IN THE EMPLOYMENT RELATIONS AUTHORITY
AUCKLAND

AA 311/10
5305939

	BETWEEN	SHEPPARD INDUSTRIES LIMITED Applicant
	AND	ADAM MARSHMENT Respondent

Member of Authority:	R A Monaghan
Representatives:	T Allan, counsel for applicant R Upton, counsel for respondent
Investigation meeting:	28 June 2010
Determination:	02 July 2010

DETERMINATION OF THE AUTHORITY
ON INTERIM APPLICATION

Employment relationship problem

[1] Sheppard Industries Limited (SIL) says its former employee Adam Marshment has breached the terms of restraint of trade, confidentiality and conflict of interest provisions in the parties' employment agreement by, among other things, entering into an employment relationship with a competitor, Specialised Bicycle Corporation Limited (Specialised).

[2] SIL seeks: an injunction or compliance orders requiring Mr Marshment to comply with the above provisions; damages; and penalties for his alleged breaches of the provisions. Those matters are to be heard at an investigation meeting scheduled for 5 and 6 August 2010. Resourcing issues currently facing the Authority meant that, even with a grant of urgency, it was unable to schedule the substantive matter any sooner than this.

[3] Accordingly SIL sought an interim order restraining Mr Marshment from working for Specialised pending the resolution of the substantive matters. The parties have attended mediation and have been unable to resolve the problem either on an interim or permanent basis.

[4] This determination addresses the application for interim orders. It does so with reference to:

(a) whether the applicant has an arguable case;

(b) the balance of convenience including the adequacy of damages as a remedy; and

(c) where overall justice lies.

Background

[5] SIL is in the business of manufacturing and assembling bicycles and accessories. It has its own brand, Avanti, and holds or has held agency or distributorship arrangements with other leading international bicycle manufacturers.

[6] One such arrangement was an exclusive distributorship agreement with Specialised - a US-based company which manufactures bicycles of a kind normally ridden by elite cyclists in international cycling events and which are referred to as 'high end' bicycles.

[7] SIL considered the Specialised brand to be a premium brand and critical to the success of its retail dealerships. Its chief financial officer, Paul Schnell, deposed that the cycling market is particularly sensitive and brand conscious, especially in response to high end brands, and that it responds to the success of high end brands in major international cycling tours such as the Tour de France. A manufacturer with a brand used in any of these tours in likely to have a significant market following.

[8] In or about 2009 Specialised sought to enter the Australasian market on its own account, having not previously traded in that market in that way before. Disputes between SIL and Specialised led the companies to enter into a Deed of Settlement Amending Exclusive Distributorship Agreement in August 2009 (the Deed). Under

the Deed: in February 2010 the parties would announce a parting of the ways; and from May 2010 Specialised would be permitted to sell model year 2011 (MY 11) and subsequent products directly in Australasia while SIL would be permitted to sell high end bicycles and accessories sourced from other suppliers. The distributorship would end completely on 31 August 2010.

[9] SIL believes Specialised has been positioning itself since September 2009 to springboard into competing directly with it when the distribution agreement ends as set out in the above summary. It says Specialised does not have its own dealership network, and sought to employ an SIL sales executive named Tony Smith. The employment agreement between SIL and Mr Smith also contained a restraint of trade provision. Mutually threatened High Court action in respect of other matters resulted in a commercially-mediated settlement which included a term permitting Mr Smith to enter into employment with Specialised. Further litigation has followed that settlement. Specialised's move into Australasia is being taken very seriously by both parties, and is hard fought.

[10] For his part Mr Marshment was employed as an account manager with SIL, commencing in 1998. In the period immediately preceding Mr Smith's departure, Mr Marshment reported directly to Mr Smith. Mr Marshment operated in the wholesale market selling to cycle stores in the central North Island excluding Hamilton.

[11] According to Mr Schnell, Mr Marshment is privy to sensitive commercial information about the development of the Specialised brand and SIL's growth in the last decade. Mr Schnell deposed that some of this information is among the most critical necessary to persuade dealers whether to remain with SIL or move to Specialised. He referred in particular to dealer buying patterns, pricing structures, the idiosyncrasies of individual dealers, product development, some strategic direction of product, strategic marketing initiatives for the next two years and target markets for growth.

