

Restraint of Trade

1. Background

- 1.1. Restraint of trade clauses are designed to prevent unfair competition after the expiry of an employment agreement or contract. Restraint of trade clauses reflect the fact that the contractor or employee will have access to information about the patients of the practice, and that it would usually be unfair for them to be able to turn that information to their personal advantage by luring patients away from the practice in the event they establish a rival practice or join another local practice.
- 1.2. Because restraint clauses are prima facie unlawful (as they are anti-competitive), any clause of this nature will need to be very carefully drafted, be as non-restrictive as possible and must identify a real need for a restraint in the particular circumstances. No guarantee can ever be given as to the eventual legal enforceability of any restraint of trade clause, and more often than not, provisions protecting the employer's confidential information or intellectual property are far more useful and enforceable and achieve the same aim.
- 1.3. Some restraint of trade clauses are based on geographical limitations, for instance the general practitioner is prohibited from setting up a practice within a particular town or within a defined radius from the employing practice. However, such clauses are not always enforceable, and depend on how reasonable they are in the particular circumstances. Because the circumstances of medical practices differ, any practice which prefers to opt for such a clause is best advised to consult their own legal advisers with a view to getting a 'tailor made' clause for their agreement/contract.

2. Restraint of Trade Clauses

- 2.1. The basic nature and objective of a restraint of trade clause will be familiar to most medical practitioners in private practice. Usually, such clauses set out to prohibit a partner or employee of the medical practice from practising medicine in the same locality as the practice for a defined period after the person has ceased to be a partner or employee.
- 2.2. Such clauses are prima facie void but may be justified in particular circumstances if the restriction is reasonable having regard both to the interests of the parties and to the public interest.

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- 2.3. The Courts' approach to restraint clauses is more strict in the context of employment law than it is in context of partnership law. This is partly in recognition that employees seldom have equality of bargaining strength with employers, and partly to prevent bona fide competition from being stifled.
- 2.4. A well drafted restraint of trade clause needs to take account of a number of considerations.
- 2.5. First, it is only certain interests of the partnership, contract or employment that properly qualify for protection under a restraint clause. In the case of a medical practice, the main such interest will be goodwill. In an English case, this was defined as 'the tendency of patients whom the medical practitioners have treated to continue to resort to that firm for further treatment,' *Whitehill v. Bradford* (1952). A common misconception is that such clauses can be used to prevent competition per se from ex partners or staff. That is not so. Such clauses can only be used to protect the practice's proprietary interests.
- 2.6. Secondly, the restraint must go no further, and extend no longer, than is necessary to protect the practice. There have been cases in which the Courts have invalidated restraint clauses which at first glance seem narrow, but which on closer inspection have been drawn wider than necessary to safeguard the firm's interests.
- 2.7. Conversely, a restraint of trade clause would be of little benefit to the practice if it is so narrowly worded that it does not give the requisite protection. This point is well shown by a New Zealand case in the printing industry where the Court of Appeal held that the effect of a restraint clause was to prevent a former employee from himself carrying on business in the printing industry or acting as a partner in a firm in the industry, but was not worded to prevent him from taking up employment with a competitor: *Graphic Holdings Limited v Dunn* (1988).
- 2.8. Some restraint clauses in medical practices are expressed so as to preclude the former partner, contractor or employee from soliciting patients of the practice for a defined period after termination of the partnership or employment. Such non-solicitation clauses are more likely to be upheld as valid than clauses which would restrict the individual from practising medicine in the locality. This is because the non-solicitation clause can be regarded as directly aimed at protecting the practice's patient connection, being plainly part of the practice's goodwill.
- 2.9. However, just because a restraint of trade clause is included in an employment agreement does not provide automatic protection for an employer. As previously noted, certain aspects will be looked at in terms of reasonableness, such as; the time period specified in the clause, the geographical distance over which the restraint is made, and the kind of work under restraint (specialist etc). In addition to this, an agreement in restraint of trade must be supported by valuable consideration.

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- 2.10. Another example of this is a general practitioner who was employed by a practice, providing both primary health care and a teaching facility. The GP had signed a contract under the status of an independent contractor. Included in the agreement was a restraint of trade clause precluding her from practicing as a general practitioner within five kilometres of the clinic and for a period of one year from the termination of her contract with the clinic. The GP was remunerated at a higher hourly rate compared to what she received prior to entering into the agreement. She became dissatisfied with the conditions while working for the clinic and subsequently resigned. She decided, along with another previous employee of the clinic, to lease premises approximately 200 metres from the clinic for the purpose of starting a new medical practice. Her former employer applied to the High Court for an interim injunction in a bid to restrain her from opening her practice at that specific location. The employer relied on the restraint of trade clause in the agreement. The GP argued the restraint of trade clause was unreasonable and frustrated the professional obligations of doctors which required them to be available to provide care as and when required. The Court had sympathy with the clinic owner's desire to have a period free of competition from previous employees to allow the new medical staff there to settle in and consolidate the clients. However, the Court held, that to allow the injunction would have a greater negative impact on the GP by not allowing her to start her business, rather than the former employer who was concerned about the competition. On the evidence provided, the Court found that there was no proof that the GP received consideration for the restraint of trade clause. There was no reference in the agreement to any connection between the hourly rate and the restraint of trade provision. There were other equally likely reasons for the increase in hourly rate. The application for an interim injunction was dismissed.
- 2.11. Under the Employment Relations Act 2000, the Employment Relations Authority and Employment Court have only limited ability to make an order varying a term of an employment agreement. It will therefore be unsafe for employers to assume that any deficiency in the drafting can be put to rights by the Authority or Court making an order modifying the restraint clause. If the Authority or Court finds that it is precluded from varying an unduly wide clause, as will usually be the case with employment restraints, the clause will be invalid in its entirety.
- 2.12. The Employment Relations Act does not apply to partnership or independent contracts, so the much wider powers of the civil courts to modify restraint of trade clauses under the Illegal Contracts Act will continue to apply in partnership contracts.

Need more help?

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