Personal service

2.32 For there to be a contract of employment, the worker must agree to provide his own services rather than those of another. However, an independent contractor is also perfectly free to agree to provide his own services and many will do so (eg artistes such as opera singers).

Control and organisation

2.33 The greater the degree of control that can be exercised by the business over the worker in terms of how, when and where he performs the task and how he organises himself, the more likely the contract is to be one of employment. Conversely, the more autonomy the worker has, the more likely he is to be an independent contractor: *Addison v London Philharmonic Orchestra* [1981] ICR 261.

Form of documentation

2.34 The form, as distinct from the content, of the documentation recording the terms of the contract may suggest the type of contract. The fact that an agreement is called a 'Consultancy Agreement' or 'Agreement for Services', avoids use of the terms 'employer' and 'employee' and contains terms consistent with a contract for services will be evidence that it is indeed such a contract. On the other hand, any of the following documents will be evidence of a contract of employment: an agreement entitled 'Service Agreement' in a form consistent with a service agreement; a statement supplied pursuant to section 1 Employment Rights Act 1996 and a memorandum under section 228(1) Companies Act 2006.

Reimbursement of expenses

2.35 Such a term is generally indicative of a contract of employment; an independent contractor normally agrees an all-inclusive price for his work. However, as with personal service (see 2.32), reimbursement of expenses is not necessarily inconsistent with a contract for services.

1(d) The power of the parties to dictate the status of the contract

2.36 There are potential advantages to both parties if the contract under which the individual works is a contract for services. The individual will normally gain the benefit of being taxed under Schedule D, whereas the business will avoid having to operate PAYE and will have none of the obligations imposed by statute exclusively on an employer (although obligations applicable to the broader concept of 'worker' – for example to give paid holiday – may still be applicable). The temptation, therefore, for parties to describe their contracts as contracts for services is great. However, describing a contract in this way will be ineffective if the contract is really one of employment – the parties cannot avoid the legal consequences of the employment relationship merely by attaching a different label to the contract: *Young and Woods Ltd v West* [1980] IRLR 201; *Consistent Group*

Ltd v Kalwak [2008] IRLR 505; and *Protectacoat Firthglow Limited v Miklos Szilagyi* [2009] EWCA Civ 98 (CA). However, where the contract could genuinely be either a contract of employment or a contract for services, then it is quite legitimate for the parties to so organise themselves as to make their relationship fall into which category they choose: *Massey v Crown Life Insurance Co* [1978] ICR 590. The intention of the parties should not be disregarded altogether where the situation is finely balanced (see Lord Hoffmann's judgment in *Carmichael v National Power plc* [2000] IRLR 43 (HL)).

2.37 Parties considering treating their relationship as a contract for services when it is obviously one of employment should exercise caution. Contracts which defraud HM Revenue & Customs, as such a contract may be found to do, are illegal and void and normally cannot be relied on as the basis of any claim even where either or both parties are ignorant of the illegal character of the agreement: *Miller v Karlinski* (1945) 62 TLR 85 (CA) applied in *Salveson v Simons* [1994] IRLR 52, in which the EAT conducted a useful review of the authorities on illegality. An exception arises in relation to discrimination law rights, which are treated slightly differently by the courts for public policy reasons. An employer cannot rely on the illegality of a contract in order to avoid liability for discrimination: *Hall v Woolston Hall Leisure Ltd* [2000] IRLR 579 (CA). A further exception is where the contract is found to be illegal as performed, as distinct from illegal as formed, and one party is innocent of the illegal purpose: *Newland v Simons and Willer (Hairdressers) Ltd* [1981] ICR 521 (EAT); or at least substantially less culpable than the other: *Hewcastle Catering Ltd v Ahmed and Elkamah* [1991] IRLR 473 (CA). In those circumstances, the innocent or less culpable party may be able to enforce the contract. Whilst it is arguable that wrongly electing to treat a contract of employment as a contract for services only means that the contract is illegal as performed, where both parties are equally culpable of perpetrating the fraud on HM Revenue & Customs, as often they will be, the exception will not assist. In cases where there is doubt about the proper status of the contract, the prudent course is to avoid the risk of an illegality argument by making full disclosure of the relevant facts to HM Revenue & Customs and obtaining their prior approval to treating the worker as self-employed (as had been done in *Young and Woods Ltd v West* [1980] IRLR 201). The 'employer' who fails to take this step faces the possibility of being unable to enforce the contract – in particular, the restrictive covenants.

2.38 Similarly, tax saving (as distinct from evasion) schemes other than the 'independent contractor route' should also only be adopted after careful thought. Whilst a scheme will not necessarily be unlawful because its only purpose is to reduce tax (*Lightfoot v D & J Sporting Ltd* [1996] IRLR 64 (EAT)), such schemes will almost inevitably come under careful scrutiny by the courts and tribunals. So, for example, in *Salveson v Simons* [1994] IRLR 52, after some years of employment at Simons' suggestion his (then) employer agreed to pay him a reduced salary but pay an amount equal to the reduction to a partnership of Simons and his wife. That partnership declared and paid tax on the sums it received, but provided no services to Simons' employer. Unsurprisingly, the arrangement was found to be illegal, with the result that Simons could not pursue

3(a) Misdeeds/misconduct

3.69 A contract of employment is not a contract of the utmost good faith (*uberrimae fidei*). An employee is not, therefore, under a duty to disclose his own misconduct: *Bell v Lever Bros Ltd* [1932] AC 161 (HL) and *Sybron Corporation v Rochem Ltd* [1983] 3 WLR 713 (CA). It has, however, been doubted in the Court of Appeal whether it is necessarily correct to say that an employee is not under a duty to disclose his own misconduct: see *Item Software(UK) Limited v Fassihi* [2004] IRLR 928, discussed at 3.71 below.

3.70 In *Nottingham University v Fishel* [2000] IRLR 471, where a university employee was in breach of an express term requiring him to obtain consent before undertaking paid work at clinics abroad, he was held not to be in breach of the duty of fidelity by failing to inform his employer of his breach of contract, since there was no such duty to disclose his own misconduct. The university's argument was that, had the university been aware of the opportunity to do outside work, it would have sought to do it itself. Elias J stated (paragraph 74):

> 'In my view the premise is wrong. I do not think that as a general principle an employee is bound to inform his employer if and when he is doing outside work in breach of his contract. Mr Dutton relies upon the case of *Neary v Dean of Westminster* [1999] IRLR 288 in which Lord Jauncey, sitting as special commissioner appointed to hear the case on behalf of Her Majesty the Queen as Visitor, held that in the circumstances of that case the employee in question was in breach of the duty of trust and confidence in failing to inform the Abbey authorities of certain activities he was conducting on his own behalf. However, in that case Lord Jauncey clearly considered that the employee had taken advantage of his position as organist at the Abbey for his own benefit. In other words, the duty to inform the Abbey authorities arose because Dr Neary had used his position to earn secret profits; he ought to have accounted for these to his employers in the absence of full disclosure and consent. It is similarly contended in this case that Dr Fishel was a fiduciary who abused his position for his own benefit. I consider that issue later in this judgment. If that is right, then it may be said that by acting in secret Dr Fishel has both acted in breach of his fiduciary duty and in breach of contract. But the contractual claim then adds nothing to the fiduciary claim. Absent the fiduciary obligation, the employee is not obliged to disclose the fact that he has earned sums from third parties. Indeed, were he to be so obliged, this would circumvent the well-established rule in *Bell v Lever Brothers Ltd* [1932] AC 161 that employees are not obliged to disclose their own past misconduct or breaches of contract.'

Nottingham University v Fishel is considered more fully in Chapter 4 relating to fiduciary duties at 4.9–4.19.

3.71 To similar effect is the decision in *Tesco Stores Ltd v Pook* [2004] IRLR 618 (at paragraph 63). However, in *Item Software(UK) Limited v Fassihi* [2004] IRLR 928 (CA) doubts were expressed in relation to the 'rule' in *Bell v Lever Brothers Ltd*: Arden LJ stated (at paragraph 60) that *Bell* was not authority for the proposition that an employee can never be under a duty to disclose his wrongdoing and (at paragraph 61) that it was unnecessary to decide whether

Bell applied where there has been a fraudulent concealment by the employee. *Fassihi* is considered more fully in at 4.132–4.138. In our view, it is likely that the courts will in future not apply a strict rule that an employee is never obliged to disclose his own wrongdoing, but will rather approach the matter on a fact-sensitive basis. So, for example, in the case of a senior employee who fraudulently conceals his wrongdoing in order to extract a large severance sum, the court is unlikely to apply the 'rule' in his favour. (This kind of case will, however, often be covered by express warranties in the severance agreement that no acts of serious misconduct have occurred.) In relation to more junior employees or less serious misconduct, however, the court is not likely to insist on self-incrimination.

