. Note that control of the production of the input

---


\(^{18}\) See 269 N.L.R.B. at 892.

\(^{19}\) See United Food & Commercial Workers Int'l Union, Local 150-A v. NLRB, 880 F.2d 1422, 1435-36 (D.C. Cir. 1989).

\(^{20}\) See Dubuque Packing Co., 303 N.L.R.B. 386, 390 (1991), *rev'g* 287 N.L.R.B. 499 (1987). "The standard we announce today addresses only decisions to relocate unit work. We express no view as to what standard will be used in analyzing the other management decisions . . . ." *Id.* at 390 n.8.
remains with the employer. Because the only effect of the subcontracting is to lower labor costs unilaterally, the subcontracting is a mandatory topic of bargaining.

In Subcontracting B, Computer hires a national plastic fabricating company which uses its own equipment and employees to produce laptop cases along with other plastic products. The employees work under the control of the plastic company using its own organization and work requirements. Here, the national plastic fabricating company can provide the laptop cases either at lower cost or higher quality. Control over production passes fully to the subcontractor.

If we assume further that the plastic fabricating company in fact pays higher wage rates than Computer, the law is reasonably well settled: Computer would not have a mandatory obligation to bargain over the decision. In terms of *First National Maintenance*'s balancing test, the decision would not be amenable to resolution through collective bargaining because the decision was made for reasons that were not under the control of the employees or the union.

If, however, the plastic firm's wage rates are lower than Computer's, we reach the variety of cases in which the employer subcontracts work previously done by unit employees to a third-party where labor costs may be one of the factors in the decision, or at least one of the sources of savings. This type of subcontracting arises frequently, and the legal treatment is unclear. The cases can be differentiated according to the importance of labor costs to the decision. At one extreme is subcontracting case A, *Fibreboard* itself, discussed above, in which labor costs are the sole justification for subcontracting the work.

As more and more assets and control move to the subcontractor, however, subcontracting ceases to be a mandatory topic. One step away from *Fibreboard* would be a case in which Computer subcontracts the work to an independent plastics firm. The plastics company buys the fabricating equipment from Computer and performs the work based on specifications established by Computer on everything from size to method of production. The contract allows Computer to reduce its manufacturing costs materially. Here, again, because control remained in the hands of Computer, it is clear that subcontracting would not have been profitable but for the lower labor costs of the subcontractor. Accordingly, bargaining

21. See *Furniture Rentors of Am., Inc.*, 318 N.L.R.B. 602 (1995), rev'd 311 N.L.R.B. 749, 756 (1993); *Furniture Rentors of Am., Inc.* v. NLRB, 36 F.3d 1240, 1249 (3d Cir. 1994) (noting that the subcontractor's labor costs were higher than the company's labor costs); cf. *Oklahoma Fixture Co.* 314 N.L.R.B. 958, 966 (1994), *aff'd*, NLRB v. *Oklahoma Fixture Co.*, 79 F.3d 1030, 1033 (10th Cir. 1996) (noting that the employer's subcontracting was non-mandatory because it was related to the ability of the company to manage the work and concerns over liability if the work was performed inadequately).
would again be mandatory. The only difference between this case and *Fibreboard* itself is that the subcontractor supervised its own employees in implementing Computer’s detailed instructions and used its own capital. These, however, are unimportant differences. Although the supervisor brought its own capital, different employees were still working with the same capital, which was the case in *Fibreboard*.

But now consider Subcontracting C: Suppose that Computer decides to end its laptop case fabrication operations, and, without first bargaining to impasse, offers its own employees the opportunity to serve as independent contractors for the firm. The fabricating machines are sold to those employees who accept the offer. Computer buys the laptop cases from the subcontractor, but no longer supervises the fabricating operations, other than demanding that the products satisfy Computer’s customers and manufacturing needs.

Although such cases are somewhat unusual, they are important to understanding the legal standard and, as discussed below, the economic logic. In two cases decided shortly after *Fibreboard*, the courts held that bargaining in such circumstances was not mandatory. Although, as in *Fibreboard*, the same employees perform the tasks in the same location, control had passed from Computer to the now independent contractors. In both *NLRB v. Adams Dairy* and *Local 777*, *Democratic Union Org. Comm. v. NLRB* [hereinafter *Yellow Cab*], the courts of appeal held that this was a critical difference because the now independent owner-distributors determined the exact tasks to be performed. Because control had passed,

---

22. See Mid-State Ready Mix, 307 N.L.R.B. 809 (1992). This case establishes that the Board will find a case mandatory where the facts are similar to those of *Fibreboard*. The employer, Torrington, “simply replaced the two employees hauling sand and stone with a nonunit employee and independent contractors, also hauling sand and stone.” Id. at 810. Although Torrington no longer transported cement powder in its own trucks, it continued to use the same products and the same technology. In addition, the subcontractors delivered materials to it under arrangements and schedules set by Torrington. See id. at 819.

23. See *NLRB v. Adams Dairy, Inc.*, 350 F.2d 108 (8th Cir. 1965). In outsourcing the work, Adams Dairy sold its trucks to the new distributors, but did not finance the sale or in any way facilitate the financing. It also sold the goods to the contractors, who, thereafter, had complete freedom to conduct the business operation subject only to certain quality conditions that needed to be met. The routes of the independent contractors did not correspond to the previous routes of the driver-salesmen. The independent contractors took title to the products at the dockside, and Adams, thereafter, legally had no concern with what was done with the products. Adams was not directly concerned with any given distributor’s profits or losses, and the distributors had complete latitude in such critical matters as the price they charged their customers, the drivers they employed, and the use of helpers. See id. at 111; see also *Local 777*, Democratic Union Org. Comm. v. NLRB, 603 F.2d 862 (D.C. Cir. 1979) [hereinafter *Yellow Cab*], rev’d *Yellow Cab Co.*, 229 N.L.R.B. 1329 (1977).

