

The Legal Implications of a Reduction in Force



By Kelly A. Schoening and Mark D. Guilfoyle

The economic recession has caused many private and public employers to take a drastic step and lay off employees. An involuntary reduction in force (“RIF”) may be the last resort for reducing workforce and shedding costs. However, RIFs also can lead to significant liability and cost companies more than what was saved by cutting payroll. It is far more complicated to reduce a workforce than most employers realize.

In 2009, the Equal Employment Opportunity Commission had the second highest year for charges, following 2008, which was the highest year. The two-year average for charges was 94,340.¹ It is likely no coincidence that charges have increased in years that unemployment has doubled.

The exposure to liability associated with an RIF is a claim of discrimination. A typical scenario is for a terminated employee to allege that his employer selected him for the RIF not because of the reasons enunciated by the employer, but because of his age, gender, race, disability, or some type of retaliation. For example, an employee terminated during an RIF can maintain a prima facie claim of age discrimination merely by showing that: (1) he is 40-years-old or older; (2) he suffered an adverse employment action; (3) he was qualified for the position; and (4) he was replaced by someone outside the protected class.²

In order to prove a case of discrimi-

nation in an RIF context, plaintiffs carry an additional burden. Courts require plaintiffs to provide additional direct, circumstantial, or statistical evidence to prove that the employee was singled out for discharge for impermissible reasons.³ The fourth element of the *McDonnell Douglas* prima facie case analysis is modified to require this additional evidence.⁴

Claims cannot always be prevented, but steps definitely may be taken to minimize liability and to make a case more defensible. Employers are best able to defend against such a claim when they are able to show that the RIF was carried out pursuant to valid selection criteria and was designed to retain the most qualified employees. In order to successfully utilize this defense—and, more importantly, to avoid a lawsuit in the first place—involuntary RIFs must be carefully planned. The following is a suggested preliminary checklist for any employer considering an RIF:

- 1) Written list of business reasons. The first step is for top management to identify in writing the business and/or financial reasons for the RIF, including economic savings and increases in efficiency. In other words, why is it necessary?
- 2) Goals of the RIF. Identify the goals of the RIF, such as labor costs to be eliminated or positions to be eliminated.
- 3) Consider alternatives. Will less drastic alternatives achieve the

goals? Employers should consider alternatives such as shortened workdays, voluntary pay reductions, reductions of overtime, reduction or elimination of outsourced labor, voluntary leaves of absence, and salary or hiring freezes.

- 4) Written selection criteria. If no viable alternatives exist, the next step is to generate a written internal statement of well-defined selection criteria for termination. How will the employer choose which employees may be terminated? A mistake here could lead to significant liability down the road.
- 5) Identify selection procedure. Identify the decision-making sequence and persons responsible for those decisions. Involve the HR department.
- 6) Assure RIF policies are followed. Some employers have written RIF policies. If so, the employer must follow the policy. Make certain that all written RIF policies are known and followed by the decision-makers administering the RIF.
- 7) Employment contracts. Some employees have employment contracts which may remove an employee from the sphere of “at-will” employment. Contracts should be terminated in accordance with their terms.
- 8) Severance packages. Finally, consider severance payments coupled with written releases. Releases can protect employers from future claims, but they must be carefully drafted in order to be effective.

To the extent possible, employers should use objective criteria such as seniority to determine who will be laid off. It obviously is much harder to dispute such objective criteria. However, employers are often reluctant to use seniority because it may not result in retaining the best employees.

If job performance is a criterion, job evaluations and discipline become very important. The evaluations or other documents in the file should support the

decision for choosing a particular employee.

Regarding severance agreements in an RIF, valid consideration must be provided to the employees in order to obtain a valid waiver. Severance agreements must be written correctly to be enforceable. For example, claims under Title VII can be waived if the consent is knowing and voluntary.

If an employee is over age forty and the employer is requesting a release under the Age Discrimination in



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Employment Act ("ADEA"), the Older Worker's Benefit Protection Act requires that several items be included in the agreement in order for the release to be valid.⁵ For instance, the employee must be provided with twenty-one days to review the agreement and seven days to revoke. The release must be knowing and voluntary; it must be written in an easily understood manner; the ADEA must be specifically referenced; rights which arise after the date of release cannot be waived;⁶ and the employee must be advised to consult with an attorney.⁷ If there is a group termination (where more than one employee is terminated), the employees must be provided with forty-five days to review the agreement and be provided with a list of employees by age and job title who are in the same category and who were included in the agreement and those who were not.