3.72 There is no general duty on employees to report a fellow employee's misconduct or breach of duty, but an employee may have such a duty; whether or not he does depends on the circumstances of each particular case: *Swain v West (Butchers) Ltd* [1936] 3 All ER 261 (CA) applied in *Sybron Corporation v Rochem Ltd* [1983] 3 WLR 713 (CA). Swain was the general manager and was found to be under an obligation to disclose unlawful orders given to him by the managing director. In *Sybron* the information was the establishment and operation by a number of employees of Sybron of rival businesses in competition with the company. The employee found to be under a duty to disclose was the European zone controller who was in de facto control of the European operation of Sybron and had a duty to report on the state of his zone every month. Factors of significance were: the position of the employee in question in the hierarchy, the recognised reporting procedure, and that there was a continuing fraud on the employer. Employees in managerial positions with reporting responsibilities and/or responsibilities for discipline are likely to be under a duty to disclose misdeeds of subordinate or superior colleagues. The seriousness of the conduct in question is important: where this is not obvious, the employer may need to draw to the attention of the workforce the seriousness which he attaches to the particular conduct. In *Distillers Company (Bottling Services) Ltd v Gardner* [1982] IRLR 47 Gardner, a loader who was employed together with other loaders, was dismissed for not reporting pilfering and abuse of alcohol by colleagues. The EAT appear to have regarded Gardner as being obliged to report the matter to his employer and that his failure to report an earlier incident of pilfering warranted a final warning. However, in relation to a later incident which led to dismissal, the EAT (inconsistently) said that it was asking a lot of an employee to report misdemeanours of his colleagues, and if this was to be the rule it should be clearly spelt out. See also *British Midland Tool Ltd v Midland International Tooling Ltd* [2003] 2 BCLC 523 (referred to at 3.42 above).

3.73 In *Pennwell Publishing (UK) Limited v Ornstien* [2007] IRLR 700 (QBD) three employees established a rival company during their employment and engaged in conduct going beyond the boundaries of permissible acts in preparation for competition, including the use of Pennwell's confidential information to establish the rival business. It was contended that one of the employees, Mr Isles, who was not directly involved in the impermissible activity, should have reported the conduct of his colleagues. The submission was accepted in relation

4.93 Decisions subsequent to *IDC v Cooley*, rather than seeking to identify a breach of fiduciary duty prior to resignation as a director, proceeded on the basis that, unlike the no conflict rule, the no profit rule may survive after ceasing to be a director or employee. Indeed, the submission to the contrary was said to be obviously unsustainable in *Island Export Finance Limited v Umunna* [1986] BCLC 460, on the basis that it would connote that, provided a director does nothing contrary to his employer's interest whilst employed, he may conceive the idea of resigning in order to exploit the opportunity of the employers and, having resigned, proceed to exploit it himself. Consistently with this, it has been suggested that the decision in *IDC v Cooley* may be better viewed as an application of the no profit rule: see *Wilkinson v West Coast Capital* [2005] EWHC 1309 at paragraph 264.

4.94 The analysis that the fiduciary duty does not survive the end of the relationship focuses attention on the director's conduct whilst still in office in planning to resign in order to divert the maturing business opportunity away from the company. In *Island Export Finance Ltd v Umunna* [1986] BCLC 460, Mr Umunna was the managing director of a company which pursued business in West Africa, and which obtained an order by the postal authorities in Cameroons for 6,000 postal caller boxes. After resigning as managing director, Mr Umunna obtained for his own company two further orders for similar equipment from the same department in Cameroons. In rejecting the claim that in doing so he breached a fiduciary duty, Hutchison J stressed the need both that there be a maturing business opportunity which the company was actively pursuing, and that the resignation be prompted or influenced by a wish to acquire that opportunity for himself (or to divert it to a third party). Neither requirement was satisfied. Whilst the analysis proceeded on the basis of a continuing duty beyond the termination of directorship, the focus was on the period of the directorship both in relation to whether there was a maturing business opportunity and in relation to whether the resignation was part of a plan hatched whilst still a director.

4.95 The CA 2006, however, adopts a third approach. Section 170(2) provides that:

> 'A person who ceases to be a director continues to be subject—
>
> (a) to the duty in section 175 (duty to avoid conflicts of interests) as regards the exploitation of any property, information or opportunity of which he became aware at a time when he was a director,
>
> (b) to the duty in section 176 (duty not to accept benefits from third parties) as regards things done or omitted by him before he ceased to be a director.
>
> To that extent those duties apply to a former director as to a director, subject to any necessary adaptations.'

4.96 Where a duty arises other than pursuant to the no conflict and no profit rules, such as disclosure obligations by reason of the duty to act in good faith in the interests of the company (see 4.132–4.150 below), the duty (though not

liability for breach of the duty) therefore comes to an end on ceasing to be a director. However the provision does not follow the line of cases to the effect that the no conflict rule comes to an end upon resignation as a director. Rather it contemplates continuation of the no conflict rule in relation to exploitation of any property, information or opportunity of which he became aware at a time when he was a director. On its face this might be read as indicating a substantial change to the pre-Act position. Thus, the obligation might be read as applying irrespective of the reasons for the director leaving office, in contrast to the position aside from the CA 2006. On a literal interpretation, it also appears to refer to *any* information, rather than imposing a limit on the use only of information akin to a trade secret or even confidential information. However, it is expressly provided that the duties continue 'subject to any necessary adaptations' (section 170(2)). In the light of this, and the terms of section 170(4) (see 4.50 above), the provision for continuing obligations is likely to be interpreted consistently with the pre-existing common law rules and equitable principles. The previous limits on continuing obligations as identified in *Island Export Finance Limited v Umunna* are likely to remain relevant, including whether there was a maturing business opportunity which the company was actively pursuing, and whether the resignation was prompted or influenced by a wish to acquire that opportunity for himself (or to divert it to a third party).

(ii)(iii) What constitutes a maturing business opportunity?

4.97 As to the requirement for a maturing business opportunity which the company was actively pursuing, relevant considerations are set out in proposition 8 in the summary in *Hunter Kane* (see 4.87 above). This connotes a specific opportunity which is being actively pursued or negotiated by the company rather than general business aims. Indeed, this is implicit in the suggestion (proposition 9 – drawn from *CMS Dolphin* at paragraph 96) that the opportunity be treated as if it were property or an intangible asset of the company. Thus, in *Island Export Finance Limited v Umunna* the mere hope that there might be further orders for postal caller boxes did not amount to a maturing business opportunity, and nor was the claimant actively pursuing such orders when Mr Umunna resigned. Similarly, in *Dranez Anstalt v Hayek* [2002] 1 BCLC 693 Evans-Lombe J (at paragraph 76) drew a distinction between diversion of specific contracts in the course of negotiation, which could be regarded as 'maturing business opportunities', and general business aims which, in that case, were to sell certain ventilators to the medical profession world wide. The company could not in any sense claim to have a property interest in the world-wide demand for ventilators.

4.98 The decision in *British Midland Tool v Midland International Tooling Limited* [2003] 2 BCLC 523 (at paragraphs 184–185) further illustrates the need for a specific opportunity in relation to which the directors could profit by diverting the opportunity. The contention that there were maturing business opportunities failed where this was based only on the opportunities afforded by the claimant's goodwill to continue to manufacture and design goods for its existing and potential customer base. This amounted to no more than an allegation that the defendants had resigned in order to be able to compete with the claimant

was held by the EAT to permit only the most minor of changes and nothing more. The clause did not override the general principle that variations to a contract of employment normally require consent. See also *Wandsworth London Borough Council v D'Silva* [1998] IRLR 193 – considered in more detail at 13.12.

5.52 In defining the employee's role the employer needs to deal with the following issues:

- Job title and duties.
- Joint appointments.
- Mobility.
- Interaction with the press/media.
- Garden leave.

2(a) Job title and duties

5.53 Section 1(4)(f) Employment Rights Act 1996 requires the employer to give the employee written notification of his job title or a brief description of the work he is employed to do. While technically, therefore, the employer can be silent on duties, it is undoubtedly good practice, and indeed increasingly common, for a list of duties to be drawn up by the employer. In deciding on the employee's title and duties some caution must be exercised.

5.54 Where a contract of employment is very specific about the employee's job title and/or duties, then there is very little scope for alteration without the employee's consent. Virtually the only qualification to this is that there is an obligation on employees to adapt to new methods and improved technology, provided that the employer arranges any necessary training in the new skills and the nature of the work does not alter so radically that it is outside the contractual obligations of the employee: *Cresswell v Board of Inland Revenue* [1984] ICR 508. In that case the introduction of a computerised PAYE system, appropriately referred to throughout the case as 'COP', was found not to be a variation of the duties of tax officers and clerical assistants.

5.55 How, then, does the employer obtain the necessary flexibility? First of all he should give careful thought to the choice of job title. Some job titles are necessarily restrictive, for example 'Senior Manager – Overseas Department'; others are more general, allowing the employer greater flexibility: for example simply 'Manager'. For senior employees unspecific job titles, such as the commonly used 'Executive', should be adopted with caution. The preferred way of obtaining flexibility for these employees, who may well be the potential competitors, is to have a reasonably specific job title, but coupled with a provision whereby the employer can require the employee to do another job. Prospective employees will normally agree to such clauses, particularly where the other job

is to be of a comparable status and there is an obligation on the employer to act reasonably.

