A global guide to ‘restrictive covenants’
Introduction

There are few areas of employment law which differ as significantly between countries as the laws relating to post-termination restrictions. The increasing trend for key employees to have international responsibilities, be globally mobile, and for post-termination restrictions to apply across many different jurisdictions is a challenge. In reality when enforcement issues arise the decisions taken in the early stages of action may determine the outcome weeks or months later.

This is why the Guide to Restrictive Covenants was created, serving over 40 key countries. Within are discussions on non-compete covenants, non-solicitation covenants and non-solicitation of employees’ clauses, issues relating to employee benefits, pension, stock plans and more...

An essential publication for anyone involved in employment law, it has been compiled by lawyers from a major international law firm, as well as partner companies based in other jurisdictions.
A global guide to ‘restrictive covenants’

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A. OVERVIEW:

Post-employment restraint clauses or restrictive covenants are commonly used by Australian employers to protect their business interests, particularly in employment contracts for professional or senior/managerial employees.

A typical restraint clause will impose restrictions on the employee not to work in any capacity for a competitor, for a specified period after they leave the employer’s business; not to solicit their former employer’s clients, customers or staff; and not to use their former employer’s confidential information.

These types of clauses operate subject to the common law doctrine of ‘restraint of trade’. This means that a restraint clause must be directed at protecting specific interests of the employer (such as trade secrets or business goodwill). The courts will not uphold a restraint clause that restricts competition per se, or unduly interferes with an employee’s right to sell his or her own labour.

In assessing the validity of a restrictive covenant, an Australian court will determine whether the restraints imposed on the employee are reasonable having regard to their duration; the geographic area in which they apply, and the activities of the employee that they seek to control.
A global guide to ‘restrictive covenants’

Australia

There is some capacity for a court to sever a restraint clause that it finds to be unreasonable, enabling the reasonable elements of the clause to be enforceable against the employee. Except for the State of New South Wales (where specific restraints of trade legislation applies), severance is usually only possible where the clause contains a series of overlapping restraints, known as a ‘step’ or ‘cascading’ restraint clause.

An employer will usually seek to enforce a restrictive covenant against a former employee through an application to a Federal, State or Territory court for an interlocutory injunction. Other remedies that may be available include a permanent injunction or an order for damages.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

An employer cannot unilaterally impose such a covenant upon an existing employee, although the employer can condition any new offer of employment upon the prospective employee (and sometimes on the offer of a promotion) into such a covenant. The inclusion of a restraint clause in an employment contract is a matter to be negotiated between the employer and employee. However, as indicated above, such clauses are commonly entered into by senior executives, managers and other professional employees.

i. Are they capable of being valid?

Although post-employment restraints are commonly used, they are presumed to be invalid and unenforceable unless it can be shown that they are necessary to protect a legitimate business interest: Nordenfeldt v Maxim Nordenfeldt Guns and Ammunition Company [1894] AC 535.

The onus rests with the party seeking to enforce a restrictive covenant to demonstrate that the clause imposes no greater restraint than is reasonably necessary to protect its legitimate commercial interests: Lindner v Murdock’s Garage (1950) 83 CLR 628. Employers cannot use a restraint clause to protect themselves against mere competition: Stenhouse Australia v Phillips [1974] AC 391.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The legitimate interests of an employer that are recognised as supporting a valid post-employment restraint include the employer’s confidential information or trade secrets; customers and clients of the employer’s business; and the employer’s staff (each of these is explained further in the relevant sections below).

A typical post-employment restraint clause that would be upheld by an Australian court would be one of between three and twelve months’ duration: see e.g. Smith v Nomad Modular Building Pty Ltd [2007] WASCA 169 (six months); Seven Network (Operations) Limited v Warburton (No 2) [2011] NSWSC 386 (eight months). The period must be reasonable to protect the legitimate interest.

That said, a restraint clauses of two years’ duration was upheld in a recent decision of the Full Federal Court of Australia: Pearson v HRX Holdings Pty Ltd [2012] FCAFC 111. In that case, relevant factors supporting enforcement of the restraint (which also contained no geographic limitation) included:

• the fact that the former employee against whom the restraint clause was directed had access to almost all of the employer’s confidential business information, such as sales and client retention strategies;

• the former employee’s status as a key figure within the employer’s human resources consultancy, until his attempt to move to a direct competitor in breach of the restraint clause;

• the original employer’s legitimate interest in protecting its client relationships;

• the fact that the former employee received shares in the business and payment for 21 months of the two-year restraint period, as part of what the Full Federal Court described as a ‘reasonable commercial arrangement as between the parties’. 
In contrast, in Wallis Nominees (Computing) Pty Ltd v Pickett [2013] VSCA 24, the Victorian Supreme Court (Court of Appeal) refused to enforce a restraint clause which purported to prevent a former employee from working for a competitor for 12 months after his employment had ended. The Court found that the duration of the restraint was longer than necessary to protect the employer’s legitimate interests in its relationships with customers.

Wallis Nominees (Computing) Pty Ltd v Pickett also illustrates that when drafting restrictive covenants, employers must be careful not to cast the restraints on an employee’s post-employment activities too broadly; and should use ‘step’ or ‘cascading’ clauses. The Court of Appeal would not sever the parts of the restraint clause which it had found to be invalid in this case, because the restraint did not include ‘cascading’ provisions which would have enabled the unreasonable parts to be excluded and the remaining parts of the clause to have effect. As the Court stated: ‘the impugned part [of the clause] must be capable of simply being removed — as if simply crossed out with a blue pen; a court can remove words from a restraint clause but not rewrite it …’. See also Integrated Group v Dillon [2009] VSC 361; Hanna v OAMPS Insurance Brokers Limited [2010] NSWCA 267.

In New South Wales, specific legislation (Restraints of Trade Act 1976 (NSW)) enables the courts of that State to read down an invalid restraint clause, to give it the extent of operation that the court considers reasonable (irrespective of whether the clause contains ‘step’ or ‘cascading’ provisions). This legislation will apply in respect of any employment contract (containing a restraint clause) that has a close and real connection with NSW: see e.g. Provida Pty Ltd v Sharpe [2012] NSWSC 1041 (where the employer’s head office was in NSW, but the employee carried out work in both NSW and Victoria, the NSW legislation was held to apply).

iii. Is it necessary to pay an employee during the period of the covenant?

No, but this may be a relevant factor in determining the validity of a restraint clause (see Pearson v HRX Holdings Pty Ltd [2012] FCAFC 111, discussed above). At the same time, the fact that payment is provided to an employee during the restraint period will not make an otherwise invalid restraint lawful (see e.g. Tullett Prebon (Australia) Pty Ltd v Purcell [2008] NSWSC 852).

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

This is a matter for negotiation between employer and employee (as explained at the commencement of section b. above).

i. Are they capable of being valid?

Yes, provided the restraint clause does no more than protect the employer’s legitimate business interests; and is reasonable in terms of its duration and geographical reach.

ii. What does it take to show they are valid?

The nature of an employer’s interest in protecting its customer base through express contractual provision binding on a former employee was described by the Full Federal Court in Pearson v HRX Holdings Pty Ltd [2012] FCAFC 111, as follows: ‘HRX had an evident interest in preserving the customer connections which are the source of its income. It is well established that an employer’s customer connection is a legitimate business interest which can support a reasonable restraint of trade where the employee in question controls the employer’s customer connections (see, for example, Jardin v Metcash Limited [2011] NSWCA 409 …’).

In Wallis Nominees (Computing) Pty Ltd v Pickett [2013] VSCA 24, the Victorian Court of Appeal stated that the obligations of an employee under the non-solicitation provisions of a restraint clause are dependent on two factors: ‘First, that an employee must be in a position to gain trust and confidence so as to be relied on in a client’s affairs. Secondly, that the relationship between employee and client is such that there is a possibility that if the employee leaves the business of the employer he or she may carry away the client’s business with them.’
A valid post-employment restraint clause will typically preclude an employee from approaching or seeking to lure away clients or customers of their former employer, during the restraint period. Usually, such a clause will only be effective in respect of clients/customers with which the employee actually had contact during his/her employment with the former employer: see e.g. John Fairfax Publications Pty Ltd v Birt [2006] NSWSC 995.

Of course, it may be possible for an employee to avoid the application of a non-solicitation clause by establishing that the former employer’s clients ‘came to them’, rather then being approached by the employee during the restraint period.

iii. Is it necessary to pay an employee during the period of the covenant?

No, but this may be a relevant factor in determining the validity of a restraint clause (see section b. (iii) above).

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

This is a matter for negotiation between employer and employee (as explained at the commencement of section b. above).

i. Are they capable of being valid?

Yes, provided the restraint clause does no more than protect the employer’s legitimate business interests; and is reasonable in terms of its duration and geographical reach.

ii. What does it take to show they are valid?

An increasing tendency in recent Australian case law is the recognition of an employer’s legitimate interest in the maintenance of a stable workforce, through post-employment restraints prohibiting an employee from poaching his/her former employer’s staff: see e.g. BDO Group Investments (NSW-Vic) v Ngo [201] VSC 206; Informax International Pty Ltd v Clarius Group Limited [2011] FCA 183.

However, post-employment restrictions on poaching or soliciting other employees of the former employer will not be enforceable in certain situations – for example, where those employees simply respond to a general employment advertisement (Allied Express Transport Pty Ltd v Mears [2010] NSWSC 1112); or there is other evidence that the employee subject to the purported restraint has not initiated contact with or sought to persuade those employees to move over to the new employer.

In some circumstances, the rival firm to which a former employee moves may also be held liable where the move occurs in breach of an express contractual restraint clause (i.e. the rival firm may be found liable for inducing the breach of contract): see e.g. Wilson HTM Investment Group Limited and Others v Pagliari and Others [2012] NSWSC 1086.

iii. Is it necessary to pay an employee during the period of the covenant?

No, but this may be a relevant factor in determining the validity of a restraint clause (see section b. (iii) above).

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

Post-employment restraint clauses typically provide an employer with protection against a former employee’s use of the employer’s confidential business information or trade secrets, during the restraint period. This aspect of a restrictive covenant will be valid provided that it does no more than protect the employer’s legitimate business interests, and is reasonable in terms of its duration and geographical reach.
The kinds of information that may legitimately be protected in an express confidentiality provision in a restraint clause include information that the employer specifically designates as confidential (e.g. John Fairfax Publications Pty Ltd v Birt [2006] NSWSC 995), and information that was only made available to the employee because of the special nature of his/her position or role within the employer’s business (e.g. Smith v Nomad Modular Building Pty Ltd [2007] WASCA 169). However, protection would not extend to information that is readily available in the public domain (e.g. GlaxoSmithKline Australia Pty Ltd v Ritchie [2008] VSC 164).

So, for example, business operational information, financial data and reports, details of customers and suppliers, marketing/strategic plans, pricing models, and trade secrets such as manufacturing formulae or processes, would all constitute genuinely confidential information which may be the subject of protection through an appropriately worded restraint clause.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

Choice of law may become an issue in the enforcement of a restrictive covenant under Australian law in one of two ways:

1. Choice between Australian and foreign law: this could arise, for example, in relation to enforcement of a post-employment restraint against an employee of an overseas-based company working in Australia. In this situation, it is likely that an Australian state or territory court would apply the law applicable to restraint clauses in that state or territory – even if the contract had been entered into in an overseas jurisdiction (following the approach adopted in Rousillon v Rousillon (1880) 14 ChD 351). An alternative approach (based on Apple Corps Limited v Apple Computer Inc (1992) Fleet Street R 431 (ChD)) would see the Australian state or territory court being guided by the law nominated by the parties in their contract (i.e. the proper law of the contract). If they chose the law of an overseas jurisdiction to regulate their agreement, then the restraint of trade principles operating under that overseas law would be applicable. Conversely if they nominated the law of an Australian jurisdiction, that would be applicable. Although the issue has not been finally determined, the Rousillon approach is considered more likely to apply (see A Stewart and J Greene, ‘Choice of Law and the Enforcement of Post-Employment Restraints in Australia’ (2010) 31:2 Comparative Labor Law and Policy Journal 305, 322-326).

2. Choice of law among Australian jurisdictions: this is generally not a major issue given the similarities in restraint of trade laws operating throughout Australia, with the exception of the specific legislation operating in NSW (see section b. (ii) above). Given that the Restraints of Trade Act 1976 (NSW) provides employers with greater scope to enforce post-employment restraints than other Australian jurisdictions, it might be expected that employers would seek to make NSW the governing law of their employment contracts (perhaps, in some instances, artificially). However, this does not (in our view) occur to any appreciable extent. As outlined in section b. (iii), for the NSW legislation to apply, there must be a real and close connection between the employment contract and the State of NSW. In some cases, this has been expressed in terms of requiring that the proper law of the contract is NSW in order to attract the operation of the NSW legislation (see e.g. K.A. and C. Smith Pty Ltd Co v Ward (1998) 45 NSWLR 702; Professional Advantage Pty Ltd Co v Smart [2008] NSWSC 873, discussed in Stewart and Greene, supra, 326-328).

i. Can an employer impose a dispute resolution method on the employee?

Like the issue whether a restrictive covenant is included in an employment contract to begin with, the dispute resolution method that operates in respect of the covenant is a matter for negotiation between employer and employee. This will usually be determined by the general dispute resolution clause which the parties include in their employment contract; and/or the clause relating to the governing law applicable to the contract.
**Australia**

**G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?**

The usual remedy sought by an employer seeking to enforce a post-employment restraint is an injunction (on an interlocutory basis) restraining the former employee from taking up a new position, soliciting the employer’s clients or staff, and/or using confidential information in breach of the applicable restraint clause. The granting of such an injunction (pending a full trial of the matter) requires the employer to establish a prima facie case of breach by the employee of the restrictive covenant, and that the balance of convenience favours the injunction being granted (American Cynamid Co v Ethicon Ltd [1975] AC 396).

If an interlocutory injunction is granted, it is rare for the employer’s claim to proceed to trial. However, when that does occur, the other main remedy that is available is an order for damages to compensate the employer for any monetary loss suffered as a result of the employee’s breach of contract. For example, in Commercial & Accounting Services (Camden) Pty Ltd v Cummins [2011] NSWSC 843, the NSW Supreme Court awarded A$117,995 in damages following an employee’s misuse of confidential client information belonging to his former employer (although note that the employer’s action in this case was based on the equitable duty of confidence rather than a contractual restraint clause).

Importantly, an employer may not be able to obtain remedies to enforce a post-employment restraint where the employee has been wrongfully dismissed or made redundant: see e.g. Ecolab Pty Ltd v Garland [2011] NSWSC 1095.

**H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:**

i. Do the same principles of enforcement outlined above at g. apply?

Under Australian law, the enforceability of post-employment restraints is a separate matter from the entitlements of employees under pension schemes (known in Australia as ‘superannuation’ entitlements) and stock plans. Employees are entitled to receive minimum superannuation contributions under federal legislation. These entitlements cannot be foregone in the event that an employee breaches a restrictive covenant (even if an employment contract made provision for such an arrangement, it would be unlawful). Stock plans are common for senior executives, through provisions setting out an employee’s share entitlements in the employment contract or a separate deed. This could conceivably include provision for the foregoing of share entitlements in the event of the employee’s breach of a restraint clause.

ii. Which covenants are typically imposed?

See (i) above.

iii. What sanctions are/can be imposed by the employer for non-compliance?

See (i) above.

iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)

See (i) above.

**I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?**

Some aspects of a restrictive covenant which are found to be invalid may be struck out with the balance remaining enforceable, although this will depend on the form and substance of the particular clause (see sections a. and b.(ii) above). There is greater flexibility to read down an invalid restraint clause in New South Wales (see section b. (ii) above).

