

ARA SUBMISSION

WORKER NON-COMPETE CLAUSES AND OTHER RESTRAINTS

MAY 2024

EXECUTIVE SUMMARY

The Australian Retailers Association (ARA) welcomes the opportunity to make a submission to Treasury in response to its issues paper in relation to worker non-compete clauses and other restraints.

The ARA is the oldest, largest and most diverse national retail body, representing a \$420 billion sector that employs 1.4 million Australians – making retail the largest private sector employer in the country.

As Australia's peak retail body, representing more than 120,000 retail shop fronts and online stores, the ARA represents the full spectrum of Australian retail, from our largest national and international retailers to our small and medium sized members, who make up 95% of our membership. Our members operate in all states and across all categories - from food to fashion, hairdressing to hardware, and everything in between.

Treasury's Competition Review Taskforce has released an issues paper and called for interested parties to make submissions in response to 19 questions outlined in the paper in relation to non-compete and other restraint of trade agreements between businesses and workers and, no-poach and wage-fixing agreements between businesses.¹

In its response to this issues paper, the ARA affirms the importance of non-compete clauses and other restraints in protecting businesses from the risk of harm that can result from a previous employee misusing sensitive business information, circulating intellectual property or otherwise conducting themselves in an unethical manner.

However, the ARA understands the importance of balancing both employer and employee interests in these considerations and, for this reason, present the following recommendations, if reform was deemed necessary.

RECOMMENDATIONS

The ARA has adopted a principles-based approach to reply to the questions contained within the issues paper, which have informed the following recommendations.

These recommendations are made to address the balance between protection of sensitive business information and worker mobility, enabling employers and employees to better understand the operation of restraints and promote the efficient allocation of labour.

In making these recommendations, we observe that it is unlikely the Australian Government would seek to completely override the common law and wrongfully take established power away from individual employers.

¹ Treasury | Worker non-compete clauses and other restraints | Treasury.gov.au

1. Further research should be conducted on the importance, effects and impacts of worker restraint clauses to better inform policy decisions, ensuring that policy decisions are wholly evidence-based.
2. Additional investigation should be undertaken into how frequently employers endeavour to enforce these provisions and the value of deterring behaviour before it has occurred.
3. The consideration of all the elements, including the importance of these provisions as protections for employers, must be considered within the review.
4. The operation and enforceability of these restraints must be preserved but, if further regulation is to be adopted, the ARA recommends that:
 - a) Post-employment restraints to be applicable to individuals occupying senior positions or those who, by virtue of their roles, have access to client data, trade secrets, business strategies or other sensitive or confidential business information.
 - b) Post-employment restraints to have a 12-month maximum period of enforceability.
 - c) Any further future regulation to post-employment restraints to be limited.
 - d) A two-year transitional period must be observed, if policy changes to worker non-compete and other restraint clauses were enacted, without retrospective application.
 - e) No-poach and wage fixing agreements to be preserved within franchise agreements where there is a reasonable need to prevent workforce insecurity or mitigate skill-shortages.
 - f) Further education to be made available to employers and employees as to the operation, useability, and enforceability of non-compete and other worker restraints.
 - g) If codification of the common law principles was sought in legislation, decision-makers should prefer that the common law principles are wholly adopted in legislation, in no way should the legislation differ, vary, or change the original legal principles.
 - h) If solely additional regulation of worker non-competes is required, this should not unnecessarily extend to other business protection mechanisms that do not unreasonably interfere with job mobility.

PRINCIPLES

As noted, these recommendations are informed by the following principles, which reflect the importance of businesses being able to protect legitimate interests, current effective legislative parameters on restraint clauses within employment contracts, insights as to the enforcement and useability of these provisions and the reality that there is limited empirical data available on their use and impact.

PRINCIPLE 1: THE MERITS OF RESTRAINTS WITHIN EMPLOYMENT CONTRACTS

Worker non-compete clauses

Contractual non-compete clauses preserve the legitimate interests of businesses by ensuring that an employee's insider knowledge into the workings of their employer's business cannot be leveraged for a competitor or to establish a competitive business.

There are several justifications that support the need for non-compete clauses within employment contracts and the preservation of this legal principle.

