Executive Employment Agreements

“What’s In Your Contract?”

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Executive Employment Agreements

• Who should receive an Executive Employment Agreement?
• Why are these agreements necessary?
• What are the benefits/risks of having these agreements?
• When is the “right” time to discuss the terms?
  – Which terms are most important to the organization?
Executive Employment Agreements

Who should have an agreement?

- Executive Director
- Chief Financial Officer
- General Manager/Head of Operations
- Head of Development
- Head of Sales and Marketing

Basically, an employment agreement should be offered to the person in any position that is critical to the operation of the organization. This could mean different positions at different organizations and, in some cases, might not extend beyond the Executive Director.
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Why Are These Agreements Necessary?

For the employer, executives can leave under their own steam or with a decisive push from above.

The latter can be tricky to engineer since there may be legal, business, financial and personal issues that can have significant consequences.

A departing executive can signal a public perception that the organization is unstable. If sudden, there could be disruption to the organization and to relationships. There may also be serious concerns about the departing executive’s remarks or actions following the departure.
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Why Are These Agreements Necessary?

For the employee, both the threat of an involuntary termination, and even the prospect of an unhappy voluntary one, may leave the executive vulnerable to significant financial losses. Potential scuttlebutt about a departure can harm an executive’s career or any potential reporting requirements may leave the executive wanting to minimize potential negative exposure.
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What are the Benefits/Risks of Having These Agreements?

For the employer, the premise of the employment relationship is the at-will doctrine. So why enter into an agreement?
The number one reason would be recruitment. A helpful recruiting tool is a workable agreement.

The Agreement gives the employer the ability to extract concessions such as a forum for resolution of disputes and can set in advance the parameters of its financial obligations to the executive, both during the contract term and once employment terminates.
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What are the Benefits/Risks of Having These Agreements?

For the executive, the agreement is critical. It avoids the implication of an at-will relationship and guarantees a specific term of employment, a guaranteed salary and a recitation of the grounds that either side can invoke to terminate the agreement.

The easiest way to protect a party’s interest when an executive departs is to think ahead when negotiating an employment contract. A well-drafted contract can limit the issues in dispute for both sides, minimize ambiguities, and put both parties on notice of their real obligations and their ability to enforce their rights.
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When is the “Right Time” to Discuss Terms

Recruiting the right candidate may mean learning what is important to the candidate and including an employment agreement that addresses key issues. When recruiting, a longer term may be preferable to a shorter one.

The agreement can contain an automatic renewal provision or notice regarding expiration and the opportunity for renegotiation.
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What Terms are Important?

The employer may not want to set a term of employment, there may be a preference for an indefinite term which is terminable with or without cause, but which if terminated without cause, provides the executive with a reasonable severance payment.

If the executive agrees to such an arrangement, the contract should also provide for the executive to invoke both not for cause and “good reason” grounds to resign, where the “good reason” resignation is coupled with severance.

It is important that the “good reason” provision is defined clearly.
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Terms to Include in Agreement – Title and Role

Title, Responsibilities and Reporting Relationship

If the organization wants to preserve its flexibility in designing, or changing, the executive’s role, it will seek language that will leave the responsibilities in the Board’s discretion, as long as they are commensurate with the position. Some employer-friendly language might be:

> During the employment period, Executive shall serve as the Chief Financial Officer of the organization, with the duties, authority and responsibilities commensurate with such position, and such other duties commensurate with the position as are assigned by the Board of Governors (the “Board”) from time to time.
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Terms to Include in Agreement – Compensation

Assuming the parties have agreed on a base salary, they still need to determine whether the contract will include built-in raises. Organizations will want to leave any raise to their discretion.

“Fringe” benefits are not fringe-like at all and are a valuable part of an executive’s compensation. Many executives will press for these to be specified in the agreement, because many employers prefer to simply state that the Executive “shall be entitled to the benefits the organization makes generally available from time to time to its employees occupying executive positions, in each case in accordance with the terms of those benefit plans.”
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Terms to Include in Agreement – Benefits

The executive will find it preferable to have the organization commit to the specific benefits to be provided, with employer and employee contributions noted:

Health Insurance, Life Insurance, short and long term disability insurance, 403(b) and financial plans, cafeteria plans, vacation and holidays, car allowance, payment of housing, relocation, tuition and tax preparation expenses.

