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OUTSOURCING: HUMAN RESOURCE ISSUES SHOULDN'T BE AN AFTERTHOUGHT!

By Judith Droz Keyes

Much has been and is being written about outsourcing. Not a legal term, "outsourcing" refers to the arrangement whereby one company looks to another company to perform some aspect of its business operation. It's like delegating, but at an inter-company rather than intra-company level. It's like subcontracting, but of an internal corporate function rather than of a contractual responsibility.[1]

Outsourcing is becoming increasingly common in a variety of situations. In the professional and service sectors, back office functions such as billing and photocopying/faxing are often outsourced. Administration of benefit plans (such as 401k plans and disability plans) is frequently outsourced. Many companies outsource recruiting. In large workplaces, food service is usually outsourced. In the technology and telecommunications industries, customer service may be outsourced. In manufacturing, fabrication of component parts is commonly outsourced. With specialization the norm and productivity the watchword, outsourcing is an idea whose time seems to have come.

INSIDE

Two Avenues to Outsourcing

There are two basic ways that outsourcing arrangements get started from a personnel perspective: one, where existing employees of the source company become employees of the vendor company; and the other, where the vendor company brings its own employees to the arrangement and the employment of source company employees is terminated. Either way, a plethora of employment law and employee relations issues are presented. Too often, these issues are considered late in the deliberation and negotiation process — and sometimes, hardly at all. This is a risky and unnecessary mistake.

While not a comprehensive list, the following are among the considerations that should be addressed early on in the process of outsourcing.

[1] Arrangements akin to outsourcing but different are the variety of "leasing" or "staffing" arrangements whereby some or all of a company's positions are staffed by people who are employed by another company for payroll and benefits purposes, but who work on the user-company's premises under the direction of the user-company's management. While these arrangements present their own significant employment law issues, this article does not address them. Nor is outsourcing synonymous with "offshoring." While outsourcing may involve a vendor company outside the United States, this is not necessarily the case. For purposes of this article, whether outsourcing involves an offshore or onshore vendor company is irrelevant.

Human Resource Considerations in Outsourcing

Union Issues. If some or all of the affected employees are represented by a union, labor responsibilities need to be addressed. If labor costs are a factor, before the decision is made, the union must be notified. Regardless of whether employees will be hired by the vendor, the union must be given an opportunity to bargain regarding the effects of the outsourcing on employees. Part of this bargaining will involve whether the vendor company has an obligation to recognize the union, and what that means for wages and benefits.

Notice Issues. Whether there is likely to be any federal or state WARN Act obligation, and if so, whether any such obligation will belong to the vendor or the source company, must be determined. Regardless of the WARN obligation, care must be taken not to give misleading information or false assurances to any potentially affected employee or applicant, once an outsourcing decision has been made or is in the offing. Management must be instructed as to how to respond to the inevitable rumors, and it should be determined early on when, where, how, and by whom information will be conveyed and the announcement made.

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Retention Issues. If it is important to retain key employees either until outsourcing comes to fruition or afterwards, retention agreements should be developed, offered, and obtained. These agreements need to be carefully constructed (do not rely on a template!) so as to allow the requisite flexibility while achieving the desired goal of stability.

Separation Pay Issues. Regardless of whether source employees will be laid off or will become vendor employees, they will cease being employees of the source company. Accordingly, whether there is an obligation to pay severance pay under source company plans or handbooks must be determined. How accumulated vacation pay or other paid time off will be handled must be resolved, especially in California, where vacation and PTO cannot be forfeited and must be fully paid out on termination. Eligibility for bonuses of all stripes must also be evaluated.

Hiring Issues. Changing employers will have an impact on employees even if they are hired by the vendor. Concerns about reporting relationships and career paths will exist regardless of whether the vendor's pay and benefits are the same, or even are better. Careful thought must be given to these intangible issues—and if retention is a concern, retention agreements should be considered. Before employment offers can be made, it must be determined not only what pay and benefits the vendor will provide, but also whether employees will be given credit for time employed by the source company for such purposes as vacation accrual and benefit vesting. If some but not all source employees will be offered positions with the vendor, how the selection will be made and by whom should be very carefully considered. The privacy rights of employees may be breached if well-meaning (or otherwise) source company managers share information about individual employees with vendor management. Personnel records of employees who are hired or are being considered for hire by the vendor should be disclosed or provided to the vendor only with permission from the employees involved. Accommodations made to disabled employees should not be negative factors in the hiring equation, and their continuing reasonableness must be objectively determined. Employees on protected leave at the time of transition must be handled with particular care with respect both to notification and to eligibility for employment with the vendor.

