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# Non-compete Clauses: Responses to Treasury Consultation Paper and to Questions.

## **Responses to Consultation Paper**

1. Our previous submission to the 'Commonwealth Treasury Competition Review of Non-compete Clauses and Other Restrictions' (William van Caenegem and Caitlyn Douglas, Bond University, May 31, 2024; 'previous submission'; see Annex 1) called for:
  - a. The introduction of an absolute statutory maximum term for employment non-competes of six months irrespective of salary levels;

- b. The introduction of statutory conditions for an enforceable non-compete, amounting to the codification of the current common law reasonableness test, plus a statutory requirement of adequate and distinct remuneration or consideration for the period of any post-employment restraint;
  - c. Statutory recognition that a non-compete is only enforceable if it serves one or both of the legitimate interests of the employer recognised in the new statutory provisions, those being: the existence of particularised trade secrets (properly so called) that the employee had access to; and/or client connection;
2. In our previous submission we also called for an express statutory provision to the effect that non-competes in employment contracts are in principle against the public interest and unenforceable. The recognised exception to that principle is that a non-compete clause is enforceable if it is not longer than six months; otherwise complies with the new statutory provisions; and is no wider than required to protect one or both of the statutorily identified legitimate interests.
  3. In our previous submission we called for an 'all or nothing' approach to non-competes. If a non-compete is held to be non-compliant in its contractual form, then it is to be held unenforceable. Courts should be expressly prohibited from rewriting or amending a non-compete clause to bring it within the reasonableness realm.
  4. The Treasury questions are framed in relation to a different model, that would introduce a salary threshold for enforceable non-competes. In the answers to Treasury questions below, I adhere 'mutatis mutandis' to the views expressed in our previous submission.
  5. Object clause: in addition to the recommendations made in our previous submission, some consideration should be given to the inclusion of an 'Object clause'. An example of such a clause is found in Patent Act 1990 (Cth) section 2A ('Object of this Act'). That clause refers to balancing competing interests, but it might be preferable here to refer to primary and subordinate interests. The former would be the public policy interest in employee mobility and a competitive labour market; the latter the interest of a firm to some level of protection for trade secrets with real value, and the special connection an employee has with particular clients.
  6. Our previous submission, although recommending a different approach, remains relevant to the Treasury proposal in a number of aspects. Where that is the case, our previous submission is cross-referenced in the answers below. Where possible the approach that requires less consequential regulation is preferred. Regulatory density and uncertainty tend to favour the stronger party in any bargaining situation (in this context, the employer).

## Responses to Consultation Questions

### 3. The ban on non-compete clauses for low- and middle-income workers

#### 3.1 Definition of a non-compete clause

1. How should a non-compete clause be defined in the Fair Work Act? Is the FTC definition appropriate for an Australian context?

***We provided a suggested definition in our previous submission (see p18). A straightforward definition is preferable, where the targeted clause is circumscribed as one 'that restricts the freedom of a worker to be employed by or undertake remunerated work for another person or for the worker's own account in any capacity'. The terms 'in any capacity' are intended to be a cover-all so that if a clause purports to restrict the freedom to undertake any kind of duty it would amount to a restraint targeted by the new provisions.***

2. Should any specific kinds of common contractual terms be explicitly included or excluded from this definition?

***The term 'non-compete' clause or 'restraint of trade' should not be used because it is 'encrusted with meaning' which may prove to be unhelpful. They are also terms that are not confined to contracts of employment, and different principles apply to their enforceability outside that context, which does not aid clarity. The words 'restrictive term' identify the targeted clauses clearly enough without muddying the waters. This was the terminology adopted in our previous submission, to cover what is intended to be rendered unenforceable under certain conditions.***

#### 3.2 Scope of workers affected

3. Should the ban on non-compete clauses apply to workers who are not employees, such as independent contractors?

***If workers are not employees a whole different set of issues arises, and it is preferable to limit the relevant provisions to an 'employee' in the sense that the term is understood and has evolved over time in employment law. It would seem somewhat illogical to extend one form of protection to non-employees but not other protections that employees properly so called are entitled to. If contractors deserve or require broader protection, then the relevant changes should be at the level of the definition of the term 'employee' and whom it encompasses (and closely related terms). If the result of evolving judicial interpretations of that term is to expand the group of persons considered employees, then the automatic consequence would be to extend to them the protection against certain non-compete clauses offered by the legislation here considered. If a contractor is restricted from working as a contractor for another organisation after cessation of their contract for services (not 'of service'), then this is perhaps a problem that falls more within the remit of competition law than of the regulation of employment.***

4. Are there any potential unintended consequences that may arise from a reliance on the high-income threshold in the Fair Work Act? If so, how could they be addressed?

***Our previous submission did not advocate for the salary threshold approach, but for an absolute time limit of six months plus an obligation to separately remunerate a person subject to a restraint, for the period of the restraint. We considered our***

*suggested approach to have a beneficial deterrent effect on employers, as they would likely not or rarely be motivated to compensate employees, in particular lower paid ones, for 'sitting out' a non-compete term. Nonetheless our proposal still gave employers scope to protect important trade secrets and client connection with a limited term restraint. Our proposal is effective and relatively simple, whereas the proposed high-income threshold appears to adopt a cut-off point whose particular value point is difficult to justify in policy terms. Furthermore, it is arguable that the mobility of high-income employees is in fact of critical importance to a dynamic economy and the most likely to be actually observed or enforced. A further risk with the threshold approach is that there is a built-in temptation for employers to game the threshold point, which might require complex countermeasures (further detailed rules). Finally, there is also the risk that alternative approaches, still detrimental in terms of employee mobility etc, might be adopted more frequently by employers, in particular gardening leave.*

5. At what point in the employment relationship should the high-income threshold be applied to determine whether a non-compete clause is allowable or not, and why? For example, should it be applied at the time the contract for employment is entered into or varied, the time the employment relationship ends, or some other time?

*This is one of the serious complications that result from the threshold approach. As indicated above we advocated for an approach (a strict term limitation coupled with a remuneration obligation) which we considered would require fewer further and complex rules or regulations to implement and make effective. Generally, we favour provisions relating to non-competes that minimise the need for consequential or additional detailed rules.*

6. Would the application of the ban to all fair work instruments, as defined by the Fair Work Act, have any unintended consequences?

**No comment.**

### 3.3 Enforcement

7. What is the appropriate penalty for breaches of the ban on non-compete clauses? Are the existing penalties in the Fair Work Act for other contraventions appropriate? Please consider the following matters in your feedback:

- (a) the type of penalty
- (b) the magnitude of the penalty, and
- (c) the circumstances in which the penalty should apply.

*In our previous submission we did not advance the option of a penalty applying where an invalid non-compete is imposed by an employer. I would reiterate that a simpler approach is sufficient: that the non-compliant term or clause is unenforceable. That is in line with the present law concerning unreasonable restraints, and requires no further penalty measures etc. It would constitute an effective deterrent against employers including a non-compliant non-compete in an employment contract. The salary threshold does lend itself to a relatively simple message that could be readily communicated to employers and employees ('If you're on less than A\$175000.00, your non-compete is invalid'). In terms of potentially valid non-competes above the threshold level, our previous submission recommended a number of measures that would make the outcome of a putative judicial review of a particular clause more predictable. They would apply to the threshold approach too.*

8. Should there be any defences available to contraventions of the ban on non-compete clauses? If so, in what circumstances?

