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FEATURE STORIES

Drafting Effective Employment Agreements: Keeping the Employer's Best Interests in Mind, Part 2

By Bennett Pine

This article is part two of a two-part series of tips on how to draft effective employment agreements from an employer's perspective.

With more and more executives, managers and professionals in the modern work place demanding (and receiving) written agreements setting forth their terms and conditions of employment, employers should be aware of what they are getting themselves into when providing such written employment contracts. In part one of our two-part series, we explored the concept of employment at will and the parties' respective preferences for having an employment agreement, as well as including the following key clauses: scope of employment, term, termination and base salary and bonuses. In part two we will continue to explore key clauses, such as company stock, benefits and vacation, as well as how to deal with confidential information, noncompetition and other standard provisions which should appear in the employment agreement.

Company Stock—Tool for Building Employee Loyalty

Compensation or deferred compensation in the form of equity in the employer (including outright grants of company stock, stock options, deferred compensation incentive and bonus grants) represent an excellent way of building employee loyalty (and amassing great wealth for employees at the same time) by linking an employee's compensation to not only his/her personal performance, but to the overall performance and profitability of the employer. Such incentive plans also can provide powerful weapons preventing an employee from joining a competitor or otherwise engaging in activities which may be harmful to the employer. Interestingly, several of our firm's clients do not require their employees to sign noncompetition/restrictive covenants (see below) at all. However, their lucrative employee stock incentive plans which grant stock annually, vesting over a number of years, contain provisions providing that, in the event an employee resigns and/or joins a competitor, the employee will forfeit all (or a substantial portion) of the stock grants. In its simplest form an employer can provide that the stock grant will not be issued until a future date e.g., 12 months later, and that the employee must continue to be employed on the issue date. Such "golden handcuffs" provide or create powerful disincentives for an employee to engage in competitive activities, without actually preventing the employee from doing so. Moreover, as compared to traditional non-compete agreements, such forfeiture for competition agreements are more likely to be enforced by the courts, regardless of the reasonableness of the restriction imposed.

Benefits and Vacation

Benefit plans typically made available to employees may include health and medical insurance, disability and life insurance, pension, 401(k), cafeteria plan, dental, vision, etc. These may be specified by the employment agreement, or the agreement simply can provide that the employee shall be eligible for those employee benefit plans for similarly situated executives or employees. It is important to include language or a reference "in accordance with the applicable plans established by the employer, which may be changed from time to time." This prevents the employee from being locked in to the precise set of benefits in existence at the time the employment agreement was entered. Vacation entitlement is typically spelled out directly in the agreement, at least for the first year. Subsequent entitlement can be pursuant to company policy.

Confidential Information

As an initial matter, the employment agreement should recite that the employee is free of any contractual restrictions (e.g., noncompete imposed by a former employer) which would prevent him from entering the agreement and commencing employment.

The agreement must contain language by which the employee acknowledges that, during the term of his new employment, he will come into possession of confidential information regarding the employer, its business, employees, clients, prospective clients, etc., and agrees not to disclose that information, other than information that is otherwise generally available to the public, without the prior written permission of the employer. The employment agreement should also make expressly clear that this limitation of the disclosure of confidential information does not expire with the term of the agreement or the period of actual employment, but survives the termination of employment for any reason. On a related note, the employment agreement should include an ownership of work product provision to ensure that all inventions, works, drawings, programs and the like created by the employee shall become and remain the sole property of the employer.

Non Competition/Restrictive Covenant

It has been generally recognized that new employment serves as consideration for a noncompete agreement. Hence, a restrictive covenant included in an employment agreement which is effective upon the commencement of the employment relationship should be legally enforceable if reasonable in terms of scope, geography and duration. During the term of employment, the agreement should recite that the employee is expected to devote his full working time to the business of the employer, and may not be engaged in any other enterprise without the employer's express consent. Exceptions can be made for community or not-for-profit activities or managing personal investments. Post-employment restrictions on competition are quite a bit trickier. While post-employment restrictions on engaging in competitive activities or employment are inherently enforceable during periods when the former employee is still receiving compensation (e.g., severance pay) from the former employer, courts are reluctant to enforce overly broad noncompetition provisions which have the effect of preventing an individual from making a living. In my experience, it is preferable to couch the restrictive covenant in terms whereby the former employee agrees not to solicit or accept employment, consulting work, business from, or otherwise perform services for, any of the customers/clients/suppliers, etc. with whom he had any contact during the employment period. Former employees should also be prevented from soliciting or offering employment to any individual with whom they worked at the former employer. While employers often seek to impose such noncompetition restrictions for very long periods of time, in my experience, a prohibition on contacting clients/customers/suppliers/employees for a period of one year is both much more enforceable and, as a practical matter, generally sufficient to protect and insulate the former employer's business interests and relationships.

Other Standard Provisions

The employment agreement should also contain a number of "boiler-plate" provisions on a variety of topics. These topics include: expenses and reimbursement; termination in the event of death or disability;

indemnification for acts done within the scope of employment; notices; entire agreement; governing law; non-assignability; dispute resolution (litigation versus arbitration or other form of alternate dispute resolution); choice of law; place of dispute resolution; binding effect; entire agreement and non-modification/waiver.

Conclusion

A well-crafted employment agreement can satisfy an employee's need for certainty and security while, at the same time, preserving an employer's interest in running its business in an entrepreneurial and cost-effective fashion. It can also serve as a tool preventing competition by former employees. Time and attention spent by the employer prior the commencement of the employment relationship can result in great savings in terms of cost, flexibility and operating efficiency, both during and after the period of employment. We have drafted many employment agreements on behalf of employers and stand ready to help your business in this regard. 

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