FOCUS ON: THE LAW

Avoiding the Big Employee–Employer Disputes

Taking measures to eliminate or correct unmet expectations in the employer-employee relationship saves time, money and a lot of headaches

All Austin-area companies—without regard to their size or industry—share a common thread. No companies are able to deliver value in their products or services without the efforts of their employees. When employers and their employees are all working toward the same goal, the chance of their joint success is high. But when the two begin heading in different directions, the results are not so pretty.

The disconnect

"In many companies, there is a disconnect between the company and its employees that can usually be prevented or at least corrected," says Greg Holloway, a mergers and acquisitions partner with the law firm of Thompson & Knight. "The downside of not finding and fixing employment related problems early is the time and money that it takes to resolve any disputes that may arise, not to mention the costs of replacing terminated or departed employees and the resulting inefficiency in the business itself."

So why does an M&A lawyer spend time thinking about employment lawsuits and employee disputes?

Holloway explains, "My clients buy and operate businesses, or work for those businesses, in order to fulfill a vision for the marketplace and to make money. Any employment issues that detract from the fulfillment of those goals is viewed by them as a negative, and rightfully so. When my clients ask me to help them with an employment problem, before I consider turning that problem over to our trial or employment department, I try to work with the client to understand more about what caused the problem in the first place. After all, any time and money not spent on the client's core business makes it more difficult for them to reach their goals.

"What I have found is that many employers and employees—across industries and geographic areas—tend to make, and repeat, the same mistakes. That causes huge frustrations for everyone involved. Employment disputes are not so much the result of poor hiring choices, as they are the consequence of unmet expectations on the part of the company and the employee. Each side may have their own idea of how the relationship should go and when those ideas diverge, problems arise."

Greg Holloway

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The surprise

Have you ever met with a friend who seemed upset at you, even though you had not seen them or spoken to them in the prior week? Most of us have had that experience, and it often leaves us puzzled. There can be much the same dilemma between employers and employees in the workplace as well.

Employees can become confused and worried when their supervisors do not take the time to give them formal and informal feedback. Or they can become increasingly agitated by an off-the-cuff statement that their supervisor made a few weeks ago. Employers can become dissatisfied when they perceive that an employee's job performance or attitude has, in their estimation, declined. In either case, one side or both may be looking to get out of the employment relationship. And all it takes is a trigger moment to ignite the termination.

"Management tends to allow employment problems to continue too long without giving the employee a good sense that, first, there is a performance issue and, second, the employee needs to take specific corrective action to get back on track," notes Holloway. "Instead, management will either let the situation reach a personal breaking point in which either the manager or the employee will become angry, or the manager will decide that without much, if any, prior written warning, an employee needs to be let go. In either case, the terminated employee may be not only hurt and confused, but surprised as well. The employee's surprise often leaves management personnel shaking their heads in amazement, but it's there."

Holloway continues, "After the initial hurt and surprise, the employee often finds an employment lawyer to help them review options. If the company didn't handle the termination properly—or sometimes even if it did—a demand letter, and sometimes a lawsuit, will soon be on its way."

Even if the employee is the one who decides to terminate the relationship, the company may not be off the hook. An employee, especially a management employee, can claim that he or she was constructively terminated because the company took away important duties or reporting lines. This time it's the company's turn to be surprised.

The beginning

Holloway contends that the heart of the problem is a series of unmet expectations on both sides of the table. He says that some of the blame can be traced to the beginning of the employment relationship. He believes that companies and employees alike can benefit by having the framework of an employment relationship set forth in an offer letter that makes it clear that the employee is being hired on an "at will" basis—that is, on a basis under which the employee is free to leave at any time and the company is free to terminate the employee at any time.

"The law recognizes that this at-will concept can be changed by the actions of the parties over the course of the relationship, but it's a good way to start things off," notes Holloway. "For those executives who receive employment contracts, the question for the company and the executive is 'How much should we change this at-will relationship to provide for a specific term of years or for severance payments in the event that employment is terminated without cause?' The danger areas are in setting contractual performance standards that no one could attain or, conversely, in making it virtually impossible to terminate an executive who is not doing his or her job."

The parties should also make it clear who owns the new ideas that will come from the employment relationship. When the employee begins work, companies should require the employee to sign a confidentiality agreement and, in some cases, an agreement that assigns to the company all patents, trade secrets, trademarks and copyrights developed by the employee during the course of employment.

