

**Relationship between Conduct of Business, Personnel Management and
Labor-Management Communications during Business Turnarounds
(Summary)**

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1. Purpose of This Report

“Business turnarounds,” which refer to the rehabilitation of the business operations of an ailing company, have been drawing public interest in recent years as an increasing number of companies have launched business turnaround efforts. In many cases, such efforts involve changes in the corporate organization and modifications of the terms of employment and working conditions. However, debate about the business turnarounds conducted so far has focused mostly on how to smoothly harmonize the interests of the parties involved in the rehabilitation process and how to maximize the economic value of the rehabilitated business operations. Meanwhile, changes in the corporate organization and the ensuing modification of working conditions and the personnel management system have relatively been neglected as topics of debate.

In this report, we define a business turnaround as an “activity intended to enable a company that finds it insolvent and difficult to operate on its own due to problems such as excessive debts and a credit squeeze to get back on its feet by focusing on the parts of its business operations where some profits can be expected.” In compiling this report, we investigated cases of rehabilitation-type bankruptcy proceedings (including proceedings based on the Civil Rehabilitation Act and based on the Corporate Rehabilitation Act) and cases of business turnaround under the framework of rehabilitation support by the Industrial Revitalization Corporation of Japan. Based on the results of these investigations, we examined (i) how issues related to the terms of employment and working conditions are handled in the turnaround process, (ii) how personnel management is conducted, and (iii) what impact business management and labor-management communications during the business turnaround process have on (i) and (ii).

2. Structure of This Report

This report consists of three parts. **Part I** first examines the background to the increase in cases of business turnaround in recent years and the institutional frameworks regarding the relationship between business turnarounds and employment and labor, which is an essential element in studying the conditions of employment and personnel management during the turnaround process. It then summarizes the issues concerning employment and personnel management that often arise from business turnaround efforts, in order to clarify the focus of this research. **Part II** looks into the results of the investigations of 26 business turnaround cases in order to identify similarities and differences between those cases with regard to how the issues concerning employment and personnel management cited in Part I are handled in practice, and analyzes how the way such issues are handled is affected by the conduct of business and labor-management communications in the turnaround process. We conclude Part II with a study on the implications of our findings and analysis of what should be done in the future to ensure appropriate employment during the process of business turnaround and restructuring. **Part III** compiles nine cases of business turnaround, selected with due consideration of the differences regarding major elements of such turnarounds, with a view to providing further details on the actual state of employment and personnel management during the turnaround process.

3. Business Management, Personnel Management and Labor-Management Communications during Business Turnarounds

– Results of Case Studies and Analysis –

As part of this research, we held hearings between May 2004 and March 2006 with 25 companies and one corporate group that had engaged in business turnaround efforts. The following is a summary of the similarities and differences between the cases we studied with regard to (i) reforms regarding the terms of employment and working conditions, such as job and wage cuts, and (ii) reforms of frameworks for executing business and overseeing that execution.

(1) Reforms Regarding Terms of Employment and Working Conditions during Business Turnarounds

1) The scale of job reduction during the business turnaround process depends on (i) whether a drastic overhaul of the framework for executing business, including the workforce, is necessary in their core business, in addition to sorting out debts, (ii)

whether there is a sponsor for the rehabilitation and (iii) needs for job reduction which depends upon how many jobs were reduced and how many employees retired voluntarily before the turnaround process started. The scale of job reduction is not affected much by whether the sponsor is an ordinary company or a business turnaround fund.

The job reduction measures implemented during the business turnaround process were (i) inviting voluntary retirement, (ii) encouraging retirement and (iii) dismissing all employees and re-employing them under new terms. In the case of (iii), the scale of job reductions tended to be relatively large.

2) The scale of wage reductions during the business turnaround process, like the scale of job reductions, tended to be large at (i) companies trying to improve their financial condition of their core businesses mainly through reducing costs and (ii) companies pursuing rehabilitation without the support of a sponsor. Wage cuts and job reductions are regarded as alternatives to each other in some cases, while in other cases, both jobs and wages are reduced on a large scale.

3) With one exception, in all the cases of business turnaround support by the Industrial Revitalization Corporation covered by this research, neither major job nor wage (basic salary) reductions were implemented as part of the turnaround process. Although it is difficult to draw a firm conclusion from this research alone, it is possible that the framework of support by the Industrial Revitalization Corporation has helped to lessen the impact of business turnarounds on the terms of employment and working conditions by providing breathing space for supported companies to sort out their debts at an early date.

4) In cases where employees were not represented by a labor union or any other organization, consultations and negotiations between the management and employees over job and wage reductions proposed by the management were concluded without requiring a particularly large amount of time. Also, at most companies where employees were represented by labor unions, job and wage cuts were implemented without a major labor-management dispute. From this, we may infer that if a reasonable amount of time is spent on consultations and negotiations over job and wage reductions, labor unions tend to put priority on the smooth implementation of business turnarounds and wage payments to employees in exchange for accepting some wage and job cuts, leading to a consensus among union members.

