

An overhead photograph of three business professionals in a meeting. A woman with dark hair and glasses, wearing a beige blazer, holds a black clipboard. A man with short brown hair, wearing a dark blue suit, holds a black smartphone. A woman with long red hair, wearing a black top, is seen from behind. They are standing on a light-colored stone floor.

Surviving the corporate crisis through staff reductions

Five steps to successful restructuring

TaylorWessing

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There are a number of ways under German employment law to cope with short-term economic downturns. These include short-time working, salary waivers, discontinuation of voluntary benefits, termination of company agreements or the reduction of overtime accounts. In view of the continuing shortage of skilled workers in Germany, companies are often interested in taking short-term measures to reduce personnel costs and not to dismiss qualified permanent staff in a hurry. But what if short-term measures are not available – short-time allowances, for example, are not granted in the case of limited production „only“ due to increased energy costs? Or what if profound and long-lasting economic crises cannot be (fully) cushioned by these short-term funds? In these constellations, companies will inevitably have to deal with the question of staff reductions. Get an initial overview of existing options for action now.

1. Restructuring, but how?

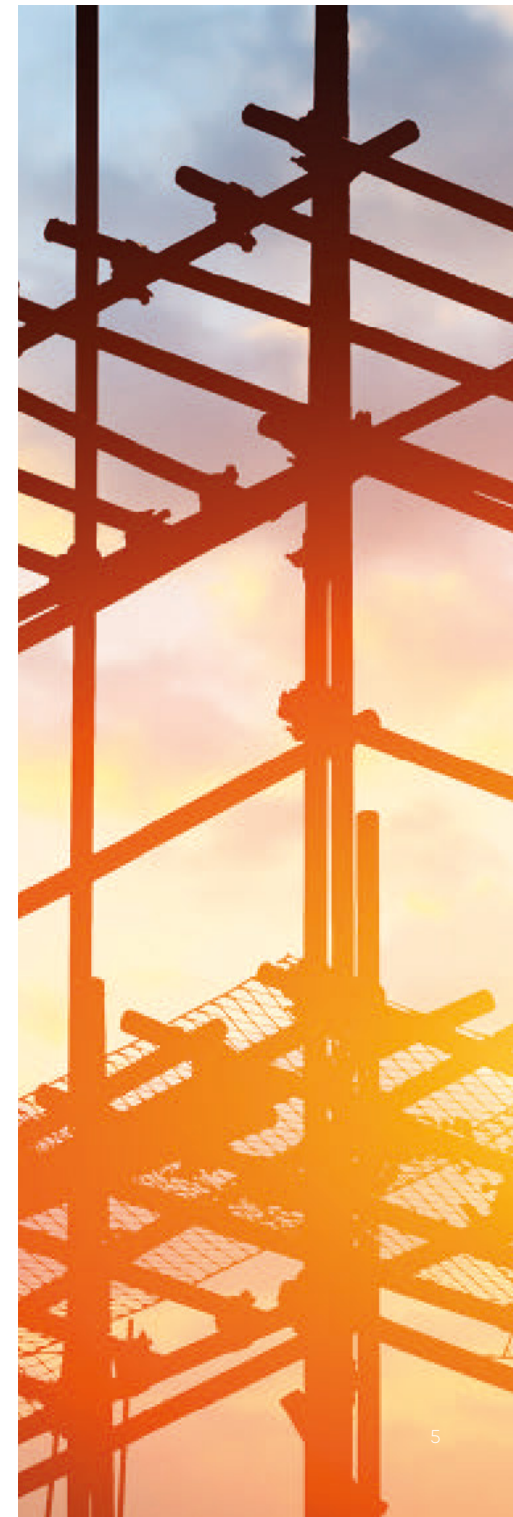
Reduction of staff as a flexible restructuring instrument

The range of possible structural changes and the employment law aspects to be taken into account are wide. In addition to restructuring measures at **company level** in accordance with the German Transformation of Companies Act (such as mergers or spin-offs) and at **operational level** in accordance with Sections 111 et seq. of the Works Constitution Act (e.g. partial or complete closure of an operation, relocation of an operation, increase in the size of an operation), there is also the possibility of a pure **reduction of personnel** without any changes at the corporate or organisational level. Whilst the individual measures regularly overlap and comprehensive restructuring is often associated with corresponding staff reductions, pure staff reductions are often considered as a means of achieving the necessary cost-cutting effects in the medium term,

without major expenditure of time, money and organisation.

