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Preparing Employment Agreements

Intellectual Property Owners Association
Trade Secrets Committee
Employment Agreement Subcommittee
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Introduction

The Trade Secrets Committee generally considers laws and policies addressing the balance between an employee's right to seek employment and an employer's right to protect its intellectual property. The employment agreement is central to the employer/employee relationship. The Employment Agreement Subcommittee has been formed to address this critical aspect of trade secret law and policy.

The goal of this document is to raise issues inherent in preparation of an employment agreement and, where possible, provide sample language currently used to tackle them. The Employment Agreement Subcommittee thanks the members of the broader Trade Secrets Committee for their support of and contributions to this work in progress.

What Is A Trade Secret?

A trade secret is information (such as a formula, pattern, compilation, program, device, method, technique, or process) that derives independent economic value from not being generally known to the public. The information may be of a technical or business nature. Examples may include manufacturing techniques, new product designs, business plans, or sales projections.

To qualify for trade secret protection, information that is considered to be a trade secret must be the subject of efforts to maintain secrecy that are reasonable under the circumstances. Trade secret protection lasts as long as the secrecy of the information is maintained. Courts nationwide recognize an employment agreement that contains suitable language to be one reasonable step a company can take to preserve the secrecy of its information.

Considerations, Recommendations, and Sample Provisions

1. Who should be party to an employment agreement?

In most cases, the employer prepares an employee agreement for signature by a prospective employee. As employee covenants and other provisions of an

employment agreement begin to take shape, the employer will be confronted with two initial questions.

A. First, which corporate entity should be named in the agreement?

The corporate entity or entities expressly named as a party or parties to the agreement should, if possible, be the one(s) in possession of the intellectual property protected by the employment agreement. Holding companies may not gain as much protection as operating companies. In any event, it is recommended to employers that each employee's obligations be made to flow to all applicable entities of a corporate or partnership structure.

Sample Language:

The "Company" means [corporate name], its successors and assigns, and any of its present or future subsidiaries, or organizations controlled by, controlling, or under common control with it.

B. Second, which employees should be asked to sign an employment agreement?

It is recommended to employers that all employees be required to undertake certain confidentiality obligations in exchange for employment.

Sample Language:

Except as specifically directed by the Company, the Employee will not, directly or indirectly, during or after the term of his or her engagement by the Company, use, disseminate, disclose, lecture upon, or publish articles concerning, any Confidential and Proprietary Information. This restriction shall not apply to information that the Employee can establish, by competent proof, (i) was known, other than under binder of secrecy, to the Employee prior to his or her engagement by the Company; (ii) has passed into the public domain prior to or after its development by or for the Company other than through acts or omissions attributable to the Employee; or (iii) was subsequently obtained other than under binder of secrecy from a third party not acquiring the information under an obligation of confidentiality from the disclosing party.

"Confidential and Proprietary Information" means information disclosed to or known by the Employee as a consequence of or through his or her engagement by the Company, about the Company's plans, products, processes, and services, including without limitation, information relating to [briefly describe the Company's business], devices and models, and any

other information relating to research, development, inventions, manufacturing, purchasing, accounting, engineering, marketing, merchandising, and selling.

C. Can an employee's covenants be assigned to a successor?

The answer varies from jurisdiction to jurisdiction. Some states will not automatically assign employee covenants to a successor upon transfer of company assets from one entity to another. Other states may allow employee covenants to be assigned from company to company if the employee has agreed to it in advance of the transfer.

Sample Language:

This agreement shall be binding upon and inure to the benefit of the parties hereto and their respective heirs, personal representatives, successors, and assigns.

2. What provisions of a covenant not to compete may be appropriate?

The contents of employment contracts may vary from employee to employee within a company. For example, a receptionist with little if any access to valuable confidential information may not be asked to sign an agreement containing a covenant not to compete. On the other hand, a project manager tasked with overseeing development of new products should almost certainly be asked to do so – particularly if the company is young or vulnerable to competition from another entity formed by or otherwise using the company's former employees.

A. What length of time may be deemed reasonable?

As mentioned above, there is a tension between an employee's freedom to pursue employment of his or her choosing, and an employer's desire to protect its intellectual property – an asset class of continued and rising importance in today's business world. The "appropriate" and enforceable duration of a restrictive covenant placed on an employee varies according to a number factors: the circumstances of the employment; the value, knowledge, and prior experience of the employee; the state and venue in which the agreement may be sought to be enforced; and other factors.

B. What geographic restriction may be deemed reasonable?

As with the duration of a covenant not to compete, the reasonableness of the geographic reach of such a covenant may vary according to the factors

mentioned above. An employer may not be entitled to restrict an employee from plying his or her trade and skills in a place and manner that will have little impact on the employer's business. But an employee may not be allowed to use an employer's valuable intellectual property assets in a directly competitive endeavor.

