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9B17M014

sunitha nath boutiques: Intellectual Property Rights (B)

Nithyananda KV wrote this case solely to provide material for class discussion. The author does not intend to illustrate either effective or ineffective handling of a managerial situation. The author may have disguised certain names and other identifying information to protect confidentiality.

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In early December 2015, Sunitha Somanath (Sunitha),[[1]](#footnote-1) the founder and chief executive officer of Sunitha Nath Fashions & Boutiques Pvt. Ltd. (SNB), was co-operating with her lawyer, Rajashri Menon, taking measures to be implemented at SNB to mitigate losses from an incident that had occurred in her company ranks. Sunitha’s most trusted employee and studio manager at SNB, Raghuveer Urs (Raghu), had quit SNB without notice. Further, it appeared that Raghu had stolen money from SNB, taken away one of SNB’s important clients, and started a business that competed directly with SNB.

Sunitha and Rajashri considered what measures needed to be implemented at SNB to contain any further damage and to preserve Sunitha’s relationships with her clients and vendors. They needed to review Raghu’s employment contract and determine what, if anything, Sunitha might do to prevent Raghu from using SNB’s resources—knowledge, processes, designs, clients, and employees—in his new business.

EMPLOYMENT CONTRACT WITH RAGHU

Rajashri directed Sunitha to retrieve Raghu’s employment contract. Sunitha provided Rajashri with what she had, but cautioned Rajashri:

Currently, Raghu was working as the studio manager, in charge of all of SNB’s offices. At the time of promoting him to studio manager a couple of months back, we did not sign a new employment contract. It was just an oral understanding, based purely on the need for managing the SSP movie project. But we had signed an employment contract when he was appointed as the assistant fashion designer.

Rajashri was surprised that her friend—a very careful and clever designer—had overlooked a business responsibility, but Sunitha explained:

We did not have time to document all the responsibilities of the new role. We were planning to get it done once the movie project was complete. Before we got there, he put me through this.

Rajashri read what Sunitha *did* have: a two-page document that provided the job description for Raghu’s position as assistant fashion designer (see Exhibit 1) and an older, single-page document that Raghu had signed when he was appointed trainee fashion designer (see Exhibit 2). Neither document included the legal aspects Rajashri was looking for in an appointment letter.

Sunitha explained that the documents were drafted by the office manager, who had some legal training. She had requested something simple to document the roles and responsibilities, with a mention of the compensation package. She also wanted some flexibility so she could modify Raghu’s roles and responsibilities as needs evolved. Hence, Sunitha asked the office manager to keep the agreement “open” and expected Raghu to execute what was delegated to him as SNB became busier and busier. When asked, Sunitha confirmed that most of SNB’s employees had signed similar employment contracts.

Rajashri explained to Sunitha:

An agreement or contract between two parties (in your case, between SNB and your employees) is a document that would be signed by both parties and would be referred to and reviewed only in extraordinary circumstances such as during a performance review, salary revision, or dispute between parties. An agreement should be as comprehensive as possible, documenting all possible scenarios that the employer and employee could reasonably encounter. The document should also prescribe the remedies available in case of a breach of contract. In a good employment contract, drafted effectively, all of your requirements could have been taken care of while still providing the flexibility necessary to have Raghu execute the work you assigned him.

To safeguard the interests of the employer, the employment contract should also contain provisions preventing employees from joining competitors or starting a competing business when they leave your employment. Such provisions are called non-compete clauses. Your employment contract does not have any such provision.

An employment contract should also contain a confidentiality clause, which is also known as a non-disclosure agreement. Such a clause would prevent an employee from sharing any confidential information the employee encounters during employment. This helps to keep sensitive business information confidential within the organization. Your employment contract does not contain this provision either.

Sunitha was surprised to hear that she might need to protect confidential information:

But we don’t have any confidential information at SNB. Everything that we do is available for public scrutiny. We are leading fashion designers in the industry, and all the information about what we do, how we do it, who we do it with, and so on, is transparent. So what is there to hide?