First, the restraints protect the intellectual property of a business from being exposed, used and copied by a competitor. Second, for businesses with commercially sensitive information, it prevents an employee from sharing this information with a competitor or establishing a competing business. Third, the restraint can prevent an employee from poaching clients or other employers of the employer for a competitor.

Fourth, and arguably, most importantly, this restraint prevents businesses from being adversely impacted economically, reputationally, and operationally, by a decision by an employee or previous employee, to share trade secrets, confidential information or privileged information with other competitors in the market.

The common law has long accepted the enforceability of such restraints, where reasonably necessary, because of these considerations and the fact that businesses also have legitimate interests requiring protection.

Non-solicitation clauses

As noted by the Issues paper, a valid non-solicitation clause can restrict a former employee from soliciting a former businesses' clients, customers, co-workers, and other business contacts.²

This restraint operates to ensure employers can manage the real risk that an employee could choose to take customers, co-workers or other business contacts with them upon the cessation of their employment with their employer. In doing so, without adequate protections, a business could be detrimentally impacted through a reduction in profit, reputation, and even operational capacity. The existence of this risk has been proven over time, as employers face former employees soliciting the business of valued clients.³

Non-solicitation clauses, similar to non-compete clauses, are not easily or readily enforceable. In assessing the lawfulness of these contract provisions, regard will be had to a myriad of factors including what the solicitation involved, whether the employee was in a position of trust and confidence, and whether there was a risk that the client may actually be solicited.⁴ These restraints typically are only reasonably enforceable for a 12-month period.⁵

These clauses are also fundamentally important in mitigating skills shortages as former employees can be restricted from approaching and poaching former colleagues. In certain industries and geographies (for example rural and remote locations) where there is a limitation on skilled workers available, these contractual prohibitions prevent 'staff-stealing' in roles that cannot be easily filled, thus preserving the sustainability of the workforce.

It cannot be assumed that these restraints are enforceable and thereby, can restrain conduct or individual freedoms in every instance.⁶ These restraints are subject to an assessment of all the relevant legal elements including whether the restraint is reasonably necessary and solicitation actually took place.⁷ Simultaneously, the purpose of non-solicitation clauses is to protect businesses from a real risk of undue harm and for this reason, they should be preserved.

² Treasury Competition Review Issues paper | Worker non-compete clauses and other restraints | Treasury.gov.au

³ See *Planet Fitness Pty Ltd v Brooke & Dunlap & Drs* [2012]

⁴ *Entello Pty Ltd v Firooztash* [2016] QDC 050

⁵ *AGA Assistance Australia Pty Ltd v Tokody* [2012] QSC 176.

⁶ See *Rushleigh Services Pty Ltd v Quarry Mining & Construction Equipment Pty Ltd* [2011] NSWSC 382; *Harrison v Schipp* [1975] 2

⁷ *Australian Clinical Labs Pty Ltd v Glew* [2019] FCAFC 124

Non-disclosure clauses

Non-disclosure clauses (NDC) in employment contracts seek to protect a business against the sharing of confidential information by an employee or former employee. This ensures that company trade secrets, financial information or customer details, another other sensitive data, are kept confidential.

These restraints safeguard business information-based assets from being disclosed to competitors or individuals outside the organisation. This also ensures that unique processes, intellectual property, or sensitive client information that a company owns, or stores is not circulated. This preserves a competitive advantage for the business, prevents intellectual property being copied and preserves client trust.

Without these restraints in employment contracts, client data could be misused, the business reputation impaired and intellectual property of the company stolen. The merits of these restraints is further emphasised by the fact the Australian Government often uses these provisions in the course of employment with their own APS staff to protect the misuse of public data.

At common law, obligations of confidence can arise in contract and equity by way of express terms in a contract or implication.⁸ While this is evidence of the existence of the duty of confidentiality in other forms, this common law element is not sufficient to solely protect the unauthorised disclosure of information⁹ the way that non-disclosure clauses can.

While other protections exist against the improper use of information by an employee or former employer, NDC's are a more effective protection. The Corporations Act 2001 (*Cth*) s183 can offer protections against the improper use of information by employees in the pursuit of gaining an advantage for themselves or another, or for the intended purpose of causing a detriment to a person.

