

Reductions in Force: Legal Do's and Don'ts

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Key Points

- Reductions in force can be accomplished through voluntary employment terminations (such as offering early retirement incentives), involuntary terminations or both. They should be designed and implemented in a nondiscriminatory and nonretaliatory manner.
- Employers should review severance pay policies as well as incentive and equity compensation plans and arrangements. If a severance plan is not already in place, consider implementing one.
- A WARN Act (or similar state law) analysis will determine whether advance notice of employment termination is required.
- Assess whether a RIF must be disclosed on an SEC Form 8-K, and assess the impact on key employees and stakeholders.

Reductions in force (RIFs) are making headlines as companies trim their worker ranks in the face of a weakening economy. Employers must decide whether to implement voluntary or involuntary RIFs (or both); the considerations for each vary greatly. We take a high-level look at the options, next steps and other considerations for companies anticipating downsizing.

Option 1: Voluntary RIFs

Voluntary RIFs include offering current employees severance pay or “buyout” programs, early retirement packages, job sharing agreements and/or reduced workweeks. If the employee does not voluntarily agree to accept the offer, he or she can continue working, unless the employer also conducts an involuntary RIF.

Why voluntary RIFs? These types of reductions may make it easier for employers to obtain releases of claims from employees in return for separation payments or benefits they would not be entitled to otherwise.

What releases of claims entail. To be valid, an employee release of claims must be (among other things):

- supported by legal consideration (*i.e.*, a payment or benefit to which an employee is not otherwise entitled);

- consented to “knowingly and voluntarily”; and
- written in a manner that can be understood by the individual waiving his or her rights or claims, or by the average individual eligible to participate in an “exit incentive” or employment termination program.

To effectively release age discrimination claims for employees age 40 and older, the waiver must also:

- specifically refer to rights or claims arising under the Age Discrimination in Employment Act of 1967 (ADEA) (discussed in detail below); and
- include any requirements under the Older Workers Benefit Protection Act, such as a 21-day or 45-day consideration period, coupled with a seven-day revocation period.

Option 2: Involuntary RIFs

An involuntary RIF is designed on the basis of a variety of criteria, such as seniority, job performance, position eliminations or closings of entire operations.

Seniority. RIFs based on seniority are likely straightforward. However, this approach does not consider individual employee qualifications and post-RIF staffing requirements.

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Position eliminations. An employer should be prepared to demonstrate:

- the legitimate business reasons for a position elimination;
- that any new positions differ substantially from former ones; and
- that employee qualifications for new or existing alternative positions were assessed objectively.

Closing entire plants or departments.

It is more difficult to challenge a RIF conducted in this manner because elimination of entire plants or departments is generally an objective process. An employer should:

- ensure that its business justification for the closing is well documented;
- if duplicative departments are to be combined:
 - consider whether employees have any transfer or “bumping” rights — which would allow otherwise laid-off workers to displace other employees — under established past practices, personnel policies or collective bargaining agreements, and
 - where such rights do exist, ensure that the transfers are offered to employees on a nondiscriminatory and nonretaliatory basis; and
- where a facility or department has a relatively greater number of protected classes of employees in the organization, consider whether the closure could lead to an adverse inference of unlawful discrimination.

As with a voluntary RIF, employers can opt to seek releases of claims from employees in connection with an involuntary RIF in return for separation payments or benefits that employees would not be entitled to otherwise.

Other Important Steps in a RIF

Review severance pay policies — written or established by past practice — to determine whether employees affected by the proposed RIF would be entitled to any severance pay. Companies should consider implementing a severance plan if they do not have one. A severance plan can be implemented for the RIF only.

Review incentive and equity compensation plans and arrangements to determine the impact of a proposed RIF on outstanding equity compensation awards and bonus entitlements.

Design and implement RIFs in a nondiscriminatory manner. Proscribed factors, such as age, race, color, sex, religion, national origin or disability, should not be factors.

A RIF may be perceived as a violation of the following or other anti-discrimination laws if certain protected categories are intentionally or disproportionately impacted:

- Title VII of the Civil Rights Act of 1964 prohibits discrimination on the basis of race, color, sex, religion or national origin.
- The Age Discrimination in Employment Act prohibits discrimination on the basis of age for individuals who are age 40 or older.
- The Americans With Disabilities Act of 1990 (ADA) extends anti-discrimination protections to disabled persons.

Design and implement RIF programs in a nonretaliatory manner, without regard to prior employee complaints.

Provide notice under the WARN Act, if applicable. The federal Worker Adjustment and Retraining Notification Act of 1988

requires certain employers to give employees, their representatives and local officials 60 days' notice of “plant closings” and “mass layoffs.” If notice is not provided, employers are subject to civil penalties and may owe employees up to 60 days' pay and benefits in lieu of notice.

The WARN Act defines:

- a “plant closing” as a permanent or temporary shutdown — of either an entire site of employment, or one or more facilities or operating units within a single facility — if the shutdown results in employment loss for 50 or more employees during any 30-day period; and
- a “mass layoff” as a RIF resulting in an employment loss at a single site of employment during any 30-day period of at least (i) 50 employees and 33% of the employees at the site, or (ii) 500 employees at the site.

State-specific WARN Acts may also be triggered by a RIF.

Additional Considerations

Maintain a solid record to demonstrate the rationale and objective criteria used in determining which employees to lay off. Performance-based termination decisions are more likely to withstand scrutiny under equal employment opportunity laws if they are supported by well-documented personnel records and based on sufficiently objective criteria.

One possible means of decreasing the likelihood of discriminatory decision-making is to **establish a committee of legal staff, human resources officials or other representatives** to assess managers' initial selection of employees for a RIF.

Consider whether any employees are on a **legally protected leave of absence**, including under the Family and Medical Leave Act, and any related job reinstatement and anti-interference rights.

Assess the **impact of a RIF on remaining employees** and any retention programs for key employees, and **on relationships with vendors, customers, clients and other stakeholders**. Prepare a communication plan and/or public relations strategy.

Have a plan regarding remaining employees, customers and stakeholders. Public company employers

should assess whether a Form 8-K disclosure with the Securities and Exchange Commission is required.

Provide impacted employees with documents including any notices, final pay, and separation and release agreements.

Consider meeting individually with each affected employee (although not legally required) to explain the reason for termination, present the separation documents noted above, and discuss the return of any company property and other administrative tasks ahead of departure.