Rajashri explained that while much of SNB’s information might be available for public scrutiny, Sunitha would be maintaining some information as confidential, even from her employees. Rajashri directed Sunitha to think about the information that she would not want her competitors to know. That could be the information that would provide SNB with competitive advantage in the market. Such information should be maintained as confidential within SNB. Rajashri advised Sunitha that any information that met two key requirements could be considered confidential information: (1) the information was not openly available, easily accessible, openly discussed and shared, or easily ascertainable; and (2) the information provided a competitive advantage to SNB.

Sunitha acknowledged that she did maintain some information as confidential and did not share it with everyone in the firm. But Raghu, in his position as studio manager, had Sunitha’s complete trust. He had access to all such data at SNB so he could manage SNB’s offices in Sunitha’s absence.

Rajashri stated that non-compete and non-disclosure clauses might have helped Sunitha in this situation:

For a design firm like yours, apart from creativity, which is individual in nature, information is a very crucial component. The information provides its holder with needed agility and uniqueness. These are the qualities that provide you with recognition and competitive advantage in the industry. You needed to give Raghu access to the information so he could do his job, but you needed to restrict Raghu’s use of the information to SNB’s business. Now he has started operating in the same space as you have been operating, and he has also taken business away from you by underbidding in a project that you were executing. Also, he has started a business that is directly competing with SNB, all of which is possible because the employment contract you have with him did not have non-compete and non-disclosure clauses.

Sunitha nodded in agreement. “I now realize my mistake in executing a very simple employment contract,” she acknowledged. Rajashri interjected, “That’s not quite all. The employment agreement doesn’t have a non-solicitation clause, either.” She elaborated:

A non-solicitation clause is also called a no-raider clause. Let me explain. You know that Raghu has already started a business, which competes directly with your activities. He needs some employees who are good at their job and who also have relevant experience in the field. Let’s assume he finds that some of his ex-colleagues here at SNB could be persuaded to join him. Because he is aware of the details of the compensation paid at SNB, he would top that salary and poach your employees, crippling your business. Not only that, he could also take away your customers and your vendors. He would be soliciting your employees, vendors, and customers to join his business by terminating their relationships with you. If there were a non-solicitation clause in his employment contract, then he would not be in a position to do such a thing.

Rajashri added that, legally, Sunitha could not take action against Raghu based on the employment contract he had signed with SNB. Based on their current contracts, Sunitha could not prevent employees from joining Raghu’s business. However, there were other ways they could prevent Raghu from poaching SNB’s clients, customers, and vendors. One approach would be to update the employment agreements Sunitha had with her remaining employees.

Rajashri explained that non-disclosure, non-compete, and non-solicitation clauses, collectively called restrictive covenants in an employment contract, tried to achieve different objectives; hence, they could not be captured with a single clause in an employment contract. Sunitha would need multiple clauses for her employment agreements. Rajashri offered to have her staff prepare a format for the clauses.

Rajashri also cautioned Sunitha not to expect permanent prohibition from such restrictive covenants. She continued, stating that if the courts found that the restrictive covenants prevented an employee from using his or her knowledge, skill, and experience to secure profitable employment (primarily, the fundamental right to carry on business, trade, and profession, which was guaranteed by the Constitution of India), then the courts could set aside such restrictive covenants. Rajashri gave an example of a recent case decided by the Delhi High Court.[[2]](#footnote-2)

Before departing, Rajashri reminded Sunitha to take care of the mitigating measures they had previously discussed. Rajashri was keen to have Sunitha quickly address some of the important needs:

Raghu had access to everything in the office, including the keys, the passwords, and so on. Now that we have evidence that he has stolen money belonging to SNB for his office interior work, we don’t know what else he would do. So, as a precautionary measure, I suggest that you change the passwords and access codes to the computers in the office. Also, get his email address deactivated immediately so that he doesn’t misuse it. Similarly, get the office locks changed, as he might have had copies of the keys made before leaving. Get these [things] done as soon as possible.

Rajashri set an appointment with Sunitha for later the same day at 5 p.m. She asked Sunitha to gather as much information as she could about the interior design work Raghu had commissioned so they could consider that matter when they met later. She also reminded Sunitha to speak to her clients and vendors to ensure their accounts were in order and to determine whether Rajashri had contacted them. Sunitha thanked Rajashri for her assistance and promised to be at her office later in the day with her research.

