IN THE EMPLOYMENT RELATIONS AUTHORITY
AUCKLAND

[2014] NZERA Auckland 478
5520829

	BETWEEN	LANCA LIMITED Applicant
	AND	MARK READMAN First Respondent
	AND	MICHAEL LENIHAN Second Respondent
	AND	GRAEME BRICKELL Third Respondent

Member of Authority:	Robin Arthur
Representatives:	Pheroze Jagose and Vonda Hodgson for the Applicant Shima Grice for the Respondents
Investigation Meeting:	30 October 2014
Determination:	20 November 2014

DETERMINATION OF THE AUTHORITY

A. In reliance on an undertaking as to damages given by Lanca Limited, its application for an interim injunction is granted on the basis of the order made in B.

B. From the date of this determination until the date stated after each respondent's name in this order, Mark Readman (1 March 2015), Michael Lenihan (27 February 2015) and Graeme Brickell (2 February 2015) must not:

(a) Canvass, solicit or accept business from any person, company, organisation or other entity who was a customer or client of Lanca Limited in the two years from 1 September 2012 to 31 August 2014; or

(b) Disclose or otherwise make use of Lanca Limited's

confidential information concerning itself, its business, and its clients and customers.

C. Costs are reserved.

Employment relationship problem

[1] Lanca Limited (Lanca) sought interim orders enjoining Mark Readman, Mike Lenihan and Graeme Brickell – formerly employed in various national or regional management roles with the company – from using its confidential information, dealing with its customers or carrying on a competing business. The interim injunction was requested for the period until the Authority could investigate and determine Lanca's application for final orders regarding restraints of trade and use of confidential information. Its substantive application also seeks penalties for breaches of fidelity and good faith allegedly committed by the three respondents before their employment with Lanca ended and an enquiry into damages resulting from their alleged breaches of their terms of employment (both before and after it ended). Lanca had provided the necessary undertaking as to damages to support its application for interim orders.

[2] Mr Readman, Mr Lenihan and Mr Brickell opposed the application. They denied all the alleged breaches, challenged the reasonableness and enforceability of restraint of trade terms in their former employment agreements and said they had given sufficient undertakings, through their solicitor, not to use Lanca's confidential information in the new business they were now running.

[3] A further – and central – issue in their defence to Lanca's claims was whether the restraint of trade provisions applied as Lanca had sold its business assets and goodwill to a competitor. This involved legal questions as to whether Lanca still had a proprietary interest in the business and customer connections referred to in the relevant terms in their former employment agreements and whether the three respondents' own new business could be said to be competing with Lanca now that Lanca's former business was owned by a third party. The three respondents had signed prospective employment agreements with that third party but had each resigned from Lanca before the sale of its business assets and goodwill to the third

party was effective and consequently never took up employment with the new owner of that business. In closing submissions Lanca's counsel described the issue of whether Lanca still had any interest to protect as "*a wrinkle*" and noted there appeared to be no case law directly on Lanca's proposition that it was still entitled to enforce the agreed terms of the restraint in this particular business situation. It was an issue, among others, that fell to be determined on the application of established legal principles to the specific facts of the case.

Issues and investigation

[4] Under s162 of the Employment Relations Act 2000 (the Act) the Authority has the discretionary power to make interim injunction orders of the type requested in the present case.[1] The answer to such an application is not reached by the rigid application of a formula but is given in response to three broad questions: firstly, whether there is a serious issue to be tried (sometimes expressed as whether there is an 'arguable case'); secondly, where the balance of convenience lies (including whether there are adequate alternative remedies available to the party seeking the injunction); and, thirdly, on standing back and considering the matter as a whole, where the overall justice lies from now until the expected date of dealing with the substantive application.[2] It relies on evidence given by affidavit only. That evidence is not tested as it would be in a full investigation meeting, but the Authority may make some common sense assessment of disputed assertions.[3]

[5] In the present case the interim injunction application has been determined on the basis of the evidence available in affidavits lodged by Lanca's director Edward Simpson, Mr Readman, Mr Lenihan and Mr Brickell and relevant background documents lodged by the parties. An investigation meeting was held for the purpose of hearing submissions from the parties' counsel and the assessment of the issues made in this determination was assisted by those submissions. I was also assisted by contextual information found in a determination of the Commerce Commission about the acquisition of Lanca's business by a competitor.[4]

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[1] *Credit Consultants Debt Services NZ Ltd v Wilson (No 2)* [2007] ERNZ 205 at [66] (EC).
[2] *Klissers Farmhouse Bakeries Limited v. Harvest Bakeries Limited* [1985] 2 NZLR 129 (CA).
[3] *Wellington Free Ambulance Service Inc v Alana Adams* [2010] NZEmpC 59 at [17]-[18] (EC).
[4] *Atlas Copco South Pacific Holdings Pty Limited and Lancaster Group Limited* [2014] NZCC 20.

[6] As permitted by s174 of the Act this determination has not recorded all the evidence and submissions received but has stated findings of fact and law, expressed conclusions on issues necessary to dispose of the matter, and specified orders made as a result.

[7] Four questions required determination by the Authority at this stage:

(i) Did Lanca have a sufficiently arguable case that the injunctive relief sought would be granted when the Authority could fully investigate and determine the matter?

(ii) Were adequate alternative remedies likely to be available to Lanca?

(iii) Where did the balance of convenience lie between the parties until the matter was fully investigated and determined by the Authority?

