

LABOR & EMPLOYMENT PRACTICE GROUP

WORKFORCE REDUCTIONS IN THE PRIVATE SECTOR

JANUARY 2009

COMPLYING WITH LAWS AND AVOIDING COSTLY LITIGATION

The slumping economy is prompting increased numbers of workforce reductions. According to the latest available statistics published by the Department of Labor, December saw a drop in payrolls of 524,000 employees, bringing the total jobs lost in the last four months of 2008 to a staggering 1.9 million. Job losses are expected to continue through early 2009. There were also 9,258 mass layoff events January through June 2008, with each event involving a layoff of 50 or more persons, and there have been thousands more layoff and downsizing events in smaller numbers that are not reflected in these statistics.

Workforce reductions are painful for affected employees, and even those retained suffer tension and morale issues. But whether for one person or several thousand, conducting a workforce reduction is a knotty process for employers also. In order to reduce the risk of litigation, employers must plan carefully and give attention to many issues. Some of the top considerations are:



- Avoiding discrimination and wrongful discharge claims;
- Crafting selection procedures;
- Providing advance notice;
- Offering severance pay;
- Entering into Separation Agreements;
- Paying final wages, bonuses and commissions;
- Paying vacation and other accrued time off; and
- Continuation of health insurance

Avoiding discrimination and wrongful discharge claims

Most often, the elimination of certain positions or an overall reduction of a workforce in a variety of positions is motivated either by the need to cut costs or a desire to improve efficiency, as opposed to targeting specific individuals for termination. An employer likely has no intent to discriminate against those terminated based on their legally protected status of race, gender, age, disability, national origin, religion or other special classification. Nevertheless, if individuals in one or more of these classes protected by federal and state non-discrimination laws are adversely affected, there can be a perception of disparate treatment discrimination or an effect of a disparate adverse impact on certain protected groups of persons selected for termination.

Employers must be sensitive to these issues when crafting reduction plans and take a close look at the characteristics of the individuals selected for termination and those selected for retention.

Frequently, when downsizing takes place to reduce costs, employers may target higher paid positions for elimination. This often results in the termination of older employees who have greater seniority, and provides the fodder for age discrimination claims.

Employees on legally protected leave, such as Family and Medical leave, worker's compensation leave or military leave are not immunized from layoffs made for legitimate business reasons unrelated to their leave status, but again, awareness and extra care should be used. In addition, if termination appears disproportionately to single out those who have engaged in protected activity, such as union organizing or complaints of harassment or illegal practices, the possibility of lawsuits increases.

Employers can best insulate themselves from these types of claims by being able to demonstrate that their decisions were based on reasonable business factors, which is why establishing overall goals to be met and designing appropriate selection processes to meet the goals becomes all important.

Crafting Appropriate Selection Procedures

No federal or state laws dictate how employers make decisions on which jobs to eliminate or whom to select for layoff. Nor are employers required to have workforce reduction policies. However, employers who do have such policies need to follow them to avoid potential breach of contract claims. Employment agreements should be reviewed to determine whether individuals working under those agreements have guaranteed employment for a certain term.

Unionized employers must also follow any layoff provisions covered in their collective bargaining agreements.

Where there are no contracts or policies in place, companies that plan a workforce reduction should design a system which is geared to accomplish their goals by utilizing business-related criteria to select those who will be terminated and those who will be retained. In general, employers usually weigh or score such factors as seniority, performance, job skills and positions to be eliminated or reduced.

A recent Supreme Court decision, *Meacham v. Knolls Atomic Power Lab.*, highlights the importance of having documented selection criteria, which are as objective as possible, and that will support the non-discriminatory bases for an employer's actions.

In that case, the company laid off 31 salaried employees with 30 being at least 40 years old. Twenty-eight of them sued alleging disparate impact age discrimination in violation of the federal Age Discrimination in Employment Act ("ADEA") and state law. In making its termination decisions, the company told its managers to tabulate scores for their subordinates by awarding points based on the worker's two most recent performance appraisals, assessing points for years of service and granting a numeric score for each of "flexibility" and "critical skills." The scores given for flexibility and critical skills were necessarily dependent on the subjective judgment of the managers and thus more suspect than the other two criteria. The Supreme Court held that the employer had the burden of proof and persuasion in producing evidence that demonstrated the factors used were reasonable and not discriminatory.

This Supreme Court decision demonstrates the importance of designing a selection process with as many objective factors as possible. When criteria involving subjectivity are necessary, it is advisable to have evaluations performed by a group of management personnel, as opposed to a single manager or department head.

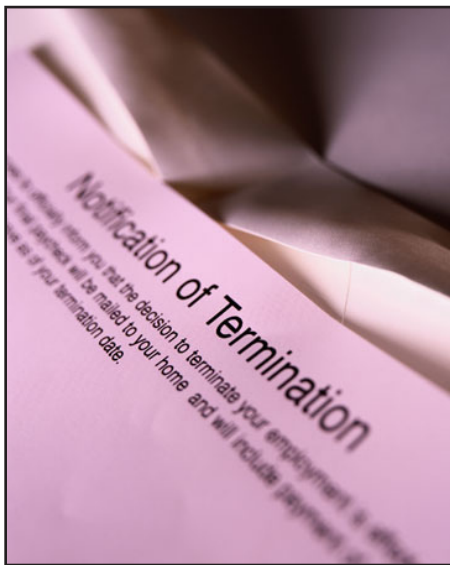
Providing Advance Notice to Workers

Management is often reluctant to provide advance notice of a reduction in force to employees who will be terminated. This reluctance may be based on fear of low morale and a consequential adverse effect on productivity or attendance, or even a fear of sabotage or document theft.