5.56 The second point for the employer to consider is the definition of the employee's duties. As a general rule the best course is to provide a reasonably specific list, but with a general 'safety-net' provision requiring the employee, in addition to the duties specified, to do such other duties which, in the opinion of the employer, are connected with or incidental to the duties set out in the job description. Where the employer has incorporated a right to change the employee's job, a right to change the employee's duties must be expressly reserved.

Precedent – Senior Executive

1.1 The Company shall employ the Executive and the Executive shall serve the Company as ***[insert job title]*** *or in such other [comparable] role as the Company may from time to time [reasonably] require.*

1.2 The Executive's duties for the Company shall be those specified in the Schedule to this Agreement or, in the event of the Executive being appointed to a new role pursuant to Clause 1.1 such other duties as are in the [reasonable] opinion of the Company appropriate to and consistent with such new role.

[1.3 The Executive may be required to perform duties for and accept office in other companies in the Group without additional remuneration].

Note: The word 'Group' should be defined in the service agreement, see 5.9–5.13.

Schedule

The Executive's duties shall be

[Set out specific duties]

In addition the Executive will perform such other duties, appropriate to his position as ***[insert job title]****, as the Company may from time to time reasonably require.*

2(b) Joint appointments

5.57 Very senior employees may argue that any attempt to appoint another employee to act jointly with them amounts to a reduction in their status and consequently a repudiatory breach of the contract. To avoid this argument being available to the employee, it is sensible for the employer to include an express term permitting such an appointment. In the case of corporate employers when dealing with board level positions (for example a managing director), the draftsman should always check that the Articles of Association would permit a joint appointment. If a joint appointment is not permissible, then the employer will either have to revise his plans or the Articles will have to be altered.

5.114 Finally, because of the EAT's decision in *Whittle Contractors Ltd v Smith* (1 November 1994, unreported) EAT 842/94 that holiday continues to accrue during garden leave, it had become common practice to include a term negating the effect of that decision. Following the implementation in English law for the first time of a statutory right to holiday (regulation 13 of the Working Time Regulations 1998), such a term can arguably no longer be included in so far as it relates to holiday equating to the statutory holiday entitlement as distinct from an extra contractual entitlement. However, there can be no objection to a term which provides that outstanding holiday as at the date of commencement of garden leave is, insofar as there is a sufficient garden leave period in which the employee is not in fact required to do any work, deemed to be taken during that period. This point has recently been confirmed by the EAT in *Industrial and Commerce Maintenance Limited v Briffa* [2008] UKEAT/0215/08/2207.

3(d) Return of property

5.115 Every contract of employment should include a term that the employee shall return all the employer's property and property of any relevant Group companies/organisations when the relationship terminates. Where the contract includes a garden leave clause, as most now do following the Court of Appeal's decision in *William Hill Organisation Ltd v Tucker* [1999] ICR 291 (see 15.19), it is prudent for the obligation also to be triggered by the employer exercising his right to send the employee on garden leave. Where a provision for the return of property on the commencement of garden leave is included, care needs to be taken to exclude from the obligation any property provided as a contractual benefit – typically a car. If that type of property is not excluded, there will be a conflict between the garden leave clause (which will, and indeed must, provide that all contractual benefits are continued) and the return of property clause.

5.116 Some employers omit an obligation to return property from their contracts on the ground that it is no more than a statement of their common law right to have their property returned on request. While an express clause will invariably incorporate that right, it can also improve the employer's position in the following ways:

- By providing that property is to be returned automatically on the employee being sent on garden leave or on termination, the employee is on notice of the position from the outset. Consequently, the need for a formal request for return from the employer is obviated. However, it is undeniably good practice for the employer to draw the obligation to the employee's attention once it is known that the employee is to be sent on garden leave or employment is to terminate.
- Where the Service Agreement provides that notes, records or documents made or compiled by the Executive during his employment are the property of the employer, it can ensure that property is delivered up even if the actual physical property (eg a diary, notebook or computer disk) belongs to the employee.

- It can set out an administrative mechanism for dealing with the return of property under which the employee lists the property returned and warrants that he has retained nothing in any form (including any copies of company property). Not only is this a useful reminder to ensure that the mechanics of return are gone through, but it can also be a significant practical deterrent to an employee proposing to keep, for example, a crucial customer list. Unless he is prepared to lie about documents returned, his only other option is to be evasive about the procedure, which in itself will arouse the employer's suspicions. A clause incorporating all these features is set out below.

5.117 Since nowadays it is common for employees to use personal computers at home to work on their employer's business, it is also worth including an obligation which requires the irrevocable deletion of information relating to the employer's business and that of the Group from the employee's computer systems. How sophisticated the procedures for enforcing this obligation will need to be will depend on the level of risk associated with the employee being able to retain and have access to information of the employer and/or the Group of which the employer is part. In cases of significant risk it may be necessary to include a mechanism under which an information technology expert has access to the employee's equipment to ensure that the process is executed correctly. In all cases it will be appropriate to provide that a hard or electronic copy of the information to be deleted is received by the employer prior to the deletion taking place. This is for two reasons: first, because in rare instances it may be the only copy of the information available and, secondly, because if subsequently the employer has reason to believe that the employee is threatening to compete, it can be a useful source of the information to which he had access at a relevant time. In some instances it can provide the key evidence on which the employer secures an injunction.

Precedent – Senior Executive

1.1 Upon whichever is the first to occur of: (a) the Company exercising its rights pursuant to Clause ***[insert clause number of garden leave clause]*** *and (b) termination howsoever arising of this Agreement the Executive shall subject to Clause 1.2:*

1.1.1 forthwith deliver up to ***[insert title of company officer]*** *at* ***[insert address]*** *all property in his possession, custody or under his control belonging to or relating to the Company [or any other company in the Group] including but not limited to keys, passwords, security and computer passes, computer hardware, facsimile machines and all documents and other records (whether on paper, magnetic tape, in electronic format or in any other form and including correspondence, lists of clients or customers, notes, memoranda, software, plans, drawings and other documents and records of whatsoever nature and all copies thereof) made or compiled or acquired by the Executive during his employment hereunder and concerning the business, finances or affairs of the Company [or any other company in the Group] or its [or their] customers.*

helpful in defining trade secrets, but they do not necessarily assist in distinguishing between trade secrets and confidential information. Indeed, somewhat startlingly (in the light of the decisions of the Court of Appeal in *Faccenda Chicken v Fowler*, *Roger Bullivant Ltd v Ellis* and *Johnson & Bloy (Holdings) v Wolstenholme Rink plc*), Staughton LJ in *Lansing Linde v Kerr* [1991] 1 All ER 418 at page 425h–j and 426d questioned whether there was a difference at all between trade secrets and confidential information! While it is true that the distinction between trade secret and confidential information is often difficult to draw in practice, the distinction is (at least according to the Court of Appeal in *Faccenda*) fundamental, and the claim of an employer (absent an express restrictive covenant) will often depend entirely (as it did in *Faccenda*) on whether the information in question falls into one or the other category. Yet there does not appear to be any difference in principle between the two categories of confidential information, the difference being rather a matter of degree (see *Faccenda Chicken Ltd v Fowler* [1987] Ch 117 at page 299ff per Neill LJ and *PSM International plc v Whitehouse* [1992] IRLR 279 (CA) at page 282).

6.52 The employer who wishes to allege that his information is a trade secret and not merely confidential must (even in obvious cases, such as secret processes) provide the court with proper details justifying this higher categorisation. We suggest that in seeking to identify what is a trade secret it is helpful to bear in mind the distinction between general skill and knowledge of the employee and information which relates to the specific business of the employer: the court ought to be careful not to raise to the status of trade secret that which is more in the nature of general skill or knowledge of the ex-employee than knowledge of the employer's specific business. Thus, in *Lancashire Fires Ltd v SA Lyons & Co Ltd* [1997] IRLR 113 at 117 Sir Thomas Bingham MR stated that the distinction between mere confidential information and trade secrets may often be on the facts very hard to draw:

> '… but ultimately the court must judge whether an ex-employee has illegitimately used the confidential information which forms part of the stock-in-trade of his former employer either for his own benefit or to the detriment of the former employer, or whether he has simply used his own professional expertise, gained in whole or in part during his former employment.'

2(e) Distinction between general skill/knowledge and confidential information

6.53 The courts have long distinguished between: (1) confidential or secret information; and (2) general skill and knowledge of the employee. In a well-known passage in *Herbert Morris Ltd v Saxelby* [1916] AC 688 at page 709 Lord Parker stated:

> 'Wherever such covenants have been upheld it has been on the ground not that the servant or apprentice would, by reason of his employment or training, obtain the skill and knowledge necessary to equip him as a possible competitor in the trade, but that he might obtain such personal knowledge of and influence over customers of his employer, or such an acquaintance with his employer's trade secrets as would enable him, if competition were allowed, to take advantage of his employer's trade connection or utilise information confidentially obtained.'

