Pulling the Plug on CIRCUIT CITY

After court-ordered bankruptcy and liquidation, the HR team helped bring a humane end to the electronics retailer.

By Adrienne Fox

Circuit City headquarters was a shell of its former self on a wintry day last February. On the company's Richmond, Va., campus—where corporate officials operated for 60 years—lay vacant buildings surrounded by empty parking lots that once held the cars of almost 2,000 associates.

This day, only a sheriff knocked on one dark door to deliver a court order garnishing the wages of an employee who had presumably lost a job weeks earlier. Still working inside was a team of HR professionals who would ultimately handle that court order as well as all the employee-related issues associated with bankruptcy.

The credit crisis, stock market plunge, high unemployment—and consumers more concerned with holding on to their homes than purchasing big-screen TVs—all contributed to the malaise. Unable to find a buyer or cash to reorganize, Circuit City Stores Inc. announced plans on Jan. 17, 2009, to liquidate 567 U.S. stores and lay off 34,000 employees. ›

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ILLUSTRATION BY LAURA BRUCE

Until the last minute, executives worked tirelessly to find a buyer or devise a plan to emerge from a November 2008 Chapter 11 filing. No buyer could cover the $2.3 billion debt and fund a turnaround. So, a Richmond judge ruled for involuntary bankruptcy and immediate liquidation of assets to pay off creditors.

Back at headquarters, employees were stunned to hear the news, despite the fact that executives had been honest about the dim prospects. With no time to grieve, Eric Jonas, senior vice president of human resources, began selecting employees to wind down the HR function. Coping with their own worries, the remaining HR associates had to change course—and their mindset—from company growth strategies to shutdown scenarios.

On March 31, Circuit City stores closed for the last time. The second-largest electronics retailer joined a string of recent retail liquidations including Linens 'n Things, Mervyns and KB Toys. It was a complex, emotional endeavor—and one that all HR professionals can learn from.

Harsh Reality

Bankruptcy filings involving business debts were up 54 percent in 2008, totaling 43,546, according to the Administrative Office of the U.S. Courts. Some blame the 2005 changes to the Bankruptcy Code for making it more difficult for companies, particularly retailers, to emerge from Chapter 11. Others point a finger at the credit crisis and drop in consumer spending.

"On a daily basis, I meet with companies in some sort of financial stress," says Lee Woodard, managing partner of the Syracuse, N.Y., office of Harris Beach and co-leader of the Financial Restructuring, Bankruptcy and Creditors' Rights Practice Group. "There is no money available on the market to refinance or reorganize to keep payroll going."

The credit crunch affects companies' and liquidators' abilities to secure loans, explains David Berliner, a partner in the New York office of BDO Consulting and leader of its Business Restructuring Group. "Before, a liquidator would pay the company a lump sum upfront based on the estimated value of the estate," he notes. "If a company needed to close five stores out of 50, it would use that cash to cover payroll or inventory for the other 45 stores and turn things around. Today, that cash is not available. So, companies are forced to close all stores."

Without money to buy out assets, liquidators serve as agents and charge management fees. The company assumes liability for employee-related issues, says Berliner.

Those Left Behind

Bankrupt companies generally either reorganize under Chapter 11 of the Bankruptcy Code or liquidate under Chapter 7. Chapter 11 usually means that the company continues in business under court protection. A judge can force a company to liquidate under Chapter 11 if the judge suspects plans have not materialized to cover debts, as was the case with Circuit City.

Either the liquidator or company managers are in charge of closing the business. Creditors prefer that managers stay on for several reasons. First, they know the business and will get more value out of the liquidation. Second, if there are problems with employees, the HR team has the experience to settle them. Third, employees who stay on during liquidation are more loyal to managers than to a liquidator. That means lower turnover and less chance of stolen or damaged inventory.

With the decision to keep an HR team, Jonas set about choosing its members. "The wind-down team has to include people who can multitask and work in ambiguous situations," he says. They have to "solve problems creatively. You're tempted to say, 'Let's keep our star players or the people with the top titles.' But you can't. You have to keep the ones who are adept at implementation and don't mind doing tasks outside of their job descriptions." In addition to Jonas and Laurie Lambert Gaffney, vice president of HR, the team consisted of four generalists: a liquidator liaison and three field HR people. In the technical area, a pension expert, a health and welfare expert, and a compensation director stayed on. Each had allotted time to complete tasks—from eight to 26 weeks and longer—and milestones to meet.

Typically in a liquidation, managers will receive retention bonuses to stave off turnover. The amount of the bonuses is limited and must be approved by the judge.