[12] Mr Marshment described his role as pretty typical for a salesperson. He deposed that he never felt he received anything strategic or groundbreaking, rather the information he received was typically about the products to be sold. He did, however, accept that he was exposed to the occasional marketing strategy, product decision or

detail which he assumed was confidential until it was delivered to the market. He added that since he left SIL he has not been exposed to that information.

[13] Mr Marshment resigned from his employment on 23 February 2010, effective 26 March 2010, intending to take up a sales position with Specialised. He advised his then-manager, Rene Verhoeven, of this intention and was placed on garden leave. The arrangements were confirmed in a letter to Mr Marshment dated 2 March 2010, which also reminded Mr Marshment of clauses 26, 28 and 29 and warned him the SIL considered his planned employment to be in breach of the restraint of trade.

[14] Further correspondence followed in which, among other things, Mr Marshment offered undertakings regarding confidentiality which have not been sufficient to satisfy SIL's concerns. Mr Marshment commenced work at Specialised on 6 April 2010 but deposed that since then he has worked from home carrying out essentially administrative tasks.

[15] With reference to events after Mr Marshment's employment at Specialised began, Mr Verhoeven deposed that Cyclezone Rotorua Limited (Cyclezone) was a key account serviced by Mr Marshment, and part of the exclusive AvantiPlus dealer network. It was known that Cyclezone was vacillating between remaining an AvantiPlus dealer or switching to Specialised. According to Mr Verhoeven, at a dealers' meeting on 5 May 2010 Cyclezone's principal owner and director Bryce Shapley, indicated that Mr Smith and Mr Marshment had been applying pressure to him to enter into an agreement with Specialised. Subsequently Mr Shapley declined to sign a proposed replacement dealership agreement and resigned from his existing dealership. Meanwhile he had become privy to confidential information shared with dealers at the 5 May meeting. SIL says this is relevant to Specialised's attempts to springboard into the market, and is the kind of problem the restraint of trade was intended to prevent.

[16] Mr Shapley denied that his decision had anything to do with Mr Marshment and deposed that in his recent limited encounters with Mr Marshment, whom he has known for a number of years, Mr Marshment has been very circumspect. In particular, Mr Marshment has not sought to solicit his business on behalf of Specialised.

Relevant provisions in the parties' employment agreement

[17] Relevant provisions in a written employment agreement between SIL and Mr Marshment dated 10 August 2005 read as follows:

> "25. Restraint of Trade
>
> 25.1 The Employee is entrusted with responsibility and has the ability to build up substantial knowledge and expertise in the course of his/her employment in the Employer's business.
>
> The Employee recognises the Employer's unique processes used in its business and the fact that it operates throughout New Zealand and Australia.
>
> 25.2 The Employee agrees that he/she shall not during the term of this agreement and for a period of six months after its cessation for any reason
>
> > Be directly or indirectly interested or engaged or concerned in (including the use of confidential information) or assist financially in any way, whether on his/her own account or as principal, employee, agent, partner, member or director, trustee, shareholder, representative, consultant or any other capacity, in any enterprise carrying on business in direct or indirect competition with that of the Employer or in any business or activity associated with the Bicycle industry and more specifically the import or design or marketing or assembly or distribution or retail sale of bicycles (except with the written consent of the Employer).
> >
> > Solicit any business or endeavour to entice away from the Employer or in any way approach any director or employee or consultant of the Employer or Company or other person (whether or not such person would commit any breach of contract or terms of employment by leaving) nor the custom of any person who is an existing client or customer of the Employer or who has been contacted by the Employer during the Employee's employment, and nor shall the Employee knowingly comply, aid or assist in the procurement of such employees or clients or customers by any person, firm or company with which the employee is associated.
> >
> > The term 'existing client or customer of the Employer' includes not only present clients or customers but also those who have been clients or customers within the six months period prior to the cessation of this agreement.
>
> 25.3 Both the Employer and employee consider these restrictions to be reasonable in all the circumstances. However if a court of competent jurisdiction finds any of them to be

unenforceable, both the Employer and Employee agree to accept any modification of the area, extent or duration of the restriction concerned which the Court sees fit to impose, or if it does not see fit, which may be required, to make the restriction enforceable.