***No; there may well be scenarios that I have not considered where an exception is warranted, but in the interests of simplicity and predictability of outcomes (which is very significant because of the chilling effect on employees' decision-making and job mobility of uncertainty) there should, if at all possible, be no exceptions.***

9. Which parties should be able to commence proceedings for a breach of the ban on non-compete clauses and why?

***In our previous submission we proposed that any clause that is non-compliant should simply be unenforceable by force of the new statutory provisions. However, when considering the salary threshold approach, if proceedings do ensue (for instance because for an employee over the threshold, bound by a non-compete, there is a dispute about remuneration or the calculation of a term, or about reasonableness or other such issues), then the employer and employee should be able to commence proceedings. The proceedings should be on an expedited basis and in a low-cost forum. An innovation we called for in this regard was the instigation of a ban on any proceedings against a new employer, who takes on an employee apparently bound by a non-compete, for the tort of interference with a third party's contractual obligations. The result would be that an employee could rely on advice and even practical or financial support from their new employer if a dispute about an existing non-compete that purports to bind the employee results in proceedings or necessitates the seeking of legal advice by the employee.***

10. What role should the Fair Work Ombudsman have in relation to the ban on non-compete clauses? Are there particular areas where employees and employers may need assistance to understand and implement any proposed ban on non-compete clauses?

***No comment.***

11. Are there any specific remedies that should be available to persons impacted by potential non-compliance with the ban? What role would the Fair Work Ombudsman have to enforce breaches of the ban, and would new compliance tools be necessary?

***No additional comment – see comments above.***

12. Should the Fair Work Commission have a role in resolving disputes that arise from the ban on non-compete clauses?

***The view we expressed in our previous submission was that anything that can assist to resolve disputes about non-competes expeditiously and cheaply should be adopted. It is critically important that employees not be threatened or burdened with long, uncertain and expensive processes or proceedings. The potential for such proceedings to ensue will otherwise encourage employees either not to leave their employment or to comply with a non-compete even where there is a reasonably arguable case that it is non-compliant. Processes or powers available to the FWC to intervene in and effectuate resolution of any dispute relating to the contemplated rules should be applicable here. Complexity, uncertainty and delay will primarily be detrimental to the interests of employees who tend to be less well resourced. They are the parties whose position the contemplated changes aspire to ameliorate.***

13. What additional powers, if any, would the Fair Work Commission require to deal with disputes it may be permitted to hear about non-compete clauses?

***No comment.***

### 3.4 Limited statutory exemptions

14. Are there any exemptions to the non-compete ban that are justified on strong public policy or national interest grounds? How should any such exemptions be applied (e.g. permanent, temporary, by application etc)?

***One reason why in our previous submission we preferred the absolute six-month limit for valid non-compete clauses that also comply with other requirements, is that the protection of genuine trade secrets might well warrant a restraint, but then only for a fairly limited term. In the threshold approach, this would only be an available legal tool in relation to employees on more than A\$175000.00. Obviously one of the justifications that validates above-threshold restraints is that the employer has genuine trade secrets to protect which the employee had actual access to. Where non-competes are unenforceable (below the salary threshold) a non-compete can no longer be used for that purpose, although an employee on a salary below the threshold is not relevantly less likely to have been exposed to genuine trade secrets of the employer. The latter will then only be able to rely on trade secrets law (breach of confidence) or specific confidentiality clauses for a remedy in relation to putative post-employment abuse of trade secrets. It is arguable that it is in the national interest, or required on public policy grounds, that more effective trade secrets protection be available than equity offers via the action for breach of confidence and than a contractual clause can provide (in particular because the law requires proper particularisation of trade secrets so protected).***

### 3.5 Transitional arrangements

15. What transitional arrangements are required to support workers, and business compliance with the ban?

***No comment.***

16. How should the ban apply to non-compete clauses contained in existing contracts after commencement?

***Perhaps the most effective solution would be to provide that all such clauses become unenforceable after a certain period (say one year) has elapsed from the moment the statutory ban has come into effect (or earlier depending on the particular non-compete's duration).***

## 4. Other reforms to employee restraints of trade

### 4.1 Non-compete clauses for high-income employees

1. What approach for employees earning above the high-income threshold best strikes the balance between the public interest in competition, productivity, job mobility and the protection of legitimate business interests?

***I refer here to our previous submission. That submissions contains a description of the principles that should apply to restraints that fall within the six-month term limit we proposed, but are equally applicable to non-competes for employees above the threshold salary level as contained in the Treasury proposal.***

2. If mandatory compensation were adopted what should be the minimum compensation required?

*In our previous submission we proposed that the compensation be a matter for statutorily unfettered negotiation between the parties. However, we also proposed that when courts undertake a ‘reasonableness review’ of a non-compete clause, an additional factor in their consideration should be the adequacy of the separate and distinct consideration for the restraint. We do not feel it necessary to further prescribe what adequate consideration might amount to, in the expectation that courts would develop jurisprudence concerning this issue. Obvious guidance points courts might have regard to would be the employee’s existing salary level; the ability and reasonable expectation of the employee finding and undertaking employment not covered by any restraints during the non-compete period; and the level of remuneration an employee might expect to obtain from such employment. The term ‘adequate’ is obviously not a term of art – ‘reasonable’, ‘proportionate’ or some other term might be more apt.*

3. If a duration limit were imposed, what would be the most appropriate maximum duration?

*In our previous submission we proposed a maximum term (‘duration limit’) of six months for all non-competes. This proposal and the reasons for it set out in our previous submission remain appropriate and relevant.*

#### 4.2 Non-solicitation clauses for clients and co-workers

4. Should the use of client non-solicitation clauses be restricted? If so, what sorts of restrictions are appropriate (e.g. duration, type of activity, and scope of clients).

*We did not make any previous submissions in relation to ‘non-solicitation of clients’ clauses. In our ‘Proposed provisions’ in our previous submission (‘Section 1 - Rule’, p18) we recommended that contractual clauses that restrict or limit ‘the right or freedom of a worker to be employed or undertake remunerated work etc.’ should be rendered unenforceable, except in certain cases of reasonable protection of legitimate interests. In my view if a non-solicitation clause reaches the level of derogation or abrogation of the relevant right and freedom to work, then a non-solicitation clause would amount to a non-compete clause under our proposed definition and be potentially unenforceable. There has been previous caselaw finding that if a non-solicitation clause (as also a confidentiality clause) is so broad as to amount to a non-compete (or a ‘restraint of trade’) it is not enforceable because against public policy, unless it is reasonable within the established principles of restraint of trade law. This jurisprudence provides some relevant guidance here.*

5. When, if ever, should it be legitimate for business to use co-worker non-solicitation clauses? If these clauses can be legitimate, what restrictions would be appropriate to impose on their use?

