IN THE EMPLOYMENT RELATIONS AUTHORITY
AUCKLAND

AA 424/08
5141131

BETWEEN	JOHN FARAC Applicant	
AND	GILLIGAN FINANCIAL SERVICES LIMITED Respondent	

Member of Authority:	Leon Robinson
Representatives:	Max Whitehead for Applicant Andrew Caisley and Emma Poyner for Respondent
Investigation Meeting:	11 December 2008
Determination:	12 December 2008

DETERMINATION OF THE AUTHORITY

The problem

[1] These parties seek the Authority's assistance as to the enforceability of a restrictive covenant agreed between them. The Applicant Mr John Farac ("Mr Farac") brings the application, commendably so, desirous of certainty with a view to ordering his future affairs.

[2] The parties were unable to resolve the problem between them by the use of mediation.

The facts

[3] Mr Farac commenced employment with the respondent Gilligan Financial Services Limited ("Gilligan") in May 2007 as an accountant. The terms of the employment were recorded in a written individual employment agreement signed by the parties on 25 and 28 May 2007 ("the IEA").

[4] The IEA contained this provision:-

> *14. Restrictive Covenants*
>
> *The employee acknowledges and agrees with the employer that he or she shall not at any time after the termination of his or her employment for a period of two years, for himself or herself or for or on behalf of any other person:*
>
> *(a) Canvass, solicit or act in competition with the employer(sic) the custom of any person who has at any time during the period of the employee's engagement by the employer been an account of the employer for a period of terms(sic) from termination of employment.*
>
> *(b) Employ, or offer employment, or cause employment to be offered to any person who at any time during the period of 2 years before such termination shall have been an employee of the employer.*
>
> ("the restrictive covenant")

[5] On 5 October 2008 Mr Farac tendered his resignation in writing to Gilligan's director Mr Allan Gerald Harold Gilligan ("Mr Gilligan") giving three weeks notice. Mr Gilligan accepted that notice. The parties agreed that Mr Farac would not work the notice period and he was paid in lieu of it.

[6] Following his departure, Mr Farac commenced practicing on his own account.

The merits

[7] Mr Farac asks the Authority to give a determination as to the enforceability of the restrictive covenant. Mr Whitehead submits it should be "waivered" which I interpret as a determination by the Authority that it is unenforceable by Gilligan and as against Mr Farac. Alternatively, Mr Whitehead argues the restrictive covenant ought to be modified.

[8] In reply, Gilligan says the provision is a reasonable and enforceable restrictive covenant. In the event of modification as the Authority shall deem necessary, it says the remaining unmodified components survive as effective and enforceable. It raises a counter-application for a compliance order in terms of a modified restrictive covenant. In essence, it asks the Authority to order that for a specified 12 month

period Mr Farac restrain from soliciting clients who were clients of Gilligan's during a specified two year period coinciding with Mr Farac's period of service.

[9] The issue for determination is a discrete one. It concerns solely the enforceability of the restrictive covenant.

[10] Mr Farac's employment terminated at the end of the notice period on 26 October 2008. He owed a duty of fidelity to his employer to that date.

[11] Gilligan is not entitled to protection from mere competition and it does not seek to obtain such a benefit. Mr Gilligan very responsibly and charitably endorses Mr Farac's endeavours to establish his own practice.

Restrictive covenants and restraints of trade

[12] The law relating to restrictive covenants is well settled. There are settled legal principles which the Authority is bound to have regard to[1]. The starting point is that restraints of trade are contrary to public policy and are therefore void. A restraint will only be enforceable to the extent that it is required to protect a proprietary interest of the employer. The scope of the restraint in time and location is relevant in determining reasonableness.

[13] In *Brown v Brown*[2], Richardson J said[3]:-

> *It is well settled law that to be enforceable a covenant in restraint of trade should be no wider than the circumstances of the case reasonably require. Reasonableness in the relevant sense relates to the legitimate interests of the parties to the covenant and to the wider public interest. So, as Lord Reid observed in* Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd *[1968] AC 263, 300 -:*
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> > In every case it is necessary to consider first whether the restraint went farther than to afford adequate protection to the party in whose favour it was granted and secondly whether it can be justified as

[1] *Brown -v- Brown* [1981] NZLR 484 (CA), *Bates -v- Gates* (1986) 1 NZELC 95,269 (CA), *Fletcher Aluminium Ltd -v- O'Sullivan* [2001] 2 ERNZ 46 (CA)
[2] at 491
[3] See also *Gallagher Group Ltd v Whalley* [1999] 1 ERNZ 490 and *H&R Block Ltd v Sanott* [1976] 1 NZLR 213, *Credit Consultants Debt Services NZ Ltd v Wilson (No 3)* [2007] 1 ERNZ 252 and *Fuel Expresso Ltd v Hsieh* [2007] NZCA 58

> being in the interest of the party restrained and thirdly, whether it must be held contrary to the public interest.

