

**IN THE EMPLOYMENT RELATIONS AUTHORITY
AUCKLAND**

[2017] NZERA Auckland 221
5643832

BETWEEN	LANCOM TECHNOLOGY LIMITED Applicant
AND	SEAN FORMAN First Respondent
AND	CHARLIE KANG Second Respondent

Member of Authority: Robin Arthur

Representatives: Andrew Schirnack and Stephanie Bonney-Lovegrove,
Counsel for the Applicant
Tim Oldfield, Counsel for the Respondents

Investigation Meeting: 18 and 19 May 2017

Determination: 28 July 2017

DETERMINATION OF THE AUTHORITY

- A. Sean Forman breached an obligation not to engage in private work without written permission from Lancom Technology Limited (LTL).**
- B. Charlie Kang aided and abetted Mr Forman's breach of duty and also breached a restriction on soliciting employees of LTL by engaging Mr Forman in a plan for a new business.**
- C. As a penalty for those breaches Mr Forman and Mr Kang must each pay \$4000 directly to LTL within 28 days of the date of this determination.**
- D. LTL's claims that Mr Forman and Mr Kang also committed other breaches and Mr Forman should be ordered to pay**

damages to LTL are dismissed.

E. Costs are reserved with a timetable set for memoranda to be lodged if the parties cannot resolve any costs issue themselves.

Employment Relationship Problem

[1] Lancom Technology Limited (LTL) sought orders for damages and the imposition of penalties against two former employees, Sean Forman and Charlie Kang.

[2] LTL employed Mr Forman to work as a software developer from 24 March 2014 to 2 September 2016. He gave one month's notice of resignation on 1 August 2016. Soon after getting Mr Forman's notice LTL's managing director Warwick Eade and general manager Waruna Kirimetiya found some information that led them to believe Mr Forman was using LTL's resources to set up in business selling a project management software programme call ProjoMojo. They believed that programme was based on an earlier one called DeveloperPath that Mr Forman had written, as an LTL employee, for the use of an LTL client. They also discovered Mr Forman and Mr Kang were the directors and shareholders of a company called Black Magic Software Limited (BMSL) incorporated on 20 June 2016 .

[3] Mr Kang had worked for LTL from 2008 until 9 October 2015. In mid-October 2015 he began working for Microsoft, employed on an agency basis through Adecco Personnel. Mr Kang's role with Microsoft included liaising with a number of its clients, including LTL. As a result he had frequent contact with LTL staff and he has access, for those work purposes, to LTL's internal instant messaging system.

[4] The concerns held by Mr Eade and Mr Kirimetiya resulted from reviewing messages Mr Forman and Mr Kang exchanged on that system. Mr Kirimetiya looked at those messages after a client complained about work Mr Forman was doing on a software development project. In this determination the work for that client is referred to simply as 'the key project'. The client considered the work was taking too long and was not done to the necessary quality.

[5] LTL believed its client's complaint was the result of Mr Forman diverting his attention and energy, including during time he was being paid to do work for LTL, into developing his own software programme for a business he and Mr Kang planned to run through BMSL. After Mr Forman's resignation, but before his employment ended, LTL arranged for other personnel to work on fixing and finishing the key project for the client. This additional work was the basis of LTL's claim for an award of damages against Mr Forman.

[6] LTL sought penalties against Mr Forman because it said his activities breached his obligations under his employment agreement. It also sought a penalty against Mr Kang on two grounds – firstly, that his business plans with Mr Forman breached restraint of trade terms in Mr Kang's own previous employment agreement with LTL and, secondly, that Mr Kang's activities aided and abetted the alleged breaches by Mr Forman of his own employment agreement.

[7] Mr Forman and Mr Kang denied their activities breached terms of their employment agreements or otherwise made them liable for the remedies LTL sought. Their statement in reply said Mr Forman was developing the ProjoMojo software but said that programme was unrelated to LTL's activities and the services it provided. They denied ProjoMojo was based on or derived from the DeveloperPath software Mr Forman had written earlier for LTL. They accepted Mr Kang had developed a website, called www.projomojo.com, for future use but said no goods were available for sale and the website's sales link was not operational. They also said BMSL had never actively traded or made any sales or profit.

The Authority's investigation

[8] Mr Eade, Mr Kirimetiyyawa, Mr Forman and Mr Kang each provided a written witness statement for the purposes of the Authority's investigation. At the investigation meeting they each, under affirmation, answered questions from me and the parties' representatives. The representatives also provided closing submissions on the issues for determination.

[9] As permitted by 174E of the Employment Relations Act 2000 (the Act) this written determination has stated findings of fact and law, expressed conclusions on

issues necessary to dispose of the matter and specified orders made but has not recorded all evidence and submissions received.

Issues

[10] The issues for investigation and determination were:

- (i) Did Mr Forman breach terms of his employment agreement by creating ProjoMojo, by not disclosing the activity, and/or by promoting the software through BMSL?
- (ii) If such breaches by Mr Forman were established, did they cause loss and if so what?
- (iii) If loss was caused, what amount of damages should Mr Forman pay in remedy?
- (iv) If Mr Forman breached his employment agreement, should he pay a penalty for breaches of his employment agreement and, if so, what amount?
- (v) Was Mr Kang's contact with Mr Forman, and their activities in setting up BMSL and planning to sell ProjoMojo, in breach of Mr Kang's non-solicitation and restraint of trade clauses in his employment agreement?
- (vi) If so, should Mr Kang pay a penalty for those breaches?
- (vii) If Mr Forman's activities were breaches of his employment agreement, did Mr Kang aid and abet those breaches?
- (viii) If so, should Mr Kang pay a penalty for those breaches?
- (ix) If any penalties are imposed, to whom should they be paid, the Crown or the applicant?