*I refer to para 88 of our previous submission. The implication of that paragraph is that ‘non-solicitation of co-worker’ clauses should be unenforceable. The ‘stability of the workforce’ presently justification sometimes proffered as an interest underpinning such clauses is in our view unpersuasive and thus not legitimate. Such clauses amount to nothing more than an unwarranted interference with competition, inimical to public policy. This applies once an employee has left their employment. If an employee during their employment encourages co-workers to leave with them in the future, then the employer who becomes aware of it may have a remedy for a breach of the duty of fidelity owed by every employee to their employer.*

#### 4.3 Other requirements for valid restraint clauses

6. Should restraints with cascading duration periods and geographic extents be allowed?

***No – in our previous submission we set out a complete framework for compliant non-competes with a maximum term of six months, and cascading clauses do not fit within this framework. Cascading clauses are uncertain and effectively delegate the task of writing a valid clause to a court. We adhere to strict application of the traditional ‘all or nothing’ approach of the common law, with no blue-pencilling or amending power, or relevant choices able to be handed to any court or tribunal by the drafters of the contract of employment. The ‘all or nothing’ approach will have a chilling effect on the adoption of non-compete clauses by employers which is, as we previously explained, a desirable outcome. The uncertainty engendered by cascading clauses tends to play out against employees and is therefore an undesirable feature of the present law.***

7. Should severability of other parts of restraint clauses be limited in other ways?

***See reply at 4.6 above.***

8. Should businesses be required to specify the legitimate interests to be protected by a restraint clause?

***In our previous submission we recommended that non-competes should only be valid if they serve a statutorily recognised interest, the only such interests being: particularised confidential information; and ‘client connection’. It is also required that the non-compete be precisely tailored to protect those interests and not be any broader than necessary. We do not recommend that the employer is statutorily required to specify these interests in the contract of employment, in the absence of which a clause would automatically be invalid. However, the employer will have to tender evidence in relation to the existence of the relevant interest(s) and how the non-competes is required in its particular terms to protect that interest. In that light, no doubt it would be good practice for an employer to specify the interest(s) served by the restraint in the contract of employment, but we do not believe it should be a mandatory requirement.***

9. Should client relationships or workforce stability ever be justified for a non-compete clause of the same duration when a more targeted non-solicitation clause could apply?

***For workforce stability clauses see 4.5 above. For client connection clauses see 4.8 above. It should not be a requirement that a client connection based non-compete clause is only valid if it can be established that a narrower non-solicitation clause could not do the work required. This would be a difficult and complex matter to prove and ‘the game would not be worth the candle’ in our view. Complexities of this kind deliver little in terms of desirable outcomes.***

10. Should other aspects of the existing common law doctrine be clarified or amended?

***Our previous submission which was predicated on non-competes of less than six months being enforceable if reasonable, set out the elements of the common law doctrine that should be codified in statutory provisions. These would be equally applicable in the context of a salary threshold approach, in relation to non-competes purporting to bind employees whose salary is above the threshold level. Additionally to those already mentioned above, we recommended and here repeat that a court should be expressly empowered to declare that a non-compete clause is unenforceable for vagueness (or ‘want of clarity’) or uncertainty.***



## 5. Restraints on concurrent employment

1. Are there any other considerations or potential unintended consequences if restraints on concurrent employment were to be regulated beyond the common law?

***No comment.***

2. If there were to be restrictions on these restraints, how should they be implemented?

3. ***No comment.***

## 6. No-poach and wage-fixing agreements

1. What civil penalty should apply to businesses that have no-poach and wage-fixing agreements in breach of the ban? Should criminal penalties also apply, in line with the cartel provisions in Part IV of the Competition and Consumer Act?

***In our previous submissions we recommended that such agreements should be subject to the full force of the competition law (the CCA).***

2. Should there be exemptions to the proposed ban on no-poach agreements? If yes, on what grounds? What restrictions should apply to their use?

***None unless perhaps in the interests of national security.***

3. Should there be exemptions to the proposed ban on wage-fixing agreements? If yes, on what grounds? What restrictions should apply to their use?

***No comment.***

## ANNEX 1

*Submission by William Van Caenegem, Professor, and Caitlyn Douglas, Research Associate, Bond University to the Australian Commonwealth Treasury Competition Review of Non-compete Clauses and Other Restraints, 31 May 2024 (also available via <https://treasury.gov.au/consultation/c2024-514668>).*

### INTRODUCTION AND POLICY ANGLE

1. *Arup, Dent, Howe and van Caenegem (co-author of the present Submission) examined non-compete clauses in 2009-2011, supported by an Australian Research Council (ARC) research grant. Findings were published in the UNSW Law Journal. This was the only empirical research on the legal practice around employment non-compete clauses undertaken at that time in Australia. Our policy focus concerned the impact of these clauses on mobility in a knowledge and skills-based economy. Our perspective was that the prevalence and proliferation of non-compete clauses in Australia was inimical to the mobility and freedom of employment that are essential preconditions of a competitive market economy.*
2. *Our particular focus was on the legal practices that had developed in the shadow of the law of employment non-compete clauses in Australia. We found that non-compete terms were often included in the form of 'boilerplate' clauses in employment contracts. Such clauses are poorly adapted to the particulars of the employee they concern. Although often unenforceable, they nonetheless affected mobility in various concerning ways.*
3. *We noted a commonly held view that non-compete clauses are either 'not worth the paper they are written on', or at the very least, of doubtful validity. Critically, this uncertainty about the enforceability of such clauses tended to disadvantage employees considering whether to comply, as the weaker party in any putative subsequent dispute or litigation. They were therefore inclined to 'play it safe' by either observing the terms of the non-compete or deferring a decision to change employment, even though the non-compete clauses that troubled them would not stand up to hypothetical judicial scrutiny.*
4. *Because an employee faced with uncertainty and in a weak transactional position would tend to comply with or be deterred by any non-compete, both valid and invalid non-compete clauses had a chilling effect on mobility.*
5. *We found that employers were more capable of absorbing the risk of litigation in relation to a non-compete because they were better resourced, better advised, enjoyed strategic benefits from enforcement action, and were more capable of gaming existing non-compete clauses to obtain concessions in the form of enforceable undertakings from ex-employees. Although such undertakings were usually less constraining than the non-compete that triggered their adoption, they still adversely affected mobility and freedom to compete with the ex-employer.*
6. *We advocated in favour of the 'all or nothing' common law approach to judicial scrutiny of non-compete clauses and against 'blue pencilling' and 'cascading clauses'. This is because when courts exercise a power to rewrite non-compete clauses to bring them within the court's bounds of reasonableness, they incentivise employers to include excessively restrictive clauses, in the expectation judges will rewrite them and that broader non-compete clauses will deter employees more.*

7. We also called for close judicial attention to, and strict observance of, the reasonableness factors that enable a non-compete to be enforced in exception to the baseline principle that they are unenforceable as illegal restraints of trade and against public policy. We argued against any expansion of the categories of 'legitimate interests' that justify a restraint.

