Who's On The Move? Protect The Assets That Ride Up And Down In Your Elevator

The Editor interviews ***Michael C. Lasky****, Davis & Gilbert LLP.*

Editor: Mr. Lasky, would you tell our readers something about your responsibilities at Davis & Gilbert?

Lasky: I co-chair Davis & Gilbert's Litigation Department. I also oversee the pro bono activities of the firm and am a member of the firm's management committee.

Editor: In addition to your busy practice, you have done a great deal of speaking and writing. How has this activity affected your practice?

Lasky: Everything I do outside my day-to-day practice – including speaking and writing, bar association work, pro bono activities and non-profit board work – has a very positive impact on my work for clients. I learned very early on in my career that these activities enhance the skills that a lawyer brings to his or her clients. I find that corporate counsel today are looking for lawyers who not only understand the law but also possess the skills that are often developed in a variety of extracurricular arenas.

Editor: One of the subjects you have addressed in your career as a speaker and writer is restrictive covenants. When I was in law school – a long time ago – one of the things we were taught was how hostile courts were to employer's attempts to impose restrictions on the future employment of their employees. Have things changed?

Lasky: When I was in law school, like you, there was really only one type of post-employment technique available to employers: what was called a non-compete clause. This was, effectively, a restrictive covenant that prevented the departing employee from soliciting business from the employer's customers for a period of time. Today, there are a number of newer and more creative techniques, which I believe reflect our movement toward becoming an information society and one in which the relationships between a company and its customers are very different from what they were in the past.

Editor: In your writing you talk about the "tools" that an employer should consider with respect to post-employment restrictions. Would you share with us what you mean by that term?

Lasky: I refer to "tools" because I think the term is useful when you consider the various goals that a company's general counsel is looking to achieve. One goal is to ensure that the company has adequate time to locate a replacement for a departing key executive. Another goal is to stabilize a key customer relationship. A third goal is to make certain that the departing employee does not become a competitive force to the company. These are separate and distinct goals, and they require different tools or techniques if the company is to be successful in achieving them.

In other words, a good "craftsman," so to speak, does not reach into his toolbox and attempt to have the hammer do the job that is more appropriate for the wrench. The same applies to achieving the company's specific goals in a way to protect its human capital and, frankly, the "contingent liabilities" that each key employee represents, especially when a key employee departs from the company.

Michael C. Lasky

Editor: Would you take us through some of these techniques?

Lasky: There are five techniques that a company should consider putting in its toolbox for different levels and types of employees. The first is a non-competition agreement. This is designed to prevent a departing employee from working for a competitor or in a competitive business for a period of time after he or she departs from the company. It is an industry-based restriction and represents a rather tight set of "handcuffs."

A second technique is a customer- or client-based restriction, i.e., a restrictive covenant. This is a provision that restricts the departing executive, for a period of time, from servicing customers or clients that he or she personally rendered services to during the period of employment.

A third technique is a non-raiding provision, which prohibits the departing employee from hiring or assisting in hiring another employee of the former employer. Here, the goal is to prevent compounding the harm that the departure of a subsequent employee or worse yet, a group of co-workers, might cause to a company.

A fourth technique is a combination of an extended notice provision and what is called "garden leave." This is particularly important in service sector industries, including financial services, real estate brokerage, marketing services and, indeed, any field where individuals hold the key to client relationships. The long-accepted idea that two weeks notice from the employee is sufficient notice of resignation is totally inadequate in today's environment. Now, there is a clear recognition that the more senior the person is in an organization, the more notice of an intention to leave – often expressed in months – is needed.

During the extended notice, an employer might decide that the departing executive should continue with his or her regular duties but work outside the office, or not work at all. Since the company continues to pay base salary, this technique is not prone to the types of challenges faced by traditional restrictive covenants because the employer is not depriving the departing employee of his or her livelihood. The departing employee has just been neutralized as a competitive force, at least for a period of time.

A fifth and final technique is to utilize the company's long-term benefits programs to enhance some of the foregoing techniques. Many companies are updating their long-term incentive or stock-option plans to include forfeitures in the event the former employee violates some requirement of the original contract of employment or a severance agreement executed in connection with the employee's departure.

General counsel are looking at what I call the protective matrix – the way in which these various five techniques should be combined to best manage and reduce the risk that the departure of a key employee raises. I recently wrote a chapter in *Human Resources 2007,* published by Thompson, which discusses these techniques in greater detail and provides samples of matrices.