(See also *Wessex Dairies Ltd v Smith* [1935] 2 KB 80.)

6.54 The distinction between: (1) general skill and knowledge; and (2) confidential information or trade secrets often lies at the heart of disputes relating to confidential information, yet despite recourse to the above-mentioned definitions of trade secrets and confidential information, it often remains very difficult to decide on which side of the line particular information falls. In particular, it is often extremely difficult to say whether a specific item of information forms part of the employee's skill and knowledge or amounts to special knowledge of the ex-employer's business (*Faccenda* provides a good example of this difficulty). However, the mere fact that the ex-employee has retained information in his memory (even though he did not deliberately memorise it to compete with his employer after termination of employment) does not mean that this information is not secret: *Amber Size & Chemical Company Ltd v Menzel* [1913] 2 Ch 239. This point was made by Bell J in *SBJ Stephenson v Mandy* [2000] IRLR 233, where he pointed out that a trade secret such as a chemical compound could well be retained in an employee's memory, but that did not mean that the information was not a trade secret. Bell J went on to draw a distinction between objective knowledge and subjective knowledge, based on a well-known passage of the judgment of Lord Shaw in *Herbert Morris v Saxelby* [1916] AC 688:

> 'Trade secrets, the names of customers, all such things which in sound philosophical language are denominated objective knowledge – these may not be given away by a servant; they are his master's property … On the other hand, a man's aptitudes, his skill, his dexterity, his manual or mental ability – all those things which in sound philosophical language are not objective, but subjective – they may, and they ought, not to be relinquished by a servant; they are not his master's property …'

It is doubtful, however, that the terminology of objective and subjective knowledge is helpful in distinguishing between trade secrets and confidential information on the one hand and an employee's general skill and knowledge on the other. It is simply an adoption of different terminology and provides no workable test. Moreover, the passage in *Herbert Morris v Saxelby* which refers to information which is the property of the employer and information which is the property of the employee is somewhat circular in determining whether or not a given piece of information amounts to the employer's confidential information or trade secret so as to render it protectable by covenant or by means of a common law or equitable duty.

6.55 It is clear that an employer cannot restrict the use by the employee of his skill or knowledge after employment. Thus, the decision of the Court of Appeal in *FSS Travel & Leisure Systems Ltd v Johnson* [1998] IRLR 382 serves as a reminder that the employer must adduce sufficiently cogent relevant evidence to identify a separate body of objective knowledge qualifying for protection by means of a restrictive covenant. It was not sufficient for the employer to assert that he

- A natural person who is a national of, or habitually resident in, a European Economic Area ('EEA') state (ie a Member State of the European Union, Iceland, Liechtenstein, or Norway); or
- A legal person incorporated under the laws of an EEA state with its central administration or principal place of business in an EEA state, or its registered office in an EEA state and its operations linked on an ongoing basis with the economy of an EEA state; or
- A partnership or other unincorporated body formed under the laws of an EEA state.

7.26 This would seem to suggest that if a US company carries on business in the UK, even if a database is created in the UK by persons employed in the UK, the database would not be protected by the database right, if the company did not have a registered office in the UK.

2. THE NATURE OF THE DATABASE RIGHT

7.27 A database right in a particular database is infringed if a person extracts or re-utilises all or a substantial part of the contents of the database without the owner's consent.

7.28 Extraction means 'the permanent or temporary transfer of those contents to another medium by any means or in any form' (regulation 12(1)). So, for example, copying the contents of a client list onto a USB drive, or disk, or e.mailing the contents of a database to another computer would be extraction. Printing off a hard copy would also constitute extraction. Re-utilisation means making those contents available to the public by any means (regulation 12(1)). In the Database Directive this is defined to include the distribution of copies, renting, on-line and other forms of transmission (Art 7(2)(b)). Although this wording does not appear in the Regulations, the Regulations should be read subject to the Database Directive in this regard.

7.29 The ECJ in the *British Horse-Racing Board* case made the following points regarding extraction and re-utilisation:

- Extraction and re-utilisation should each be interpreted widely as referring to any unauthorised appropriation or distribution to the public.
- The extraction or re-utilisation need not be directly from the database, but may be from a copy or other extract.
- It is irrelevant whether the extraction or re-utilisation is for the purposes of competition; nor is it relevant whether the extraction or re-utilisation takes place in the course of an activity which is not the creation of a new database (*British Horse-Racing Board*, paragraph 47).
- However, unauthorised consultation of the database is not extraction or re-utilisation.

7.30 Extraction does not necessarily require the mechanical copying of the database, eg by cutting and pasting it into a computer file, or by photocopying a print out. Extraction may be carried out by an employee consulting the database and manually transcribing its contents: see *Case C-304/07: DirectMedia Publishing GmbH v Albert-Ludwigs-Universitat Freiburg* [2008] WLR (D) 312, ECJ. In that case, the University had a collection of verse titles which it published on the internet. It was accepted for the purposes of the reference that the collection constituted a database. DirectMedia produced a CD-ROM of German verse. It did so by consulting the University's database, assessing which poems it wished to include and manually transcribing the title. The ECJ held that this was an extraction, but left the question of whether the extraction was of a substantial part to the national court.

7.31 In the employment context, it is more likely that databases will be infringed by extraction rather than re-utilisation. An employee who takes with him to his new employer a copy of a client list or other database can easily be seen to have carried out an extraction: see eg *Crowson Fabrics Ltd v Rider* [2008] IRLR 288 (Ch D). However, re-utilisation requires making the contents available to the public (regulation 12(1)), and this is much less likely to occur. There may be cases in which an employee takes a database so that he can publish it himself, if the employer and employee are both in the business of making databases available to the public. However, in most employee competition cases, the employee will take a database to use it himself, not to publish it. If the employee keeps a copy of a database and consults it for his own purposes (eg to contact clients on a client list) this would not amount to re-utilisation.

7.32 To amount to an infringement, the extraction or re-utilisation must be of a substantial part of the database. 'Substantial' means substantial in relation to quantity, or quality, or a combination of both (regulation 12(1)). A substantial part, evaluated quantitatively, refers to the volume of data extracted from the database and/or re-utilised, and must be assessed in relation to the volume of the contents of the whole of that database. A substantial part, evaluated qualitatively, refers to the scale of the investment in the obtaining, verification or presentation of the contents extracted and/or re-utilised, regardless of whether that subject represents a quantitatively substantial part of the general contents of the protected database. A quantitatively negligible part of the contents of a database may in fact represent, in terms of obtaining, verification or presentation, significant human, technical or financial investment (see *British Horse-Racing Board*).

3. DURATION OF THE DATABASE RIGHT

7.33 The database right lasts for 15 years from the end of the calendar year in which the making of the database was completed (regulation 17(1)).

7.34 Regulation 17(3) allows for renewed protection where changes are made to the database. However, the drafting of the provision is unclear. Regulation 17(3)

avoid the risk of the tribunal reducing any award to the employee (by between 10% and 50% – in accordance with its powers under section 31(2). From April 2009, these prescriptive rules will be relaxed. Following the Gibbons Report of 21 March 2007, by the Employment Act 2008 the statutory grievance procedure will be abolished, as will the requirement that a grievance must be lodged before any constructive dismissal claim can be brought. However, a revised ACAS Code of Practice on Disciplinary and Grievance Procedures is to be introduced and section 3 Employment Act 2008 retains the principle of reducing compensation for non-compliance with that Code of Practice by 'no more than 25%'. Until 6 April 2009, with the exception of employees with less than one year's service, compliance with the current regime is in the employee's interests. After 6 April 2009, subject to transitional provisions set out in the Employment Act 2008 (Commencement No 1 Transitional Provisions and Savings) Order 2008 (SI 2008/3232), the regime will become less prescriptive, but where the employee's goal is to buy time, and to avoid the risk of a reduction in his compensatory award under section 3 Employment Act 2008, it will still be appropriate for a grievance to be lodged.

Acts/omissions inconsistent with accepting the breach

9.60 In the same way that there is no distinct time frame within which the innocent party must accept a repudiatory breach, there are no absolute rules as to what acts or omissions of the innocent party will result in his having waived the repudiatory breach. An employee who, without protest, works in accordance with a significantly revised shift pattern unilaterally imposed by his employer is likely to be found to have agreed to a variation to his contract and have waived the employer's breach. Contrast, with those situations, however, the employee who expressly protests in writing against a proposed change to his terms of employment which has immediate effect and continues to perform the contract in its original form. The employee in that position is unlikely to be found to have waived the employer's breach, at least in the short to medium term. Similarly, where the breach is unacceptable conduct on the part of the other party, and the protest records the fact of the behaviour in question and makes it very clear that exception is taken to the behaviour, that too is unlikely to amount to waiver of the breach. As already suggested at 9.59 above, where the innocent party in this situation is the employee, he should also consider in an appropriate case lodging a formal grievance.

