

Restrictive Covenants: Recent Cases

To be enforceable, restrictive covenants should go no further than is reasonably necessary to protect the legitimate business interests of the employer. To determine whether a covenant is acceptable the courts will consider the duration, scope and geographical limitations of the covenant. This *DechertOnPoint* considers some recent cases that deal with issues of enforceability and breach of restrictive covenants.

Towry EJ Limited v Barry Bennett and others (High Court, 2012): Proving Solicitation

The defendants were financial advisers and stockbrokers who were employed by Towry EJ Limited ("TEJ"). The defendants resigned or were dismissed for redundancy following the sale of TEJ and went to work for a competitor. A large number of clients followed the defendants to the competitor company. TEJ claimed that the defendants had breached their post-termination restrictions which prohibited them from soliciting clients for 12 months after the termination of their employment.

Three important points were decided by the Court:

- It was not necessary for TEJ (whose advisory and investment services had been transferred out of its business) to have a continuing business interest at the time of the trial in order to be able to enforce the restrictive covenants. While this is relevant to determine whether or not the protection is reasonably necessary — that question is to be decided as at the date when the restrictive covenant was entered into.
- Solicitation is not determined solely by whether the employee made the first contact but whether there is an element of persuasion in their communications with clients. Therefore a contractual non-solicitation clause of this kind means

former employees "*must not directly or indirectly request, persuade or encourage clients of their former employer to transfer their business to their new employer*".

- TEJ needed to demonstrate that the unprecedented loss of clients was due to solicitation by the defendants, however, TEJ had not managed to prove this. The Court found that TEJ had understated other relevant factors such as the trust and loyalty that the clients may have felt towards its former employees and the clients' dissatisfaction with their new advisers at TEJ. It was also relevant that the defendants' new employer had behaved impeccably and sought to ensure that the individuals would not breach their restrictive covenants.

Customer Systems plc v Ranson and others (High Court, 2011): Limiting the Scope of Non-compete Covenants

Customer Systems plc ("CS") provided specialist information technology consultancy through a group of companies. CS employed Mr. Ranson as a senior sales manager. He set up a competing company of his own while still employed by CS. A number of CS' employees left to join Mr. Ranson's new company.

The Court had to consider whether the employees had breached their restrictive covenants which prevented them from undertaking direct or indirect employment with

any of CS's present or past customers with whom they had been personally involved whilst working for CS.

The Court decided that the covenant was unreasonable and unenforceable. This was because:

- there was no time limit on the interval between the employee's involvement with the customer and the employee leaving CS — also, the employee's level of involvement may have only been slight; and
- the covenants were not restricted to employment in the same field in which CS operated and therefore applied to any kind of employment which an employee could take up with a customer or former customer.

Monster Vision UK Ltd v McKie (High Court, 2011): Legitimate Business Interests

Monster Vision UK Ltd ("MV"), a company that provides interactive advertising solutions, was seeking the continuation of an injunction against Mr. McKie which restrained him from acting in breach of his restrictive covenants. Mr. McKie had been the sales director of MV and was subject to restrictive covenants prohibiting him from competing with MV, soliciting any of MV's customers or employing any of MV's employees for a period of two years. The non-compete covenant was limited geographically to the countries in the world in which MV or any of its affiliates had or reasonably planned (as at the termination of Mr. McKie's employment) to conduct business.

The Court held that, although the two year period for the non-competition covenant was arguably reasonable, it was nonetheless unenforceable because:

- its scope restricted any competition by Mr. McKie and so went beyond what was necessary for the protection of MV's legitimate business interests;
- its application to affiliates was unreasonable;
- its application to any country in which the company or its affiliates had plans to have business was too vague; and
- a non-solicitation clause would have been adequate and possible to police.

The Court also held that the non-employment covenant was unenforceable because it went beyond merely restraining Mr. McKie from soliciting or actively poaching MV's employees.

Landmark Brickwork Ltd v Sutcliffe and others (High Court, 2011): Certainty of Covenants

Mr. Sutcliffe had been Landmark Brickwork Ltd's ("LB") managing director but had been summarily dismissed by LB on the grounds that he had started to establish a rival business. LB was seeking to obtain an injunction (based on the contractual restrictive covenants) for six months preventing Mr. Sutcliffe from competing with LB or soliciting or dealing with any customer or supplier of LB.