However, many times over, employees are not aware of this obligation, and therefore, it is difficult to prevent this behaviour from occurring. Secondly, unlike a contractual term such as an NDC, the legal elements may be difficult to prove and by the time, an employer could obtain a remedy, commercially sensitive and confidential information would have already been circulated, and the corresponding impact to businesses, sustained.

These clauses cannot be construed to easily impact worker mobility or the creation of a new business. The obligation typically exists to protect the sharing of privileged information. While perhaps the argument can be made this could potentially limit the information an employee can circulate this is often within narrow limits, for a defined purpose and prescribed time.

No-poach agreements

The purpose of a no-poach agreement between businesses is to deter one business poaching another's workforce. This agreement prevents businesses, that may have difficulties hiring or retaining staff for certain roles, within certain industries or at certain times of the year, from being adversely affected by staff shortages.

For example, in rural locations, whereby the local labour market can be more limited, these agreements work to ensure the workforce remains stable. These agreements also ensure that a business's sensitive information or intellectual property is not shared with competitors.

⁸ Australian Law Reform Commission | Obligations of confidence | ALRC

⁹ Australian Law Reform Commission | Obligations of confidence | ALRC

Another important consideration, relative to their use, is the fact that such covenants prevent staff turnover in industries faced with constant workforce insecurity, or skill-shortages in operationally essential roles.

As noted by the issues paper, these agreements can also protect businesses from incurring costs without the pay-off of being able to keep the staff they trained. In rural locations, within small businesses, or involving roles of a particular speciality, this is of particular importance.

As no-poach agreements are regulated under the common law restraints of trade doctrine, with the exception of New South Wales, these covenants are recognised as difficult to enforce. For this reason, the regulation of such agreements under competition law or for instance, the *Fair Work Act 2009 (Cth)*, would be unnecessary, cause greater complexity and not give regard for the reality that these covenants are already adequately regulated for.

Wage-fixing agreements

Wage fixing agreements are agreements between two businesses or more that set a cap on wages and/or employment conditions for employees.¹⁰ These agreements are often used to prevent staff turnover or mitigate skills shortages in businesses.

While there is the reality that these agreements can place a cap on the compensation available to employees, employee wages and entitlements can never fall below the law, regardless of agreement and therefore, an employee's entitlements must meet the minimums under the *Fair Work Act 2009 (Cth)* and modern awards. Another relevant consideration is the fact these agreements are still subject to the common law restraints of trade doctrine.

Within Australia, these employment contract terms are likely more practiced between franchises. The effect of which is that staff will not seek to change roles from one franchise to another, which is an important protection for businesses that share employees under service agreements.

For businesses in industries suffering skill shortages, or barriers to hiring staff, these agreements are important to protect the sustainability of the workforce. Relatedly, these agreements are often only used for employees of a certain classification, role or occupation, so for instance, were an employee to move to a different role or be promoted, the agreement would likely no longer apply. Moreover, these agreements only typically operate within a company that has franchises, or between a limited number of businesses.

PRINCIPLE 2:

REGULATION OF WORKER-NON COMPETE AND OTHER RESTRAINTS OF TRADE

As it currently stands, the law on worker non-compete clauses and other restraints safeguards employee interests by regulating their use by businesses to be for the purpose of protecting a legitimate business interest.

This regulation protects against the misuse of these provisions, ensuring their use is limited to that which is reasonably necessary; and courts have long identified the validity of these restraints to the extent they are not unreasonable or contrary to the other necessary legal elements.

However, these risks to business interests cannot be overstated.

¹⁰ Treasury Competition Review Issues paper | Worker non-compete clauses and other restraints | Treasury.gov.au

These restraints safeguard business reputation, sustainability and profitability and prevent a business from incurring any undue detriment resulting from a current or past employee's actions. These provisions provide employers with a mechanism for legal recourse only where a legitimate business interest is observed.

The common law restraint of trade doctrine recognises that 'worker restraints of trade are presumed to be against the public interest and therefore void and unenforceable unless they are reasonably necessary to protect the legitimate interest of the employer'.¹¹

The legal test for determining the validity of a restraint of trade clause is therefore as follows:

1. there must be a protectable legitimate interest, as not just any business interest will suffice and
2. the restraint must be reasonably necessary to protect those interests. As remarked by Lord Parker in *Herbest Morris Limited v Saxelby* worker restraints 'afford no more than adequate protection to the party in whose favour it is imposed'.

