

Employee Count Threshold Brief

Executive Version

Decision-ready intelligence for growth-stage founders who cannot afford to discover their people debt during due diligence.

What This Brief Does

Every growth-stage company crosses three headcount thresholds where the rules change, the risks multiply, and the cost of inaction shifts from manageable to deal-killing. This brief identifies the exact threshold points, the specific exposures that appear at each one, and the controls that must be in place before you cross each line.

These are the visible risks. The full assessment surfaces four additional exposures — the Shadow Liabilities — that only appear during acquisition due diligence after it is too late to fix them without delaying or killing your deal.

PHASE 1: FOUNDATION

Employee Count Threshold: 1 to 14 Employees

Classification and Onboarding Chaos

THE RISK:

One worker classification error triggers back tax liability, a Department of Labor audit, and immediate investor confidence problems. The exposure is not theoretical. Average reclassification liability for a single misclassified worker — including back taxes, unpaid overtime, benefits owed, and legal defense costs — typically ranges from \$100,000 to \$175,000 before penalties and interest. This is seed-stage capital destruction.

The IRS Common Law Control Test and the Department of Labor's economic reality test are separate frameworks administered by separate agencies. A single misclassified contractor can trigger liability under both simultaneously, meaning your exposure compounds across two enforcement channels at once.

DEPLOY BEFORE YOU CROSS THIS THRESHOLD:

- ✓ Offer letters with explicit employment terms, at-will language, and IP assignment clauses for every employee
- ✓ Worker classification defense file for every 1099 contractor documenting behavioral control, financial control, and type of relationship factors
- ✓ Time tracking system for all non-exempt workers matching actual operations and pay cycles

Three Thresholds. Four Hidden Exposures. One Assessment.

The risks on these pages appear on every compliance checklist. What does not appear — the Shadow Liability Ledger covering the Contractor Reclassification Time Bomb, the Multi-State Nexus Trap, the Verbal Equity Promise, and the Exempt Classification Error — surfaces exclusively during acquisition due diligence. Continue to see what your threshold controls are missing.

CONTINUED

PHASE 2: DANGER ZONE

Employee Count Threshold: 15 to 49 Employees

Performance Issues Become Legal Exposure

THE RISK:

At 15 employees, Title VII of the Civil Rights Act applies. Informal performance management — the verbal feedback and undocumented conversations that worked at 8 people — becomes discrimination lawsuit vulnerability overnight. Typical settlement exposure for a single wrongful termination or discrimination claim exceeds \$125,000 before legal fees. The discovery process that accompanies employment litigation exposes your entire organization to investor scrutiny at precisely the moment you can least afford it.

This threshold also activates state-level leave and accommodation obligations in most jurisdictions, creating a second compliance layer that most founders do not discover until an employee requests leave and the company has no documented process for handling it.

DEPLOY BEFORE YOU CROSS THIS THRESHOLD:

- ✓ Anti-discrimination and harassment policies with documented manager training and acknowledgment records
- ✓ Performance documentation system with written warnings, improvement plans, and pre-termination review protocols that managers will actually use
- ✓ Leave and accommodation intake process with clear eligibility determination authority and centralized tracking

PHASE 3: COMPLEXITY THRESHOLD

Employee Count Threshold: 50 to 99 Employees

The Compliance Cliff That Tanks Valuation

THE RISK:

At 50 full-time equivalent employees — not 50 headcount, but 50 FTEs including proportional part-time workers — the federal compliance landscape changes materially. The Family and Medical Leave Act applies. The ACA employer mandate activates, requiring Forms 1094-C and 1095-C reporting. Missing or incomplete leave administration and benefits systems at this threshold can reduce exit multiples by 0.5x to 1.0x based on patterns observed in lower middle market M&A transactions, as private equity buyers systematically discount offers when they discover administrative debt during due diligence.

The full-time equivalent calculation is a common founder blind spot. An employer with 35 full-time and 30 half-time employees is an Applicable Large Employer subject to ACA obligations even though full-time headcount appears to be 35. Buyers find this during payroll records review. You will not find it until they do.

DEPLOY BEFORE YOU CROSS THIS THRESHOLD:

- ✓ FMLA-compliant leave administration system with eligibility determination, designation notices, and manager decision authority that does not create operational bottlenecks
- ✓ ACA benefits eligibility tracking with automated reporting covering full-time equivalent calculations, not just raw headcount
- ✓ Compliance calendar with clear ownership covering FMLA administration, ACA reporting deadlines, OSHA filings, and state-specific obligations built into a system, not stored in founder memory

What These Three Phases Do Not Show You

The risks on the previous pages appear on every compliance checklist. They are the visible surface of your people operations exposure. The full assessment covers four additional exposures that do not appear on standard checklists and surface exclusively during acquisition due diligence — after it is too late to fix them without delaying or killing your deal.

*These include the **Multi-State Nexus Trap** — the compounding tax and penalty exposure created by remote employees in states where you are not registered — and the **Verbal Equity Promise**, the promissory estoppel claim that materializes when a key employee discovers at closing that the equity conversation from three years ago was never formalized. The other two shadow liabilities follow the same pattern: invisible until a buyer's counsel finds them, expensive to resolve under deal pressure.*

The Valuation Reality

When sophisticated buyers evaluate your company they calculate what it will cost to operate your business after they own it. Chaotic people operations translate directly into valuation reductions through two mechanisms depending on how your company is valued.

\$1,350,000

Valuation reduction for profitable companies at a 6x EBITDA multiple when buyers assume a VP of HR hire to fix people operations chaos.

\$11,250,000

Valuation reduction for a \$15M revenue growth-stage company at a 0.75x revenue multiple discount based on observed lower middle market M&A transaction patterns.

Your Next Step

The three threshold risks above are the ones every founder eventually learns about. The question is whether you learn about them from this brief or from a buyer's due diligence counsel. The Shadow Liability Ledger covers what comes next.

The full assessment includes:

- ✓ 15-Question Executive Readiness Scorecard calibrated to your headcount phase
 - ✓ Shadow Liability Ledger with four detailed exposure analyses and dollar calculation frameworks
 - ✓ Dual-method Valuation Impact Calculator for both EBITDA and revenue multiple scenarios
- Complete 90-Day Remediation Framework with sequenced priorities, timelines, and budget ranges

Founder rate \$97 through March 31. Standard investment \$197.

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