

MANUFACTURING & INDUSTRIAL: OUTLOOK & TRENDS

Learn about trends, opportunities and challenges
in the manufacturing and industrial space.

BASS
BERRY
SIMS



Centered to deliver.

MANUFACTURING & INDUSTRIAL: OUTLOOK & TRENDS

As the manufacturing and industrial sectors continue to embrace digital transformation and navigate complex global markets, the year ahead presents both new opportunities and challenges. From evolving data privacy and AI regulations to legal considerations in property selection and renovations, manufacturers must stay agile to remain compliant and competitive.

***Manufacturing & Industrial: Outlook & Trends* explores key topics, including the impact of privacy laws on manufacturing operations, legal hurdles in industrial property redevelopment, and the critical lessons learned from John Deere's Foreign Corrupt Practices Act violations. Together, these insights highlight a handful of key trends and issues impacting the regulatory and operational landscape within the manufacturing and industrials industry.**

Trends in Indemnification Terms for Environmental Matters

Contributors: Frank Pellegrino, Courtney Black, Steve Taylor, John Dawson

A seller's post-closing indemnity obligation is a topic our industrial clients want to discuss in detail when buying or selling a business. The indemnification section of the definitive purchase agreement allocates risk between the parties and therefore is heavily negotiated. While the relative bargaining power of the parties will influence such negotiations, the nature of the acquired business also plays a role in defining the indemnification terms. It should therefore be no surprise that in the industrial space, both parties pay close attention to the indemnification terms for environmental matters.

The general survival period establishes the amount of time in which the buyer can bring indemnification claims against the seller for losses resulting from the seller's breaches of its representations and warranties. According to recent deal studies on private mergers and acquisitions (M&A) transactions from the last two years, approximately 20% of transactions analyzed in the manufacturing and industrial sectors had a general survival period of 12 months and 12% of such transactions had a general survival period of 18 months (Practical Law, "What's Market" Analytics). However, certain representations are carved out from the general representations and treated as fundamental representations, resulting in a longer survival period equal to the applicable statute of limitations, another fixed period, or indefinite duration. The general statute of limitations on environmental laws is six years - in deals that involve industrial businesses, buyers typically try to require the seller to bear the unknown risk of the full statutory lookback period. Whether or not environmental representations are deemed fundamental largely depends on the bargaining power of the parties and the nature of the business. For example, recent deal studies indicate that approximately 13% of the transactions analyzed with survival provisions carved out seller's environmental representations from the general survival period.

The buyer may also propose "specific indemnities," which allocate to the seller the losses resulting from specific liabilities identified during due diligence. In industrial acquisitions, buyers often seek specific indemnities for compliance with environmental laws and/or permit deficiencies because of the significant impact such deficiencies can have on the business. Depending on the extent of the deficiency, it may be costly to come into compliance with the applicable environmental laws and securing deficient permits may require fundamental changes to business operations. For manufacturers, the business' compliance with environmental laws and permitting requirements can therefore not be underscored when it comes to limiting potential post-closing obligations.

For acquisitions that instead utilize representations and warranties insurance policies (RWI Policies), there are certain limits on environmental liabilities that buyers should be aware of. For example, there are certain standard environmental exclusions in RWI Policies (e.g., asbestos). There is also a recent trend among RWI Policies for broader environmental exclusions, especially for contamination-related liabilities. While RWI Policy exclusions are otherwise generally deal-specific, buyers are required to procure Phase I and Phase II Reports more frequently. Any findings therein are discovered during the carrier's diligence and subsequently excluded from the RWI Policy. Although an additional cost to consider, should the parties have difficulty allocating any environmental exclusions between themselves, there are also environmental insurance policies that sellers can purchase to cover their exposure and address levels of risk tolerance. Furthermore, resolving claims under RWI Policies can turn into a mini-litigation - often taking six months or more to adjudicate.

In sum, the indemnification terms for environmental matters will play an important role in the negotiations of an industrial acquisition. In the traditional indemnification structure, sellers will have to establish their risk tolerances for longer survival periods and specific indemnities for environmental liabilities. In acquisitions utilizing RWI Policies, buyers and sellers will be tasked with allocating any environmental exclusions between themselves. Buyers may also have to devote significant time and resources to recover under RWI Policies.

Key Employee Benefit Plan Considerations in M&A Transactions

Contributor: Curtis Fisher

An often overlooked area of concern in M&A transactions is the review, integration, and transitioning of the target's employee benefit plans. In particular, in a stock sale or merger transaction, the liabilities of the target's employee benefit plans are assumed, making it essential to thoroughly review these plans. Early in the deal process, decisions regarding the transition of the target's employees and their benefit plans should be prioritized, especially in sectors like manufacturing and industrial, where workforce stability and benefits can significantly impact operations.