24. See *Yellow Cab*, 603 F.2d at 874 (“[The fundamental question is whether the employer] has the right to control the driver during the course of his operation of the cab in
the savings, as in case B above, were likely to come from a more efficient operation and not simply from lower wage rates.

C. Successorship Obligations of a Purchaser

From a corporate law perspective, there are two ways to transfer assets that, leaving aside tax considerations and opportunistic behavior, serve two very different purposes. When the predecessor wishes to transfer the operations as a going concern, the transaction is typically structured as a merger or a stock sale. In such cases, from both the corporate law and labor law perspectives, the transfer is essentially a non-event. All contracts, leases and licenses remain in effect, and the firm, under its new ownership, bears all obligations that the firm under its old ownership had, including the duty to bargain.

By contrast, when a firm does not wish to transfer operations as a going concern, but, rather, wishes to liquidate, it will typically dispose of the assets piecemeal. Under corporate law, an asset purchaser generally takes on only those obligations of the asset seller that it explicitly or implicitly assumes. Because this general rule can, in certain cases, lead to manipulation of the transactional forms in order to impose costs on third parties, the rule is subject to several exceptions. For example, the general rule, when combined with the corporate law rule that permits corporations to dissolve and cut-off future claimants, creates an opportunity for firms to avoid liability to long-tail tort claimants, which in turn creates a possibility for the externalization of risk. To avoid this problem, the law seeks to impose liability on the asset purchaser as a way of forcing the asset seller to internalize the cost of future accidents.


26. Specifically, suppose that Firm X makes widgets that tend to explode after twenty years. If Firm X continues, it will be liable for the damages caused by the exploding widgets. Suppose, however, that Firm Y buys only the assets of Firm X, and then Firm X dissolves after paying off all current and contingent creditors. Under the traditional corporate law framework, when the widgets began to explode twenty years later, the victims would be without recourse. If the victims were to sue Firm Y, they would be met with the argument that Firm Y acquired only the assets of Firm X, not the liabilities, and is therefore not liable. If they were to sue Firm X, they would be met with the argument that Firm X no longer exists and, even if victims could trace the former shareholders of X, that their claims are barred as a matter of the law governing the dissolution of corporations. Such externalization is inefficient in the obvious way: because the future victims cannot negotiate an appropriate price to bear the risk of explosion, widget manufacturers will fail to internalize the full costs of widgets.

27. For a summary, see Rock & Wachter, supra note 1, at 203.
A similar legal structure has evolved under the National Labor Relations Act. In *Fall River Dyeing & Finishing Corp. v. NLRB*, the Supreme Court held that, when substantial continuity exists between the business of the asset seller and purchaser, the asset *purchaser* has a duty to bargain with the seller's union if "the majority of its employees were employed by its predecessor." Note, however, that the seller's decision to go out of business (either by selling stock or by selling assets) is not a mandatory topic of bargaining, although the seller does have a duty to bargain over the "effects" of the decision to exit.

Substantial continuity has two elements: continuity of operations and continuity of work force. The courts and the Board measure substantial continuity of operations by whether the purchaser has "acquired substantial assets of its predecessor and continued, without interruption or substantial change, the predecessor's business operations." In measuring substantial continuity of operations, the NLRB examines a number of factors, including whether the business of both employers is essentially the same; whether the employees of the new company are doing the same jobs in the same working conditions under the same supervisors; and whether the new entity has the same production process, produces the same products, and has the same body of customers. Substantial continuity of the work force depends on what proportion of the new employer's work force was employed by the old employer.

Because the successor has no duty to hire the predecessor's employees, however, the Court concluded that triggering the duty to

---

29. *Id.* at 41.
30. *See First Nat'l Maintenance, 452 U.S. at 681.*
32. *See Fall River, 482 U.S. at 43.*
33. A threshold question is whether the changes resulting from the capital market transaction have affected the "appropriateness" of the bargaining unit. In making its bargaining unit determination, the NLRB looks to a "community of interest" among the workers. The factors in defining a community of interest include, for example, the similarity in the method of determining compensation; the similarity in benefits, hours, or other terms and conditions of employment; and common supervision and determination of labor relations policy. *See Archibald Cox et al., Labor Law: Cases and Materials* 283 (10th ed. 1986). *Fall River* did not resolve the ambiguity in prior cases with respect to whether the duty to bargain attaches if the asset purchaser hires a majority of the seller's represented employees but those employees do not constitute a majority of the employees of the purchaser. *See Fall River, 482 U.S. at 46 n.12.* The Board, supported by the courts of appeal, has held that work force continuity only exists if a majority of the asset purchaser's employees were employed by the seller. *See Saks & Co. v. NLRB, 634 F.2d 681, 684-86 & nn.2-3 (2d Cir. 1980) (citing relevant cases); Spruce Up Corp., 209 N.L.R.B. 194, 196 (1974), enforced, 529 F.2d 516 (4th Cir. 1975); United Maintenance & Mfg. Co., 214 N.L.R.B. 529, 532-34 (1974).*
bargain "rests in the hands of the successor." The courts have made it clear, though, that an asset purchaser cannot avoid a duty to bargain by discriminating against employees of the seller because of their union status. What counts as antiunion animus in the failure to hire employees of the asset seller has been litigated extensively. Critical factors that suggest antiunion animus include: efforts by the new employer to discover from the old employer the union sympathies of its employees, followed by a refusal to hire those identified as sympathetic; hiring criteria with a disparate impact; and an overall scheme designed to ensure that fewer than a majority of the employees are union members. Factors inconsistent with animus include unsuitability for new employer's operations, and uniformly applied, valid business reasons for hiring a totally inexperienced work force. In the aggregate, these factors suggest that, if a new employer maintains the old operations intact, the hiring of new, inexperienced, nonunion employees in preference to experienced, union employees indicates antiunion animus. By contrast, if operations are changed so substantially that experience in the old operation would be of little value in the new operation, no such inference is warranted.