Contributed by Anthony Forsyth, Chris Leong and Heidi Roberts
Hong Kong

A. OVERVIEW:
Post-termination restrictive covenants are fairly common in Hong Kong employment contracts, particularly for senior employees or those with valuable connections, relationships or access to confidential information.

The principles for restrictive covenants are well established. Contractual terms restricting an employee’s activities after the termination of their employment are generally void for being in restraint of trade and contrary to public policy unless the employer can show that the provision is reasonable in all the circumstances to protect a legitimate interest of the employer.

In broad terms, the legitimate interests a court might allow to be protected fall into the following categories:

(a) trade connections such as customers or suppliers and, more generally, goodwill;
(b) trade secrets and other confidential information; and
(c) stability of the workforce.
Hong Kong

Once a legitimate interest has been established, the employer should impose a restrictive covenant which only goes so far as to be reasonably necessary to protect that particular interest by reference to the relevant activities, the duration and the geographical scope sought to be covered by the restraint.

Whether a restriction is reasonable is judged at the time the restriction is entered into.

Common post-employment restrictions in the employment context include non-solicitation, non-dealing and non-competition clauses.

The most common remedy for breach of a restrictive covenant is an injunction, using the civil courts, to restrain the employee’s or the new or prospective employer’s activities but other forms of remedies are available.

Other remedies include damages for breach of contract although this is often difficult to establish.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The general principles mentioned above apply. A non-competition restriction is typically harder to enforce than a non-solicitation and non-dealing clause.

It is arguable that the employer’s interests are adequately protected by a non-solicitation and/or non-dealing covenant and the employee’s implied, and usually express, confidentiality obligations.

Although restrictions for up to six months can in certain circumstances be enforceable, a three month restriction is much more likely to be effective, particularly where the period of restraint is reduced by any period of garden leave served by the employee.

An issue with non-competition restrictions in Hong Kong is the geographical limitation.

A general blanket restriction which prohibits the employee from taking employment within the whole of Hong Kong will only be enforceable where it can be shown to be justifiable to protect an employer’s legitimate interests. In some circumstances even restricting someone from taking up employment in Central does, in reality, often mean that he is being restricted from taking up employment in Hong Kong and may be unenforceable.

In each case it will depend on the specific circumstances of the employee and the particular legitimate interests which the employer is trying to protect.

iii. Is it necessary to pay an employee during the period of the covenant?

There is no legal requirement to pay an employee during the period of a non-compete post-termination restrictive covenant. However, paying the employee could help address the argument against a non-compete covenant being enforceable because it prevents the employee from earning a living.
C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes. These can either prevent the solicitation of clients/customers or additionally the acceptance of work from the client/customer even if not previously solicited by the employee.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

Although non-solicitation/dealing clauses are generally easier to enforce than a non-competition covenant in the sense that they are less obstructive on an employee, the general principles mentioned above apply.

The covenants should be restricted by reference to customers/suppliers with whom the employee has had dealings during a specified period before the date of cessation of the employee’s employment.

Again, a reasonable time limit to this restriction may be the amount of time that it is likely to take for the influence of the departing employee to be replaced by the influence of that employee’s successor.

These restrictions can cover non-solicitation of, or non-dealing with, customers/clients. Solicitation tends to cover more active targeting of customers. Non-dealing prevents the employee from accepting business from a customer even if they had not actively sought out that business.

A non-dealing covenant is therefore more difficult to enforce, although it has been upheld where the employer can demonstrate that solicitation is hard to police, and is usually used together with a non-solicitation covenant. It is necessary for the employer to show a legitimate interest in having the covenant upheld.

Prospective customers/clients can be included in this type of restriction but this would generally be limited to those that the employee was actively targeting prior to cessation of employment.

iii. Is it necessary to pay an employee during the period of the covenant?

There is no legal requirement to pay an employee during the period of a non-solicitation of customer post-termination restrictive covenant.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Non-solicitation clauses have been upheld by the Court.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

If a post-termination of employment non-solicitation of employee covenant is sufficiently tightly worded then certain employees can be protected. It has been held that an employer may have a legitimate interest in maintaining a stable workforce in a highly competitive business.
Therefore, any clause which seeks to prohibit the poaching of employees will need to assess how long the departing employee will have influence over existing employees and the scope of the class of employees over whom the influence will exist.

In order to improve the chances of the clause being enforceable, the scope should be limited to employees with whom the departing employee had contact for a period prior to departure and be limited to senior employees already in the employ of the employer. Smaller companies may be able to enforce a restriction that covers a wider set of employees.

Unfortunately, the ability for an employee to make payment of wages in lieu of notice and leave tends to reduce the effectiveness of these clauses and in practice it is often difficult to prove that the employee was solicited by the ex-employee.

iii. Is it necessary to pay an employee during the period of the covenant?

There is no legal requirement to pay employees during the period of a non-solicitation of employees post-termination restrictive covenant.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

Yes.

There are a variety of restrictions that can apply during or after termination of employment.

A common clause is to restrict the use and disclosure of confidential information and company property, during employment and after its termination. The restriction on use and disclosure of confidential information often does not have a set time limit after termination and instead apply for as long as the information retains its confidential nature.

Other post-termination restrictions can cover non-solicitation of or non-dealing with suppliers, distributors or intermediaries such as brokers, depending on the employer’s business. These are similar to the customer/client restrictions mentioned above. Employees can be prevented from interfering with the ex-employer’s business or connections, although this tends to require some kind of active attempt or intention to damage the ex-employer’s business.

Restrictive covenants are sometimes supplemented by provisions such as a requirement to inform their employer if they are aware of a raid on the employer’s workforce (a team move), to alert the employer to another employee’s wrongdoing or even to the employee’s own wrongdoing, or to provide a prospective new employer with a copy of the restrictive covenants. However, breach of this type of clause may only result in nominal damages.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

Choice of law will be relevant to which law governs the contract (and therefore how the contract should be interpreted and enforced).

In summary, if Hong Kong law applies to the contract, then the principles mentioned above will apply to the interpretation and enforcement of restrictive covenants.

i. Can an employer impose a dispute resolution method on the employee?

It is generally still unusual to see alternative dispute resolution procedures provided for in Hong Kong employment contracts.

Since the primary remedy for enforcing restrictive covenants is an injunction, which is usually obtained through the Courts, there would typically be no obvious benefit in having an alternative dispute resolution procedure which prevents the employer from seeking an order for an injunction.
Hong Kong

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

The most common remedy for breach of a restrictive covenant is an injunction using the civil courts, to restrain the employee’s or the new or prospective employer’s activities but other forms of remedy are available including an order to pay damages.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

A forfeiture of an award or partial award, for prohibited competitive activities can be challenged if the employee claims that the provisions allowing forfeiture are unenforceable as being in restraint of trade. The same approach will be taken to evaluating these clauses as is taken when looking at the equivalent clauses in employment contracts.

ii. Which covenants are typically imposed?

Covenants imposed will tend to mirror the covenants contained in the standard form employment contracts, although there is no requirement that this is the case. As such these covenants could range from non-competition covenants through to non-dealing and non-solicitation of customers clauses.

iii. What sanctions are/can be imposed by the employer for non-compliance?

Injunctive relief is less common, as the plan documentation does not usually impose a specific prohibition on the relevant behaviour – rather forfeiture of all parts of the award if the behaviour occurs. It is more common for a forfeiture provision to apply to unvested incentive awards if the participant engages in the relevant behaviour. In addition, there may be claw back of amounts paid (or repayment of any value realised on sale of shares delivered) on the vesting of awards. Where shares are delivered, it may be possible to prohibit sale of the shares until expiry of any relevant covenant period, possibly coupled with some form of security over the shares. Injunctive relief may be available if the award documentation contained a prohibition on the relevant behaviour.

iv. Are there any limits to what an employer can forfeit (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?

There are generally no specific limits in relation to long term incentive arrangements. However, there may be limits to what the employee is prepared to agree to. In addition, the provision must meet the criteria outlined in (a) above to be enforceable.

An employer should be conscious of obligations under the Employment Ordinance in relation to timing of the payment of sums due to the employee and unlawful deduction from wages, to the extent that the relevant incentive arrangement may be caught by the employment Ordinance (e.g. the payment is “wages” or is an “end of year payment”).

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

An invalid clause is unenforceable.

Although a court will not rewrite an invalid clause to make it enforceable, it may apply the ‘blue pencil test’ and sever a particular part (which is considered invalid) of the restrictive covenant and uphold the remainder of the covenant.

For example, if the non-competition clause is held to be invalid, then the employer could still rely on the non-solicitation and non-dealing clauses provided those aspects of the restrictive covenant were found to be enforceable.

It is important to note that a court will only apply the ‘blue pencil test’ if the unenforceable element can be severed without having to modify or add to the remaining wording and if, by doing so, it does not materially change the nature of the original restriction.

Contributed by Duncan Abate, Hong Tran, Kay McArdle
A. OVERVIEW:

In India, post-termination restrictive covenants, such as non-solicit and non-compete clauses are routinely included in employment contracts. While Indian courts have upheld non-solicitation of customer clauses, non-compete provisions which extend beyond the term of employment are not enforceable. Companies generally retain post-termination non-compete clauses in the employment contracts since they act as a deterrent to the employees.

Under section 27 of the Indian Contract Act, 1872 any agreement in restraint of trade is void. Consequently, non-compete covenants (requiring past employees not to accept employment with competitors of the employer) extending beyond the term of the employment contract are not enforceable in India. Courts do not recognize reasonable non-compete restrictions and have on several occasions held that all post-termination non-compete provisions are in the nature of restraint of trade and therefore unenforceable.

However, commercial non-solicitation clauses between parties restricting them from offering inducements to employees, customers, clients and suppliers of the other are enforceable. Usually employers include post-termination non-solicitation for any period between 6 – 12 months.
India

The most common remedy for breach of non-solicitation obligations is an injunction using the civil courts, to restrain the employee’s activities. Other possible remedies, though untested, include damages for breach of contract and other forms of financial compensation.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

No.

i. Are they capable of being valid?

No.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

As mentioned above, non-compete clauses, in any form, are unenforceable in India.

iii. Is it necessary to pay an employee during the period of the covenant?

Not applicable in the Indian context.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes. Such clauses can prevent the solicitation of a client/customer by a former employee, but cannot be wide enough to prohibit acceptance of work from the client/customer if not previously solicited by the employee.

i. Are they capable of being valid?

Yes, to a limited extent.

ii. What does it take to show they are valid?

It is not common to have contact prohibition clauses. Even when such clauses are present they would be enforceable to the extent of non-solicitation of customers/clients. As mentioned earlier, such obligation cannot be wide enough to prohibit acceptance of work from the client/customer if not previously solicited by the employee.

iii. Is it necessary to pay an employee during the period of the covenant?

There is no legal requirement to pay employees during the period of post-termination contact prohibition clauses.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Clauses on non-solicitation of employees have been upheld by the Court in commercial contracts. Similar principles should apply to non-solicitation of former colleagues as well. However recruiting former colleagues, where there is no solicitation, is not unlawful.

i. Are they capable of being valid?

Yes.
ii. What does it take to show they are valid?

Most restrictions of this type will define the employees who cannot be approached or hired by reference to their seniority, grade or level, or their role in or importance to the business. They often only apply to colleagues that the departing employee had a reasonable level of contact with, knowledge of or responsibility for, and within a defined period before the departing employee leaves. Smaller companies may be able to enforce a restriction that covers a wider set of employees.

While non-solicit obligations are enforceable, the onus would be on the employer to prove that there was actual solicitation by the former employee which led to the hiring. In India, while solicitation can be prohibited, it is not possible to prohibit the hiring of employees by a former employee. Accordingly, in practice, it is difficult for employers to prove that a non-solicitation of employees’ clause has been breached, because merely showing that the employee has been hired by a former colleague is not necessarily a breach of the non-solicitation clause.

Therefore, non-solicitation of employees clauses are generally the weakest type of covenant and the easiest to circumvent.

iii. Is it necessary to pay an employee during the period of the covenant?

There is no legal requirement to pay employees during the period of post-termination non-solicit clauses.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

During the existence of an employer-employee relationship, employers will be able to enforce non compete clauses, which prevent the employee from engaging in any competing business, colluding with a competitor etc. As mentioned above, though such clauses will not be enforceable post termination, they would be enforceable during the course of employment.

Additionally, in order to protect trade secrets and confidential information, employers often include a clause prohibiting employees from disclosing certain defined forms of confidential information (such as client information, intellectual property related information etc.) during the course, and after the termination of the employment. Such covenants are enforceable.

The scope of non-solicitation covenants, similar to the customer/client restrictions mentioned above, can be wide enough to cover suppliers, contractors, dealers, distributors or intermediaries such as brokers, depending on the employer’s business.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

Irrespective of the choice of law provision, the Indian courts would continue to have jurisdiction when the employee is working in India. When the parties are in India, the courts would normally apply the local law when determining whether the restrictive covenant is enforceable. Hence the choice of law provision would have no impact.

Can an employer impose a dispute resolution method on the employee?

The primary method for seeking relief for breach or threatened breach of restrictive covenants is injunction, which can be sought by approaching the courts. Therefore, the use of methods of alternate dispute resolution, such as arbitration, mediation etc., may not achieve the desired result since it will prevent the company from seeking injunction.
India

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

As mentioned above, the courts are unlikely to enforce non-compete covenants. However, with regard to the other restrictive covenants, an employer can pursue the following remedies:

- **Damages** – The company may approach a court to seek remedies for breach of contract. However, the remedies are likely to be limited to damages only based on the actual loss suffered by the company.

- **Injunction** – Where the restrictive covenants have not been breached, the company could approach the court for an injunction (which would prevent the employee from approaching employees and customers/clients of the company or disclosing confidential information, as the case may be).

- **Tortious Interference** - Another option that exists (in cases where the former employee has joined a competitor) is to seek damages from the company which the former employee has joined. The damages can be claimed under the law of torts if it can be shown that such a company had induced the former employee’s breach of contract. Considering the company will have a greater paying capacity than the former employee, this could be a viable option.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

Generally, restrictive covenants are not relevant to, or enforceable against, an employee’s pension benefits. Benefits and pensions which are statutorily due to an employee cannot be withheld subject to his/her non-adherence to any restrictive covenants. If the employer and employee have entered into a contractual arrangement whereby the employee will become entitled to certain additional amounts if he complies with some specific restrictive covenants, the same may be enforceable.

However, even these contracts should be worded so that the amounts payable are purely contractual. The language of the contract should not be such that these amounts may be deemed to be ‘wages’ and capable of being claimed by the employee as a matter of right, as wages.

ii. Which covenants are typically imposed?

See h. (i) in relation to pension benefits.

If the employer and employee were to contractually enter into agreements of the nature mentioned above, then the restrictive covenants that can be enforced may include non-solicit, confidentiality and other standard clauses in the employment contract (but not post-termination non-compete clauses, which, as discussed above, are void in India).

iii. What sanctions are/can be imposed by the employer for non-compliance?

See h. (i) in relation to pension benefits.

For others, sanctions will usually include claw back/forfeiture of the amount that would have become due if the employee had complied with the restrictive covenants.

iv. Are there any limits to what an employer can forfeit (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?

Claw back of paid or vested amount would normally be difficult to implement because once a right has accrued and been paid, it is difficult to claim it back under Indian law. In addition to the difficulty of recovering such benefits from employees, there will also be difficulties from a tax regulation perspective since an employee will not be able to recover paid income tax from the government directly.
India

Further, for employees earning less than INR 10,000 the provisions of the Payment of Wages Act would be applicable which permits deductions in only certain limited circumstances.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

Restrictive covenants that are invalid are unenforceable. A court can apply the rule of severability and hold that a particular element of a restrictive covenant is invalid and uphold the remainder of the covenant.

However, a court will not re-write a covenant. It will only apply the rule of severability if the unenforceable element can be severed without having to modify or add to the remaining wording and if, by doing so, it does not materially change the nature of the original restriction.