9.61 In *Owens v Wealden District Council* UKEAT/0186/05/CK neither the giving of contractual notice by the employee nor her agreement to extend that notice by two weeks were found by the EAT to amount to affirmation of the contract. As the EAT pointed out, section 95(1) Employment Rights Act 1996, which sets out the requirements for a constructive dismissal, specifically contemplates that the employee may give notice. Ms Owens had given her notice on the very day upon which the 'final straw' in the council's alleged course of repudiatory conduct had occurred. Furthermore, the agreed extension of notice was simply to reflect the fact that the council had delayed its recruitment and selection process, presumably for Ms Owens' replacement, whilst her concerns

were investigated. See also *Bashir v Brillo Manufacturing* [1979] IRLR 295 (EAT), where Mr Bashir's delay in resigning and acceptance of sick pay during a period when his employer was seeking to demote him to a more junior position, which Mr Bashir consistently refused to accept, did not amount to affirmation of the contract.

9.62 For an unusual case on whether a contract has been affirmed and repudiatory breach on the part of the employee (as opposed to the employer) had been accepted, see *White v Bristol Rugby Limited* [2002] IRLR 204. In that case, the employer's refusal to pay Mr White for a period in which he failed to attend for work was found to be neither an acceptance of Mr White's repudiatory breach nor a repudiatory breach by the employer. Whilst recognising that a contract may be drafted so as to require the employer to pay the employee where the employee simply refused to work through no fault of the employer, Mr White's contract was not so drafted. Mr White was a professional rugby player who entered into a three-year contract with Bristol Rugby Limited to play for Bristol Shoguns. The contract was to commence on 1 July 2001. Before that date Mr White changed his mind about joining Bristol Shoguns. Initially he sought to exercise an alleged oral opt out agreement under which he claimed that by returning an advance of salary of £15,000 he was free to walk away from the contract. Bristol Rugby argued there was no such arrangement and returned Mr White's cheque. Bristol Rugby was very keen to have Mr White join the Bristol Shoguns and offered Mr White an increase in the agreed remuneration, which he refused. When the time came for the contract to commence, Mr White failed to attend the club's premises or to make any contact with Bristol Rugby. In response, although still making it clear they wished Mr White to join them, Bristol Rugby declined to pay Mr White. Mr White applied for a declaration that he was not bound by the contract or, if he was, that Bristol Rugby were in repudiatory breach which he, White, had accepted. Mr White's claim failed on all counts. The court ruled that the contract contained no opt out provision. Any alleged oral term was precluded by an entire agreement clause. Furthermore, any alleged representation on which Mr White sought to rely, although the court found as a fact none was made, was also irrelevant; the contract included an express term that neither party had relied on any written or oral representation in entering into the contract. More importantly for the purposes of this chapter, the court found that there was nothing in the conduct of Bristol Rugby that amounted to either an acceptance of Mr White's repudiatory breach or a repudiatory breach which Mr White could have accepted. Bristol Rugby had consistently made it clear that they wanted Mr White to join the club, that his contract was being held open and they had done nothing inconsistent with that position. Had Bristol Rugby engaged another player as a replacement for Mr White, the position would have been different, but they had not done so.

9.63 Some of the cases (especially those involving statutory claims of unfair dismissal) ask whether the repudiatory breach was the cause of the employee's resignation. We will look at those cases briefly in the following paragraphs. In our view, however, these cases simply express, in different terminology, the key requirement that the repudiatory breach must have been accepted and not

during employment from engaging in preparatory activities. Likewise, where there is a garden leave clause, the overall period of garden leave together with the restrictive covenant must be considered: *Credit Suisse Asset Management v Ltd v Armstrong* [1996] ICR 882. While the Court of Appeal in that case did not require the period spent on garden leave to be 'set off' by another contractual provision against the restrictive covenant period, nonetheless it did require the overall periods of garden leave and restrictive covenant to be considered in the round. It should also be noted that, in the years following this decision, as a matter of caution, the practice is quite widely followed of including a contractual 'set off' of time spent in the garden against the restrictive covenant period. We regard this as a wise course to follow.

11.12 Different considerations will apply according to the type of interest which is sought to be protected. In the case of covenants designed to protect customer connection, the question is what is the minimum time required to protect the customer connection. This will normally be the time which it would take a replacement employee to establish a relationship with the customers such that the influence of the ex-employee will have been removed: *Middleton v Brown* (1878) 47 LJ Ch 411 at page 413 and *Stenhouse Australia Ltd v Phillips* [1974] 1 All ER 117. This, of course, depends substantially on the nature of the business and, in particular, the degree of customer loyalty, which may in turn depend on such factors as the nature and frequency of customer contact. The fact that the particular business is cyclical can be significant. For example, in the insurance industry, where most policies are renewed annually, a one-year covenant may be more readily justifiable (indeed 13 months is often advised, to take account of a month of grace usually allowed for the renewal of insurance policies).

11.13 In *Beckett Investment Management Group Ltd v Hall* [2007] EWCA Civ 613, [2007] ICR 1539, [2007] IRLR 793, where the claimant sought to enforce a 12-month non-dealing covenant against its former employees (who were registered independent financial advisers, the first defendant having been employed as a sales director and the second defendant as financial consultant), the Court of Appeal did not agree with the judge below that 12 months was too long and that a three-month duration would have been sufficient. The Court of Appeal regarded the rationale of the judge below for a three-month period as simplistic in so far as it addressed the relationship between the claimants and the clients, and as deficient in having no regard to what the claimants would need to do to persuade clients to remain loyal. The ex-employees in question were not run of the mill, expendable employees, but were of enormous importance to the success of the employer. To have any prospect of retaining the clientele, the ex-employer would need to recruit, organise, train and project suitable replacements. The judge had instead chosen to attach significance to the fact that a non-dealing clause would prevent a client from doing business with someone in whom he had confidence for a period which the judge considered to be too long. During the period of restriction, the client was not compelled to remain with the covenantee. If he could not await the expiration of the period of restriction, he could in the meantime seek the advice of any service provider with which the covenantor was unconnected. For these reasons, the

Court of Appeal concluded that the confinement of reasonableness to a period of three months was wrong. In concluding that 12 months was a reasonable period, specific regard was had to the seniority and importance of the two ex-employees, to the evidence about business patterns, to the logistics of replacing them, and to the uncontradicted evidence of an industry standard of covenants of 12 months' duration.

11.14 Difficult issues arise when considering teams of employees. Often, more junior employees subject to shorter notice and covenant periods will move first to a competing employer: see *GFI Group Inc v Eaglestone* [1994] IRLR 119. They are then able to keep the 'seat warm' for the more senior employees who were members of the same team – and who remain on the payroll of the (first) employer. To avoid such planned 'staggered' team moves, it may be appropriate to seek covenants of the same period for all team members. In our view, a court would be likely to regard as reasonable a somewhat lengthier period in relation to a more junior employee in these circumstances than might otherwise be justifiable when considering him in isolation. However, there is a danger that the court might look at the periods individually and without regard to the context of a possible team move. It is, of course, possible to draft covenants so that their period increases where, for instance, more than a certain number of employees leave at the same time or, say, within the previous six months of the covenanting employee's departure. We do not recommend this technique. It is likely to be complicated to draft and may even fail on grounds that the period is too vague or unpredictable. (The employer should also consider having common notice periods, although this would need to be balanced against the risk to the business of thereby causing team members to end employment at the same time.)

11.15 In the case of non-competition or non-solicitation/dealing covenants designed to protect confidential information the principle factor will ordinarily be the 'shelf life' of the confidential information. Where there are secret (unpatented) processes which are expected to remain confidential for a long time, a long period (even an indefinite one) may be justified. In a world of rapidly developing technology it may be difficult to justify a long period, even in the case of technical secrets. In the case of customer information such as prices, special requirements and the like, only short periods (usually in the three to 12-month range) will ordinarily be justifiable. Different considerations will apply according to whether the covenant is a non-solicitation/dealing covenant or a non-competition covenant: in the former type of covenant a longer period may be tolerated. Lifetime restrictions will not normally be upheld: *Sir WC Leng and Co Ltd v Andrews* [1909] 1 Ch 763.

I (d)(i) Examples of periods

11.16 Each case depends on its own facts and, generally, reference to other cases in relation to periods upheld or not upheld may be apt to mislead. In the most general way it may be said that employment covenants in excess of 12 months should be regarded as potentially vulnerable. The reverse is not necessarily true – even 12 months may be too long where the cycle of business is very short. For

absence of any effort to 'formulate the covenant in a way which focuses upon the restraint necessary in respect of a particular employee' rendered the covenant unenforceable. It is most unlikely that *Wincanton* would be decided differently today. The court cannot be expected to assist an employer who makes no attempt to formulate the covenant properly. Further, it is an abuse for such an employer to enjoy the benefit of wide covenants vaguely drafted and then only at the doors of the court (as against those employees who have the will and the means to challenge the covenants) to seek to argue for a narrow prohibition, in order to 'rescue' the covenants.

12.15 The prudent employer will not rely on the courts applying benign modes of construction, but will ensure that his restrictive covenants are drafted as clearly and precisely as possible. However, it is a counsel of perfection to require the draftsman to cater for all possibilities and express himself perfectly at all times. By understanding the need to be as clear as possible in his drafting and the rules of construction, the draftsman can avoid at least some of the potential pitfalls. He is also best placed to know how to challenge the covenants of other draftsmen when acting for the (ex-)employee or the poaching employer.