Whilst operational changes (such as the closure of (part of) an operation or the relocation of an operation abroad) can only be reversed at great economic cost, the pure reduction of personnel is reversible once the economic crisis has been overcome by hiring new staff and in-sourcing tasks temporarily outsourced to external companies. The extent to which rights of co-determination of the works council exist in the case of pure personnel reductions pursuant to Sections 111 et seq. of the Works Constitution Act or whether a notification of mass redundancies pursuant to Section 17 of the Dismissal Protection Act becomes necessary, depends in particular on the number of employees affected by the personnel reductions within the company (see 3.). Exceeding

the relevant thresholds may also make the pure reduction of personnel time-consuming and costly. In addition, in the event of drastic personnel changes, the effects on personnel and business policy such as the potential departure of managers, a possible deterioration in cooperation with existing works councils, possible strikes and defensive measures by the trade unions and possible damage to reputation through media attention must also be taken into account. When making a strategic corporate decision on the choice of the right restructuring measure, the respective consequences under tax law must likewise be taken into account.



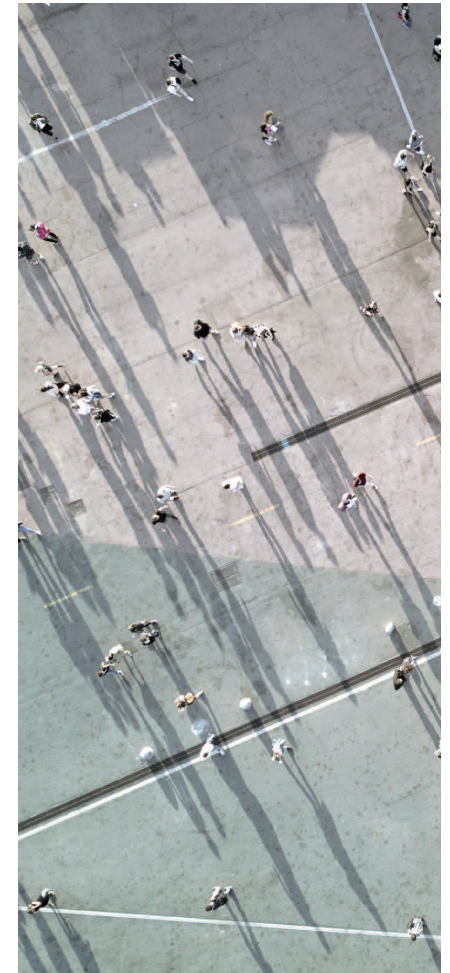
2. Staff reduction, but how?

Voluntary programmes as an alternative to dismissal

In view of the high level of employee protection existing in Germany, the question usually arises from the company's point of view as to whether a necessary reduction in personnel should be carried out by giving notice or on a voluntary basis by concluding termination agreements on financial terms fixed in advance. The advantages of so-called **voluntary programmes** are obvious: the financial outlay is easier to calculate in advance and procedural risks in connection with enforced redundancies are minimised. Staff cuts can often be carried out more quickly and without the need for social selection (the legally compliant implementation of which often leads to an unwanted ageing of the workforce, particularly in times of crisis), compliance with existing special protection against dismissal or overcoming any collective-law provisions on immunity from

dismissal (e.g. within the framework of existing agreements on safeguarding sites or collective agreement provisions on protection against dismissal). Finally, voluntary staff reductions are easier to justify to both employees and the public and avoid the development of a negative operating climate and possible damage to the company's reputation. In order to avoid the risk that, even within the framework of a voluntary programme, only those top performers with positive job prospects on the labour market who are urgently needed during the crisis are prepared to leave the company voluntarily, the company's offers of termination should either be targeted at specific employees / groups of employees (so-called **selective offer procedure**) or the conclusion of the termination agreements offered by the employee are in each case subject to

the approval of the company (so-called **double voluntary nature of the open bid procedure**). If, due to the number of employees affected by the planned staff reduction, the works council has participation rights under Sections 111 et seq. of the Works Constitution Act, the works council may, however, insist on the negotiation of a reconciliation of interests and the conclusion of a social compensation plan. The works council could possibly obtain an injunction to prevent the implementation of the voluntary scheme and force the company to conclude a social plan. This will of course be detrimental to the time saved by implementing a voluntary scheme. When deciding for or against a voluntary programme it should also be borne in mind that the funding of the voluntary programme often sets a precedent for any social plan that may be required later on.