Contributed by Ajay Raghavan
A. OVERVIEW:

Post-termination restrictive covenants are frequently used in Japan, especially in contracts that involve employees in senior positions or specialists who have access to valuable and/or confidential information. Although post-termination restrictive covenants are useful to protect the employer’s trade secrets, they may infringe on an employee’s right to choose his/her occupation which is guaranteed under Article 22 of the Constitution of Japan. Accordingly, post-termination restrictive covenants may be deemed invalid on the ground that they are against public order under Article 90 of the Civil Code of Japan.

Courts will generally examine if a post-termination restrictive covenant is “reasonable in scope,” taking into account:

(1) if and how the post-termination restrictive covenant is necessary to protect the employer’s legitimate interest, and
(2) if and how the post restrictive covenant restricts the employee’s freedom to choose his/her occupation.

Whether a post-termination restrictive covenant is “reasonable in scope” is based on factors such as:

(1) the purpose of the post-termination restrictive covenant,
Japan

(2) the position, role and seniority of the employee,
(3) the time period of restriction,
(4) the geographical extent of the restriction,
(5) the scope of restriction in terms of type of business or job, and
(6) the existence and amount of compensation paid in return for the restriction.

Remedies for breach of a post-termination restrictive covenant are:
(1) an injunction to restrain the employee’s activities, and
(2) a claim for compensation for damages against the employee.

In addition, many companies in Japan include a provision in their retirement allowance rules that either no retirement allowance, or only a reduced retirement allowance, will be paid to the employee if the employee takes any action which can be a ground for a disciplinary dismissal, including the breach of a post-termination restrictive covenant.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The general principles mentioned above regarding post-termination restrictive covenants also apply to the validity of a post-termination non-competition covenant. In determining the validity of a post-termination non-competition covenant, the court will examine factors such as:

(1) the purpose of the covenant,
(2) the position, role and seniority of the employee,
(3) the period of restriction,
(4) the geographical extent of the restriction,
(5) the scope of restriction in terms of type of business or job, and
(6) the existence and amount of compensation paid in return for the restriction.

When drafting post-termination non-competition restrictions, it is important to ensure that the period of restriction, the geographical extent of the restriction and the scope of restriction (in terms of type of business or job) are reasonably limited considering the purpose of the restriction (i.e., the contents of the interest that the employee wishes to protect by the covenant) and the position, role and seniority, etc. of the employee.
C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

Although the general principles mentioned above regarding the validity of post-termination non-compete restrictions will apply, post-termination non-solicitation clauses do not directly infringe upon an employee’s constitutionally guaranteed right to choose his/her occupation. Thus, non-solicitation clauses are generally enforceable. In practice, the scope of the prohibited customers/clients is often limited to customers/clients with whom the employee actually had contact, or for whom the employee was responsible in the course of the performance of his/her duties for a limited period during his/her employment (e.g. 12 months before the termination of employment).

iii. Is it necessary to pay an employee during the period of the covenant?

As is the case with post-termination restrictions, compensation is one of the factors that courts will consider to determine the validity of a clause prohibiting contact with customers/clients. In some cases, the courts have enforced post-termination clauses prohibiting contact with customers/clients even where no compensation was paid.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

During the term of employment, in general, even if there is no agreement between the employer and the employee that specifically prohibits the employee from soliciting his/her colleagues, it is considered that the solicitation of colleagues is prohibited. However, the court will determine whether the employee breached the prohibition based on various factors such as:

(i) the employee’s position (i.e., if and how strongly the employee has the power to influence his/her colleague), and

(ii) the manner of solicitation (i.e., if the solicitation is made in accordance to a plan; if the solicitation involves a large number of employees; and whether the manner of solicitation performed infringes against general societal appropriateness).
After termination of employment, in principle, a former employee is not restricted from soliciting his/her former colleagues unless otherwise agreed with his/her former employer. In the case involving an agreement between the former employee and the former employer, the agreement on the restriction is treated in the same basic manner as a restriction against soliciting colleagues during the employment.

iii. Is it necessary to pay an employee during the period of the covenant?

During the term of employment, no additional compensation is required for covenants to be valid. After the employment is terminated, as mentioned above, compensation is one of the factors that the courts will consider in determining the validity of the post-termination restrictive covenant, including a clause prohibiting solicitation of colleagues.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

Yes. During the employment and after the termination of employment, it is fairly common to restrict the employee from disclosing or using confidential information and the company’s property. Companies often do not set a limitation on the period of such restrictions; instead, these restrictions apply as long as the company’s information retains its confidential nature. The former employer and former employee sometimes dispute whether or not certain information qualifies as “confidential information” or “company property” and whether such information or property is subject to the confidentiality obligation. Accordingly, it is important for the employer to clearly specify, to the greatest extent possible, the information and company property that is subject to the confidentiality obligation (e.g. in a written oath submitted by the employee at the termination of employment etc.).

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

An agreement between an employer and an employee to choose a governing law other than Japanese law is, in principle, valid. However, under the Act on General Rules for Application of Laws of Japan, even if the employer and the employee choose a governing law other than Japanese law, if the employee manifests his/her intention to the employer that a specific “mandatory provision” from within the law of the place with which the employment contract is “the most closely connected” should be applied, such a mandatory provision shall apply.

If the employment contract provides that the employee should work in Japan, Japanese law is deemed to be “the most closely connected” to the employment contract.

Also, the principles regarding the validity of post-termination restrictive covenants mentioned above are considered to be “mandatory provisions.” Accordingly, even if it is agreed that laws other than Japanese law govern the post-termination restrictive covenant, if the employee who worked in Japan during his/her employment manifests his/her intention to the employer to apply the principles regarding the validity of post-termination restrictive covenants, these principles shall apply. The employee may manifest that he/she would like the mandatory provisions to apply at any time. Typically, the employee does so when a dispute regarding the non-competition restrictive covenants arises after termination of his/her employment.

i. Can an employer impose a dispute resolution method on the employee?

Generally speaking, no. Under the Arbitration Act of Japan, an arbitration agreement between an employer and an employee regarding a future employment dispute (including future disputes regarding non-competition restriction covenants) is invalid. Rather, either the employer or the employee is entitled to seek release by filing a formal litigation claim, a preliminary injunction and/or a labour tribunal proceeding in Japan.
Japan

Regarding international jurisdiction over a future employment dispute (including disputes involving post-termination restrictive covenants), an employer may agree with an employee that courts in a particular county where the employee provided his/her services at the time of termination of employment shall have such jurisdiction, although the agreement must be made at the time of termination of employment and jurisdiction must be non-exclusive.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

The most direct remedy for breach of a restrictive covenant is an injunction or preliminary injunction in order to restrain the employee’s and/or the new prospective employer’s activities. The employer may also claim compensation for damages caused by the employee’s breach to the post-termination restrictive covenants. Finally, prior to commencement of legal proceedings, a lawyer’s warning letter is frequently sent. In many cases, the warning letter is sufficient to either cease the breaching activity or else to facilitate a negotiated settlement.

In addition, many companies in Japan include a provision in their retirement allowance policies that no retirement allowance or only a reduced retirement allowance will be paid to employees if employees take any action which can be a ground for a disciplinary dismissal, including the breach of a post-termination restrictive covenant. As retirement allowances are generally considered as a type of deferred payment of salary for an employee’s work during his/her employment, courts will examine whether the application of such a provision in the retirement allowance rules is reasonable on a case-by-case basis.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

In addition to covenant enforcement described above, the Labour Standards Act of Japan prohibits the employer from agreeing with the employee in advance on the amount of the compensation for damages owed to the employer in the event of the employee’s breach of the employment contract. A provision in the contract or a company’s rules on the benefits, pensions or stock plans regarding the forfeit of the employee’s rights to receive these forms of compensation in a case where the employee breaches a post-termination restrictive covenant may be interpreted as such an agreement and deemed invalid depending on the contents of the provision.

ii. Which covenants are typically imposed?

ANSWER: It is common to include a provision in the retirement allowance rules that no retirement allowance, or only a reduced retirement allowance, will be paid to the employee if the employee takes any action which can be a ground for a disciplinary dismissal, including the breach of a post-termination restrictive covenant. All types of the post-termination restrictive covenants mentioned above can be the subject to such a provision.

iii. What sanctions are/can be imposed by the employer for non-compliance?

In the event of an employee’s non-compliance, the employer may decide not to pay any benefits or reduce the amount of the benefits that the employee will receive based on a provision in the contract or a company’s rules regarding the forfeit of the employee’s rights to receive the benefits. However, the employee may then make a claim to the court to receive these denied payment benefits, arguing that the provision itself is invalid or that the provision should not apply to the employee.
Japan

iv. Are there any limits to what an employer can forfeit (e.g., retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?

As mentioned above, the Labour Standards Act of Japan prohibits the employer from agreeing with the employee in advance on the amount of compensation damages the employer would receive for the employee’s breach to the employment contract. After the employee’s right to receive the benefits vests, retroactive forfeiture may be interpreted as such an agreement and invalidated.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

In principle, a post-termination restrictive covenant that unreasonably restricts the employee’s freedom to choose his/her occupation is invalid and unenforceable as a whole. However, there are some court cases that determined the validity of broad post-termination restrictive covenants by limiting the scope of such covenants’ application. That said, it is prudent to draft a “cascading” type of restrictive covenant (e.g., a time period of one (1) year, but if that is held to be invalid, a time period of six (6) months, and if that period is held to be invalid, a time period of three (3) months).

Contributed by James M. Minamoto & Emi Uchida
A. OVERVIEW:

The present law in Malaysia is in favor of rigid statutory interpretation and is protective of an individual’s right to earn a livelihood. Unlike the Common Law jurisdiction, Section 28 of the Malaysian Contracts Act 1950 (“CA 1950”), which deals with restraint of trade, is not concerned with reasonableness of the restraint in trade. Once the Malaysian court finds that a covenant is in restraint of trade and none of the exceptions applies, the clause will be void.

This is evident from the case of Wrigglesworth v Wilson Anthony wherein the judge held that under Section 28 of the CA 1950, English law decisions relating to restraint of trade were not relevant as all covenants in restraint of trade were void under the same provision. Hence the test of reasonableness could not be applied in such cases.

Section 28 of the CA 1950 provides that “Every agreement by which anyone is restrained from exercising a lawful profession, trade, or business of any kind, is to that extent void” with three exception situations, as follows, where:

1. There is an agreement not to carry on business of which goodwill is sold; or
2. There is an agreement between partners prior to dissolution;
3. There is an agreement during the continuance of a partnership.

Exception 1 is concerned with an agreement for the sale of goodwill of a business. The seller of the goodwill of a business may agree with the buyer that he would restrain himself from carrying on a similar business, within specified local limits, so long as the buyer or any subsequent buyer thereto, carries on a similar business. Such covenant is valid and enforceable, provided the limits imposed appear to the court reasonable, considering the nature of the business.

A covenant in which a partner agrees not to carry on a business similar to that of the partnership within such local limits as are referred to in Exception 1, upon or in anticipation of a dissolution of the partnership is valid and enforceable under Exception 2. A covenant in which a partner agrees not to carry on a similar business during the continuance of the partnership is similarly valid and enforceable under Exception 3.

The High Court in Worldwide Rota Dies Sdn Bhd v Ronald Ong Cheow Joon took a different view on the law of restraint of trade. In this case, Clause 10 of the employment contract provided that upon the defendant’s resignation, he shall not be engaged in work or own the same trade as the plaintiff company in Malaysia, Singapore, Thailand, Indonesia, Philippines and Taiwan for an immediate period of three years from the date of resignation. It was held that a restraint is permissible if it is fashioned in such a way as to prevent a misuse of trade secrets or business connection. In so ruling, Abdul Malik Ishak J held:

“In considering s 28 of the Contracts Act 1950, there must be some measure of flexibility. The commercial reality of the matter dictates this kind of approach. Regard must always be had to the nature of the business conducted by the employer. The test of reasonableness must be applied in construing a restraint of trade clause.”

We are of the view that the aforesaid decision of Wordwide Rota Dies Sdn Bhd (supra) run foul of the express provision of Section 28 of the CA 1950 and is not reflective of the present law in Malaysia relating to restraint of trade. As restraint of trade in Malaysia is absolute regardless of the geography and duration it seeks to cover, any form of restrictive covenant is therefore void and unenforceable.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

No

i. Are they capable of being valid?

No

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The effect of having a non-competition clause in an employment contract is that the employee will be prohibited from joining any organization that is deemed to be a competitor to its employer. When the employee is prohibited from joining any organization after they cease employment with their former employer, this will amount to restraint of trade which is expressly prohibited under Section 28 of the CA 1950. No matter how narrow or wide the covenant was drafted, the employer would not be able to impose a non-competition covenant against its employee. However, if the employer can prove that the non-competition clause falls within the exception to Section 28 of the CA 1950, it may be valid and enforceable.

iii. Is it necessary to pay an employee during the period of the covenant?

Not applicable.
Malaysia

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

No

i. Are they capable of being valid?

No

ii. What does it take to show they are valid?

Based on our answer in b(ii) above, a post-termination clause that seeks to prohibit contact with customers/clients will be caught by Section 28 of the CA 1950 as it amounts to restraining an employee’s trade.

In the case of Svenson Hair Centre Sdn Bhd v Irene Chin Zee Ling, an injunction was sought by the employer against the ex-employee to restrain the ex-employee from contacting or corresponding with all or any of the employer’s present customers. The injunction was allowed. The Court held that the injunction sought was merely to stop her from calling, approaching or contacting the employer’s customers that appear on the customer’s list, as opposed to stopping the employer from working with the competing business.

We take the view that the restrain sought by the employer in the above case amounts to restraint of trade under Section 28 of the CA 1950. By prohibiting contact with customers/clients, the ex-employee is restrained from freely conducting their own trade in any manner they wish. Although it is arguable that the list of customer is the employer’s confidential information but that does not mean that the customer can only conduct business with the employer. In the circumstances, the injunction should not be allowed as it contravenes the express provision of the law. It is unlikely that the above decision will be followed by other Malaysian courts.

iii. Is it necessary to pay an employee during the period of the covenant?

Not applicable

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

No

i. Are they capable of being valid?

No

ii. What does it take to show they are valid?

In addition to our answer in b(ii) above, it will be very difficult to prove that the employee was solicited or enticed by the ex-employee to leave the employer.

However, it is arguable that the restrictive covenant serves to limit the ability of the ex-employee to hire the employee of the employer. It does not restrain the ex-employee from hiring the current employee of the employer. It is useful to refer to the case of Hua Khiow Steamship Co Ltd v Corp Chop Guan Hin (1930) that drew the distinction between restraining the manner in which a trade is carried out and restraining the trade itself.

iii. Is it necessary to pay an employee during the period of the covenant?

Not applicable
E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

Another type of restrictive covenant is to restrain the employee or ex-employee from using, divulging or disclosing any confidential information or trade secrets of the employer. This type of restrictive covenant was held to be valid on the ground that the employee owes an implied duty to the employee prohibiting the employee from using any confidential information obtained during the course of employment. It must be emphasized that the law imposes a general duty on the employee to act in good faith and hence comes the obligation not to use or disclose trade secrets or to do what they have covenanted not to do.

In order to prove that the information in question constitutes a trade secret of the employer, the following would be considered.

a. the nature of the employment, i.e. whether the employee was regularly exposed to confidential information and only a limited number of employees had access to the information;

b. the nature of the information itself;

c. whether the confidentiality of the information was emphasized by the employer; and

d. whether the relevant information could easily be isolated from other non-confidential information which was part of the same package of information.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

Choice of law refers to the set of law that parties to an agreement choose to govern the agreement. A choice of law clause is vital especially when the agreement involves multiple parties from different jurisdictions. Generally, the Malaysian courts would give effect to an express choice of law clause. In the absence of an express choice, the Court will have to determine if there is an implied choice by reference to which the contract was made, and such implied choice is to be inferred from the terms of contract or surrounding circumstances.