2(c)(i) The modern approach to construction of contracts

12.16 As a starting point, and before focusing on particular rules of construction and how they have been applied in restrictive covenant cases, it is useful to have regard to Lord Hoffmann's summary of the proper approach to construction of contracts in *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 WLR 896 (HL). This case involved a dispute relating to allegedly negligent advice given in connection with the sale of home income plans. The issue before the House of Lords was whether on the proper construction of a contract, there had been an effective assignment of certain of the investor's rights to the Investors Compensation Scheme. At pages 912–13 Lord Hoffmann, having referred to the fact that 'Almost all the old intellectual baggage of legal interpretation has been discarded', summarised the principles as follows:

> '(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.
>
> (2) The background was famously referred to by Lord Wilberforce as the "matrix of fact", but this phrase is if anything an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties, and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.
>
> (3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification. The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this

> exception are in some respects unclear. But this is not the occasion on which to explore them.
>
> (4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same meaning as its words. The meaning of words is a matter of dictionaries and grammar; the meaning of a document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meaning of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must for whatever reason, have used the wrong words or syntax (see *Mannai Investment Co Limited v Eagle Star Life Assurance Co Ltd* [1997] 3 All ER 352, [1997] 2 WLR 945).
>
> (5) The "rule" that words should be given their "natural and ordinary meaning" reflects the commonsense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had. Lord Diplock made this point more vigorously when he said in *Antaios Cia Naviera SA v Salen Rederierna AB, The Antaois* [1984] 3 All ER 229 at 233 [1985] AC 191 at 201:
>
> "... if detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business common sense, it must be made to yield to business common sense."'

For a recent example of the application of Lord Hoffmann's approach in the context of restrictive covenants, see *Beckett Investment Management Group Ltd v Hall* [2007] 1RLR 293 (CA). Whilst Lord Hoffmann's summary is very useful, it remains helpful for the draftsman to focus briefly on the various rules of construction as they have been applied in the context of restrictive covenants in employment contracts.

2(c)(ii) Words used are given their ordinary meaning

12.17 The basic rule is that words are to be given their ordinary and natural meaning, subject to some limited exceptions. In *Mallan v May* (1844) 13 M&W 511 the rule was stated in the following way (at page 517):

> 'Words are to be construed according to their strict and primary acceptation, unless from the content of the instrument and the intention of the parties to be collected from it, they appear to be used in a different sense, or unless in their strict sense, they are incapable of being carried into effect.'

As seen at 12.16, this rule now operates in a slightly modified form, per Lord Hoffmann in *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 WLR 896 (HL) at page 913. Where it is plain from the background to the contract that something has gone wrong with the language so that the words given their ordinary meaning do not reflect the parties' intentions, the words will be interpreted in the context of the parties' intentions; as Lord Hoffmann

the proposed change was explained to the employee, that the employee understood the consequences of refusing to agree to the change and that discussions took place with the employee prior to dismissal in which the employee had an opportunity to raise his concerns with the employer.

13.30 Employees with the necessary continuity of service to present a claim of unfair dismissal may allege that the dismissal was unfair, notwithstanding that all procedural rules have been followed. Special rules apply where there has been a transfer to which the Transfer of Undertaking (Protection of Employment) Regulations 2006 applies and these are set out at 13.54–13.78. In other cases, the only ground on which the employer can defend such a claim is what is sometimes referred to as the 'safety net' category of 'some other substantial reason': section 98(1)(b) Employment Rights Act 1996.

13.31 The leading case on this point remains *RS Components Ltd v Irwin* [1974] 1 All ER 41 (NIRC), in which RS Components succeeded in justifying the dismissal on the grounds of 'some other substantial reason'. Since the factual background in *RS Components* is a fairly typical example of when employers want to introduce new covenants, it is worth looking in some detail at the case and the process adopted by RS Components in seeking the consent of its employees. RS Components were distributors of electrical components in England and Northern Ireland. They operated through a team of 92 salesmen, each of whom worked in an allocated territory and visited customers in accordance with a schedule provided by RS Components. In the two years preceding the dismissal of Irwin, RS Components had lost a number of orders to ex-salesmen. Those ex-salesmen, using knowledge gained in their employment of the names and addresses of customers and the times of calls by RS Components staff, set up their own businesses and called upon the customers to solicit orders shortly before the customer was due a visit by the RS Components representative. This resulted in loss of business and complaints being received from RS Components salesmen, who were paid partly by salary and partly by commission. RS Components took advice and concluded that the appropriate way forward would be to introduce a reasonable non-solicitation of customers' covenant. RS Components issued new service agreements to its salesmen on 1 February 1973 containing a 12-month non-solicitation covenant. The service agreements contained other alterations, but none was relevant to the unfair dismissal claim. The covering memorandum required the employee to consider the new agreement carefully and to sign and return it by 23 February. Although the memorandum sought the employee's views it also made it clear that the revised terms were the only terms on which the company could continue to employ and that the new terms would come into effect from 1 March. On 21 February, Irwin wrote to the company saying he would not sign the covenants. Subsequent attempts to persuade him to change his mind, including a personal interview with the Chairman, failed and consequently, at the beginning of March, his employment was terminated by a payment in lieu of notice. Of the 92 salesmen Irwin was one of only four who refused to sign. The Industrial Tribunal (as it then was) held that the covenant was reasonable and would probably have been enforceable and that the effect on the future interests of RS Components of Irwin's refusal to agree to the covenant

was so substantial as to justify dismissal. However, by a majority the Industrial Tribunal found Irwin had been unfairly dismissed, since on the proper construction of the phrase 'some other substantial reason', it had to be read ejusdem generis (that is be restricted to the same class of reasons) with the other reasons for dismissal contained in what was then the Industrial Relations Act 1971 (now section 98(2) Employment Rights Act 1996. On appeal, the National Industrial Relations Court (the predecessor of the EAT) allowed RS Components' appeal, holding that the phrase 'some other substantial reason' was not to be construed ejusdem generis and that Irwin's dismissal was a fair dismissal for 'some other substantial reason'. Two further points are worth noting. The first, referred to in the Industrial Tribunal's decision, was that it recognised a need for uniformity amongst the terms of employment of the sales staff and it placed some reliance on the fact that as there had been an opportunity for 'consultation and explanation' it could not be said that Irwin had been treated unfairly. The second is the recognition, as part of the justification of the National Industrial Relations Court's decision, that cases could clearly arise where it would be essential for an employer to introduce restrictive covenants. The two examples referred to are where covenants are necessary to limit the use of knowledge acquired in employment of a new technical process or where a licensing agreement imposed on the licensee an obligation to extract restrictive covenants from its employees. As Brightman J put it (at page 45), 'It would be unfortunate for the development of industry if an employer were unable to meet such a situation without infringing or risking infringement of rights conferred by the 1971 Act'.

13.32 A recent ruling of the EAT in *Forshaw v Aircraft Ltd* [2005] IRLR 600 suggested that a dismissal for refusal to accept a new restrictive covenant could not fall within the category of some other substantial reason where the proposed covenant was itself unreasonable. In other words, the employer failed on the first limb of the grounds for defending an unfair dismissal claim. In our view, that decision was incorrect and, more recently, in *Willow Oak Developments Ltd v Silverwood* [2006] IRLR 607 the Court of Appeal, disapproving *Forshaw*, confirmed that the mere fact that the proposed covenant was unreasonable did not preclude the employer relying on the category of some other substantial reason as the reason for dismissal. The Court of Appeal ruled that the question asked by section 98(1)(b) Employment Rights Act 1996 was whether the reason was 'of a kind' such as to justify dismissal, ie it falls within a category that is not excluded by law as a ground for dismissal, for example because it is 'whimsical or capricious'. In *Willow* the Court of Appeal ruled that refusal to sign a covenant protecting the legitimate interests of the employer was a reason that in law was a valid reason for dismissal and therefore the EAT had correctly proceeded to the second stage of assessing whether the employer had acted reasonably in treating that reason as sufficient to justify dismissal under section 98(4). The employer ultimately lost in *Willow* but it did so because of the procedure adopted in seeking consent, including an initial request to sign the covenants within 30 minutes and a failure to warn of the consequences if the employee did not sign.