[11] In closing submissions, made at the end of the investigation meeting, Mr Forman and Mr Kang sought to challenge the reasonableness and enforceability of the non-solicitation and restraint of trade provisions in their employment agreements. LTL objected to the submission because it was not raised as a defence in the statement in reply from Mr Forman and Mr Kang or addressed in any direct or substantive way in their written witness statements or during the testing of their evidence at the Authority investigation meeting. While the Authority's role is to determine matters according to the substantial merits of a case, so it may not be as concerned about the technicalities of what a party had or not pleaded as might apply under a court's more

particular rules or procedure, LTL's objection was a fair point well made.¹ At the outset of LTL's claim the statement of reply from Mr Forman and Mr Kang had not openly challenged the reasonableness and enforceability of the solicitation and restraint provisions. Neither was that argument the subject of any direct evidence or questioning during the investigation. Rather their defence had focussed on the notion that their actions had not breached the relevant terms. Matters of fact and interpretation about whether they had been in business, in competition, or used LTL's property were relevant, properly in contention, and were tested in questioning during the investigation meeting.

[12] In those circumstances this determination has assumed, as not in issue, that LTL had legitimate proprietary interests in protecting, for its exclusive use, the work it had paid employees to do (including by writing computer code to create specific software programmes) and in limiting the ability of former employees to use relationships they had developed while working for LTL to lure away staff or clients. The restraint terms were in the employment agreements of Mr Kang and Mr Forman had entered at the start of their respective periods of employment, so the necessary consideration for them could be deemed to have been provided at that time. In the absence of tested evidence to the contrary, the six-month length of those terms could be taken to have been accepted as not unreasonably long. However those terms were enforceable only to the extent reasonably necessary to protect LTL's proprietary interests and to enable it to prepare for competition. Determining the enforceable extent was guided by two overlapping and not necessarily compatible principles of public policy: firstly, that agreements were made to be kept and, secondly, restraints were not enforceable to an extent that went beyond what was reasonably necessary to achieve those legitimate purposes and became simply a means to prevent fair competition and the free use of skills and experience.

[13] In this case Mr Kang and Mr Forman confirmed in their oral evidence that they both knew about the restraint terms in their employment agreement and had, as Mr Kang put it, discussed this "early on". Their argument was that their activities – in registering BMSL, creating a website for ProjoMojo and having Mr Forman work on writing the programme – did not breach those terms. LTL's contrary view was to the effect that Mr Kang and Mr Forman knew they were breaching those terms and

¹ Employment Relations Act 2000, s 157 and s 160(1)(f) and (2).

took some care to avoid detection of their breaches. Either way, the point was that the only issues open to determination were whether the actions of Mr Kang and Mr Forman were within or outside the scope of the requirements of the terms, as worded and properly interpreted. Contrary to their closing submissions, whether those terms were, in their entirety, unreasonable and void or unenforceable, was not fairly at issue at that stage.

Liability of Mr Forman – the alleged breaches

[14] LTL sought six findings that Mr Forman had breached the terms of his employment agreement by:

- (i) contrary to clause 18.7, failing to declare his interest in BMSL;
- (ii) contrary to clause 18.7 and clause 44, failing to obtain written permission from LTL prior to obtaining an interest in BMSL;
- (iii) contrary to clause 30, undertaking work for BMSL without written permission from LTL;
- (iv) contrary to clause 34, infringing LTL's intellectual property rights in DeveloperPath by developing ProjoMojo without LTL's authority;
- (v) failing to be open, candid and informative in a meeting with Mr Eade and Mr Kirimetiawa on 15 August 2016; and
- (vi) contrary to clause 18.4, delivering significantly poor performance on the key project, contrary to clause 18.4.

[15] Relevant clauses from Mr Forman's written employment agreement were:

18 **Employee obligations**

...

18.3 During normal working hours employees shall devote the whole of their time, attention and abilities in carrying out their duties.

18.4 Employees shall carry out their duties well, faithfully and diligently, providing the Employer the full benefit of the Employee's experience and knowledge.

...

18.6 Employees must not engage in any paid or unpaid employment which might adversely affect the performance of the duties of their position with the Employer, without the written permission of the Employer.

18.7 Employees must declare **any interest in any business of any kind** in which the Employee may potentially be in conflict or in competition with the business of the Employer. Further, employees may not,

whilst in the employ of the Employer, **invest personal moneys, obtain an interest in or establish any other business that may be deemed to be in competition with the Employer or its principals,** without the written permission of the Employer.

...

30 **Private work**

30.1 No private work is to be conducted on or off the Employer's premises or using the Employer's vehicles, without the written permission of the Employer.

...

34. **Intellectual Property**

34.1 Any original work, process, design or other material produced or to be published by the Employee and arising from the employment with the Employer, shall remain the property of the Employer which shall have full rights to such work, process, design, or other material whether those rights are exercised in any form or not during the employment or on cessation of the employment.

...

44. **Restraint of trade**

44.1 Employees shall not at any time during the term of this agreement and for a period of 6 months after the termination of employment with the Employer **establish, purchase, or obtain an interest in, either directly or indirectly any business in relation in any way to the Employer** within a radius of 20 kilometres, without the express written consent of the Employer, provided that such consent shall not be unreasonably withheld.

(emphasis added)

(i) failure to declare an interest and (ii) failure to obtain written permission prior to obtaining an interest – breaches of clauses 18.7 and 44?

[16] Mr Forman accepted he had not told LTL about his interest in BMSL and had not sought LTL's written permission before obtaining that interest. What was in dispute was whether that interest, as a 50 per cent shareholder and as a director of BMSL, came within the scope of the terms of clauses 18.7 and 44.