If the Court is unable to imply the choice of law, the Court may adopt the system of law, with which, the transaction has the closest and most real connection. Examples of this are; (a) the place of performance of the contract; (b) the place where the contract was made; (c) the links of the parties of the contract to any particular countries; (d) the site of the immovable property if such property is involved, and (e) the currency in which money under the contract is expressed.

While a choice of law clause governs the law that will apply, a jurisdiction clause refers to a situation whereby parties have agreed to the courts of a named country taking jurisdiction over any disputes that may arise from the contract.

Malaysian courts, like the English courts, can give effect to the agreement of parties to apply foreign law (being the choice of substantive law).

With regards to the effect of the choice of law clause on the restrictive covenants, it would very much depends on the express choice made by the parties. If the parties agree to apply Malaysian law, it faces the risk of being caught within Section 28 of the CA 1950. In the event the parties chose to apply UK law, the court would still have the jurisdiction to hear the matter. However, the application of English law is subject to variation, if it is contrary to public policy in Malaysia.

i. Can an employer impose a dispute resolution method on the employee?

It is unusual for an employment agreement to provide for a dispute resolution method. This is on the basis that the Malaysian Industrial Relations Act 1967 has provided that when an employee filed a written complaint over unfair dismissal, both the employee and the employer are required to attend a reconciliation process. When the matter could not be settled at reconciliation stage, the matter will then be referred to the Industrial Court for adjudication.
Malaysia

Even if the employment agreement provides for a dispute resolution method, the clause does not debar the employee from filing a complaint for unfair dismissal under Section 20 of the Industrial Relations Act.

Therefore, a dispute resolution method does not serve any purpose or benefit to the employer and the same might be held invalid as it purports to curtail the employee’s statutory right under Section 20 of the Industrial Relations Act.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

Since restrictive covenants are prohibited under Section 28 of the CA 1950 and therefore invalid, it is impossible to enforce the same in our jurisdiction.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

Not applicable

ii. Which covenants are typically imposed?

Any restrictive covenants that an employer seeks to impose do not extend to employee benefits, pensions and stock plans as the same are provided by a third party and not within the power of the employer. By reason of the foregoing, there are no restrictive covenants imposed in relation to employee benefits, pensions and stock plans.

iii. What sanctions are/can be imposed by the employer for non-compliance?

Since any restrictive covenants will be caught by Section 28 of the CA 1950, the employer will not be able to enforce sanctions for non-compliance.

iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)

Not applicable for reasons in h(i), (ii) and (iii) above.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

A restrictive covenant which is found to be in breach of restraint of trade will be void and unenforceable. However this does not affect the remaining provisions in the contract as the Court will apply the principle of severability, i.e the void provision will be severed from the contract.

Contributed by Nadarajah Sivabalah and Nadia binti Abu Bakar
A. OVERVIEW:

Restrainment of trade clauses in employment agreements are generally presumed to be unenforceable because they are anti-competitive and contrary to the public interest. They will only be upheld by the Employment Relations Authority (Authority) or Employment Court (Court) if they are deemed necessary and reasonable in order to protect an employer’s genuine proprietary interests. In the event of a challenge, the onus is on the party seeking to enforce the clause to demonstrate that it is reasonable.

In determining the “reasonableness” of restraint of trade clauses, the Authority and Court consider factors such as:

(a) whether the employer had a genuine proprietary interest/s;
(b) the scope and duration of the restraint;
(c) the geographical area of the restraint;
(d) the nature of the business;
New Zealand

(e) the seniority of the employee;

(f) whether any consideration has been paid to compensate for such restrictions; and

(g) the impact on the restraint on the individual (for example the ability to earn a living).

The Authority or Court are unlikely to enforce a clause which simply seek to restrain competition in general and does not protect a legitimate proprietary interest that the employer is able to point to.

The courts are able to apply section 8 of the Illegal Contracts Act 1970 in the context of actions relating to restraint of trade clauses. This section allows the courts to modify a restraint of trade clause (i.e. its duration, geographical coverage and/or scope) to make it reasonable. If the restraint is modified by the court, the employee will be bound to comply with the restraint in its modified form.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The factors mentioned above apply in determining whether a non-compete clause is reasonable, and thus enforceable. As well as duration, geographic coverage and scope, the clause must be necessary to protect a legitimate proprietary interest of the employer in the nature of trade secrets or business connections.

Non-compete clauses are more difficult to enforce than those prohibiting solicitation only (e.g. of customers, suppliers or employees).

The roles for which a non-compete clause may be appropriate include senior sales staff, senior management and any staff that have important relationships with clients or access to trade secrets or other highly confidential information.

In most cases, a restraint against competition will also only be reasonable for a period of one to three months. In exceptional circumstances, a restraint for a longer period of time may be justified, particularly if the employee is key and separate consideration is paid to the employee for entering into the restraint.

For a restraint of trade to be enforceable the employee must have received consideration for their agreement to be bound by the restraints. This is not to say, however, that extra consideration is a pre-requisite for an enforceable restraint. There does not need to be “extra consideration” over and above the consideration for the underlying employment agreement, provided the restraint is entered into at the commencement of employment.

Additional and separate consideration will be critical where the restraint (or a more onerous restraint) is proposed by way of a variation, or attempted variation, to the original employment agreement.

iii. Is it necessary to pay an employee during the period of the covenant?

No. There is no legal obligation to pay employees during the period of a restraint of trade. Doing so will however assist with the enforceability of a restraint.
New Zealand

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid?

The same principles that are outlined above in relation to non-compete clauses apply to contact prohibition clauses. Such restraints will only be enforceable if reasonable.

Non-solicitation clauses are, generally, easier to enforce than non-compete clauses. Therefore, a longer restraint period and/or a wider geographical restriction and scope will more likely be held to be reasonable.

Reasonable prohibitions on non-solicitation will usually be confined to clients, suppliers or customers whom the employee has actually dealt with (usually within the 6 to 12 months prior to termination of the employee’s employment).

iii. Is it necessary to pay an employee during the period of the covenant?

No, for the reasons given in (b)(iii) above.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid?

The principles outlined above also apply to non-solicitation of employees.

iii. Is it necessary to pay an employee during the period of the covenant?

No, for the reasons given in (b)(iii) above.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

As well as non-solicitation of clients, customers and employees, it is common for employment agreements to contain a clause restricting the solicitation of suppliers of the employer. The same principles that apply to non-solicitation of clients and customers apply for suppliers.

It is common for employment agreements to restrict the use or disclosure of confidential information relating to the affairs, clients or trade secrets of the employer. These clauses usually apply during employment and after termination. There will also be common law protections based protecting the misuse of confidential information obtained during employment.
New Zealand

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

Generally, where parties have expressly selected a system of law to govern the agreement, that choice will be given effect provided that it is bona fide and legal, and there is not public policy reason for avoiding the choice.

However, the courts have held that a choice of law clause will not be effective where a foreign system of law is chosen which has little or “no connection” with the employment agreement and thus comprises a contracting out by the parties of the governing application of New Zealand employment law.

i. Can an employer impose a dispute resolution method on the employee?

In New Zealand, the Authority has exclusive jurisdiction to make determinations about employment relations problems generally, including disputes over restraints of trade. However, the Authority must consider whether mediation is required in the first instance. The Court deals with de novo hearings, appeals and matters removed from the Authority.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

Either an employer or an employee may seek to have the Authority determine whether a restraint of trade clause is enforceable.

An employee may apply to the Authority seeking a declaration that a restraint of trade is invalid.

Employers seeking to enforce a restraint of trade clause can apply for an injunction to restrain the employee from commencing employment for another employer. Injunctions can be granted by both the Authority and the Court.

Before the Authority or Court will order an injunction it must:

(a) be satisfied that there is an arguable case in respect of the alleged breach of the restraint clause;
(b) consider the balance of convenience; and
(c) consider the overall justice of the case.

In addition to seeking an injunction to restrain an employee from working for a competitor, an employer can also seek remedies for breach of the restraint clause if it is held to be enforceable.

To be successful in a claim for remedies, the former employer must be able to show that they suffered financial losses as a direct result of the employee’s breach of the restraint of trade clause. If this occurs, the employee may be ordered to pay damages for the losses incurred as a result of the breach of the clause (including an account of profits).

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

Generally, restrictive covenants are not relevant to, or enforceable against, an employee’s pension benefits.

In relation to long term incentive awards, the sanction is usually forfeiture of the award, or, in some cases, claw back of any amounts already paid. The former employer would not need enforcement (as it would be in the employer’s powers not to deliver the cash or shares pursuant to the award) – although it may be challenged by the participant, but such challenges would generally involve a claim for breach of contract. Employers should ensure that any such provisions do not, in practice, operate as a penalty clause, which are typically unenforceable.
New Zealand

Historically it was usually determined at the time of termination whether a participant would retain his award ("good leaver") or lose his award ("bad leaver"), and if the award was retained it would usually vest and be paid out at the time of termination. It is becoming more usual for retained awards to be paid out to good leavers at the original vesting date, rather than on termination, which has led to an increase in forfeiture or claw back provisions relating to specified post-termination activities.

A forfeiture of an award or partial award, for prohibited competitive activities can be challenged if the employee claims that the provisions allowing forfeiture are unenforceable as a restraint of trade. The same approach will be taken to evaluating these clauses as is taken when looking at the equivalent clauses in employment contracts.

ii. Which covenants are typically imposed?

See h. (i) in relation to pension benefits.

Covenants imposed will tend to mirror the covenants contained in employment agreement, although there is no requirement that this is the case. As such these covenants could range from non-competition covenants through non-dealing and non-solicitation of customers clauses.

iii. What sanctions are/can be imposed by the employer for non-compliance?

See h. (i) above in relation to pension benefits.

Injunctive relief is less common, as the plan documentation does not usually impose a specific prohibition on the relevant behaviour – rather forfeiture of all parts of the award if the behaviour occurs. It is more common for a forfeiture provision to apply to unvested incentive awards if the participant engages in the relevant behaviour. In addition, there may be claw back of amounts paid (or repayment of any value realised on sale of shares delivered) on the vesting of awards. Where shares are delivered, it would be possible to prohibit sale of the shares until expiry of any relevant covenant period, possibly coupled with some form of security over the shares. Injunctive relief may be available if the award documentation contained a prohibition on the relevant behaviour.

iv. Are there any limits to what an employer can forfeit (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?

See h. (i) above in relation to pension benefits.

There are generally no specific limits in relation to long term incentive arrangements. However, there may be limits to what the employee is prepared to agree to.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

Restraints of trade that are invalid are unenforceable. Under section 8 of the Illegal Contracts Act 1970, the Court or the Authority has the ability to modify a restraint of trade clause to make it reasonable. This is typically done by reducing the duration, geographic coverage or scope of the restraint. If the restraint is modified, the employee will be bound to comply with the restraint in its modified form.

Contributed by Phillipa Muir and Carl Blake
A. OVERVIEW:

The employer and employee may agree on confidentiality of commercial secrets and intellectual property. Employees with a confidentiality obligation can also be bound by a non-compete obligation after cessation of employment. For such provision to be enforceable, the employer must pay consideration on a monthly basis during the post-employment non-compete period. Violation of a non-compete provision will subject the employee to a preset penalty for breach of contract. The employer and the employee may agree upon the scope, area and period for non-competition. The maximum period may not be more than two years after the end of employment.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes.
PRC

i. Are they capable of being valid?
Yes.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?
The following elements should be considered:

1. Length of the restricted period: the non-compete period is capped at two years after the termination/expiry date of the employment.

2. Applicable positions: employees who could be subject to non-compete obligations are limited to senior managers, senior technical employees, and other employees restricted by confidentiality obligations.

3. Scope: the employer can restrict the employee, after the termination or expiry of employment between the parties, from:
   a) being employed by any of its competitors who manufacture, operate or engage in products or business falling within the same category as those of the employer;
   and/or
   b) engaging in, on their own behalf, the manufacture or operation of products or business falling within the same category as those of the employer.

4. Compensation: an employer shall pay economic compensation [see paragraph 5 below] to an employee for his continuous observance of a non-compete obligation on a monthly basis after the termination / expiry of his employment. Otherwise, the employee will no longer be bound by the agreed responsibilities.

5. Standard of compensation: no currently effective national law or regulations have imposed any minimum or maximum standard. However, according to the Judicial Interpretation IV of the Supreme People’s Court on Several Issues Concerning the Application of Law in Hearing Labor Dispute Cases (“JI IV”), which came into force on February 1, 2013, 30% of the monthly average of the employee’s salary over the last 12 months prior to departure may be considered by the courts as the minimum reasonable compensation for non-compete obligations.

6. Termination: according to the JI IV, during the non-compete period, an employer is entitled to terminate the non-competition agreement with the employee at any time. However, in such case, the employee will be entitled to an additional 3- months’ non-compete compensation.

There is an unanswered question as to whether such additional compensation may also be payable where the employer releases the employee before the start of the Restricted Period. The courts may, in practice interpret this additional compensation to be payable to help tide over the employee while finding a new (competing) job and require a period of prior notice (corresponding to the 3 months’ compensation) to be served to release in advance or payment in lieu of notice to be paid.

7. Continuous Performance: according to the JI IV, where an employee is in breach of the non-compete restrictive covenant then, in addition to liquidated damages, the employer is entitled to request the employee to continue his performance of the non-compete obligations in accordance with the contract.

iii. Is it necessary to pay an employee during the period of the covenant?
Yes, please refer to Para. 4 and Para. 5 to ii above.
C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

PRC employment law is silent on this aspect. Such a covenant is negotiable and can be contractual.

iii. Is it necessary to pay an employee during the period of the covenant?

No, there is no legal requirement.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

PRC employment law is silent on this aspect. Such a covenant is negotiable and can be contractual.

iii. Is it necessary to pay an employee during the period of the covenant?

No, there is no legal requirement.

E. OTHER COVENANTS: Are there any other types of employment - and post-employment-related covenants which are common in this jurisdiction?

Confidentiality covenant.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

In the context of employment within China, PRC law will be the governing law. No choice of law is permissible.

i. Can an employer impose a dispute resolution method on the employee?

It is a mandatory legal requirement that labour disputes must be submitted to the competent labour dispute arbitration committee first, before going to the court. In terms of disputes relating to non-compete covenants, these can be either resolved as a labour dispute (in which case the labour dispute arbitration procedure will be gone through first) on the basis of PRC employment laws, or resolved as a civil tort case on the basis of PRC Anti-unfair Competition Law (in which case it can go directly to the court).
G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

Where an employee violates the non-compete obligations, the employer is entitled to:

(i) claim for the agreed liquidated damages, and
(ii) demand that the employee continue to observe their non-compete obligations. However, due to the lack of effective judicial measures, in reality it would be difficult to prevent the employee from working with the competitors.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

No.

ii. Which covenants are typically imposed?

PRC law is silent in this regard.

iii. What sanctions are/can be imposed by the employer for non-compliance?

PRC law is silent in this regard.

iv. Are there any limits to what an employer can forfeit (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?

PRC law is silent in this regard.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

It will be ruled as void and the Court will not re-write the covenant.

Contributed by Andy S.K. Yeo and Helen Liao
A. OVERVIEW:

Post-termination restrictive covenants are often assessed against the precepts of public policy, management prerogative, legitimate business interests and reasonableness.