Below we've highlighted a few key concerns we routinely address in M&A transactions regarding retirement plans, with a focus on the unique challenges faced by manufacturing and industrial firms.

TERMINATION OF TARGET PLANS

A prompt decision to terminate or continue the target's retirement benefit plans is crucial once a Letter of Intent (LOI) is entered into. For manufacturing firms, where employee retention is vital due to specialized skills and training, a decision regarding the target's 401(k) plan should be made quickly. Once a transaction closes, any existing 401(k) plan cannot be terminated and must instead be merged into the acquirer's plan, which can be a time-consuming and costly endeavor. Additionally, if the target has a "cash balance" or other defined benefit pension plan, the decision to terminate and fully fund the plan needs to be made swiftly. The purchase agreement should ensure that the costs associated with such funding and termination are clearly apportioned to the target and its shareholders.

COLLECTIVELY-BARGAINED EMPLOYEES

In manufacturing and industrial settings, collective-bargaining agreements are common, particularly in unions representing skilled trades and laborers. If any target employees are covered by such agreements, it is imperative to quickly review these contracts during the diligence process to determine any multiemployer plan liabilities. Multiemployer plans—often used in manufacturing sectors—are maintained by unions to provide pension benefits and are typically contributed to by various unrelated entities. These plans can be severely underfunded, leading to significant liabilities that must be considered when assessing the overall value of the target. In the case of an asset sale, the target may be subject to withdrawal liability, further complicating the transaction.

IDENTIFYING COMPLIANCE CONCERNS

A comprehensive review of the target's retirement plan documents and records is essential to identify any material compliance issues. Common compliance challenges in manufacturing and industrial firms include late deposits of 401(k) deferrals and loan repayments, misclassification of independent contractors, exclusion of eligible employees, late Form 5500 filings, and nondiscrimination testing failures. Early identification of these issues allows for a proper risk assessment and facilitates discussions about indemnity and other protections that should be negotiated with the target.

Increased Union Activity and NLRB Regulations Affecting Manufacturing

Contributors: Tim Garrett, Lymari Cromwell

Union activity and heavy regulation by the National Labor Relations Board (NLRB) have been impacting manufacturing in recent months and years. The NLRB's General Counsel has been quite active in returning to Obama-Board-era scrutiny of handbooks and work rules, as well as severance agreements that contain confidentiality clauses and non-disparagement provisions. For example, the standard for evaluating whether certain work rules violate employees' Section 7 rights almost guarantees that an NLRB investigator will find that certain work rules over-reach and violate the law. That finding could require not only re-writing the overly broad rule but also "undoing" any discipline (including a termination) that resulted from enforcement of the unlawful rule.

The NLRB also adopted a controversial new structure in a union organizing setting. In a case known as **Cemex Construction Materials Pacific LLC (Cemex)**, the NLRB announced a new procedure that applies when an employer receives a demand for recognition from a union claiming to have majority support among employees in an appropriate unit. Previously, an employer could ignore such a demand, and the union would then have to file a petition with the NLRB for an election. There would then be several weeks of "campaigning" followed by an NLRB-scheduled election. Now, an employer, when faced with such a demand for recognition from a union, must either recognize the union and bargain or file a petition with the NLRB for an election. Plus, if the employer who is seeking an election by filing this petition commits any unfair labor practice that would result in setting aside the election, the petition for the election will be dismissed (canceling the election), and the NLRB will order the employer to recognize the union and be required to bargain with it.

Navigating the Loan Landscape: Opportunities and Challenges for Middle-Market Manufacturers

Contributor: Leslie Ford

The loan market for middle-market companies (typically defined as those with annual revenues between \$10 million and \$1 billion), including those in the manufacturing and industrial sector, in the first three quarters of 2024 saw a continuation of the higher interest rate environment that began in 2022. This is attributed in large part to the Federal Reserve's efforts to combat inflation and a challenging macroeconomic environment, including global political tensions and economic uncertainty. Higher interest rates over the past few years have impacted the cost of borrowing, making it more expensive for manufacturing and industrial companies to secure attractive financing for capital expenditures, equipment upgrades, and operational expansions. This has led many companies to pursue debt restructuring transactions where available, to gain access to greater flexibility and better terms. For their part, lenders are eager to deploy capital but are simultaneously cautious about credit risk, placing a greater emphasis on a company's creditworthiness.