How, then, are our three successorship cases described above to be analyzed? In Exit A, Computer exits the laptop business by disposing of the business intact, as a going concern, by selling the stock of the laptop subsidiary to Newco, who continues to make laptops the same way. In this case, the duty to bargain carries forward.

In Exit B, Computer exits the laptop business, and disposes of its assets either piecemeal or wholesale to a buyer who redeployes the assets to make different products differently, and who does not retain the

34. Fall River, 482 U.S. at 41.
36. For a general discussion, see the cases cited in 1 THE DEVELOPING LABOR LAW, supra note 5, at 797 nn.168 & 170. United Food & Commercial Workers Int'l Union v. NLRB, 768 F.2d 1463, 1470-71 (D.C. Cir. 1985), rev'd in part and aff'd in part, 268 N.L.R.B. 1483 (1984) [hereinafter Spencer Foods], provides one case in point. In Spencer Foods, the court found that an asset purchaser discriminated against the union when it adopted a hiring standard which disqualified many former union members from consideration for reemployment but did not apply the standard uniformly in comparable situations. Id. at 1474-76. By way of contrast, in Inland Container Corp., 267 N.L.R.B. 1187 (1983), modified by 273 N.L.R.B. 1856 (1985); 274 N.L.R.B. 887 (1985); 275 N.L.R.B. 378 (1985), Inland claimed that it refused to hire the predecessor's workers because, having not been trained in the "Inland Way," they had formed "bad habits." When the record showed that Inland applied this rule in comparable situations, the Board found no antiunion animus. See Inland, 267 N.L.R.B. at 1190. Subsequent evidence that Inland only hired applicants willing to work in a nonunion environment, however, led the Board to reverse this finding. See 275 N.L.R.B. at 382-88.
37. See, e.g., United States Marine Corp. v. NLRB, 944 F.2d 1305, 1315-17 (7th Cir. 1991), cert. denied, 112 S. Ct. 1474 (1992); Spencer Foods, 768 F.2d at 1474-76.
employees. As a result, while there may or may not be substantial continuity of operations, there is no substantial continuity of workforce and, thus, no duty to bargain, absent a finding of antiunion animus.

By contrast, in Exit C, Computer sells its assets, its laptop machines, to a new operator who continues to produce laptops the same way using most of the same employees. In such cases, the duty to bargain carries forward.

III. THE ECONOMIC LOGIC OF THE LEGAL STRUCTURES

A. The Economic Model of the Employment Relationship: Contracting Over Investments in Match

Our analysis draws on the “Internal Labor Market” (ILM) literature in labor economics. In this model, the relationships between a firm and its ongoing employees can best be understood as a structured market, with its own governance procedures that set, for example, wages, hours, conditions of employment, promotion opportunities, and the grievance process. The interactions between the firm and its employees are frequent, iterative and complex, with the job and relationship evolving over time. The goal of the firm and its employees is taken to be the maximization of joint profits. Like any other relationship, the employment relationship is assumed to be based on the potential for mutually advantageous exchange.

There are two central features of the typical employment relationship that shape the nature of the interaction and the solutions that emerge. First, the relationship is characterized by investments in the firm-employee match that are lost if that match terminates. That is, the match investments are sunk. Investments in match are defined as investments that are more valuable to the contracting parties than to a third party. We use the term “match-specific” investments in place of the perhaps more common “firm-specific” or “transaction-specific” investments or “investments in human capital” because of its greater precision. Some but not all investments in human capital will be investments in match. The term is more accurate than “firm-specific” investments because it focuses better on the contracting problem: some investments in match may, indeed, be more specific than the firm level.

Second, the relationship is characterized by bilaterally asymmetrical information. While the employees have superior information with respect

to their work effort and opportunities for employment outside the firm, the employer has the information advantage with respect to the technology and the market demand for the output produced by the employees.

The sunk investments in match create the potential for opportunistic behavior. The potential is aggravated by the asymmetry of information which sometimes enables the opportunistic party to disguise its actions. In addition, the asymmetry of information acts as a side constraint on any solutions to minimize opportunistic behavior.

For the employment relationship to induce the parties to invest optimally in their match, solutions must be found to constrain such behavior. Consider the standard problem posed by investments in match-specific training. If a trained employee can produce more than an employee hired from the outside, and if the employer bears the cost of training, the employee, after being trained, can “hold up” the employer by threatening to leave to work elsewhere unless the employer increases wages. Similarly, if the employee bears the cost of training, the employer, ex post, can hold up the employee by threatening to fire the employee unless the employee accepts lower wages. Such threats are credible because the investing party, but not the non-investing party, stands to lose the return on its match-specific investments. The standard solution to this problem is joint investment in the training: because both parties will bear a loss if the relationship is terminated, the ability of either party to use the threat of terminating the relationship to gain a greater share of the joint surplus is reduced.