(iv) Where did the overall justice lay meanwhile?

The commercial context and the employment relationships

[8] I have summarised some facts about the commercial context and the employment relationships that were relevant in determining the issues and have set out further details, where necessary, elsewhere in the determination.

[9] Lanca, under a previous company name, and three related companies operated a business importing, distributing, installing and servicing various international brands of air compression and vacuum equipment for various industrial and commercial uses.[5] The business of those companies operated under the name of 'Ash Air'.

[10] Mr Simpson had begun the business some 35 years earlier. Ash Air had grown to employ around 115 staff in 12 branches across New Zealand, including in Auckland, Mount Maunganui and New Plymouth.

[11] On 24 March 2014 Mr Simpson (along with his daughter Annette Zaloum, who was also a director of the relevant companies) signed an agreement (the SPA) for the sale of the Ash Air business to Atlas Copco South Pacific Holdings Pty Limited

[5] The Lanca name is used in this determination to minimise potential confusion between its previous company name – Ash Air (NZ) Limited – and the Ash Air business (of Lanca and the three related companies) sold to Atlas Copco South Pacific Holdings Pty Limited.

(Atlas Copco). The purchase arrangements included Mr Simpson being engaged on a consultancy basis as general manager of the business for a year following the sale and Ms Zaloum being offered ongoing employment as its financial controller.

[12] Through the sale Atlas Copco was to purchase Ash Air's assets, brand and goodwill. The price Atlas Copco paid was not disclosed in the affidavit evidence but Lanca counsel referred in oral submissions to the sum as being in the "*many millions*". The amount paid for the goodwill was also described as "*many millions*".

[13] Atlas Copco already operated a similar business in New Zealand importing and distributing its own brands of air compressors and other equipment.

[14] Its acquisition of the Ash Air business required Commerce Commission clearance that no substantial lessening of competition in the New Zealand market was likely to result. The Commission gave that clearance in a decision dated 30 July 2014.

[15] Settlement of the purchase occurred on 1 September 2014.

[16] Soon after news of the intended sale of the Ash Air business became publicly known in late March 2014, one international company cancelled its New Zealand distribution agreement with Lanca. The company was Gardner Denver. Lanca was the New Zealand agent for distributing the CompAir brand of air compressors made by Gardner Denver. Lanca imported and distributed other brands from other manufacturers but CompAir provided its largest number of products.[6]

[17] Gardner Denver and Atlas Copco are international competitors in the manufacture and distribution of air compression and related equipment. Gardner Denver did not want its CompAir equipment being distributed in New Zealand by a business that was to become a local subsidiary of its international competitor Atlas Copco.

[18] The SPA required Atlas Copco or its nominee to offer Lanca's employees ongoing employment. Atlas Copco arranged for its employment of staff and contracts with customers to be made through a local nominee company, Exlair (NZ) Limited (Exlair).

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[6] Simpson affidavit at para 12.

[19] Mr Readman, Mr Lenihan and Mr Brickell each received an offer of employment from Exlair in early April. Each man signed an employment agreement with Exlair that was said to be on the same terms and conditions of employment that they had as current employees of the Ash Air business. The important feature of that process of offer and acceptance – for the purposes of this determination – was that the offer of employment was said to be "*wholly conditional*" on two facts: completion of the proposed purchase of the Ash Air business and the employee still being employed by Lanca at that completion date. If the purchase did not "*proceed for any reason*" the agreement would "*cease*" and no employment relationship would commence between each of them and Exlair. The wording drew a careful distinction between the existence and operation of the employment *agreement* and the commencement of the employment *relationship*. The consequence of the sale not going ahead would be automatic cessation of the agreement while its completion provided automatic commencement of the employment relationship with Exlair.

[20] The Exlair agreements signed by Mr Readman, Mr Lenihan and Mr Brickell each had a clause headed "Non-competition and confidentiality" with the following terms (with the emphasis added in bold being mine):

> *4.1 During the period of* ***six months*** *after the termination of his/her employment under this agreement the employee shall not:*
>
> *(a)* ***canvass, solicit*** *or accept* ***business of any kind carried on by the employer from any person, company****, organisation or other entity* ***who has been a customer or client of the employer and/or [Lanca and related companies] within the preceding two years****; or*
>
> *(b) employ, or offer employment, or cause employment to be offered, to any person who at any time during the period of the preceding two years shall have been an employee of the employer and/or [Lanca and related companies]; or*
>
> *(c)* ***be involved in any way*** *(whether as owner, officer, shareholder, agent, employee or in any other manner)* ***in any business which is in competition with the business of the Employer and/or [Lanca and related companies]****, and which is* ***carried on within 50 kilometers (sic) of the employer's premises****.*
>
> *4.2 The parties acknowledge that during the course of his/her employment the employee will have access to confidential information concerning the employer, its business, its clients/customers and persons dealing with the employer.*
>
> *4.3 The employee shall keep all such information absolutely confidential both during the term of this agreement and subsequently. To this end the employee*

shall not disclose any such information to any third party expect as directed by the employer in the course of his/her duties under this agreement and shall not make use of any such information for any purpose whatsoever other than the discharge of his/her duties under this agreement.

4.4 The employee shall not use for his/her benefit, or the benefit of any other person, any information gained in the course of his/her employment and not publicly available.
…

[21] Except for the added wording about Lanca (and related companies), the terms in the Exlair employment agreements were the same as in the earlier, and then existing, employment agreements that Mr Brickell and Mr Readman had signed with Lanca.