[17] The second sentence of clause 18.7 was not enforceable. Getting written permission to make an investment or to take steps in establishing a business that might compete was not a reasonably necessary means of protecting LTL's legitimate proprietary interests. Giving the employer notice of such activities might be. Notice would also be consistent with the mutual good faith obligations. It would enable the employer to discuss the implications of that activity with the employee and, if necessary, to take protective steps on matters such as changing or controlling the employee's access to some information or involvement with particular client

relationships. To require more, such as prior written permission, was not consistent with public policy principles concerning personal freedoms referred to earlier in this determination.

[18] Only the first sentence of clause 18.7 was reasonable and enforceable, if what Mr Forman did fell within its scope. Did his activities amount to “an interest in any business of any kind” that might potentially be in conflict or competition with the business of LTL?

[19] That question also had to be considered in relation to whatever his obligations were under the clause 44.1 restraint of trade. Those obligations applied to him not only after the end of his employment but during it. Clause 44.1 included a strangely worded phrase referring to “any business in relation in any way to the Employer”. Read literally, the words “in relation” made no sense. From the context and apparent purpose of the clause it appeared those two words were meant to be or were meant to mean “in competition” with LTL’s business.

[20] Against that background, the first point of contention in applying the relevant parts of clause 18.7 and 44.1 was whether the mere act of incorporating a company, and being a shareholder and director of it, amounted to an interest in a “business”. The second point was whether BMSL had in fact, once incorporated, engaged in the activities of a “business”.

[21] Using ordinary and plain meanings of the word, a business is a commercial activity, that is concerned with or engaged in the activity of buying and selling, making or intending to make a profit.²

[22] A company may be the entity or vehicle by which a business is to be conducted but the act of incorporating a company does not amount, in and of itself, as activity meeting that definition of a business. As Mr Forman submitted, this conclusion was consistent with the common law position on breach of the implied duty of fidelity in an employment relationship. Registering a company intending to operate a business, which might compete with the current employer after the

² Concise Oxford English Dictionary (11th edition, Oxford University Press, 2004), definitions of “business”, “commercial” and “commerce”.

employee's employment had ended, did not of itself breach the duty of fidelity.³ Something more was required.

[23] And LTL's claim about Mr Forman's interest in BMSL was really about more than the formalities of incorporation of an entity with the Companies Office. It was referring to the activities of writing the ProjoMojo software and setting up the website for the planned business. LTL assumed those activities were for the purposes of BMSL and a business that company intended to operate. Mr Forman said he had written the software code at home and in what he considered were his own hours. He accepted he had given Mr Kang feedback about the content, style or formatting of the ProjoMojo website that Mr Kang was preparing.

[24] BMSL was clearly the vehicle that Mr Forman and Mr Kang intended to use to conduct a business once development of the programme was complete and could be sold. This was confirmed by a line along the bottom of the website Mr Kang had prepared that read: "2016 Projo by Black Magic Software Ltd. All rights reserved." To an ordinary reader it identified the programme as owned by BMSL and BMSL as the operator of any trading activity conducted on the website. Mr Eade and Mr Kirimetiya read the contents of the website which was publicly available through an internet search.

[25] However the evidence fell short of establishing that those activities of Mr Forman and Mr Kang amounted to actually conducting a business at the time.

[26] There was certainly preparation for what they hoped would enable them to conduct a business through BMSL. But no trading activity had yet been carried out. The website included a page where the product could be ordered but was not operative. A sign up page on the website had this heading: "Projo is currently in private beta testing". It included some testimonials that were really a 'mock up' using the photos and names of friends of Mr Kang. Mr Kang said those people had not seen the website or software at that time. There was no evidence to the contrary on that point.

[27] Some instant messages Mr Forman and Mr Kang exchanged on 20 July 2016 showed they hoped to have the software ready for testing with users by around 1

³ *Rooney Earthmoving Limited v McTague* [2009] ERNZ 240 at [157].

August. However there were no sales of the product. It was not completed. No one had purchased a copy or license to use it. As a result there was no revenue from it.

[28] One further element of clause 18.7 also needed to be considered. Even if Mr Forman's activities amounted to an interest in a business, was that business "potentially ... in conflict or in competition" with LTL's business?

[29] As Mr Forman submitted, that reference to LTL's business had to be interpreted as being the business activities LTL carried out at the material time. The relevance of this point concerned the existence of the DeveloperPath programme Mr Forman had made for the use of an LTL client. The client, after a trial of it, had not wanted to use it. LTL then effectively 'shelved' DeveloperPath.

[30] Although Mr Forman said he wrote DeveloperPath at his own initiative and "mostly in my own time at home", he did so as an LTL employee and for an LTL purpose. At least some of the time spent doing so, even on his version of events, was in LTL working hours. The programme remained LTL's property as something Mr Forman had made as its employee.

[31] LTL had a history of taking some programmes it had created for particular uses on particular client projects – a process that it called 'tooling' – and later developing them for sale to other clients, that is commercialising the product. It had made no plans to commercialise DeveloperPath but could, in some unspecified point in the future, have taken steps to do so. However, at the material times of Mr Forman's activities, LTL had no such project management software in development or available for sale.

[32] The result of those circumstances was that the product Mr Forman was developing, through the code he was writing, was not "in competition" with an existing business activity of LTL. There were other points of dispute, considered elsewhere in this determination, about whether his activities nevertheless used LTL's intellectual property in DeveloperPath to write ProjoMojo, but what he did was not in breach of the part of clause 18.7 that was reasonable and enforceable.

[33] The same interpretation, and conclusion, applied to the provisions of clause 44.1. Mr Forman's activities had not yet amounted to a "business" and, even if it had, his intended business activity of selling a project management software programme

was not in competition with LTL's existing or planned business activity. In that way it had no relation in any way to LTL.

