EMPLOYMENT CONTRACTS: BEST PRACTICES & COMMON MISTAKES

Ferraiuoli LLC
Looking Forward

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The Lawyers for Employers

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Katherine González-Valentín has over 20 years of experience as an employment law and litigation attorney and nationwide speaker representing companies and training management and professionals. She is a Capital Partner and Director of the Labor & Employment Department in **Ferraiuoli LLC,** former Chair of Litigation, and the first female partner to become member of the law firm's Executive Committee.

Katherine advises employers and their management team on legal aspects concerning employment relationships and human resources management and represents them in labor claims before different state and federal forums. Her experience goes beyond the local arena, as she represents companies in cases and with operations in the continental United States and works with international companies. She also handles litigation relating to the health insurance industry and Medicare. Katherine worked in two other top Puerto Rico law firms as an employment law attorney and was an Assistant U.S. Attorney in the Civil Division of the U.S. Attorney's Office in Puerto Rico, where she represented the United States and federal agencies in employment discrimination and other civil litigation before the U.S. District Court for the District of Puerto Rico.

In 2016 Katherine was recognized with the *Woman Who Leads*™ award and is listed as a leading employment law attorney in Puerto Rico by Chambers & Partners and Best Lawyers. She has evolved into a distinguished speaker on employment law topics and civil practice and has been invited to talk in forums in Puerto Rico, New York, Washington, D.C. and Rode Island, to name a few. Some of the topics she has covered include, for example, supervision and disciplinary practices, discrimination, retaliation, harassment, women in the law, workforce diversity and inclusion, leaves of absence, employment policies, internal investigations, privacy, social medial and technology in the workplace. A former Federal Bar Association (FBA) Puerto Rico Chapter President, Katherine also served in the Board of Directors of the FBA at the national level and is board member of various non-profit and employment-related associations in Puerto Rico including the Association for Labor Relations Professionals, Industrial Women Chapter and Fundación Dorada.

Corie is a Shareholder at Seaton, Peters & Revnew, P.A., based in Minneapolis, Minnesota. She is the past Chair of the FBA's Labor & Employment Section (2016/17), and has been a board member since 2013.

Corie represents, counsels, and defends employers in a full range of employment law issues and litigation. She has extensive knowledge of federal, state and local prevailing wage laws and ordinances, as well as other wage and hour laws. Corie works closely with management on matters such as accommodations, harassment investigations, discipline and termination issues. She also assists clients with non-compete agreements, contract review, negotiation of contracts, corporate governance, mergers and acquisitions and shareholder disputes. She is also a qualified neutral under Rule 114 of the Minnesota General Rules of Practice.

Agenda

- At-Will v. Just Case Employment Agreements
- Just Cause/For Cause Employment Agreements
- General Drafting Considerations
- Restrictive Covenants Drafting Considerations
- Arbitration Agreements & Clauses
- State Law Issues – Puerto Rico

At-Will v. Just Cause Employment Agreements

At-Will Employment: Defined

- Garden variety employment relationship
- At-will employment is a relationship in which an employer may discharge an employee for any reason or no reason, and the employee is under no obligation to stay on the job.
  - Some states have public policy exemptions
  - Some states have covenant of good faith exemption ("just cause")
  - Some states have implied contract exemption (handbooks, verbal assurances, etc.)

At-Will Employment Agreements

- "At Will" Does Not Equal No Employment Agreement
- Drafting Considerations:
  - Make sure you have the "at will employment" language in the agreement.
  - Consider using the title "Compensation Agreement" instead of "Employment Agreement"
  - Example:

At Will Relationship. The Company has retained Employee as an at-will employee and nothing in this Agreement shall be interpreted or construed to alter this status, or to confer upon the Employee any right with respect to continuance of employment by the Company for any specified duration or by any of its affiliates, nor interfere in any way with the right of the Company or of any such affiliate to terminate the Employee's employment at any time.