However, it should be noted that there were a handful of cases in which employees complained about the measures proposed by the management. This suggests (i) that a labor management dispute could arise if the proposed job and wage cuts are too steep, as it would be difficult to secure sufficient time for labor-management communications to form a consensus, and (ii) that the labor-management relationship could be undermined if there is no consensus among employees on the revisions of the terms of employment and working conditions proposed by the management.

5) There were few cases in which the terms of employment and working conditions reflected wishes of employees that were at odds with the proposals made by the management. However, this does not mean that labor-management communications play a small role. Given that, in the cases of companies implementing unusually steep job and wage cuts, we have recognized progress in business turnarounds following frequent and close exchanges of information, we may assume that adequate labor-management communications can contribute significantly to reducing adverse effects, such as an erosion of employees' morale, by giving them a clear picture of the business turnaround.

6) In some of the cases that we studied, an industry-based union to which company-based unions affiliate was involved in the business turnaround process as part of efforts to minimize the impact of revisions of the terms of employment and working conditions on employees. This indicates that the involvement of personnel with experience of business turnarounds, including staff members of industry-based unions, could lead to more favorable results for labor unions and employees by enabling them to make alternative proposals.

(2) Personnel Management Related to the Reform of Business Operations

1) During the business turnaround process, it is necessary not only to promote measures focusing on cost reduction, such as business crisis management and financial restructuring, but also to implement measures to reform business operation itself, such as setting a strategic focus, and carrying out organizational reform, necessary for boosting profitability and earning profits on a sustainable basis.

In cases covered by this research, companies implemented measures to improve business results and efficiency, such as (i) developing new products, (ii) advancing into new product segments in which they can take advantage of their original technologies, (iii) specializing in products and services with high value added, (iv) reviewing and

improving manufacturing processes and (v) reforming information infrastructure, in addition to cost reduction measures, including closing unprofitable stores and factories and reforming the procurement of raw materials.

2) Among the measures implemented in order to enhance employee awareness and motivation in line with the reform of business operations described above were (i) communicating the corporate policy and stance regarding the business turnaround throughout the company by various means, and (ii) adopting employee proposals regarding the business turnaround.

3) In the retail, tourism and insurance industries, companies focusing on education and training of employees in order to smoothly reform business operations devoted efforts to the education and training of store clerks and sales personnel in particular, since their business performance depends in large part on how they handle customers. Meanwhile, manufacturing companies usually conducted employee education and training with the support of outside consultants in order to enhance the productivity of their manufacturing facilities, and, in most cases, aimed to establish a Toyota-style production system, regardless of the type of products they produced.

4) We found that companies carrying out business turnarounds without the support of a sponsor did not actively engage in efforts to change the mindsets of employees, enhance their motivation or strengthen employee training. This may partly reflect the fact that all such companies studied by us were small or medium-sized companies. In any case, without the participation of an outsider in the business management, it is probably difficult to implement measures that involve introducing new perspectives, knowledge and expertise, such as changing the mindsets of employees and strengthening employee education and training.

5) The number of companies that overhauled the employee evaluation and treatment systems, in addition to reforming business operations, was larger than the number of companies that made efforts to change the mindsets of employees, enhance their motivation or strengthen training. This indicates that company managers generally regard reforming the employee evaluation and treatment systems as the top priority when launching into business turnarounds. Although merit- and performance-based employee treatment was usually preferred, some companies dared to adopt seniority-based treatment in light of the nature of the core businesses.

6) There were not many cases in which employees and labor unions showed notable reactions to the new personnel management measures adopted as part of the reform of business operations. At companies with no labor union, individual employees showed various reactions to such measures, prompting the companies to respond on a case-by-case basis as necessary. However, we assume that in such cases, the absence of any parties or organizations responsible for collecting employee opinions and forming a consensus makes it impossible for employees to react in ways that would have a company-wide impact.

Meanwhile, among companies with labor unions, differences in the levels of labor-management communications – as represented by the presence or absence of periodic dialogue or the frequency of dialogue – did not lead to noticeable differences in the ways their labor unions responded to personnel management measures. We surmise that whether labor unions can make significant responses or not is primarily affected by how they have been involved in the management of their companies in the past and what kind of guidance and support they receive from outside parties, such as industry-based unions.

4. Implications of Business Turnaround Seen in Terms of Impact on Workforce

Of the findings of our research, what are the matters that require particular consideration in future labor-management efforts regarding business turnarounds and in future policy-making by the government? Also, what are the implications for future actions that should be taken by the labor and management and future policies that should be adopted by the government in light of our findings?