3. Redundancies, but how many?

Avoidance of participation and notification obligations in staff reductions

If there is a works council, the question arises from the point of view of the company whether a pure reduction in personnel without other changes at the operational level would result in co-determination rights of the works council according to Sections 111 et seq. Works Constitution Act or triggers Section 17 (2) of the Dismissal Protection Act.

Pursuant to Section 111 (1) of the Works Constitution Act, in companies with generally more than twenty employees entitled to vote, the employer must inform the works council in good time and comprehensively about planned changes in operations which may result in significant disadvantages for the workforce and must discuss the planned changes in operations with the works council. Before implementing the planned change in operations, the employer must attempt to reach a so-called **reconciliation of interests** with the works

council in accordance with Section 112 of the Works Constitution Act.

In this respect, the works council has a say in the “whether” and “how” of the planned measure. Before the company can carry out the planned measure, it must exhaust all possibilities to reach an agreement with the works council; as a rule, it can only be assumed that negotiations will fail after the conciliation body has been called upon without success. If the company begins to implement the change without having attempted to reconcile its interests, the works council may, under certain circumstances, prevent the implementation of the operational change by means of an interim injunction. In this case, employees are also entitled to severance pay pursuant to Section 113 (3) (1) of the Works Constitution Act vis-à-vis the company (which can, however, be offset against any social plan claims due

to the existing identity of purpose by way of fulfilment effect).

In addition to the necessary negotiations to reconcile interests, the company must also reach an agreement with the works council in the event of a planned change in operations on the compensation or mitigation of the economic disadvantages incurred by the employees as a result of the change in operations (so-called **social plan**). In this respect, the works council has a mandatory right of co-determination. This means that if no agreement is reached, the works council can appeal to the conciliation body and force the social plan to be drawn up. Interest reconciliations and social plan negotiations can delay the implementation of the planned staff reduction measures by several months and increase the pressure on the company to grant generous benefits under the social plan.

However, not every pure reduction in personnel represents a change in operations in the aforementioned sense requiring participation.

This is dependent upon the number of employees affected by the planned staff reduction in the respective company.

If a company is not already forced to make staff cuts on a certain scale because of its existing financial situation, the question of how many employees can be made redundant without the involvement of the works council is therefore of considerable practical importance in terms of both time and money.

According to the established case law of the Federal Employment Court, a **reduction of operations subject to co-determination** within the meaning of Section 111 of the Works Constitution Act exists in the event of a pure reduction in personnel if the information required for the notification of collective redundancies in accordance with Section 17 (1) of the Dismissal Protection Act reaches the relevant threshold values. Since the threshold values are only standard values, in individual cases a change in operations can also be present if the respective threshold value is slightly undercut.

According to the threshold values of Section 17 (1) of the German Dismissals Protection Act, on the basis of corporate planning, generally with

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|--------------------------------------------|-----------------------------------------------------------------------------------------------------|
| 21 to 59 employees in operation | more than 5 employees, |
| 60 to 499 employees in operation | 10 per cent of the employees regularly employed in the company, or more than 25 % of the employees, |
| at least 500 employees in operation | at least 30 employees |

must be affected by redundancies.

Dismissal in this sense includes both dismissals for operational reasons (modification) and termination agreements.

In small business operations with up to 20 employees, the numerical limits of Section 17 (1) of the Dismissal Protection Act cannot simply be applied, since the provision pre-supposes that more than 20 employees are employed. In the opinion of the Federal Employment Court, a change in operations due to a pure reduction in personnel in small business operations as a rule only exists if, in accordance with Section 112a (1) No. 1 of the Works Constitution Act, at least six employees are affected.

For **large business operations** with more than 600 employees, the Fed-

eral Employment Court assumes a minimum figure of five percent.

Section 112a (1) of the Works Constitution Act restricts the **obligation to draw up a social plan in cases of pure staff reductions** - i.e. if the planned change in operations consists solely of the dismissal of employees for operational reasons without other changes in operations within the meaning of Section 111 of the Works Constitution Act - if certain thresholds deviating from Section 17 of the Dismissal Protection Act are not exceeded.

The conclusion of a social plan by appealing to the conciliation body can only be enforced by the works council in cases of pure staff reductions if in companies with regularly

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|---------------------------------|-----------------------------------------------------|
| up to 59 employees in operation | 20 per cent of employees, but at least 6 employees, |
| 60–249 employees in operation | 20 per cent of employees, or at least 37 employees, |
| 250–499 employees in operation | 15 per cent of employees, or at least 60 employees, |
| from 500 employees in operation | 10 per cent of employees, but at least 60 employees |

should be made redundant for operational reasons.