The ILM literature shows that many standard features of the employment relationship can be best understood as incentive compatible solutions to similar problems of opportunistic behavior. One example is the common practice of laying off employees during times of product market downturn (and running the risk of losing an employee in whom the employer has invested resources in training), rather than reducing wages (and keeping the trained employee on the payroll). Despite the bilateral investments in the match, a reduction in wages is not incentive compatible, given the asymmetry of information: the employer has an incentive to misrepresent product market conditions, to reduce wages, and gain a larger

39. We define opportunistic behavior as behavior whose purpose is to capture ex post a larger share of the parties' joint surplus from the sunk investments in match.

share of the joint surplus. By contrast, layoffs are incentive compatible because the employer will bear a loss of output which it will be willing to do only if product market demand has in fact declined.\textsuperscript{41}

The rules governing firms' exit from an industry parallel those governing temporary layoffs. The rule that firms can unilaterally implement a decision to go out of business has strong incentive compatible properties. Once out of business, the firm has lost whatever value is in the ILM. Hence, the firm will only close when the ILM is indeed unprofitable. The rules governing the process control the firm's incentives to profit from the process or to pretend to be going out of business, by imposing direct costs (severance pay) and indirect costs (laying off less expensive junior workers before more expensive senior workers) on such a firm.

The above analysis extends to subcontracting and successorship, which generate different avenues for opportunism on the part of the employer. In the prototypical subcontracting arrangement, the employer hires a subcontractor who provides a labor input and terminates the match with its own employees who had provided the service. The employer, however, typically continues to operate unchanged in the principal product market. Although such actions may be justifiable because the existing match-investments have proven unprofitable, they create a possibility of opportunistic threats or actions that merely redistribute the surplus from existing employees. By contrast, in successorship, the employer typically sells the assets that generate the product. In this case, the predecessor employer can only be acting opportunistically if it can sell the assets at a higher price to the successor, by putting the successor in an improved position to act opportunistically.

B. The ILM Analysis of Subcontracting Doctrine

Asset restructuring involving the subcontracting of work raises specific difficulties not found in other types of restructuring. In particular, because the firm continues in its product market after the prototypical subcontracting, the firm's major sources of revenue are left unchanged and the firm retains the control over product market based assets. Restructuring that primarily involves labor cost changes is sensitive to

\textsuperscript{41} The ILM relationship between the parties is protected by either of two mechanisms. In the union sector, the parties write explicit contract terms, enforceable by third parties, to protect their investments. In the nonunion sector, the parties typically use norms that are intended to be self-enforcing and are thus not enforced by third parties. Even in the union sector, however, the written contract terms have central self-enforcing features. Since third-party enforcement is always costly, the ability to rely on the other contract terms is important.
opportunistic behavior, as the firm can redirect payments from its employees to its own profits without directly impacting revenue. However, not all subcontracting is open to opportunism on the part of the employer. Some types, although affecting labor costs, are implemented because of changes in the external environment which have made the parties' match-assets no longer profitable to the employer under the current terms. For example, some types of subcontracting are motivated by the need to adjust to technological or regulatory changes, in which labor costs are only peripherally involved. The three fact patterns developed above are useful in showing how the law differentiates between these cases.

**SUBCONTRACTING A: Potential Opportunism.** The ILM is efficient, but Computer denies that any surplus exists and subcontracts the work. The subcontractor's only function, however, is to supply lower cost labor to Computer. Since the same work is performed in the same place using the same equipment, the ILM is clearly still profitable and is retained unchanged. From Computer's perspective, only the wage rate was too high. By outsourcing the work, Computer increases its own profits by inserting new employees into the match-assets created with its former employees. The employer's actions are not self-enforcing since its actions allow it to capture the entire surplus created by the match-assets.

**SUBCONTRACTING B: Efficient Liquidation.** Here, the ILM is defective, either creating no surplus or incurring losses. By subcontracting the work and allowing the subcontractor to exercise full control of the manner in which the work is performed, Computer exits this part of the supply chain and abandons the match-assets. The subcontractor employs its own match-assets using its own employees and capital. Because the old match-assets are abandoned, there is no potential for opportunism by Computer.

**SUBCONTRACTING C: Efficient Transfer.** The ILM is efficient, but Computer does not realize sufficient profits to retain this part of the supply chain. Alternatively, Computer believes that the match-assets are more profitable if controlled by its employees. By selling the physical assets of the match to the employees, Computer exits the supply chain. The match-assets, however, remain in place, but with the right to control passed to the employees who now become independent contractors. The potential for opportunism is low since Computer no longer retains control over the match-assets and the profits generated by the assets. Because the employees can decline the option of becoming independent contractors, which would force Computer
to hire independent contractors at market rates, Computer cannot capture the match surplus by setting a supercompetitive price for the match-assets that it sells to its own employees.

The task of labor law subcontracting doctrine can be best understood as facilitating subcontracting case B and C transitions, while preventing case A transitions. The goal is to create incentives for the optimal levels of investment in match-assets. This is accomplished by allowing firms to exit unprofitable matches while preventing them from capturing the employees' share of the surplus in profitable matches.

