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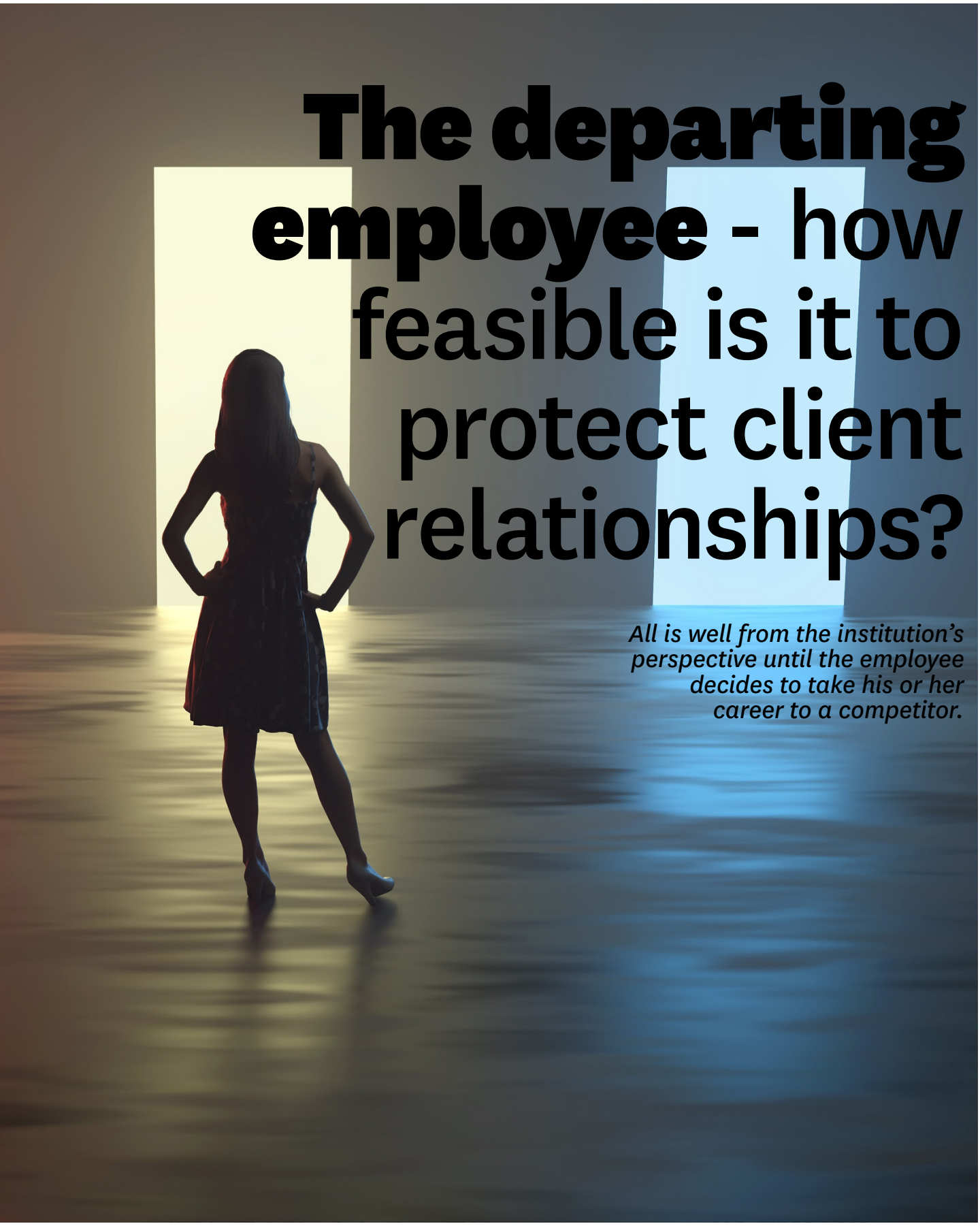

The departing employee - how feasible is it to protect client relationships?

All is well from the institution's perspective until the employee decides to take his or her career to a competitor.

BY:
Helen Colquhoun, Head of Employment Hong Kong
Alex Ma, Associate
DLA PIPER

AS A FINANCIAL HUB, HONG KONG IS HOME to many global private banks and wealth management institutions which offer investment and other financial services to a high-net-worth client base for whom personal relationships are tantamount. Significant effort, both by the institution and even more so by the individual client relationship manager, can go into developing and sustaining these valuable client relationships.

All is well from the institution's perspective until the employee decides to take his or her career to a competitor. This poses a real and immediate risk given that typically the majority of clients are more keen to maintain the relationship with the individual wealth manager than with the institution itself. It has therefore become common place for employment contracts in this industry in Hong Kong to contain provisions around both garden leave during any notice period (in an effort to try to build up relationships with a new advisor before the departing employee can join the competitor) and restrictive covenants (to try to protect relationships after the employee has left). Within Hong Kong, both approaches carry some risk of successful challenge or circumvention, but if such provisions are drafted carefully and deployed appropriately, they can provide important protection to institutions. In this article, we focus upon the use (and misuse) of restrictive covenants in Hong Kong.