In the case of a **gradual reduction in personnel**, the decisive factor is whether it is based on **uniform corporate planning**. A close temporal connection between several waves of redundancies can be an important indication of uniform planning from the outset. Thus, if the staff reduction is based on uniform corporate planning, staggering the staff reduction over time to an extent below the relevant threshold values does not lead to the avoidance of co-determination rights under works constitutional law; the number of employees covered by each wave of redundancies must then be added together in accordance with the voting rights.

A later wave of redundancies may also be the result of **new planning**. This is particularly true if new circumstances have arisen after the first wave of redundancies which were not originally planned and scheduled by the company. If the company first carries out the agreed redundancies, which alone do not constitute a change of business, and only then decides to make further redundancies due to new circumstances, the waves of redundancies are not to be added together under co-determination law.

If a number of employees corresponding to Section 17 (1) of the Dismissal Protection Act is to be dismissed within 30 calendar days (the date of receipt of the declaration of termination / conclusion

of the termination agreement is decisive here, not the time of termination of the employment relationship), a **notification of mass redundancies** must be submitted to the Federal Employment Agency prior to the dismissals.

If the company intends to make notifiable redundancies, it must also conduct a **consultation procedure** with the works council in accordance with Section 17 (2) of the Dismissal Protection Act. The consultation procedure is legally independent of the rights of participation of the works council under Sections 111 et seq. Works Constitution Act. However, if the same works council body is responsible in each case, the two procedures can be combined to a certain extent. If a required notification of mass redundancies is not (duly) submitted or the consultation procedure is not (duly) carried out, this leads to the invalidity of the termination or the termination agreement. Unlike in the context of Sections 111 et seq.

Works Constitution Act, the **staggered timing of the planned re-**

dundancies may, however, remove the requirement for the notification of collective redundancies and the consultation procedure. If gradual dismissals are carried out on the basis of a uniform entrepreneurial decision, the number of employees regularly employed in the enterprise will regularly depend on the number of employees existing at the time of the entrepreneurial decision also for subsequent waves of dismissals. In order not to fall within the scope of Section 17 of the Dismissal Protection Act it may however be appropriate from a business perspective to carry out several waves of redundancies in such a way that the applicable threshold is undercut within the relevant 30-day period. In general, however, it is not possible to avoid having to make a new social selection for each wave of redundancies in the context of operational cutbacks.



4. Redundancies, but for whom?

Options for the best selection process

If a job is lost, the company is obliged as a matter of principle and in the framework of **social selection**, if the contract is terminated for operational reasons in accordance with Section 1(3) of the Dismissal Protection Act, that the person least in need of social protection be selected from amongst several comparable employees in the same company. Sufficient account must be taken of the length of service, age, maintenance obligations and severe disability of the employees. In weighing up these social selection criteria, the company has a certain scope for assessment, but the selection of employees affected by compulsory redundancies is not at the discretion of the company according to the legal concept. Especially in crisis situations it is often of immense importance for the company to keep young, dynamic employees as know-how and performance providers in the company and to part with older employees with

longer periods of service who are usually more worthy of protection.

By means of the so-called **key player clause** pursuant to Section 1 (3) (2) of the Dismissal Protection Act, the company can - at least in theory - exclude comparable employees from the social selection process whose continued employment is in the justified operational interest, particularly because of their knowledge, skills and performance. This is, however, an exceptional provision, for whose conditions the company bears the full burden of proof and demonstration in proceedings for protection against dismissal. As a rule, only the exclusion of a few specialists - who will often not be comparable with other employees - can be justified on the basis of this exceptional provision.

The assessment of how the social selection criteria are to be weighed up in relation to each other can only be checked for gross defectiveness under Section 1 (4) of the Dismissal Protection Act if it is based on a **personnel selection guideline** drawn up in conjunction with the works council under Section 95 of the Works Constitution Act. Within the framework of such directives, the social selection criteria are usually given a certain number of points on the basis of a specific points system, which can then be used to calculate, on a case-by-case basis, the social protection status of comparable workers to be included in the social selection. This weighting process carried out by the operating parties is subject to limited judicial review for gross defectiveness. This is the case if the weighting process applied does not take account of individual social criteria at all, is clearly inadequate or is of clearly excessive importance. The weighting of individual criteria can of course indirectly influence the social selection to a certain extent.