[22] Mr Brickell had signed his employment agreement with Lanca on 19 August 2010. Mr Readman, who had worked for Lanca since 1996, had signed his employment agreement with Lanca sometime in January 2014 although the version as signed by him and Mr Simpson was 'backdated' to 23 January 2012.

[23] Mr Lenihan's employment agreement with Lanca, signed on 25 April 2009, had some wording in the relevant term different from the agreement he signed with Exlair. Under the heading of "*Non competition and confidentially* (sic)" it read:

16.1 The employee agrees that all information received by him during the employment relating to the customers business including information about the customers of the employer will be kept confidential.

*16.2 During the period of employment and within **one year** of its termination for whatever reason the employee shall not be engaged or interested directly or indirectly alone or in partnership or as a director or shareholder of a company in **any business similar to that carried on by the employer**. In particular the employee shall not during that time **approach or solicit the customers of the employer** or otherwise make use of information acquired by the employee during the employment.*

[24] The differences with the terms applying to Mr Lenihan included the scope of the confidentiality obligation (supposedly on "*all information*"), no geographic boundary to competition with the employer's business (not 50 kms), no timespan on the customer connection (not just those who had dealt with the business in the previous two years) and a one year restraint rather than the six months said to apply to Mr Brickell and Mr Readman under their employment agreements with Lanca (and Exlair).

[25] The common features of all six sets of terms were limits on the use of Lanca's confidential business information, not being part (during the restraint period) of a business of the kind or similar to that of the employer, and not soliciting customers.

[26] By at least various times in July 2014 each of the three respondents had decided not to take up employment with Exlair on completion of the sale. Mr Brickell resigned from his position as Lanca's New Plymouth branch manager on 3 July 2014 and worked out his notice until 1 August 2014. Mr Lenihan resigned from his position as Lanca's central area operations manager on 22 July 2014 and worked until 26 August 2014. Mr Readman resigned from his position as northern or national operations manager on 31 July 2014 and worked until 28 August 2014 (when he was asked to leave).

[27] All three men were said to be subject to ongoing confidentiality obligations to Lanca, which they appeared to accept. Through their solicitor by letter on 8 October 2014 they provided what were said to be undertakings and reassurance that they had not disclosed to any third party any confidential information they had gained as a result of their employment with Lanca and would "*continue to keep confidential any confidential information they have about [Lanca] and any other commercially sensitive information*".

[28] However Lanca doubted the respondents had observed those limits on the use of its confidential business information and alleged Mr Readman, Mr Lenihan and Mr Brickell were in business and employed on a basis that breached their ongoing restraint of trade obligations in their former employment agreements with Lanca.

[29] In his resignation letter dated 22 July 2014 Mr Lenihan advised Mr Simpson that he was resigning his position with Lanca "*to take up a role working with Gardner Denver*". Mr Simpson replied to the resignation letter with an email in which he referred to the restraint provisions in Mr Lenihan's employment agreement and said Mr Lenihan would "*not be able to solicit Ash Air clients without consequences*" and that it was "*not right or correct that Ash Air have spent years and a large investment in our customer base and then for you to attempt to transfer that to GD*".

[30] Mr Lenihan said in his affidavit that Gardner Denver had approached "*several senior managers at Ash Air to come and work for them*" after it had cancelled Lanca's distribution agreement in New Zealand. He said that in early July he had asked Gardner Denver to consider giving him its CompAir agency for New Zealand.

[31] On 2 September 2014 Mr Lenihan incorporated a company called General Compression Limited (GCL) in which he is the sole shareholder and director. A few days later GCL published a web site highlighting CompAir products.

[32] An email mistakenly sent to a Lanca address after Mr Lenihan had left the business showed arrangements he was making on 29 August 2014 for GCL business cards for himself, Mr Readman and Mr Brickell. Mr Lenihan was referred to as GCL's National Sales Manager. Mr Readman was described as GCL's General Manager. Mr Brickell was described as General Manager – Oil and Gas. The details for each included a GCL email address.

[33] An email found on the Lanca computer system included an exchange of emails on 2 August 2014 between Mr Brickell and Mr Readman that was copied to Mr Lenihan. Mr Readman had forwarded to Mr Brickell a copy of an email that Mr Readman wrote to an Atlas Copco executive about his decision to resign from Lanca. Mr Brickell's reply to Mr Readman included this comment: "*With hindsight I think if you had have stayed on in any way they would have litigated the fuck out of all of us.*" Mr Readman's response to that email (also copied to Mr Lenihan) read: "*Agreed mate. We are too smart for those cunts.*"

[34] Mr Simpson's affidavit referred to two occasions where he considered Mr Lenihan and Mr Readman had separately breached their obligations to Lanca. He produced an email that Mr Lenihan had sent to a manager at a Norske Skog plant on 16 September. Mr Lenihan's message included this pitch for business:

> *"… I am emailing you as General Compression is now the CompAir agents for NZ as Ash Air has been brought* (sic) *out by Atlas Copco and are now selling the brand Chicago Pneumatic. I was the one who originally sold Norske the compressors and dryers in the power plant. I would like to offer you a competitive service contract to take on the servicing of these compressors and downstream equipment.*
>
> *Please let me know if you are interested as we have an operation already set up in Mt Maunganui as well as Auckland and New Plymouth. We would really appreciate the opportunity as General Compression is proudly NZ owned and*

> *operated and will only be supplying genuine CompAir parts when serving CompAir machines. …*

[35] Mr Simpson also referred to a second-hand report he got about Mr Readman visiting a manager at VisyPET, a business that was a large customer of Ash Air in Auckland. Mr Readman confirmed he did go to VisyPET but said he was looking at second hand equipment for sale. He said it was not a "*sales call*" by him and he did not ask the VisyPET representative to contact him.