The legal rule accomplishes this task by focusing on the right to control the surplus to be realized from the use of the match-assets and not on labor costs alone. Contrast *Fibreboard* and *Adams Dairy*. In *Fibreboard*, the employer merely replaced its employees with those of the subcontractor. Nothing else had changed, and the match-assets, minus the employees, remained in use. The new subcontractor, presumably, paid market wages to hire its employees. Hence, the match-assets, in prevailing wages terms, were not unprofitable in themselves. By subcontracting, Fibreboard's managers, a joint creator of the match-assets, retained the profitable ILM structure, but used lower-wage subcontracted workers to perform the same work. Since there were no changes in operations, the result was a pure shift in the surplus from the match from workers to the firm. The rule in *Fibreboard* deters such opportunistic behavior. Fibreboard was not permitted simply to implement the change. Instead, prior to implementation, it would need to bargain to impasse and to accept the risk of a strike. *Fibreboard* is thus the classic example of case A subcontracting.

In *Adams Dairy*, on the other hand, the Dairy itself exited the ILM, leaving the employees who were willing to remain in place in charge of the match-assets. The right to control the method in which the match-assets were used was transferred to the employees. The employees, and not Adams Dairy, were now the residual claimant on the returns generated by the match-assets. Although Adams Dairy would hope to have lower distribution costs than before, the ability to sell the assets at a super-competitive rate was limited by the ability of the employees to refuse the offer, at which point the assets would have to be sold to a third party. By "cashing out" of their investment, the decision by Adams Dairy was not prone to opportunism. By accepting the offer, the employees could change the method in which the match-assets were used in any fashion that would increase their return. The decision would be most profitable to the firm if,

42. In *Fibreboard*, the subcontractor provided workers to do "the same task in the same plant under the ultimate control of the same employer." *Fibreboard*, 379 U.S. at 224 (Stewart, J., concurring).
in fact, the assets were more profitable if left to the employees' control. In such a case, the firm would be able to cash out with lower distribution costs and the former employees, now independent distributors, would have higher income.

The legal rule, used in *Adams Dairy* and then formalized in *Yellow Cab*, creates appropriate incentives for the efficient transfer of assets. When the employer believes that the parties' surplus is maximized by making employees the owners of the match-assets, it is free to exit the match unilaterally and to sell the match-assets to the employees who wish to purchase them. To protect against opportunistic transfer, however, the employees must be given the right to control the variables at the core of entrepreneurial control. That is, the employees must be truly independent owner/operators and the employer must have truly cashed out of both the supervisory and the residual claimant roles. With the employer unable to exercise any supervision, it cannot take steps to redistribute the surplus realized by the employees indirectly. *Adams Dairy* and *Yellow Cab* are thus classic examples of case C subcontracting.

The same economic factors are also at work in case B subcontracting. In cases where the motivation for the subcontracting did not involve labor costs, the decision to subcontract is a permissive topic. In *Oklahoma Fixture Co.*, the employer's decision to exit from the wiring work was driven by its inability to manage that line of business and its fear that accidents would cause it to lose the business of its one main customer. Although the record is vague on the topic, it appears that the subcontractor would hire union labor and pay approximately the same wage rates as did Oklahoma Fixture. Consequently, the employer was not decreasing its labor costs by subcontracting. In this situation, the employer was not acting opportunistically. By abandoning the match-assets, it would suffer a loss on that investment, as would the employees who would be laid off. Effectively, the match-assets were no longer profitable when judged against a market test.

Requiring bargaining in such circumstances, however, would allow the union to act opportunistically. Since the decision was motivated by factors outside of the union's control, it is unlikely that bargaining would change the outcome. Since mandatory bargaining introduces the potential for costly delay, the union could threaten to impose that delay in order to extract some payment for allowing the firm to move forward with an inevitable decision.44

The key factor for distinguishing between opportunistic and efficient


44. Note that the "effects" of the decision are a mandatory bargaining topic. Hence, the firm must bargain over any severance payments or job-transfer rights with the union.
subcontracting is whether control over match-assets has been transferred, and not merely whether labor cost savings are present. Subcontracting is opportunistic if and only if the employer will retain control over the work, that is, when the factors identified in *Fibreboard* are present: similar work, similar workplace, with control under the ultimate control of the employer.  

A failure to appreciate the importance of control has led to inconsistency in cases in which labor costs are a factor in the decision, but not necessarily the causally decisive factor. As testimony to the confused state of the law, the Board has not agreed upon a method for determining when labor costs are the motivating factor behind the decision. The D.C. Circuit's criticism of the plurality standard in *Otis II* was based on the fact that the Board had not indicated the factors it would use to determine when a decision "turned upon" labor costs. The D.C. Circuit thus held that:

> [If] the Board desires to adhere to the "turned upon" formula as controlling . . . it must identify for us the kinds of factors it takes into consideration in determining the employer's contemporaneous motive for its decision, and then apply those factors to the record in this case in order to determine whether . . . [the facts] support[] the conclusion that the company's decision "turned upon" entrepreneurial factors, rather than labor costs.  

When the Board abandoned *Otis II* and announced a new test in *Dubuque Packing*, it did not provide an answer to the question. In fact, the legal rule for subcontracting became even murkier since the *Dubuque Packing* test applied only to matters of relocation.

