



PrivateEdge

Guide to Business Protection and Restrictive Covenants

This note provides a short guide to the steps an employer can take to protect itself from competition from ex-employees

Restrictive covenants?

- Employees, particularly senior ones, often have access to many types of confidential information. This might include business plans, customer details or other valuable information about your business. Sometimes ex-employees take advantage of this confidential information or customer connections when their employment ends. The employee might join a competitor or even set up their own business to compete with you.
- Employees must observe certain terms that are implied into every contract of employment (these are called implied terms). One of these implied terms is the duty of confidentiality, however this is not a very wide duty and does not generally include the period after termination (except in relation to the most significant and confidential information referred to as a trade secret). Express terms are those specifically mentioned in a contract and if you want to protect your business and customer contacts they can be vital. Express terms can be specifically tailored to reflect your circumstances and when used to protect a business are known as "restrictive covenants".
- If properly drafted and reasonable, restrictive covenants can:
 - limit the employee's behaviour and prevent them from damaging your business;
 - deter employees from joining competitors;
 - deter potential new employers, who face the risk that the restrictions will be enforced by the courts, and may themselves be vulnerable to claims, such as inducing a breach of contract.
- Many employers include restrictive covenants in the contracts of employment of senior, highly skilled or customer relationship holding staff at the start of the employment relationship.
- A typical restrictive covenant in a contract will stop an employee from competing with your business for a certain period after the employee has left, or prevent the ex-employee from approaching or dealing with your customers by using knowledge of those customers gained during his previous employment.
- A restrictive covenant is designed to protect your businesses interests or property (e.g. client databases or confidential information) and it must not extend further than is reasonably necessary to protect those interests. The courts do not allow clauses to be enforced that are included in contracts purely to stifle or stop competition all together.

Types of restrictive covenant clauses

- The following are types of restrictive covenants often used by employers:
 - non-competition clauses – restrictions on the outgoing employee working in similar employment for a competitor;
 - non-solicitation clauses – which prevent poaching of clients/customers/suppliers of the former employer;
 - non-dealing clauses – which prevent an outgoing or former employee from dealing with former clients/customers/suppliers, regardless of which party approached the other;

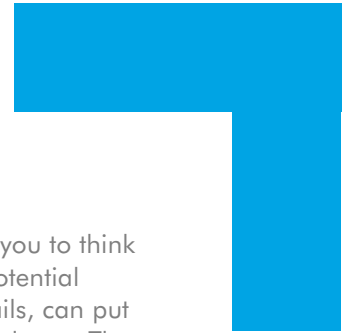
- non-poaching clauses – which prevent an employee poaching former colleagues (typically senior ones).
- For a restrictive covenant to be valid it must not be too 'wide', which means not too onerous for the employee. It will be for you, in the event of the clause being challenged, to show that it is justified and not unreasonable, for the departing employee, given the circumstances of your business. It is helpful to be aware of the following:
 - The extent of the geographical area of any restriction and the length of time post termination that the restriction will last must be justified. For example, stating in an outgoing employee's contract that they cannot work for competitors in the UK when you only operate in London is probably not reasonable or justified.
 - As a very general rule, a restriction for more than 6-12 months will be difficult to justify.
 - It is helpful to state the activities you are trying to restrict.
- The restrictive covenant must be proportionate to the employee's position within the business. As more senior employees will be in contact with more sensitive information, more onerous restrictions placed upon them may be justified. A 'one-size fits-all' policy on restrictive covenant clauses risks the clause becoming unenforceable.
- Carrying out a periodic review of restrictive covenants may be useful so that a business's changing interests can be protected. Employee role changes, promotions or other changes to employment contracts are good opportunities to review.

Garden leave

- A 'garden leave' clause means that the employer can require the employee to remain away from the workplace during all or part of the employee's notice period. The employee remains employed but is not required to work during the garden leave. The employee continues to receive his/her usual salary and benefits.
- The benefit of a garden leave clause is that it prevents the employee from taking up other employment with a competitor whilst enabling the employee's successor to have a useful handover period and develop relationships with the employee's customers and contacts. Whilst on garden leave the employee usually has no access to your confidential information and what information they do have will become out of date.
- In order to be able to place an employee on garden leave safely and lawfully, it is best to have an express clause in the contract of employment. This is very important, because if you breach the contract of employment by placing an employee on garden leave without an express clause in the contract, the employee may be able to argue that the whole contract no longer applies, so you lose the benefit of all the restrictive covenants.

Where a restrictive covenant is breached

- If you believe that an employee has breached a restrictive covenant, the most common remedy sought is an injunction (or 'interdict' in Scotland). This means that the court will be asked to stop the employee from working in their new job immediately or prevent them from using confidential information. The court will then hear the full evidence at a later date in another trial.
- You can claim a financial remedy or damages if you believe a restrictive covenant has been breached. The courts will need you to show loss resulting from the breach. This will normally be loss of profits on contracts or opportunities that you have missed out on because of the actions of the employee.
- Where the employee has been persuaded by a competitor employer to breach restrictive covenant clauses, you might choose to sue the new employer instead (particularly as the competitor company is likely to have greater financial resources from which to pay any award of damages made).



Practical tips

- Legal action in this area can be very costly and time consuming, so it is important for you to think about that you want to achieve from taking a particular approach and consider the potential financial outcomes of this too. Strong evidence of wrongdoing, for example copy emails, can put you in a good position from which a compromise could be negotiated with the ex-employee. The law in this area can be very complicated, and legal advice should always be obtained before taking any action.



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