Non-compete clauses – a legal update

The judgment of the Court of Appeal in the recent case of Boydell v NZP Ltd is a timely reminder of the extent to which courts are prepared to strike-through or delete certain parts of post-termination non-compete restrictions in order to render them enforceable.

Case background

Dr Boydell worked as Head of Commercial – Speciality Products for NZP Ltd. The company operated within a niche area of the pharmaceutical sector.

Dr Boydell resigned and went to work for NZP's main competitor which prompted NZP to apply to the court for injunctive relief to prevent him from working for its competitor for the duration of his 12 month non-compete clause.

The non-compete clause in Dr Boydell's contract of employment prevented him from being involved in any activity for the benefit of any third party that carried out any business which would complete with the business of NZP or any other company in the group.

The High Court granted NZP an interim injunction enforcing the non-compete clause. In doing so, the Judge severed or struck-through certain parts of the clause, including removing the reference to "other group companies". This decision was appealed by Dr Boydell who argued that the Judge could not use severance to significantly change the effect of the restraints.

Legal position

A post termination restrictive covenant will be void for being in restraint of trade unless an employer has a legitimate proprietary interest to protect and the protection that is sought is no more than is reasonable having regard to the interests of the parties and the public interest.

When courts assess the reasonableness of a non-compete restriction, they should consider whether some lesser form or protection, such as a non-solicitation, non-dealing or confidentiality provision would give an employer sufficient protection.

Courts are permitted to "sever" or strike through any unlawful words from a restrictive covenant that would otherwise be too wide in order to create an enforceable restriction, however they are not permitted to, essentially, re-write the covenant.

In the case of Tillman v Egon Zehnder Ltd which we reported on in 2019, the Supreme Court loosened the severance test quite significantly, ruling that the severance of certain parts of a restriction would only be inappropriate if it caused a major change to the overall meaning and effect of the restriction.

Court of Appeal Decision

In the recent case, Dr Boydell's main points of appeal were that:

- The decision of the High Court to sever the group company wording significantly changed the nature of the restraint contrary to the principles in the Tilllman case; and
- Even if the severance of those words was allowed, the non-compete clause was too wide to be enforceable in any event.

The Court of Appeal rejected Dr Boydell's appeal. It found that:

- the High Court was entitled to sever the group company wording from the clause. It found that if a non-compete clause covered what it needed to and what was contemplated by the parties but also unintentionally covered areas which were "fantastical" then it may still be valid. It stated that if there were two realistic constructions of a clause, then the court should rely on the one which would result in a valid clause. In this case it meant that the removal of the "fantastical" part of the restriction (i.e. the reference to group companies) by the High Court was permissible as it had not changed the overall effect of the clause; and
- The clause was not too wide to be enforceable after severance. Where an employer is a large public company with multiple areas of activity, a wide covenant may be difficult to justify. However, this is less likely to be the case where an employer has a particularly niche or specialised business.

Comment

Employers might think that this case gives them carte-blanche to draft employment restrictive covenants more widely than they would have done before, in the knowledge that certain parts could still be deleted by the courts and ultimately enforced. However, we would still recommend erring on the side of caution and obtaining expert legal advice before including post-termination restrictions in employment contracts or seeking to take steps to enforce them.

In reality, an employer will be in a much more favourable legal position if it can point to a reasonably drafted clause that is capable of enforcement without alteration in the first place rather than seeking to rely on severance to improve its position as a last resort.

It is worth noting that a consultation instigated by BEIS on measures to reform post-termination non-compete clauses in employment contracts, including possibly banning them altogether, closed on 26 February 2021. We currently have no indication from the government about a timescale for its response to this consultation. Whilst we consider it unlikely that non-compete clauses will be banned altogether, we do believe that some sort of reform is inevitable. Options that may be considered are the introduction of a statutory restriction on the maximum length of a non-compete clause or the introduction of legislation that would require employers to compensate employees for the duration of a non-compete clause if they wish to enforce one, as is currently the case in Germany, France and Italy.

Watch out for further legal updates on this topic in the future.

How we can help

If you need guidance on non-compete clauses please get in touch with our employment team.

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