Although there was previously a question as to whether an employee could release a claim under the FMLA, the recent amendments clarified that employees may release such claims without first obtaining approval from the Secretary of Labor.⁸ Employees cannot waive their right to file a charge of discrimination with the Equal Employment Opportunity Commission ("EEOC") because such claims belong to the government and not to the

employees.⁹ However, employees can waive their rights to receive any compensation or benefit from such a charge.

When drafting severance agreements, employers should consider whether to allow the employee the opportunity to resign in lieu of termination of employment. They should also consider whether to pay severance in a lump sum or over a period of time. There is a benefit to the employer to pay over time so that the employee cannot apply for unemployment insurance benefits until the severance payments run out. Other issues to consider are whether unused vacation will be paid out, the type of reference that will be provided to the employee, and whether the employee will be eligible for re-employment. It is advisable to include a non-disparagement clause so that the employee does not speak ill of the employer. Employers should also require a return of all property including files, equipment, and documents. There should be a confidentiality agreement so that the employee does not tell others about the severance package. Lastly, the attorney drafting the severance agreement should ascertain whether any employment agreement including a non-compete clause exists. If there is such an agreement, it must be terminated according



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to its terms; and any non-compete provisions should be addressed so that they are not waived.


Some severance plans may be subject to Section 409A of the Internal Revenue Code by virtue of the severance agreement and can subject the employee to hefty taxes. If the termination is involuntary or there is a good reason in a voluntary termination, there is an exemption from 409A. There is also an exception for short-term and small dollar amounts.

Some employers have tried to cut expenses without permanently cutting staff through the use of furloughs. If a furloughed employee is hourly, there is no concern with the use of furloughs, but a problem arises if the employee is salaried. The Department of Labor ("DOL") addressed the use of furloughs for salaried employees and potential violations through two Opinion Letters in 2009.¹⁰ The Fair Labor Standards Act requires that employees who are exempt from overtime be paid on a salaried basis despite the quantity or quality of work. If an employee is ready, willing, and able to work, deductions may not be made from the weekly salary if the deduction is occasioned by the

employer.¹¹ The DOL does allow employers to deduct from accrued leave accounts in the case of a furlough, but under no circumstances can the weekly salary be reduced.¹²

Employers also must abide by the WARN Act when considering a reduction in force.¹³ If the employer has more than 100 employees, the WARN Act applies.¹⁴ The Act comes into play in the event of a plant shutdown or a mass layoff. A plant shutdown is the closure of an entire plant. A mass layoff occurs when the employer reduces staff by greater than 500 employees or lays off greater than fifty employees and if the number laid off constitutes greater than 33% of the workforce.¹⁵ There are several requirements under the Act, including providing sixty days' notice to the workers and notice to the State's unit for displaced workers. Failure to abide by the WARN Act causes significant penalties.¹⁶

A reduction in force can be very useful to cut expenses and stay competitive. An RIF may be the only difference between a company staying in business or not. However, if an RIF is not done properly and after careful planning, it can backfire and cost a company more

by having to defend discrimination claims or being assessed penalties. 

ENDNOTES

1. www.eeoc.gov
2. *Geiger v. Tower Automotive*, 579 F.3d 614 (6th Cir. 2009).
3. *Schoonmaker v. Spartan Graphics Leasing, LLC*, 595 F.3d 261 (6th Cir. 2010); *Barnes v. GenCorp., Inc.*, 896 F.2d 1457 (6th Cir. 1990).
4. *McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973).
5. 29 U.S.C. § 626(f); 29 C.F.R. § 1625.
6. *Alexander v. Gardner-Denver Co.*, 415 U.S. 36 (1974); *Adams v. Philip Morris, Inc.*, 67 F.3d 580 (6th Cir. 1995).
7. *Id.*
8. 29 C.F.R. § 825.220(d).
9. 29 U.S.C. § 626(f)(4); 29 C.F.R. § 1625.22(i)(2).
10. Department of Labor, Fair Labor Standards Act Opinion Letter 2009-14, 2009-2 (2009).
11. 29 C.F.R. § 541.602(a).
12. *Id.*, §§ 541.600, 541.602.
13. 29 U.S.C. § 2101.
14. *Id.*
15. *Id.*
16. *Id.*

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