



# Client Alert

## Compensation Considerations in Light of COVID-19

March 24, 2020

### Contact

**Manan (Mike) Shah, Partner**  
+1 212.530.5501  
[mdshah@milbank.com](mailto:mdshah@milbank.com)

**Joel I. Krasnow, Partner**  
+1 212.530.5681  
[jkrasnow@milbank.com](mailto:jkrasnow@milbank.com)

**Nicholas DeLuca, Associate**  
+1 212.530.5391  
[ndeluca@milbank.com](mailto:ndeluca@milbank.com)

**James Beebe, Associate**  
+1 212.530.5206  
[jbeebe@milbank.com](mailto:jbeebe@milbank.com)

**Kelly P. Bartley, Associate**  
+1 212.530.5012  
[kbartley@milbank.com](mailto:kbartley@milbank.com)

**Christina Skaliks, Associate**  
+1 212.530.5282  
[cskaliks@milbank.com](mailto:cskaliks@milbank.com)

**Jon Sorger, Associate**  
+1 212.530.5677  
[jsorger@milbank.com](mailto:jsorger@milbank.com)

---

### Background

The COVID-19 virus and nationwide quarantines have disrupted businesses throughout the country. The impacts of the virus and the associated quarantines could last for weeks or months and businesses are facing unprecedented challenges in addressing the short-term and long-term effects. While each company will face unique circumstances, below are some general considerations that a company should keep in mind regarding employee compensation and benefits matters.

### Performance Goals

Many companies set their annual or long-term performance goals in the first quarter of the year. Accordingly, performance goals for bonus and equity programs for 2020 (and, in the case of some long-term programs, possibly future years as well) have likely already been set by the board or compensation committee. The events of the last few weeks are likely to have substantially affected the assumptions upon which the goals were based, and what may have been a realistic and appropriate performance goal in January may now look unreasonable and unachievable. Accordingly, boards and compensation committees should consider whether to re-assess their goals to make them more realistic and to better reflect a company's updated priorities. Given the extreme volatility of the current period, it may make sense to wait until economic conditions stabilize to make such a re-determination. If any board or compensation committee has yet to establish performance goals for 2020, it should consider expressly reserving the right to adjust such performance goals to account for the impact of COVID-19 or alternatively include a qualitative performance goal that will give the board or committee additional flexibility.

## Reductions in Force

An unfortunate reality for many companies is that reductions in force may be necessary to manage liquidity, business downturns, and, in some cases, to maintain the company's status as a viable going-concern. While state laws vary, the federal Worker Adjustment and Retraining Act of 1988 generally applies to a company with more than 100 full time employees if there is a layoff of 50 or more employees at a single site of employment. These laws generally require at least 60 days' advance notice of any reductions in force. While there are exceptions, including exceptions for unforeseeable business circumstances and natural disasters which make giving 60 days advance notice unworkable, such notice must still be given as soon as practicable. Federal and state WARN requirements contain many nuances and exceptions, and state laws may impose more onerous restrictions, so a company should make sure to consult with legal counsel to appropriately navigate these requirements in connection with any substantial reduction in force.

## Pay Cuts and Other Cost-Cutting Measures

Company-wide pay cuts are being considered by many companies as a way to manage cash while limiting the number of terminations. In connection with any pay cuts, it is important to be mindful of any "good reason" provisions in agreements with employees which may be triggered. Such provisions generally include a reduction in compensation as one of the prongs, but some may contain exceptions for company-wide reductions in pay, and nearly all contain exceptions for any actions consented to by the affected employee. If such provisions are triggered, an employee may be able to resign and receive severance, accelerated vesting, or other benefits at a time when the company may need to retain the affected employee. Further, any severance or accelerated payment obligations which may be triggered could further exacerbate any liquidity issues a company may be facing.

In considering the elimination or reduction of any fringe or other benefit, including severance, a company should take care to analyze the implications of such measures under the plan document, state law and ERISA, as applicable. Further, any company considering suspending or reducing safe harbor matching contributions mid-year to a safe harbor 401(k) plan should ensure that it does so in a manner complying with Section 401(k) of the Internal Revenue Code and applicable IRS guidance and notice requirements.

