



Compensation of Employees for Service Inventions: **View from the Trenches**

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Outline of Presentation



*Balancing reasonable
and fair compensation
for employees with the
need for clarity and
certainty*

Real World Concerns

- Start-Ups and Other Hi Tech Companies
- Acquisition of Israeli Companies
- R&D Centers for Global Technology

Possible Solutions

- Government/Institutional
- Company-Initiated
- Economic Schemes

The Problem

Employees deserve reasonable and fair consideration for service inventions

"Doing Business" in the real world requires clear rules and predictability

Uncertainty can deter productive economic activity, reduce the value of Israeli companies

A proper balance needs to be reached



Start-Ups and Other Hi Tech Companies

Typically (but not always) R&D employees are well paid

Typically (but not always) R&D employees receive options which allows them to share in the “upside” of the value of the company

Typically, R&D employees are employed for the express purpose of developing products and with an expectation of developing new IP



Start-Ups and Other High Tech Companies

- Good practice: All employees (or just those doing R&D work) sign a Proprietary Information Assignment Agreement ("PIAA")
assigning all IP rights to the employer
- Following Actelis, a well-drafted PIAA also contains *an express waiver of the right to royalties or other compensation* under Section 134 of the Patent Law
- Uncertainty after Beyer: will or will not the well-drafted PIAA be enforceable?
 - Compensation Committee proceedings generally unpublished; no right of appeal
 - Minimal precedent available; most cases settle
 - Increase in employee claims already significant

If PIAA Not Enforceable:

- The employing company is exposed to future compensation claims
- No available guidance regarding time limits for bringing claims
 - From when does the statute of limitations run?
 - Can claims be brought after the employee has left the company?
- No available guidance on whether there is any monetary limit on size or type of claim
 - Fixed payment? Size of payment? Factors taken into account?
 - Royalty?
 - No one knows the value of the IP when it is first invented
- No available guidance on who can bring a claim
 - Only employees on whose name a patent is registered?
 - Any employee who was involved in the development of any kinds of valuable intellectual property?
- Bottom line: Uncertainty!!!!

Acquisition of Israeli Companies

Many Israeli companies are acquired primarily for their IP assets

Buyers want to know that the company holds its IP free and clear of third party claims, including claims from present or past employees

This is a fundamental aspect of all technology acquisition agreements: Company provides a representation that the IP is free and clear

As a result of the Beyer uncertainty, a company will never know if its IP is free of employee claims

Acquisitions: Methods for Dealing with Possible Claims Against the Target's IP

- Scenario: What if employee claims are brought after the company is acquired? The Buyer seeks compensation for the claim.
- Indemnification from Selling Shareholders
 - Direct indemnification usually impractical
 - Selling shareholders (which can include employees) also want certainty
- Escrows
 - Limited in amount
 - Limited in time after the closing
- Problem: How much is enough? How long is enough? How many employees can claim the same patent or invention?
- One major Tech Buyer already told us: no more deals in Israel

R&D Centers

Israel has encouraged global tech companies (IBM, Microsoft, Google, Oracle, Intel) to set up R&D Centers in Israel

- The global tech companies provide funding and direction
- These are the biggest tech employers in Israel

Underlying assumptions until now:

- All IP is owned by the employer (R&D Center)
- R&D Center assigns all IP to global tech company
- Therefore, global tech company owns the IP it financed

Now: R&D Centers may be exposed to employee claims

- R&D Centers may leave Israel for other competitive locations

Possible Solutions

Government / Institutional

Company - Initiated

Economic Schemes



Government/Institutional

Legislation

Regulatory action

Statement of Intent ('no action letter') by the Compensation Committee

Procedural Review for greater certainty and consistency

BUT: time is of the essence; the hi tech industry requires guidance and fast

Company-Initiated Solutions

Clarify that it is expected that R&D employees will create IP as part of their job

Clarify that options are granted as compensation for development of IP

Clarify that a portion of salary is compensation for development of IP

Acknowledge that payment on exit is compensation for service inventions

Easily implemented BUT no one knows if any of the above will be respected by the Compensation Committee

Economic Schemes

Pay a one-time bonus for each patent

- To achieve certainty, amount must be fixed in advance
- In some European countries, €2,000 to €4,000

Create an "IP Compensation Fund"

- Employer contributes a percentage of revenues or profits
- Employees receive compensation based on formula taking into account their contribution to IP development

May be premature, and no one knows if any of the above will be respected by the Compensation Committee

- In some jurisdictions, compensation must be determined after the invention is created

Procedural Rules for Greater Certainty

Limit the time for bringing claims for compensation

- Right now, statute of limitation appears to be only limit
- Within X months of registering the patent?
- Within Y months of an M&A or other “change of control event”?
- By the end of the fiscal year in which the inventing takes place?

Limit the maximum recovery per patent or per invention

- Would allow potential purchasers to assess risk
- Would allow escrow to be effective

Conclusion



- Uncertainty hurts companies, employees and has an overall adverse impact on the Israeli economy
- Other jurisdictions have found solutions; we must do the same, and fast
- Goal: reward employee creativity while encouraging Israeli businesses and maintaining a predictable business-friendly environment for foreign investment