(iii) undertaking work for BMSL without written permission – breach of clause 30?

[34] As Mr Forman submitted, clause 30 was effectively a further covenant of restraint. It purported to restrict any other work outside the LTL workplace and outside the hours LTL paid him to work, as well as what was permitted to happen on LTL's premises.

[35] As a restraint, the clause was enforceable only to the extent reasonably necessary to protect LTL's legitimate proprietary interests. It could not reasonably be enforced to restrict all private work at any time anywhere. Otherwise, as Mr Forman submitted, it would unreasonably restrict use of his free time, such as if he chose to work as a volunteer for a charity.

[36] What was reasonable and enforceable was a requirement for written permission for private work done on work premises and, because Mr Forman sometimes did LTL work at home, during any hours that LTL paid for him to work there. In *Space Industries (1979) v McKavanagh* the Employment Court stated that no exception could be taken to an employee preparing for a new business while still employed, but this must not be at the expense of their current employer.⁴

[37] LTL did have a legitimate proprietary interest in controlling and getting the benefit of the time it paid Mr Forman to work for it. It was consistent with the requirement of clause 18.3 for Mr Forman to devote the whole of his time during normal working hours to carrying out his duties. However, by use of the written permission allowed for under clause 30, LTL could elect to waive its control of, and benefit from, some of that time.

[38] What was meant by "private work" also needed to be considered in the context of other clauses in the employment agreement that restricted doing work elsewhere or for others. Under clause 18.6 Mr Forman could not do paid work elsewhere if it might adversely affect the performance of his duties for LTL. Under clauses 18.7 and 44.1 he could not work for actual and existing competitors of LTL. Those restrictions

⁴ [2000] 1 ERNZ 490 at 503.

overlapped with clause 30's prohibition on private work. However clause 30 extended to any work that was for Mr Forman's own interest or benefit, whether he was paid for it or not. Time spent on writing the code for ProjoMojo and taking steps to set up the business through which he and Mr Kang intended to sell that programme amounted to private work of that type. If done in working time paid for by LTL, at its work premises or elsewhere, that private work would require written permission.

[39] Instant messages exchanged between Mr Forman and Mr Kang, on a system LTL provided access to and during Mr Forman's working hours, showed they spent some time talking about ideas for the business they planned to establish.

[40] Some of their comments appeared light-hearted while others indicated serious thought and actual steps being taken. One example occurred in the mid-afternoon of Friday, 26 February 2016, a work day for Mr Forman but one he spent working away from the LTL office. A message from Mr Forman said he was "at home" because Mr Eade and Mr Kirimetiya were in Australia demonstrating an LTL service. During the ensuing message discussion Mr Kang said "I think we need to make an enterprise product first, make billions, then side into gaming". After further exchanges about the prospects for developing successful games and the costs of hiring developers, their message conversation continued:

Mr Kang: you don't think project management software would take off?

Mr Forman: I dunno about developerpath
Lots of things are similar enough

Mr Kang: not in the current iteration
but the general idea of a management system that focuses on
the user rather than the project

Mr Forman: Oh yea
Hell yea

Mr Kang: I think it's got potential
More than Pokémon

Mr Forman: I guess

[41] On 3 March 2016 they discussed business names:

Mr Kang: i can't think of a good name
sigh
also need a .com

Mr Forman: Names can come later

Mr Kang: i want to nab the domain

[42] Other examples included an exchange (on 13 June 2016) about the BMSL name being approved by the Companies Office, with Mr Kang commenting that he could now “get IRD done and talk to the bank”, and (on 20 July 2016) messages from Mr Forman about adding a registration page to the ProjoMojo website and arranging for people to test it by 1 August.

[43] Mr Forman’s closing submissions made two arguments about the application of clause 30 to the time spent on such messaging.

[44] Firstly, he said there was no evidence he had received any remuneration from BMSL as the entity was not trading and could not have engaged him to perform work. It was not a compelling argument as it set the scope of what was “private work” too narrowly, particularly given his submissions had earlier used the example of someone doing unpaid work as a volunteer. The information and ideas Mr Forman exchanged with Mr Kang in those messages, and the time taken to do so, was work being undertaken to advance his own private interests.

[45] Secondly, he submitted private work conducted on LTL’s premises by discussing BMSL was a technical breach only as the discussions took a matter of minutes each time. He referred to Mr Eade having conceded, in answer to questions at the investigation meeting, that LTL accepted some business time would be lost through employees engaging in some social chatter during working hours. Mr Forman submitted such exchanges between him and Mr Kang, about video games and arranging some social activities, took more time than the ones about BMSL and their intended business activity and, so, should not be seen as a breach. It was a submission that minimised the time taken and its use of LTL resources (being the paid time and use of its instant messaging system) for what Mr Forman intended would be to his eventual private commercial benefit. The time he spent on the exchanges, and the content of what he and Mr Kang said in them about their business plans, was clearly private work within scope of the clause. It was a breach of its terms.

(iv) Was DeveloperPath used to develop ProjoMojo, in breach of clause 34?

[46] In closing submissions LTL invited the Authority to conclude, on the balance of probabilities, that ProjoMojo was an evolution of its DeveloperPath programme and Mr Forman had breached LTL's intellectual property rights by using that programme as a basis for developing ProjoMojo.

[47] There was clearly some possibility Mr Forman's actions amounted to such a breach. However the evidence of LTL, and particularly of Mr Eade, failed to establish the probability that was so to the level of being more likely than not, that is to the necessary civil standard of the balance of proof.

[48] Mr Eade made some allegations about the nature of the ProjoMojo programme, particularly the code and structure used, but LTL had not pursued or provided the evidence necessary to establish those allegations as more than assertions.