However, this is not an effective way of defining the group of comparable workers to be included in the social selection process.

If the reduction in personnel is a change of operation subject to co-determination within the meaning of Section 111 of the Works Constitution Act, the parties to the employment contract may, in a written reconciliation of interests, designate by name those employees to whom notice of termination is to be given. If such a **list of names** is available, it is presumed under Section 1 (5) of the Dismissal Protection Act that the terminations are due to urgent operational requirements. Moreover, the social selection can only be reviewed by the courts for gross defectiveness. In contrast to the establishment of personnel selection guidelines, this restriction of judicial reviewability does not only relate to the weighting of the social selection criteria in relation to each other, but also to the social selection as such and thus also to the determination of the group of comparable employees relevant for selection and -

at least according to the prevailing view in literature - the non-inclusion of certain employees in the social selection on the basis of justified company interests. In this respect, the list of names is a useful instrument for reducing the process risks that exist on the company side, particularly in connection with complex selection processes. However, it should not be overlooked that the operating parties may not make any arbitrary selection decisions. Companies are therefore well advised to **document the considerations underlying the selection process with a view to possible dismissal protection proceedings**. Furthermore, the works councils will often only be prepared to conclude such a list of names if appropriate financial concessions are made within the framework of the social plan.

Even if the law on the key player clause, personnel selection guidelines or the list of names contains certain instruments - which give the company greater scope in the social selection process or restrict the possibility of judicial review of

their implementation, it is ultimately not possible to achieve the best selection on a large scale. As a result, this can only be achieved by means of a **voluntary programme** which is specifically aimed at those employees who are dispensable from the company's point of view. However, to the extent that these are workers with poorer prospects on the labour market and - especially in times of economic downturn and declining employment - low motivation to change jobs, the voluntary programme will regularly have to provide for a correspondingly high financial endowment. Although this may pay off in the long run, it is often difficult to achieve in times of acute financial crisis and uncertainty.



5. Redundancies for operational reasons, but how?

Minimising procedural risks

If the necessary staff cuts cannot (only) be made on a voluntary basis, but if redundancies become necessary for operational reasons, there is inevitably the risk of a large number of subsequent dismissal protection proceedings. If the dismissals prove ineffective in the course of the judicial review and it is not possible to reach a settlement with the employee, the company is not only burdened with the risk of default of acceptance of wages, but may also be threatened with the failure of the planned staff reduction and the cost reduction aimed at by this. However, these risks can be significantly reduced by observing a few formalities as part of careful preparation of redundancies for operational reasons. The following indications make no claim to completeness. Rather, they are limited to those aspects which are often not given sufficient attention in the context of corporate planning.

Urgent operational requirements for termination within the meaning of Section 1(2) of the Dismissal Protection Act may arise for external reasons (e.g. loss of jobs due to a lack of orders or a decline in turnover) or internal reasons (loss of jobs due to **business decisions** such as rationalisation measures or conversion or restriction of production). While business decisions as internal causes for the loss of jobs are only subject to an abuse of rights control by the courts and are not examined for their factual justification or expediency, a judicial review is carried out if the company makes external reasons responsible for the loss of jobs. In the opinion of the Federal Employment Court, in this case the company may only cut as many jobs as appears to be justified on the basis of the external reasons used.

In the process of protection against dismissal, the company is thus subject to the procedural challenge, which is regularly difficult to overcome, of having to demonstrate and, if necessary, prove on a 1:1 basis that the external circumstances have led to the loss of a specific number of jobs. In order to avoid this risk of litigation, companies are well advised not to rely on external reasons in the process of protection against dismissal to justify the loss of jobs, but to rely exclusively on an internal corporate decision. External economic developments affecting the company can only be used as co-determining motivational factors for the organisational decision taken by the company, but not as a direct reason for the loss of jobs. Even in the case of a business decision, however, it must be noted that in dismissal protection proceedings, if the employee disputes the decision, the company must fully explain and, if necessary, prove whether such a business decision actually exists. This means that the company has to present and, if necessary, prove who made which

business decision and when. In this respect, it is recommended that the **decision of the responsible decision-makers be documented in writing under the relevant date** before the notice of termination is given.

Section 1 (2) of the Protection against Dismissal Act also requires that the urgent operational requirements prevent the **continued employment** of the employee affected by the dismissal for operational reasons.

