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Global Workforce Solutions

Recession Risk and Workforce Reorganizations:

3. External Events: Managing the Unexpected

Overview

As discussed in the previous two installments in this series dealing with voluntary separation programs and global reductions in force, workforce reorganizations can take various forms and, even within a particular scenario, there can be many nuances.

One constant, however, is usually advance planning. The importance of this cannot be overstated, especially in a transactional context. But what happens when this is not possible?

In this final installment in the series, we use a fictional scenario to illustrate the types of issues that can arise in a transactional context where external factors–such as the onset of a global recession–cause the parties to re-think their integration plans.

Covington's Global Workforce Solutions team is well placed not only to assist companies in designing and implementing a reduction in force ("RIF") in such circumstances, but also to handle the complex employment, benefits, and tax issues that arise as a result of a change in direction part-way through a RIF.

Illustrative Scenario

Buyer and Seller signed a share purchase agreement in **January 2022** whereby the former would acquire the entire share capital of the latter.

Closing was set for the middle of **October 2022,** provided certain commercial and financial conditions were met by the end of **September 2022.**

As part of the integration of Seller's business into that of Buyer, the parties anticipated that **5-10%** of Seller's workforce would no longer be needed. An enhanced severance package was agreed for this group of employees as part of the RIF and their employment would terminate at closing. This was communicated to them following signing.

By the end of **July 2022,** the impact on both businesses as a result of the looming fears of a global recession was such that the parties were now looking at a **40%** reduction in headcount, across both groups and involving additional jurisdictions.

Continued

It is not unusual for integration plans to change between signing and closing, but it is rare for such plans to change to the extent in this scenario. We consider some of the common issues that can arise in such circumstances.

1. Employee Consultation, Consents, and Timing Issues

As explained in the previous installment in this series, in many countries proposing to lay off multiple employees can trigger collective obligations and there is often a threshold number for such triggers.

In some countries, the need to reduce headcount further could trigger the relevant thresholds. At the same time, the business may still need to retain some of the affected employees for a period post-closing but require flexible retention periods. The rigidity of individual and collective statutory employment rights and the statutory regulation of pension and other employee benefits in some countries—coupled with the lack of time to plan for this eventuality—can create a number of challenges.

The parties would likely need to consider ways to structure the new RIF so as to avoid triggering collective requirements in some jurisdictions. Such collective obligations would likely impact both the timing and the achievement of certain commercial synergies within pre-set timeframes. Also, if retention arrangements had already been put in place with certain key employees, and would now need to be revisited, this could be a delicate matter from both legal and employee relations' perspectives.

2. Employee Communications

Ordinarily, companies will have a comprehensive, coordinated communication strategy to ensure that all stakeholders receive the appropriate communications at the appropriate time. Employees, shareholders, public markets, and potentially governments or other stakeholders will likely all be entitled to information about a RIF at some point in time.

But where employee "buy in" is key to the success of a RIF, a change in the messaging (e.g., from *"most will continue as usual"* to "*the transaction will result in a number of job losses"*) creates additional challenges and can even cause employees to question the reasons behind the RIF. Also, where collective consultation requirements have been triggered, in some countries the ability to consult with employees individually is lost, restricting the ways in which an employer can communicate with its employees, and adding yet another layer of complexity.

In the scenario above, more information about both the original post-closing integration plan and the revised plan would likely need to be divulged to employees than originally anticipated. Covington's Global Workforce Solutions team has frequently assisted clients with navigating this process, in particular the potential pitfalls of group-wide communications to employees in different jurisdictions.

3. Challenges with "Enhanced" Severance

The enhanced severance package originally agreed for the Seller's employees who were impacted by the transaction could of course be extended to the expanded group of affected employees, subject to funds being available to cover the increased cost. In most cases, whilst the increase in the number of employees subject to the RIF will create an additional cost in the short-term, this will be offset by the savings to the business (in employment costs) that the RIF creates over time.

3. Challenges with "Enhanced" Severance (Continued)

A bigger challenge arises where the value of that separation package does not amount to much of an enhancement on entitlements under local law. In most countries outside the U.S., employees are entitled to notice and sometimes statutory severance payments on termination of employment, and in some countries the latter is calculated on both fixed and variable compensation (including the value of equity-based awards).

There are likely to be various cases where the "enhanced" severance package either (i) amounts to less than an employee's contractual and/or statutory entitlements under local law, or (ii) only exceeds the value of these by a fraction and is not enough to persuade employees to sign up to separation agreements containing a waiver and release, given that protection from involuntary dismissal exists under local law.

Consider the scenario where employees have also already been told that their vested and unvested equity would be cashed out at a particular price, or that they will receive a cash retention bonus connected with the integration, in return for remaining in employment until closing. In many jurisdictions employees will be able to argue that these sums are already contractual, thereby preventing these "benefits" from being used to further enhance severance packages with minimal cost to the employer.

How Covington Can Help

Our Global Workforce Solutions team has worked with a number of clients in the period between signing and closing where external events have forced them to re-consider integration plans.

Often, the in-house team handling such exercises is made up of people from various areas of the business, and includes in-house legal counsel, HR, payroll, local country managers, and local regulatory advisers. We have generally assisted with:

- Drafting both global and local employee communications, working with all internal stakeholders.
- Preparing for collective consultation processes and advising on the relevant reporting and/or disclosure requirements.
- Restructuring previously agreed separation plans and, in some cases, creating separate local separation plans.
- Preparing forms of separation agreements for use in multiple jurisdictions and ensuring conformity on matters which, for regulatory reasons, had to be consistent across all jurisdictions.
- Revisiting equity award agreements in the context of putting in place retention arrangements, and working with the original corporate deal team to implement these.
- Advising on individual cases and potential termination-related claims.
- Preparing individual meeting scripts and other termination-related documents, in collaboration with the HR and legal teams.
- Guiding HR with the execution of separation agreements and the making of payments under those agreements in order to comply with local laws (including tax laws).

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The areas highlighted above are provided by way of example. This is not an exclusive list of the issues that can arise in the illustrative scenario above. Even within each of these areas, other issues can (and do) arise due to the nature of the parties' business operations and the specific synergies that commercial teams need to achieve within pre-set timeframes.

If your company currently finds itself in a similar situation, please do contact our Global Workforce Solutions team to see how we might be able to support you.

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