In *Rock-Tenn Co. v. NLRB*, the employer subcontracted the work to a national trucking company which integrated the work with its other business. Despite this, the Board believed, and the D.C. Circuit concurred, that labor costs were the "primary concern" in the decision. But the Board never explained how it determined that labor costs were the primary factor and, in ruling on the case, it failed entirely to appreciate the importance of "control" over the work. From the opinions, it appears that Rock-Tenn entirely left the trucking business, giving complete control over the work to the subcontractor, which is substantial evidence that Rock-Tenn had abandoned any match-assets and thus that the subcontracting was not opportunistic. Despite this, the issue did not even enter into the Board's reasoning. The Board's focus on labor costs rather

---

45. *See Fibreboard*, 379 U.S. at 224 (Stewart, J., concurring).
46. *United Food & Commercial Workers Int'l Union, Local 150-A v. NLRB*, 780 F.2d 1422, 1435 (D.C. Cir. 1989) [hereinafter *Dubuque Packing*].
47. 101 F.3d 1441, 1446 (D.C. Cir. 1996).
48. *See id.*
than control led it to confuse an example of Subcontracting B (efficient liquidation) with Subcontracting A (opportunism).

C. The ILM Analysis of Successorship Doctrine

Similarly, from an ILM perspective, three situations are of interest in determining whether successorship doctrine deters rent seeking.

EXIT A: Efficient Transfer. The ILM of the old firm creates a surplus. The new firm recognizes that the ILM creates a surplus and in order to preserve the efficient ILM, willingly retains the old firm’s employees and assumes both the collective bargaining agreement and the duty to bargain. Case A apparently characterizes most changes of control and rarely leads to litigation. When the new firm wishes to acquire the old firm as a going business, and to continue it as such, the new firm has no reason to disrupt established and efficient labor relations. Consolidations are difficult enough without making them more so by sowing discord. The easiest way to accomplish Case A transitions is by a merger or stock sale.

EXIT B: Efficient Liquidation. The ILM of the old firm is defective, either creating no surplus or incurring losses. If assets are disposed of wholesale, the new firm recognizes that the old ILM is defective. The new firm reconfigures the operations, including personnel practices and structures, and hires few, if any, of the old firm’s workers. Case B transitions are typically asset sales. Case B cases are largely self-enforcing: the firm makes credible its assertion that the ILM generates no surplus by jettisoning it. By dissolving the old ILM, the firm precludes itself from capturing joint surplus generated by that ILM.

EXIT C: Potential Opportunism. The ILM of the old firm is efficient, but the new firm denies that any surplus exists. At the same time, the new firm attempts to capture the joint surplus by hiring most of the old firm’s employees at a wage closer to the employees’ opportunity wage and by refusing to bargain collectively. In exit case C, the new firm tries to have it both ways. It tries to maintain an efficient ILM while reducing the share of the joint surplus paid to the workers. Unlike case B situations, the new firm’s representation is not self-enforcing. By (mis)representing that no joint surplus exists, perhaps by threatening not to hire the old workers except at lower wages, the firm creates a basis for reducing workers’ wages—and thus their

49. This is an anecdotal impression. We do not know of any evidence on the relative frequency of cases A, B, and C.
share of the surplus—while at the same time maintaining and benefiting from the efficient ILM. As was true in subcontracting law, the task of labor law successorship doctrine can best be understood as facilitating cases A and B transitions, while preventing case C transitions. A failure to control the opportunistic behavior of case C will undermine the creation and maintenance of productive ILMs.

Consider, now, the legal doctrine. Recall the fundamental legal differences between mergers and stock sales, on the one hand, and asset sales on the other. As discussed above, the duty to bargain continues unchanged through a merger or stock sale. Because the merger form is the legal form most often used to transfer productive ILMs intact, this rule largely blocks the employer’s case C attempt to maintain the ILM but increase its share of the joint profit by, for example, misrepresenting the condition of the product market. This is precisely what happened in *Esmark, Inc. v. NLRB*: the old firm was preserved entirely intact with the same workers and the same operations. The court correctly held that the collective bargaining agreement and the duty to bargain continued unchanged through the sale of stock. Similarly, the doctrine prohibits union attempts to use the vulnerability of the firm during such a transition to gain a greater share of the joint surplus.

More subtly, the legal rule also blocks the attempt to transfer a productive ILM organization but eliminate the old workers. Contrast *Esmark* with *Spencer Foods*. In *Spencer Foods*, the original owners closed the plant and laid off the workers. After an eighteen-month hiatus, following a stock sale, the new owners reorganized operations slightly and reopened the plant. The new Spencer Foods refused to bargain with the old union, accepted applications from all interested persons, including former employees, but hired only a very small proportion of former Spencer employees. The union charged—and the administrative law judge, the Board, and the court all agreed—that Spencer Foods relied on hiring criteria designed to keep the former unionized Spencer employees to

---

50. *See* *Esmark, Inc. v. NLRB*, 887 F.2d 739 (7th Cir. 1989). Esmark, a conglomerate, owned the leading meat packer, Swift & Co. Swift’s fresh meat operations had been losing money. Esmark claimed that, although Swift’s plants were efficient in that the workers were productive and the output was of high quality, the wage rates at the two rendered them uncompetitive. Esmark sought to reorganize operations to put the two plants outside the master collective bargaining agreement and outside the existing duty to bargain with the union. Five days before Esmark sold 65% of the fresh meat operations to the public, it closed the two plants and laid off the workers. Eight days after the public offering, New Sipco, the subsidiary that now owned the plants, informed the union that it would reopen the plants and, as a “successor employer,” would unilaterally set lower wage rates. *See id.* at 742-44, 759.