These restrictive covenants are typically embodied in employment contracts that are governed by the Labour Code of the Philippines and the Civil Code of the Philippines. There is no specific Labour Code provision that prohibits post-termination restrictive covenants, but it must be emphasized that the law favors the employees, and all doubts must be resolved in favor of the employee. Nevertheless, this does not necessarily mean that post-termination restrictive covenants are invalid, per se. An employment contract, just like any other contract under the Civil Code, may contain provisions as the employer and employee may deem convenient, provided that they are not contrary to law, morals, good customs, public order or public policy. In the same vein, the courts cannot stipulate for the parties nor amend their contract if their contract does not contravene the law, morals, good customs, public order or public policy.
Philippines

Management prerogative means that the law recognizes the rights of management, which are protected and recognized in the interest of fair play. Post-restrictive covenants, which are often imposed to protect the rights of management, are upheld so long as these are exercised in good faith for the advancement of the employer’s interest and not for the purpose of defeating or circumventing the rights of the employees under the Labour Code, Philippine law or regulations.

Legitimate business interests are also considered, such as safeguarding business confidentiality and protecting one’s competitive position.

Lastly, the restrictive covenants must be reasonable as to time, trade (or scope) and place.

If an employee violates a post-employment restrictive covenant, the employer may seek injunction from the courts and/or file an action for damages against the employee.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The general principles discussed above apply. In a 2007 Supreme Court decision, the Supreme Court upheld a non-compete clause because it was specifically limited as to time (i.e. two years) and limited as to trade (i.e., only businesses akin to the employer’s business). Earlier jurisprudence also requires that the clause should be limited as to place.

iii. Is it necessary to pay an employee during the period of the covenant?

It depends. If the covenant is incorporated in the employment contract, the employee is deemed already compensated as the non-compete clause is one of the terms and conditions of employment. On the other hand, if the non-compete clause is required at the time of the separation of the employee, it must have additional consideration to be valid following the law on contracts.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

There is no Supreme Court decision with a categorical ruling on the requirements for validity of contact prohibition clauses. However, given that these are generally incorporated in employment contracts that are governed by the Labour Code of the Philippines and the Civil Code of the Philippines, it is arguable that like other post-termination restrictive covenants upheld by the Supreme Court, these contact prohibition clauses must yield to the general principles discussed above.

iii. Is it necessary to pay an employee during the period of the covenant?

Please see answer to c (ii) above.
D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes.

i. Are they capable of being valid?
Yes.

ii. What does it take to show they are valid?
There is no Supreme Court decision with a definitive ruling on the validity of non-solicitation clauses.

However, inducing an employee of a competitor to move to one’s business may constitute a tortious interference under the Civil Code of the Philippines. For a third person to be liable for tortious interference under the Civil Code of the Philippines, it must be proven that: (1) there is a valid contract; (2) there is knowledge on the part of the third person of the existence of a valid contract; and (3) interference of the third person is without legal justification or excuse.

iii. Is it necessary to pay an employee during the period of the covenant?
The covenant is typically incorporated in the employment contract, for which the employee receives compensation.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

Generally, employment contracts in the Philippines contain conflict of interest clauses where employees are required to avoid any activity, relationship or interest that may run counter to the responsibilities which they owe to their employer. The Supreme Court upheld a provision where an employee of a certain drug company was prohibited from marrying an employee from a competing drug company.

Also, non-disclosure/confidentiality provisions are valid in the Philippines. Where businesses have trade secrets or business secrets to protect, employees and employers may validly stipulate that the employee is not allowed to disclose or use any such information obtained during the period of his employment. However, Courts are reluctant to implement non-disclosure/confidentiality clauses against employees who by virtue of their rank or position, eg., rank and file employees, do not have access to confidential or secret information.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

The employer and employee are free to stipulate their choice of law, but in no case can they deprive the Labour Courts of their original and exclusive jurisdiction over the enforcement of restrictive covenants insofar as these involve claims for damages arising from the employer-employee relationship.

i. Can an employer impose a dispute resolution method on the employee?
Yes. Sec. 3, Art. III of the Philippine Constitution upholds the “preferential use of voluntary modes of settling disputes, including conciliation, and shall enforce their mutual compliance therewith to foster industrial peace.” In this regard, the National Labour Relations Commission has recently issued a department order requiring the submission of labour complaints cognizable by the Commission to mediation or conciliation before the same is submitted to the Labour Arbiter for resolution.
Philippines

G. ENFORCEMENT: How are covenants typically enforced in your jurisdiction?

The employer may seek an injunction and/or file an action for damages against the (former) employee. Alternatively, if there is still an existing employer-employee relationship, the employer may have grounds to dismiss the employee.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

Yes. Please note that for termination for violation of a restrictive covenant (i.e., a termination for just cause), the employee is deprived of separation benefits, without prejudice to the benefits or privileges they may have that are voluntarily agreed upon by both employer and employee.

ii. Which covenants are typically imposed?

The employer and employee are free to stipulate which covenants are imposed.

iii. What sanctions are/can be imposed by the employer for non-compliance?

This is subject to stipulation of the employer and employee, as long as these do not contravene law, morals, good customs, public order or public policy.

iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)

Please see answer above.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

It is considered as not written and it has no force or effect.

Contributed by Enriquito J. Mendoza, Rena M. Rico Pamfilo and Amanda F. Nograles
Singapore

A. OVERVIEW:

Commonly used in contracts of employment to prevent employees from taking advantage of resources or goodwill obtained during their employment to unfairly put themselves in competition with their former employers after resignation, post-termination restrictive covenants have featured quite prominently in recent jurisprudence in Singapore.

The general position is that post-termination restrictive covenants are prima facie against public policy and thus unenforceable, unless an employer can prove that

(1) there was a legitimate proprietary interest to be protected,

(2) the restrictions satisfy the twin-tests of reasonableness and

(3) the restrictions go no further than is necessary to protect the legitimate proprietary interest(s) concerned.
Singapore

Traditionally, domestic Courts have recognized three groups of legitimate proprietary interests capable of being protected by restrictive covenants: trade secrets and confidential information; trade connections, and to maintain a stable and trained workforce. Although the Courts have stopped short of any express statement that these categories are not capable of expansion under appropriate circumstances, there has yet to be any instance of such arguments being canvassed by employers.

The crucial time for ascertaining whether or not the restrictive covenant in question is in fact reasonable is at the time at which the contract is made.

As to whether the scope of such restrictive covenant is reasonable, Courts have in particular, usually assessed them in terms of the geographical limit and period of restriction. Relevant considerations in such an assessment include the roles, duties and seniority of that particular employee and whether there are any additional factors in respect of that particular industry. However, note that no one factor is decisive. The Courts have consistently stated that no two cases are the same and what is reasonable will depend on the particular factual matrix of the case, thus the Court will conduct a holistic assessment before determining if a restrictive covenant is reasonable.

In a majority of cases, the remedy asked for by employers for a breach of a restrictive covenant is an injunction, to restrain either the employee or the new or prospective employer’s activities. However, depending on the category of legitimate proprietary interest that the employer has sought to protect, financial compensation may also be appropriate in certain circumstances.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes. Assuming that this has been crafted in as part of the employment agreement at the time the employee joins, then the key consideration is whether such a clause is reasonable or otherwise as explained in the response in (a) above. Where this has been requested at the time of the termination of the employment agreement, then in addition to reasonableness, there must be valid consideration provided.

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The general principles mentioned above apply. However, the Courts generally adopt a stricter approach towards restrictive covenants in an employment context compared to the context of the sale of a business. It is clear that a bare and blatant restriction of the freedom to trade will not be enforced and the likelihood of any post-termination restrictive covenants being upheld following the Courts’ scrutiny will depend on whether the scope and duration of the restriction is reasonable, followed by a consideration of whether a less onerous restriction, such as a non-solicitation clause, would have been sufficient.

With regard to the period of restriction, the relevant industry concerned and the employee’s seniority and role in his/her former employer’s business will make for key considerations. For example Courts have found a 1-year restriction to be too long in the context of a Managing Director in charge of business strategy and operations, while the same was held valid in relation to a Managing Director for a brokerage firm. While there is no existing jurisprudence to indicate either way, it may be that restrictive periods of 1 – 3 years may be held reasonable as a preliminary benchmark, while the Courts have held that a restrictive period of 3 years to be unreasonable. However, note that should the employee have been put on garden leave by the employer previously, such period may be taken into account by the Court in assessing whether the period of restriction is reasonable.

More recently, the Courts have held that, where an employment contract already contains a confidentiality clause, an employer seeking to uphold any restrictive covenants must show another legitimate proprietary interest apart from that being of the protection of trade secrets. In such a case, the alternative legitimate proprietary interest of protecting trade connections, if proven, will generally suffice.
iii. Is it necessary to pay an employee during the period of the covenant?

There is currently no legal requirement for employees to be paid during the period of any post-termination restrictive covenants. However, whether an employee is paid during such period will also be relevant in the assessment of whether any restriction is reasonable.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes. Such non-contact clauses are usually in the form of non-solicitation clauses which may prohibit the solicitation by the employee of either their former employer’s customers, including existing customers and those from which the employer is trying to solicit business.

   i. Are they capable of being valid?

Yes

   ii. What does it take to show they are valid?

The general principles mentioned above apply. In general, such non-solicitation will extend to persons who are existing customers, persons who are not customers yet but with whom negotiations are going on with a view of making them customers and customers who are no longer patronising the employer at the time that the employee leaves, but remain in the habit of dealing with the employer.

However, for such non-solicitation clauses to be held valid, such aforementioned persons must be either persons with whom the employee had contact or about whom they became aware or informed about in the course of their employment or persons with whom the employee worked or supervised the work of during a defined period of time prior to the employee leaving their employment; usually 1 year.

   iii. Is it necessary to pay an employee during the period of the covenant?

No, for the reasons noted in the response to (b)(iii) above.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment); and

Yes.

   i. Are they capable of being valid?

Yes.

   ii. What does it take to show they are valid?

The general principles mentioned above apply. In respect of clauses regarding the non-solicitation of former colleagues, the Courts have stated the preference not to lay down any blanket rule. However they have also stated that it would generally be more difficult to justify a non-solicitation clause which covers the solicitation of just “any” employee.
Singapore

A clause prohibiting the solicitation of any employee, without reference to their importance to the business and whether or not they have any knowledge or experience in relation to the employer’s field of activity would generally be regarded as unreasonable and thus unenforceable. Therefore, such clauses are usually restricted to colleagues over whom the employee had influence and may well be inappropriate in relation to members of staff whom the employer can easily replace. However in the final analysis, much is dependent upon the particular factual matrix.

While in practice it may be that it is usually difficult for employers to prove that a non-solicitation of employee’s clause has been broken, in certain circumstances, the employer may well consider taking action against its former employee for breaching a non-solicitation clause by way of an action in tort for inducing breach of contract.

iii. Is it necessary to pay an employee during the period of the covenant?

No, for the reasons noted in the response to (b)(iii) above.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

Confidentiality clauses that restrict the use or disclosure of confidential information during and after employment are commonly used in addition to post-termination restrictive covenants. Such confidentiality clauses are intended to apply during and after termination, and generally have no time limit to their applicability insofar that the information is not in the public domain. However, note that where there is a confidentiality clause, the matters stated in the response to question (b)(ii) above must be considered.

In addition to confidentiality clauses, intellectual property clauses are also used to restrict the employee from using intellectual property discovered by them during the course of their employment or those belonging to the former employer. Similarly, such clauses generally have no time limit to their applicability.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

If Singapore law applies to the contract, the principles mentioned in the response above will apply to the interpretation and enforcement of restrictive covenants. Being a common law jurisdiction as well as a commonwealth nation, the Courts may in certain circumstances also consider relevant cases from other jurisdictions such as Australia, New Zealand, Hong Kong and the United Kingdom in coming to their decision.

i. Can an employer impose a dispute resolution method on the employee?

It is generally unusual to see alternative dispute resolution procedures imposed in employment contracts. While there may be internal dispute resolution procedures in-place in an employment contract, these are usually intended to be grievance procedures that kick-in if an employee is dissatisfied with the employer’s disciplinary process for one reason or an other.

As injunctions are the most commonly preferred remedy for enforcing restrictive covenants, most enforcement is sought through the Courts.
G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

Typically, where an employer is successful, the Court will order an injunction in the employer’s favour, restraining the employer’s or the new or prospective employer’s activities, in so far as such activities breach the terms of the restrictive covenants sought to be protected by the former employer. However, injunctions remain equitable remedies in the Court’s discretion and there is no guarantee that the Court will or will not grant an injunction in any given case. In limited circumstances, such injunctions may also be in the interim, and last until the case is decided whereby the Court may order a final injunction or otherwise.

Other forms of injunction such as those to enforce a garden leave provision preventing a third party from unlawfully inducing a breach of contract or to restrain their unlawful activity may also be sought for. However, the form of the injunction generally depends on the scope of the restrictive covenants sought to be protected and how it has been breached.

Apart from injunctions, remedies including damages and other forms of financial compensation for breach of contract are most frequently imposed by the Courts.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

There are currently few or no local cases where restrictive covenants are tied against an employee’s pension benefits.

In relation to financial incentives, the Court has made a distinction between those that have ‘vested’ in the employee and loyalty payments. In relation to the former, conditions attached to the payment of such amounts (forfeiture provisions), if they have been vested, due and payable to the employee as at the termination of his employment, if they prohibit the employee from joining a competitor under the threat of forfeiture, will be assessed by the Court under the doctrine of restraint of trade. However, loyalty payments, where additional moneys are paid to employees if they do not join competitors for a certain period may be permissible compared to the forfeiture provisions mentioned previously. The Court will consider the true nature of any provisions in an employment contract, to ensure that they do not escape its scrutiny if it is in fact a restriction regardless of how a clause is phrased.

Sometimes, where an employee’s training/education has been paid for by the employer, the employer will seek to claw-back such payments should the employee leave the employment of that employer or join a competitor. Note that in such cases, the sum sought to be clawed-back must represent a genuine pre-estimate of loss suffered by the employer. Otherwise, the clause(s) may be found to constitute penalty clauses, which are typically unenforceable.

ii. Which covenants are typically imposed?

In the majority of cases, the covenants imposed relate to non-compete by the employer upon termination or will tend to mirror the covenants contained in the standard form employment contracts, although there is no requirement that this be the case. As such these covenants could range from non-competition covenants through to non-dealing and non-solicitation of customers clauses.

iii. What sanctions are/can be imposed by the employer for non-compliance?

Due to the nature of such clauses, where there is usually no imposition of prohibition on any specific behaviour, but rather the forfeiture of such incentives, or parts, on the occurrence of a behaviour, injunctive relief is less common than financial disincentives. However, as stated in the response to question (h)(i) above, the extent or validity of any forfeiture will depend on whether such incentives have already been vested and accrued to the employee in question prior to their termination or after.

In relation to claw-back of other payments/benefits, the general principles as stated in the response to question (h)(i) above apply.
iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)

As stated above, for any forfeiture provision to be held valid, the Court will assess it based on the principles applicable to restraint of trade in general.

In relation to claw-back of other payments/benefits, the general principles as stated in the response to question (h)(i) above apply.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

As stated, restrictive covenants that do not meet the requirements under the general principles are invalid and thus unenforceable. In practice, most restrictive covenant clauses are accompanied with a modification clause which allows that in the event that any part thereof is deleted or reduced in duration, such restriction shall continue to apply to the extent allowed by such deletion or reduction.

Such clauses are intended to provide for the event that the Court applies the ‘blue pencil’ test and severs a particular element (which is considered invalid) of a restrictive covenant and upholds the remainder of the covenant which is considered valid. To the extent that such practices unconsciously encourage the use of ‘cascading’ clauses, there is no definitive judicial pronouncement on whether such clauses are acceptable.

Contributed by Kala Anandarajah
South Korea

A. OVERVIEW:

Post-termination restrictive covenants are essentially contractual provisions made between the employer and the employee and so are, in principle, enforceable. However, because they are imposed on the employee for the benefit of the employer, there have been cases where the Korean courts have invalidated or limited the effects of such covenants because they affect the employee’s freedom to choose an occupation specified in the constitution and guarantee of livelihood. In such cases, the most important factor that the courts would consider is whether or not the purpose of the post-termination restrictive covenants is to protect the justifiable interests of the employer.