25.4 The Employee shall keep confidential and shall not use any information relating to the Employer's business, technical processes, designs or intellectual information relating to patents or pending patents or registered trademarks after the Employee's termination of employment.

25.5 The Employee acknowledges that the remuneration and other terms of this Agreement shall form the consideration of this provision.

28. Confidentiality

28.1 Except in the proper performance of the employee's duties he/she shall not at any time use or divulge to any person any knowledge or information which he/she may acquire during the course of his/her employment by the Company concerning the business, operations, affairs, property, customers, clients, suppliers, employees and principals of the Company.

28.2 This restriction shall continue to apply after the termination of employment without limit in point of time, but shall cease to apply to knowledge or information which may become public knowledge or a matter of public record without breach by the employee of this restriction.

…

29. Conflict of interest

29.1 The Employee shall refer all business contacts and all ideas, inventions and opportunities of which the Employee becomes aware and which relate to the business of the Company or of its principals and shall not establish himself or herself or engage in private business or undertake other employment in competition with the Company's business without the written consent of the Company.

29.2 Failing to seek such consent or engaging in other employment without the Company's consent will be considered serious misconduct."

Arguable case

[18] On the presently available material the issues likely to arise in the substantive hearing include whether:

(a) there was consideration for the restraints entered into in the 2005 employment agreement;

(b) the restraints were reasonably necessary to protect a proprietary interest of SIL's;

(c) with reference to that interest and viewed as at the time of entry into them, the restraints were reasonable in terms of, -
. the nature of the activity to be restrained,
. the geographical coverage of the restraint, and
. the period of restraint;

(d) Mr Marshment has breached the terms of the restraints to the extent that they are reasonable; and

(e) Specialised is seeking to springboard directly into competition with SIL, part of which includes the securing of key SIL staff.

[19] These issues are principally concerned with clause 26 of the parties' employment agreement. Clauses 28 and 29 were not directly the subject of allegations or submissions.

1. Consideration for the restraints

[20] Mr Marshment deposed that, although there was a restraint of trade provision in a previous employment agreement between himself and SIL, the 2005 provision was a variation not supported by consideration and is not enforceable. However he was not able to provide a copy of the earlier agreement, or identify the variation.

[21] If I decided this point against SIL I would in effect be determining the bulk of its substantive claim. In any event I do not accept that a restraint provision in another person's employment agreement was likely to be the provision also previously applicable to Mr Marshment. Without the earlier agreement between SIL and Mr Marshment, or information about the circumstances of the change (if any) in 2005, I do not take this issue into account in determining whether the orders sought should be granted. It will, however, remain to be argued during the substantive investigation if Mr Marshment wishes to pursue it.

2. Proprietary interest

[22] SIL says it has a proprietary interest in its relationships with its dealers. The background as I have set it out is sufficient for an arguable case that is so.

3. Reasonableness of the terms of the restraints

[23] The first sentence in clause 25.3 of the employment agreement asserts the parties' agreement that the restrictions are reasonable. However that is not determinative of the matter, and the clause itself envisages a finding to different effect regarding reasonableness on the part of a court of competent jurisdiction. While the provision must be given some meaning, it remains open to assess whether it is arguable that the restraints are indeed reasonable despite the assertion.

[24] I turn first to the nature and extent of the activity restrained. It is strongly arguable that Specialised is carrying on business in direct or indirect competition with SIL, and accepted that Mr Marshment is its employee. With reference to the existence of the proprietary interest to be protected, it is strongly arguable that a restraint on activity of this kind is reasonable.

[25] Secondly, there is a question of the reasonableness of a six-month restraint. SIL said relatively little about the question, other than by reference to the seasonal nature of cycling events and the lead-in time necessary for the sales and marketing activity associated with them. However while the period might be at the upper end of a scale applicable to someone working at Mr Marshment's level it is at least arguable that a six-month restraint is reasonable, and I have no basis on which to assess what lesser period is the maximum that would be reasonable.