8. We raised the desirability of statutory intervention with various options canvassed. Some were procedural but we do not reiterate those here. The other options are included in our consideration under 'OPTIONS FOR REFORM AND EVALUATION OF THOSE OPTIONS' below.

9. In terms of the importance of employee mobility in a knowledge, information and skills driven economy, we relied on our own analysis and also on extensive US research and publications that address these issues. The previous work of van Caenegem, co-author of the present Submission, highlighted the local significance of this issue, and stressed the importance of mobility as a longstanding pillar of the market economy, a central aspect of human freedom, and a crucial driver of innovation and creativity.

10. A core point is that individual workers should be free to determine in what organisational context their skills and experience are optimised. This approach benefits both basic freedoms and economic efficiency. Liberty of employment should only be displaced with the clearest possible real-world justification. Non-compete clauses shackle a critical freedom of choice and personal welfare optimisation and starve a significant engine driving competition of fuel.

11. Subsequent and more recent work on the importance of employee mobility, specifically in information, knowledge and skills driven economies (of which the United States is the prime example), has done nothing but further reinforce the point that non-compete clauses cause significant detriment. The writings of Gilson, Lobel, Lemley, Starr, Marx, Bishara, Lipsitz, Fleming and others are sufficiently rigorous and persuasive to convince the US government to prohibit non-compete clauses altogether. This is a federal intervention in a previously state-regulated matter, where California stood out as a pre-eminent innovation and knowledge-driven economy, in part because non-compete clauses had been outlawed there for many decades. The work of Gilson brought attention to this causal connection between the absence of non-compete clauses in labour contracts and the dynamism of the Californian innovation-based economy. That proposition has not been fundamentally shaken by any subsequent work of the scholars mentioned above or others.

12. The United Kingdom has also resolved to greatly restrict non-compete clauses, limiting them to a maximum term of three months.

13. These developments reinforce our previously expressed view that it is timely to subject these clauses to close scrutiny and limit, if not prohibit, their adoption in employment contracts. As will be seen below, we do not advocate for a complete prohibition, but for a form of regulation that will be effective to deter the spread of non-compete clauses throughout the economy but retain some ability to protect trade secrets where the employer finds that genuinely necessary. Our view is that this is important in an economy such as Australia's, which is driven by knowledge, skills and information but also relies on a more traditional industrial base, in such industries as mining and agriculture. It would further ensure that non-compete clauses are not a surreptitious instrument for simply preventing competition but where upheld, do serve a legitimate interest.

14. Our focus on mobility when considering non-compete clauses accepts that there are many other perspectives that form a valid basis for policy evaluation. Nonetheless, our view is that none of these perspectives stress putative benefits of non-compete clauses. Rather, they suggest that priorities such as reinforcing workers' rights; vindication of the right to work as a fundamental human freedom; improving worker income levels; redressing bargaining

*imbalances; and maintaining the competitiveness of a market economy all support a restrictive approach to non-compete clauses.*

15. *In any case, we believe that moving to restrict non-compete clauses in employment is warranted from a mobility-enhancing perspective alone, because of the fundamental economic importance of such mobility. This Treasury Review, is in any case, focused on the competition aspects of the non-compete controversy.*

16. *We also make the point that eliminating non-compete clauses is a ‘zero sum game’: employers might lose by the greater freedom of employees to leave them, but they also win by employees having greater freedom to join them. Their ability to do so would tend to generate beneficial competition between employers in the provision of more attractive and effective workplaces, and more meaningful work.*

## **BASIC LEGAL PRINCIPLES**

17. *Non-compete clauses in employment contracts have been the subject of countless items of academic and judicial analysis and have now attracted significant political attention as well. That they involve balancing competing public and private interests, has been highlighted in a range of valuable discussions in the literature about their development over time.*

18. *More specifically, the ARC research-based article by Arup, Dent, Howe, and van Caenegem referred to above, provides a nuanced understanding of the context in which non-compete clauses operate at common law. The law is also well documented in Heydon’s text, and in further recent analytical accounts of non-compete law in Australia. With this in mind, our Submission does not seek to restate the established law exhaustively and in detail.*

19. *Notwithstanding this, to understand our proposals and recommendations for reform in the current Submission, it is important to reiterate some basic legal principles and recent controversies.*

20. *In Australia, the enforceability of non-compete clauses is largely regulated by the common law restraint of trade doctrine as espoused by Lord Macnaghten in Nordenfelt v Maxim Nordenfelt Guns and Ammunition Co Ltd (‘Nordenfelt’).*

21. *More specifically, Nordenfelt stands for the presumption that restraints of trade are unenforceable because they are contrary to public policy. Despite this general principle, Lord Macnaghten went on to determine that the presumption can be rebutted if a clause is reasonable in that it does no more than protect an employer’s legitimate interests and is not injurious to the public interest.*

22. *Regarding legitimate interests, it has been subsequently recognised that an employer is entitled to protect confidential information (including trade secrets), and customer connection by way of a non-compete agreement. To this has been recently added, the maintenance of a stable and trained workforce, sometimes referred to as ‘staff connection’. Without elaboration on each interest here, the court ultimately assesses the extent to which ‘legitimate interests’ deserve protection in terms of the duration, nature, and geographic area covered by the non-compete clause in question.*

23. *Notwithstanding some minor clarifications and developments, the essence of the Nordenfelt doctrine has otherwise remained firmly in place for more than one century. Upon examination of this doctrine over time, it is clear that the enforceability of a non-compete clause is independent of the validity of the employment contract, and a clause cannot be allowed to stand if it merely protects against competition. Hence, the courts have been said to operate as ‘guardians of the public interest’, overriding otherwise valid clauses in employment contracts for the benefit of free competition and mobility where the circumstances allow.*

24. A consequence of this guardianship is the common law court taking an ‘all-or-nothing’ approach. That is to say, the Nordenfelt doctrine does not allow any opportunity to partially enforce or judicially rewrite non-compete clauses. Rather, emphasis is placed on the employers’ responsibility to draft the clause in reasonable terms; if they fail to do so the court will not ‘save their bacon’. The extent to which this approach, although beneficial, is adequate to protect the public interest is often debated and ultimately shapes this Submission.

25. It is sometimes argued that the presumption against enforceability wrongly allows parties to deviate from a contractual term that they freely entered into, interfering with the fundamental tenet of freedom of contract and that *pacta sunt servanda*. While this is true to some extent, it ignores the unequal bargaining power that exists during the drafting and negotiating of employment contracts. Since it also is common practice for employers to impose non-compete clauses on a ‘take-it-or-leave-it basis’, the impact of this line of reasoning has unsurprisingly been limited in the cases.

26. As suggested in the above section ‘INTRODUCTION AND POLICY ANGLE’, this Submission instead focuses on the need for greater protection of the public interest, that being society’s interest in a free and mobile labour market. This is particularly necessary given recent studies by the Australian Bureau of Statistics, finding that approximately 1 in 5 employers use non-compete clauses in their businesses. This proliferation in contemporary society demonstrates just how timely it is for Australia’s current approach to undergo significant reform.