Sample Language:

During the term of this agreement and for a period of two (2) years thereafter, the Employee will not render services anywhere within the United States of America, directly or indirectly, to any Competing Organization, except that the Employee may accept employment with, or render services to, (i) a Competing Organization whose business is diversified, and which, as to part of its business, is not a Competing Organization, provided that the Company, prior to the Employee's accepting such employment or rendering such services, shall receive separate written assurance satisfactory to the Company from such Competing Organization and from the Employee that the Employee will not render services directly or indirectly in connection with any Competing Product or Service (ii) any university or academic institution so long as such employment or engagement does not involve use or disclosure of any Confidential and Proprietary Information or research on or development of any Competing Product or Service. The Employee agrees to disclose to every Competing Organization by which the Employee may subsequently be employed or engaged, the restrictions upon his or her services herein contained.

"Competing Organization" means any person or organization engaged in or about to become engaged in research on, or development, production, marketing, or selling of, a Competing Product or Service.

"Competing Product or Service" means any product, process, or service of any person or organization other than the Company, in existence or under development, that competes, directly or indirectly, with a product, process, or service upon or with which the Employee has worked for the Company or about which the Employee acquires Confidential and Proprietary Information.

C. Is a restriction on solicitation necessary?

A non-solicitation provision may provide the company additional protection against the use of valuable customer information, for the benefit of a competitor, by a departed employee. A non-solicitation restriction is a more specific type of covenant not to compete that may warrant

consideration particularly for employees in sales or other fields that directly interact with customers, have access to customer pricing information, or know specific customer-acquisition/retention strategies. The enforceability of a restriction on solicitation may be judged by the reasonableness of both its duration and the type of conduct that is being curtailed. And the amount of resources the employee and employer each invested in developing valuable customer information may also bear on the length of time and type(s) of restricted activities that are deemed appropriate. The duration of a non-solicitation covenant may not need to be as long as, *e.g.*, the period of a restriction on competition.

Sample Language:

In consideration of my employment as a [sales representative] and in recognition of the investment the Company makes in developing good will with its customers, I agree that for a period of six (6) months following termination, for any reason, of my employment not to solicit, entice away, or divert any person or entity who is a customer of the Company with whom I have communicated during the twelve (12) month period prior to the termination of my employment.

3. Are there other affirmative steps employees should be required to take?

In all cases, an employee should be required to mark and designate confidential materials as such during the course of his or her employment.

Sample Language:

The Employee agrees to mark or otherwise designate all documents (in electronic or other form) containing confidential, proprietary, and/or trade secret information – on every page of the document (e.g., in a header, footer, or title block) – with the following designation of confidentiality:

PROPRIETARY AND CONFIDENTIAL
[COMPANY NAME]

In addition, an employer may ask its employees, perhaps annually, to certify that they have reviewed their employment agreements, understand the contents of the agreements, and continue to agree to be bound to them. Such a certification requirement may help promote an employee's compliance with his or her obligations under the employment agreement.

Sample Language:

The Employee agrees to annually review this Agreement, and provide a written certification of understanding and compliance with this obligation. The Company will provide the Employee with a certification form.

4. What obligations should the employee have upon termination of the employment relationship?

Certain obligations of an employee will necessarily end upon termination of the employment relationship (regardless of the reason for termination). But it is in an employer's interests to require that certain employee covenants survive after the employee leaves the company.

Sample Language:

Upon termination of his or her engagement by the Company, the Employee shall deliver to the Company all notes, reports, notebooks, letters, manuals, prints, drawings, photocopies, files, computers, disks, and all other materials relating to the Company, including copies thereof, that are in possession of or under the control of the Employee.

The Employee's obligations to the Company regarding Confidential and Proprietary Information and the Employee's covenant not to compete with the Company as set forth herein survive the termination of this agreement.

5. Where and how will the employment agreement be enforced?

It is generally recommended that an employer specify in advance of a conflict concerning the employment agreement which type of dispute resolution will be available to the parties, and whose law (*i.e.*, which state) will be used to decide the conflict.

A. Is arbitration a good idea?

Although courts are perhaps the most commonly considered venue for resolving disputes over employment agreements, arbitration may also be available if the parties agree to use it. There are advantages and disadvantages to using arbitration. From an employer's perspective, one potential advantage an arbitration proceeding may have over a courtroom setting is the ability to keep the proceedings secret. When a trade secret or other confidential information is the subject of a conflict, it may be preferable and logistically more feasible to present a compelling case for an employer when there is little or no risk that the public will be able to access

the dispute resolution proceedings. Another consideration, which could be favorable or disfavorable to a particular employer, is that an arbitration proceeding does not use a jury as the fact-finder.

Sample Language:

Any dispute arising from or relating to this agreement shall be decided by arbitration in the County of [employer's choice], by the American Arbitration Association and in accordance with the rules and regulations of that association. At the request of either the Company or the Employee, arbitration proceedings will be conducted in the utmost secrecy, and, in such case, all documents, testimony and records shall be received, heard, and maintained by the arbitrators in secrecy, available for inspection only by the Company or by the Employee and by their respective attorneys and experts who shall agree, in advance and in writing, to receive all such information confidentially and to maintain the secrecy of such information until such information shall become generally known.

