COVID-19 and Private Equity: U.S. Employment and Compensation Considerations

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The abrupt economic slowdown and wide-spread stop-work orders arising from the COVID-19 pandemic have put a sharp focus on nearly all areas of human capital and workforce management. On April 16, 2020, Debevoise's Private Equity Group held a COVID-19 briefing focusing on these issues, including workforce re-engagement strategies, areas of potential employment litigation arising out of furloughs and reductions in force, the new landscape in employee health and safety, and compensation plan considerations.

To access the on-demand recording of the presentation, please click here. Highlights include the following:

Weighing workforce reduction options

Tricia Bozyk Sherno

For portfolio companies considering workforce reductions, there is no one-size-fits all approach: The nature of the business, the post-pandemic business outlook, work flow and availability of CARES Act benefits are all factors when choosing to implement wage and hour reductions, furloughs and layoffs—or a combination of the three. At the same time, some general observations can be made:

Wage and hour reductions are often an attractive option for businesses whose employees (whether management or rank-and-file) have highly specialized functions and training that makes workforce consolidation or reduction impractical. This approach has the benefit of near-immediate cost savings while still retaining employees, and, depending on state unemployment eligibility requirements, allowing employees to

receive partial unemployment benefits. However, employers must navigate state employment regulations, which may include, for example, advance written notice requirements and salary floors for employees who are exempt from overtime under the Fair Labor Standards Act. Wage and hour reductions can also affect benefit eligibility.

Furloughs — effectively "temporary unpaid leaves of absence"—have been common for businesses suffering a lack of work that is significant but expected to be short-lived. Employees can be recalled quickly and with minimal administrative overhead, and furloughed employees retain health benefits and, depending on the applicable state's law, can collect unemployment, including the additional $600 weekly payment under the CARES Act. However, employers risk losing key employees who decide not to return when recalled. Looking ahead, remember that furloughed employees will expect advance notice regarding return-to-work dates. Continue to keep them informed of their status and reopening plans to manage expectation (but be careful to ensure that they do no work in the meantime, as discussed in more detail below).

Layoffs offer the clarity of a clean break, but carry legal risk, which, if not properly handled, can eat into whatever cost savings the layoffs bring. Litigation risk can be mitigated through severance payments in exchange for a general release from claims. Even when not required by an employment contract or collective bargaining agreement, the legal protection may be well worth the cost.

Preparing for a likely rise in employment litigation

Jyotin Hamid

As was the case after the global financial crisis, large-scale workforce reductions conducted quickly in a time of confusion are very likely to spawn a sizable uptick in employment litigation once the dust settles. Employers should prepare for attacks on four fronts:

Individual wrongful termination. Many employers are under the mistaken impression that they are inoculated against such claims if they use legitimate, non-discriminatory criteria to make their workforce reductions. However, an individual plaintiff does not have to show adverse impact against a protected class—only that their own age, gender, race, or, in certain circumstances, purported whistleblowing activity contributed to their selection for furlough or layoff. Even if criteria used were facially neutral, if they included any degree of manager discretion or subjectivity, plaintiffs may have a foothold that, even in a weak case, may have some settlement value. It is critically important for employers to note that while there is solid case law supporting terminations made on clearly business-oriented, non-discriminatory criteria, those precedents are unlikely to

cause a plaintiff's action to be dismissed at the outset of a case. Any given individual wrongful termination suits thus may pose a small risk, but they are costly to defend against and the *collective* risk can be meaningful, given that a single plaintiff's successful challenge to the criteria used for a layoff or other reduction may invite similar suits from other employees were subject to the same action.

Class-wide challenges. That the criteria used for workforce reduction are neutral and non-discriminatory on their face offers little defense if the reduction results in a statistically significant adverse impact on a protected class and such impact cannot adequately be explained by business necessity. That impact may well be inadvertent. For example, a decision to furlough the most recently hired workers may be more likely to affect members of racial minority groups if the company has grown more diverse over time. The question in litigation will be whether the criteria used was driven by "business necessity"—a higher standard than mere neutrality. While there will be fewer class-wide than individual suits, the exposure from any single class-wide action will be significant. In any event, companies should be sure to have their legal and HR departments work together to track patterns that might emerge, either within business units or across the enterprise.

WARN Act suits. Many employers assume, with sound reasoning, that the COVID-19 pandemic squarely qualifies for an exemption to federal and state requirements specifying advance notice before facility closures for circumstances that could not have been foreseen in advance. However, even under "dramatic, unforeseen circumstances," employers must give as much notice as possible—opening the door for claims that a one-week notice could have been, say, two weeks. (Plaintiffs' argument will be strengthened if they can point to examples of longer lead times at similar enterprises.) Also, the longer the pandemic continues, the harder it will be for employers to argue that the need for workforce reductions are "unforeseen."

Working-while-furloughed and overtime claims. If exempt workers do *any* work during a given week, they have a claim for a full week's pay at regular salary. Similarly, if non-exempt workers perform work while furloughed, they must be compensated for the time they spend working, including any overtime hours. While most employers will have policies to prevent furloughed employees from working, the speed with which furloughs have been implemented, against a backdrop of confusion and uncertainty, makes for a high risk of non-compliance. Similarly, it is likely that in many businesses, insufficient controls are in place for workers whose hours have been reduced, setting the stage for wage and hour claims.