[26] Finally, there is no geographical limit on the restraint. Such lack usually lends itself at least to a modification of the kind suggested in the second sentence of clause 25.3. That matter was not developed for the purposes of the interim application, except to the extent SIL indicated an Australasia-wide restraint was expected. At the other end of the scale I observe that Mr Marshment deposed he has avoided activity within his former central North Island region but has already contacted stores in the lower North Island and upper South Island.

[27] Accordingly while a restraint applying without geographical limit is likely to be unreasonable, it is arguable that a modified restraint would be reasonable. No modifications were suggested, so I cannot take that matter any further.

[28] Finally, it is arguable that Cyclezone's business was obtained in breach of the restraint on soliciting business or custom away from SIL. I say this on the basis of the untested information provided about Cyclezone, and acknowledging that the matter of Cyclezone's business will no doubt be fully tested in evidence during the substantive hearing.

Balance of convenience and damages as a remedy

[29] Mr Verhoeven assessed damages with reference to the loss of Cyclezone, and cited a loss of $279,400 calculated over a three year period. SIL submitted that damages would be an appropriate remedy but for Mr Marshment's likely inability to pay. That inability meant the balance of convenience favoured it.

[30] Mr Marshment provided few details of his financial position but advised that he has two residential properties, one of which is rented, and gave information about the mortgages, current council valuations and income in respect of the properties. On that information at least he has valuable assets and is not impecunious, although the extent to which he has the resources to meet an order of the magnitude cited is debatable.

[31] Mr Marshment also produced a copy of a deed of indemnity between himself and Specialised. The deed is undated, but with certain qualifications it is expressed to cover any and all claims including damages and penalties brought against him by SIL in relation to the restraint of trade and allegations of breach of the restraint.

[32] Counsel for Mr Marshment submitted in turn that Mr Marshment has sufficient assets to meet a claim for damages, and referred to the likelihood that Specialised would indemnify Mr Marshment in respect of any order against him.

[33] SIL raised a concern about the enforceability of the indemnity if an award of damages was made in its favour, and Mr Marshment was unable to meet it. SIL

pointed out that Specialised is a US-based company and there was nothing to indicate it had assets in New Zealand capable of being applied to any order if the indemnity were enforced. It also raised a wider concern about the jurisdiction in which the indemnity would be enforced, although I note the indemnity provides that New Zealand law is to apply.

[34] Overall, I cannot say that Mr Marshment is likely to be able to meet an award of damages of the levels indicated, and it is arguable that he could not.

[35] Additional matters bearing on the balance of convenience concerned Mr Marshment's loss of opportunity to work for his chosen employer for several months in the event that an interim order is made, and it is subsequently found there was no breach. However Mr Marshment has been carrying out work for and receiving his salary from Specialised for the last three months, and any financial effect should that cease can in principle be compensated by an award of damages. In any event, there has been no suggestion that Specialised will stop paying Mr Marshment's salary for a period if an interim order is made and no suggestion that it will terminate his employment.

[36] Finally, the substantive matter is to be heard in five weeks. Any disadvantage or inconvenience Mr Marshment may suffer as a result of the grant of an interim order is likely to be short-lived.

[37] Therefore I find that the balance of convenience favours SIL.

Overall justice

[38] There is nothing to add to the above assessment. Overall I find SIL has an arguable case that Mr Marshment has breached the parties' restraint of trade, and that the balance of convenience tips in its favour.

Orders

[39] I have been asked to make an order restraining Mr Marshment from working for Specialised pending the resolution of the substantive matter, subject to any modifications to the restraint which I am not in a position to make.

[40] With reference to clause 26 of the agreement with SIL Mr Marshment is ordered to refrain from carrying out his obligations under the employment agreement with Specialised, and otherwise to observe the terms of the clause, pending the resolution of the substantive matter or the expiry of the period of restraint whichever is earlier. Mr Marshment and Specialised will need to address how this should be accommodated in terms of their employment relationship.

Costs

[41] Costs are reserved pending a determination of the substantive matters, unless the parties resolve the employment relationship problem themselves.

R A Monaghan
Member of the Employment Relations Authority