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Hong Kong employment law update – non-compete restrictive covenants



In *Manulife Financial Asia Limited* ("P") v *Kenneth Joseph Rappold* ("D1"), *Prudential Services Limited* ("D2") and *Prudential Public Limited Company* ("D3"), the High Court considered D1's move to join D2 as its Chief Transformation Officer ("CTO") in April 2024 and rejected P's attempt to obtain an interim-interim injunction¹ concerning a 12-month global non-compete covenant ("Covenant").

How the Court reached its decision and what was said about the Covenant is of particular relevance to employers and human resources teams. We explain why below.

Facts

P is an insurance company operating in 12 markets in Asia.

D2's owner is D3. D2 is a competitor of P. D1 was P's Chief Financial Officer for Asia from early 2018 to 31 October 2023. His employment contract included the Covenant which stated:

¹ Interim-interim relief is a urgent temporary stop-gap measure awarded when the Court has to do practical justice on the balance of fairness even though it may not have sufficient time to consider the matter fully.

'... You agree that you will not at any time during your employment with the Company and for a period of 12 months ... be employed in a Similar Capacity by a Competitor ... without ... prior written consent.

"Similar Capacity" means the same or similar position, or having the same or similar responsibilities, accountabilities and duties that you have or had in connection with your employment

A "Competitor" is any person or company engaged in or planning to engage in business that: (1) is the same or similar to the business of, in whole or in part, to those of the Company or Manulife and its affiliates and subsidiaries, including without limitation providing financial protection, wealth management, asset management and other financial products and services; or (2) involves the selling or offering of products, processes, programs, or services that are the same or similar, in whole or in part, to those of the Company or Manulife and its affiliates and subsidiaries or that were under active consideration by the Company or Manulife and its affiliates and subsidiaries during your employment with the Company'

D1 left P for a career change. On learning D2 and D3 planned to recruit a CTO and being an opportunity which was too good to miss, D1 applied for and then secured the job. Thereafter, in late January 2024, D1 informed P he intended to join D2. He also sought an acknowledgment that he could commence his employment without being in breach of the Covenant.

Discussions with P followed during which D1 stated he: (i) thought the Covenant was unenforceable; (ii) had none of P's property; (iii) had no intention to use P's information he may have in his head; and (iv) would in any event undertake that he will not use or disclose any of P's confidential information.

The undertaking referred to in (iv) above was offered in exchange for P agreeing that D1 could start employment without restraint but no agreement was reached between the parties. Shortly before D1's start date of 2 April 2024 proceedings were commenced against him where an injunction preventing him from taking up his employment as D2's CTO was sought. In response, D1 went on unpaid leave and his start date was delayed to 22 April 2024.

Principles

Non-compete covenants in employment contracts seeking to restrict employees from working for a competitor are not enforceable unless the employer can show they:

- (i) Are reasonable in the interests of the parties and justice; and
- (ii) Are no wider than is reasonably necessary for the protection of the employer's legitimate business interests.

The greater the duration of the restrictive covenant or the wider its geographical scope, the more difficult it will be to show it was reasonable. The time for ascertaining the reasonableness of a non-compete covenant is the time that the employment contract containing the restriction was entered into, not the time of the dispute.

Issues

With the Covenant expiring on 31 October 2024 before any trial could be held, when considering the injunction the Court would accordingly pay greater regard to P's prospects of success taking whatever course appeared to carry a

lower risk of injustice if it should turn out that it was wrong. In this regard the Court stated there would be injustice to D1 if it found that there was not a serious issue to be tried² about the Covenant.

Finding

On the evidence before it the Court found P had not demonstrated it had reasonably good prospects to show the Covenant would be enforceable.

Worldwide Effect

With no geographical limits the Covenant prohibited D1 from being employed anywhere by any person coming within the Covenant's definition of a '*Competitor*'. The lack of such a limit in a non-compete clause was regarded as a remarkable feature needing full justification and without such restraints would be held to be far too wide to be enforceable.

To tackle this issue P blue-pencilled³ certain phrases in the Covenant⁴ to attempt to limit its scope to Asia but this approach was rejected because the phrases concerned the nature of the position or job duties of D1 not the locations they were being done in. The Court stated it should not be redrafting restrictive covenants and if P wanted the Covenant to contain any geographical restrictions they should have expressly provided for them. To read any geographical limit into the Covenant after the blue pencil deletions would be contrary to ordinary principles of contractual interpretation.