Employee health and safety: Return to work is not a return to normal

Brooke J. Willig

While the last weeks have been dominated by responding to the economic slowdown and stop-work orders arising from the pandemic, many employers are now looking ahead to the eventual resumption of operations. When that happens, employee health and safety will be at the top of the agenda. The health and safety principles that have emerged during the pandemic are likely to provide a useful framework for best practices during the return to work:

Distancing. Employers may want to have employees who can work from home continue to do so. For those returning to facilities, staggered shifts and/or a gradual return to capacity should be considered. Employers should give thought to minimizing contact through physical barriers and a reformatting of the workplace, and establishing policies covering shared spaces.

Equipment and cleaning. Personal protective equipment is likely to be prevalent and may in some circumstances be required. Be careful, however, that all employees performing similar tasks are given equal access to that equipment. Similarly, be aware of applicable OSHA rules, such as those that govern the use of respiratory protection, even on a voluntary basis. Minimize the use of shared equipment and ensure regular and adequate cleaning and disinfecting protocols—especially after a worker has had, or is suspected to have had, the virus.

Employee monitoring and management. While the specifics of testing and monitoring are likely to be heavily shaped by government directive, employers should plan now because ongoing monitoring is likely to be key to containing the virus. Employers should establish and enforce policies governing when employees should stay home, whom employees need to notify when sick, whom employers need to inform of illness or exposure to minimize transmission while preserving confidentiality, and how best to protect co-workers, customers and others. Note that the obligation to maintain the confidentiality and privacy of employee health records is an ongoing obligation, which extends down even to individual temperature checks.

Government guidance. As we have seen during the pandemic, guidance can fluctuate significantly in the face of unfolding events. Companies must remain agile in their ability to respond as guidance evolves. Further, employers should expect new regulations, and directives may be followed by increased enforcement. Employers should make sure to monitor and adjust policies, prioritize compliance and ensure good recordkeeping.

Communicate with employees. Keeping employees informed in the face of evolving practices will require a concerned effort. Remember that communication is a two-way street; employee concerns may well highlight otherwise-unnoticed health risks. And while companies will not be under obligation to accommodate every COVID-related concern, some accommodations may be required under the ADA.

In addition to heightened health and safety practices, employers should brace themselves for an **increase in health and safety related lawsuits**, including retaliation claims if workers are disciplined for refusing to work or reporting an unsafe work environment under certain circumstances, and claims from employees arguing that they contacted COVID-19 at work. Even though it may be an uphill battle for employees to show that contracting COVID-19 was a risk particular to their employment rather than a one borne by the public generally, the possibility of such suits is all the more reason to scrupulously follow government guidance—and document accordingly.

Retaining and motivating key employees in the post-pandemic age

Jonathan F. Lewis

Having the right management team in place will be essential to moving forward in the eventual economic recovery. At the same time, large-scale disruptions such as the COVID-19 pandemic can alter the effectiveness of incentive plans. Boards, CFOs and compensation committees should review the following:

Short-term incentives (e.g., cash bonuses): Benchmarks established in January may be less relevant today; for example, cost-cutting, rather than hitting revenue targets, may be the goal to reward now. However, any changes to incentives should made only when there is sufficient clarity to do so, as successive changes to compensation plans can be demotivating. Indeed, under some circumstances, the best course of action may be to do nothing at the moment and communicate that compensation decisions are being postponed until there is less uncertainty. If any changes to short-term compensation are made, public companies should calibrate their timing in light of disclosure requirements. (Some public companies may want to keep in mind that proxy advisors are stating they disfavor such midstream corrections.)

Long-term incentives (e.g., equity): Decisions on this front are likely to be made by the portfolio companies on a case-by-case basis. The relevant considerations here include, as examples, how long the portfolio company has been held, the post-pandemic business outlook, whether that outlook is likely permanent or temporary, and the extent to which the incentives have moved out of the money. There may be other considerations as well, such as a concurrent addition of new equity investors or strategic

partners, or possible non-cash accounting charges that a change to LTI would bring. As with short-term incentives, it is important to communicate to management that any changes are being made to enhance, as much as possible, alignment, motivation and wealth creation. Here, too, waiting for clarity may be the best next step—sponsors may want to wait a year or more before making any LTI alterations.

Boards and management teams should also assess the **flight risk of key talent**. Evaluate the non-compete and non-solicitation agreements, as well as other restrictive covenants at place in the portfolio company, including who has them, their length of term, what they cover, and the likelihood of their enforceability. In all of these actions, good, normal, boring corporate governance will assist in minimizing litigation risk.

Planning for a changed landscape

Tricia Bozyk Sherno

While it's not possible to know the extent to which work life will change after the pandemic, portfolio companies planning for the future should consider the following:

Remote work is here to stay. Companies that have resisted remote working arrangements—including when requested by an employee with a disability—will have a difficult time maintaining an argument that remote work poses an undue hardship on the business if the pandemic has put their remote work capabilities on display. It would not be surprising for remote working to become more standard at many businesses.

ADA prohibitions on medical inquiries will likely continue to be a secondary priority to pandemic response. The imperative to test and monitor employees will take precedence, at least for the foreseeable future.

Health, safety and worker protections will come to the fore—for employees and regulators. Companies will need to strike a respectful, balanced and realistic tone on what will now be a key element in how employees regard their employer. These concerns are also likely to be reflected in federal and state legislation regarding sick leave and protections for independent contractors.

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For more information regarding the coronavirus, please visit our Coronavirus Resource Center.

Please do not hesitate to contact us with any questions.

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