EPILOGUE

After Rajashri left, Sunitha reflected on the events that had transpired during the day. She had lost her most trusted employee when he quit SNB without informing her. The employee had started his own firm competing directly with SNB and had taken one of SNB’s key clients with him. He had also been interacting with SNB’s vendors and customers, encouraging them to join his competing business. And before leaving, the employee had arranged for his office interior to be completed and the work paid through SNB’s accounts—a theft of ₹400,000 (about US$6,000).[[3]](#footnote-3) The silver lining to this incident was that she had also learned how *not* to structure an employment contract and the importance of including non-disclosure, non-compete, and non-solicitation clauses in employment contracts.

Sunitha recalled what Rajashri identified as the two key requirements of confidential information: (1) the information is not openly available, easily accessible, openly discussed and shared, or easily ascertainable; and (2) the information provides a competitive advantage to SNB. Sunitha wondered what kinds of information, available in a fashion-designing firm like SNB, would meet the requirements of confidentiality. She was also wondering what she needed to do to protect such information.

Given that she did not have a strong employment contract with Raghu, and the contract she did have did not contain a non-solicitation clause, Sunitha wondered what preventive measures she should adopt to prevent her existing employees from leaving her. Specifically, she was wanted to prevent Raghu from poaching her existing employees. Rajashri had also reminded Sunitha that some restrictive covenants in employment agreements would not be enforced by the courts if they infringed on the constitutional right of freedom of an employee to carry on business, trade, and profession. Sunitha made a mental note to ask Rajashri how to include restrictive covenants that the courts would uphold, thereby effectively preventing similar incidents from happening again at SNB.

Sunitha had much to review and clarify with Rajashri during their meeting in the evening.

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EXHIBIT 1: EXTRACT From THE EMPLOYMENT AGREEMENT Appointing Raghuveer Urs as ASSISTANT FASHION DESIGNER

Dear Mr. Raghuveer,

Based on your performance during your work at Sunitha Nath Boutiques (SNB) as a trainee fashion designer with us from December 2011 to November 2012, we are happy to hereby offer to promote you to assistant fashion designer at SNB upon the terms and conditions listed below.

In addition to your existing role as trainee fashion designer, you are expected to fulfill the following roles and responsibilities:

1. Analyse trends in the fashion industry and predict the future of fashion apparel and accessories for men, women, and children;
2. Design custom apparel for clients, based on the orders approved by the supervisor;
3. Compare different fabrics and integrate them into your designs as well as get them ready in the design outputs;
4. Prepare sketches, both rough and detailed, of apparel and accessories, and prepare written specification sheets describing factors like colour schemes, construction, measurement, embellishments, and textile, along with samples of materials to be used;
5. Co-ordinate with fabric suppliers and other vendors to ensure that all the material required to construct an apparel is available with the tailor to stitch the apparel;
6. Prepare layouts and marks and cut the fabric based on the pattern and designs finalized with the clients, for apparel and accessories for men, women, and children;
7. Advise workers, including tailors, about sewing the garment together on procedures like type of stitching, positioning of collars, sleeves on garments, and also getting the errors rectified, if any;
8. Coordinate with tailors and other workers to achieve the desired apparel within the stipulated time limit and within the budget;
9. Create illustrations for magazines, brochures, pamphlets, and other branding material of SNB, utilizing the designs, paints, and other photographs approved by the supervisor;
10. Review market and product/service trends and also predict market trends for different product/service categories, and prepare a monthly report that could be used in the organization as a handbook for marketing relating activities;
11. Negotiate and finalize assignments from customers and supervisors;
12. Prepare the marketing plan for the clients based on the preferences of the target market and the target product/service;
13. Negotiate and discuss with clients and the supervisor the finalization or desired changes to the designs and also the marketing plan;
14. Coordinate with the technical merchandising consultant to finalize the designs;
15. Coordinate with the clients regarding the finalization and acceptance of fabrics, designs, accessories, models, location, plot, theme, and its representation;
16. Coordinate with various parties like models, photographers, designers, printers, and tailors, to produce a desired marketing collateral for the client;
17. Render drawings of apparel and/or accessories and other complementary articles using various art forms, for the branding activities of the clients’ products/services;
18. Instruct clients’ publicity departments about the strategy to be adopted;
19. Prepare designs and graphic material for use as embellishment, illustration, advertising, or cosmetics on promotional material for the clients, as part of the product promotions, public relations, advertising activities, or branding exercise;
20. Create and promote new fashion designs and art;
21. Negotiate and contract with models, musicians, caterers, and other service providers to manage staging of shows;
22. Co-ordinate the fashion promotional activities, such as fashion shows, trade exhibitions, manufacturers’ displays, merchandisers’ conventions, among others;