If, at the time of receipt of the notice of termination, there are vacant workplaces in the **company or operation** where the employee could continue to be employed by way of transfer or change of employment, possibly after carrying out reasonable re-training and further training measures, the notice of termination is not socially justified and therefore ineffective. The same applies if such jobs become vacant with reasonable certainty by the end of the period of notice or in the foreseeable future after expiry of the period of notice. In particular, the Federal Employment

Court's broad understanding of the priority of change of employment over termination of employment, according to which an offer of a vacant job may only be omitted in extreme cases, often leads to a not inconsiderable risk of litigation in larger companies, which have to fill vacant jobs throughout the company even if staff are reduced at the same time.



However, employees often only become aware of existing vacancies through **internal or external job advertisements** by the company. To a certain extent, the risk can be minimised by postponing such job advertisements for a certain period of time. In addition, the presentation of the **requirement profile** for the vacant workplace is subject to its availability within the company, which is only to be checked for obvious lack of objectivity. Insofar as certain personal or factual requirements are necessary for the proper performance of the job, the company's decision as to which requirements are to be placed on the job holder can only be reviewed in court for obvious lack of objectivity. The decision of the company to have certain activities carried out only by workers with certain qualifications must be respected by the employment courts in any event, if the qualification features have a comprehensible reference to the organisation of the work to be performed. Within this framework, the risk of existing opportunities for further employment can therefore

also be minimised to a certain extent by defining the job profile of the vacancies accordingly.

If the reduction in personnel amounts to notifiable **mass redundancies** within the meaning of Section 17 (1) of the Dismissal Protection Act (see 3. below), a notice of termination may only be validly declared when the mass redundancies have been notified. If the notice of termination is received by the employee before the date of receipt of the proper notice of termination by the competent Employment Agency, it shall be invalid. Although this does not prevent the decision to dismiss from being taken and the letters of dismissal from being signed before the notice of collective redundancy is given, the worker may not receive the notice of dismissal until after that date.

Particularly in the case of time-critical staff reduction measures, which often do not allow much time for manoeuvre in view of the applicable notice periods and require a prompt notice of termi-

nation, it is advisable to **carefully document both the time of receipt of the confirmation of receipt from the Federal Employment Agency and the time of personal delivery or posting of the notice of termination letter by post**. Since the concept of dismissal also covers the conclusion of termination agreements, the above also applies - albeit only in theory, as a rule - to the signing of termination agreements.

Finally, particularly in the case of international corporate structures where the managing directors of domestic companies are based abroad, it should be noted that terminations and termination agreements always require the **written** form for their effectiveness under Section 623 of the German Civil Code.

This means the handwritten signature; the electronic form is excluded. The use of stamps, facsimile or other mechanical aids is therefore not sufficient. It is also insufficient to send the notice of termination by e-mail, even if it is

digitally signed, or to send a notice of termination with a scanned signature. Even the transmission of a signed letter of termination by fax does not satisfy the written form requirement. In this context, it should also be noted that the notices of termination must always be **signed by the person(s) entitled to terminate** the contract. In the case of legal entities and private companies, these are primarily the representatives of the executive bodies entered in the commercial or association register. If notices of termination must be given promptly and the signatures of the **executive representatives** cannot be obtained in time, the signatures can alternatively be provided by appropriately **authorised persons** on site.


However, it should be noted that the employee is to be given an **original signed power of attorney** together with the notice of termination. Otherwise, according to Section 174 sentence 1 of the German Civil Code, there is a risk that the employee immediately rejects the termination, which leads to the

ineffectiveness of the termination. In time-critical situations, this alternative only makes sense if the authorised person has already been provided with original power of attorney in the required scope in advance. The presentation of the original signed power of attorney in accordance with Section 174 sentence 2 of the German Civil Code is only not required if the **employee has been informed of the power of attorney**. This applies in particular to the granting of a **power of procurement**, which has been entered in the commercial register and made known. If only joint power of attorney exists, the other signatures must also be obtained.


The appointment of the **head of the human resources department** also includes the notification that he or she is entitled to give notice of termination.

The selection and implementation of the appropriate measures always depends on the circumstances of the individual case. The above overview therefore does not replace an examination of the legal situation in your company and

does not constitute legal advice. Our specialists, Dr. Kilian Friemel and Christiane Richter-Wienke, will gladly answer your questions and support you in the concrete implementation of the measures best suited to your company.




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