27. Another aspect of the law that invokes a need for statutory reform is the contractual use of ‘cascading’ or ‘laddered’ non-compete clauses. Put simply, these clauses contain several variations of the non-compete terms, with each variation decreasing in severity. They are used by employers particularly to avoid the court’s ‘all-or-nothing approach’ by reliance on the rules of severance that exist in contract law generally. Although there is some debate about the acceptance of cascading non-compete clauses, the courts have often severed unreasonable parts of such clauses and enforced those parts that are otherwise reasonable. The availability to the court of severance in this context, goes back to the old decision in *Attwood v Lamont*. Since employers tend to game this ability in their favour, we see the present state of the law as disadvantageous in this regard. At [32] below, this Submission addresses recent beneficial, but ultimately insufficient, evolution in relation to severance.

28. Beyond this broad Australian common law context, it must be noted that New South Wales (‘NSW’) takes a distinct approach to non-compete clauses. The Nordenfelt doctrine is there subject to the relevant provisions in the *Restraints of Trade Act 1976 No 67 (NSW)* (‘RSA’). A material effect of this statute is that it allows the courts to enforce non-compete clauses to the extent that they are reasonable. This judicial power to construe broad – and otherwise unenforceable – clauses as narrowly as required to make them reasonable, is concerning as it results in employer overreach with chilling effects on employee mobility. This being said, it is clear that the NSW approach does not provide beneficial guidance for statutory reform, but rather reinforces the need for a stricter, and also nationally consistent, framework.

29. Noting the abovementioned context, including the history and conflicting positions that persist in Australia’s approach to non-compete clauses, our Submission further addresses some recent developments that further inform our recommendations for reform.

## **RECENT LEGAL DEVELOPMENTS**

‘Genuine attempt’ and unreasonable delay

30. One of the most commonly cited cases in recent times is *Just Group Ltd v Peck*, which was decided before the Victorian Court of Appeal. Just Group Ltd sought to enforce its non-compete clause against an employee, Nicole Peck, after she began working at a rival retailer, Cotton On. This clause essentially prevented Peck from working with 50 retailers (including Cotton On) anywhere in Australia and New Zealand for a period of twelve to twenty-four months. At first instance and again on appeal, the courts recognised the employer's legitimate interest in protecting confidential information, but nonetheless held that the restraint provisions were too broad, and unreasonable.

31. The importance of this case rests with the court's discussion of severance in obiter dicta. This is because the Court of Appeal effectively modified the requirements that were established in *Attwood v Lamont*. Rather than requiring that it be established that the provision 'ought to be severed', it was noted that a non-compete clause must reflect 'a genuine attempt to establish reasonable protection for the legitimate interests of the employer'.

32. The court is here seeking to prevent employers from automatically and indiscriminately including overly broad and standardised non-compete clauses in employment contracts and then recruiting the court to undertake the proper drafting exercise. This exemplifies the court's concern with the way non-compete clauses negatively impact employees themselves and the broader public interest. Although the 'genuine attempt' requirement was only established in obiter and is limited to cascading non-compete clauses, the modification still reflects a positive development of the common law that limits employers' bargaining options. *Just Group Ltd v Peck* displays a tendency towards reform that requires a stricter approach to non-compete clauses.

33. Another key recent case is *Scyne Advisory Business Services Pty Ltd v Heaney* in NSW. For context, the employee in this case, Ms Heaney, was subject to a twelve-month non-compete clause. She resigned and subsequently took gardening leave upon request but refused to make an undertaking that she would not act in breach of her non-compete clause. Three months after giving notice of her resignation, Ms Heaney began work at a competing company, and the old employer sought an injunction.

34. Justice Parker noted that he was 'inclined to grant relief' on the circumstances before him but ultimately held that 'it would be most unreasonable now to restrain Ms Heaney... because [her old employer] has now belatedly discovered the urgency of its case'. In other words, the court refused to grant interlocutory relief because of the old employer's three-month delay from the date they became aware of a potential breach.

35. Beyond providing important precedent for factors impacting the discretion to grant injunctive relief, this case is telling because of the court's reticence towards the enforceability of non-compete clauses. In avoiding a firm decision on the legitimacy of the employer's case, it seems the court was reluctant to offend against public policy favouring employee mobility, particularly where the employee had already taken their skills and talents elsewhere.

36. These developments in the common law demonstrate that courts are open to new ways of achieving protection for employee mobility and a free labour market. It demonstrates their vigilance in the face of the firmly established and inescapable precedent that allows some 'reasonable' restraints to stand. This supports our Submission for reform as it demonstrates that the proposed changes are not contrary to the spirit of the law and its incremental evolution but are rather in sympathy with them and with broader public needs.

#### *Developments in New South Wales*

37. As explained in the BASIC LEGAL PRINCIPLES section (above), NSW takes a distinct approach which differs from every other jurisdiction in Australia. By virtue of the NSW courts being able to apply the RSA and read down non-compete clauses, it is arguable that the risk for

employers that adopt broad non-compete clauses in that jurisdiction has been reduced during and in the shadow of litigation. This begs an important question about the ability of employers to capitalize on the RSA.

38. This circumstance was recently examined in *Allied Express Transport Pty Ltd v Braim*. In this case, the applicability of the RSA was a key issue in relation to the enforceability of a restraint of trade clause against two defendants, namely, Mr Braim and South Pacific Laundry Pty Ltd ('SPL'). The employer argued that the RSA was applicable because the contract was expressly 'governed by the laws of [NSW]'. On the other hand, the defendants argued that the laws of Victoria were rather applicable because that is where Mr Braim resided, and SPL carried on business.

39. Although Justice Williams found that there was no breach or apprehended breach of the restraint clause, it was held in obiter that the RSA would have applied. In his reasoning, his Honour noted that the court should not decline 'to give effect to the parties' choice of governing law for the employment contract'.

40. This case represents an interesting – and rather ambiguous – development of the law. Whereas Australian courts have not historically hesitated to downplay freedom of contract for the benefit of the public interest, Justice Williams' comments seem to do just this. Although there are good policy reasons to uphold the contractual intentions and autonomy of parties, the potential consequences in relation to a strategic use of the RSA cannot be ignored. In other words, this obiter risks incentivising employers to manipulate the governing law of a contract so that they may craft broad non-compete clauses that a court will read down in the unlikely event of being challenged by an employee. We have already noted the chilling effect this will have on employee mobility.

41. Whether this interpretation is accepted or not, the inconsistency that exists between NSW and other states is made particularly clear in *Allied Express Transport Pty Ltd v Braim*. To the extent that this creates a room for dispute and argumentation in itself, and further complicates the applicable rules on non-compete clauses, it is clear that the unified federal framework we argue for below is warranted, even necessary.

