

Under the Employment Relations Act 2000

**BEFORE THE EMPLOYMENT RELATIONS AUTHORITY
WELLINGTON OFFICE**

BETWEEN Cullen Building Supplies Limited (Applicant/Respondent)

AND Hugh Caddick (First Respondent/Applicant)
AND Bunnings Limited (Second Respondent)

REPRESENTATIVES Penny Swarbrick for Applicant/Respondent
David France for Respondents/Applicant

MEMBER OF AUTHORITY G J Wood

INVESTIGATION MEETING 24 March 2005

FURTHER SUBMISSIONS 26 April 2005

RECEIVED BY

DATE OF DETERMINATION 23 May 2005

DETERMINATION OF THE AUTHORITY

Introduction

1. Cullen Buildings Supplies Ltd (Cullens) claims penalties against a former employee, Mr Hugh Caddick, and his present employer, Bunnings Ltd (Bunnings), for breaching the restraint of trade clause in Mr Caddick's employment agreement with it. In turn, Mr Caddick seeks penalties against Cullens for requiring him to take garden leave when he announced his resignation from it.

Facts

2. Cullens is a building products retailer in Hawera, which trades under the Placemakers brand. The company operates its store in a joint venture with a subsidiary of Fletcher Building Ltd.
3. Fletchers operate the Benchmark brand on the basis of defined areas. Customers who are account holders within each area serviced by a company such as Cullens can and do charge all purchases, whatever store they are purchased in, to their core account. In Cullens' case it services the Taranaki market, except that it is bounded by Mt Taranaki in the north.
4. Mr Caddick first started work for Cullens in 2002 as an account manager, in effect a sales representative role. A new individual employment agreement was entered into between Mr Caddick and Cullens on 1 October 2004. The new agreement not only provided for a pay increase for Mr Caddick of \$6,000 per year, but also contained a restraint of trade and non-

solicitation clause and standard restrictions on Mr Caddick's behaviour in terms of confidential information during and post-employment. The restraint clause states as follows:

"12.4 Restraint of Trade and Non-Solicitation

On the termination of your employment, except with the prior consent of the company, you agree:

- (a) You will not at any time during the period of 1 month from the employment termination date, be directly or indirectly employed, interested, engaged or concerned in any business which competes, or is likely to compete, with the business carried on by the company whether as a principal, employee, firm, contractor, consultant or otherwise; and*
- (b) For a period of 1 months following the termination of your employment for whatever reason, you shall not, either personally, or as an employee, consultant or agent for any other entity, seek to solicit or carry out any work of the same nature for any client or customer of the company with which you had any contact or dealings whilst employed by the company; and*
- (c) For a period of 1 months following the termination of your employment for whatever reason, you shall not, either personally, or as an employee, consultant or agent for any other entity, solicit or engage or employ any employee of the company or attempt to entice or encourage, any employee to resign his or her position."*

5. While it is clear that Mr Caddick would not have received a pay increase had he not signed the new employment agreement, Mr Cullen did not tell him that part of the reason for his increased salary was the introduction of the restraint of trade clause. On the other hand, Mr Caddick did not seek any changes to the restraint of trade clause. Other parts of the agreement that Mr Caddick did not agree with were negotiated over and changes made.
6. The contract required one month's notice to be given by either party, but did not specifically provide for payment in lieu of notice.
7. Bunnings Ltd also operate a building products store in Hawera, trading under the Benchmark brand. The store there was not running too smoothly and a new manager was sought. Mr Caddick applied for the job and was offered it and accepted it on 2 February 2005. On 3 February he resigned from Cullens, telling Mr Cullen that he was taking up the position of manager of Benchmark in Hawera.
8. Mr Cullen expected that it would take six weeks for it to get in a replacement for Mr Caddick. The next day Mr Cullen prepared a letter about Mr Caddick's leaving, which he discussed with him. This letter noted that a month's notice of resignation was required but that he was not required to attend work during this period. The letter also informed Mr Caddick of his employment obligations during the notice period, which was to run until 3 March. The letter also set out the requirements of the restraint of trade clause and informed Mr Caddick that he would not be able to commence any work for Benchmark until 4 April. Mr Cullen and Mr Caddick then signed the letter, as required of Mr Caddick by Mr Cullen. Mr Caddick asked Mr Cullen how far over the country the clause extended to, but did not receive a response.
9. Bunnings wanted Mr Caddick to start work for it as soon as possible. Mr Caddick consulted a lawyer, who had concerns about the potential for Mr Caddick to be sued for being in breach of his employment agreement; including the possibility of an injunction, if he was to start with Bunnings before the restraint expired. Mr Ron Aylan-Parker, the Human Resources Manager of Bunnings, considered, however, that the restraint was most likely

unenforceable and that Cullens would do nothing about it if Mr Caddick commenced employment at Hawera halfway through the restraint.