The consideration of public interest, as explored in *Buckley v Tutty (1971)*¹², is founded upon the understanding that a person should not unreasonably be prevented from earning a living in whichever way lawful, and the public should not be unreasonably deprived of the services of a person prepared to engage in employment.

These prohibitions on the lawfulness and enforceability of non-compete and other restraints of trade clauses firmly regard their use is only suitable when reasonably necessary to protect a legitimate interest. The scope of this common law legal protection is therefore rendered narrow, and consequently, it should be no surprise that on average across Australia only 33% of these restraints are upheld.¹³

In a recent case example, *Just Group Limited v Peck (2016)*,¹⁴ a non-solicitation clause was rendered unenforceable because the restraint would prevent an ex-employee from being able to engage in activity which was the 'same as or similar' to the work she undertook, and it would unreasonably preclude her from working for other businesses where the confidential information obtained in the course of employment was irrelevant. This is clear evidence that there are already sufficient safeguards to ensure that restraints are restricted to reasonable use.

In New South Wales, the *Restraints of Trade Act 1976 (NSW)* applies instead of the common law doctrine, presuming these restraints are valid to the extent they are not against public policy. However, while the presumption is different to the common law doctrine, the consideration of public policy is still prevalent. For this reason, consistent throughout Australia, the enforceability of such restraints presents challenges.

PRINCIPLE 3:

RESEARCH ON WORKER NON-COMPETE CLAUSES AND OTHER RESTRAINTS WITHIN AUSTRALIA

As noted by Treasury, research on non-compete clauses and other restraints is relatively limited within Australia. This presents challenges when it comes to assessing the actual impact, influence and enforceability of these provisions which, in turn, creates challenges for government making data-driven policy decisions.

The issues paper does present some data but the ability to rely upon this data, with confidence, is questionable.

¹¹ Treasury Competition Review Issues paper | Worker non-compete clauses and other restraints | Treasury.gov.au; *Herbert Morris Ltd v Saxelby* [1916] 1 AC 688

¹² *Buckley v Tutty (1971)* 125 CLR 353

¹³ University of Melbourne | Employment Restraints of Trade: An Empirical Study of Australian Court Judgments by Hui Chia, Ian Ramsay:

¹⁴ 264 IR 425

The issues paper¹⁵ cites a survey conducted by e61 Institute,¹⁶ which concluded that around 1 in 5 Australian workers are subject to a non-compete clause, spanning a diverse range of sectors from professional services to childcare workers and yoga instructors.

The research conducted by the e61 Institute surveyed 3,000 participants and of those surveyed, there was no clear empirical data on the duties undertaken by these individuals and/or the information that they had access to. For this reason, it would be wrong to assume that, from this data, 1 in 5 Australians are truly subject to these restraints without a greater understanding of the ins and outs of their roles, and their relationship to the business - factors which can influence the need for inclusion of restraints within employment contracts.

Additionally, there is a difference, which is not explored in the survey, between an employee believing they cannot share confidential business information post-employment and an actual restraint being included within their employment contract.

However, as the issues paper observes, the issue as to the enforceability of the provisions (whether they be real or perceived restraints) is unclear can restrict employee mobility or the creation of a new business. This would support the proposition that there should be greater clarity as to enforceability for both employers and employees, as per the ARA's recommendations outlined herein.

It must be noted, the importance of these restraints as a deterrent of unethical behaviour is valuable and should be preserved.

PRINCIPLE 4:
USEABILITY AND ENFORCEABILITY OF NON-COMPETE & OTHER RESTRAINTS

As noted above, there is limited data on the prevalence, use and impact of worker restraint clauses. For this reason, it is imperative for Treasury to consider the fact that these contractual provisions also have a useful role in deterring unethical behaviours from current or past employees that would otherwise harm a business.

While the law recognises reasonable restraints as the basis of a legitimate and important cause of action, in practice, an equally important function is to provide an employee with the full terms of their employment obligations, removing any ambiguity as to what conduct is inappropriate. An employee's duties, such as fidelity and good faith, can also be implied by common law, therefore, the inclusion of some of these elements in writing is crucial for an employee to understand them.