42. In contrast to such an expansive application of the RSA, in *McMurphy v Employsure Pty Ltd* and *Kumaran v Employsure Pty Ltd*, the NSW Court of Appeal adopted a more conservative attitude. In this case, the court refused to read down a nine-month restraint of its own motion, despite lesser durations being available in the cascading structure of the non-compete clause in question. Since the employer did not make alternative Submissions for a lesser restraint to be enforced, pursuant to s 4(1) of the RSA, the court simply held that the nine-month term was unenforceable. According to the court, the onus of persuading it to read down a non-compete clause rests on the party seeking to enforce it.

43. This decision again proves the court's reluctance to enforce non-compete clauses - even in the face of a statute that permits the reading down of such restraints. The court acted in harmony with the judicial tendency to protect the public interest over the putative interests of the employer. In this regard we point to what was said in [36] above: common law decision-making reflects persistent judicial reservations about non-compete clauses and their adverse effects. A more restrictive regulatory approach would therefore not be 'incoherent' or constitute a sudden reversal compared to judicial attitudes and decision making.

44. The NSW cases also demonstrate significant variability in the presence of a statute like the RSA. We reiterate here that the ensuing uncertainty in NSW also plays in favour of better resourced employers, perhaps even more so than in common law states as they can hope that a judge will rewrite an excessive restraint.

## **DEFINING THE TARGET OF REFORM**

45. Before canvassing various options for reform, we define ‘non-compete clauses’. We use this term instead of ‘restraints of trade’. We are referring only to non-compete clauses in employment or work contracts and labour markets, not other non-competes. It is well established that non-compete clauses in employment are a separate class that demands far more restrictive legal oversight than for instance non-compete clauses connected to transfers of goodwill.

46. It is self-evident that any measure or statutory intervention should extend to both *de iure* and *de facto* non-compete clauses, defining the latter by reference to substance and not form. We should have regard to the effect and not the nomenclature of the target clauses in employment contracts. We therefore adopt a definition of an employment non-compete as ‘any contractual term that expressly restricts or limits the right or freedom of a worker to be employed by or undertake remunerated work for another person or for the worker’s own account in any capacity’ (below referred to as a ‘restrictive term’). What is traditionally known and recognised as a ‘non-compete clause’ or a ‘restraint clause’ or something similar clearly falls under this definition. But the definition is also effective to apply to a confidentiality clause that is expressed in such broad terms as to amount to a non-compete, and to non-solicitation clauses with the same practical effect.

47. Our definition also extends protection against non-compete clauses to participants in the ‘gig economy’, even if their contractual relationship to the party paying for their work is not strictly or legally speaking an employment relationship, but a contractor relationship. They would be persons that ‘undertake remunerated work for another person’, with person here being defined as a natural or corporate person. Employees that set up their own business post-termination are also covered as they either work for ‘another person’ in the form of a company they have established, or for their ‘own account’. In other words, a non-compete that restricts an employee from performing work for another as a contractor would also be covered.

48. We include the terms ‘expressly restricts’ so that terms that define duties of an employee during the term of employment, or the implied or express duty of fidelity, cannot be construed as ‘restrictive terms’. Our definition is not intended to apply to work undertaken for others during the currency of the contract that purports to impose the restraint by the operation of one of its terms.

## **OPTIONS FOR REFORM AND EVALUATION OF THOSE OPTIONS**

49. The case for reform of the law on employment non-compete clauses, including in Australia, has been sufficiently made out (see above [11]). We already argued for reform more than a decade ago on the basis of our findings in the ARC funded research project, and van Caenegem has consistently supported such reforms in various writings which are in line with what other scholars have argued in terms of the benefits of employee mobility.

50. The more recent legal developments in the caselaw as described have not impacted our views on this topic or led us to revise our position. We argue that the judges applying the common law are both expressly and implicitly aligned with a policy that deters non-compete clauses. We also argue that a national approach is required to minimise gaming of jurisdictional issues and reduce complexity as much as is possible.

51. Our focus in this Submission is therefore primarily on analysing the spectrum of reform options and advancing a concrete proposal for reform. We note that in the United States (‘US’) the preferred option is a complete ban on non-compete clauses, while in the United Kingdom the preferred option is a three-month maximum term limit for any non-compete.



52. *We are conscious of the fact that any regulatory intervention, although in our view well aligned with the present attitude of the judges, is still quite a departure as the common law has not previously been trammelled by regulation in any way. At this point, except for NSW (but in an incidental manner there), non-compete clauses in employment are entirely governed by the common law in every state of Australia .*

53. *We reiterate that the starting point of the common law is that any contractual restraint on competition per se is against public policy and unenforceable. However, a court can make a contrary order if it determines that the non-compete is reasonable to protect a recognised interest, in terms of time, geographical reach, and targeted activities.*

54. *We recognise that regulatory intervention will potentially cause some incoherence, trigger gaming and circumvention, generate unintended consequences and possibly have perverse effects . We therefore favour a well-designed intervention that is as resistant as possible to such developments and is not overly prescriptive. We favour a solution that minimises transaction costs while effectively realising the policy goal of deterring encumbrment of mobility.*

55. *In our view, prescriptively regulating non-compete clauses has the potentially negative consequence of supporting their continuing prevalence, because it will result in a 'tick-a-box' approach. Prescribing the proper formation of non-compete agreements in detail also gives the impression of a regulatory imprimatur. Whereas, our view is that any prescription should deter their adoption and limit them to the narrow category of case where recognised interests so genuinely warrant their terms that the employer is willing to offer distinct and separate remuneration for them.*

56. *Below we consider some principal options and then advance our preferred option.*

#### *Option: Prohibition of non-compete clauses*

57. *Prohibition in the manner proposed in the US, is a very radical departure from the present, and longstanding situation, although perhaps less there than would be the case in Australia. A high-profile, real-life model of how prohibition can operate exists in California and some other states have trended in the same direction. No such developments have occurred here. Prohibition would obviously require more specific regulations concerning existing non-compete clauses and transition to the new regulatory environment.*

58. *Prohibition would interrupt a longstanding Australian practice concerning certain employees, certain industries and certain types of contracts of employment. However, we also acknowledge that the use of non-compete clauses has in recent times gone beyond the confines of those traditional realms both in this country and seemingly in other market economies such as the US and the UK. Prohibition would obviously stop this evolution in its tracks.*

59. *Prohibition does not alter or eradicate the underlying conditions and concerns that make non-compete clauses desirable tools for employers seeking to protect legitimate interests, in particular relating to trade secrets and training outlays. That employers often want nothing other than to throw roadblocks to competition in the path of departing employees does not mean they never have legitimate interests to protect. These interests will persist and in the face of prohibition employers will look for alternative ways to protect their perceived interests. Employers may therefore: rely more readily on breach of confidence (trade secrets) actions against ex-employees; rely on the Corporations Law for the same purpose; attempt to disguise what are effectively non-compete clauses; use garden leave; use non-poaching agreements with other employers; and turn to other as yet unknown and putatively undesirable practices.*

60. *The weak level of protection that the law affords to trade secrets, and evidentiary difficulties when an action for breach of confidence is brought against an ex-employee are one important reason why non-compete clauses are often preferred to NDAs or reliance on equity. Prohibiting these clauses might trigger more trade secrets cases and attempts by employers in aggregate to influence the relevant law in their favour. They might cause judges to become more sympathetic to such claims, as has to some degree happened in the US over the years.*