10. It was therefore agreed that Mr Caddick would work in New Plymouth one week into the restraint and then commence work at Hawera a week later. Bunnings also agreed to pay any legal costs that Mr Caddick might have to meet should this strategy be challenged.
11. Once Mr Caddick informed Mr Cullen that he had started work at the Hawera branch of Bunnings on 15 March Cullens told Mr Caddick and Bunnings that this was unacceptable, but nothing changed. Thereafter these proceedings were set in motion. The Authority held a conference call with the parties that very day. Mr Aylan-Parker suggested that a way to avoid the need for an injunction would be for Bunnings to not require Mr Caddick to work at the Hawera branch until the end of the restraint period, but that was not ever followed up by a formal undertaking, as might have been expected. The parties attended mediation, but were unfortunately unable to resolve their differences.
12. Mr Caddick subsequently filed a counterclaim. He seeks damages and penalties against Cullens for its failure to make commission payments over the month of February 2005, its effective suspension of him for that month and for requiring him to sign a variation to his employment agreement on 4 February 2005 without giving him reasonable opportunity to seek advice. The counterclaim was joined with the existing proceedings.
13. The investigation meeting on 24 March was originally set down simply to deal with issues of compliance only. However, following undertaking by Bunnings and Mr Caddick, issued by way of consent order, all the compliance issues were resolved. I then agreed to the parties' joint request to deal with all the other matters outstanding by way of a full investigation meeting.
14. The parties were given another opportunity to resolve matters following that meeting, but were unable to do so. However, Cullens did make it clear that it was no longer pursuing damages as a result of the breach of the restraint of trade clause. Cullens subsequently also agreed to pay Mr Caddick his incentive pay entitlements for the month of February 2005.

Enforceability of the Restraint Clause

15. *Cain v Turner and Growers Fresh Ltd* [1998] 3 ERNZ 314 is a case with some similarity to this one, because it involved a sales supervisor with a lot of industry experience who had built up a significant base of relationships with the suppliers of Turners and Growers. Mr Cain sought voluntary redundancy, which was agreed to, provided he agreed to be bound by a restraint of trade clause preventing him from working for a competitor for six months. Though agreed to at the time, Mr Cain later sought an injunction and damages for breach of contract because Turners and Growers decided to pay his redundancy pay in instalments to ensure that the restraint of trade clause was complied with by Mr Cain.
16. It was held that a covenant in restraint of trade is void and unenforceable unless proved to be reasonable. On the issue of consideration the Court held, at 329, that "*the law concerns itself not with the sufficiency and the amount of the consideration, but with consideration in the sense of a reasonable motive for entering into the contract, a benefit furnished to one party by the other*".
17. In that case the consideration provided by Turners and Growers was the fact that it allowed Mr Cain to take voluntary redundancy.

18. At 330 it was held that:

“...even if otherwise amounting to a contract, a covenant in restraint of trade would be void as contrary to public policy unless proved to be reasonable as between the parties and in the public interest. A restraint of trade cannot begin to qualify as reasonable unless it crosses the threshold of appearing to be for the legitimate protection of some proprietary interest of the employer, and not for the purposes of restricting competition.

I am prepared to hold that in this case that threshold has been crossed. The legitimate interest that the defendant had was its interest in the commercial relationships that on its behalf the plaintiff had cultivated and developed over his 19 years of employment, and particularly in more recent times. Such relationships did not amount to trade secrets or other confidential information, and it is precisely in that situation that employers are told by the Courts that if they wish to protect their position they should obtain a covenant in restraint of trade because they cannot rely on their notion of what seems to them confidential being always upheld. The reasons for that are self evident: employees should not remain subject to their employer’s control after the employment.

It is not, however, enough that the covenant should be for a legitimate purpose. It must also be reasonable if it is to be valid. This is also so for the obvious reason that, upon leaving an employment, an employee should in general and despite agreements to the contrary be free to pursue such career in or out of employment as he or she may see fit without further control from the employer. It is also in the public interest that the employee’s talents and skills should be available to other employees and to the public at large.

The evidence that I have heard does not support the reasonableness of a New Zealand- wide restraint of 6 months’ duration. The period of six months was selected by the defendant not out of any consideration of the extent of the need it had for protection, but merely because this period coincided with the time equivalent of the redundancy compensation seen as salary...The most that would be reasonable on such evidence as I had would be restraint of three months ...

While there is very little evidence on the areas in which plaintiff carried out his duties, Ms Dobson’s concession that the restraint could be confined to the Wellington region was in my view properly made.”