"There can be carve-outs that give the employee some rights to an idea that he or she has previously been exploring or would like to pursue, but in general the agreement is designed to give the company comfort that it will own its intellectual property free of claims from its employees," says Holloway. "Most companies and employees recognize the need to keep confidential the information and trade secrets of the company."

In establishing personnel policies, many companies like to put together a detailed employee handbook that sets forth a myriad of rules and procedures.

"Some policies are a good idea, but companies should recognize that it is their departure from their own rules that will cause them problems in an employment dispute. Employees find it troubling when companies selectively enforce the rules against some but not all employees. It's better to keep the rules to a minimum and to enforce those rules uniformly," says Alan Marks, an employment attorney with Thompson & Knight. (For more on this subject, please see page 40.)

Companies should likewise avoid establishing job descriptions that are so specific that they do not allow management to adjust personnel responsibilities from time to time, says Holloway. At the same time, employees need to have performance standards—some of which are objective and some of which are subjective—that they are expected to meet.

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Frank Hill

The review

In the ideal world, management would give feedback (with constructive criticism as well as praise) to employees as projects are completed. Whether or not this periodic feedback is given, companies should give their employees meaningful reviews at least once per year. The purpose of the reviews is to 1. Give positive reinforcement to successful employees; 2. Give constructive criticism to employees who are in the early stages of not meeting performance standards; and 3. Give longer-term underperformers notice that they must take specific remedial action or face the possibility of termination.

"The review process is where many companies fall short," states Holloway. "Larger companies often manage this process very well, although they might not do as well in reviewing their own executive management. Middle-sized and smaller companies frequently lack a good formalized process, and for understandable reasons. Reviews take management time away from day-to-day operations, and, let's face it, no one likes to deliver bad news to their personnel. So, if there is a review, it probably glosses over the bad news and leaves the employee believing that everything is okay. Any termination of employment then becomes the surprise event that we discussed earlier.

"It's fair to the company and to the employee to tell them that they are not meeting expectations," continues Holloway. "In the meeting, tell them where they are falling short of their performance standards. Give them a specific time, with specific goals, to reach the required standards. During or after the meeting, reinforce the time and goals with them in writing. Follow up after the allotted time to see how they performed. Better yet, meet with them during their performance time to address their interim progress or failure. At worst, the employee will have a much better idea of why he or she is being terminated. At best, the company will have helped an employee get back on track. I'm no expert on employee morale, but I would think this sort of open process would be beneficial around the office in general, as long as the reviews are done properly and in good faith."

Frank Hill, a trial partner with Thompson & Knight who has handled numerous employment disputes, agrees, "I've seen many expensive lawsuits brought as an emotional reaction to rudeness. A combination of courtesy, fairness and honesty will prevent most of them. An employer should treat employees with respect and honesty. The good, the

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bad and the ugly should be documented. An employer can't gloss over an employee's faults in work performance evaluations and then expect to convince either the employee, or a jury, that the employee was a failure."

Holloway stresses that a well thought-out review procedure is a good idea not only because it is fair, but because it can help in the defense of many employment claims by disgruntled, terminated employees. "The company often needs to show that the termination decision, if particular to that employee, was based on performance of the employee and not other unrelated factors," he says.

The dispute

Of course, not all disputes or lawsuits will be avoided by even the most careful contracting and review process. So, what should a company do when it is faced with a lawsuit, a claim in arbitration or an administrative claim? Above all, be professional.

The dispute is part of your business, whether you like it or not. If your review and termination process were done properly, the truth will be on your side.

"Unfortunately, the truth can get distorted by careless communications made by either the employer or employee," notes Hill. "A few angry words contained in an e-mail can forever poison a jury's view of either party. Do you want your case decided based upon a single unprofessional comment? On the other hand, communications that are straightforward and factual lend credibility to the speaker. Never send an e-mail when angry or emotional. Try to follow the '30 minute rule.' Wait at least 30 minutes after composing an important e-mail and then re-read it to make sure that it is 100 percent professional."

It is very important to deal with asserted claims as early as possible, say Holloway. Many states, including Texas, allow for the employee to receive reimbursement of their attorneys' fees in some employment actions. Some states, again including Texas, can impose penalties on an employer's failure to pay wages properly earned. It is not uncommon to have a relatively small claim rise to a significant dollar amount due to the effect of attorneys' fees (for the company and the employee) and penalties.

The success

"We hear companies tell us frequently that it's their people who make the difference as to whether their company succeeds or fails," relates Holloway. "So why shouldn't they do everything they can to build value in the employment relationship?"

The Top Ten "Do and Don't" List for Companies – With Existing Employees

1. DON'T give employees a job description that is overly detailed and inflexible. DO give them general guidelines that allow for management flexibility.