61. *We would also expect to see an increase in the number of claims brought by employers under the Corporations Act 2001 (Cth) for breaches of the various 'officer and employee' duties. For example, section 183 prohibits employees of a corporation from improperly using a company's information to gain an advantage for themselves or someone else or to cause detriment to the corporation.*

62. *Employers might also react by limiting the circulation of information within organisations, and by taking a more conservative attitude to providing free training and career development support for their employees. Greater limits on internal circulation of knowledge and information within organisations are well known to have adverse effects on innovation and economic development. This is one significant reason why the UK government has opted for a maximum term rather than prohibition of non-compete clauses.*

63. *We consider that the arguments made in the US concerning potential disincentives for general firm investment if non-compete clauses are prohibited are too speculative and general to carry much weight in the current debate.*

64. *Prohibition of non-competes requires more careful consideration of what amounts to a non-compete, and how to combat a variety of probably determined efforts to circumvent the prohibition. It would also require consideration of who to extend the prohibition to, for instance, workers in the 'gig economy' and how to achieve such an extension.*

#### *Option: Prescriptive regulation of non-compete clauses*

65. *Some jurisdictions already regulate non-compete clauses in more detail. This approach is particularly prevalent in civil law jurisdictions in Europe, and tends to go hand in hand with a requirement for separate consideration. Some other proposals would require a clear indication in advertisements that a job is subject to a non-compete; a condition that clauses only take effect after 6 months; the creation of a public register of company users of non-compete clauses; and annual review of non-compete clauses etc.*

66. *However, our view is that such prescriptive regulation of these clauses runs the risk of giving them the rule giver's imprimatur and making them more prevalent. Employers might be encouraged by the certainty that compliance with prescriptions brings, to include non-compete clauses more often. Most of these proposals would not have much direct deterrent effect or greatly affect the cost of imposing non-compete clauses. They would result in tick-a-box compliance.*

67. *This would go contrary to our policy conclusions that exactly favour further deterring the adoption of non-compete clauses in employment contracts. Our preference is for regulations that dissuade use of non-compete clauses, rather than regulations that aim to redress the bargaining imbalance in relation to them, by imposing certain detailed constraints on and surrounding the bargain. As indicated above, this is in part because non-compete clauses do not only negatively impact the personal interests of the employee, but also the public interest in maintaining a free market for labour in aggregate.*

68. *One possible more prescriptive approach favours prohibition but with a 'carve-out' for CEO level employees, or for employees with salary levels over a certain amount per annum. We*

*consider that this will trigger gaming or adjustments to firm practices in relation to remuneration and job descriptions. We are also not convinced that there is more persuasive policy justification for periods of exclusion of CEO level employees from the labour market than for lower paid employees. On one view the mobility of high-level employees is at least as important, if not more important than that of employees at lower salary levels or lower levels of skill and responsibility. In any case it would be difficult with any certainty or rational underpinning to select a particular salary level. Further, the effect of the amount set might be geographically random or disproportionate, and a rational and appropriate level would have to vary from industry to industry.*

69. *One suggestion is that separate legal advice be required for a valid restraint, that advice being provided to the employee by a lawyer independent of the employer. This also we consider a complex and potentially expensive option. On the other hand, it would also have a deterrent effect and would mitigate the inclusion of ‘boilerplate clauses’ in employment contracts that prove to be unenforceable.*

70. *Requiring distinct consideration or remuneration during the period of a non-compete does address the adverse impact a restraint period might have on a worker who cannot take the most remunerative employment otherwise available to them. If separately and properly remunerated, a non-compete becomes more of a burden for employers and would therefore become less prevalent. As it stands, the law and policy proceeds on the basis that consideration for a non-compete clause is absorbed or reflected in the other benefits an employee obtains. This is a highly abstract presumption, and it would be fair to say that the non-compete period is most often effectively uncompensated. Although an ex-employee is free to take employment and earning an income during the restraint period, just not of a kind covered by the non-compete, we do favour a requirement of separate and distinct compensation (see further below).*

#### *Option: A maximum term for non-compete clauses*

71. *We consider that a three-month maximum as proposed in the United Kingdom comes close to prohibition. This is because in most cases it would be ineffective at protecting legitimate employer interests; in case of conflict post-termination the three month term would be mostly consumed by disputation or litigation; any breach would often be detected only when a substantial time from termination has elapsed; and if violated such a short restraint is unlikely to trigger action from an employer engaging in a rational cost/benefit analysis concerning enforcement action. Three-month restraints would be largely pointless and at best an unhelpful complication.*

72. *As a free-standing measure, a three-month limit might also have the effect of encouraging adoption of restraints that are compliant on that aspect; just another term in a boilerplate provision. A three-month term is likely to be seen as justified because an employee immediately (‘from one day to the next’) starting work with a rival of the ex-employer is simply ‘beyond the pale’, whereas we view that ability exactly as critically important for competition.*

73. *We also consider that a one year maximum, or even a two-year maximum as exists in Germany for instance is too long, even if it would still be subject to the existing common law reasonableness standard. Setting such a maximum term would potentially encourage employers to adopt this term as a standard inclusion. In most industries there would be little justification in terms of protectable interests, for such a long restraint. A one-year restraint takes an employee out of their most efficient employment for a very long time. It denies society access to their optimal skills for a long period and disturbs normal patterns of acquisition of experience and learning in the employee’s preferred field of employment for too long.*

*Preferred option: a six-month term limit*

74. Our preferred option is to impose, by way of an Australia-wide statutory reform, an absolute and universal maximum six-month term limit on employment non-compete clauses. Importantly we would combine this with limited regulation, and every non-compete would remain subject to reasonableness review.

75. Justification for the six-month maximum term lies in part in what we say above about the disadvantages of a three-month term, and about the fact that we consider a twelve-month maximum term too long. We also rely on our arguments that the case for total prohibition is tempered by certain persuasive and significant policy concerns as canvassed above. A six-month term therefore represents a compromise, where we consider it a duration sufficient to protect the most genuine and legitimate interests of employers, and disincentivise them from placing restrictions on training and information sharing, but not so long as to have an overly deleterious impact on the private interests of the employee concerned and the aggregate public interest in a free, mobile, and competitive market for labour.

76. The six-month maximum term or any other lower term imposed by a contract of employment should still be subject to reasonableness review in the current manner. Separate and distinct remuneration for it should also be required. Below we additionally advocate for codification of the standards to be applied in such a review, based on the current common law position.

*Preferred option: additional rules*

77. The additional regulatory intervention we support is to require separate and discrete consideration (remuneration) for any period of restraint (up to the proposed statutory maximum of six months).

78. To be enforceable, such consideration must be agreed on at the time of engagement and be expressly reflected in a clause in the contract of employment. We do not consider that regulations should prescribe a minimum or set level of such consideration as is the norm in certain jurisdictions (eg 50% in Germany). Parties are free to negotiate the consideration which could be a percentage or fraction of salary for the term of the restraint or a lump sum or other form of payment.