19. The contract was modified accordingly and no damages were able to be claimed.
20. Applying those principles to this case it is clear that the contract is unreasonable only on the grounds of geographical area. The duration of the restraint of trade clause was never disputed. The proprietary interests are exactly those set out in *Cain* relating to customer contacts. For the same reasons as in *Cain* I do not accept that the confidentiality and non-solicitation clauses are sufficient to protect those interests.
21. I also accept that there was consideration for the restraint of trade clause. The new contract proffered to Mr Caddick was fully negotiated, although there was no specific discussion on the restraint of trade clause itself. Mr Caddick gained a significant pay rise as a result of entering into the new employment agreement. Consideration therefore flowed from Cullens to him.
22. In terms of geography, it seems to me that having no geographical restraints at all is quite unreasonable. Cullens operates in the southern half of Taranaki. Any Benchmark customers who come from outside of that area, such as New Plymouth, can operate their accounts at Cullens but can have the account remitted to their local branch. The dividing line in the agreements between the different Benchmark franchises for Taranaki is Mt Taranaki. I therefore modify the agreement to the Taranaki region south of Mt Taranaki.

Penalties for Breaches of the Restraint Clause

23. The approach of the Authority to penalties has been examined in *Xu and Naenae Auto Service Station Ltd v McIntosh* (unreported, Goddard CJ, WA 13A/04, 18 November 2004). At Para 47 it was held that:

“...A penalty is imposed for the purpose of punishment of a wrongdoing which will consist of breaching the Act or another Act or an employment agreement. Not all such breaches will be equally reprehensible. The first question ought to be, how much harm has the breach occasioned? How important is it to bring home to the party in default that such behaviour is unacceptable or to deter others from it?”

The next question focuses on the perpetrator’s capability. Was the breach technical and inadvertent or was it flagrant and deliberate? In deciding whether any part of the penalty should be paid to the victim of the breach, regard must be had to the degree of harm that the victim suffered as the result of the breach”.

24. Mr France submitted that at the time of the alleged breach, the restraint as it reads is unenforceable and thus there was no breach and no basis for awarding a penalty. I do not accept that submission. It is only common sense that the provision as modified by the Authority must be enforceable from inception, because otherwise in the vast majority of cases in the civil jurisdiction, where such restraints may not be subject to final as opposed to interim consideration until after they have been exhausted, there would be little benefit, if any, in modifying them. However, I do accept that Bunnings did believe at the time that the restraint was unenforceable, as Mr Aylan-Parker was unaware that such restraints could be modified. Mr Caddick, on the other hand, was concerned about the restraint, but has been indemnified by Bunnings. This proves conclusively that Bunnings did aid and abet Mr Caddick to breach the restraint clause.
25. It is clear that Cullens have not suffered any great losses as a result of the breach, except that it has no doubt faced considerable legal costs, which can be addressed later.
26. In terms of the deliberateness of the breach, I determine that Bunnings encouraged Mr Caddick to breach the restraint and took the risk that it would prove enforceable. Both Mr Caddick and Bunnings had alternative options such as seeking the urgent assistance of the Mediation Service and/or the Authority. Upon taking legal advice they remedied the situation to a great degree, by agreeing to abide by the restraint. On the other hand, it is important that parties in default in cases like this should be penalised to show that such behaviour is unacceptable and to deter others from it. I determine that an appropriate penalty to be awarded against Bunnings is \$5,000 and against Mr Caddick, \$2,500. Given that Cullens have suffered no loss, it is appropriate, consistent with issues of public policy that the penalties be paid to the Crown, as section 136 implies.

Penalties for Garden Leave

27. While it is clear that the employment agreement does not provide for garden leave Mr Caddick not only accepted being placed on garden leave as he was going to work for Cullens’ main opposition, but he expected this course of action by Cullens. In any event he has not suffered any damage. Cullens have undertaken to pay him his commissions for the month. I do not accept that he would have been happier working at Cullens over that month than being placed on garden leave.

28. The key factor here is that, unlike Cullens, who did not accept Mr Caddick's breach of the restraint clause, Mr Caddick accepted, at the very latest by 4 February, that he would not have to work during the notice period, but would remain an employee of Cullens. Although no consideration was provided for that agreement, it showed Mr Caddick's view at the time, which was also demonstrated by his discussions with Bunnings. In these circumstances I consider that even if there had been a technical breach of the employment agreement by Cullens in requiring Mr Caddick to go on garden leave, there is no requirement for a penalty, as Mr Caddick was not damaged in any way by the requirement. Furthermore, even if there were a breach of section 63A of the Act as claimed by Mr Caddick, it was only technical in nature and therefore does not warrant a penalty either, for this reason and those given above.

Conclusion

29. Any breaches by Cullen Building Supplies Limited of the employment agreement it had with Mr Hugh Caddick have either been remedied or did not damage Mr Caddick in any way. Therefore no penalties are appropriate. By contrast, Mr Caddick's decision to work for Bunnings Limited during the term of a restraint of trade provision, as modified, has led the Authority to order him to pay a \$2,500 penalty to the Crown. Bunnings Limited is also ordered to pay a penalty to the Crown, in the sum of \$5,000, for aiding and abetting that breach of Mr Caddick's employment agreement.

Costs

30. Costs are reserved.

G J Wood
Member of Employment Relations Authority