Transition Issues. If source company employees become vendor employees mid-year, the impact of tax withhold-

SAN FRANCISCO ADOPTS LOCAL MINIMUM WAGE OF $8.50

By Kendra F. Barnes

San Francisco employers soon must pay employees a minimum wage of $8.50 per hour. This new requirement is the result of Proposition L, passed by the voters in November.[2] It requires employers with 10 or more employees to pay at least $8.50 per hour for all work performed within San Francisco beginning February 23, 2004. Non-profit organizations and businesses with fewer than 10 employees will pay a minimum wage of $7.75 beginning January 1, 2005, and $8.50 (as adjusted) beginning on January 1, 2006. The new law does not apply to employees who work less than two hours a week within the geographic bounds of the city or who are covered by a collective bargaining agreement that expressly waives the provisions of the ordinance.

The minimum wage will be adjusted yearly based on increases in the Regional Consumer Price Index. By December 1 of each year, the Living Wage/Living Health Division of the Office of Contract Administration (the "agency") will publish and make available the adjusted minimum wage rate for the upcoming year. The agency will also publish a notice informing employees of the city minimum wage and their rights under the ordinance. All employers must post this notice in a "conspicuous place" at any San Francisco workplace or job site. The notice is available at www.ci.sf.ca.us/oca/lwlh/fw/notice.pdf. The notice must be posted in English, Spanish, Chinese, and any other language spoken by at least five percent of the employees at the workplace or job site. Employers must also provide each employee at the time of hire with the employer's name, address, and telephone number in writing. Finally, the ordinance requires employers to retain payroll records for four years and to allow the agency to access such records.

While the ordinance is limited to the City and County of San Francisco, it may not be the last of these ordinances should the federal and state minimum wages remain at their current levels. So far there are only two other places in the country—Washington, D.C., and Santa Fe, New Mexico—that have similar local minimum wage ordinances. ■

[2] The full text of the code can be accessed at www.sfgov.org/site/government_index.asp#codes.

NEW CAL-OSHA FORMS AVAILABLE

By Kendra F. Barnes

Reminder: California employers are required to post OSHA Form 300A from February 1 through April 30. This posting reflects work-related injuries and illnesses for the past calendar year. OSHA recently updated this form, which is available at www.osha.gov/recordkeeping. ■

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ing and cafeteria plan (§ 125 plan) balances needs to be assessed and communicated to employees. COBRA notification must be given where benefit eligibility is impacted.

Supervision Issues. Once the transition has been made, there will be a close and ongoing relationship between source company management and employees, and employees of the vendor company. To avoid a "joint employer" relationship, the source company must relinquish control and decision-making to the vendor. This will be more or less difficult depending on the work site of the now-vendor employees. While the source company's on-going evaluation of the quality of the vendor's effort is both warranted and essential, evaluating individual vendor employee performance is risky. It is the vendor company that will be obligated to ensure its employees are not subjected to discrimination or harassment on the basis of an impermissible consideration (age, pregnancy, religion, sex, race, etc.) and are not retaliated against for whistleblowing or engaging in other protected activity. It is incumbent on the vendor

employer to ensure the proper classification of employees as exempt versus non-exempt (or sometimes as independent contractors), and to pay employees properly under federal and state wage/hour laws. In the case of non-exempt employees, this includes maintaining accurate time records, paying for overtime properly, and in California, mandating the taking of meal periods and permitting the taking of rest breaks. Fulfillment of these important obligations requires the cooperation of the source company, and that requirement should be clear in the outsourcing contract.

Asset Protection Issues. Vendor employees – including those who were once source company employees – should commit to protecting the source company's trade secrets and confidential information to the same extent as source company employees. Agreements prohibiting unfair competition (non-solicitation of employees and clients and non-competition, where permitted) by vendor employees should also be negotiated at the outset of the outsourcing arrangement.

Separation Issues. The outsourcing relationship may not last forever. The respective rights of the source company and the vendor company with respect to hiring employees, ownership of inventions and ideas, and competition should be determined at the beginning of the relationship, not put off until the time of dissolution.

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In 2004, companies must be more productive, cost-effective, and nimble than ever before. At the same time, employment laws are more protective of workers, including the "contingent" workforce, than at any time in history.

Outsourcing may well be a good solution to the challenge of achieving corporate goals. Employment laws and human resource issues need not be an impediment to outsourcing — but neither should they be an afterthought. ■

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