## Equity Awards

Most executive teams are compensated with equity awards. It is likely that such awards have declined in value in recent weeks. If the decline in equity values continues for a substantial period of time, a company should consider whether the existing awards provide sufficient retention value on a go-forward basis. Such considerations are likely premature at this point. It would be prudent for a company to make such a determination later in the year if retention concerns prove to be an issue.

The decline in equity values may also have an unintended impact on any long-term incentive programs which provide for regular equity grants equivalent to a specified dollar value (e.g., many director programs are set up in this manner). For any grants under these programs which occur during this time, a company may end up granting much more equity than intended, which could have an outsized dilutive impact and may also result in a company running up against, or exceeding, its equity plan limits, whether on individual grants or on the total amount of equity reserved. For purposes of valuing the amount of equity awarded, a company could consider using a longer time horizon to determine the share value (e.g., instead of using a 30-day volume weighted average price (VWAP) or the prior day closing price, utilize a 90-day VWAP) to the extent its plans or awards permit the use of such a valuation period.

The equity value decline may also provide a window of opportunity to make equity grants at a low value. Option awards must generally be granted with an exercise price which is no less than the fair market value of the underlying equity. If the underlying equity is currently at a depressed value, options could be issued at this time with a strike price that is reflective of this equity value. This would provide the recipients with the potential for exceptional value on these awards if share prices return to normal levels in the future. Given the current volatility of stock prices, it is possible that the strike price of stock options will be higher than the company's stock price shortly after grant, resulting in an underwater option. Additionally, with respect to any new grants of restricted stock, recipients may choose to make an 83(b) election on such grants if the underlying value is sufficiently low. The 83(b) election permits the recipient of restricted stock

to take the value of the stock into income at the time of grant with future appreciation being eligible for capital gains treatment. However, a company should remain mindful that any 83(b) election will result in a withholding obligation on the part of the company based on the value of the stock for which the 83(b) election is made. Generally, a company either requires the recipient who makes the election to provide the cash necessary to satisfy the withholding obligation or, if liquidity issues are not a concern, a company may provide loans to executives equal to the tax amount due, with such loans being secured by the underlying shares. A company should make sure that executives engage with their own legal and tax advisors on the risks and benefits of making any 83(b) election.

Finally, a company should revisit its succession planning in order to avoid any disruption in case a key employee is unable to perform key functions for a prolonged period of time as a result of potential infection.

This crisis poses unique challenges for all industries and navigating the complexities of what will be a very fluid situation will require thoughtful planning, both legally and from a commercial perspective. Companies are advised to carefully consult with their legal and other advisors on the specific actions taken during this time.

Joel I. Krasnow	<a href="mailto:jkrasnow@milbank.com">jkrasnow@milbank.com</a>	+1 212.530.5681
Manan (Mike) Shah	<a href="mailto:mdshah@milbank.com">mdshah@milbank.com</a>	+1 212.530.5501
Kelly P. Bartley	<a href="mailto:kbartley@milbank.com">kbartley@milbank.com</a>	+1 212.530.5012
James Beebe	<a href="mailto:jbeebe@milbank.com">jbeebe@milbank.com</a>	+1 212.530.5206
Nicholas DeLuca	<a href="mailto:ndeluca@milbank.com">ndeluca@milbank.com</a>	+1 212.530.5391
Christina Skaliks	<a href="mailto:cskaliks@milbank.com">cskaliks@milbank.com</a>	+1 212.530.5282
Jon Sorger	<a href="mailto:jsorger@milbank.com">jsorger@milbank.com</a>	+1 212.530.5677

---

### **Executive Compensation and Employee Benefits Group**

Please feel free to discuss any aspects of this Client Alert with your regular Milbank contacts or any member of our Executive Compensation and Employee Benefits Group.

This Client Alert is a source of general information for clients and friends of Milbank LLP. Its content should not be construed as legal advice, and readers should not act upon the information in this Client Alert without consulting counsel.

© 2020 Milbank LLP

All rights reserved. Attorney Advertising. Prior results do not guarantee a similar outcome.