In several situations, however, advance notice may be required. Employment agreements may require providing advance notice of no-cause terminations. Union contracts may have provisions requiring advance notice, and even without such contract provisions, employers may have a legal obligation to provide sufficient notice to give the union the opportunity to bargain over the effects of a downsizing.

In some situations, the federal Worker Adjustment and Retraining Notification Act (WARN Act) requires employers with a total of 100 or more employees to provide 60 days advance notice of reductions in force during any 30 day period.

The WARN Act applies if 50 or more employees suffer an employment loss due to a shutdown of a single site of employment or an operating unit or department within a single site of employment. It also applies to other layoffs which result in an employment loss for 1/3 of the workforce at a single site and at least 50 employees, or 500 employees, regardless of whether this is 1/3 of the workforce.



The WARN Act has some exceptions, and determining its applicability is quite complex. The Act also requires that notice be provided to state and local officials and union representatives. If an employer has 100 or more employees nationwide and is planning either a single layoff or multiple layoffs over a three month period of time, it is highly advisable to seek legal counsel. Also, some states have their own version of the WARN Act with a lower threshold than 100 employees, so state law should be reviewed.

Offering Severance Pay

There are no federal laws that require private employers to pay severance to terminated employees. Also, very few states require private employers to provide severance pay to terminated employees. However, state laws should be checked. (For example, Maine requires large private employers to pay severance.)

Union contracts should be reviewed. Many have provisions requiring severance pay in the event of layoffs. Even if no provision for severance is included within an existing collective bargaining agreement, an employer may need to bargain with the union concerning severance pay.

Employment agreements may have provisions for payment of severance and should be carefully reviewed. Executive contracts often have change of control provisions requiring hefty severance pay in the event of executive terminations due to the sale of a business or division.

If an employer's own policies provide for the payment of severance, then these must be followed. Some of these plans may be covered by the Employee Retirement Income Security Act ("ERISA") which protects employees entitled to benefits under a wide range of employee welfare plans. Others may be protected under state laws or precedents which interpret employee handbooks and policies as creating contractual obligations.

Finally, while details are beyond the scope of this newsletter, the American Jobs Creation Act of 2004 added Section 409A to the Internal Revenue Code. This section is designed to regulate deferred compensation and, depending on the amount and payout structure, severance pay may fall under this section with resulting tax consequences. There are certain exceptions for terminations related to reductions in force, but if substantial severance payments over time will be made, it is highly advisable to have the plan reviewed by legal counsel.

Separation Agreements

One of the most effective ways of avoiding litigation and resolving many of the difficult issues surrounding a reduction in force is to offer terminated employees a written Separation Agreement that requires them to release all employment claims, including those related to termination, in exchange for receiving severance pay and other benefits.

Typically, such an agreement requires a release of all state and federal discrimination claims, all contract and tort claims, and virtually all other employment related claims. There are some limitations. For example, it is generally against public policy to waive any claims for unemployment benefits, although this is dependent on state law interpretation. Similarly, in general, claims of retaliation for seeking workers' compensation benefits may be released but not the workers' compensation claims

themselves. Wage and hour claims under the Fair Labor Standards Act may not be waived without approval of the Department of Labor or Court of competent jurisdiction.

Importantly, whenever a waiver is requested in connection with an exit incentive or other employment termination program offered to a group or class of employees, in order to release an age claim under the ADEA, which applies to those who are 40 or older, the Separation Agreement must attach information showing the title and age of employees in the same position or department who are being eliminated and those being retained. The employee must also be told to seek the advice of an attorney before signing the Agreement, must be given 45 days to consider whether to enter into the Separation Agreement, and must be given 7 days from the date of signing the Separation Agreement to revoke the waiver of an ADEA claim and reject the Agreement.

If severance payments are mandated by a company policy or employment agreements, then some extra amount of severance or other additional consideration, such as payment for health insurance or outplacement services, must be offered to the employee in exchange for the release of claims.

Payment of Final Wages, Bonuses and Commissions

Some states, including Missouri, require the payment of all wages due and owing on the final date of employment. Other states require payment on the next normal pay date or within two weeks of termination. Employers should also review bonus and commission policies to determine whether these amounts will be considered “earned” and therefore owed to terminated employees either in whole or in some proportionate amount. State laws sometimes govern these payouts.

Payment of Vacation Days and Other Accrued Time Off

The obligation to pay accrued but unused vacation to terminated workers will depend both upon the employer’s policy and upon state law.

Some states, Illinois for example, require payment for all unused accrued vacation days. Other states only require employers to follow written policies or past practices. These same considerations will apply to personal days or other paid time off. State laws should be carefully reviewed on these issues.

Continuation Of Health Insurance

Under the Consolidated Omnibus Budget Reconciliation Act (“COBRA”), employers with 20 or more employees that provide group health insurance must offer employees enrolled in such plans the opportunity to continue their coverage at their own expense, usually for up to 18 months. However, many states also have health insurance continuation requirements. For example, in Missouri, health insurance continuation for 9 months for terminated employees applies to employers having 1 or more employees.

CONSIDERING OTHER ALTERNATIVES

Many times substantial workforce reductions cannot be avoided due to the need to close down entire operations, dramatically reduce costs quickly or redirect the focus of a business. However, when considering implementing workforce reductions, it may also be worthwhile to view other options, such as reductions in hours, job reassignments, or pay or benefit cuts. These sometimes offer the possibility of trimming costs with a less devastating impact on the employees and fewer risks for the employer.

Offering voluntary exit plans based on a combination of age and years of service coupled with severance and a release of claims sometimes offers another less painful solution to the dilemma of necessary reductions in the workforce.

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