

## Forfeiture-for-Competition Clauses in Employment Contracts

In employment contracts, there is commonly a clause which prohibits an employee from working for a competitor upon termination of his employment. It has long been established that such a clause, commonly known as a "non-compete clause" or a "restraint of trade clause", must be shown to be reasonable in order to be enforceable. This principle of law was founded on public policy considerations which seek to strike a balance between an individual's freedom to work for himself or herself and not (in principle) to deprive himself of his or her labour or skills, while balancing the freedom of contract.

Over the years, remuneration packages and terms of employment have evolved to include, amongst other things, financial incentives for employees who remain with the employers and conversely, financial disincentives for the employee should he resign or join a competitor.

In this article, we highlight the recent case of **Mano Vikrant Singh v Cargill TSF Asia Pte Ltd** [2011] SGHC 241, where the Singapore High Court addressed the issue of whether a clause in an employee incentive award plan which forfeits deferred incentive payments in the event the employee resigns and competes with his employer (referred to as a "forfeiture-for-competition" clause) is in substance a restraint of trade clause.

The High Court ruled that forfeiture-for-competition clauses are not restraints of trade clause as they "do not prohibit the employee from competing with the employer." The forfeiture-for-competition clause merely sets out what the employee would have to forfeit should he choose to compete upon his resignation and as such, served to "operate as a financial disincentive for the employee to compete" after he leaves the employer. If the employee decides to compete upon leaving his employment with full knowledge of the financial disincentive, being the forfeiture of his deferred bonus, he would have made a calculated decision having evaluated the detriment of losing the deferred bonus against the gain in joining the competitor.

As the forfeiture-for-competition clause was not held to be a restraint of trade clause, the employer need not show that such a clause is reasonable in order to enforce it.

### Brief facts

In **Mano Vikrant Singh v Cargill TSF Asia Pte Ltd** [2011] SGHC 241, the plaintiff, Mr Mano Vikrant Singh (the "Plaintiff") had in addition to his employment contract with his employer Cargill TSF Asia Pte Ltd (the "Defendant"), also signed the following:-

- (a) a non-compete agreement wherein the Plaintiff agreed, inter alia, not to compete with the Defendant for a period of one year immediately following his termination of employment with the Defendant.
- (b) an individual incentive award plan (the "Incentive Award Plan"). The terms and conditions of the Incentive Award Plan (the "Incentive Award Plan T&Cs") provided that half of the individual incentive award would be paid out as a cash award and the remaining amount would be paid out as a deferred incentive. The Incentive Award Plan T&Cs contained a forfeiture clause which provided that the deferred incentives that have been awarded but not yet distributed will be forfeited if the Plaintiff competed with the Defendant within a period of two years from the date of his resignation.

The Plaintiff was awarded a bonus and the cash component was paid to him, with the remaining portion of the bonus deferred in accordance with the Incentive Award Plan T&Cs.

Shortly after the Plaintiff was awarded the cash component of the bonus and whilst still an employee of the Defendant, the Plaintiff incorporated a company ("X"). He subsequently resigned from his employment with the Defendant. Two years later, the Plaintiff demanded payment of the deferred portion of his bonus on the grounds that the forfeiture-for-competition clause was a restraint of trade which was unreasonable, and therefore void and unenforceable. The Defendant claimed that the Plaintiff in setting up a competing business in X, had breached the forfeiture-for-competition clause and was therefore not entitled to the remaining deferred portion of his bonus.

## Summary of the High Court Judgement

In ruling that the forfeiture-for-competition clause was not a restraint of trade clause, the High Court considered English and Australian cases as well as case law in the United States, though none of the decisions of the courts in these jurisdictions are binding on the Singapore courts. The High Court noted that English and Australian cases tended to regard forfeiture-for-competition clauses as restraint of trade clauses and therefore only enforceable if the employer can establish that such clauses are reasonable. The Singapore High Court noted that the legal position in the US on this issue was divided, but that the majority view in the US was that the restraint-of-trade doctrine does not apply to forfeiture-for-competition clauses. The common underlying rationale behind such a view was that a forfeiture-for-competition clause did not prohibit competition per se, and that the employee in such a situation had a choice, that being a choice to compete against his employer, although in making such the choice, it came with the consequence of forfeiture or denial of a benefit.

The High Court held that the forfeiture-for-competition clause merely contractually defines when the Plaintiff loses his entitlement to the deferred incentive payments and did not prohibit the Plaintiff from competing with the Defendant. In addition, the High Court noted that the Plaintiff had "a choice not to accept the Incentive Award Plan T&Cs which is separate and distinct from the Employment Contract and had a further choice having agreed to the Incentive Award Plan T&Cs to compete with the defendant after leaving the defendant's employment. The only consequence from the exercise of his choice to compete is that he has to be held to his bargain in forgoing his Deferred Incentive Payments."

The High Court was also persuaded by case law on "payment-for-loyalty" clauses which provide for the forfeiture of benefits if the employee resigns, even if the employee does not compete with the employer upon his resignation. Viewed in this context, the High Court held that in substance, payment-for-loyalty clauses are similar to forfeiture-for-competition clauses as both types of clauses provide a financial disincentive to an employee should he breach the conditions agreed. The Court noted that such payment-for-loyalty clauses have consistently been upheld by English and Australian courts as not being restraint of trade, the rationale being that such "payment-for-loyalty" clauses do not affect the employee's ability to work after leaving or with whom he might work for. In certain situations,

the loss of an inducement can even enable an employee headhunted by another employer, to negotiate more favourable terms in the new employment.

## Conclusion

Employers and employees will have to be mindful of the terms of the employment contract (taken in totality). The High Court's decision has highlighted the fundamental distinction between clauses which prohibit competition as compared to other clauses which do not prohibit competition but merely serve to define the financial benefits forfeited or given up should an employee resign and join a competitor.

If you wish to have further information on this update or wish to discuss how it may potentially have an impact on your business, please feel free to contact the following:



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