EXHIBIT 1 (continued)

1. Coordinate with merchandisers, manufacturers, suppliers, and customers in gaining advice regarding type of fashions that would be purchased for a particular fashion season and prepare a report thereon; and,
2. Execute any other tasks delegated to you by your supervisor.

Your primary location of work would be #1201–1202, 12th Floor, UB City, Bengaluru. You would be reporting to Mr. Saravanan, Office Manager, for administrative purposes and to Ms. Sunitha Somanath, chief executive officer and managing director of SNB, for design related works.

You would be paid ₹XXX per month as salary for your services. In addition, you would also be paid a travel allowance of ₹XXX, and a telephone allowance of ₹XXX. You would also be eligible for the medical and other benefits available to SNB employees at your grade.

If you wish to accept this offer of promotion, please sign the form of acceptance at the bottom of the enclosed copy of this letter and return it so as to reach us at the above address not later than the 25th day of November 2012.

Yours sincerely,

Sunitha Somanath

Chief Executive Officer and Managing Director

Source: Company files

EXHIBIT 2: EXTRACT From THE EMPLOYMENT AGREEMENT Appointing Raghuveer Urs as TRAINEE FASHION DESIGNER

Dear Mr. Raghuveer,

Based on your performance during your internship with us from June to November 2011, we are happy to hereby offer to employ you as a trainee fashion designer at the Sunitha Nath Boutiques (SNB) upon the terms and conditions listed below.

Our boutique caters to the needs of the elite class in India, both in terms of their fashion needs as well as their merchandising needs.

Your roles and responsibilities, upon joining the organization, would be as follows:

1. Help designers create new designs for apparel and accessories for men, women, and children;
2. Help designers in sketching and researching products, fabrics, and fittings; prepare reports and portfolios, and assisting in presenting the same to the clients;
3. Assisting the designers during fashion shows, demonstrations, and other events that SNB decides to participate in;
4. Co-ordinate with suppliers and customers, thereby assisting the designer in completing her tasks; and,
5. Execute any other tasks delegated to you by your supervisor.

Your primary location of work would be #1201–1202, 12th Floor, UB City, Bengaluru. You would be reporting to Mr. Saravanan, Office Manager, for administrative purposes and Ms. Sunitha Somanath, chief executive officer and managing director of SNB, for design related works.

You would be paid ₹XXX per month as salary for your services. In addition, you would also be paid a travel allowance of ₹XXX, and a telephone allowance of ₹XXX. You would also be eligible for the medical and other benefits available to SNB employees at your grade.

If you wish to accept this offer of employment, please sign the form of acceptance at the bottom of the enclosed copy of this letter and return it so as to reach us at the above address not later than the 25th day of November 2011, indicating your expected date of joining the services.

Yours sincerely,

Sunitha Somanath

Chief Executive Officer and Managing Director

Source: Company files

1. In India, the naming convention varied. People belonging to certain regions and communities had surnames, while others did not. Surnames could either be family names, community names, or the father’s or husband’s name. Sunitha had adopted her father’s name as her surname. Instead of addressing her as Ms. Somanath, she would be addressed by her first name, which was also a common practice in India. [↑](#footnote-ref-1)
2. *Desiccant Rotors International v. Bappaditya Sarkar*, CS(OS) No.337/2008, (2009). [↑](#footnote-ref-2)
3. ₹ = INR = Indian rupee; all dollar amounts are in U.S. dollars unless otherwise specified; US$1 = ₹62.13 on April 1, 2015. [↑](#footnote-ref-3)