13.33 For employers proposing to dismiss for refusal to sign a new covenant, *Willow Oak Developments Ltd v Silverwood* [2006] IRLR 607 is an object lesson

- Each of the elements of the particular cause of action in order to show a serious issue to be tried; in cases based on contract, this involves identification of the contract, particular terms relied on, the facts constituting breach, and reference to the loss or expected loss flowing from the breach. Where the injunction sought is to enforce a non-solicitation/dealing covenant or non-competition covenant, all the facts relevant to show the reasonableness of the covenant must be covered, including the particular interest which the covenant is intended to protect. In breach of confidence cases it is necessary to set out all the facts relied on as proving that the information is a trade secret or confidential (see Chapter 6).
- The facts generating a claim for injunctive relief, in particular where the injunction is on the basis of threatened (not actual) breach (quia timet), the grounds for such apprehension must be set out.
- The elements relevant to the balance of convenience, for example:
  - > The nature of the potential harm to the applicant, if the injunction is not granted, and the reasons why such harm is not compensatable in damages; what is known about the financial position of the respondent and (where appropriate) that the harm which the applicant might suffer is not easily quantifiable;
  - > The reasons why the cross-undertaking in damages will provide adequate protection to the respondent; the financial position of the applicant and (where appropriate) that any loss to the respondent is easily quantifiable.
- Where the party is under a duty to make full and frank disclosure, all other facts which are required to comply with that duty.
- If the application is made without notice, the facts justifying this course.

For an example of a witness statement, see Chapter 18, Appendix 5.

7(c) Witness statements/statements of case/court records/hearings in breach of confidence cases – maintaining confidence

7(c)(i) Particularity needed in witness statements/statements of case

14.72 Particular difficulties may be experienced in the preparation of witness statements in confidential information cases. The employer will need sufficiently to identify the secrets or confidential information to persuade the court that there are genuine trade secrets or items of confidential information and the reasons why the information is regarded as confidential (see Chapter 6). Against this is the need not to refresh the (ex-)employee's knowledge of the confidential information or trade secrets in question – or indeed (in cases of uncertainty as to precisely which of a range of secrets the (ex-)employee has learnt) not to disclose the full range of secrets to him. Normally in the case of commercial secrets it is

easy enough to describe the class of documents (eg customer list) without revealing its contents. In cases of technical secrets it is usually also possible to describe the class of secrets and the reasons why the information or particular elements of it are secret or confidential without divulging the detailed contents – but not always. The dilemma is described by Graham J in *Diamond Stylus Co Ltd v Bauden Precision Diamonds Ltd* [1973] RPC 675:

> '[The applicant's] difficulty is that if he does disclose in detail what his process is, he thereby gives away secrets, which is the one thing he does not want to do, though he may in such a case be able to make out his prima facie case by showing that the respondent has used part or the whole of that process. If on the other hand he is not prepared to disclose his secret then he is in obvious difficulty in showing that what the respondent has done is to take that secret, because there is not ex hypothesi sufficient identification of the latter to enable a satisfactory conclusion to be drawn.'

14.73 In *Under Water Welders & Repairers v Street and Longthorne* [1968] RPC 498 Buckley J said that:

> 'It is not to be expected that a [applicant] who is seeking to protect some commercial secret will disclose the nature of that secret, particularly in interlocutory proceedings.'

Buckley J (somewhat surprisingly) granted an injunction despite finding that the applicants had not in their evidence condescended to any details as to precisely which characteristic of the process gave it a confidential character.

14.74 However, in *Diamond Stylus* Graham J distinguished *Under Water Welders*, saying:

> '... each case must be judged in the light of its own particular facts and the governing principle in each case is that the [applicant] must make out a prima facie case if he is to be entitled to an interlocutory injunction. It may be in some cases that a [claimant] is able to do that without disclosing much in the way of detail about his particular process in which he claims secrecy or confidence. On the other hand there are other cases where it seems to me, depending on the surrounding circumstances and the state of knowledge generally in the art [state of the art], that he may have to go further and disclose at any rate the essential features of his process which he says have been taken.'

14.75 Although, since the decision of the House of Lords in *American Cyanamid Co v Ethicon Ltd* [1975] AC 396, the applicant need only show a serious question to be tried as to the existence of a trade secret, we suggest that it remains unwise not to provide adequate evidence in this regard. In *Lock International plc v Beswick* [1989] 3 All ER 373 at pages 378h–j Hoffmann J said:

> 'It is of course tempting in an action such as this, concerned with the technicalities of electronics, to say that the questions at issue can only be investigated at the trial and that for *Cyanamid* purposes the [claimant] must be treated as having an arguable case. It would however, be unjust to the respondents simply to allow the [applicant] to blind the court with scientific banalities.'

Gorman [2009] EWCA (Civ) 387 the Court of Appeal adopted a similar approach in an agent's case, holding that it was strongly arguable that where an employer discovered that his agent was in serious breach of the duty of good faith and then discovered that he was tied to a rival company, the employer had no duty to provide work, the obligation being interdependent with the agent's duty to act loyally.

2(k) Is a protectable interest required?

15.26 Another somewhat odd aspect of *William Hill Organisation Ltd v Tucker* [1998] IRLR 313 was a passage by Morritt LJ (at paragraph 25) where he appeared to suggest that the courts should not enforce a garden leave clause 'to any greater extent than would be covered by justifiable covenant in restraint of trade'. It is not clear exactly how far this statement extends. If what Morritt LJ had in mind was that the court should have regard to potential abuses which may arise from garden leave and not enforce garden leave in a manner which is unreasonable, having regard to restraint of trade principles, there can be no difficulty with this. If, however, it was intended to mean that garden leave clauses are to be scrutinised as if they were post-termination restrictive covenants, that is dubious. In particular, since during garden leave the employee remains an employee subject to the duty of fidelity, one would expect that the employer would be entitled to bargain for a greater measure of protection than the ex-employer (see 3.66–3.67 as to the effect of garden leave on the duty of fidelity). During employment the employer is entitled to protect himself against (mere) competition from the employee – something which cannot be achieved by a post-employment restrictive covenant. It is for this reason that in *Crystal Palace v Bruce* [2001] All ER (D) 331 Burton J held that (arguably) – and notwithstanding the above dictum of Morritt LJ – it is not necessary for the employer who seeks to impose garden leave to identify a protectable interest of the sort necessary to justify a post-termination restrictive covenant. Reliance in this regard was placed on dicta in *Provident Financial Group plc v Hayward* [1989] ICR 160 at page 169 to this effect and in *Credit Suisse v Armstrong* [1996] ICR 882 at pages 892–4. Accordingly, in *Crystal Palace* one of the bases for the grant of a garden leave injunction against a football manager was that he should not be entitled to 'snap his fingers' at his contract of employment in order during its agreed term to join a competing club.

2(l) When and for how long garden leave will be ordered

15.27 Garden leave will only be enforced for a limited period – ie the minimum length of time adequately to protect the employer's legitimate interest: see *Cantor Fitzgerald International v George* (17 January 1996, unreported) (CA). However, in contrast, with restrictive covenants the court may where appropriate reduce the duration of garden leave to a period less than the notice period: *GFI Group Inc v Eaglestone* [1994] IRLR 119; and see *Credit Suisse Asset Management Ltd v Armstrong* [1996] IRLR 450 (CA). Generally, garden leave injunctions will not be awarded for longer than six months. Garden leave will only be enforced where the employer can show that some detriment will result

from the employee working for a rival (*Provident Financial Group plc v Hayward* [1989] ICR 160), such as where the employee has been exposed to confidential information of the employer.

2(m) Interplay between garden leave and restrictive covenants

15.28 In *TFS Derivatives v Morgan* [2005] IRLR 246, the employee argued that the court should refuse to enforce various restrictive covenants on the basis that it would have been more appropriate for the employer to have invoked its right to place him on garden leave in order to have obtained legitimate protection. Cox J rejected this argument on the basis (among others) that notwithstanding the employer's contractual right, placing the employee on garden leave may have constituted a breach of the implied term of mutual trust and confidence. In our view, it would be a very rare case where the invocation of a contractual right to put an employee on garden leave would amount to a repudiatory breach of contract. In many cases where there are both garden leave provisions as well as post-employment restrictive covenants in the contract of employment, the employer may (in particular where there are any doubts regarding the effectiveness of the post-employment restrictions) be best advised to keep the contract alive and rely on the garden leave provisions. The advantages of so doing arise from the fact that the courts are more amenable to granting relief to the employer during the subsistence of the employment contract than thereafter (see 3.11–3.12 and 10.2–10.4). More specifically, the courts will during employment:

- Protect confidential information which does not amount to trade secrets; and
- More readily restrain competitive activity.

15.29 Conversely, where employment is at an end, the courts will:

- Carefully scrutinise covenants restraining competitive activity, including confidentiality covenants;
- Protect only trade secrets or confidential information in the nature of a trade secret.