B. Which state's law should govern dispute resolution concerning the employment agreement?

An employment agreement can make an express choice of law to govern enforcement, interpretation, and remedies under the employment agreement. Employers are often encouraged to consider specifying their respective state of residence or principle place of business as the state whose laws will govern disputes about the employment agreement. This may allow for a favorable jury pool in the event a trial is needed. Another factor an employer should consider is whether particular states or jurisdictions have developed and applied rules or doctrine that are comparably more favorable to employers than employees.

Sample Language:

This agreement shall be governed for all purposes by the laws of the State of [employer's choice]. If any provision of this agreement is declared void, such provision shall be deemed severed from this agreement, which shall otherwise remain in full force and effect.

Some jurisdictions have what they view as "fundamental public policies" that will generally override the parties' contractual choice of law. While this reality should not deter employers from making an express choice of law in their agreements, it is something to consider carefully in evaluating probable outcomes if there is litigation. A company with multiple offices might consider prefacing its choice of law provision with a preamble

explaining that it is selecting one particular jurisdiction to promote uniform treatment of the workforce. Although such a provision may not be controlling in all jurisdictions, it may help support an express choice of law where the jurisdiction chosen might otherwise seem remote to certain employee's worksite.

Sample Language:

In order to ensure that all of our employees throughtout the country will be treated the same regardless of the state in which they work, the law governing this contract will be the law of [employer's choice], the state of [the Company's headquarters, or perhaps the Company's incorporation].

6. How can an employer enhance its ability to obtain injunctive relief?

An employer faced with the possibility that an employee will misuse the employer's confidential or trade secret materials may pursue injunctive relief. Under the appropriate circumstances, the employment agreement can be used as evidence of the employee's understanding that confidential and proprietary information provided through the employment relationship is valuable, and that disclosure of such material may cause the employer irreparable harm.

Sample Language:

The Employee acknowledges that the Company's Confidential and Proprietary Information constitutes unique and valuable assets of the Company, the loss or unauthorized disclosure of which would cause the Company irreparable harm. Upon the breach or threatened breach by the Employee of any of the confidentiality provisions herein, the Company shall be entitled to an injunction, without bond, restraining the Employee from committing such breach. This right to an injunction shall not be construed to prohibit the Company from pursuing any other remedies available to it for such breach or threatened breach, including the recovery of damages.

7. Does an employer want to shift attorney's fees?

One way to discourage employee misconduct may be to contractually shift responsibility for enforcement of the employment agreement to the employee.

Sample Language:

The prevailing party in any action, arbitration, or other proceeding shall be entitled to an award of all costs and attorneys fees incurred in seeking

enforcement of or defending against enforcement of this agreement or any portion thereof.

8. Should an employment agreement refer to and incorporate by reference other Company policies, procedures, or guidelines for protecting confidentiality?

It is often desirable for an employer to have well-defined policies on maintenance and retention of paper and electronic documents, use and disclosure of certain materials within and without the Company (also known as "need to know" policies), and facility security and access control. All employees should be made aware of these policies. And employees should agree to remain familiar with and abide by each of them. The employment agreement can establish a procedure to keep employees abreast of company rules.

Sample Language:

The Employee shall annually review and continually abide by all company guidelines, polices, and procedures, including the following:

The Company's Document Maintenance and Retention Policies and Procedures

The Company's Use and Disclosure Policies and Procedures

The Company's Security and Controlled Access Policies and Procedures

[List other company guidelines, policies, or procedures.]

To the extent it is reasonable, careful attention should be paid to developing, implementing, and routinely refreshing awareness of these types of inter-company rules. Although an effective employment agreement is one way an employer can protect its valuable trade secret assets, other protections are often appropriate as well.

Employers may also use other types of agreements and covenants to further protect their valuable information. Examples include: (1) confidentiality or "non-disclosure" agreements for consultants, visitors, advisors, and others exposed to confidential information; and (2) bans on soliciting employees to join a new company.

9. Can some employee covenants survive if others are deemed unenforceable?

The answer varies from jurisdiction to jurisdiction. Some states allow reformation of an employee covenant or severability of an unenforceable provision from the

remainder of a contract. Other states prohibit reformation altogether. Still others allow reformation or severability only if the parties have agreed to it.

Sample Language:

In the event any provision of this agreement is deemed invalid or unenforceable for any reason, or in the event any provision of this agreement is judicially amended or reformed, all remaining provisions of this agreement shall remain in full force and effect.

10. Can an employer implement a new employment agreement for current employees?

Many companies have employment agreements already in place, but those agreements may be in need of revision or standardization across a workforce. Depending upon the size and age of the company, several different employment agreements may have been used. Fresh consideration to support employees' new and different obligations may be necessary.

There may be several approaches an employer can consider. *One*, new contracts can be implemented upon promotion of an employee. *Two*, new contracts can be signed by the entire workforce all at once. For logistical reasons, however, this may not be practical for companies of any substantial size. *Three*, a "bonus" can be paid for changing/increasing an employee's obligations. *Four*, a new contract can be required at an annual review and presentation of a raise. But as with all of the considerations and sample provisions discussed in this paper, it is important for a company to understand the law in the relevant jurisdiction(s) before selecting or implementing a new strategy. For example, certain jurisdictions require more than just continued employment or a company-wide raise to support new employment agreements for current employees.

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