When speaking with retailers, we noted specifically that businesses would rarely seek to try and enforce restraints of trade in contracts. There are several reasons for this, including the fact that the law is complex, and it is therefore hard to determine whether a provision will be deemed enforceable. Another reason is that a single breach of a clause or multiple small breaches will not warrant the commencement of costly and uncertain legal proceedings.

Retailers have also reported to us, through discussions and consultations, that if a breach did occur, in many instances the employers first course of action would be to simply send a *cease-and-desist* type letter. In doing

¹⁵ Treasury Competition Review Issues paper | Worker non-compete clauses and other restraints | Treasury.gov.au

¹⁶ E61 Institute | The ghosts of employers' past: how prevalent are non-compete clauses in Australia? (e61.in)

so, an employer would state their entitlement to legal recourse if the action(s) contrary to the employment contract did not cease, and in many cases, this would resolve the issue in the first instance.

It is important to also note that these contractual provisions are only enforceable against employees that are participating in wrongful behaviour. For other employees, the contractual provisions are merely rules established to protect employer interests in circumstances whereby an employer interest could be unduly harmed.

Restraint of trade clauses provide a mechanism for the adequate protection of employer interests. They do this by deterring unethical behaviour by employees, often without any need to enforce contractual provisions. This deterrence is valuable to ensure that businesses are protected from harm, by limiting the likelihood of individuals engaging in such behaviours. While as noted previously, providing only for an avenue of legal recourse for a business once harm has already been done, is ineffective, unfair and does not afford a proper protection.

The ARA warns against adopting international standards within Australia because the legal landscape in other countries is different to that of Australia. We note that there is currently no uniform international approach to worker non-compete clauses and similar restrictions. Where there are legal measures in place - for instance in the United States - restrictive covenants are thought to be generally enforceable if they are narrowed to protect legitimate business interests and if they do not unreasonably restrict an employee earning a living.¹⁷

This approach can easily be observed to yield the result that these contract terms are enforceable. This means that the need for the regulation of worker non-compete clauses and other restraints in other countries is not readily comparable. For this reason, caution should be exercised in comparing policy decisions in other countries, especially when the economic, legal and labour-market environment is different and thus, can yield vastly diverse results for Australia.

HYPOTHESISED OUTCOMES FROM ARA'S RECOMMENDATIONS

If the ARA's recommendations were to be adopted, the outcome would be greater clarification as to the operation of non-compete clauses and other restraints for employees and employers. In doing so, this would enable employees and employers to better understand their lawful use, and enforceability, ensuring the misuse of such provisions is limited.

If regulation of worker non-compete clauses and other restraints is required, restricting the use of post-employment restraints on certain individuals and for a prescribed time, would ensure that any alleged adverse effects on job mobility is restricted, and at the same time, business interests can still be protected.

However, enacting any policy changes within this area requires a transitional period so that businesses and employees can adapt to these changes and make appropriate updates to employment contracts and business processes so-to avoid adverse impacts.

Correspondingly, if only non-compete clauses require legislative reformation, this should not extend to other restraints unnecessarily. Thus, striking a balance between what policy reformation is required and the perseverance of business-based protections so businesses can rightfully mitigate vulnerability.

¹⁷ American Bar Association | Comparative Perspectives on Non-Compete Clauses in the United States, United Kingdom, and Singapore (americanbar.org)

The strict codification of the common law legal principles would also work to ensure that ambiguity as to the lawfulness, operation and enforceability of these provisions was removed, creating greater transparency for their use within employment contracts.

Preserving the use of no-poach and wage fixing agreements within franchise agreements and to the reasonably necessary extent to preserve workforce insecurity and mitigate skill-shortages would also work to balance employer and employee interests. This would ensure only a limited number of employees would be subject to such restraints, and only where reasonably necessary, reducing any alleged adverse effects on job mobility.

CONCLUSION

The importance of worker non-compete clauses and other restraints is undeniable in the protection of legitimate business interests. However, existing regulation and convention ensures they are only used where needed to reasonably protect legitimate business interests or in New South Wales, to the extent they are not contrary to public interest.

As there is limited empirical data available on their actual impact, use and enforceability, the ARA warns that changing laws without proper investigation and research could create unintended adverse outcomes.

The ARA thanks Treasury for the opportunity to make a submission in response to its issues paper on non-compete clauses and other restraints. Any queries can be directed to policy@retail.org.au.