8 Catastrophic Downsizing Mistakes and How to Avoid Them

Steven T. Hunt, Ph.D.
Click to follow my posts: www.linkedin.com/in/steventhunt

Difficult economic times demand difficult leadership decisions, including those that involve workforce reductions. Laying off part of your workforce is not easy, but it's even more problematic if the headcount reductions do not deliver the intended business returns. And even worse if they actually prove detrimental to the long-term health of the business. This article outlines the eight critical mistakes that organizations contemplating workforce reductions should avoid in order to minimize negative short-and long-term impact on their business.

Letting go of employees, especially ones that have proven to be hard working and dedicated, is one of an organization's most difficult decisions, and it often falls on the CFO. The downsizing decisions that are made at this critical juncture will have both short- and long-term impacts on the company's ability to compete, or even survive. Organizations contemplating potential workforce reductions should recognize and actively avoid the following eight catastrophic mistakes that can occur during a downsizing.

1. Downsizing when it isn't necessary.
Research shows that companies that downsize tend to perform more poorly than competing organizations that are able to avoid workforce reductions[i]. Even more concerning, these lower performance levels often persist for years following layoffs. You can reasonably conclude from this finding that if your goal is to cut costs, layoffs should not be considered until after you have fully explored a range of other cost-cutting methods. This includes suspending non-critical expenses, eliminating unprofitable projects and programs, and exploring whether employees will take voluntary reductions in pay and benefits to save costs.

2. Eliminating critical talent.
If layoffs are not tightly targeted, you risk losing skills and knowledge needed to run your business. Downsizing decisions should be informed by a careful and systematic evaluation of the level and criticality of each employee's skills. Do not eliminate people unless you are confident that they will not walk out the door with crucial skills and knowledge required to keep the company running.

3. Spreading reductions equally across departments.
Do not make the common mistake of implementing downsizing by telling each manager or department head that they have to reduce workforce costs by the same percentage. This ignores the reality that some departments are more critical to business growth and revenue than others. It also treats work teams as though they all perform at the same level. It treats managers who tolerate substandard performance the same as those who have developed high-performing teams and may have already removed underperformers. Instead, workforce reductions should be based on systematically evaluating the following two factors in order of importance. First, the value employees provide to the business based on the nature of their role and/or quality of their performance. Second, the costs employees create for the organization in terms of salary and job expenses.

4. Reducing the workforce without restructuring the work.
It is important to approach workforce reductions as a form of organizational restructuring and not simply a reduction in force. You need to determine how people's jobs, responsibilities, and work processes are going to change as a result of the reduction. Do not simply fire employees and expect the

remaining survivors to "do more with less." Such an approach will lead to excessive burnout, poor performance, and turnover among the very employees you most want to keep during these troubled times.

5. Not cutting enough.

Companies understandably often seek to minimize the size of an initial workforce reduction. Rather than making cuts based on conservative and accurate financial predictions, companies may base initial layoffs on optimistic assumptions about future business conditions. This can lead to scenarios where companies make multiple recurring rounds of layoffs. This workforce instability breeds stress among employees who constantly worry whether they will be the next to be laid off. High performers start to seek job opportunities in other companies that will provide a more stable work environment. Meanwhile, employees who do not have outside opportunities start to perform more poorly as a result of increased fear and anxiety over their job future. It is better to make one difficult but significant workforce reduction and avoid further cuts in the future, rather than making a series of shallow layoffs over time which can destabilize the organization and create a feeling of the company slowly dying "the death of a thousand cuts."

6. Violating legal requirements and guidelines.

There are a variety of complex and often confusing legal requirements associated with workforce reductions. These may include the need to demonstrate that downsizing decisions do not adversely impact employees from certain demographic groups, providing advanced notice to local communities about workforce reductions, and ensuring that laid off employees receive appropriate severance and healthcare coverage. These requirements vary from state to state and in some cases from city to city, and become even more complex when layoffs occur in multiple countries. As soon as you realize you may have to make workforce reductions, proactively seek guidance from your human resource department and legal counsel to begin planning for possible legal issues. Complying with these regulations could be far more complex and time consuming than you might expect.

7. Treating people poorly.

There are many examples of companies using downsizing processes that treated hard working and loyal employees almost as though they were criminals. For instance, bringing people into a meeting room, telling them they are being let go and then herding them out another door into the parking lot. Or escorting veteran employees to their desks to clear out their belongings and then marching them out the door under the watch of armed security guards in front of former co-workers. There are real instances of companies sending termination notices to employees via mass e-mail. Or laying off employees without warning or severance and then refusing to give them any references other than verifying their former employment.

There are two major problems with these insensitive downsizing processes. First, assuming the organization survives and begins to grow again, you may want to rehire these employees. They are more likely to return if they were treated fairly and respectfully when they were let go. Second, treating downsized employees poorly undermines the morale and trust of employees who remain. These "survivors" will resent the company if they feel it treated their former coworkers like excess baggage to be thrown away when things got bad. They will also wonder "is that how they will treat me if I'm let go?" When planning layoffs, the costs associated with severance packages and outplacement services should not be viewed as money spent on laid off workers, but as investments to ensure the loyalty and commitment of the employees who remain.

8. Under-communicating.

Some organizations approach communication during a downsizing as an exercise in suppressing information. They shield employees from the truth about the company's financial situation lest it create fear and unplanned turnover, or get out on the street and negatively impact the confidence of customers or investors. However, communication and dialogue between employees and leaders is critical to the success of any change effort. This is especially true during workforce reductions when people are worried about fundamental needs such as pay and healthcare. Open and active communication plays a key role in effective downsizing through:

- ✓ Establishing a sense of fairness. Clearly communicate the reasons why the company was forced to make reductions, explain the methods used to determine who to let go, and let people know what the company has done to ensure proper and fair treatment of employees who lost their jobs.
- ✓ Building employee confidence in the future. Employees remaining with the company must understand what the future holds for them within the company. Leaders and managers need to explain the company's strategy to emerge from the current crisis and the opportunities it will provide to those who remain on board.
- ✓ Accruing important accounting costs. Certain restructuring costs associated with downsizing can only be received if proper communication has been made to employees. For example, companies cannot accrue costs for severance unless employees have been made aware that they are eligible to receive it.
- ✓ Giving employees a sense of control. People do not fear change — they fear the uncertainty that accompanies change. The most effective way to address this is to give employees a sense of control over the changes they are experiencing. This requires providing information about the challenges and constraints the organization is facing, enlisting their support in developing methods to overcome these challenges, and listening and acting on their suggestions.

Workforce reductions are inherently difficult, risky, and emotionally exhausting events. When a company implements layoffs, it is statistically more likely to have lower levels of performance for years to come. Avoiding the eight mistakes outlined here cannot guarantee a rapid return to full productivity, but it reduces the chance that workforce reductions will create catastrophic failures and a permanent loss of company value.

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[i] Cascio, W.F., Young, C.E., & Morris, J.R. (1999). Financial consequences of employment-change decisions in major US corporations. Academy of Management Journal, 40, 1175-1189.