[49] Mr Forman had offered, in a meeting on 7 September 2016, to hand over the ProjoMojo programme to LTL as a means of resolving its concerns. LTL did not accept that offer because Mr Forman would not agree to also hand over ownership of BMSL for \$1 and pay \$8000 to LTL. However his offer to let LTL see the programme was not subject to any conditions.

[50] LTL had failed to take a reasonable and available opportunity to corroborate its suspicion by making a detailed comparison of the framework and code used.

[51] Asked at the Authority investigation about this, Mr Eade accepted there were software programmes that could have been used, with relative ease, to compare the code used in ProjoMojo and DeveloperPath. If it had done so, LTL may have been in a stronger position to establish its allegations that ProjoMojo used original work or design that Mr Forman had produced for LTL and that remained its property. Mr Eade said he had not accepted the opportunity to look at ProjoMojo because it would have opened him up to hours of argument about the code. Mr Eade also said he could not be confident Mr Forman would have provided the code he had been writing. It was not a compelling argument as the comparative software would have enabled some check on when the code was written.

[52] Mr Eade gave evidence that Mr Forman had, when confronted in a meeting on 9 August 2016, admitted he used DeveloperPath to develop the ProjoMojo software, knew he used LTL's intellectual property, and knew he had breached his employment agreement by doing so. Such startling and complete admissions, if made, were surprisingly absent from the copy of the handwritten notes Mr Eade produced as those he took in that meeting. Typewritten notes Mr Eade said he made soon after the meeting included four lines labelled as "quotes" by Mr Forman: "I know you own all of the software"; "I know I breached my contract"; "I didn't bring it to you because I knew how that would end"; and "I didn't have enough money to take three months off to write the software".

[53] Only the second of those supposed admissions came close to confirming Mr Eade's assertion about what Mr Forman had said on 9 August. Mr Forman's evidence about that comment was that he had accepted he breached his employment agreement by using company resources to talk to Mr Kang during work time. He denied having admitted to the allegation about using DeveloperPath to develop ProjoMojo. The evidence in support of Mr Eade's account on this point was not sufficient for it to be preferred over that of Mr Forman as being more likely than not to be correct.

[54] Other supposed similarities with ProjoMojo, described in the evidence of both Mr Eade and Mr Forman, were too general to establish improper use of LTL's intellectual property rights in DeveloperPath. Both were said to be project management software, written in JavaScript and using a grid format for labelling of some items. Those elements were too generic to amount to an idea or its execution that could be said to specifically belong to LTL. Without a closer analysis of the inner workings and content of ProjoMojo, which LTL had not taken the opportunity to make, a breach of clause 34 was not established to the necessary evidential standard.

(v) failure to be candid and informative in 15 August 2016 meeting?

[55] At the end of their brief meeting on 9 August Mr Eade advised Mr Forman to get some legal advice. He arranged for them to meet again on 15 August.

[56] LTL submitted Mr Forman had failed to engage with Mr Eade and Mr Kirimetiya at that 15 August meeting because Mr Forman retracted his supposed "earlier admissions", denied he breached LTL's intellectual property rights, did not

satisfactorily answer questions about when he and Mr Kang had started BMSL and their work on their business plans, and had not adequately prepared for the meeting. Those were simply arguments that Mr Forman did not tell Mr Eade what he wanted to hear. What had happened in the intervening period was that Mr Forman had, as a result of his own research, come to a firm view he had not breached LTL's intellectual property rights. He took a more combative approach, including by giving Mr Eade copies of two Court decisions that he considered supported his view. Mr Eade's typed meeting notes recorded his own, similarly combative, response:

I said repeatedly ... throughout the meeting that was his prerogative to disagree about the breaches but while he kept me in the dark about the details of [BMSL] I'd have to piece it together and go to employment court to find out. If it was legit, and the E. court agreed he has nothing to worry about. It was my opinion that there have been significant breaches but only my opinion. ...

[57] Mr Forman accepted, in answer to questions at the Authority investigation meeting, that he was not candid in his 15 August meeting with Mr Eade about the "timeline" for setting up BMSL but said he was candid about making software and planning to go into business with Mr Kang. Given the other conclusions in this determination about whether setting up a company was a breach of duty, and Mr Eade's own declarations about the prospect of litigation, I was not persuaded Mr Forman's responses during the 15 August meeting were misleading, deceitful or otherwise in breach of whatever good faith obligations both he and Mr Eade had during that conversation.

(vi) poor performance on key project – breach of clause 18.4?

[58] LTL submitted Mr Forman had failed to give it the full benefit of his experience and knowledge by not carrying out the key project well, faithfully and diligently.

[59] Mr Kirimetiayawa said an important client had asked in late 2015 for a new version of software LTL had developed for that client five years earlier. He assigned Mr Forman to run this project (referred to as the 'key project' in this determination). He did so because Mr Forman had done other work for that client throughout his time at LTL. Mr Kirimetiayawa said Mr Forman was the only person within LTL who had a working knowledge of the code that made up that software. He said Mr Forman had

also scoped work, developed budgets and managed projects for other clients before being assigned the key project.

[60] Mr Forman had prepared an estimate that writing the software for the key project would take 80 hours of his time, followed by two weeks of testing and feedback, with a start date of 9 June and a completion date of 8 July 2016. He estimated a cost of \$12,000 plus GST. The client accepted a quote for that amount.

[61] Mr Kirimetiyyawa and Mr Forman attended weekly conference calls with the client about the key project from 16 June to 14 July. Mr Kirimetiyyawa learned during the 1 July conference call that the project was behind schedule. He said he realised then that the project was nowhere near completion, “full of bugs” and the remaining time would not allow LTL to deliver the product in its entirety on deadline. He said the client was concerned because it was relying on LTL to deliver the new software platform so it could release its own product.

