Many restraint of trade clauses are overly optimistic as to what the law will allow.

Restraint of trade

Andrew Lockhart-Mirams explains restrictive covenants and goodwill.

There has been a series of high profile cases in the High Court in London concerning the protection of goodwill in practices and businesses, and the enforceability of restrictive covenants following the termination of employment.

There are normally two types of protection which are relevant and sought by practice owners. Firstly, those joining practices wish to defend the goodwill of what they have come into, seeking to prevent those from whom they have purchased the practice to set up in competition immediately after the sale. Secondly, those with established practices may wish to prevent those engaged in the practice from seeking to depart and take the patients of the practice with them.

Andrew Lockhart-Mirams
is the founder of Lockharts Solicitors and a member of NASDAL.

Business sales

If you purchase a business you will inevitably pay a premium for the goodwill of the practice. Goodwill is a difficult concept to precisely define, but in the case of dental practices this is usually calculated by reference to the existing patient base and/or the turnover of a business. On purchasing a business, it is likely that you would want to prevent the seller from:

- solicitation of the existing patients of the practice;
- solicitation of current employees of the practice; and
- competing with the practice.

The typical restrictive covenants found in a sale purchase agreement would include:➲

A restrictive covenant is void as an unlawful restraint of trade unless the employer can show it goes no further than is reasonably necessary to protect his legitimate business interests.

- a non-competition clause;
- a non-solicitation clause; and a
- non-dealing clause.

In a business sale case, the purchaser's legitimate interest lies in protecting the value of the business which he has acquired as a going concern. The purchaser has an obvious interest in preventing the vendor from competing in such a way as to erode the value of what he has just sold. The law recognises that as a legitimate interest, especially if the vendor seeks to compete by attracting patients of his former business, or by attracting employees of his former business, or by using confidential information relating to the former business.

Whilst the law recognises these legitimate interests, it does not recognise them unless they are qualified. For a restrictive covenant to be enforceable it must be reasonable and go no further than is necessary to protect the legitimate interest.

There are many potential traps for the unwary in any business purchase or sale, of which restrictive covenants are just one example. Those looking to buy or sell a practice should take expert advice early in the process to ensure their protection throughout the transaction and afterwards.

Associates and employees

All associates and employees should have appropriate contracts setting out their duties and rights in the practice. Where appropriate, restrictive covenants can be included in employment agreements, just as they can in business sale agreements.

Whether there is a contract in place or not, it is a breach of duty for an employee to misuse confidential information belonging to his employer, for example, copying and taking a patient list in order to contact patients following departure.

It is possible to obtain an injunction against former employees under a so-called a 'springboard' which restrains the use of confidential information, or benefit from previous wrongdoing where this can be proved.

However, on the assumption that an associate, or employee, has done no wrong leaving the practice, but merely wishes to set up in competition, this will not be a breach of the duty of fidelity.

A restrictive covenant is void as an unlawful restraint of trade unless the employer can show it goes no further than is reasonably necessary to protect his legitimate business interests. This means that if a clause is aimed to prevent the former partner or associate working 'within five miles for five years', the court will not reduce it to 'within two miles for six months' if it concluded that the original clause was unreasonable but would have upheld the reduced ambit, had it been in the agreement in the first place.

In order to enforce a restriction in an employment contract, the employer must be able to identify some advantage or asset inherent in the business which can properly be regarded as his property, and which it would be unjust to allow the employee to make use of for his own purposes.

A restraint of trade clause just to prevent competition will not be upheld. There must be something in which the business has a legitimate interest in protecting.

In a recent case a springboard injunction and awards of damages were made where the employees had taken part in significant wrongdoing prior to their departure from a business. However, the restraint of trade clauses all failed before the court and were held to be unenforceable, as the business could not find (in the industry concerned) any objective basis for imposing terms in restraint of trade.

In many cases, especially where legal advice is not taken, restraint of trade clauses are overly optimistic as to what the law will allow. Deciding what the business wants to protect and what is likely to be reasonable in the circumstances are considerations that should be given before seeking to impose these terms. Careful drafting and identifying appropriate issues capable of protection is the key to having meaningful restraint of trade clauses in an employment contract.