

From restraint to restricted

Employers may be stifling competition with clauses preventing staff from joining rivals, writes **Rachel Nickless**.

Restraint of trade clauses aimed at stopping staff moving to a competitor for a year or more are often not worth the paper they are written on, but the tide has turned thanks to a tough economic climate and a willingness by NSW courts in particular to uphold them, employment lawyers say.

Restraints of trade are supposed to protect the "legitimate interests" of a business, such as confidential information and customer and employee relationships.

But critics say they are now so ubiquitous, and their legal effects so uncertain, they are damaging healthy competition.

"It's gone too far," says Phil Heyward, principal of a boutique Sydney employment practice that services both staff and employers.

Restraint clauses are being used to stifle competition and the Australian Law Reform Commission should review them, he says.

It is difficult even for lawyers to predict whether and to what extent a restraint of trade will be enforced by a court, Heyward says. "The courts aren't setting enough clear principles to allow informed advice on the duration and scope of restraints."

The reasonableness of a restraint is determined on the facts of each case, so it is difficult for a court to give such detailed guidance.

University of Adelaide professor Andrew Stewart says the widespread use of cascading restraint of trade clauses is a big concern and the clauses should be banned.

These clauses set up a series of alternative restraints running from those that are for a short period and a small geographic area, to restraints that run for a lengthy period and over a big region.

The idea is that if a court finds the large restraint unreasonable, it will uphold a lesser restraint. So far, the courts have approved cascading clauses, although the issue is yet to be considered by the High Court.

"It's inherently uncertain and vague and gives employees no real idea of what they have agreed to," Stewart says.

"The whole point of the doctrine of restraint of trade is that we should not lightly allow the interference with a person's freedom to trade."

Some employment lawyers say employers are increasingly inserting tailored restraint clauses into employment agreements and growing more willing to try to enforce them for senior executives or sales staff. Restraints are also being used



Former Seven chief sales and digital officer James Warburton after losing his restraint case.

Photo: TAMARA VONINSKI

for an increasingly broad range of staff.

"Once it was the domain of senior executives, now it's common, almost usual, in middle management and below," Heyward says.

Maurice Blackburn principal Josh Bornstein agrees it is becoming common for employees lower down the chain to be covered by restraints of trade.

Managing principal and founder of law firm People & Culture Strategies, Joydeep Hor, says using longer notice periods rather than restraints

not have bothered to enforce a restraint of trade clause, in the current tough climate they are very concerned to protect their customer base and intellectual capital, he says.

Employers are also spending more time tailoring restraint clauses for their senior staff in the recruitment, insurance or banking industries especially, Burke says.

Allens Arthur Robinson partner Simon Dewberry says: "Employers are getting better at getting [restraint] clauses right and courts are getting more comfortable with enforcing

former employers. In a recent NSW case, Red Bull Australia's former general manager, Michael Stacey and former marketing director Christian Graebner were forced to quit their new jobs, even though their restraints of trade were due to expire in a little over two months and they gave undertakings not to compete with Red Bull.

Another high-profile case occurred in May, when Seven Media Group (now Seven West Media) brought a successful action in NSW to stop former chief sales and digital officer James Warburton joining Ten Network until January next year.

Last year, the NSW Court of Appeal upheld the validity of a year-long, Australia-wide restraint of trade imposed by OAMPS Insurance Brokers on a former insurance broker, Peter Hanna, even though it was part of a cascading restraint that included nine different non-compete clauses.

In contrast, Victorian courts are taking a more cautious approach.

In a 2010 case, Victorian Supreme Court judge James Judd refused to uphold a six month restraint of trade against David Allison, a former director of a large association of independently owned accounting practices, BDO.

This was partly because enforcing the restraint would impact on four relatively junior former BDO employees who had been hired by Allison.

But the restraint of trade clauses which make it to court are just the tip of the iceberg. "Ninety-five per cent of the restraints of trade disputes we see are resolved before litigation," Hayward says.

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Using longer notice periods rather than restraints of trade would be a fairer way of ensuring employees don't jump ship to a competitor immediately.

Joydeep Hor, People & Culture Strategies

would be a fairer way of ensuring employees don't jump ship to a competitor immediately.

Employees could then work out their notice or be put on "gardening leave" where they are not allowed to work but are still paid by their employer, he says. The advantage of notice periods is that the employee is paid and the situation is more certain for both sides, he says.

But several lawyers who act for employers see the benefits of widespread use of restraint clauses.

Middletons partner Seamus Burke says these clauses are becoming more important because of the tight economic conditions. "We've been finding people have been moving to get more money, typically at a competitor in what they know," he says.

And while bosses previously might

restraints, even when they are for long periods, provided they are properly drafted."

Just how successful an employer will be in getting a restraint of trade upheld may depend on the jurisdiction, with NSW courts more willing to uphold restraint clauses than courts in other states.

This can partly be explained by the NSW Restraint of Trade Act, which allows courts to replace a restraint of trade clause that they deem to be unreasonable with a new clause.

In other states, courts can only delete words from a contract, which means a clause deemed unreasonable is struck out.

But several senior lawyers say there is also a noticeable trend among NSW judges since 2005 to hold employees to their promises with