[62] He said Mr Forman then assured him he was only a few days behind schedule and he could complete outstanding work and have it up and running by 17 July. On 18 July Mr Kirimetiyyawa and another LTL employee began nightly testing of the software. This testing continued over the following 15 days, up to 2 August. He said when Mr Forman attempted to fix bugs and errors they identified, other features in earlier versions of the software would then break and not work the next night.

[63] On 1 August Mr Forman gave notice of his resignation to Mr Kirimetiyyawa but assured him he would stay and finish the key project. The client had agreed to extend LTL’s delivery date until 8 August. On 8 August the client’s information technology director complained to Mr Kirimetiyyawa, saying the key project was the worst piece of work LTL had done for the client in 20 years. The client’s director complained that the code was not complete and features in earlier versions were now missing.

[64] Mr Kirimetiyyawa’s inquiries into those circumstances led to him reading the instant messages between Mr Forman and Mr Kang, including references to BMSL. He then searched for information about that company on the Companies Office website and reported his findings to Mr Eade.

[65] LTL said the problems caused by what it considered to be Mr Forman's lack of attention to the key project included a long delay before it got another development project from that client and extra costs in fixing the key project. Those costs were said to include the expense of getting a senior developer, seconded from a related business founded by Mr Eade, to work for three days to complete the key project. LTL also had two developers work on migrating data and fixing errors during the following months.

[66] LTL said it billed its client for the \$12,000 budgeted for the key project but its actual costs totalled \$30,000.

[67] Mr Forman accepted he initially estimated the key project would need 80 billable hours but said he later revised that estimate to 200 billable hours. He said it was impractical to complete the project by scheduling a guaranteed 40 hours of development work each week for five weeks along with his other office and client responsibilities as a team leader. He also accepted he had been "overconfident". He said he had not previously experienced failure on a project and thought he could handle it although he had not previously been responsible for a fixed time, fixed budget project. His previous work for that client had been on small updates or new programmes. The key project was larger and needed more work done to change the style of its existing code base. He admitted he ended up "cutting corners" to get the platform ready for testing but denied problems with the project were the result of working on ProjoMojo instead.

[68] LTL sought damages totalling \$63,654 said to reflect its costs in remedying Mr Forman's poor performance on the key project. This included \$5,520 for three days of Mr Kirimetiya's time, \$3,600 for three days of Mr Forman's time, \$9000 for the time of the senior developer from Mr Eade's other business, \$27,525 for the time of two other LTL developers and a supposed \$18,000 credit applied to the client's account.

[69] However LTL's claim of a breach of duty by Mr Forman, with a consequent liability for damages, was not sufficiently established for the following four reasons.

[70] Firstly, the evidence did not compellingly establish, as more likely than not, that Mr Forman failed to be diligent and failed to use his two years' experience and knowledge as a developer in carrying out his work on the key project. He did spend

some work time on messaging Mr Kang and exchanging ideas about their business plans. However those messages also revealed he spent additional time and worked late on the key project and other client work he was expected to complete.

[71] Secondly, even if it were accepted he had breached that duty, there was a break in the chain of causation between any such failure and the loss. This break in the causal chain was the knowledge Mr Kirimetiya had at a quite early stage about problems and delays. On his own evidence about the 1 July weekly conference call with the client, Mr Kirimetiya knew Mr Forman was struggling by then on completing the key project. He accepted Mr Forman's assurances but there was no significant follow-up or check on progress that might have been expected from a general manager overseeing a project for what he said was "a very important client" who had generated "millions of dollars in fees over the years". Mr Kirimetiya was then involved from 18 July to 2 August with a daily testing programme that revealed ongoing problems.

[72] Mr Kirimetiya knew about the problems with the key project for more than a month before the 8 August complaint by the client. In his oral evidence he accepted those difficulties were unusual in his experience of Mr Forman, whose work was previously of a high standard. He could have acted earlier, but did not, to closely examine what was causing the problems and arrange additional resources or attention to address them. What LTL did later to supposedly address shortcomings in Mr Forman's work could have been done sooner and with less negative consequence on its relationship with its client. Those consequences were reasonably foreseeable to Mr Kirimetiya but he had not act prudently by doing more to avoid or minimise them from when he became aware of their extent on 1 July and from 18 July.

[73] Thirdly, there is reason to doubt whether an employer may sue an employee for negligent performance of their duties, as noted by the Employment Court in *George v Auckland Council*:⁵

... [I]t is strongly arguable that in the modern context of employment relationships in New Zealand, and in light of the mutual obligations conferred on the parties under the Act, an employer may not seek to recover damages from an employee arising from acts of negligence committed during the course of their duties. If it were otherwise it would likely have a chilling effect on the way in which employees undertake their duties, could lead to

⁵ [2013] NZEmpC 179 at [147].

reactive claims or threats of claims against those taking personal grievances which would undermine the statutory framework for resolving employment relationship issues, and expose employees to significant potential financial liability for a breach even in circumstances that could never justify a dismissal. It also raises policy concerns about the fair allocation of risk and which party is best placed to mitigate potential liability.

[74] In LTL's case the risk was fairly allocated to LTL and its general manager, Mr Kirimetiya, who was aware of the problems and did not act to investigate and potentially solve them sooner.

[75] Fourthly, LTL's claim for what it said were its subsequent remedial costs was so inflated and exaggerated that it lacked credibility. A supposed credit of \$18,000 to the client was the result of a mistakenly sent invoice. A supposed \$3000-a-day cost for the senior developer seconded from Mr Eade's other business was fairly described in Mr Forman's closing submissions as "plucked out of thin air". It was based on what Mr Eade accepted was a "nominal" hourly rate.

