

## Restrictive Covenants

A restrictive covenant is where an obligation is imposed on an employee or director either in an employment contract or financing document preventing the employee/director from doing something during or after his employment has terminated. This usually covers engaging in competitive businesses or poaching staff or customers. Particularly where post-employment issues are addressed (e.g. competition), care is required in drafting as the terms may be unenforceable if they are unreasonably wide.

A court will enforce a restrictive covenant only if:

- It protects a legitimate business interest of the employer and:
- The nature, scope and extent of the covenant goes no further than is reasonably necessary to protect that interest, i.e. the covenant must give no more than adequate protection

Legitimate business interests are interests of a proprietary nature - not merely interests in avoiding competition. There are two principal types of business interest that an employer is entitled to seek to protect. These are:

- Its trade connector or goodwill
- Its business secrets or confidential information

Assuming that the employer has legitimate business interests, do they need protecting from the particular employee? An employer should ask himself the following questions:

- Does the employee have access to the confidential information/trade secrets?
- Does the employee have significant dealings with and influence over clients?
- Does the employee have significant dealings with and influence over suppliers?
- Is the supplier in any way exclusive?
- Does the employee have significant influence over members of the workforce?
- What detriment will be caused to the employer by the ex-employee joining a rival?

### Various Types of Covenants

- Non-competition
- Non-solicitation of employees
- Non-solicitation of clients and suppliers

## Reasonableness is a Key Issue

To decide whether a covenant is reasonable the following criteria are relevant:

- Consider the seniority of the employee and the nature of the occupation
- The ex-employee should only be restrained from carrying out the sort of business in which he or she was engaged as an employee
- The ex-employee should not be restrained from carrying on activities outside the employer's area of business, and the more closely this can be defined the better, consistent with protecting the employer's legitimate business interests.
- The period of the restraint is an important factor in determining reasonableness
- For covenants aimed at protecting customer connection, the question is how long is the minimum time required to protect the connection?
- Closely define the scope of confidential/secret information clauses and the relevant categories of customer/key employees.
- The period of notice necessary to terminate the contract of employment may be a factor in determining reasonableness.

## GENERAL TIPS

### Non-Poaching Cause

Particular care should be taken to ensure that the courts will not find it to be wider than necessary to protect the employer's legitimate business interests. Consider the status of the employee within the organisation and the power of that employee to entice his or her colleagues away.

### Non-Solicitation Clause

Again, care must be taken when drafting such clauses. Restrictive covenants should, if they are to be upheld, try to prevent the former employee from contacting those customers he or she dealt with personally within a defined period of time, following termination of the contract of employment, and from soliciting those clients with whom he or she had actually dealt.

Another suggestion is that, in the interests of certainty, customers to whom the clause applies should be clearly identified. Obviously, the clause must be tailored to match the turnover rate of customers. It is recommended that a covenant of this nature should actually stipulate that the ex-employee will not solicit customers with whom he or she dealt in a defined period, for example six to 12 months, whatever is appropriate, falling immediately prior to the ending of the employment. The restraint should not prevent the employee dealing with client he or she has not worked with for a substantial period of time.

## **Non-Competition Causes**

An employer may want to restrain an employee from disclosing confidential information once his or her employment has ended. There is an implied duty not to disclose such information once employment has ended but this is only likely to protect confidential information of a restrictive kind such as information more in the nature of trade secrets. It is therefore advisable to include an express clause in the employee's contract of employment.

An employer can strengthen its argument that particular information is confidential by ensuring that the relevant information is always treated as confidential, for example it should always be stamped as such.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.