For or Just Cause Employment: Defined

- Employment that can only be terminated without any further employer obligations under a set of conditions specified in an employment agreement.
  - Common examples include:
    - Intentional wrongdoing
    - Fraudulent conduct
    - Theft
    - Failure to perform job responsibilities
    - Breach of company policies

For/Just Cause Employment: Best Practices

- Link termination to just/for cause section in employment agreement or employee handbook.
- Give the company wiggle room to terminate employee for bad acts not specifically listed in the section regarding for/just cause termination.
- Consider including a “catch all” provision.
- Important terms need to be clearly defined.
  - Willful
  - Gross X
  - Neglect

For or Just Cause Employment: Common Mistakes

- Failing to specifically include what constitutes for or just cause in the company's employment agreements.
- Failing to comply with discipline procedures in employment contracts.
  - Due process/ grievance procedures.
- Failing to provide a just cause for termination .

Employment Agreement Drafting Considerations

Employment Agreement Drafting Considerations

- Employee should sign before first day of employment (in Minnesota, they MUST sign before the first day to have restrictive covenants be valid).
- Include clause requiring that employee sign employment agreement and other agreements as a condition of employment.
  - "WHEREAS, an express condition of Employee's at-will employment with the Company, Employee agrees to the terms and conditions set forth in this Agreement, and Employee desires to do so; now, therefore:"
- It is not necessary to identify whether employee is considered an exempt or non-exempt employee.
- Include a duty to comply with obligations of former employers.

Employment Agreement Drafting Considerations

- Consider preparing new or modified agreement with a promotion or pay raise.
  - Business need to revise agreement?
  - Include new information?
  - Access to confidential information?
- If the company refers to benefits in the agreement, indicate that the plan documents control.
  - "All aspects of such benefits are controlled by their respective policies, plan documents and summary plan descriptions and nothing contained herein shall be construed to alter any fringe benefit plan or the foregoing documents, or waive any limitations, conditions or eligibility requirements contained therein."
- If the non-compete agreement is separate, attach it to the employment agreement.
  - Attach other documents referred to in the employment agreement if possible.
  - If required, attach draft severance agreements to the agreement.
  - Beall v. Edwards Lifesciences, LLC – District of Columbia

Employment Agreement Drafting Recommendations

- Wage confidentiality provisions - beware.
  - The NLRA which allows employees to discuss their salaries and prohibits employers from enforcing or imposing pay secrecy policies.
  - California Equal Pay Act – employers are prohibited from retaliating against employees who discuss their salaries.
- Ensure that wages earned in which the employee is entitled to in one year are not paid the next year.
  - Earned wages for one year must be paid by March 15 the following year.
  - If compensation is intended to be deferred compensation plan, comply with IRC 409A.

Employment Agreement Drafting Considerations

- Incentive compensation agreements - prospective amendment of terms
- Stock options or deferred compensation: include language such as “target” or “estimated.”
  - Employee may be eligible for commissions and/or bonuses as offered by the Company from time to time.
  - “The Company shall provide for a bonus for each calendar year during which this Agreement is in effect which will be targeted at twenty-five percent (25%) of the actual base salary received by Executive pursuant to the base salary section hereof in connection with achieving business plan financial objectives.”
- If a bonus is intended to be non-discretionary, state it clearly.
- Ultimately, use specific but modifiable language that allows for future changes in business conditions.
  - If the company states it shall do something, without any qualification or ability to modify, it might be stuck.
    - Use statements such as “initial compensation” of, “benefits generally,” “to the extent _____, the Company shall,” and other similar phrases.

Executive Employment Agreements: Defined

- Provisions to consider:
  - Compensation
  - Equity grants
  - Benefits
  - Term
  - Termination – for cause
  - Liability protection
  - Non-compete, non-solicitation, confidentiality, inventions provisions (VP R&D)
  - Dispute Resolution
  - Golden Parachute (money guaranteed upon merger or takeover)

Restrictive Covenants Drafting Considerations

Restrictive Agreement Drafting Considerations

- Include a clear assignability clause and avoid conflicting language.
  - "The Company may assign its rights and delegate its responsibility under this Agreement to any affiliated company or any corporation which acquires all or substantially all of the operating assets of the Company by merger, consolidation, dissolution, liquidation, combination, sale or transfer of assets or otherwise. Except as herein provided, the Parties may not assign any rights or obligations under this Agreement."