[36] The initial attempt by Lanca's lawyers – who also acted for Atlas Copco in its acquisition of the Air Ash business – to enforce the respondents' alleged restraint obligations was made in letters to Mr Readman and Mr Lenihan on 29 August 2014. Those letters introduced the lawyers as acting for Exlair and stated that "*as purchaser of the Ash Air business and its goodwill, our client is entitled to the benefits of the covenants that you have made to Ash Air*". In a reply letter Mr Lenihan denied any obligations to Atlas Copco and Exlair, said he was never employed by Exlair and no enforceable restraint of trade existed. In a similar reply Mr Readman also stated that Atlas Copco's purchase of the Ash Air business assets did not transfer his employment obligations from Lanca.

[37] In their statement in reply the respondents denied, for two reasons, that Lanca had any legitimate proprietary interests left to protect – firstly, the assets (including the goodwill in the business) were now owned by Atlas Copco and, secondly, Gardner Denver's cancellation of Lanca's distribution agency for CompAir meant the opportunity to market those products was no longer open to Lanca.

[38] They relied on a letter from Ms Zaloum to employees in the Ash Air business, dated 1 August 2014, which had advised Lanca would cease trading on 31 August 2014 and their employment would transfer to Exlair beginning on 1 September. Each of the respondents had given notice of resignation from Lanca by 1 August and had finished their employment by the transfer date.

[39] The respondents' argument about whether Lanca retained any legitimate proprietary interest focussed attention on the terms of the SPA regarding the assets purchased, the warranties given by Lanca and what was included in the goodwill sold.

[40] The SPA described the assets purchased as "*including the Goodwill, Plant and Equipment, Inventory and the Business Premises*". Goodwill was defined as "*the*

goodwill, trading reputation and intangible assets of the Businesses" and included – in parts relevant to this determination – the following:

> *(a) all rights [Lanca and the three related companies] have in all Contracts except for the avoidance of doubt, all Excluded Contracts;*
>
> *(b) all rights that [Lanca and the three related companies] have against any person to the extent that they relate to the Businesses or the Assets, including all statutory rights, choses in action, rights owing by law and the benefit of all warranties and covenants.*
> *…*

[41] The SPA definition of Contracts included a definition of Excluded Contracts. A contract of employment was defined as an Excluded Contract.

[42] Those definitions were important in considering whether the confidentiality and restraint obligations in the respondents' employment agreements were – under (a) – contractual rights *excluded* from the goodwill sold with the Ash Air business or were – under (b) – benefits of covenants *included* in the goodwill purchased by Atlas Copco. If the latter were the case, Lanca might be said to have no rights to protect and enforce as they now 'belonged' to Atlas Copco.

[43] However Mr Simpson's affidavit referred to another aspect of the terms of the SPA said to relate to the ongoing interests of Lanca. He said Lanca faced a serious risk that the respondents' actions may breach a number of warranties given in the SPA, for which Lanca could be liable in damages to Atlas Copco. In Lanca's submission relevant warranties in a potential damages claim against Lanca included the accuracy of warranties given in the period from 24 March to 1 September 2014, indemnity for loss from any breaches by Lanca, full disclosure about "*trading prospects*", no unauthorised disclosure of trade secrets or other confidential information, no notice of termination or resignation by management staff from 1 December 2013, and no knowledge of material events adversely affecting the financial position of the business of which the purchaser would not reasonably have been expected to have been aware.

Legal principles

[44] There was no significant controversy in the parties' submissions about the relevant principles to be applied in relation to an interim injunction and restraint of

trade provisions. They differed, in any real way, only on the application of the various principles to the facts of the particular case. Those facts included various points of dispute about what had happened in respect of employment agreements made with the three respondents and the existence or continuation of any 'business' by Lanca with which the respondents were said to be competing.

[45] Relevant principles included the following:[7]

> *[16] Contractual provisions restricting the activities of employees after termination of their employment are, as a matter of legal policy, regarded as unenforceable unless they can be justified as reasonably necessary to protect proprietary interests of the employer in the public interest: [citations omitted].*
>
> *[17] The onus of establishing that a restrictive provision is reasonable is on the employer. Such a provision should be no wider than is required to protect the party in whose favour it is given.*
>
> *[18] Restraints are enforced only to the extent required to protect a proprietary interest of the employer. The nature of the employee's role and the employer's business, the geographical scope of the restraint, and its nature and duration are relevant factors in assessing whether a restraint is reasonably necessary.*

Arguable case

[46] The question of whether Lanca has an arguable, but not necessarily certain, prospect of success at the Authority's investigation of the substantives issues (about final orders, penalties and damages) focussed on three disputed points:

(i) The existence of a legitimate proprietary interest; and

(ii) Whether the restraint terms said to apply to the three respondents were reasonable and enforceable; and

(iii) Whether there was any real breach of the terms.

Does Lanca still have a sufficient, legitimate proprietary interest?