15.30 Furthermore, an employee is not entitled to 'credit' as against the period of the (post-employment) restrictive covenant for time spent on garden leave: *Credit Suisse Asset Management Ltd v Armstrong* [1996] IRLR 450 (CA), applied in *Brake Bros v Ungless* [2004] EWHC 2799. In *Armstrong*, it was held that the judge had not erred in concluding that the applicants were entitled to the protection of restrictive covenants prohibiting the respondents from competing with or soliciting the applicant's business for a period of six months after their employment terminated, notwithstanding that the applicants had already had six months of complete protection by placing the respondents on 'garden leave' throughout their notice periods. If a restrictive covenant is valid, the employer can expect to have it enforced, subject to the usual grounds on which an injunc-

- The primary basis of assessment is 'to consider the sum that would have been arrived at in negotiations between the parties had each been making reasonable use of their respective bargaining positions without holding out for unreasonable amounts': *Amec Developments Ltd v Jury's Hotel Management (UK) Ltd* [2001] 1 EGLR 81 at page 83.
- The outcome of that hypothetical negotiation must be determined by reference to the parties' actual knowledge at the time that negotiations would have taken place. This would normally be on the date of the breach.
- The fact that the innocent party would never have agreed to any such sale or relaxation is irrelevant.
- The conduct of the wrongdoer is also irrelevant as to the breach of contract.
- The decision to award damages under this head is discretionary according to the circumstances of the case, but the decision should be taken when damages would be an inadequate remedy and where without an award under this basis the innocent party would obtain no just recompense for the breach by the wrongdoer in doing what he agreed not to do.
- The decision whether or not to award damages on this basis can take into account factors such as delay in intimating the claim and prosecuting the action, if appropriate. Those factors also could be taken into account at a later stage in quantifying the claim. Thus, it may be possible to argue that where a wrongdoer was led to believe that no claim would be forthcoming on this head and acted to its detriment in reliance upon that, that may bar the claim completely. Equally, part of a claim may be disallowed by reason of delay if the delay caused prejudice: see *Shaw v Applegate* [1977] 1 WLR 970 and *Gafford v Graham* (1998) 77 P & CR 73 (CA).

16.18 The most significant feature of *Wrotham Park* damages is that they arise out of a hypothetical negotiation. Flowing from that, the evidence relevant to the assessment is evidence as to what would have been in the parties' knowledge at the time of the hypothetical negotiation. This could be critical where, for example, the wrongdoer has made profits far in excess of what was, or even could have been, anticipated. Without evidence to the contrary it is likely that the court will, as it did in *Wrotham Park*, simply equate actual profits with anticipated profits. It also follows that the court can take into account all factors that would have been relevant to a negotiation, such as some diminution to the claimant's reputation or costs savings for the defendant, and is not limited merely to a percentage of profits figure.

2. DAMAGES FOR INDUCING BREACH OF CONTRACT AND OTHER ECONOMIC TORTS

2(a) The economic torts: inducement of breach tort compared with conspiracy

16.19 The different kinds of claims that may be made against third parties are considered in detail at 14.37–14.57. The most frequently encountered claims within the context of this book are:

- Claims usually made by the (ex-)employer against the new employer (or some other third party, including other (ex-)employees) for inducing breach of contract by the (ex-)employee. The elements of the tort, in particular the necessary knowledge of the third party, were recently considered by the House of Lords in *OBG Ltd v Allan* [2007] UKHL 21: see 14.38–14.48.
- Claims for conspiracy to cause harm by unlawful means (see 14.54–14.56). While there is a prospect of a higher award of damages in the case of the tort of conspiracy than with other torts which are not based on dishonesty (see 16.21 below), it may be a matter of fine judgment whether it is appropriate to plead conspiracy when there are other economic torts which can be pleaded against the relevant third parties. For example, in a team move case the claim can often be pleaded against the new employer on the basis of knowing inducement of the departing employee to breach his contract of employment (including, where appropriate, his restrictive covenants), or breach of confidence. To add a claim of conspiracy (or, for that matter, dishonest assistance in breach of fiduciary duty) may simply be for the claimant to take on a disproportionately greater burden, together with the attendant risk of an adverse issues based costs order.

16.20 Dishonesty-based claims are in the nature of fraud claims which have to be distinctly pleaded and proved (see PD 16, paragraph 8.2(1). In *Hornal v Neuberger* [1957] 1 QB 247 (CA) it was held that where fraud, or another matter which is or may be a crime, is alleged against a party or against persons not parties to the action, the standard of proof to be applied is that applicable in civil actions generally, namely proof on the balance of probability, and not the higher standard of proof beyond all reasonable doubt required in criminal matters. However, there is no absolute standard of proof. In all cases the degree of probability must be commensurate with the occasion and proportionate to the subject-matter. The elements of gravity of an issue are part of the range of circumstances which have to be weighed when deciding as to the balance of probabilities. Accordingly, wherever dishonesty is pleaded, the court will require a greater degree of persuasion. Where the court is not satisfied that the defendant has in fact been dishonest, this may influence (even subconsciously) the court's approach towards the other pleaded causes of action which are not dependent on proof of dishonesty. Therefore, in some cases it may be best not to rely on dishonesty based torts. In other cases, eg of flagrant concerted unlawful activities, it will be entirely natural to rely on torts such as conspiracy or dishonest assistance in breach of fiduciary duty – and indeed not to do so might create an impression that the claimant has no real faith in his case.

2(b) Measure of loss for economic torts

16.21 The approach to an award of damages for economic torts (eg inducing a breach of contract or conspiracy) is in line with other torts. The economic torts are referred to at 14.37–14.57. The claimant is entitled to be put in the position in which it would have been but for the commission of the torts, which may include

taking further investigations into your conduct and all their rights in relation to your conduct, and indeed that of your colleagues and new employer, are expressly reserved. The evidence our client already has in its possession gives rise to substantial claims against you. Any amounts which you and People 'R' Us Ltd earn in relation to contracts which have been improperly entered into are held on constructive trust for our client.

Our client is not prepared to countenance any further breaches by you of your obligations to the ongoing detriment of their legitimate interests. As a first step our client requires you to comply with the requests set out below by 5:00pm on [date].

Our client's requirements are as follows:

1. You provide a written undertaking that with immediate effect you will comply in all respects with Clauses [•] and [•] of your Service Agreement.
2. You deliver up to our offices all and any property (including copies of documents) of Smith & Jones in your possession or under your control, including but not limited to:

   (i). Customer files;

   (ii). Strategy and reorganisation reports relating to our client's customers;

   (iii). The card index used by you and/or business cards containing details of our client's customers;

   (v). Customer lists and data printout sheets of customer details;

   (vi). The diary belonging to our client; and

   (vii). Any notes or memoranda made or used by you in the course of your employment with our client.

   With regard to any property/information which you hold in an electronic format on your own personal property eg a home computer, blackberry (or similar), that information should either be downloaded onto a disc(s) or be printed out and the disc(s)/printouts delivered to our offices. The disc(s)/printouts should be clearly marked to identify their source. You are specifically required to preserve all information and property in whatever format that property/information is held. You must not destroy or delete or tamper with or attempt to destroy/delete or tamper with any property /information. Similarly you must not under any circumstances use or disclose such information for any purpose other than in accordance with our client's instructions and your written undertaking that you will not do any of the things which you are prohibited from doing by this paragraph is required.
3. You provide a written schedule of each and every one of Smith & Jones' customers to whom or with whom you have at any time whether before or after the termination of your employment with Smith & Jones directly or indirectly through another employee or agent of People 'R' Us Ltd: (a) made any approaches; or (b) had any dealings in connection with your

move to People 'R' Us Ltd or in furtherance of the interests of yourself or People 'R' Us Ltd. In relation to each customer, potential customer or candidate you must identify the date(s) of the approach and/or dealings, the substance of the approach and/or dealings, the current position regarding an outcome of the approach and/or dealings and quantify any income earned or that may be earned as a result of any of the aforementioned conduct.

4. You provide a complete list of all and any confidential information or property that you have directly or indirectly disclosed or provided to People 'R' Us Ltd identifying in relation to each item: (a) on what date the particular piece of information/property was disclosed or provided to People 'R' Us Ltd; (b) to whom it was provided and in what medium; (c) the current whereabouts of the property/information including whether it has been incorporated into any electronic records/systems held by or on behalf of People 'R' Us Ltd and (d) each and every use that has been made of the property or information.
5. You provide written undertakings that all evidence which is relevant to this matter will be preserved in whatever format the evidence takes. You must not destroy or delete or tamper with or attempt to destroy or delete or tamper with any such evidence.
6. You confirm in a signed witness statement including a statement of truth that you have complied with all of the above requirements and that all the responses you have given to our enquiries are accurate in all respects.

Should you ignore this letter or fail to comply with any of the requirements listed above then you should be in no doubt of the seriousness of the situation. We have instructions to make an immediate application to Court for appropriate Orders the costs of which will be for your account.

We strongly recommend that you seek legal advice as a matter of urgency. [Pending your taking legal advice we draw your attention to the Practice Direction on Pre-action Conduct (a copy of which is enclosed) and in particular Paragraph 4 of that Practice Direction which sets out the Court's powers to impose sanctions for failure to comply with the Practice Direction.]**

We await your compliance with the requirements listed above by 5:00pm on [date]*. Following that compliance our client will review matters and consider what further steps are necessary to protect its legitimate interests. In the meantime, all our client's rights are expressly reserved.

Yours faithfully

* depending on the urgency of the situation the timeframe for this date should normally be between three and five working days.
** to be included from 6 April 2009 for recipients who are not legally represented.

Note: from 6 April 2009 where funding arrangements within the meaning of CPR Rule 43.2(1)(k) have been entered into the Letter of Claim should include notification of the arrangement. No such arrangement has been entered into in this instance.