If post-termination restrictive covenants are found to be enforceable, the employer can file a civil claim for a preliminary injunction and damages against the employee who violated the covenants. In special cases, (e.g. the employee infringing upon the employer’s trade secrets) criminal proceedings may be commenced. However, because it is difficult to prove the amount of damages, it is helpful to include a liquidated damages clause. Nonetheless, we must bear in mind that the court may reduce the amount of the liquidated damages.
South Korea

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes. A number of Korean companies include a non-compete clause in employment contracts or enter into separate, non-compete agreements. Judicial precedents regarding non-compete clauses define such clauses as ‘an agreement that the employee will not engage in competitive behaviour such as being hired by the employer’s competitors or establishing and managing a competing company.’

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

There is no law that clearly limits non-compete clauses. Therefore, a non-compete clause, which is an agreement between the employer and the employee, is in principle enforceable under the freedom of contract principle. However, according to precedents, if a non-compete clause is deemed to excessively limit the employee’s freedom to choose an occupation, which freedom is guaranteed by the constitution, the non-compete clause can become invalidated under the Article 103 of the Korean Civil Code as it would violate the principle of good morals and social order. In deciding whether to invalidate a non-compete clause, the court would take into consideration the following factors:

(i) the interest sought to be protected under the non-compete clause;
(ii) the position of the employee prior to their termination;
(iii) the scope of the restriction including the length of the restriction period, geographical restriction, etc.;
(iv) the compensation to the employee in consideration of unavoidable encroachment on the employee’s right to work;
(v) the reason(s) for termination of employment; and
(vi) the public interests

‘The interest sought to be protected’ includes not only the employer’s trade secrets, but also exclusive knowledge and information of the employer that the employee agrees to keep as secret. It also includes the employer’s relationship with its customers and maintenance of the employer’s credibility. ‘The interest sought to be protected’ is the most important factor in assessing the validity of a non-compete clause. Generally the protection of technology information of the employer is deemed to be more important than the protection of management information of the employer (such as business plan, sale strategy, price, profit margin, etc.) in assessing the validity of a non-compete clause.

As for ‘the prior position of the employee’, a non-compete clause is more likely to be deemed valid if, for example, the employee was a high-ranking executive officer responsible for handing confidential business information or the employee handled such confidential business information for a long period of time.

As for ‘the scope of the restriction’, a non-compete clause is likely to be deemed to be valid if the scope of the non-compete clause (as it relates to length of period of restriction, restricted geographical area and restricted line of business) is excessively wide (considering the employee’s position at the employer), because the employee’s freedom to choose an occupation becomes more limited as this scope becomes wider.

‘The compensation in consideration of non-compete clause’ has recently being considered as an important factor in determining the validity of a non-compete clause. There are precedent cases, however, where a non-compete clause was deemed to be valid in light of other factors despite an absence of compensation. Therefore, compensation is not absolutely necessary. However, in the case of an employee who does not handle technology information, such as a sales employee, it is safer to provide compensation in order to have the non-compete clause be deemed valid. Compensation need not be monetary benefit. Benefits provided in non-monetary forms such as promotion, or opportunities to study abroad, etc., can constitute consideration in connection with a non-compete clause.
South Korea

According to the precedents, if ‘the reason for termination’ was not a voluntary separation by the employee but a unilateral termination by the employer, a non-compete clause is unlikely to be deemed valid. However, in case of a voluntary resignation, precedents exist where a non-compete clause was deemed valid.

Lastly, in light of ‘the public interests’ factor, if a non-compete clause would harm fair competition in the market, a non-compete clause used by an employer that is a monopoly, for example, is likely to be invalidated. Conversely, if a violation of a non-compete clause can lead to infringement of confidential business information, such a clause is likely to be deemed valid.

iii. Is it necessary to pay an employee during the period of the covenant?

As explained above, compensation is not necessary. Also, there are many types of non-monetary compensation. Some precedents have held the following as being compensation: (i) a payment of USD 100~200 as monthly stipend for security purposes, (ii) a severance package, and (iii) an offer of an opportunity to study abroad.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes. In businesses such as insurance where customer sales profoundly affect the business, post-termination clauses often prohibit solicitation of current or potential customers for a certain period of time after separation.

i. Are they capable of being valid?

ANSWER: Yes.

ii. What does it take to show they are valid?

ANSWER: A non-solicitation agreement, like a non-compete clause, limits an individual’s business activity, and therefore the discussions on non-compete clauses above will be similarly applied to non-solicitation agreements. However, a non-solicitation clause does not limit the employee’s freedom to choose an occupation as much as a non-compete clause. Therefore, the court is more likely to consider it to be valid.

A lower court, for example, invalidated a non-compete clause but held a non-solicitation clause as valid where a branch manager entered into a contract with one insurance company, which included a non-compete clause and a non-solicitation clause, and then transferred to another insurance company.

iii. Is it necessary to pay an employee during the period of the covenant?

ANSWER: No. Although no clear precedent exists, it is reasonable to assume that compensation for a non-solicitation clause is not necessary as it is not necessary for a non-compete clause. In the lower court case mentioned above, the lower court held the non-solicitation clause as valid without taking into consideration whether there was any compensation for the non-solicitation clause.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes. In an industry such as the Information Technology industry where technology and manpower are considered important, it is common to prohibit solicitation of the employer’s employees or business partners for a certain period of time after separation. In many cases, the relevant agreement contains both a clause prohibiting any contact with the employer’s employees and customers and a clause prohibiting solicitation of the employer’s employees or business partners for a specific period of time.
South Korea

i. Are they capable of being valid?
Yes.

ii. What does it take to show they are valid?
The answer to section c (ii) above applies here. A lower court held that both the non-compete and the non-solicitation of employees clauses as valid in a case where a director of a systems integration company transferred to a competitor after having signed an agreement containing both a non-compete clause and a non-solicitation of employees clause. However the restriction period for the non-compete clause was 1 year and the restriction period for the non-solicitation of employees clause was 2 years. The court reduced the restriction period of the non-solicitation of employees clause to 1 year to match the restriction period for the non-compete clause on the principle of equity between the non-compete clause and the non-solicitation of employees clause. The court’s decision does not mean that the enforceability of the non-solicitation of employees clause and enforceability of the non-compete clause is judged as being the same.

iii. Is it necessary to pay an employee during the period of the covenant?
Although no clear precedent exists, compensation for the non-solicitation of employee clause is not mandatory and nor is it mandatory for the non-compete clause.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?
The most common covenant among post-employment covenants is the confidentiality agreement. In most cases, a confidentiality agreement consists of (i) an agreement that the company has work-for-hire related rights, (ii) prohibition of the possession, use, and disclosure of the company’s confidential information after resignation, and (iii) a consent to monitoring to ensure compliance with the confidentiality agreement.

One point to be careful about is that the protection period for trade secrets may be more restricted by Korean courts depending on the length of time necessary for a competitor to develop and/or acquire such trade secrets even if the protection period is not defined under the contract. The range of the trade secret protection period held as valid is wide. It ranges from 4 months to 3 or 5 years. In addition, lower courts have held as valid trade secret protection periods of up to 10 years.

Also, in regard to post-employment covenants, if the employee finds a new employment or an offer of an employment, he or she may become obliged to provide in advance information about the identity of the new employer or the offeror and/or working conditions to the current employer. He or she may also be obliged to notify the new employer or the offeror in advance of his or her obligations under the post-employment restrictive covenants.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?
The choice of law question can be divided into two issues: (i) jurisdiction and (ii) applicable law.

With regard to jurisdiction, Korea’s Private International Act states that if “the party or the source of dispute has actual relation to Korea,” the Korean courts will have jurisdiction. Also, most precedents invalidate clauses specifying foreign courts as having exclusive jurisdiction if the relevant party’s address or location of evidence is in Korea. Therefore, it is difficult for foreign companies to block litigation in Korea regardless of the relevant jurisdiction clause, if such foreign companies hire Korean employees and such Korean employees work in Korea.
A global guide to ‘restrictive covenants’

South Korea

With regard to applicable law, Korea’s Private International Act views parties’ agreement as the most important factor in determining choice of law. However, with regard to employment contracts, the Private International Act states that ‘it is impossible to deprive a worker of protection imposed by compulsory provisions of a country where such worker provides his or her labor’. Therefore, if a court holds post-employment restrictive covenants as part of a valid employment agreement, it is difficult to rule out the possibility in which the court holds in light of the factors in section b (ii) above that post-employment restrictive covenants (including non-complete clauses) are invalid as they violate a compulsory provision of the Article 103 of the Korean Civil Code even if the parties contractually agree to a foreign law as the applicable law. However, a lower court precedent exists where it was held that a violation of the non-compete clause is not a violation of the employment contract as it is a covenant that becomes effective only after the employment is terminated.

i. Can an employer impose a dispute resolution method on the employee?

Depending on the parties’ agreement, disputes regarding post-employment covenants can be decided via ADR procedures such as mediation, arbitration, etc. However, from the point of view of the former employer who requires a prompt remedy against infringement of its rights, it may be ineffective to go through mediation or arbitration procedure that requires additional steps (e.g., judgment for enforcement). In particular, as Korean courts hold the restrict period in non-compete clauses as valid up to 1 year in most cases, it is not desirable in enforcement of such clauses to go through redundant procedures.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

Generally, with regard to a former employee who violates post-employment covenants, it is most common for the employer to seek a preliminary injunction. Theoretically, damage claims are possible. However, if no liquidated damages clause exists, it is very difficult to prove the amount of damages.

In addition, although it is possible to seek preliminary injunction and a damages claim against the new employer, it is insufficient that the new employer was simply aware of the employee’s post-employment restrictive covenants regarding the former-employer. It must be proven that the new employer proactively induced the employee’s breach of the post-employment restrictive covenants.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

Under Korean law, a provisional attachment for damages claim will not be granted against half of the amount of the retirement pension or more.

With regard to employment benefits such as ex-gratia settlement payments, it is usually provided in the resignation agreement together with the post-termination agreement that the settlement payment shall be returned if the employee breaches any obligations in the resignation letter including the post-termination covenants, which is a kind of liquidated damage. In this case, provisional attachment against settlement payments already paid will be effective.

With regard to stock options, the stock option agreement may provide that the exercised stock option shall be subject to forfeiture when the employee breaches any material obligations to the employer including the post-termination covenants.

ii. Which covenants are typically imposed?

Non-competition covenant is mostly imposed.

iii. What sanctions are/can be imposed by the employer for non-compliance?

See sections g and h. (i) above.
iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)

See section h. (i) above.

Further, with regard to the return of the settlement payment, the court may at its discretion reduce the liquidated damages if it finds the amount to be excessive.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

Even if the validity of the post-employment restrictive covenants is established, the Korean courts may reduce the scope of the restriction if it finds the scope of time/location to be excessive. For example, in case of the non-compete clause, even if a restrictive period longer than 1 year has been prescribed the court could reduce such a period to between 6-12 months.

Contributed by Seoung Soo Lee, Sung Il Yoon and Jin Ho Joo
Sri Lanka

A. OVERVIEW:

The laws of Sri Lanka, like those of South Africa, have been influenced by two of the world’s important legal systems - the civil law and the common law systems. The English common law, which originated in England and spread to English colonies, has exercised a much greater influence in Sri Lanka than the Roman-Dutch law. Roman-Dutch law is the residuary law of Sri Lanka, and is applied in all situations where there is no relevant statute law or, in the case of those subject to the special personal laws, (e.g the Thesawalamai, Kandyan law), where those laws are inapplicable or silent. English law was also imposed into the domestic legal system through the Civil Law Ordinance which enacted that English law would apply in various areas including banking, partnership, maritime matters etc. Statute law is the primary source of law in Sri Lanka. The content of statute law may be based on English law or may be enacted in view of local needs and circumstances, or may be a restatement of customary or religious law or principles of common law. Some statutes incorporate by reference the English law on a particular subject. Where there is no applicable statutory provision, the Courts will first ascertain whether the parties are governed by one of the special personal systems of law, and if not, the Courts would then apply the Roman-Dutch law.
Sri Lanka

It is common practice that employers will, where there is a risk of confidential information being divulged by an employee, impose obligations of confidentiality and/or impose restraints on employees being employed by a competitor/soliciting customers. There is not much reported case law in Sri Lanka dealing with restrictive covenants, and the legal position with regard to the validity of restraint of trade clauses is neither very clear nor well settled. There is considerable uncertainty in this area of law though it is likely that a Court would be guided by English law principles.

In Sri Lanka, the law of contract is a mixture of English common law principles and of Roman Dutch law principles and concepts. In general terms, English common law appears to recognize the category of agreements in restraint of trade as illegal and void unless reasonable, whereas under the Roman-Dutch Law there does not appear to be any express principle expounded by the authors per se that invalidates such agreements. As a result, agreements in restraint of trade should, arguably, be treated as valid since the residuary law of Sri Lanka is the Roman Dutch law. However, the influence of English common law decisions and principles in this area is strong, and there has been a tendency by the Sri Lankan judiciary to follow the persuasive authority of decisions of the Courts in England in regard to restraint of trade. Courts in Sri Lanka have held that all contracts in restraint of trade are prima facie void and each case must be examined having regard to its special circumstances to ascertain whether or not the restraint is justified. The only ground of justification is that the restraint is reasonable having regard to interests of both contracting parties as well as to the interests of the public. These decisions followed the British case law precedents brought to the attention of the Court in which it had been held that whether partial or general, covenants in restraint of trade, are prima facie void and unenforceable unless the test of reasonableness can be proved.

The Sri Lankan Constitution accords certain fundamental rights to citizens which include the freedom to engage by himself/herself or in any association with others in any lawful occupation, profession, trade, business or enterprise subject to such restrictions as may be prescribed by law in the interests of national economy or in relation to the professional, technical, academic, financial and other qualifications necessary for practising any profession or carrying on any occupation, trade, business or enterprise, and the licensing and disciplinary control of the person entitled to such fundamental right, and the carrying on by the State, a State agency or a public corporation of any trade, business, industry, service or enterprise whether to the exclusion, complete or partial, of citizens or otherwise. [Article 14 of the Constitution].

The Constitution provides that the fundamental rights enshrined therein are justiciable in respect of State or administrative action which infringes such rights. However it is possible that an argument based on the fundamental right could be raised. We are not aware of any reported judgment in which the impact (whether direct or indirect, if any) of the provision in the Sri Lankan Constitution has been considered.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?

Yes

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

Generally, an employer cannot prevent an ex-employee from competing as this is considered by some Court decisions as being contrary to the important public policy underpinnings – freedom of contract and competition. Sri Lankan Courts, over the years, have heavily restricted the application of restrictive covenants emphasizing that such agreements must be reasonable and should not unreasonably restrict an employee’s right to continue in employment and ability to make a living.
Sri Lanka

However such a restriction may be justified if it is designed to protect a legitimate business interest such as confidential information, and if it is reasonable as between the parties as well as in the public interest. The mere fact that an employer has a legitimate interest to protect does not of itself provide legality to a restraint of trade clause imposed by such an employer in the contract of employment. A covenant which restrains an employee from competition would invariably be held to be void as being unreasonable, unless there is some exceptional proprietary interest owned by the employer, whether in the nature of a trade connection or in the nature of trade secrets, which requires protection. A restraint against competition by an employee has been held to be justifiable if its object is to prevent the exploitation of trade secrets learned by the employee in the course of his employment. In such a trade secrets case the employer would have to prove definitely that the employee has acquired substantial knowledge of some secret process or mode of manufacture used in the course of his business. Even the general knowledge derived from secret information which has taught an employee how best to solve particular problems may not suffice.