Liability of Mr Kang – the alleged breaches

[76] LTL sought findings that Mr Kang breached the terms of his former employment agreement by:

- (i) contrary to clause 43.1, soliciting Mr Forman to leave his employment with LTL; and
- (ii) contrary to the restraint of trade provisions in clause 44.1, establishing or obtaining an interest in a business.

[77] It also sought a finding that Mr Kang aided and abetted Mr Forman's breaches of his employment.

(i) Solicitation – a breach of clause 43.1?

[78] The employment agreements of Mr Kang and Mr Forman had the same restraint of trade provision at clause 44.1, set out earlier in this determination. The non-solicitation clause was:

43. Non Solicitation

- 43.1 The Employee shall not at any time during the period of employment or for a period of six months after termination of employment, for whatever reason, either on the Employee's own account or for any other person, firm, organisation or company, solicit, endeavour to

entice away from or discourage from being employed by the Employer, any other employee or actual client/customer or prospective client/customer of the Employer.

[79] The six month period during which the non-solicitation and restraint trade clauses applied to Mr Kang after he left LTL's employment ran to 9 April 2016.

[80] The witness statements of Mr Forman and Mr Kang said they had "started talking seriously" in March 2016 about developing project management software, after first discussing the idea in January 2016. Their 26 February and 3 March message exchanges, set out earlier in this determination, showed they were discussing details about the business they hoped to established. When questioned at the Authority investigation meeting Mr Kang gave various answers about where the initiative for their plans came from. He denied he had approached Mr Forman and said it was "a joint effort to explore ideas" but also said he "broached the subject". He said he had "initiated a conversation".

[81] He accepted he had also talked with Mr Forman about whether they had the same terms in their employment agreements, including the restraint of trade provisions. Mr Kang said this conversation as occurred "around May-ish". His vague recall somewhat conveniently put the timing of that conversation after the 9 April date that his restraint period ended. It was not convincing evidence in the context of the other evidence from him and Mr Forman and what they had said in instant message exchanges before then.

[82] On the balance of probabilities Mr Kang had, before 9 April 2016, solicited Mr Forman to leave his employment so they could go into business together once Mr Forman developed a product to sell. Mr Forman decided to stay in LTL's employment meanwhile so he could continue to pay the mortgage on his house. Mr Kang's discussions with Mr Forman about business plans had however, in effect, traded on a relationship he had developed with Mr Forman through working at LTL. He was contractually bound not to take advantage of such relationships within the proscribed six month period. He had breached the non-solicitation clause because he had endeavoured to entice Mr Forman away from his employment with LTL.

(ii) Breach of restraint of trade?

[83] Mr Kang had not, however, breached the terms of the restraint of trade in clause 44.1. The reasons for that conclusion are the same as those given earlier in this determination about whether Mr Forman's activity breached that same term. Their preparatory activities, in registering the company and developing the website, were not yet a "business" and the product Mr Forman was developing was not in competition with LTL's planned or actual business at the time.

(iii) Aiding and abetting breaches by Mr Forman?

[84] Of the six breaches of duty LTL alleged Mr Forman committed, this determination has found only one was established – undertaking private work without LTL's written permission. The evidence for the breach was found in the instant messages between Mr Forman and Mr Kang. Mr Kang took part in those exchanges so the question for resolution was whether being a participant in the conversations amounted to aiding and abetting Mr Forman's breaches? If it was, Mr Kang would be liable for a penalty under s 134(2) of the Act.

[85] The messages were exchanged on the Skype for Business application. They comprised just over 30 A4 pages of the documents provided for the Authority investigation. They were sent on dates between 11 February and 20 July 2016. In the first message, sent at 6.29 pm on 11 February Mr Kang suggested Mr Forman go home but Mr Forman replied he would be working until about 8pm as he had not arrived at work until 10.30am.

[86] On the last day of these messages, on 20 July, Mr Kang suggested Mr Forman might want to use a "chat app" called Line rather than Skype for Business. His reason for that suggestion was found in a following message he sent that (as written) read: "SFB data belongs to lct". He was explaining that the messages they exchanged on LTL's internal system, which used the Skype for Business application, could be read by LTL. He wrote that message in response to a message from Mr Forman that read: "Just assume that all my conversations with you are not for lancom eyes unless they view my messages which is rude". Mr Kang then told Mr Forman to "just jump on skype, don't use skype for business". The last message in this evidence, from Mr Forman to Mr Kang, read: "I'm on my own skype". Whatever exchange they then

had could not be accessed by LTL and was not part of the evidence in the Authority investigation.

[87] It was clear from those messages, and others they exchanged during the intervening days, that Mr Kang was aware Mr Forman was at work for LTL at the times they were communicating through that medium. Mr Kang initiated many of those exchanges. Their messages contained multiple references to other LTL staff, including whether or not Mr Kirimetiwaya was in the office at the time.

[88] Exchanges that were merely social chatter, such as plans for after work events or gaming activities, could be put aside as falling within the margin Mr Eade had accepted as tolerable for such communication by employees in working hours. However, in light of the finding that some of their exchanges were for the purpose of advancing their private plans for a business, those communications from Mr Kang aided and abetted Mr Forman's breach of his obligation not to do private work in time paid for by LTL. The fact of the breach, and its private purpose, was not negated Mr Forman's submission that the exchanges took only a matter of minutes on various days and that he was doing other LTL work at the same time.

Penalties

[89] On the findings made in this determination:

- (i) Mr Forman was liable to a penalty for breaching clause 30 of his employment agreement by conducting private work in LTL's time without written permission; and
- (ii) Mr Kang was liable to a penalty for breaching clause 43 of his employment agreement by soliciting Mr Forman away from his employment with LTL and, under s 134(2) of the Act, for aiding and abetting Mr Forman's breach of duty to LTL.

