

The Cost of Downsizing

Revenues for many cities and towns are, or soon will be, declining from a combination of factors: property tax caps, late or unpaid property taxes, reduction in tax base, reduction in income taxes, and reduced utility revenues. All of these can be traced to legislative changes or impacts from the current state of the economy. Additionally, the expansion of the homestead deduction starting in 2009 will further reduce the tax base and revenues in rate-controlled funds.

The demand for services, however, rarely decreases.

It is difficult right now for communities to know with a great degree of certainty what their near term financial position will be and what that landscape will be. Now more than ever, strategic planning is critical to address these questions. Major operational changes are hard to implement and difficult to reverse; so the ability to target what level of operational savings is needed cannot be understated, nor the upfront planning needed to implement such changes.

Downsizing the labor force is one of the first strategic steps that may be considered to reduce operational expenses, since labor and costs related to the workforce make up the majority of most budgets. Before making any decisions, remember that downsizing has related costs as well.

Those costs can include:

- Unemployment benefits
- Accrued time, including comp time
- Severance pay
- Outplacement assistance
- Covering the responsibilities of the replaced position (including training costs and overtime)
- Fees for a labor attorney or expanded services from local counsel
- Health insurance – employers are responsible for a 65% health insurance subsidy for involuntary terminations from September 2008 through December 2009 due to new COBRA regulations, although the subsidy is later reimbursed through a payroll tax credit (watch the potential cash flow impact).

It is important to study these costs before making downsizing decisions to avoid negative, unintended consequences to both the short-term and long-term cash flow.

After evaluating carefully the financial landscape (immediate, next 24 months, and long-term) a rational determination can be made if a reduction in force (RIF) is needed. The work does not stop there, as many questions need to be addressed in the planning and implementation of the downsizing. Below are areas to consider:

- Look ahead and consider what skills will be needed, how top talent can be retained, and do services need to be reduced.
- Establish criteria for downsizing decisions. Will it be by performance? By seniority? The criteria cannot be vague, and they must be defensible.
- Once a list of individuals identified for a possible RIF is developed, review the list to ensure the result is not discriminatory by age, race, gender, religion, or disability. Consultation with legal counsel is imperative.

- Under the Older Workers Benefit Protection Act of 1990, workers who waive their Age Discrimination Employment Act (ADEA) rights must do so knowingly and voluntarily, and they must have 45 days to consider the agreement.
- Have an action and communication plan for handling the RIF that covers when and how employees will be notified, how their work will be concluded, and security measures regarding access to facilities, equipment, and computer systems.
- A corresponding plan is needed for employees who remain. Expect low morale and perhaps reduced productivity as people adjust to the new situation. Have a retention strategy that minimizes the possibility that remaining employees leave because they fear for their own future or feel overwhelmed with picking up additional responsibilities.

As cost-reduction options are evaluated, there are other alternatives to a RIF such as: reducing pay with a corresponding reduction in hours, furloughs, alternative work schedules, instituting a hiring freeze, freezing pay rates, reducing benefits, offering incentives for early retirement, or not filling positions created by normal retirements. Involve managers and employees in cost-reduction discussions as careful evaluation of the work flow process may lead to pleasant surprises of where efficiencies can be achieved and a RIF may be minimized.

The overall goal is to deliver services to constituents as efficiently as possible. The impact of downsizing the workforce is more involved than just looking at total salaries or wages that may be eliminated. By evaluating the financial and operational impact of all alternatives, you are poised to make the right strategic decisions.

By: Todd Samuelson, Umbaugh
With Kind permission from Indiana Association of Cities and Towns

[Back To Story Page](#)