51. *See id.* at 752.
a minimum and thus keep the union out of the plant.\textsuperscript{52}

The court held that, because the layoffs were not intended to be permanent, but only part of the "'sale of an ongoing business enterprise to L[and] O['] L[akes], i.e., a business which encompassed the resumed operations of the Spencer plant by S[pencer] F[oods] [albeit] under new management,'"\textsuperscript{53} and because there was an expectation that the plant would be reopened, the duty to bargain carried forward beyond the expiration of the CBA and through the hiatus. Moreover, the court held that applying discriminatory criteria to avoid rehiring old workers was itself an unfair labor practice.\textsuperscript{54}

From the ILM perspective, \textit{Spencer Foods} is more problematic than \textit{Emark}. At first blush, it seems to involve a classic case B situation: the new Spencer Foods, by not rehiring the old employees, made clear that it did not value the old ILM. The old Spencer Food's history of poor labor relations is consistent with this hypothesis. While in \textit{Emark} the firm attempted to have it both ways—to retain the ILM intact (including employees) but avoid bargaining with the union—the new Spencer Foods put its money on the line. How, then, could Spencer Foods have been behaving opportunistically?

Doctrinally, the answer is straightforward: antiunion animus is always an unfair labor practice.\textsuperscript{55} Moreover, the economic rationale for this general rule is similarly straightforward. Without such a bar, workers would be unable to escape from their free-rider problems and bargain collectively. Hence, for unions to facilitate efficient contracting in ILMs, a rule prohibiting antiunion animus is necessary.

The successorship context itself also provides two additional answers. First, to the extent that employees are asked to make ongoing investments in the organization of work—investments that may be sunk—they will not make optimal investments unless they are protected from ex post attempts to grab an additional share of the joint surplus from those investments. That is precisely what the firm may be doing when it seeks to retain the organization of work, but to staff it with new, cheaper employees. In this regard, the situation is nearly identical to the \textit{Fibreboard} situation, discussed above.

There is a second explanation as well. Consider a broader time frame. Suppose that in the first period the firm refuses to rehire former employees

\textsuperscript{52} See \textit{Spencer Foods}, 768 F.2d at 1467-68, 1475.
\textsuperscript{53} Id. at 1472 (quoting \textit{Spencer Foods}, 268 N.L.R.B. at 1509).
\textsuperscript{54} See id. at 1475-76.
in order to keep out the union, but during the second period it rehires the skilled former employees as it terminates the unskilled and inexperienced new hires. Under such circumstances, in the second period the workers would bear the cost and delay of reorganizing and renegotiating, having just suffered an extended layoff due to their union membership. By delaying the re-establishment of the efficient ILM in order to eliminate the union, the firm might secure a greater share of the joint surplus. Indeed, more generally, given that the division of the joint surplus—as in other bilateral monopolies—depends on the bargaining abilities of the participants, investing in a reputation for toughness may be worthwhile.

Consider, now, the alternative transactional form, the sale of the assets themselves. Recall, from above, that absent tax and strategic considerations, firms will sell assets when the ILM is unproductive and when they wish to liquidate it. In the paradigmatic sale of assets, the asset purchaser wishes only to acquire pieces of the asset seller, not to acquire the asset seller as a going concern. The normal asset sale is thus a case B situation: the asset purchaser does not value the old ILM and, by jettisoning it, precludes itself from capturing any of the old ILM’s joint surplus. Normally, as described above, an asset purchaser only takes on those obligations that it assumes.

Importantly, case B situations are largely self-enforcing. In these cases, the firm’s representation that the old ILM is inefficient, combined with the firm’s actions in reconfiguring the assets and not hiring the old workers, makes the assertion inherently credible. By dissolving the old ILM, the firm puts its money where its mouth is. While the firm may be wrong—it may be that the old ILM creates joint surplus—it cannot be acting opportunistically.

Thus, in the case B situation, in which the asset purchaser does not continue the old operation or hire the old workers, there is no continuing ILM that requires protection; hence, the law treats the former workers exactly the same as any other creditor of the firm. When the ILM is discontinued, the corporate law’s protection of creditors of the asset seller protects former employees’ contractual claims. Workers may only collect from the asset seller anything to which they are contractually entitled under the collective bargaining agreement, such as unpaid wages, accrued vacation pay, and accrued pension contributions. The asset purchaser has no special obligations to the seller’s employees.

Moreover, such a rule helps to discourage both the destruction of productive ILMs and the preservation of unproductive ILMs. An ILM may be inefficient because the workers have used their right to strike to extract a contract that transfers the firm’s share of the surplus to the workers. Similarly, workers may want to retain an ILM which is inefficient for other reasons in order to maintain contract provisions that
return a surplus to them, even when the firm is generating losses. In both cases, a predecessor firm stuck with such an inefficient ILM can jettison it through an asset sale. Faced with the potential exit of the firm through an asset sale, workers will be less likely to use their bargaining power to extract a surplus that leaves the firm with losses.

That the prototypical asset sale involves an inefficient ILM also explains why asset sales are governed by different rules than mergers. The corporate law goal of encouraging efficient restructuring of those assets that do not generate a surplus, while retaining those that do, requires standard form mechanisms that can be applied to the two situations at low cost. This explains why the merger cases do not apply to asset sale cases, contrary to the expectations of traditional labor law scholars.

Of course, as in the corporate context, a background rule that asset purchasers do not take on the seller’s obligations creates the potential for case C strategic manipulation. The background rule offers asset purchasers an opportunity to retain the productive old ILM, but to secure a larger share of the joint surplus by using an asset sale rather than a merger in order to escape from the duty to bargain. Consequently, asset buyers and sellers will have an incentive to share in the additional portion of the joint surplus that the sale captures from the employees.