[47] The evidence from Ms Zaloum's letter of 1 August and Mr Simpson's affidavit confirmed Lanca no longer traded. Consequently, the respondents submitted, Lanca had no arguable case that it had a proprietary interest to protect from competition. And, as Lanca had lost the CompAir agency with Gardner Denver in March 2014, Lanca had no proprietary interest in that relationship since then.

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[7] *Pottinger & Ors v Kelly Services (NZ) Limited* [2012] NZEmpC 101 at [16] – [18] (footnotes omitted).

[48] They also submitted that the warranties given to Atlas Copco by Lanca in the SPA were not open ended, the acquisition was completed and there was no real risk of claims for breach of warranty as the letters from Atlas Copco's lawyers to the respondents in late August showed Lanca had met disclosure duties in the period from agreement to completion of sale (between March 2014 and 1 September 2014).

[49] But Lanca argued the sale of the goodwill (including the trade and customer connections of the Ash Air business) to Atlas Copco did not extinguish its legitimate proprietary interest, for which the restraints on the respondents were necessary. The sale price of the business (of an undisclosed amount but in the many millions, including for goodwill) demonstrated the value of the 'property'. Lanca's interest, which survived the sale and the end of its own trading in the Ash Air business, was said to be in protecting the value of the purchase price and avoiding losses from a potential breach of warranty claim (if Atlas Copco were to make one).

[50] I have accepted that Lanca – arguably, if not certainly – retained a legitimate proprietary interest in the trade and customer connections that it had established by its investment and endeavour in developing the Ash Air business. While it may have realised a current market value of that interest through the purchase price achieved in the sale, its ability to do so relied – again, arguably – in some part on having a means to protect the value of the property sold to the purchaser. That means was the ongoing effect of the restraint terms. If those terms were no longer enforceable, a significant portion of the business purchased by Atlas Copco (specifically, some of the goodwill) could be of substantially less value. In that way I considered it met the broad definition of a legitimate interest justifying protection given in *Stenhouse Australia v Phillips*:[8]

> *The employer's claim for protection must be based upon the identification of some advantage or asset inherent in the business which can properly be regarded as, in a general sense, his property, and which it would be unjust to allow the employee to appropriate for his own purposes, even though he, the employee, may have contributed to its creation.*

[51] The effect of the restraint terms (and a right to enforce them) was arguably such an 'advantage'. It is a view that depends on an interpretation of the SPA definition of goodwill (that was sold to Atlas Copco) as excluding rights that Lanca had under contracts of employment – thereby meaning that restraint terms in the

[8] [1974] AC 391, 400 (per Lord Wilberforce).

respondents' employment agreements (and the benefit of them) were not 'sold' to Atlas Copco. It is a view that is contrary to Lanca's submissions that Atlas Copco also, under another part of the definition of goodwill in the SPA, was entitled to the 'benefit' of any covenants that Lanca held. In discussion on its submission Lanca's counsel suggested Lanca retained an exercisable right under the employment agreement while Atlas Copco had the benefit of the restraint covenants, through the terms of the SPA, as an enforceable *chose in action*. I have not agreed with Lanca's proposed interpretation on that point, or at least would say that it was only weakly arguable. If Lanca's interpretation was correct, the result would have the same effect as (or be analogous to) an assignment of a restraint of trade. Such assignment, without the consent of the employees involved, has been held by the Employment Court to be a matter of some doubt or at least no generally applicable principle and depending significantly on the particular facts of each case.[9] Of significance on that point is the fact that Atlas Copco did not appear to have pursued its initial claim (in its lawyers' letters to Mr Lenihan and Mr Readman on 29 August) that it was entitled to the benefit of the covenants given by the respondents to Lanca. Instead, it was Lanca that pursued the claim in the Authority, relying on the employment agreement and the former employment relationship.

[52] The notion of a residual or retained proprietary interest was not straightforward in the particular circumstances of the sale of the business assets and goodwill. However the categories of case in which covenants in restraint of trade may be enforced are not confined, rigid or exclusive.[10] And I considered the respondents' position that they were entitled to eschew ongoing obligations in respect of their former employer – by trading on connections and Ash Air's reputation for servicing CompAir products developed while they were on Lanca's payroll – did not sit easily with the body of case law developed over many decades about the balance between the property (that is proprietary) rights of former employers and the rights of work and entrepreneurship of former employees.[11] Mr Lenihan's email to Norske Skog was a clear example of seeking to trade on the reputation of Ash Air, and his work for it, that went beyond a mere expression of his skill and experience.

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[9] *PGG Wrightson Limited v Jary* [2008] ERNZ 476 at [16] and followed in *William Skerrett Investments Limited v Camelot New Zealand Limited* [2013] NZERA Christchurch 224 and *Precision Tracking (NZ) Limited v Tait* (ERA, CA 216/09, 16 December 2009, Member Doyle). See also *Choses in action* Laws of New Zealand at para [14] footnote 13.
[10] *Dawnay Day & Co Ltd v de Braconier d'Alphen* [1998] ICR 1068 (CA) at 1106 per Evans LJ.
[11] See, for example, *Dawnay Day & Co Ltd v de Braconier d'Alphen* [1997] IRLR 285 (HC) at 290.

[53] My assessment on that point, made within the inevitable limitations of the arrangements for determining an interim injunction application, may eventually not prove correct but I concluded Lanca's position on its legitimate proprietary interest was, at least, sufficiently arguable.