[14] I add to these well-known authorities one fundamental notion arguably underlying the development of the law of intellectual property. It is that one should not "reap where it has not sown"[4].

[15] I immediately note that the clause at issue in this present case is not a restraint of trade. It is a non-solicitation clause. Mr Farac is not restrained from competing with his former employer Gilligan. In that regard, the interference with his right to earn his living and the public policy in the mobility of his labour is less significant than would be the case if absolute competition were in issue. It is not.

[16] Next I note that the clause is inelegant in its drafting. Although sub-part (a) refers to "act in competition", that seems to me to have been an ill-considered insertion. It is my view that the clause essentially being about non-solicitation, any reference to non-competition is incongruous in context. I am satisfied that the clause is imperfect insofar as it refers to acting in competition. For these reasons, I do not consider restricting competition can be enforced.

[17] There is a further difficulty. The reference to "terms" in the same sub-part (a) lacks meaning. I am unable to objectively determine its significance and precise meaning. It is likely an error.

[18] However, while I accept the clause's drafting is inelegant, I am not prepared to find that it must fail because it is too vague. I ascertain objectively, that the parties agreed and intended it to be so that Mr Farac ought not for a period of time solicit or canvass or attempt to convert for his own purposes, Gilligan's clients. That is what Mr Farac agreed to. He agreed the same in good faith. I accept that he was provided an opportunity to take advice, and further, that he did take advice. He told the Authority he consulted his neighbour, a solicitor, about the IEA. He said he particularly discussed the restrictive covenant clause with his neighbour.

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[4] *International News Service v Associated Press* 248 U.S. 215, 239 (1918) (Brandeis, J., dissenting)

The determination

[19] It is because I accept the clause is not one which seeks to restrain competition, I do not accept Mr Farac's contention that a three month restraint ought to imposed by way of modification. There is no issue as to restraining Mr Farac from competing. Rather, the issue is how long he should be prevented from approaching Gilligan's clients with a view to converting their business to his own.

[20] I am satisfied that there is an interest capable and worthy of protection here. It is Gilligan's client base. I therefore agree that I ought to act to provide some measure of protection to Gilligan in the form of restricting Mr Farac's activities. The question then becomes what is likely to be a reasonable restriction. Just as I do not agree that a three month restriction is reasonable, nor am I persuaded that a two year restraint is reasonable.

[21] I accept Mr Gilligan's evidence that one accountancy season being a 12 month period would provide Gilligan sufficient time to find and settle in a replacement. Additionally, that same period would permit a replacement employee a reasonable period to cement client relationships and to protect such relationships from disturbance by Mr Farac. Having accepted this evidence, I regard it as a restriction no wider than is necessary. I also accept that typically and predominantly clients seek professional accountancy services on an annual basis at the end of each accounting period conventionally the financial year.

[22] For these reasons and because of the drafting difficulties I have earlier referred to, I do not enforce clause 14 of the IEA in its literal form. I accept the parties agreed that Mr Farac should be restrained in his subsequent activities. I give effect to that agreement taken with advice and undertaken in good faith. I accept that Gilligan has an interest being its client base that is capable and worthy of protection. But I do not enforce a non-solicitation period of 2 years.

The resolution

[23] Instead I exercise my jurisdiction under the *Illegal Contracts Act 1970* as available to me under section 162 of the *Employment Relations Act 2000*. I modify the clause in question to be as follows:-

> ***That for a 12 month period beginning on 27 October 2008 the applicant will not:-***
>
> ***(a) solicit, or attempt to solicit any client of the respondent for whom the respondent provided accountancy services at any time between 26 October 2006 - 26 October 2008 with the exception of clients listed in the attached Schedule A;***
>
> ***(b) be involved in any way in employing or offering employment to any of the respondent's employees who were employed with the respondent at any time during the period 26 October 2006 - 26 October 2008, with the exception of Ms Nataly Ireland.***
>
> ***In the event of any of those clients listed in Schedule A wish to transfer work to the applicant, the respondent shall take all reasonable steps to facilitate the transfer of the work in a smooth and orderly fashion.***

[24] **Of my own motion pursuant to section 137 of the *Employment Relations Act 2000*, I also order Mr Farac to comply with the modified clause I have set out at paragraph [23] above. The order is to be obeyed for the specified 12 month period beginning on 27 October 2008.**

Costs

[25] In the event that costs are sought, I invite the parties to resolve the matter between them, but failing agreement, Mr Caisley is to lodge and serve a memorandum as to costs within 14 days of the date of this Determination. Mr Whitehead is to lodge and serve a memorandum in reply thereafter but within 28 days of the date of this

Determination. I will not consider any application outside that timeframe without leave.

Leon Robinson
Member of Employment Relations Authority