In such a selective lending environment, lenders are looking for manufacturing and industrial companies with strong credit history, growth potential or a unique value proposition, and some companies have found it difficult to access capital.

As traditional banks have tightened their underwriting criteria over the last few years, many middle-market companies have turned to alternative sources of financing, particularly the private credit market. Banks that depend on selling or “syndicating” their position in larger loans to other banks have encountered greater difficulty doing so in recent years, and combined with the slowdown in the M&A market, this has led to a sluggish syndicated loan market. Private credit (loans provided by non-bank institutions, also called “direct lending”) increasingly has been filling this gap. Direct lenders originate loans and hold them until maturity (a “lend to hold” model), meaning that they do not rely on syndication (although they frequently will form a small “club” of 2-6 other direct lenders). These lenders primarily target middle-market and smaller borrowers, including many manufacturers that may not fit the traditional banking mold. Given the capital-intensive nature of the manufacturing industry, which often requires significant investment in machinery and technology, the ability to secure direct loans that offer flexibility in terms and structure can be very beneficial for companies in this sector.

The private credit market is not subject to many of the same regulations as traditional banks. Therefore, they typically have a greater appetite for more highly leveraged transactions or untraditional financings, making them particularly attractive to manufacturing and industrial companies needing greater flexibility in loan terms, especially those facing variable cash flows or looking to invest in innovative processes. One such model is the “recurring revenue” financing, in which underwriting is based on recurring revenue instead of EBITDA. This approach allows some manufacturers to access financing even though they may have low or negative EBITDA (and thus may not be a viable credit for a traditional bank) because they are generating recurring revenue and thus have significant growth potential.

On the flip side, there are potential downsides for borrowers engaging in the private credit market. Direct loans have traditionally been more expensive (although credit spreads on direct loans and broadly syndicated loans have converged somewhat in recent years). And because many of the banking regulations coming out of the 2007-2008 financial crisis do not apply to direct lenders, they have greater opportunities to take on riskier transactions. Some regulators view this as a potential systemic risk in the economy, given reduced oversight of this growing segment of the credit market.

The Federal Reserve's September 2024 half-point interest rate cut, which was larger than expected and the first cut since March 2020, may help alleviate some pressure on financing costs, potentially contributing to a rebound in financing activity in the fourth quarter of 2024 and beyond. This reduction could drive increased deal flow in both the broadly syndicated and private credit markets, creating opportunities for manufacturing companies to secure the necessary capital to invest in efficiency improvements, automation, and other strategic initiatives aimed at enhancing competitiveness.

Privacy Laws Impacting Manufacturing

Contributors: Emily Burrows, Alex Davenport

In today's digital age, manufacturing companies are increasingly reliant on technology to streamline operations, improve efficiency, and enhance product quality. They are embracing emerging technologies like artificial intelligence (AI), which are fueled by massive amounts of data and cloud computing. However, this reliance on emerging technologies and data also raises significant concerns about data privacy and security.

With the rise of smart factories, connected devices, AI-enabled robotics, and advanced data analytics, manufacturers must navigate a complex landscape of privacy and AI-related laws and regulations that impact operations. Further, many legal requirements are currently being drafted or are already signed but not yet effective, which will continue to inform the enforcement environment. Manufacturers subject to these regulations should be agile and resilient to protect valuable assets and avoid regulatory penalties, mass litigation, and other risks.

THE IMPACT ON MANUFACTURING OPERATIONS

Data Collection and Management

Manufacturers often gather vast amounts of data—from machine performance metrics to customer feedback. Privacy laws require that companies only collect data that is necessary and relevant, leading to a reevaluation of data management practices. This may involve implementing data minimization strategies, where only essential data is collected and retained.

Supplier Relationships

Manufacturers often rely on a network of suppliers and vendors, which can complicate data privacy compliance. When sharing personal data with third parties, manufacturers must ensure that these partners adhere to the same privacy standards. This necessitates thorough vetting processes and contractual agreements that outline data protection responsibilities.

Integration of AI and Machine Learning

AI and machine learning (ML) (a subset of AI that uses algorithms to analyze data and recognize patterns to make decisions and perform tasks) can be used to help reduce costs, increase efficiency and quality, and improve safety and worker experience. However, AI and ML must be used in compliance with privacy laws (and all other laws) applicable to the manufacturer. Further, AI-specific laws at the state, federal and international levels are in effect or will be coming into effect in the coming years.

