

Negotiating Employment Agreements: 14 Key Issues



Compensation

- Does the base salary increase each year of the contract?
- Is there a signing bonus, especially if the employee would be losing options or other benefits for making the job switch?
- What quarterly or annual bonus is available? Is the bonus guaranteed, dependent on achievement of milestones, or wholly discretionary with the Board of Directors?
- Under what circumstances can the employee's base salary be reduced? Some agreements give the company the right to reduce base salary up to a certain percentage if other similar situated employee salaries are similarly reduced (such as might occur when the company is in financial distress).



Equity Grants

- What percentage of equity grant is appropriate – a percentage of issued and outstanding stock or a percentage of fully diluted stock?
- Should the grant be tax advantaged incentive stock options, non-qualified stock options, stock appreciation rights, or restricted stock units?
- If stock options, what is the exercise price?
- What is the vesting period for the equity grant? A typical scenario is 4-year vesting with a one year "cliff vest," meaning the employee must be employed at least one year before anything becomes vested.
- If the employee is terminated without cause, does some portion of the equity grant get accelerated vesting?
- How long does the employee have to exercise options after termination of employment? The typical period is 90 days. But this can vary depending on whether the termination is for cause, not for cause, or voluntary quitting by the employee to accept another job.
- Is there any acceleration of options upon an acquisition of the company? Does it require an acquisition plus a termination of the employee's employment (a so-called "double trigger")?
- Are the shares obtained upon exercise of an option subject to repurchase on termination of employment? If so, at what price?
- Are the shares obtained upon exercise of an option subject to a right of first refusal? If so, on what terms?



Scope of Employment

- What is the title of the employee's job?
- What are the employee's responsibilities?
- Can the employee be demoted? Can the employee's responsibilities be substantially modified, decreased, or increased?
- Is the employee guaranteed a seat on the Board of Directors while an employee?
- Where is the place of employment?
- Can the employee be relocated unilaterally to another city, or only with the employee's consent?
- Is the employee allowed to be involved in other activities (e.g., a directorship on other Boards, involvement in community activities)?



Benefits

- Will the employee participate in all of the benefit plans of the company?
- Which of these plans should be in place for the employee? Are all of the payments for the benefits the responsibility of the company?
 - a) Health and medical (including spouse and dependent coverage)
 - b) Disability
 - c) 401(k)
 - d) Pension
 - e) Cafeteria Plan
 - f) Life Insurance
 - g) Stock option/stock grant
 - h) Vision
 - i) Dental
 - j) Executive financial counseling

- How much vacation per year is the employee entitled to? Does unused vacation continue to accrue for the benefit of the employee and payable on termination of employment?
- How much accrued vacation can carry over to subsequent years?
- Any special loans or forgiveness arrangements?
- Are some of the benefits taxable to the employee? Should employee be reimbursed for the tax?



Term and Termination

- How long is the employment term or is the employment "at will"?
- What are the grounds on which the company can terminate the employee?
- What are the terms, if any, for compensation in the event of early termination?
- What are the circumstances that the employee can be fired "for cause," such as:
 - a) Conviction of a felony or any act involving moral turpitude;
 - b) Commission of any act of theft, fraud, dishonest or falsification of an employment record;
 - c) Breach of the employment agreement;
 - d) Failure to perform reasonable assigned duties; and
 - e) Improper disclosure of the company's confidential information
- Is employee entitled to severance pay on termination without cause? How much? Is it a lump sum or payable over time?
- If terminated without cause, is the company required to continue paying for benefits or COBRA benefits for some period of time?
- If employee is to receive a severance payment, the employee should be required to sign a release of liability for the benefit of the company.



Reimbursement of Expenses

- Will the employee's business expenses be reimbursed within a set time period?
- Is there a car or car allowance, cellular phone provided, or other such amenities?
- Are moving expenses to be reimbursed?
- Is there a relocation package available for employee?



Liability Protection for the Employee

- Does the company have Directors' and Officers' ("D&O") insurance coverage?
- Do the company Bylaws provide for indemnification protection for officers and employees?
- Does the company's corporate charter limit the liability of officers and directors to the maximum extent permitted by law?
- Is there an Indemnification Agreement that protects the employee, covering:
 - a) Indemnification protection for claims
 - b) Automatic advancement of legal expenses
 - c) Protection even if the employee is no longer employed by the company? (Note statutory limitations on indemnification.)



Confidentiality Restrictions

- Many companies have a separate form of employer Confidentiality and Invention Assignment Agreement that can be incorporated by reference. The employee must be careful not to use or divulge confidential information of a prior employer – the new employer will often want a covenant from the employee prohibiting such use or disclosure.
- If there are confidentiality restrictions on the employee, are the following excluded from the definition of "confidential information"?
 - a) Information that is or was publicly known, or which becomes publicly known through no fault of employee.
 - b) Information that is or was obtained from a third party who had the right to disclose the information without restriction.
 - c) Information independently derived by the employee without reference to the confidential information.
 - d) Information that was already lawfully in employee's possession or knowledge prior to the disclosure of the confidential information.
- How long do the confidentiality restrictions last?



Invention Assignment Issues

- What is the scope of the company's rights to the employee's development of new inventions, trade secrets, and ideas?
- Do the invention assignment provisions comply with applicable law?



Disability and Death

- What is defined as a disability event?
- What happens on disability? Does the employee continue to receive salary and benefits for some period of time?
- What happens on death? Can medical and other benefits continue for some period for the spouse and children?



Post-Employment Limitations

- Are there limitations on the employee soliciting company employees? For what period?
- Is there a covenant not to compete after termination of employment?
 - a) For what geographic regions?
 - b) For what period?
 - c) What is the scope of the covenant?
 - d) Are the restrictions enforceable under applicable law? (Generally not permitted in California.)



Dispute Resolution

Most Employment Agreements have multiple provisions dealing with disputes between the company and the employee:

- How are disputes resolved?
- Should confidential binding arbitration be the exclusive way to resolve disputes?
- In what city must disputes be brought if litigated or arbitrated?
- What is the governing law?



Golden Parachute

A "Golden Parachute" is a payment to or other benefit guaranteed to a company executive in the event the executive is fired as a result of a takeover of the company:

- In the event of a change of control of the company, is the employee entitled to terminate employment and receive the golden parachute payment?
- What are the tax implications of the golden parachute payment? Will the company also gross up the parachute payment to cover the tax?
- Will the company reimburse the employee's expenses in connection with an IRS audit claiming additional tax?



Miscellaneous Provisions

Good employment agreements have a series of "miscellaneous" clauses including those that address these issues:

- Is there an attorney's fees clause where the prevailing party in a dispute would be entitled to recoup its attorneys' fees incurred?
- Does the employee represent and warrant that his resume and information provided to the company are correct and complete?
- Are all the terms of the employment reflected in the agreement, thus allowing a clause stating there are no other terms of the employment relationship?