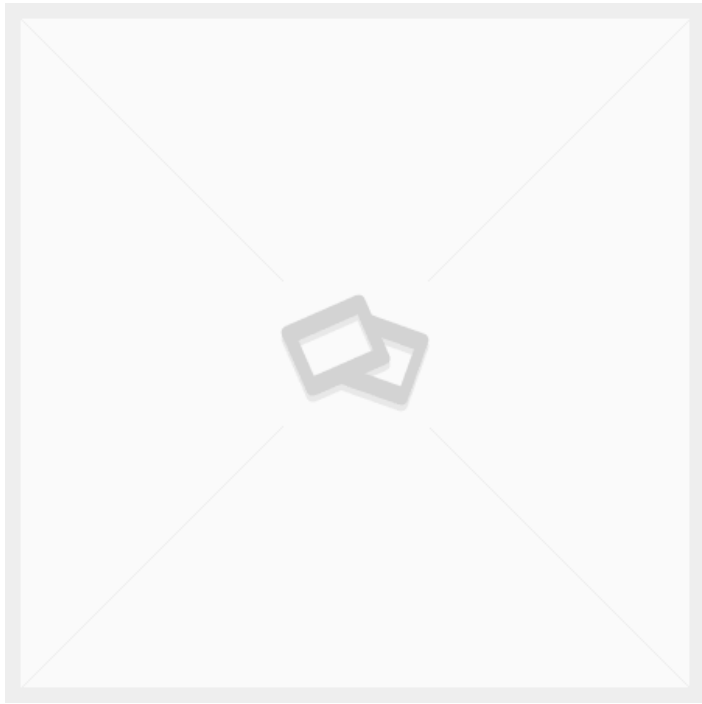


EMPLOYMENT LAW UPDATE ON RESTRAINT CLAUSES

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Category: [CNPupdates](#)



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Case note on Lek Gwee Noi v Humming Flowers & Gifts Pte Ltd

On 8 April 2014, the High Court of Singapore made a ruling regarding the width and enforceability of certain restrictive covenants in an employment contract. A summary of the case and its impact on drafting employment contracts are set out below.

Case Summary

Lek Gwee Noi (the "**Employee**") was employed as a sales manager at Humming Flowers & Gifts Pte Ltd (the "**Employer**"), a flowers and gifts company. In November 2011 the Employee resigned from the Employer and by December 2011 her notice period and employment came to an end. She later informed the Employer that she intended to set up her own business selling flowers and gifts. The employee was subject to an employment contract (the "**Contract**") which was signed by the Employee pursuant to an acquisition of the Defendant's business by Noel Gifts. The Contract contained express post-termination non-competition and non-solicitation covenants, which, the Employer reminded her, were terms she was subject to and the Employer threatened to sue her if she breached them.

The terms of the post-termination restrictive covenants prevented the Employee for 2 years from the date of termination from, amongst others things: (i) setting up a business similar to the Defendant's business in Singapore, Malaysia and anywhere else the Defendant may carry out business (the "**Non-Compete Covenant**") (ii) solicit orders from any person or company who was a customer of the "relevant Company" while the Employee was employed by the Defendant or from any customer of the Defendant (the "**Non-Solicitation Covenant**"). The Employee commenced proceedings to seek a declaration that these terms were void and unenforceable.

The decision of the High Court (the "Court")

The Court upheld the decision of the District Judge and dismissed the Defendant's appeal, holding that the restrictive covenants were void and unenforceable because, while there was a legitimate interest for the Defendant to protect, the restrictive covenants were not reasonable.

Legitimate interest

The threshold condition set by the common law is that restrictive covenants are not void if

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they protect a legitimate interest of the employer and they are reasonable in the interests of the parties and in the public interest. The legitimate interests the law considers are not finite but commonly include interests protecting trade secrets or confidential information, protecting a trade connection and protecting a stable, trained workforce.

The law takes a stricter approach in determining enforceability of restrictive covenants in employee contracts as opposed to those found in a sale of business contract because (i) an employee has less bargaining power (ii) the employee's only asset would be the ability to sell his labour (iii) a sale of business, without restrictive covenants, would be valueless to the purchaser where an employee provides continuous value to the employer whether or not it later competes with the purchaser (iv) on accepting a restrictive covenant the employer gains the bargaining power because the employee has limited ability to withdraw his services and seek employment elsewhere (v) it is in the public interest to permit employees to move freely within their labour market and use their skills as otherwise it would distort the labour market. These reasons were recently considered in the case of *Smile Inc Dental Surgeons Pte Ltd v Lui Andrew Stewart* SGHC 241. Our summary of this case can be accessed [here](#).

The Court approached the restrictive covenants as between an employer and an employee instead of as a business acquisition covenant, since the Employee was not a shareholder of the Defendant (thereby having no say in the acquisition of the Defendant), the acquisition of the Defendant was independent of the Employee's continued employment, the Employee did not receive any benefit from the acquisition apart from an insignificant increase in salary and the employee had no connection to the goodwill (i.e. the trade connection that attracts custom to a business) acquired in the Defendant.

In this case, it was found the Defendant had legitimate interests to protect because:

- the Employee, being a senior salesperson in the Defendant, was in a position to habitually handle confidential information so the Defendant had trade connections to protect.
- the Employee had access to confidential information of commercial significance, so, even if it did not amount to trade secrets, it was confidential enough to require the same level of protection as trade secrets.

Reasonableness of Non-Competition Covenant

However, the Non-Competition Covenant was not found to be reasonable. In determining the reasonableness of such clauses the court would consider (i) geographical restrictions (ii) activity restrictions. The geographical restrictions and activity restrictions would turn on the

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meaning of "**relevant Company**" in the Non-Competition Covenant. Since "**relevant Company**" was defined in the Contract to include any company in the Defendant's group of companies, it meant the Non-Competition Covenant would prevent the Employee from engaging in activities outside her scope of employment as long as any company related to the Defendant engaged in those activities as well. This was not found to be reasonable as it went beyond what was necessary to protect the Defendant's trade connection. The geographical restrictions extended to Malaysia where the Defendant had no business interests, which again made the Non-Competition Covenant unnecessarily wide.

Reasonableness of Non-Solicitation Covenant

The Court held that the Non-Solicitation Covenant extended to prevent the Employee from soliciting orders from customers of all the companies within the group of companies related to the Defendant even if her connection with those companies was purely incidental and she had no trade connections with the customers of those companies. The Non-Solicitation Covenant also prevented the Employee from taking away the business of "any" customer of the Defendant thereby protecting those customers who became customers even after the termination of the contract, even if the employee could not possibly have a trade connection with such customers. The Court also found the two years restriction unreasonably long given the legitimate interest it was seeking to protect. The purpose of such restraints is to prevent a departing employee from relying on his trade connection to draw customers away from the employer for a reasonable period of time and for the employer to be given the breathing space it needs to transfer that trade connection to its other employees. The Court found that while the Employee did exercise influence over the Defendant's customers, it found 1 year was enough to rebuild these trade connections.

Implications of this case

This case reminds employers and lawyers hired to draft employment contracts to cater the terms of the restrictive covenants to the nature of employment, considering factors like the employee's position in the company and the employee's scope of work. The restrictive covenants, in this case, may have been more applicable to an employee in a higher ranking position than a sales manager or an employee who was engaged in work with companies related to its employer. Practitioners and employers should also consider the reasonableness of the length of any restraint period based on the strength and persistence of the trade connection or trade secret it seeks to protect and the time taken to build and cement a new trade connection (which in turn depends on the industry, life cycle of trade connections and the role of the departing employee in the employer's business).

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