Reasonableness and enforceability of the restraint terms

[54] The respondents advanced several propositions against the arguability of the reasonableness and enforceability of the restraint terms to which they were said to be subject. These included:

(i) the employment agreements were not fairly made in the first place or had become inapplicable as a result of changes to their work position or location; and
(ii) the terms were an unreasonable prohibition on competition; and
(iii) Mr Lenihan's term of restraint was unreasonably long; and
(iv) A purported geographic limit on Mr Brickell was inapplicable and the absence of any reference to a geographic scope in Mr Lenihan's terms made any limit unreasonable.

(i) Were the agreements unfairly made and subsequently inapplicable?

[55] Mr Readman said he had signed his employment agreement in January 2014 without being provided a proper opportunity to read it and get advice. Although Mr Simpson disputed that account Mr Readman said he was under pressure to sign the agreement quickly because Mr Simpson had said it was paperwork necessary for the sale of the Ash Air business. Mr Readman said he did not read it but had told Mr Simpson, before signing it, "*don't screw me*".

[56] Mr Lenihan said Lanca had not told him of his right to seek independent advice before he signed his employment agreement in 2009 and he was not given a new employment agreement when he was promoted from Mount Maunganui branch manager to central operations manager in April 2011.

[57] Mr Brickell said he had no current written employment agreement at the time he resigned from Lanca because, after signing an agreement with Lanca in 2010, he had worked for, and was paid through the books of, another company in the Ash Air

business. When he returned to working directly for Lanca in early 2013 he was not given a new employment agreement.

[58] Those arguments, in respect of each man's employment agreements, were technical or (on a common sense assessment of their evidence) somewhat contrived. Any merit in them, I concluded, was significantly undermined by their actions in signing the Exlair employment agreements in April 2014. Each of those agreements had the same restraint provisions and there was no evidence of a lack of opportunity for the respondents to seek advice or any suggestion that they were not prepared to commit to and be bound by such restraint terms at the time. Those agreements themselves never became effective because each man had resigned from Lanca before the 'trigger' date was reached. The point, however, was that those agreements were said to contain the standard terms on which they were *already* employed at the time by Lanca. None of the respondents demurred or sought amendment.

(ii) Were the terms an unreasonable prohibition on competition?

[59] One of the restraint terms stood little or no prospect of being found reasonable or enforceable. In Mr Lenihan's case it was clause 16.2 that prevented him from being involved in any business similar to that carried on by the employer. In the case of Mr Readman and Mr Lenihan it was clause 4.1(c) that purported to prevent them from being involved "*in any business which is in competition with the business of the Employer*". Both clauses were under a heading in the respective employment agreements that began with the words "*non-competition*". The case law clearly prohibits a blanket ban on competition per se as noted in this explanation given in *Green v Transpacific Industries Group (NZ) Limited* (and referring to a similarly worded clause numbered 7.1):[12]

> *The effect of cl 7.1 is that all that the company is required to establish is the fact of competition in business. As it stands, cl 7.1 purports to prohibit competition by Mr Green even in respect of customers or potential customers who are or were not customers of Transpacific. Whilst a restraint may be lawful to the extent that it protects reasonably a proprietary interest that the employer has, including in business with its customers, the law does not extend to prohibiting competition alone as cl 7.1 purports to do. Clause 7.1, if it were valid, would prohibit Mr Green from engaging in economic activity (including being an employee of another waste disposal enterprise) if that entity competes for business with Transpacific irrespective of whether there was an actual or had ever been a previous commercial relationship between Transpacific and the potential*

[12] [2011] NZ EmpC 6 at [27].

> *customer of Mr Green or his new employer. The title to cl 7 of the employment agreement ("COVENANT NOT TO COMPETE") illustrates the misunderstanding of what the law allows and prohibits: competition per se is not able to prohibited.*

[60] The offending clause in the *Green* case said the employee would "*not work for a Competitor either directly or indirectly*" for the period of the restraint term. However the Court's decision in *Green* then accepted there was a sufficiently arguable case of reasonableness of restraints in an accompanying clause that referred to business with:

> *"a customer or actively sought prospective customer of the [former employer] with whom you have dealt, whose dealings you have supervised or about whom you have acquired confidential information in the course of employment".*

[61] The Court said those connections amounted to proprietary interests that the employer was "*very arguably entitled to protect by a reasonable restraint*".[13]

(iii) Was Mr Lenihan's longer restraint term reasonable?

[62] The respondents submitted there was no rationale for Mr Lenihan being subject to a 12-month restraint when the periods applicable to Mr Readman and Mr Brickell were six months.

[63] Mr Simpson's evidence was that Mr Lenihan had a longer restraint period because his role demanded significant client contact, he was involved in overseeing sales in the central region and he attended all sales meetings with the national sales manager relevant to his region. However he also described Mr Readman as having "*a significant amount of face to face contact with our clients*" and Mr Brickell as have strong relationships with oil and gas customers across the country. In that light the arguability was very weak for the reasonableness of a restraint period for Mr Lenihan that was twice as long as the others. On the evidence at this interim stage, I concluded a period of more than six months was not sufficiently arguable and was not likely to be upheld as reasonable in any final orders.

[13] At para [28].

(iv) Geographic limits

[64] Mr Brickell's employment agreement, signed in 2010, referred to the location of the position as being at "*Auckland Head Office*" and said his primary place of work would be at Lanca's "*premises*" at a specified Auckland address. However he had moved to New Plymouth in early 2013 to work for the Ash Air business there and soon after became its New Plymouth branch manager. On that basis the respondents' submitted the geographic limit of 50 kilometres referred to in his restraint term could only apply to a radius of that length from the Auckland office and not the New Plymouth branch office from which he had worked since 2013.