The challenge for the legal rule is to preserve the necessary option of dissolving an inefficient ILM and disposing of assets while blocking the opportunistic use of that transactional form. The legal rule described above represents an attempt to do this.

Recall the rule: when there is no substantial continuity, there is no duty to bargain collectively until the union establishes majority support; when there is substantial continuity, majority support is presumed, and the firm must bargain collectively until it establishes lack of majority support. As discussed above, when the asset purchaser jettisons the old ILM, as demonstrated by lack of substantial continuity, no danger exists of opportunistic behavior on the part of the firm. But when the asset purchaser retains the old ILM, a potential for opportunistic behavior arises that courts must constrain in order to facilitate optimal investments in ILMs.

The necessity of controlling this sort of opportunistic behavior provides an explanation for why labor law successorship doctrine grants greater protection to employees than corporate law successorship doctrine grants to creditors generally. In the general corporate case, courts protect creditors either by requiring that the asset seller make provision for long-tail claimants before dissolution or by using asset purchasers as a conduit to impose these costs on asset sellers. But the ILM differs significantly: labor law successorship doctrine must protect the forward-looking, match-specific investments in the continuing ILM.
The duty to bargain is critical to labor law's attempt to constrain opportunistic behavior while facilitating nonopportunistic reconfigurations of assets. As discussed earlier, the duty to bargain is an obligation to meet and confer "in good faith" over mandatory topics, without any obligation to reach an agreement.\textsuperscript{56} Such a duty to bargain will facilitate the renegotiation of terms and conditions equivalent to those in the prior ILM. But this duty only protects workers in whom the firm has made productive investments. It does nothing to protect employees who are easily replaced. In particular, the duty to bargain will not allow such employees to protect any union wage premiums that they previously secured in the old collective bargaining agreement.

The duty to bargain constrains opportunistic behavior in this context in two ways. First, by relieving the union from the burden of showing majority support, with the attendant costs of organizing and costs of delay, imposing a duty to bargain lowers the employees' costs of protecting or reestablishing the bargain over the division of the joint surplus that they had previously struck with the asset seller. Second, by forcing the asset buyer to corroborate claims regarding the condition of the product markets, this duty makes it more difficult for the new employer to secure a greater share of the joint surplus by misrepresentation.

Consider, for example, \textit{Fall River},\textsuperscript{57} in which a majority of the asset purchaser's work force had worked for the asset seller, doing essentially the same work. In such circumstances, employees face a continuing danger that the purchaser will act opportunistically, claiming that the ILM is inefficient in order to appropriate a portion of the joint surplus while at the same time taking full benefit of its value. Imposing a duty to bargain helps to maintain the presumptively efficient ILM while preventing the asset purchaser from using the uncertainty of the changeover to secure a greater share of the joint surplus.

Moreover, such a rule imposes a minimal burden on the asset purchaser. If the purchaser values the ILM, as demonstrated by its decision to continue operations and to hire the old employees, then it must continue the practice of bargaining collectively. If, on the other hand, the purchaser does not value the ILM, it will not hire the old employees and will have no obligation to bargain collectively. Indeed, in \textit{Fall River} the Supreme Court seemed largely to have made a version of this argument:

Thus, to a substantial extent the applicability of [the duty to bargain] rests in the hands of the successor. If the new employer makes a conscious decision to maintain generally the same business and to hire a majority of its employees from the

\begin{flushright}
\textsuperscript{56} \textit{See generally id.} ch. 13. \\
\textsuperscript{57} \textit{See Fall River}, 482 U.S. at 27.
\end{flushright}
predecessor, then the bargaining obligation of § 8(a)(5) is activated. This makes sense when one considers that the employer intends to take advantage of the trained work force of its predecessor.58

The rule prohibiting discrimination against employees of the asset seller on the basis of their union membership reenters at this point. As with the merger context, if the asset purchaser could maintain operations unchanged but escape from the duty to bargain by refusing to hire former union members or by refusing to recognize the union, then an opportunity would exist for unproductive strategic behavior. The rule against antunion animus blocks this prospect. If an asset purchaser leaves operations unchanged but employs practices that effectively exclude former union employees, such action constitutes evidence of antunion animus. After all, so long as operations are unchanged, one would expect that the old employees in whom the firm has made match-specific investments would be the most attractive candidates. If a firm disproportionately excludes the most attractive applicants, one can infer that it excluded them in order to keep out the union. By contrast, when no substantial continuity in operations exists, no such inference arises. To the extent that the operations are changed, the match-specific investments in and by the old employees have little value—indeed, they may even impose a cost—and criteria of selection that have the effect of hiring new workers do not suggest animus. In this way, the law governing successorship, like the law governing subcontracting, discourages opportunistic behavior by both employers and employees.

IV. CONCLUSION

In this Article, we have described when a duty to bargain about subcontracting and successorship arises under the National Labor Relations Act, and have explained many (but not all) features of the current law as at least a roughly effective mechanism for encouraging efficient restructuring while discouraging opportunistic behavior by the contracting parties. The incentive-compatible contracting analysis that we use here reveals the economic logic that underlies the legal doctrine, thereby providing what both the cases and the more traditional analyses fail to provide: a positive theory that provides a guide for analyzing new cases. But, as we show in other work, the applicability and importance of this analysis is not limited to the collective bargaining context, a relatively marginal sector of the economy. Rather, because the NLRA system provides our clearest window into the informal and implicit contracting

58. Id. at 40-41.
between firms and employees, our analysis provides the basis for a general analysis of bargaining over asset restructuring.