



MDJ LAW – LEGAL UPDATE APRIL 2007

In this update we discuss recent developments on restraints of trade in employment agreements and the test of “justification” in respect of an employer’s actions.

RESTRAINTS OF TRADE

The recently reported case of an ex-Fuel Espresso barista, Mr Hsieh, highlights the importance for employers of including restraints of trade in a timely manner.

In *Fuel Espresso Ltd v Victor Hsieh (WC5/07)*, the Employment Court was asked to review the restraint of trade clause in Mr Hsieh’s employment agreement after Fuel alleged he had set up a coffee cart in breach of that clause. The Court considered the fact Mr Hsieh was paid a basic wage for a café employee slightly above the minimum wage. Further, there was no mention in his employment agreement that he was paid any more than anybody else at Fuel that might have amounted to consideration for the restraint of trade (i.e. a payment or other benefit provided to Mr Hsieh in exchange for his agreement to a restraint of trade). The Court held that the absence of consideration for the clause meant that Fuel was unable to rely on it.

However, the Court of Appeal subsequently held that Fuel was able to rely on the restraint of trade clause, as it was in place from the commencement of Mr Hsieh’s employment and so there was no need for separate consideration for its inclusion (separate consideration would be required if the parties agreed to the restraint *after* Mr Hsieh was first employed). The Court also noted that in such circumstances there is no need to evaluate how adequate (or otherwise) the consideration for the restraint is.

What does this case mean for you? Where a restraint of trade clause has been included, the timing of its inclusion will determine what is required. Where the restraint is to be included from the outset, there is no requirement to assess consideration separately, i.e. the employer does not need to be able to point to an express amount of dollars as consideration for the restraint of trade. However, we do still suggest that in some circumstances the employment agreement expressly refers to consideration for the restraint in some manner, for example, by stating that the wages or salary paid includes consideration for that restraint.

Conversely, where the employer wishes to add a restraint provision after the employment has commenced, there will need to be separate consideration. This could either be by way of an identifiable additional sum to be paid to the employee expressly as consideration, or via stating in the amended employment agreement that, for example, the increase in the wages or salary payable under that agreement includes consideration for the restraint.

As employment specialists, we are happy to advise you on how best to address these issues and on such clauses.

JUSTIFICATION FOR DISMISSAL OR OTHER ACTION

Section 103A of the Employment Relations Act 2000 ("the ERA") came into force on 1 December 2004. It provides the test that justification "*must be determined, on an objective basis, by considering whether the employer's actions, and how the employer acted, were what a fair and reasonable employer would have done in all the circumstances at the time the dismissal or action occurred*".

This replaced the previous test of what a fair and reasonable employer "*could*" do. The first Employment Court decision in relation to this section was Air New Zealand v. Hudson 30/5/06 (nearly 18 months after the amendment) a case of dismissal for alleged misconduct. The Court has confirmed in Simpsons Farms Ltd v. Aberhart 14/9/06 that the new test applies to all dismissals (including redundancy) and disadvantage claims. The test has now been clarified further in X v. Auckland District Health Board 23/2/07.

Summary of Some Key Points from the cases:

- The test is now what a fair and reasonable employer would do, not what they could do.
- The Authority or Court's inquiry involves two separate considerations: first, what the employer did, and, secondly, how the employer acted (during each step of the process followed).
- The Court or Authority must be satisfied that what the employer did and how the employer acted were what a fair and reasonable employer would have done in all the circumstances at the time: the standards of a hypothetical employer are applied to the conduct of the actual employer.
- In doing so the Court or Authority must use its knowledge of employment relations to determine whether what the employer did met those standards.
- The Employer must provide all relevant information to the employee.
- Acting other than in good faith (as defined following the 2004 amendments to the ERA) will militate against a finding of justification.
- Questions of justification must be judged at the time the action occurred. Therefore, if relevant events later come to light or the employer may consider that there were other grounds based on things known at the time, these cannot affect considerations of justification. They may, however, be relevant to remedies.

Section 103A will remain difficult to apply until further cases are decided by the Courts. Each case needs to be assessed on its facts, and therefore specific advice before acting is desirable.

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