[65] By contrast Mr Lenihan's restraint terms referred to no geographic limit so were, in the respondents' submission, therefore cast on a worldwide basis that was unreasonable considering the branch area or region in which he had worked for Lanca.

[66] Neither point, in my assessment, was relevant given the limited portion of the restraint terms (apart from the protections against use of confidential business information) that were sufficiently arguable as likely to be held reasonable and enforceable in an Authority determination of final orders. That portion was the terms in the respondents' respective employment agreements that related to contacting and soliciting business from customers of Lanca. It was those trade and customer connections in which Lanca had an arguably enduring and protectable proprietary interest (on the particular terms of the SPA). The general geographic scope was thus irrelevant and inapplicable because the arguable restraint related only to particular, identifiable customers, whether they were located five, 50 or 500 kilometres distance from any branch or head office premises of Lanca.

[67] So what survived the respondents' detailed critique of the restraint terms were two important elements of Lanca's arguable case – firstly, the reasonableness and enforceability of the restraint terms in respect of contact with its customers and, secondly, sufficient doubt that the provisions for (and undertakings about) use of confidential information rendered the restraints unnecessary (and therefore unreasonable).

[68] The second element relied on the principles and concerns described in this way by the Court in *Allright v Canon New Zealand Limited*:[14]

> *... It is not possible to say as a matter of principle that, where the key interest of the party seeking to enforce a restraint is to protect its confidential information, that a restraint of trade will not be reasonable in addition to an express commitment to confidentiality. Inevitably, whether or not that is so will depend on the particular facts of the case. ...*
>
> *... In this case, it seems to me that there is very real weight in the submissions Mr Hood has advanced regarding innocent disclosure and, particularly, inadvertent use of the defendant's confidential information. This is not a case of a particular process or other specific trade secret which a departing employee might be expected to keep confidential without great difficulty. Rather, it is a case where the departing employee, through the importance of his position, has a very extensive knowledge of the employer's business at all levels. That knowledge includes a myriad of detailed information, some of which is confidential and some of which is not but which, in many cases, will be intertwined. The information comprises not only facts but also opinions and plans of possible action.*

[69] Together Mr Lenihan, Mr Readman and Mr Brickell – now collaborating in business together through their new positions at GCL – had considerable knowledge of the ins and outs of the operation of Lanca, its customers and the arrangements for the installing and servicing of the specialised equipment sold to them. Even if the undertakings offered indirectly through their solicitor as to the use of confidential information were sincerely made and binding, the risk of breach of the enduring confidentiality obligations from their former employment agreements with Lanca was significant. Mr Lenihan's email to Norske Skog showed his willingness to use Lanca's business information for GCL's potential commercial benefit. While he was free to use his general knowledge, skill and experience, the email showed use of actual business information (about the history and arrangements with that customer) that would normally be considered confidential to the employer. His actions supported Lanca's position that the restraint term was reasonably necessary to protect its residual proprietary interest against such customer contact.

Breach of the restraint terms

[70] The respondents submitted there was no, or at least insufficient, evidence of any real breach by them of the terms of the restraint (to the extent that they accepted the terms were applicable or enforceable against them).

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[14] (EC, AC 47/08, 3 December 2008, Judge Couch) at [27]-[28].

[71] Two alleged breaches – referred to in Mr Simpson's affidavit evidence – were weak, second-hand accounts of possible canvassing by Mr Readman and Mr Brickell of customers that they had dealt with when employed at Lanca. Mr Readman's own affidavit evidence denied he had any sales-related contact with VisyPET while Mr Brickell's affidavit was silent on Mr Simpson's allegation, except to deny he was doing anything to harm Lanca (who he said no longer had any customers anyway).

[72] However the example and content of Mr Lenihan's email to Norske Skog appeared to be a clear breach of the arguably reasonable element of his restraint terms relating to customer contact. It relied on business information he had gained from his role with Lanca. His affidavit confirmed the contact and said he intended asking if GCL could beat the servicing price Norske Skog was currently paying the Ash Air business. His evidence also showed that he recalled some details of that customer's 'spend' on Ash Air services. As the three respondents were now working together in GCL's business, the risk demonstrated by Mr Lenihan's actions could reasonably be ascribed to the other two men as well.

Availability of an adequate alternative remedy

[73] The respondents submitted damages that might result from any misuse of confidential information and solicitation of customers by them – if that were established and was a breach of their duties – were capable of a relatively straightforward assessment. I doubt that proposition. Losses of goodwill and opportunities of future custom are recognised as difficult to quantify.[15]

[74] Lanca's submissions on its potential liability under the terms of the SPA warranties did not really assist on this point but Lanca did validly identify a real issue about the respondents' ability to pay damages. The respondents had not provided any undertaking to do so and they gave no evidence that they were 'good for the money' if they had to pay for damages resulting from breaching any restraint terms found reasonable in the Authority's full investigation.[16] The affidavit evidence from Mr Lenihan, GCL's sole director and shareholder, suggested marginal availability of funds because of his commitments to leasing a building and paying creditors for stock

[15] *Marshment v Sheppard Industries Limited* [2010] NZEMPC 98 at [49].
[16] *Marshment,* above, at [37].

ordered along with personal mortgage and family financial commitments. In those circumstances I concluded damages were not likely to be an adequate alternative remedy to an interim injunction.