[90] The breaches occurred at various times between January and August 2016. The factors for determining whether to impose penalties for those breaches, and the level of each penalty, could be drawn from s 133A of the Act, applying from 1 April 2016, and earlier case law.⁶ For this determination, the factors considered were:

- (i) The seriousness or gravity of the breaches; and

⁶ See *Borsboom v Preet PVT Ltd* [2016] NZEmpC 143 at [5]-[6].

- (ii) Whether the breaches were one-off or repeated and were deliberate rather than technical and inadvertent; and
- (iii) The impact on and any harm caused to LTL; and
- (iv) The vulnerability of LTL; and
- (v) The need for deterrence; and
- (vi) Whether Mr Forman and Mr Kang showed any remorse or took any steps to mitigate actual or potential adverse effects of the breach; and
- (vii) The range of penalties in comparable cases; and
- (viii) The totality principle and ensuring a proportionate outcome was reached.

[91] Mr Forman and Mr Kang acted deliberately in their preparations for a future business. The parts of that activity that breached their respective duties were repeated during the period, specifically by the instant messages that comprised unauthorised private work by Mr Forman and in which Mr Kang abetted Mr Forman's breach of duty. However those activities could reasonably be seen as a single course of conduct, thus being a one-off breach and treated globally. Their respective breaches were serious and of some gravity because they each broke contractual obligations of importance to LTL's business. LTL relied on employees, or former employees, honouring their agreements.

[92] Discovery of, and inquiry into, the activities through which the breaches occurred required Mr Eade and Mr Kirimetiya to spend management time that they would otherwise likely have spent on other more productive work. LTL also sought an award of special damages on that basis. The cost of that time has been treated in this determination as a factor relevant in the assessment of penalties only, and not double counted by also awarding special damages.

[93] The harm caused to LTL by the breaches included the cost of legal fees incurred for attendances about the issue prior to the commencement of proceedings. Those fees were also the subject of a claim for special damages but have been treated in this determination as a factor only relevant to the assessment of penalties and not double counted for any other purpose. If it were otherwise, those legal fees would have fallen in what the Court of Appeal in *Binnie v Pacific Health Limited* described as the blurred margins between special damages and any party to party costs that

might be due in this particular proceeding.⁷ There was no bright line between such damages and costs as Mr Eade had, from 15 August, talked about litigation.

[94] The harm of the extra time and effort LTL said was incurred in fixing the key project has already been considered in respect of its claim for damages. It was not relevant in respect of the breaches being considered for the purpose of an assessment of penalties.

[95] LTL relied on the terms of its employment agreements so was vulnerable in the event that those terms were deliberately breached. However, the particular breaches for which Mr Kang and Mr Forman were liable to penalties caused no direct commercial harm to LTL, such as loss of sales or other business. Mr Forman's resignation resulted from Mr Kang's solicitation to engage in their planned business but he may have left in any event, to travel or pursue other career opportunities.

[96] Employment agreements are made to be kept, by both parties. A penalty was warranted to deter other parties breaching such terms in future.

[97] As both Mr Forman and Mr Kang denied they had committed any breaches, neither showed any real remorse for them. Mr Forman, however, had in meetings with LTL on 15 August and 7 September 2016 attempted to mitigate LTL's concerns, including by handing over the PromoMojo software. He also provided a statutory declaration confirming he had returned all copies of any Lancom information.

[98] Also relevant was that neither man had, on any evidence available to the Authority, ended up profiting from their activities. Their business plan for ProjoMojo appeared to have been entirely fruitless.

[99] The stress and cost of having been involved in subsequent Authority proceedings would probably deter either man repeating such breaches in other employment in the future, however a penalty was appropriate to deter others from breaching such obligations. Both men were, at the time of the Authority investigation meeting, in paid employment. Mr Forman also had a significant asset in the form of a house. They each had means to meet a penalty.

⁷ [2002] 1 ERNZ 438, at [18].

[100] Balancing those factors, and considered against the range of penalties awarded in comparable cases, \$4000 was an appropriate and proportionate penalty for Mr Forman to pay for his breach of duty. The amount of \$4000 was also an appropriate and proportionate penalty for Mr Kang to pay for his solicitation of Mr Forman and aiding and abetting Mr Forman's breach of duty. Those amounts would likely deter others from committing such breaches.

[101] LTL sought an order directing any penalty ordered be paid to it, not the Crown.⁸ LTL bore whatever harm resulted from the established breaches by Mr Forman and Mr Kang. They breached terms of their employment agreements, not statutory duties. Those two factors supported making the order sought. Mr Forman and Mr Kang must pay the penalties ordered directly to LTL within 28 days of the date of this determination.

Costs

[102] Costs are reserved. The parties are encouraged to resolve any issue of costs between themselves. In light of the mixed result for the parties on both sides of this proceeding, they may be able to do so on the basis that costs lie where they fall.

[103] If they are not able to resolve any costs issue, and an Authority determination on costs is needed, whichever party or parties consider they are entitled to an award of costs should lodge and then serve a memorandum on costs within 14 days of the date of issue of this determination. Replies to any memoranda lodged should be made within 14 days of the date of that service. Costs will not be considered outside this timetable unless prior leave to do so is sought and granted.

[104] The parties could expect the Authority to determine costs, if asked to do so, on its usual notional daily rate unless particular circumstances or factors required an upward or downward adjustment of that tariff.⁹

Robin Arthur
Member of the Employment Relations Authority

⁸ Employment Relations Act 2000, s 136.

⁹ *PBO Ltd v Da Cruz* [2005] 1 ERNZ 808, 819-820 and *Fagotti v Acme & Co Limited* [2015] NZEmpC 135 at [106]-[108].