

Legal Alert: Employment Issues for Nonprofits in Financial Distress

Nonprofits in Financial Distress: Q&A with an Employment Attorney

Although the economy is showing signs of recovery from the 2008 collapse, this recovery has yet to hit the nonprofit sector. Consequently, a number of nonprofits are experiencing economic distress and are even closing.

The Law Project asked long-time volunteer attorney Charles Krugel to answer common questions from nonprofit boards, and to alleviate concerns about laying off employees when it's apparent that financial difficulties, including the possibility of closing might occur. Keep in mind that this is only general information for employees "at will" and does not apply to employees with employment contracts, and nonprofits seeking legal advice should contact competent legal counsel.

1. When should the board tell employees, funders and partners of economic difficulties?

As soon as possible. Once the organization's executives and board members know of the issues, they should immediately and jointly inform employees and other concerned parties.

A key factor is that the message should come from the executives and directors together. Any mixed messages or appearance of a fracture will create doubt and fear. Doubt and fear tends to escalate, and unfortunately resolving those concerns will likely take up an increasing amount of time. Getting ahead of these issues and the doubt and fear they entail is essential.

Moreover, notify the auditors as soon as possible, since the nonprofit may have uncashed checks and other such payments that require attention.

2. If employees ask if they will be fired or laid off, what should the board tell them?

Be honest and tell them what you know. If you don't know the answer to something, tell them that you don't know. If you're not sure whether there will be layoffs, tell them that. Tell employees that these concerns are so new that, in addition to the board, they're among the first to know about them.

Also, ask your employees for their input, and advice for solutions. In times of trouble, it's possible for your employees to come up with solutions. Seek their advice before it's too late.

3. How much confidentiality of information should be maintained?

Once the board and employees know about the situation, don't expect much confidentiality. Frankly, confidentiality isn't much help anyway. It insulates from possible solutions and causes the board and management to expend a great deal of energy trying to "keep a lid" on issues. If no one knows you're in trouble, no one will offer to help.

4. If we have to lay off employees, when should we pay their final compensation and what should be included as final compensation?

First, review the employment policies, handbooks and other relevant documents. Determine if any promises have been made to employees concerning paid time off (e.g., vacation days, sick time, personal days) or other reimbursements such as gas and travel reimbursements.

Under Illinois law, all final compensation should be paid in the next regular paycheck, unless you have a written agreement or policy otherwise.

Moreover, as a general rule, the only owed paid time off is accrued vacation time. Absent a "use it or lose it" policy, or some other restriction, all accrued vacation time should be included in the final paycheck. Consequently, accrued and paid sick or personal time off isn't owed to the employee, unless your organization has an internal rule otherwise.

Once management knows what forms of compensation are owed, make sure that final paychecks are issued by the next regular pay date. If this cannot happen, then inform employees in writing and seek either their acknowledgement or agreement to receiving less than full compensation. This acknowledgement or agreement could help alleviate concerns with regulatory agencies like the Department of Labor.

5. How long should the board or management maintain records of final payouts, layoffs, closing, etc.?

As a general rule, the IRS requires that you maintain tax records for seven years. Although most employment related agencies require you to maintain records for a lesser amount of time, it's wise to be conservative and save records for seven years. This way, you won't expend time and energy trying to figure out what to keep or not to keep.

6. If a nonprofit learns it is in financial trouble, is that the time to start revising policies and procedures?

No, unless you've sought advice from competent legal counsel, stick with what is already in place, since any changes might be misunderstood or misinterpreted, which could lead to further troubles.

7. What should the board or management do if they discover that employees or associates are stealing funds, vandalizing property or otherwise acting out against the nonprofit or the board in a possibly illegal way?

Contact the police immediately and file a report. Get a copy of the report and any report numbers. Don't hesitate about this. Just do it and press charges if you can.

8. What should the board or management do if employees aren't acting in an illegal manner, but are otherwise behaving inappropriately?

This requires finesse to deal with. You want to balance between allowing people to vent their frustrations and fears along with not modeling appropriate behavior for children, volunteers & associates. It's best not to respond in a way that could escalate a situation. Try to maintain rationality while allowing the individual to vent. Maybe move them to another location or schedule a meeting for a later time and date. There are an infinite number of ways to prevent a situation from escalating into violence or otherwise inappropriate behavior.

This same advice applies to online or social media communications. It's better to let employees and associates verbally vent than to act out in more irrational or inappropriate ways.

For the past eight years, Charles Krugel (www.charlesakrugel.com) has helped The Law Project clients with employment issues pro bono. Charles also serves on numerous nonprofit boards, including the Chicago Bar Foundation's Young Professionals Board, the Kelly Hall YMCA in West Humboldt Park, and Youth Outreach Services.

Organizations in economic distress and potentially facing termination of employees as a result should contact The Law Project at 312-939-3638 or visit our [Resources for Nonprofits](#) page for additional resources.