2. DO provide useful feedback on projects. **DO give positive reinforcement as well as constructive criticism**, as warranted.

3. DO provide periodic and formal performance reviews. If praise is warranted, give it. If corrective action is needed, give specifics. DON'T mistake bluntness and rudeness for honesty in the reviews, however.

4. DON'T criticize the person themselves; focus on job performance. Keep the meetings on a professional level.

5. DON'T meet alone with employees for formal reviews. Always have at least one other member of the management team present in each review.

6. If an employee's job performance has fallen below acceptable levels, **DO provide the specific corrective plan in writing to the employee**. Give the employee a reasonable amount of time (with a specific deadline) to complete the corrective plan.

7. DON'T let your anger play a role in the termination of an employee. Try to bounce the facts and circumstances off another member of management before taking any action.

8. DO handle terminations in a professional, discrete manner. Have another member of management present, and try to meet with the employee at times when others are less likely to be present, such as lunchtime or the end of the day. Have security available in extreme cases.

9. DO ask terminated employees at the time of the exit interview **to sign a statement that they are returning all confidential information in their possession or control**. Ideally, this requirement will have been included in an offer letter or other agreement signed previously by the employee.

10. DON'T discuss the nature of the termination with other non-management personnel. DON'T give out information to other prospective employers, other than the date of an employee's employment at your company.

The Top Ten "Do and Don't" List for Companies – With Prospective and New Employees

1. When hiring new employees, DO have them acknowledge in the offer letter that they are "employees at will," meaning that they can volunteer to leave the company's employ at any time and they can be asked to leave the company's employ at any time, with or without notice and with or without any reason. The employees that you would want to stay for a few weeks after giving or receiving notice of termination will probably be willing to stay for an extra couple of weeks, whether or not you have a mandatory two week notice policy.

2. DO require all employees to sign a confidentiality agreement and, if the employee will be involved in any way in your company's intellectual property (such as patents, trademarks, trade secrets, copyrights or the like) or if you are primarily a technology company, require all employees to **sign an assignment of inventions agreement** on the first day of their employment as a condition to their employment. Make sure you know what you own, and protect it well.

3. DON'T assume that every employee will be bound by a non-compete agreement with your company. Texas law (and the laws of other states) tend not to favor the enforcement against employees of non-competition agreements and clauses. The enforcement of these agreements and clauses is very fact-specific. Protect yourself primarily with enforcement of the confidentiality and invention assignment agreement. And pay attention to number 5 on this list.

4. DO require that all new employees represent in writing to you on (or preferably prior to) the first day of their employment **that they will not be subject to or violating any non-compete, confidentiality or assignment of invention agreements with a former employer** in the course of fulfilling their job duties to you. If the prospective employee is subject to such an agreement, ask them for a copy—and then read it! If you forget to take this step, you might very well receive a "nastygram" from another company. At least, it will be a distraction and annoyance. At worst, it will cost you the loss of some of your technology (if the other company can prove it is theirs) and your time and money.

5. DO require that prospective employees disclose to you whether they are subject to any non-solicitation agreements with a prior employer. Non-solicitation agreements can cover the solicitation of prior co-workers as well as prior customers. The courts tend to enforce these agreements more frequently than non-competition agreements (again, based on the specific facts), so pay attention to these agreements before you hire someone.

6. DO carefully draft and review any employee policy handbook before providing it to a new employee. Companies commonly include in the policy handbook a series of detailed rules that they may not in fact follow. Companies typically forget to provide flexibility for the varied situations that arise in the employment relationship.

7. When quoting salary levels to new and prospective employees, **DO provide the amounts that they will receive per paycheck (normally twice a month)** and then say "which, if annualized, would be $__________". Don't give someone only an annual salary figure and perhaps the argument that they had an expectancy of being hired for at least a year. Make sure that you are clear that the employee's salary will be reduced by withholding of all applicable payroll taxes.

8. DO make sure that the employee signs an agreement allowing you to set off against future paychecks (such as their last paycheck) **the amount of any unpaid loans and advances to them**. This could be an item that is included in their offer letter (which you should ask them to sign).

9. Especially if you are a new company, **DON'T offer a new employee a high salary if you believe that there is a good chance that you will not have sufficient funds to pay the salary amount**. You might consider paying minimum wage, with the possibility of significant stock and/or cash bonuses based on the performance of the company and the employee. State employment laws can make it difficult to substitute stock for wages after the work has already been performed.