"I told my team, 'Your first and primary responsibility is to find a job,' " recalls Jonas. "The retention bonuses and the continued salary are nothing to sneeze at, but in the end, you are shutting down an organization."

Business Ends, Now What?

The team must wind down the estate efficiently. "Efficiency means returning as much capital as you possibly can so that there is money available for the unsecured creditors," says Jonas. "Many of those unsecured creditors are associates."

"Secured creditors"—usually banks—have liens on property, while "unsecured creditors" are paid on a pro rata basis only after the claims of all secured creditors are satisfied.

"This casts you in a different role as an HR executive; you work for the estate, not the associates," explains Jonas, noting that there was no money for severance or outplacement services. "There are walls you have to bring down to do this kind of work. This tests your objectivity."

Circuit City created a management board in charge of closing the business, with representatives from distribution, finance, HR, information technology, legal and merchandising. Gaffney represented HR on the board, meeting daily to discuss assignments. Her team unwound contracts for health and welfare, 401(k)s, outsourcing, and pensions, and served as conduits to communicate with current and past employees.

These tasks were uncharted for the HR team members. To guide them, restructuring consultants with New York-based

Bankruptcy To-Dos

Health care insurance, pension plans and compensation issues top the to-do lists of HR executives at a company closing down.

"All employee records must be reviewed and corrected," says Laurie Lambert Gaffney, vice president of HR at Circuit City. "We made sure employees' addresses were up-to-date to distribute W-2s and final paycheck stubs. We also are still responsible for associate relations issues" because of the liquidator's consulting relationship.

If bankruptcy and liquidation become the only option, HR managers have a limited time to notify employees and close down. "I see many claims by employees who worked for the company in the past but didn't work at the time of bankruptcy," says David Berliner, a partner in the New York office of BDO Consulting.

Berliner works with companies that have not kept meticulous vacation and sick-time records. "The individual store manager would keep paid-time-off records, and that works great when everything is operating fine. But in a bankruptcy, headquarters is scrambling to get that information from the supervisors before they leave," he says. "All of a sudden, you have an employee disputing the amount of vacation he took and wanting to get paid for it.

"There's a [deadline] set by the court, and notice is sent to creditors, including employees, to make a claim in a certain amount of time, usually a few months," Berliner continues. Employees can file a claim to challenge wages paid, and HR managers must check the books and challenge those claims, he says.

Claims usually involve allegations of inadequate notice under the Worker Adjustment and Retraining Notification Act, which requires 60 days' notice for mass layoffs.

Traditional pension assets should not be at risk when a business declares bankruptcy. The Employee Retirement Income Security Act requires that promised benefits be adequately funded and that pension funds be kept separate from business assets and held in trust or invested in an insurance contract. If a company does not have funds to pay all pensions, they are guaranteed by the federal Pension Benefit Guaranty Corp. up to a certain amount.

For 401(k) plans, the bankrupt company stops making any matching contributions and keeps the plan operating until all employees have transferred their accounts to new providers. HR professionals need to notify plan providers of contract termination and instruct employees to contact the provider for transfer paperwork. "Some people move the plan immediately, while others hold on, not knowing what to do," says Berliner. "The form can seem daunting."

If the company had self-funded insurance plans, such as health or workers' compensation, employees have a limited time to file claims. There may be an uptick in claims while people rush to make medical appointments before the insurance money runs out. "I worked with a company that didn't have enough money to pay for all the claims," explains Berliner. "We contacted local health care providers to negotiate the amounts owed. We agreed to pay immediately at a reduced rate if they agreed not to go after the employee for the money."

Circuit City had a self-insured health care plan, so COBRA wasn't an option for its associates.

"What many people don't realize is if you go online to apply for coverage and you get rejected, you automatically get put into another category and are subject to higher premiums—if you get approved," notes Gaffney. "We had to quickly communicate with our associates and lead them to our carriers first because they wouldn't reject them. Then, they could shop around." The HR team worked with insurance carriers and turned over census files so the carriers could talk directly with former plan participants.

—Adrienne Fox

FTI Consulting provided frameworks and checklists. Nevertheless, "We had to decide how to do everything," says Jonas.

From the Chapter 11 filing forward, the executive and HR teams openly communicated with employees. They held town hall meetings with employees and met with directors. They created workshops for managers and instructed them on how to operate.

"Circuit City had honest and straightforward communications within the legal confines," says former HR manager Dave Phillips. But when a company ceases to exist, no communication vehicles remain. Even the consumer web site shut down.