79. Because the employee's agreement concerning the level of consideration would be required, the employer is motivated not to seek a non-compete (because a clear cost is attached to it) so that routine or boilerplate inclusion is deterred. It would also motivate employers to include only restraints that are properly adapted to the individual worker. Although still in a weaker bargaining position we believe the worker would be in a better position than currently to withhold their agreement unless on terms they genuinely find satisfactory.

80. We also propose that the level of remuneration be an additional factor relevant to the reasonableness evaluation, which would increase the level of risk for an employer seeking to include inadequate distinct consideration in the contract of employment.

81. We would also require the employer, when notice is given by either party, to notify the employee whether the non-compete clauses will be activated or not.

82. Further, we advocate for codification of the present law concerning illegality of non-compete clauses and the reasonableness exception. In particular: clear identification of protectable interests, the requirement of proper adaptation to the safeguarding of those interests, both in terms of time and area, and clear identification of restricted activities that accord with and do not extend beyond the actual duties undertaken by the employee.

83. We also advocate for protection of a new employer from liability for tortious interference with contractual relationships that bind their new or prospective employee. At present, if an employee subject to a non-compete seeks employment in a manner that is arguably in breach of their restraint clause, their intended or actual new employer is potentially liable for tortious interference if they encourage their new or intended employee to ignore the restraint they are under. If the new employer is protected from such liability, and for instance if they undertake to fund any challenge or litigation related to the restraint, there is a clear benefit. This should therefore be permissible because assistance from a new or intended employer would redress the common imbalance of resources between an ex-employer and a departed employee faced with threats of or actual litigation in relation to a putative breach of their non-compete.

84. Any non-compete agreement should remain subject to the existing common law reasonableness standards, although it might be apt that the presumption of invalidity be reversed as the non-compete would have to have been entered into in the manner described above. This is because the principle of freedom of contract, or to contract on certain terms, normally demands that parties adhere to their bargain. That is arguably even more the case where clear and distinct consideration is attached to a certain obligation. However, since this would weaken the employee's position we do not strongly advocate for it here.

85. Transitional provisions would obviously be required. We believe that the simplest solution is to allow existing arrangements to stand, subject as they are to judicial scrutiny. Any agreement or contractual term entered into or amended after the commencement date would be subject to the newly promulgated rules. In that manner the overwhelming majority of non-compete clauses would be subject to the new rules within a relatively short period.

#### *Arguments in favour of the preferred option, and its anticipated effects*

86. Our preferred option provides an employer who has genuine concerns about trade secrets and client connection, means to legally implement a non-compete. However, those means should only be available where separate remuneration distinct from any other form of benefit is specified in the contract of employment. An employer must also choose whether to activate the non-compete or not at the time of notice. The 'boilerplate problem' will be mitigated by these means as the employer would be less inclined to include standard terms in every employment agreement at the time of engagement. The number of non-compete agreements would be considerably reduced but the device would not be denied to employers who consider that there is a real requirement for such a restraint and to employees who are willing to entertain them in part because they are adequately remunerated.

87. Our proposal to codify the standard of reasonableness and retain its application prevents 'slippage' in the common law, gives a clear framework to those who will draft non-compete clauses, and recognises that a non-compete is the exception and not the rule. However, we propose that the adequacy of distinct and separate compensation for the non-compete clause, required under the mooted rules, be an additionally relevant factor in the reasonableness evaluation.

88. We advocate for the only protectable interests to be particularised trade secrets and direct and actual client connection. We do not agree that 'stability of the workforce' is a proper 'interest' that should be the subject of non-compete protection (more specifically a 'non-solicitation of staff clause'). In part this is because we consider that a current employee who encourages others to end their employment relationship so as to join a competing employer or embark on a new competing venture, is engaging in conduct that breaches their obligation of good faith and fidelity. If a departed employee engages with remaining employees after termination, then so be it: a 'staff connection clause' is nothing more than a direct protection from the kind of competition in the labour market from which no employer should be immune. It

*is not a different interest that deserves some opportunity for contractual safeguard, and we disagree with the characterisation of ‘staff connection’ as some form of ‘goodwill’ and hence a proprietary asset. In any case such clauses are not really ‘non-compete’ clauses but something more limited analogous to non-solicitation of clients clauses and some NDAs.*

89. *So-called garden or gardening leave would not be ‘caught’ by our proposed rule, since it does not concern working for another employer or for the employee’s own account for a particular period. That complete prohibition would trigger more gardening leave situations is a possible and detrimental outcome, and that is one reason why we advocate for a six-month maximum to be retained, subject to consideration. Our recommendation would result in a choice for employer and employee: either a garden leave-type protection with a longer than usual notice period and a largely inactive employee still enjoying their undiminished entitlements; or a limited term non-compete in return for a negotiated amount and subject to an express choice to enforce it at the end of the employment relationship. We consider this an appropriate choice for an employer to have and to make in the light of their specific circumstances, expectations and requirements.*

90. *We consider that non-poaching agreements are a matter for competition law and do not address them here other than to say that they are not to be favoured. We do not address non-solicitation of client clauses or confidentiality clauses unless they are so drafted to fall within our definition of non-compete clauses (see above).*

## **PROPOSED [DRAFT] PROVISIONS.**

*Note: These proposed provisions are only intended to state clearly what the key elements of our preferred option are.*

### **Section 1 Rule**

*Any express contractual clause in a contract of employment that restricts or limits the right or freedom of a worker to be employed by or undertake remunerated work for another person or for the worker’s own account (‘restrictive term’) in any capacity is unenforceable.*

### **Section 2 Exceptions**

1.1 *A restrictive term which is operative for a period of six months from the date of termination of a contract of employment or less is binding in exception to the Rule, if the restrictive term is reasonable in accordance with the standard of subsection 1.2.*

1.2 *A restrictive term is reasonable if it does not extend in terms of geographical extent, duration, and scope of activities beyond what is necessary to protect an interest of the employer recognised in subsection 1.3 (‘recognised interests’).*

1.3 *The recognised interests are: a. the employer’s particularised confidential information; and/or b. the connection between the clients or customers of the employer and the employee.*

1.4 *A court must declare a restrictive term unenforceable if it is not reasonable.*

1.5 *A court cannot sever, vary or alter a restrictive term but must declare it either enforceable or unenforceable.*

1.6 *A court may declare that a restrictive term is not enforceable because of vagueness or uncertainty and must declare a restrictive term that includes alternatives unenforceable.*

*1.7 A restrictive term is not enforceable in the absence of separate and distinct remuneration specified in the contract of employment, or if the employer fails to pay the separate and distinct remuneration in the terms so agreed.*

### *Section 3 Liability for Interference*

*Giving advice or assistance of any kind to a party subject to a restrictive term does not amount to tortious interference with a contractual agreement in and of itself.*

*NOTE: These draft provisions are provided to summarise and clarify the position taken; the specific language is obviously a matter for expert statutory draftspersons.*