The Court held that:

- restraints must be certain in scope to be enforceable. In this case, the application of the non-compete covenant to an area described as "to the south" of certain identified counties and in respect of "any other place" in which LB operated were inherently uncertain and as such unenforceable; and
- a restriction on Mr. Sutcliffe accepting unsolicited business was unreasonable because in such circumstances there was no risk that Mr. Sutcliffe would exploit either his customer connections or LB's confidential information.

The Court did grant interim injunctions prohibiting Mr. Sutcliffe from soliciting and dealing with LB's customers but held that the enforceability of those covenants was a serious issue to be considered at the full trial. This was because the restrictions extended to customers with whom Mr. Sutcliffe had no personal dealings and may therefore have gone further than necessary to protect LB's business interests. The issue was not determined at the injunction hearing but the Court commented that Mr. Sutcliffe's position as managing director may have led him to possess confidential information in relation to, and gain influence over, customers he had not personally dealt with (in other words, the absence of Mr. Sutcliffe's personal dealings with clients may not have rendered the covenant unenforceable).

Tim Russ & Co v Robertson and others (High Court, 2011): Legitimate Business Interests

Mr. Robertson was an employee of Tim Russ & Co (“TR”) which operated an estate agency in Haslemere. Robertson resigned from his employment and set up a rival estate agency approximately 1.5 miles from TR’s Haslemere office. TR sought to enforce Mr. Robertson’s non-compete covenant which prohibited him from setting up a competing business within five miles of the Haslemere office for 12 months.

The Court held that:

- the covenant’s geographical scope was not the only factor to take into consideration;
- TR had to demonstrate a legitimate business interest and since that interest was customer connections TR would need to have recurring customers;
- since Mr. Robertson had not, while employed by TR, dealt with its recurring customers, TR could not demonstrate that the covenant was necessary to protect its customer connections; and
- even if there had been a customer connection properly protectable in relation to Mr. Robertson, 12 months was an excessive period of protection.

Lonmar Global Risks Limited v West, Mee, Karpus, Tyser & Co Limited (High Court, 2010): Duration of Solicitation/Dealing Covenants

Lonmar Global Risks Limited (“LGR”) was a Lloyd’s insurance and reinsurance broker and Tyser & Co Limited (the fourth defendant) was a direct competitor. The first three defendants were summarily dismissed by LGR on the grounds that they were soliciting clients and other employees and taking steps to move work and employees to Tyser. One issue for the Court was whether the post-termination restrictions imposed upon Mr. West and Mr. Mee were unenforceable for being too wide.

The Court held that:

- an employer has a legitimate interest in protecting its relationships with clients introduced or brought over to it by an employee; and
- the 12 month duration of the restrictions against the employees soliciting and dealing with clients was reasonable as clients renewed contracts with LGR on an annual basis. Accordingly, any shorter period would not allow LGR to adequately protect its legitimate interests.

Associated Foreign Exchange Ltd v International Foreign Exchange (UK) Ltd and another (High Court, 2010): Customer Connections

The claimant company was seeking an interim injunction to prevent a former employee (who had bought and sold currency from existing clients and pursued new clients) from breaching certain restrictive covenants after he commenced employment with a competitor (the first defendant). The individual was prohibited from soliciting business from customers or potential customers for 12 months and from dealing with any customers or potential customers for six months following the termination of his employment.

The Court held that:

- The claimant company did have a legitimate business interest to protect because a recently departed employee would have knowledge of the most profitable clients and potentially have had recent dealings or communications with customers so that their influence with the customers may be significant.
- The non-solicitation covenant was not enforceable because it went beyond what was reasonable considering that the former employee had not held a senior position and it had not been established that there was likely to be an adverse effect on the employer’s client connections after any significant break (such as six months).
- Had it found to the contrary regarding the duration of the restraint, it was unlikely that it would have been either reasonable or necessary to extend the protection beyond customers to potential customers.



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