Accordingly with the Covenant being a worldwide restriction, P therefore needed to show it was reasonable or necessary to protect its legitimate business interests however the only justification P raised was that during his employment D1 knew confidential information belonging to P. But D1 was only responsible for P's affairs in 12 markets in Asia and therefore any confidential information D1 had access to would be restricted to these markets. The need to preserve confidential information in this instance could not justify a global restriction prohibiting D1 from being employed in countries where P did not operate. This all meant that the Covenant went further than necessary for the protection of the P's legitimate business interests.

12-Month Restriction

In order to justify the 12-month restriction, P's evidence gave examples of confidential information which D1 had access during his employment concerning P's strategies and new products. But the evidence failed to: (i) address the confidential information's shelf life or explain how it had a life cycle of 12 months; or (ii) show how the confidential information could be used during the 12 months to the material detriment of P's businesses.

Both (i) and (ii) were needed to properly assess whether the 12 month duration of the Covenant was reasonable and necessary.

² The serious issue to be tried phrase: (i) comes from the well-known American Cyanamid test applied by the Courts to decide if an interim/pre-trial injunction should be granted; and (ii) means there needs to be a good and arguable case on its merits.

³ A legal *doctrine* through which Courts may strike out those aspects of a contract which would make it unenforceable while keeping the remainder so that the covenant could survive.

⁴ Deleted were the references to '*Manulife*' in the definition of '*Similar Capacity*' and the reference to '*Manulife and its affiliates and subsidiaries*' from the definition of '*Competitor*'.

Confidentiality Terms In D1's Employment Contract

P also submitted that the confidentiality terms of D1's employment contract were not sufficient to protect P because it was difficult to police the terms and/or prove whether certain information may or may not be confidential.

The Court however stated that it was incumbent on P to precisely identify the items of its confidential information which would require a restrictive covenant and could not be properly protected by any confidentiality terms in the employment contract. Here P had not precisely identified those items of confidential information which could not be properly protected.

Timeframe

D1 had stated that the Covenant applied to all work he had done in the 5 years of his employment by P because it had no limit to its timeframe. This was counterproductive to P's ability to enforce the Covenant because restrictions in respect of activities in which an employee had no recent involvement would often be regarded as unreasonable.

Detriment To Parties

The Court accepted and could not ignore the risk that any injunction imposed on D1 may well cause him irreparable harm in that he might lose the opportunity to join D2 as its CTO, a too good to miss opportunity. D2 had suggested it could not wait for D1 until October to fill the strategic role. The risks of the job offer being withdrawn were the Court found not fanciful.

As regards to the prejudice suffered by P, if there was an injunction this was premised on D1 retaining in his mind confidential information belonging to P that he would divulge D2 and D3. But there was no indication from the evidence that D1 would do that when he had expressly acknowledged that he continues to be bound by the confidentiality terms in his employment contract and had even offered to provide a Confidentiality Undertaking. In the circumstances, no breach of confidence by D1 was therefore likely.

Conclusion

The Court's views on the lack of any prospects of P succeeding in establishing that the Covenant was enforceable at trial meant that the balance of convenience was against granting any injunctive relief: which was the course that carried a lower risk of injustice if it should turn out that it was wrong.

The case is another reminder how difficult it can be for an ex-employer to enforce a non-compete restriction. Parties seeking to do so need to be mindful about evidential burdens that they are under to justify the scope and length of a particular restriction.

Here D1 offered to give a Confidentiality Undertaking which the Court held would have the force of a Court order and result in serious consequences including contempt of Court and committal proceedings on a breach. On the facts, the Court felt that this provided P with sufficient protection.

This article was written by Ian Childs the practice group leader of the commercial litigation team in Hong Kong.

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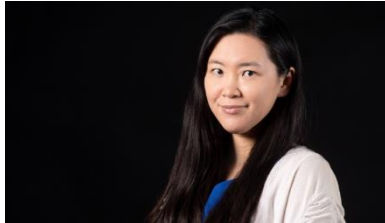


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