While the organization will want to reserve the right to modify the benefit plans, the executive may press for language providing that the type and level of benefits specified will not be altered.
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The Most Critical Piece

The following section is really the most important piece of the employment agreement and provides the real reason for having agreements in place for your critical positions.
YOU ARE FIRED
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Terms to Include in Agreement – Terminations

The legal issue that presents the most likely ground for contention in any contract negotiation is how the contract can be terminated and what are the consequences of a termination.

*The employer* will want to maximize its discretion in terminating the executive’s employment, minimize the executive’s ability to terminate the contract, and minimize the payments it must make to the executive after a termination.

*The executive* will want to limit the employer’s discretion in a termination, broaden the ability to resign, and maximize the financial benefit if the contract is ended.
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From the *executive’s* perspective, the contract should not include a provision permitting the organization to terminate employment without cause, unless the organization commits to a substantial severance payment, lengthy notice and, if appropriate, continued vesting in any financial arrangements.

The *employer’s* counter argument is that a termination without cause is not necessarily one without fault. The employer may want to terminate “without cause” based on personal or business conflicts, underperformance or disagreements over business matters, either substantive or stylistic.
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Payments for not-for-cause Terminations

What should the payment be in a termination without cause?

The executive’s goal will be to get the full benefit of his bargain: payment of continued salary and benefits for the remainder of the contract term, and continued or accelerated vesting in financial plans.

The employer’s goal will be to incur the least financial consequences for a not-for-cause termination, but tempered by its desire to recruit the executive and not leave him feeling, as a new employee, that the employer is unreasonable or cavalier.
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Payments for not-for-cause Terminations

Typical contractual severance arrangements include payments of six to twelve months of salary and full benefits; payment of COBRA benefits for some period of time following the severance period and outplacement services.

This is where the organization must look to its financial picture and determine what the organization can bear.
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Payments for “Cause” Terminations

How the parties define “cause” may be the most critical drafting issue.

The *executive* will want “cause” to have a high threshold, so that it requires a far greater showing than dissatisfaction with performance. The executive will also want both notice and an opportunity to cure allegations before they entitle the employer to terminate the contract.

The *employer* will want to maximize its ability to find cause, will want to limit the types of breaches which are curable and will want to require the executive to rapidly cure them (*which may really mean no cure is possible.*)
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Terminations by the Executive for Good Reason

Most contracts contain a provision outlining the grounds on which the executive can resign “for Good Reason”.

A Good Reason provision will require the executive to give the employer written notice of the grounds constituting good reason, and give the employer an opportunity to cure them. The executive is normally required to provide notice within a stated time period after he becomes aware of the facts underlying a breach, to prevent the executive from silently accumulating Good Reasons as they snowball. If the organization cures the alleged breach, the Good Reason evaporates, and the executive cannot invoke it.
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Non-solicitation of employees, confidentiality, proprietary information and trade secrets

Volumes have been written on these topics and there is a lot of information available. Due to various laws and regulations around this topic, research will be needed and probably legal advice, when adding language to an agreement.

The executive will want to press for reasonable time limits. Most employers have a legitimate interest in not having a former employee poach other employees, it is likely that such provisions will be included in the agreement, although the scope is going to be a compromise.
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Non-disparagement

Employers normally include a non-disparagement provision, covering the contract term and “any time” in the future. The employee will normally seek mutuality, although many employers are only willing to agree, in a subsequent severance agreement, that specified individuals will not disparage the executive after termination.
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Remedies

The parties will have to choose between litigation or arbitration, although normally the contract reserves the employer’s right to litigate disputes concerning competition and confidentiality.

From the executive’s perspective, disputes over compensation and cause/not for cause termination are better suited to arbitration than claims of employment discrimination, which a plaintiff will normally want to be heard by a jury.
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Conclusion

The choices the parties make in structuring their employment agreement will be a huge factor if the sky does fall and the relationship falls apart.

*By thinking ahead during negotiations, both parties can maximize their advantages and maintain financial solvency even if the relationship founders.*