(1) Need to Create Favorable Environment for Rapid Start of Business Turnarounds and Establishment of Framework for Quick Support

Although a business turnaround involves a certain degree of job and wage reductions in most cases, sharp cuts are not always necessary. Some of the cases examined by this research involved few job and wage cuts as part of the business turnaround process. It should be borne in mind that most of the cases that largely avoided job and wage reductions represented either a business turnaround supported by the Industrial Revitalization Corporation or a “prepackaged type” business turnaround. Of course, this does not mean that these types of business turnaround can always avoid or minimize the impact on the terms of employment or working conditions. Nonetheless, it indicates that the impact is likely to be reduced by a business turnaround based on support from

the Industrial Revitalization Corporation, as it enables the quick sorting out of debts, and by a prepackaged type business turnaround, the goal of which is to achieve quick rehabilitation before the enterprise value is eroded. There have already been calls for the need to establish institutional frameworks to promote a quick start to and support for business turnarounds, from the viewpoint of avoiding an erosion of the enterprise value. However, our findings convince us that the establishment of such institutional systems is also essential from the viewpoint of reducing the impact on the terms of employment and working conditions.

(2) Need for Establishment of Effective Execution at Individual Companies

In most of the cases that we examined, the management played the leading role in implementing measures regarding the terms of employment, working conditions and personnel management during the business turnaround process, regardless of the presence or absence of a labor union. At most companies, labor unions and employees agreed to the broad outline of the proposed personnel management measures, including job and wage cuts.

A business turnaround requires quickly paving the way for an improvement in business performance, so it is necessary to implement employment adjustment and reform the personnel management system swiftly. Therefore, we assume that it is desirable that a management team acting on the wishes of shareholders (corporate sponsors in most cases of business turnaround) implement various measures smoothly with a clear intent and responsibility. Should the management team fail to perform this function sufficiently, it would rather be desirable even from the viewpoint of labor unions and employees that a new management team be installed, in order to achieve a stronger management initiative in promoting business turnaround efforts.

However, if the management takes an excessive approach to implementing measures regarding the terms of employment and working conditions in an effort to achieve a quick business turnaround, a labor-management dispute may arise. Given that the labor side complained about the measures proposed by the management side in some of the cases covered by our research, the right approach to a business turnaround is, basically, for the necessary measures to be carried out by the management based on its own intent and responsibility, but with opportunities for labor-management communications being provided in order to seek the opinions of employees and form a labor-management consensus, so that the wishes of the workforce can be reconciled with the goal of improving business performance quickly.

(3) Need to Foster Personnel Capable of Supporting Activities of Employees and Labor Unions

In some of the cases we studied in this research, labor unions, in an effort to minimize the erosion of employee morale, successfully persuaded companies proposing job and wage cuts to accept their demands for smaller cuts, and companies proposing the dismissal to implement the agreement which promises the reemployment of all the dismissed employees and retaining of their previous working conditions. In one case, the company president abruptly applied for civil rehabilitation procedures and lost the trust of employees, so the labor union took the initiative in promoting business turnaround efforts with due consideration of the needs of employees.

However, it is difficult for employees and labor unions to be effectively involved in the business turnaround process in order to achieve smooth and swift rehabilitation, as in the above cases. Employees and labor unions would be required to have sufficient knowledge regarding the management and financial affairs of the business, as well as the know-how to maintain morale of employees who are upset and collect their opinions to form a consensus. However, we assume that it is quite rare for labor unions and employees at individual companies to make efforts on a daily basis to acquire knowledge regarding how the terms of employment and working conditions should be handled in the business turnaround process, or to study what measures may be directly taken by the management regarding the terms of employment and working conditions.

In many of the cases where employees and labor unions were involved in determining the terms of employment and working conditions and the personnel management system, the support provided by industry-based unions played a significant role. Some such organizations were actively providing support to their affiliated unions when such unions face corporate bankruptcy and rationalization, with dedicated staff assigned to accumulating the necessary know-how, and it was evident that this know-how was highly effective in helping employees with no experience of business turnarounds to cope with the turnarounds of their own companies.

The problem is that the support of such staff, who may be referred to as “turnaround managers acting from the viewpoint of employees and labor unions,” is only available for company-based unions affiliated with industry-based unions that are actively involved in such support. In the future, it will be necessary to promote the training of such staff at other industry-wide labor organizations and to foster such staff at a regional level, so that companies employees whose labor unions do not affiliate with any industry-base unions or who do not belong to any labor unions can receive such support.

(4) Response to Sharp Job and Wage Reductions

The analysis of the wage and job reductions implemented in the studied cases shows that sharp job and wage cuts are highly likely when there is no sponsor for the business turnaround or when the profit structure of the core business operations needs to be radically reformed. In order to minimize the possibility of sharp job and wage cuts, it is necessary, first and foremost, to create a favorable environment for the rapid start of business turnaround efforts and for the establishment of a framework that enables quick support for such efforts. However, even if a favorable environment is created, it would be impossible to completely prevent any sharp job and wage reductions that may be implemented as part of the business turnaround process. Therefore, it is also necessary to study how to handle cases in which such cuts are unavoidable.

One way to cope with those employees who would be compelled to be dismissed by possible large-scale job reductions would be to establish a network of labor unions between companies in each region or industry, so that they can collaborate in an effective manner when a case of business turnaround arises. Meanwhile, labor-management communications could provide an effective solution to how to deal with wage reductions, as indicated by our finding that frequent and close exchanges of information facilitated the implementation of business turnarounds at companies that were reducing jobs and wages more sharply than others.