The balance of convenience

[75] The respondents submitted the balance of convenience weighed against the interim orders sought because:

(i) Lanca delayed making its application; and

(ii) Lanca lacked "*candour*" in what it said about the employment agreements; and

(iii) Lanca had ceased to trade so there was no evidence of any harm to Lanca from the respondents "*go[ing] about their business*"; and

(iv) Damages were an adequate alternative.

[76] Lanca submitted the following factors weighed in favour of the interim orders:

(i) The period of restraint was no longer than the respondents had contracted for and they had the benefit of Lanca's undertaking, with Lanca being good for the money because it had funds available from the sale of the Ash Air business; and

(ii) The respondents were not prevented from earning a living except for the disruption caused to business plans they had undertaken in full knowledge of their restraints.

[77] My assessment of the balance of convenience was influenced by my conclusion that the scope of the restraint terms that were likely to be upheld as reasonable and enforceable was limited to the restrictions on canvassing and soliciting customers of Lanca during the previous two years (and, consequently, an interim order could go no further than that). On that basis I considered the likely relative negative effects on Lanca of not granting the interim injunction sought were greater than those on the respondents of doing so.

[78] Contrary to the respondents' submissions, Lanca application was not unduly delayed. It was lodged within four weeks of becoming aware of Mr Lenihan's incorporation of GCL and (through the business cards email) learning of the three

respondents' positions in that business and only two weeks after learning of Mr Lenihan's email to Norske Skog. The respondents' other suggested factors in the balance were really only matters of disputed evidence.

[79] For the respondents, the terms of an interim order (and the resulting inconvenience) would still allow them to carry on developing their new business based on their CompAir agency – with the exception, for a relatively short period, of not seeking to deal with enterprises that were customers of Lanca over the previous two years. The Commerce Commission determination identified a number of other air compression equipment distributors and servicing firms in the New Zealand market. So, while Lanca had a significant share of that market, there were clearly other customers of other businesses that the respondents could (and probably were already) canvassing through their GCL business. Such customers would, and could, also include those customers of Atlas Copco in New Zealand who were not previously also customers of Lanca, as such Atlas Copco customers were not covered by the restraint terms arguably binding on the respondents.

[80] In terms of effects on third parties, in relation to the balance of convenience, I considered Atlas Copco and, generally, businesses in the New Zealand market for air compression products and services. Atlas Copco may face competition from GCL for its customers but they were outside the terms of the restraints on the respondents in any event. Businesses in the market for air compression products and services would not be subject to any long term inconvenience or loss of benefits to them from competition for their custom.

The overall justice of the case

[81] The respondents submitted the overall justice lay in denying Lanca's application. They suggested that conclusion should be reached from the answer to the question: who gets hurt? Lanca was not trading, its customers had passed to a third party (being Atlas Copco), and if the interim orders were granted, the respondents would suffer.

[82] However I have concluded the overall justice lay with Lanca for the relatively short period for which I considered it was reasonable to make interim orders

consistent with the sufficiently arguable terms of the restraints. The respondents had gone into their business with "*eyes wide open*" about the risks and with a deliberate plan to seek advantage based on the trade and customer connections developed by Lanca's business, not just the exercise of their skill, experience and knowledge of air compression equipment and servicing. While there is a public interest in allowing competition, there is also a public interest in protecting proprietary interests and the honouring of obligations entered into in employment agreements.

[83] I also considered Lanca had the stronger prospect of establishing at the Authority's full investigation of its claim, at least in respect of the soliciting term for a six month period, that the restraints on the respondents were reasonable and remained enforceable at Lanca's suit. I also considered other discretionary factors – such as the context of a broader commercial battle (between Gardner Denver and Atlas Copco internationally and locally)[17] and the supposed tentative preference in interim injunction applications for the *status quo ante* – did not change the conclusion on the overall justice of the matter.

Outcome and orders

[84] Although there was some variation in the wording of the restraint terms between the respondents' three employment agreements with Lanca, I considered the sole term – concerning soliciting of customers – for which an interim injunction should be granted was best expressed in the wording given in the agreements of Mr Readman and Mr Brickell. It was the same wording Mr Lenihan had agreed to with Exlair. It was also more limited and 'reasonable' than the actual broader wording of Mr Lenihan's agreement with Lanca, in the sense that it better defined which customers were in its scope (those of the last two years) and its length was six months, not one year. As a matter of likelihood I considered the term applying to Mr Lenihan would, at the Authority's full investigation, be modified in that way.[18] A single, consistent wording of the order for all three respondents also assisted with ease of compliance.

[85] The six month period of the interim order's application had to be adjusted according to the date on which each respondent ended their employment with Lanca.

[17] *Marshment* above at [55].
[18] Illegal Contracts Act 1970 s 8(1)(b).

The result was that, for Mr Readman, it applies up to 1 March 2015; for Mr Lenihan, up to 27 February 2015; and for Mr Brickell, up to 2 February 2015.

Next steps

[86] The Authority will shortly contact the parties to confirm scheduling of its full investigation of Lanca's claim for final orders, penalties and an enquiry into damages. As advised to the parties' counsel at the investigation meeting for submissions on the interim application, the likely date for such an investigation is in March or April 2015.

Costs

[87] Costs are reserved.

Robin Arthur
Member of the Employment Relations Authority