Employee Data Privacy and AI Considerations

With the rise of remote work and digital monitoring tools, manufacturers seek less friction and more convenience for the verification of identities and face new challenges in protecting employee data. Privacy laws often require companies to inform employees about data collection practices and obtain their consent, especially with respect to the collection of biometric data (i.e., fingerprint and retina scans, face prints, etc.). Certain AI laws also focus on the use of AI in recruitment, hiring, promotion and discipline. Disclosures regarding the use of AI in hiring may be required depending on the jurisdiction.

Cybersecurity Measures

As manufacturers adopt more connected devices and Internet of Things (IoT) solutions, the risk of data breaches increases. Privacy laws often mandate specific cybersecurity measures to protect personal data. Manufacturers must invest in robust cybersecurity infrastructures to safeguard sensitive information, protect against data breaches and other cyber threats, and comply with legal requirements.

STRATEGIES FOR COMPLIANCE

To navigate the complexities of privacy and AI laws, manufacturers can adopt several strategies:

1. **Conduct Regular Audits:** Regular data privacy audits can help manufacturers identify what data is collected and for what purposes, which enables manufacturers to understand their vulnerabilities and ensure compliance with applicable laws.
2. **Implement Privacy by Design:** Incorporating privacy considerations into the design phase of products and processes can enhance compliance. This approach emphasizes the importance of data protection from the outset, rather than as an afterthought.
3. **Invest in Training:** Educating employees about privacy laws and data protection practices is crucial. Training is particularly important when AI is being used in a manner that could put personal data or safety at risk or when AI involves confidential information from the manufacturer. Training programs can raise awareness of the importance of data privacy and ensure that all employees understand their roles in safeguarding sensitive information.

4. **Engage Legal Experts:** Given the complexity and evolving nature of privacy laws, consulting with legal experts can help manufacturers stay informed about regulatory changes and ensure compliance.

CONCLUSION

The impact of privacy and AI laws on the manufacturing sector is profound and multifaceted. As manufacturers embrace digital transformation, they must prioritize data privacy to protect themselves, employees and stakeholders. By understanding the regulatory landscape and implementing robust compliance strategies, manufacturers can navigate these challenges while fostering trust with customers and partners alike.

Legal Considerations When Selecting/ Renovating Existing Industrial Properties for Manufacturing Operations

Contributor: Cheyne Harris

When selecting a new location for business operations, manufacturers may consider revitalizing and renovating vacant industrial properties rather than elect to lease or purchase and develop a new facility.

As construction costs continue to escalate and unimproved industrial property within established core industrial areas within cities become harder to find, the renovation and redevelopment of older vacant industrial properties and buildings is becoming more common. The benefits of renovating industrial buildings range from minimizing the impact on the environment's carbon footprint by recycling existing structures to the reduction in building material costs. In addition, there are several federal and state tax incentives available to businesses that elect to redevelop existing industrial properties. However, even though there are numerous benefits associated with the renovation and adaptive reuse of industrial properties, unfortunately, there are also certain legal and practical challenges that may arise. Those challenges include zoning and environmental issues as well as building regulations.

ZONING

Zoning is one of the first legal considerations that must be explored and addressed when redeveloping an existing industrial property. Most municipalities have zoning ordinances that dictate a property's permitted uses, bulk requirements, and other development requirements and restrictions. It's important to research all of these zoning items at the outset of any adaptive reuse project as they present challenges that may affect how the property is redeveloped and whether the project is viable. For example, a city's local zoning ordinance may not allow or contemplate certain types of manufacturing facilities within a selected property's designated zoning district. In that instance, the project may not be worth pursuing as the cost and time required to obtain the necessary zoning amendments, variances or approvals may be too high or time consuming.

Manufacturing businesses must also confirm whether a particular property can meet the bulk (or site) requirements imposed by the local zoning ordinance both now and in the future. The bulk requirements under certain zoning ordinances are often determined based on the type and size of manufacturing operations at the property as well as the number of employees at the property. Accordingly, the local zoning ordinance may have certain open space and parking requirements that prohibit a business from developing the property to meet its current manufacturing operations or its future operations should the business ever plan to expand its operations at the same location. Furthermore, it may not be practical or feasible to satisfy all of the zoning requirements associated with the type of manufacturing use due to certain site constraints such as the existing footprint of the building or the necessary points of access into the property.

ENVIRONMENTAL

Older industrial properties may present certain environmental issues that may not otherwise exist with newer undeveloped properties. Depending on the property's prior use and the type of materials used in the construction of the original improvements, there may be hazardous materials and substances present at the property that require removal and remediation before the project can move forward. Generally, it's best to avoid these particular properties as the cost to remove the hazardous substances and complete any necessary remediation is usually very high and sometimes prohibitive. Businesses may also be taking on certain environmental liabilities that could have been avoided by selecting a different property. Accordingly, before selecting or acquiring any industrial property, businesses should hire an environmental consultant to perform a site assessment to determine if any of these environmental issues exist.