Editor: Is there a way to avoid expensive injunction lawsuits that typically are involved in stopping a former employee from violating a restrictive covenant?

Lasky: Absolutely. Many companies are designing their post-employment restrictions to include an agreed upon, pre-set monetary formula for a specific type of violation. These types of liquidated damages provisions, which may accompany some or all five of the techniques discussed above, can provide a great deal of positive leverage to the former employer in negotiating a positive result (and some revenue replacement) without the immediate need to bring an injunction action or establish "causation." In other words, corporate counsel should consider not only which tool to use, but whether liquidated damages or an injunction should be the pre-determined remedy. Too many agreements, unfortunately, only specify the company's "right," but fail to specify or thoroughly consider the company's most appropriate remedy in the event of a violation, or draft the specifics into the agreements.

Editor: Companies differ. How do you go about advising a company in developing the best toolkit for its particular circumstances?

Lasky: It is essential to have an understanding of the company and its business. That includes both the company's compensation and benefits programs, as well as the client or customer relationships that the company seeks to protect. It is also important to review very carefully the existing policies and practices of the company, including any employment manuals. The company's culture is very important as well: some may be heavy-handed and believe in the deterrent effect of a punitive approach to departing employees – threatening them with a lawsuit – while another company may be committed to appealing to their sense of honor. The matrix I referred to – and the advice that I give in putting it together – will depend on all of these factors.

Editor: What are some of the common problems that counsel should avoid?

Lasky: For starters, counsel should avoid the kind of sweeping restrictive covenant or non-compete arrangement that extends to all the world and goes on forever. The courts focus on reasonableness: what is reasonable to protect the legitimate business interests of the employer. If, for example, the departing employee has spent his time on five customers, the focus of the restriction should be limited to those customers, not every customer of the company.

A second common mistake is the notion that one size fits all. The departing senior executive is much more important in this context, and if all of the post-employment restrictions that are brought to bear at that level are also being utilized for departing middle management, there are going to be issues. The company should refine its goals here and develop a matrix for each category of employees.

Another common error concerns the value of time. In businesses that are heavily dependent on key customer relationships, it is usually important for the company to buy itself some time to bring in a replacement and familiarize him or her with the business and the customers.

The last common mistake concerns not paying sufficient attention to the remedy for a violation. This means drafting remedies into the documents – an employment agreement, an employment handbook, a code of conduct, or some other undertaking – that put a price tag on the violation, an objective quantification of what the violation means. This, too, is something that should be addressed.

Editor: You've been talking about the situation where the employee is leaving the employ of the client employer. What about an incoming employee – say, an extremely attractive candidate for employment – who has just left a competitor? How can the employer best protect itself where the candidate misleads the employer about his or her legal obligations to the former employer? Or, worse, is in possession of trade secrets or other confidential information of the former employer?

Lasky: The hiring intake process for incoming employees – particularly where the former employer is a competitor – is crucial. If the initial hiring and interview process is sound – if the due diligence on the candidate's obligations to the former employer has been fully reviewed by both the human resources professionals and by the legal department – the chances of something slipping through the cracks are remote. A good intake process leads to an informed decision on whether or not to offer employment.

Any contract of employment should require the acknowledgement, for example, that the newly hired employee has disclosed all obligations to the former employer and is not in possession of trade secrets or other confidential information of that employer. If, subsequently, those representations turn out to be untrue, immediate termination of employment could ensue. A good contract of employment should also provide for indemnification on the part of the employee where the employer is exposed to claims relating to any such misrepresentation.

Editor: Is there anything that you would like to add?

Lasky: It is extremely important for counsel to pay attention to how and when restrictions are implemented. This is often overlooked, and companies focus on what the agreement says, not on the surrounding circumstances. In many jurisdictions the likelihood of enforcement may depend, for example, on whether the post-employment restriction was in place *when* the executive accepted the position, as opposed to being implemented *after* he or she had signed on. If the restriction is being imposed in connection with an enhanced bonus or some new benefits program, attention should be paid to the ultimate standard of reasonableness that might have to be shown in court. The restriction must relate to the legitimate business needs of the company, and the process of implementation must be reasonable. Sufficient time must be allowed for the employee to seek legal advice, for example. Success in this area is very largely a matter of thoughtful communication and implementation.

Please email the interviewee at mlasky@dglaw.com with questions about this interview.