- Include a duty to disclose clause to future employers.
  - "Employee shall disclose and make available this Agreement to any employer, or potential employer, or other business in which Employee may hereafter render services, and shall keep the Company apprised of Employee's employment status for a period of twenty-four (24) months following the termination of this Agreement (and any severance payments made hereunder) or Employee's employment with the Company. The Company shall have the right to notify any potential employer of Employee of the existence of this Agreement."

No-Poach Agreements Among Competitors

- On April 3, 2018, the DOJ filed an antitrust complaint against Knorr-Bremse AG and Westinghouse Air Brake Technologies Corporation for agreeing not to, "solicit, recruit, hire without prior approval, or otherwise compete for employees."
- DOJ challenged the above "no-poach" agreement as a per se violation of Section 1 of the Sherman Act, which prohibits conduct that unreasonably retrain trade.
- On July 11, 2018, the parties entered into a final judgment, outlining the parties' agreement.
  - Defendants were enjoined from entering into or enforcing any No-Poach Agreement or provision, which was defined as "any Agreement, or part of an Agreement, among two or more employers that restrains any person from cold calling, soliciting, recruiting, hiring, or otherwise competing for (i) employees located in the United States being hired to work in the United States or outside the United States or (ii) any employee located outside the United States being hired to work in the United States."
  - Nothing in final judgment prohibited defendants from attempting to enter into or enforcing non-compete agreements.

Arbitration Agreements & Clauses

Class Action Waivers: Background of Epic v. Lewis

- Section Seven of NLRA provides that employees have the right to engage in "concerted activities," and employers cannot restrict or interfere with that right.
- FAA provides that, "a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction … shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."
- Accordingly, "courts must place arbitration agreements on an equal footing with other contracts and enforce them according to their terms," unless barred by a "generally applicable contract defense".

Class Action Waivers: Epic Systems v. Lewis

- The Supreme Court held the “law is clear”—arbitration agreements are interpreted as written because Congress, through the FAA, wanted the agreements enforced in that manner.
- The majority found that the Federal Arbitration Act "instructed federal courts to enforce arbitration agreements according to their terms" and that the NLRA "does not mention class or collection action procedures" and thus cannot be read to displace the Arbitration Act.
- “While Congress is of course always free to amend this judgment, we see nothing suggesting it did so in the NLRA—much less that it manifested a clear intention to displace the FAA.”
- The court reasoned that the NLRA “does not even hint at a wish to displace the [FAA]—let alone accomplish that much clearly and manifestly, as our precedents demand.”
- Employers currently facing class or collective actions in federal or state courts may be able to compel individual arbitrations if the employees previously entered into agreements waiving their rights to participate in class or collective actions.

Companies Dropping Arbitration Requirement

- In November, Google ended its policy of forcing its workers to settle sexual harassment claims through private arbitration.
  - The announcement followed a 20,000 staged walkout.
- Facebook quickly followed suit and ended its arbitration process for claims of sexual harassment.
- Uber, Lyft, and Airbnb also recently ended their arbitration requirements for these claims.
- Several large law firms have also followed suit after complaints from law clerks.
- These clauses continue to be enforceable in light of Epic Systems, but companies are not enforcing them under pressure for their employees.

State Law Issues – Puerto Rico

- Employment at Will vs. Puerto Rico Act No. 80 of 1976
  - Key Amendments to Act 80 by the Labor Transformation & Flexibility Act (LTFA) of 2017
- Employment Agreements Drafting & General Considerations
  - The Employee Handbook
  - Verbal or Written
  - Language & Interpretation
  - Probationary Period & Temporary Employment
  - Statute of Limitation
- Restrictive Covenants
- Arbitration Agreements

Employment at Will vs. PR Act No. 80

- Puerto Rico is not an employment at will jurisdiction
- Act No. 80 = the Unjust Dismissal Act regulates employment termination of any person hired for an indefinite period of time

Employment at Will vs. PR Act No. 80

- Employers must have **"just cause"** to terminate the employment of an employee hired for an indefinite period of time.