BUILDING REGULATIONS

Another challenge to consider when determining the feasibility of redeveloping an existing industrial property is bringing the property into compliance with current building codes and regulations. In addition to local municipal requirements, the property may also need to be updated to comply with federal statutes like the Americans with Disabilities Act and federal safety standards such as those under the Occupational Safety and Health Act. Depending on its location, the redeveloped property may also be required to conform to specific energy efficiency standards, the extent and severity of which can vary widely from jurisdiction to jurisdiction. The age of the property can be a deciding factor in whether updating the property to adhere to current regulations and laws will be cost prohibitive—the older the property, typically the more costly it will be to bring the property into compliance with current requirements.

CONCLUSION

Before deciding to rehabilitate and renovate an existing industrial property, businesses should weigh the unique pros and cons of engaging in a renovation project versus leasing, purchasing and/or developing a new facility. Ultimately, the issues noted above should always be considered when making this determination.

John Deere Pays Nearly \$10 Million for FCPA Violations Related to Thai Bribery

Contributor: Thad McBride

On September 10, the Securities and Exchange Commission (SEC) [announced](#) that Deere & Company (John Deere), a manufacturer of agricultural and other equipment, agreed to pay almost \$10 million to resolve alleged violations of the FCPA. The FCPA prohibits bribery of foreign officials and requires publicly traded companies, like John Deere, to abide by specific books and records and internal accounting controls provisions.

The violations involved John Deere's subsidiary, Wirtgen Thailand, which John Deere acquired in 2017, and which apparently engaged in eye-catching bribery schemes to obtain business. For example, in 2019, Wirtgen Thailand paid for four Thai Department of Highways (DOH) officials to tour Switzerland instead of traveling for a legitimate purpose to the company's German facility. Wirtgen Thailand submitted a bid on a DOH tender during the trip and was awarded the tender soon afterward. Wirtgen Thailand also regularly entertained Thai officials at massage parlors. Bribes were apparently paid both directly and through a third party.

The payments were inaccurately recorded in the company's books and records as legitimate expenses and - probably not surprisingly - lacked detail. To settle the matter, John Deere agreed to pay a monetary penalty of \$4.5 million and disgorge approximately \$5.4 million, the profit (and interest on that profit) the SEC calculated the company made through bribery. In announcing the settlement, the SEC highlighted John Deere's failure to adequately integrate Wirtgen Thailand into its internal control system following the acquisition.

The settlement is thus a valuable reminder of the importance of thorough due diligence during an acquisition and, perhaps even more importantly, comprehensive compliance integration post-closing.

Contributors & Contact Information

Courtney L. Black

615.742.7888 | courtney.black@bassberry.com

Emily A. Burrows

615.742.7848 | eburrows@bassberry.com

Lymari Martinez Cromwell

615.742.6219 | lymari.cromwell@bassberry.com

Alexandria Wood Davenport

615.742.7786 | adavenport@bassberry.com

John W. Dawson IV

615.742.7796 | jdawson@bassberry.com

Curtis L. Fisher

615.742.7892 | cfisher@bassberry.com

Leslie M. Ford

615.742.7791 | lmford@bassberry.com

Tim K. Garrett

615.742.6270 | tgarrett@bassberry.com

Cheyne W. Harris

901.543.5913 | cheyne.harris@bassberry.com

Thaddaeus R. McBride

202.827.2959 | tmcbride@bassberry.com

Frank M. Pellegrino

615.742.7947 | fpellegrino@bassberry.com

T. Stephen C. Taylor

615.742.7758 | staylor@bassberry.com

About the Bass, Berry & Sims Manufacturing & Industrial Team

With a proud tradition of representing leading manufacturers, Bass, Berry & Sims combines in-depth industry knowledge with comprehensive legal solutions tailored to the unique challenges of today's competitive marketplace. Our experienced attorneys collaborate across various sectors to provide proactive counsel in areas such as contract negotiation, mergers and acquisitions, finance, environmental, and regulatory compliance, among others. We are committed to helping clients navigate the complexities of the manufacturing and industrials industry, ensuring their operations are both efficient and legally sound. More information about the firm's experience in this sector can be found [here](#).



@BassBerrySims



Bass, Berry & Sims



@BassBerrySims

BASS BERRY & SIMS

Centered to deliver. bassberry.com