"We didn't know how we were going to find answers," says Stephanie McGrath, a former marketing brand manager. "We packed up and left two days after the announcement. In the first few days, you are in shock and don't know what to ask. It's not until later that people start thinking of questions."

HR generalist Cathy Gilmour had one week to research and launch a communications strategy for former employees. "There was no time to debate options or to seek approval," says Gilmour, who created a page on LinkedIn and posted questions and answers. The site also became a place for associates to post job leads and communicate. "We only monitor it for misinformation or inflammatory statements," she says.

Gilmour also created a page (www.cityconnections.ning.com) on another social networking site that lists resume tips, job leads and updates from the company.

Online Resources

For more information about bankruptcies, including the WARN Act and legal requirements, see the online version of this article at www.shrm.org/hrmagazine.

Above and Beyond

Regional HR Director Rich Salon's role was to help the home-delivery distribution and service centers close down. On his own time, however, Salon worked tirelessly to find job leads for associates.

Shortly after the announcement, "The HR team came together and said, 'We're dumping about 34,000 associates onto a job market that is probably the worst we've seen in our lifetimes. Some of them had worked for Circuit City for 10, 20 and 30 years. What can we do?' " recalls Salon. He fielded calls from companies with openings and sent notices to other companies trumpeting the skills of his associates. Wanting to do more, he organized a job fair at headquarters to help nearly 2,000 former employees find work. The HR team publicized the event through the Internet, via the media and by word-of-mouth.

At the bare-bones affair, prospective employers were provided with tables and little else—not even coffee. Representatives of 80 companies came from Colorado, Georgia, Illinois, Massachusetts and Pennsylvania as well as Virginia. They ranged from ACN, a telecommunications network marketer, to the Federal Reserve. University counselors came to discuss continuing education. Entrepreneurial groups sent experts to explain how to start a business. Ukrop's Super Markets Inc. of Richmond gave away grocery coupons, and relocation companies offered discounts.

The most popular events at the job fair, however, were resume-writing and interviewing workshops held by former Circuit City HR professionals. Why would they take time from their own job searches to spend unpaid hours educating former associates? "You support those people for so long that you want to help," says Jennifer Stern, a former HR manager. "If I can spend five minutes improving someone's resume that turns out to be the difference in getting an interview, that's worth it to me."

Melissa Hagerman, a former HR manager, and Phillips also reviewed resumes during the two-day job fair. "The executive team from [acting CEO] Jim Marcum on down wanted to make the landing as soft as possible," Phillips says. "We thought, if it's going to crash, let's try to mitigate the impact."

Circuit City veteran Chris Geith attended the job fair—the first one of his career. "I set a goal to make two contacts—and I did," says Geith, former regional vice president who oversaw stores in 11 West Coast states with 15 district managers in 129 locations. "Even if you didn't get a job from the job fair, you were encouraged by the turnout of companies that are hiring."

One week after the fair, companies had extended 32 offers, including seven from Bank of America. Recruiters at other organizations flew people to their offices for second interviews. "The interest level was great, and they gave positive comments about our associates' skill levels," says Salon.

Salon brushes off accolades, somberly noting, "I've only been here for three years, but some of these associates have given their blood, sweat and tears for decades. I would love to see every associate not go a day without pay, but that's not reality. We've received a lot of great feedback and appreciation from our associates for the work we've done, and that's rewarding."

Go Out with Dignity

Gaffney wonders why HR professionals at other expiring companies don't do what her team has done. Every company has internal talent to take these measures, Gaffney says. "The people you lay off today could be your co-worker, neighbor or boss tomorrow."

Not that Circuit City leaders didn't make their share of mistakes: The retailer suffered an employee relations blow in March 2007, laying off 3,400 highly paid employees with the intent to replace them with lower-paid ones—a decision HR leaders fought. "Despite HR counsel, which included alternatives, the executive team elected to move forward with the original plan," recalls Jonas. "As an HR team, we did the best we could to mitigate the fallout." An age discrimination class-action lawsuit filed in California was settled in December 2008 for $15 million.

Even with this blemish, Jonas reflects proudly on his HR team's record. "I witnessed the growth of this function and saw people rise to the occasion. … I wish we had more time."

Geith, now a vice president for Barnes & Noble, adds: "With downsizing, our HR team was always respectful and fought for the benefits and the rights of the separated employees. When there was money, there was severance and outplacement. When there wasn't, there was heart and soul in the solutions."

Jonas sums up: "Lead with integrity, serve with humility and treat people respectfully is how we run our business. And this is how we will wind down our business." HR