- If it is determined that there is **no just cause**, the employee is entitled to an indemnification or severance payment commonly known in Spanish as the ***"mesada"***.

- The payment of the *"mesada"* is the **exclusive remedy** available for an employee that alleges unjust termination.
  - EXCEPT if an employee establishes other causes of action (e.g. discrimination or retaliation, among others), this could entail other remedies, such as payment for damages (but not duplicative).

- Act No. 80 provides a formula for calculating the *"mesada"* based on the highest salary earned by the employee in the last 3 years and the amount of completed years worked for the employer.

Employment at Will vs. PR Act No. 80

- What constitutes **just cause** for termination under Act No. 80?
  - The statute does not provide an exhaustive list
  - It includes circumstances attributable to employers and employees that as a **general rule** constitute just cause

    - **Employees**:
      - The employee engages in a **pattern** of improper or disorderly conduct (**examples = new**);
      - The employee incurs in a **pattern** of deficient, inefficient, unsatisfactory, poor, tardy and/or negligent performance (**examples new and old**);
      - The employee **repeatedly** violates the reasonable rules and regulations set forth by the employer of which he/she has timely received a written copy;

      - **EXCEPTION:** GROSS MISCONDUCT – TERMINATION ON THE FIRST OFFENSE.

Employment at Will vs. PR Act No. 80

- What constitutes **just cause** for termination under Act No. 80?
  - **Employers**:
    - Total, temporary or partial closing of the operation of one establishment,
    - Technological or reorganizational changes, as well as those of the product's style, nature or services rendered to the public; and/or,
    - Reductions in employment that respond to a reduction in the volume of production, sales, or profits, anticipated or present at the time of the discharge OR with the purpose of increasing the competitivity or productivity of the establishment.

Employment at Will vs. PR Act No. 80

Termination of Employment - Severance Payment – "Mesada"

That was then	This is now
• Less than 5 years of service: 2-months' salary plus 1-week of pay for each full year of service. • 5 to 15 years of service: 3- months' salary plus 2-weeks' pay for each full year of service. • More than 15 years of service: 6-months' salary plus 3-week's pay for each full year of service.	◻ New employees ◻ After approval of automatic probationary period ◻ 3-months' salary plus 2-week's pay for each full year of service • Capped at 9-month salary ◻ N/A employees hired before Labor Reform

Employment at Will vs. PR Act No. 80

Unjust Dismissal Act

That was then	This is now
• 3-year statute of limitation for claims under Act 80	◻ 1-year statute of limitation for claims under Act 80 – <u>from termination of employment</u>.
• Severance payment cannot be waived and any agreement waving severance payment is null and void.	◻ Claims made before the effective date of the Act shall be subject to the 3-year statute of limitation. ◻ Severance payment can be settled for less than what is established by law.

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Employment Agreement Drafting Considerations

- The Employee Handbook – an employment agreement? Kodak case
- *LTFA Art. 2.4*: Employment agreements may be verbal or written unless special law provides otherwise
- No need for written agreement in general but
  - Think "EVIDENCE"
  - Some agreements still need to be executed in writing; e.g.,
    - Non-competition agreements
    - Some agreements with non-exempt employees

Employment Agreement Drafting Considerations

- Written - Agreements with non-exempt employees
  - To reduce the statutory meal period
  - To fragment the use of vacation leave
  - To use non-working days as part of the vacation period
  - To partially liquidate and pay accumulated and unused vacation leave in excess of 10 days
  - To accumulate vacation leave in excess of one year and up to two years
  - Voluntary agreements with non-exempt employees to establish alternate, weekly work schedules to fulfil a 40-hour week in no more than 10 consecutive working hours per day, without incurring daily overtime liability

Employment Agreement Drafting Considerations

Probationary Employment Period

Generally no need to have just cause as defined under Act No. 80

That was then

- 3 months probationary, could be extended to 6
- **Written**, signed before starting to work and delivered
- No grammatical errors in defining applicable period!