Following English case law precedent, it is likely that an agreement not to trade in a particular place for the lifetime of the promisor would not be considered to be such an unreasonable restraint as to be void if the trade is unique/extraordinary to that particular place. If a partial restraint is limited as to time but unlimited as to space and unreasonable, the restrictive covenant would likely be held to be void. However, a condition which limits the space but does not fix the time may be held to be valid if reasonable in the circumstances. Where the type of business to be protected is specialised and the market limited, it is likely that a Court would hold that even a restriction covering the entirety of the county is not unreasonable.

There is not sufficient case law on the basis of which particular lessons in drafting/drafting points can be obtained.

iii. Is it necessary to pay an employee during the period of the covenant?

No, there is no principle mentioned in the little locally reported case law that is available, which provides that it is necessary to pay an employee during the period of the covenant.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes

i. Are they capable of being valid?

Yes

ii. What does it take to show they are valid?

It would appear from case law that a restraint protecting an employer’s customers being enticed away from the employer by a former employee would only be valid in cases where the nature of the employment is such that the customers dealt with the former employee directly and personally, with the result that such former employee would probably gain their custom if the former employee were to set up a business of his/her own. It would also appear that a court would more readily enforce a customer specific restriction but enforcing this restriction must also be reasonable so as to permit freedom of trade and the ability for the employee to use his skills.

iii. Is it necessary to pay an employee during the period of the covenant?

No. There is no principle mentioned in the little locally reported case law that is available, which provides that it is necessary to pay an employee during the period of the covenant.
Sri Lanka

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes. There is no principle mentioned in the little locally reported case law that is available which provides that an agreement restricting solicitation and hiring of former colleagues would be invalid.

However if a former employee engaged in such conduct and such conduct was viewed by a Court as amounting to unfair competition, irrespective of whether or not the restraint was legally valid, it could be prevented.

Unfair competition is defined by section 160(1) of the Intellectual Property Act No. 36 of 2003 (“the IPA”) as any act or practice contrary to honest practices in trade or industry and in particular in terms of section 160(2) of the IPA as any act or practice carried out or engaged in, in the course of industrial or commercial activities, that causes, or is likely to cause, confusion with regard to another’s enterprise or its activities, in particular, the products or services offered by such enterprise.

Section 170(1) of the IPA provides that where a person to whom any recognised rights granted under the Intellectual Property Act, including an infringement of section 160, proves to the satisfaction of the Court that any person is threatening to infringe or has infringed his rights or is performing acts which makes it likely that infringement of a right under the IPA, will occur, the Court may grant an injunction restraining any such person from commencing or continuing such infringement or performing such acts and may order damages and such other relief as the Court, may deem just and equitable. The IPA also provides that an injunction may be granted along with an award of damages and shall not be denied only for the reason that the applicant is entitled to damages.

i. Are they capable of being valid?

Yes.

ii. What does it take to show they are valid?

That the restraint is reasonable in the circumstances of the case.

iii. Is it necessary to pay an employee during the period of the covenant?

No. There is no principle mentioned in the little locally reported case law that is available, which provides that it is necessary to pay an employee during the period of the covenant.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

The Supreme Court of Sri Lanka in Coats Thread Lanka v. Sumarasundara 2011 BLR 37 discussed restrictive covenants that are imposed on the employee whilst the employee is in the service of the employer. In this case the restrictive covenant provided that “You will not be able to enter into any activities similar to that for which you are employed by this company or obtain employment elsewhere while in service with us.” The Court was of the opinion that a person is entitled to seek employment with multiple employers so as to maximize his monthly income so far as the test of reasonableness is satisfied. The Court held that where such employment impacts adversely on the quality of his work, appropriate action can be taken at that stage and that such concerns of the employer cannot restrict a person’s reasonable right to seek employment at multiple establishments.

Another familiar category of covenants in restraint of trade is that type of covenant by which a vendor of the goodwill of a business agrees with the purchaser not to carry on a similar business in competition with the purchaser. Such restraints would likely be successfully enforced more readily and more widely in favour of a purchaser than in the case where such a restriction on carrying on a similar business is imposed on an employee in a contract of employment. The argument for resolving the issue more readily in favour of a purchaser would be that the purchaser has paid the full market value for the requisition of his interest, and the interest so purchased would suffer if the vendor were free to continue his trade/business with former customers.
A global guide to ‘restrictive covenants’

Sri Lanka

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

The question of the applicable law or choice of law, would come into play once it has been established that a court hearing the matter has jurisdiction over the matter and one party is seeking to apply foreign law instead of the law of the forum. Sri Lankan Courts have had experience with choice of law disputes in the commercial law context. In situations where a choice of law clause was not contained in a contract, the Supreme Court of Sri Lanka held that the choice of law may be ascertained within the context of a contractual agreement. The Court in International Science and Technological Institute (ISTI) v. Rosa and Others, (1994) 1 S.L.R. 413 adopted both English and Australian private international law principles and held that the proper law may be ascertained through either express selection of the parties, by inferred selection from the circumstances, or through a determination by the court of the system of law with which the transaction has the closest and most real connection. However, even if a restrictive covenant were found to be governed by foreign law and the substantive content of the governing law would consider such a restrictive covenant as legally enforceable, it is possible that a Sri Lankan Court requested to enforce the restrictive covenant might decline to do so if it was of the view that the covenant sought to be enforced was contrary to public policy.

i. Can an employer impose a dispute resolution method on the employee?

Section 47A of the Industrial Disputes Act provides that any contract or agreement whereby any right conferred on any workman (employee) by or under the said Act or by any award made under the Act by an arbitrator or an industrial court or a labour tribunal is in any way affected or modified to his/her detriment, or whereby any liability imposed on any employer by or under the Act or by any such award is in any way removed or reduced, shall be null and void in so far as it affects or modifies any such right or removes or reduces any such liability. It is likely therefore that any provision imposing regular arbitration (what is meant by “regular arbitration” is arbitration other than arbitration provided for under and in terms of the Industrial Disputes Act) would be null and void. Since there is a time limit of six months within which an application to a Labour Tribunal can be made by an employee for relief, it is likely that any provision imposing a requirement of going through conciliation/mediation, would be null and void.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

As mentioned previously, an agreement in restraint of trade would likely be considered to be prima facie void, yet if it could be justified as being reasonable it would likely be enforceable.

Sri Lankan law follows the English remedy for a breach of a restrictive covenant which is injunctive relief. A Court may issue either an interim or final injunction. Enjoining orders are also available under certain circumstances. A Court would have to be satisfied that there is a serious question to be tried at the hearing and that on the facts before it there is a probability that the plaintiff is entitled to relief in order to issue an injunction. The Court would also take into consideration whether the circumstances are such that a decree which may ultimately be entered in favour of the party seeking the injunction would be nugatory or ineffective if the injunction is not issued. It should be noted that, Courts here have long followed English law authority that an injunction will not be allowed against an employee if the consequences of that injunction would be to put the employee in a position that he could have to go on working for the former employer or starve.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

There is nothing expressly stipulated in Statute law or in reported case law in regard to the specific issues which may arise relating to employee benefits, pensions and stock plans in the context of restrictive covenants. Employee share ownership schemes are not very common and the contents of such schemes are not generally publicly known.
Sri Lanka

ii. Which covenants are typically imposed?
Not applicable.

iii. What sanctions are/can be imposed by the employer for non-compliance?
Not applicable.

iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)
Not applicable.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

If a covenant is found to be null and void/unenforceable as against public policy, it is unlikely that a Court would re-write the covenant. If the covenant were found to be void it would not be possible for the person seeking to enforce the covenant to obtain an order for specific performance. In Sri Lanka the doctrine of severability may apply. Under this doctrine the invalid part or element of the contract or covenant may be severed whilst keeping the rest of the wording unchanged. It is likely that a Court in Sri Lanka would apply the English “blue pencil rule” pursuant to which severance could be effected when the part severed can be removed by running a blue pencil through it without affecting the meaning of the part remaining.

Contributed by John Wilson
A. OVERVIEW:

The right of enterprises to stipulate post-termination restrictive covenants to protect their interests is well recognized in Taiwan, and includes non-competition, prohibition on contact, and prohibition on solicitation/inducement. There is no strict differentiation between the above types of restrictive covenants and such provisions are often included under the umbrella of a “non-compete clause”.

The basis and enforceability of restrictive covenants originates in the principle of fairness under contract law. The concepts of contract law by which all post-termination restrictive covenants are evaluated are whether one party has exploited an unfair advantage in bargaining power in the negotiation of the contract, and whether there is a clear inequality in the rights and obligations of the parties in the contract.

To provide more clarity on the above abstract legal concepts, the Council of Labor Affairs has outlined five factors under which a post-termination restrictive covenant will be judged as fair and enforceable:

(1) The enterprise has a legitimate interest to protect through such non-compete covenant;
(2) the employee held a certain job or position at his/her former employer’s enterprise;

(3) the restrictions on who, where and when the employee may seek his/her next employment must be reasonable;

(4) a measure to compensate the employee in consideration of the losses resulting from such restrictions; and

(5) whether the act of the employee working for a competitor would result in a breach of trust or a breach of the principle of good faith in fact.

However, as all of the above are necessarily fact-intensive evaluations, it is not always easy to discern how the Taiwan courts will rule on a particular issue. In terms of relief sought for a breach of the non-compete covenant plaintiff-employers often first seek an injunction to halt the breach and then seek damages from the ex-employee.

**B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?**

Yes.

i. Are they capable of being valid?

Yes. Subject to the balancing factors above, there is no law that prohibits a post-termination non-competition restrictive covenant on an employee.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?

The five balancing tests mentioned above in Section (a) are the primary factors that a court would apply to determine whether a non-competition restrictive covenant is enforceable. As alluded to above, non-competition restrictions are used by employers to prevent ex-employees from disclosing “legitimate business interests” to competitors. The “legitimate business interests” have been interpreted broadly beyond simple trade secrets to include business strategies, or any other matter that could seriously interfere with the employer’s business operations. Notwithstanding the breadth of the term, the employer is still required to concretely demonstrate how the disclosure of the “legitimate business interest” would seriously impact the continued operations of the employer’s company (e.g. if the employer alleges that it has a legitimate interest to protect its “trade secrets”, the employer must show how such “trades secrets” actually qualify as a type of trade secret to be protected under the Trade Secrets Act.)

The second factor is fairly straightforward, as only employees that are operating at a level in the employer’s organization where he or she comes in to contact with the employer’s trade secrets or research data should be bound by such a non-competition covenant after the end of his/her employment.

In terms of duration, the courts have commonly found that a period of two years or less for a non-competition covenant is acceptable. The employer would also be required to state a specific geographical region in which the non-competition obligation is in effect; the general rule here is that, for the sake of competition in a free market, markets where the employer has not yet developed a presence or is planning to move into are off-limits for non-compete obligations on the employee.

Finally, the requirement of good faith means inquiring whether the ex-employee appeared to act with malice in its employment with competitors, such as poaching the former employer’s clients or stealing key information from the former employer, or otherwise engaging in bad faith behavior that would make the ex-employee’s acts unworthy of protection under Taiwan law.

Given the above, a reasonable non-competition clause should be in writing and expressly contain the following elements:

- Duration of the non-competition period

- The region in which the non-competition clause applies
Taiwan

- Type and scope of employment prohibited during the non-competition period
- Penalties for breach
- Special circumstances (e.g. force majeure conditions)

iii. Is it necessary to pay an employee during the period of the covenant?

Currently, opinion in Taiwan is split with regard to whether an employer is obliged to pay an employee during the period of the covenant. Part of the question depends on whether the ex-employee would be severely hindered in pursuing his/her livelihood as a result of this stipulation. As such, while there are no guidelines on the amount an employer should pay or the payment method to be applied, it remains one of the factors that the court will review in evaluating the fairness of the covenant and, by extension, whether it is enforceable. Therefore, if an employee is paid in consideration for his/her non-compete obligation, a Taiwan court is more likely to find the non-compete covenant to be enforceable.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?

Yes. This could involve a prohibition on the ex-employee from contacting, visiting or inviting the employer’s clients, as well as soliciting them with services or sales.

i. Are they capable of being valid?

Yes, and they generally face a lesser level of scrutiny than non-competition covenants in court because it does not necessarily impose a heavy restriction on the right to choose employment provided under the Constitution.

ii. What does it take to show they are valid?

As stated above, in practice, a court will examine the same factors as it does with respect to non-competition covenants because Taiwan law does not mandate a separate review procedure for a covenant prohibiting the ex-employee from contacting customers/clients.

iii. Is it necessary to pay an employee during the period of the covenant?

The reasonableness analysis would be similar as in Section (b)(iii) above.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?

Yes.

i. Are they capable of being valid?

Yes.
Taiwan

ii. What does it take to show they are valid?

The same balancing factors for non-compete clauses will once again apply to prohibitions on solicitation of employees. The analysis, however, will depend on whether the plaintiff-employer is able to show causation that the ex-employee induced current employees of the employer to leave. This is a very high bar, as the employer is unlikely to be aware of every detail of the lives of the ex-employee or of the current employees that are allegedly induced to leave his/her position with the employer to satisfactorily prove to a court that the current employees quit solely due to the improper exhortations and inducements of the ex-employee. For example, a court refused to find tortious interference of the employment contract between the current employee and the employer when an ex-employee established a competing company and hired his former colleague through offering a better compensation package. Therefore, since there is no effective way this kind of clause can prevent an ex-employee’s former colleagues from working with him/her in law or in practice, it can be said that the primary intent of a non-solicitation clause is to prevent ex-employees from improperly soliciting his/her former colleagues instead of interfering with an individual’s right to choose his employment under the Constitution.

iii. Is it necessary to pay an employee during the period of the covenant?

The reasonableness analysis would be similar as in Section (b)(iii) above.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?

1. Minimum service requirement

While there is no prohibition against requiring an employee to stay for a minimum amount of time before leaving the employer, the Taiwan Supreme Court has recognized that such requirement may be enforceable under certain circumstances and should not be rejected as a matter of fact. A minimum service requirement will be evaluated on the “necessity” and “reasonableness” of such an agreement. “Necessity” has been interpreted as an employer’s need to protect its investment or interests, such as large employee training expenses, and “reasonableness” with respect to whether the duration specified is appropriate.

2. Confidentiality agreement

Generally, the only factor for confidentiality agreements post-termination would be the duration of agreement. For information that is very critical to the operations of the employer, a court is likely to find that requiring the ex-employee to maintain confidentiality for an extended period of time to be reasonable. On the other hand, if the confidential information involves a particular product cycle, the duration should only be as long as the lifetime of that particular product. Note that while the justification for a non-competition clause is usually based on confidentiality concerns, the propriety of a confidentiality agreement is not evaluated at the same scrutiny level or legal bases as that of non-competition clauses.

As both of these are fact-intensive inquiries, the enforceability of such covenants will depend largely on the circumstances of the matter in question.
Taiwan

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?

For the choice of law in restrictive covenants, like any other contract, the Taiwan court will examine whether the contract has stipulated a specific set of laws to apply, and whether the terms stipulate that the Taiwan courts have jurisdiction. In the absence of either or both of the above, the Taiwan court will engage in a jurisdiction analysis to determine whether the court is able to hear the case, and whether Taiwan law may be applied to the issues.

In matters where foreign law governs the contract but the Taiwan court has jurisdiction, the court will apply the foreign law unless the application of such law violates public policy or disturbs the moral standards of the Taiwanese public.

i. Can an employer impose a dispute resolution method on the employee?

While an employer may stipulate in the employment contract to resolve disputes through arbitration or other alternative dispute resolution mechanisms, in practice, the most effective method for an employer to enforce the restrictive covenant is obtaining an injunction in court against the ex-employee before initiating an action to seek damages. As such, the courts remain the employer’s best option to obtain a remedy in restrictive covenants in comparison to other dispute resolution mechanisms.