10. DON'T enter into employment agreements with employees that have both extremely "high thresholds for a cause termination and significant severance payments." High "cause" thresholds can make an uncomfortable situation linger, for both parties.

Alan Marks

OFTEN THE FIRST LINE OF DEFENSE

EMPLOYEE HANDBOOKS & WRITTEN POLICIES AND PROCEDURES

The most recent statistics reveal approximately 20 percent of all lawsuits filed in federal court concern labor and employment-related issues. Is it time for you, as an employer, to conduct a review of the legal systems you have in place?

The legal review should encompass a thorough review of how you handle employment matters, including practices before the employment relationship begins, during its existence, and after its termination.

According to Alan Marks, the following are a few questions you need to ask yourself and take action on NOW:

- Do I have formal job application and hiring forms? Are inappropriate inquiries made regarding race, gender, nationality, religion and other personal matters unrelated to job performance?
- Do I have an employee handbook? Has it been updated lately to reflect the most current law?
- Does the handbook contain appropriate disclaimers that preserve managerial discretion and guard against the handbook being interpreted as a binding contract?
- Do I have current and enforceable policies and procedures concerning drug and alcohol testing, absenteeism, leave of absence, Americans With Disabilities Act, the Texas Workers Compensation Act and the Family Medical Leave Act?
- Have all employees acknowledged in writing receipt of the handbook and policies and procedures?
- Am I in compliance with all state and federal posting requirements?
- Do my payroll and timekeeping practices comply with state and federal law?

"Your employment liabilities start when you hire your first employee," says Marks. "Every organization involving people has to have terms of employment and rules to govern employee as well as employer conduct if it is going to survive. It's appropriate for companies of all sizes to have an employee handbook and/or written policies and procedures."

Marks added that, "Even though your organization is small, a handbook or written policies, at a minimum in the form of formal memos on company letterhead, can provide a useful way of communicating the organization's philosophy, expectations and policies to workers and establishing procedures for supervisors to follow in dealing with employee grievances and other matters."

Marks notes that a wide variety of subjects can be covered in an employee handbook. Some of the most commonly covered are: at-will employment, pay procedures, benefits (including any paid vacation, sick leave, and holidays, and other forms of leave), meal and rest breaks, personal conduct (work rules), attendance and punctuality, sexual and other forms of harassment, equal employment opportunity, disciplinary procedures and termination. In addition, many employers include policies on performance appraisals, smoking, safety procedures, appropriate dress and appearance, use of communications systems (including the proper use of telephones, computers, e-mail, and Internet access), and drug and alcohol use.

Employers can use their employee handbook to outline their commitment to equal employment opportunity and intolerance of sexual harassment. Employers who maintain a handbook that reflects their current policies and is consistent with the most recent employment laws can be confident that they are following necessary legal mandates and fostering a fair and equitable work environment.

Marks stresses that, "Cases decided in the last several years have shifted the landscape for employment lawsuits, and employee handbooks and internal policies and procedures are often an employer's first line of defense."

He points out that clearly written policies that are regularly re-viewed can be both an effective employee relations tool and a good defense against employee lawsuits. In contrast, policies that are poorly drafted or applied can have exactly the opposite effect. They can lower morale and become evidence against a company in court.

"One of the best ways for employers to avoid liability is to strictly adhere to the policies and procedures set forth in the company's employee handbook while creating and maintaining a safe environment for all employees," says Marks.

WATCH THE CLOCK!

Greg Holloway and Zack Aspegren

"Deadlines in filing employment claims at the federal and state levels are important," says Frank Hill. "Both employees and employers need to determine what deadlines will be applicable to them for not only filing their lawsuit or arbitration claim, but for securing the possibility of seeking certain remedies specified under the law. A missed deadline can absolutely cost you money."

Greg Holloway notes that time is also a critical factor in early discussions regarding employment claims. "An employment claim is unlike many other commercial claims. An employment claim often carries with it a large measure of emotion, on both sides of the table. If an employer receives demands from a highly compensated employee in connection with that employee's departure from the company, speed and care in the response are critical to the company's ability to address the demands effectively."

Holloway notes that, as success-driven individuals, departing executives are often hurt by the departure itself. Any slowness by the company in its response to the executive's claims may be perceived by the executive as an indicator that the executive's efforts were never fully valued in the first place, even though the company may not have that in mind. If given too much time to stew over the situation, the executive may seek employment counsel (if they have not already done so) and may, with or without counsel, revise upwards their demands on the company. "The moral for companies," says Holloway, "is to act thoughtfully, rather than rashly, but be communicative!"