This is now

- **No longer written**
- Now is automatic
- 12-months for exempt employees (administrator, executive, professional)
- 9-months for non-exempt
- Applies to new hires on or after 1/26/2017
- **Practical considerations 2 year after implementation of LTFA**

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Employment Agreement Drafting Considerations

- *LTFA Art. 2.5 - Language*
  - It can be drafted in any language known by the employee
  - If the employee signs it a presumption is created that the employee knows the language in which the agreement is drafted

- Practical Consideration
  - For agreement in English include paragraph in Spanish where employee acknowledges he/she knows and understands English

Employment Agreement Drafting Considerations

- *LTFA Art. 2.6 – Documents & Electronic Signatures*
  - Electronic signatures and notices have the same legal effect
  - Electronic signatures and acknowledgments of receipt are allowed in every employment agreement and employment-related document
  - Notices required by law can be by electronic means but in a manner that they are effectively communicated to all employees
- Practical Considerations
  - Adopt and use electronic filing systems that are cost-effective and efficient. Your business may be subject to audits by the WHD, PR-DOL, SIF, ICE and quick access and production of documents is essential.
  - Keep evidence of publication and receipts.

Employment Agreements Drafting Considerations

- *LTFA Art. 2.12* Rules of Interpretation of Ambiguous Provisions
  - Pursuant to what the parties agreed upon
  - Legal provisions
  - Purpose of the relationship
  - Productivity
  - Nature of the employment relationship
  - Good faith, use and customs generally observed by the business …

Employment Agreements Drafting Considerations

- *LTFA Art. 2.12* Rules of Interpretation of Ambiguous Provisions
  - The same interpretation criteria applies to the employer's policies and rules
  - **RESERVE**: However, in cases where the employer reserves its right to interpret ambiguous provisions such reserve will be honored except
    - If it is capricious, arbitrary or a special law provides otherwise.

Employment Agreements General Considerations

LTFA Art. 4.14(d) Temporary Employment Agreements

- Increased clarity and flexibility for the use of temporary employment agreements so that employers are not exposed to severance payment liability under PR Unjust Dismissal Act for the continued or extended use of termed agreements
- Agreement with person who temporarily provides services or provides them for a term of specific duration
- Can be renewed but if the practice, circumstances and frequency of renewals creates an expectation of indefinite continuity the employment will be deemed without term and will require just cause for termination
- Temp agreement that does not exceed 3 years including renewals is presumed valid
- The duration of a temporary employment agreement with employee who qualify as exempt as administrators, executives and professionals will be regulated by the express intent of the parties to the agreement.

Employment Agreements General Considerations

Another Change Resulting from the LTFA

- Statute of Limitation Employment Agreements
  - 1 year from the moment in which the cause of action is actionable
    - Applies to causes of action resulting from an employment agreement or the benefits therein
    - Causes of action originating before the LTFA are subject to the statute of limitation previously applicable (15 years)

Restrictive Covenants

- Confidentiality
- Non-Solicitation of Employees
- Non-Compete

Restrictive Covenants

Non-Competition Agreements

- Must respond to the employer's legitimate interest, such as the protection of the business from the adverse effect of competition by a former employee
- Restrictions on the employee's future functions must be limited to activities similar to the activities the employee performed during his or her employment
- Duration cannot exceed one year after termination of employment
- Must specify geographical boundaries where the prohibition is to apply, limited to what is necessary to avoid competition. Alternatively, it should be limited to those customers the employee personally served for a reasonable period of time prior to the termination of employment or during a period immediately before termination, and who were still customers of the employer when the employee's employment ended
- Employee must receive adequate consideration
- Consent, object and cause

Arbitration Agreements

- Puerto Rico has a strong public policy favoring arbitration
- Disputes over discrimination and sexual harassment are excluded from arbitration. Medina Betancourt v. La Cruz Azul de P.R155 D.P.R. 735, 498 (2001); Vélez v. Serv. Legales de P.R. Inc., 144 D.P.R. 673, 684-685 (1998)
- If the employee, however, is given the option to choose between two forums (arbitration and court) to resolve his/her discrimination and/or harassment claims, then the clause would be valid. Quiñones v. Asociacion, 161 D.P.R. 668 (2004)

QUESTIONS?