With regard to requiring the employee to bring a claim in a foreign jurisdiction, it would be very difficult, if challenged by the employee, for an employer to argue that a Taiwan court has no jurisdiction in hearing a labor complaint that involves a Taiwan-based employee. Therefore, in practice, if a Taiwan-based employee initiates a claim against the employer in a Taiwan court despite express stipulations otherwise in his/her employment contract, a Taiwan court would likely find that it has jurisdiction to hear the matter.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?

As stated above, an employer would typically seek a preliminary injunction against the ex-employee in court to stop the offending act. There are two elements used by the Taiwan courts in determining whether a preliminary injunction is appropriate:

(1) The damages suffered by the employer if the preliminary injunction is not granted would be greater than the damages suffered by the ex-employee if the preliminary injunction is granted; and

(2) the preliminary injunction order is necessary to prevent serious harm or imminent danger.

For the first inquiry, the court will measure between the harm to the employer based on the legitimate business interest at issue (e.g. disclosure of certain trade secrets) versus the harm to the ex-employee (restriction on his/her choice or opportunity to obtain a livelihood, the scope of the restrictive covenant, etc.).

The key issues for the second inquiry are “whether the employer can demonstrate that a preliminary injunction order is necessary to prevent the harm, and the urgency of such a measure that requires a court to take this action before debating the merits of the case.”

Due to the timeframe involved, under Taiwan law, the court may at its discretion order the petitioner-employer to post a monetary security against the harm suffered by the ex-employee due to the preliminary injunction as a condition to granting the preliminary injunction. In practice, the amount of security required is often based on the compensation received by the employee during the period of the restrictive covenant.

Money damages, unless otherwise stated as punitive damages (which are allowed under Taiwan law), will fall under damages for non-performance of contract. If liquidated damages are stipulated, the court will evaluate whether the amount is appropriate based on objective facts, which include evidence on the overall socio-economic environment at the time, the damages incurred by the employer as a result of the breach, the ex-employee’s gains from the breach, the compensation due to the ex-employee during the period of the restrictive covenant, etc. As such, the stipulated damages may be reduced if the court finds that the amount disproportionately favors the plaintiff-employer at the expense of the ex-employee’s interests.
H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

Under Taiwan law, restrictive covenants can never be enforceable against an employee’s statutory pension benefits. While an employer may stipulate in the restrictive covenant to require the employee to return the bonuses, dividends, incentives awards and other monetary benefits, or received during his/her employment. In practice, however, since the employee will be required to return such monetary awards in cash, the above is generally included as part of the damages sought from the ex-employee for his/her breach of the covenant.

For shares in the enterprise held by the ex-employee, if the employment contract stipulates that such shares shall be converted to cash based on the closing price on the date of the employee’s departure and returned to the company as such, the net effect is the same as above. Besides, the courts have allowed private contracts between the employee and the company restricting transfer of the company shares that the company issued to the employee gratuitously, and that the company has the right to seek ownership of such shares from the employee upon breach of the non-compete covenant, as such contract is an expression of the intent of the employee and should therefore remain enforceable.

ii. Which covenants are typically imposed?

Other than statutory pension benefits as stated above, there are a wide variety of restrictive covenants that may be based on the forfeiture of dividends, bonuses and stock, such as non-competition, prohibition on contact and minimum service requirements. Covenants on the above items will generally be incorporated in the employment contract.

iii. What sanctions are/can be imposed by the employer for non-compliance?

As above, in case of breach, the employer may require the employee to forfeit the bonuses, dividends, etc. that he/she has received, or an amount equivalent to their value or benefits as damages.

iv. Are there any limits to what an employer can forfeit? (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)

Please see Subsection i under this Section above. For limitations to the amount of damages an employer may seek from the ex-employee, please see Section g above.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

A restrictive covenant that is found to be invalid based on the criteria stated above in this questionnaire will be deemed unenforceable against the ex-employee. Under Taiwan contract law, while an unenforceable provision will generally render the entire contract unenforceable, the contract may still remain enforceable if the invalid section is severed without materially modifying the rest of the contract. In practice, if a court finds that the scope of the restrictive covenant is so wide that it infringes on rights under the Constitution (i.e. restricting the ex-employee’s ability to obtain a livelihood), the court may take steps to reduce the scope of the restrictive covenant by severing the provisions that overstep the legal bounds.

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Contributed by: Tilleke & Gibbins

A. OVERVIEW:

Restrictive covenants are governed primarily by the Civil and Commercial Code, the Unfair Contract Terms Act, and Section 14/1 of the Labour Protection Act.

Pursuant to Section 150 of the Civil and Commercial Code, an act is void if its object is expressly prohibited by law, is impossible, or is contrary to public order or good morals. It is possible that particular restrictive covenants could be held invalid on the basis that they are illegal or contrary to public order or good morals. For restrictive covenants which are not void, the Unfair Contract Terms Act and the Labour Protection Act potentially apply.

The Unfair Contract Terms Act stipulates that contract terms which are not void, but which cause a person whose right or freedom has been restricted to shoulder more of a burden than a reasonable person could have anticipated under normal circumstances, shall only be enforceable insofar as they are fair and reasonable in the circumstances. Courts are to consider the geographic scope of the area specified and the period of restriction of right or freedom, as well as the ability and opportunity of the employee to carry on his or her occupation or otherwise engage in business, as well as all legitimate advantages and disadvantages of the contracting parties.
Thailand

In determining to what extent particular terms are enforceable as fair and reasonable, courts are to take all circumstances into account, including good faith, bargaining power, economic status knowledge and understanding, adeptness, anticipation, guidelines previously observed, other alternatives, and all advantages and disadvantages of the contracting parties according to actual conditions; ordinary usage applicable to such kind of contract; time and place of performance or making the contract; and whether one party is made to bear a much heavier burden than the other.

In some circumstances, the Trade Competition Act may also be relevant. Under the Trade Competition Act, certain contractual provisions can be held void on the basis that they are anticompetitive.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?
Yes.

i. Are they capable of being valid?
Yes.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?
The court has the authority to consider whether non-competes are valid, taking into account the factors outlined in section a above. Generally, to be enforceable, a non-compete should have a defined geographic scope and a defined period of time which does not extend beyond two years after termination of employment.

iii. Is it necessary to pay an employee during the period of the covenant?
The law does not require payment to a former employee during a non-compete period. Even though this is not required by statute, some practitioners take the position that payment in respect of a non-compete functions to make it more enforceable.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?
Yes.

i. Are they capable of being valid?
Yes.

ii. What does it take to show they are valid?
The court has the authority to consider whether such restrictions are valid, taking into account the factors outlined in section a above. It should be noted that we more frequently see clauses providing for non-solicitation of customers/clients, rather than clauses prohibiting all contact.

iii. Is it necessary to pay an employee during the period of the covenant?
The law does not require payment to a former employee during a period of no-contact or non-solicitation of customers/clients.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?
Yes.
Thailand

i. Are they capable of being valid?
Yes.

ii. What does it take to show they are valid?
The court has the authority to consider whether such restrictions are valid, taking into account the factors outlined in section a above.

iii. Is it necessary to pay an employee during the period of the covenant?
The law does not require payment to an employee/former employee in respect of a period of non-solicitation/restriction on hiring of such person’s colleagues/former colleagues.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?
Other frequently included restrictive covenants concern intellectual property and protection of employers’ confidential information. Enforceability of such provisions is also subject to other laws beyond those outlined here.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?
This issue typically arises in the larger context of considering the extent to which an employment agreement can provide for the applicability of foreign law. The Act on Conflict of Laws provides that the parties to a contract can agree on the governing law of the contract, so long as the chosen foreign law is not contrary to the public order or good morals of Thailand. On the basis that the Labour Protection Act, the Labour Relations Act and the Unfair Contract Terms Act implement matters which are arguably fundamental public policy, the position would be that the parties could agree to apply foreign law, but only insofar as such foreign law does not run contrary to the above laws.

i. Can an employer impose a dispute resolution method on the employee?
Thai courts are not bound by contractual provisions on choice of forum. With respect to arbitration provisions, however, Thailand is a party to the New York Convention and, as a general matter, Thai courts will enforce arbitration provisions in contracts, so long as one of the parties raises the issue and so long as the agreement to arbitrate is not void, inoperative, or impossible to perform under the Arbitration Act or the Civil and Commercial Code, or other laws. In this regard, there remains some question as to the validity of arbitration clauses in employment agreements.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?
Final remedies include payment of monetary damages, delivery of property, specific performance, and/or restraint from performance of a particular act. The specific award would depend on the circumstances of each case, but courts typically prefer to award monetary damages. However, permanent injunctions are sometimes issued to prevent infringement or unauthorized disclosure of an employer’s trade secrets.

Temporary relief (which can include injunctions, restraining orders, and attachment) is typically difficult to obtain as the courts usually require very strong evidence of an imminent threat to justify such relief.
Thailand

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?

In principle, restrictive covenants can be contained in any document which constitutes part of an employee’s employment agreement. In this regard, the same principals of enforcement as outlined in section g above would be applicable, regardless of whether the relevant restrictive covenants are contained in an employee’s ‘main’ employment agreement, or in a separate document signed by both parties.

Questions commonly arise, however, with regard to what enforcement actions the employer might have beyond those remedies described in section g above. In the event of breach of a restrictive covenant, it would generally not be lawful for the employer to deny payment of any benefits to which an employee is entitled by statute (e.g. statutory severance, payment for unused annual leave, etc.). As for provident funds, these are handled by a separate fund manager, and it would generally be beyond the ability of an employer to deny payment to an employee, if the employee is lawfully entitled to payment in accordance with the applicable provident fund regulations.

With respect to employment benefits which are not required by statute, such as those under performance bonus plans and employee share schemes, it would be possible to write the applicable terms such that entitlement would be lost if an employee breached particular restrictive covenants. Were the matter to proceed to litigation, however, the employee may challenge the validity of the restrictive covenant(s) (see factors in a above), as well as the forfeiture provisions.

ii. Which covenants are typically imposed?

It is unusual for restrictive covenants to be written into performance bonus plans and employee share schemes.

iii. What sanctions are/can be imposed by the employer for non-compliance?

Performance bonus plans and employee share schemes could be written to provide for an employee to lose entitlement to certain benefits, but as noted above, an employee may challenge the validity of the restrictive covenant(s) (see factors in section a above), as well as the forfeiture provisions.

iv. Are there any limits to what an employer can forfeit (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?

The law does not impose specific limits on what could be forfeited under performance bonus plans or employee share schemes. However, the relevant restrictive covenant(s) and/or forfeiture provisions may be subject to challenge.

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

Pursuant to the Civil and Commercial Code, a restrictive covenant could be void on the basis that it is illegal or contrary to public order or good morals, in which case it would simply not be enforceable; depending on the agreement in which it exists, this may or may not invalidate the entire agreement. With respect to restrictive covenants which are not void, courts are empowered, pursuant to the Labour Protection Act and the Unfair Contract Terms Act, to order that terms which excessively restrict the right or freedom of an employee in professing an occupation, shall only be enforceable insofar as they are fair and reasonable in the circumstances, and do not cause the employee to bear an unforeseeable burden.

Contributed by Tilleke & Gibbins
A global guide to ‘restrictive covenants’

Vietnam

Contributed by: MBJSM (Vietnam)

A. OVERVIEW:
Post-termination restrictive covenants are not common in Vietnam. Except for confidentiality obligations, other restrictive covenants are not provided for by the laws of Vietnam and are unlikely enforceable by Vietnamese courts.

The remedies available for breach of the confidentiality obligations under Vietnamese law are compensation for actual and direct damages and penalty. To require for compensation and penalty, there should be in place an agreement between the employer and its ex-employee.

B. NON-COMPETE CLAUSES: Can an employer require a post-termination non-competition covenant from an employee?
Yes.

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Vietnam

i. Are they capable of being valid?
Although an employer can require a post-termination non-competition covenant from an employee it is unlikely to be enforceable by a Vietnamese court because of the existence of a general principle of the Constitution according to which a citizen has the right to work. Any restriction of this right would be deemed as an incursion on the fundamental rights of citizens. In practice, such a restrictive covenant would be enforceable if the employer pays the employee an amount for the period during which the employee is not allowed to work for a competitor.

ii. What does it take to show they are valid (legitimate interest, drafting pitfalls to avoid)?
Please see (i) above. The employer should provide evidence that the employee has been paid for the period during which he/she is not allowed to work for a competitor.

iii. Is it necessary to pay an employee during the period of the covenant?
There is no legal requirement. It is subject to agreement between the parties.

C. CONTACT PROHIBITION CLAUSES: Can an employer require a post-termination clause prohibiting contact with customers/clients?
There is no law regarding contract prohibition. In practice the parties may agree on prohibition of contact with customers/clients but this prohibition would be hard to enforce.

i. Are they capable of being valid?
Please see response above.

ii. What does it take to show they are valid?
The employer would need to show that there is an agreement in place and that due to the employee’s breach, the employer has incurred actual and direct damages/losses.

iii. Is it necessary to pay an employee during the period of the covenant?
There is no legal requirement. It is subject to agreement between the parties.

D. NON-SOLICITATION OF EMPLOYEES CLAUSES: Is it possible to impose a clause prohibiting solicitation and/or hiring of former colleagues (both during and after employment)?
There is no law regarding non - solicitation. In practice, the parties may agree on prohibition of solicitation and/or hiring of former colleagues (both during and after employment) but this prohibition would be hard to enforce.

i. Are they capable of being valid?
Please see above.

ii. What does it take to show they are valid?
The employer would need to show that there is an agreement in place and that due to the employee’s breach, the employer has incurred actual and direct damages/losses.
Vietnam

iii. Is it necessary to pay an employee during the period of the covenant?
There is no legal requirement. It is subject to agreement between the parties.

E. OTHER COVENANTS: Are there any other types of employment- and post-employment-related covenants which are common in this jurisdiction?
The only restrictive covenant which are recognized and provided for by the laws of Vietnam are confidentiality obligations. In this regard, the Labour Code provides that for an employee working in a position directly involving business or technological secrets, an employer has the right to agree with the employee in writing on the contents, duration of confidentiality obligations and compensation for damages in case of breach.

F. CHOICE OF LAW: What is the impact of the choice of law on the enforcement of a restrictive covenant?
For an employment matter, the governing law must be the laws of Vietnam.

i. Can an employer impose a dispute resolution method on the employee?
No, the dispute resolution method must be in accordance with the labour laws of Vietnam. The parties are encouraged to settle any dispute through negotiation and mediation.

G. ENFORCEMENT: How are covenants typically enforced in this jurisdiction?
An employer seeking to enforce a covenant has the remedies of compensation for actual and direct losses/ damages and/or penalty. It may initiate a lawsuit to recover damages caused by the breach. Please see in the overview section above.

H. SPECIFIC ISSUES RELATING TO EMPLOYEE BENEFITS, PENSIONS AND STOCK PLANS:

i. Do the same principles of enforcement outlined above at g. apply?
There is no legal provision regarding employee benefits, pensions and stock plans in case of breach of post-termination restrictive covenants. Where the parties agree on these matters, the principles of enforcement of these specific issues are same as those outlined at item (g) above.

ii. Which covenants are typically imposed?
Only confidentiality obligations may be enforced.

iii. What sanctions are/can be imposed by the employer for non-compliance?
Compensation for direct and actual damages/losses and penalty.

iv. Are there any limits to what an employer can forfeit (e.g. retroactively forfeit for matters prior to adoption of the forfeiture/claw back provisions)?
Damages/losses to be compensated must be direct and actual.
Vietnam

I. IMPACT OF INVALIDITY: What happens if a covenant is found to be invalid? Can a Court re-write the covenant or is it void?

The court would declare that the covenant is void.

Contributed by Phuong Mai Nguyen
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