Restrictive covenants

There is often a misconception that restrictive covenants are per se unenforceable in Hong Kong. In fact, whilst the starting point is indeed that any term which seeks to restrict the rights of an employee following employment is generally void and unenforceable, there is an exception if the employer can show that the restrictive covenant:

1. serves to protect the employer's legitimate business interests (which can include trade connections and confidential information);
2. is sufficiently clear and unambiguous (key to note is that any ambiguity is construed against the employer); and
3. is reasonable (after taking into account the interests and circumstances of the employer and employee and any public interest), requiring an overall assessment as to whether the restraint is no more than is reasonable and necessary to protect a legitimate business interest.

The real difficulty arises from the fact that each case will be highly fact specific, and a restriction that may be deemed enforceable in relation to one employee could similarly be struck down as unenforceable in relation to another employee of the same institution. Whilst in some jurisdictions a court will essentially re-write an otherwise unenforceable covenant in order to render it enforceable,

FOR KEY CLIENT-FACING EMPLOYEES, IT IS THEREFORE PRUDENT TO ALSO INCLUDE WELL-TAILORED 'NON-DEALING' CLAUSES, WHICH AIM AT PREVENTING AN EMPLOYEE FROM WORKING WITH CLIENTS IRRESPECTIVE OF WHICH PARTY MADE THE FIRST APPROACH POST-DEPARTURE.

it is important to note that employers in Hong Kong do not get the benefit of this approach. The courts may in certain circumstances sever unenforceable parts of a covenant, but they will not otherwise re-write or amend a covenant that is otherwise unenforceable. It is therefore critical to ensure that restrictions are appropriately tailored at the outset with due consideration given to an employee's seniority, role, and access to client confidential information. A boilerplate or one-size fits all set of restrictions will not work and will leave the company largely unprotected on departure.

Provisions relating to protection of client relationships are key in the wealth management industry, with the most popular being restrictions aimed at preventing an ex-employee from soliciting clients for a period of time. When considering reasonableness in relation to client provisions such as these, courts will consider factors such as:

1. the duration of the restriction - there are no fixed rules as to what will be deemed to be overly long, and different durations can (and should) be used for different categories of restrictions. In relation to client non-solicitation provisions, in principle the duration should be limited to the time it would reasonably take for a replacement employee to establish a relationship

with the clients in question. As a rule of thumb, for key senior employees a client non-solicitation clause of up to 12 months will stand a reasonably good prospect of success;
2. the seniority, role and position of the employee; and
3. the scope of the restriction - in particular whether the restriction is limited to only those client relationships for which the particular employee was responsible over a defined period of time or about whom the employee had access to confidential information - a restriction that seeks to protect an institution's whole client base or every client the employee has ever spoken to is highly likely to be struck down.

Many employers have discovered the hard way that proving 'solicitation' can be difficult and costly. For key client-facing employees, it is therefore prudent to also include well-tailored 'non-dealing' clauses, which aim at preventing an employee from working with clients irrespective of which party made the first approach post-departure.

Restrictive covenants should also be amended from time to time when the business (and the nature of the employee's role) evolve - critically, the reasonableness of a restriction will be judged by whether it was reasonable when entered into.

Employers frequently fall into the trap of having to rely on a covenant that was entered into several years before when an employee (likely at that point in a more junior role) joined and which is likely to be irrelevant and/or inappropriate to their role and seniority on departure. Promotions, changes to remuneration and role changes should be used as an opportunity to re-visit an employee's existing restrictions to determine if they are still appropriate.

In a recent case, *Winta Investment (Hong Kong) Limited v Ng Kam Chit* [2018] HKEC 890, an employer attempted to enforce a restrictive covenant against an employee (a delivery driver) who was leaving to join a competitor.

In essence, the restrictive covenant was drafted to prevent the employee form soliciting and interfering with the employer's customers for a period of 10 months following the termination of employment. At court, the employer argued that the restriction was reasonable and necessary to protect its legitimate interests for the following reasons:

1. the particular industry is very competitive;
2. the delivery driver holds commercially sensitive information (including customer's names, addresses and contact details); and
3. the employee is paid commission, therefore demonstrating that the employee's role included sales and promotion of the business.

In considering whether the restrictive covenant is enforceable, the court reiterated that the factual circumstances in regards to the employment to be highly relevant. In summary, the court opined that:

1. the starting point is that a restrictive covenant (a form of restraint of trade) is prima facie, unenforceable unless it can be shown that it is reasonable to protect a legitimate interest of the employer; and
2. confidential information such as trade secrets and customer lists are capable in principle of being protected in a restrictive covenant.

However, the court was unconvinced that in this particular case, the employee, as a delivery driver was in a position to have any meaningful influence over customers. As such, the restrictive covenant was held to be unenforceable.

One would think that in a wealth management environment, where the client-facing employees are the key persons representing the institution, it would be much easier to enforce the restrictive covenants. While this may be true in principle, the courts look at all of the circumstances when deciding on the enforceability of a restrictive covenant.

In *Cantor Fitzgerald Europe & Anor v Jason Jon Boyer & Ors* [2012] HKCU 478, four senior employees of Cantor resigned in 2011 and each of them entered into employment contracts with Mansion House, at the time, a start-up brokerage house in Hong Kong. The employment contracts with Cantor contained a non-solicitation of employees clause and a non-compete clause for a period of 12 months. Cantor took the employees to court for breach of their restrictive covenant obligations under their employment contract.

In particular, Cantor argued the non-solicitation clause was reasonable because "*it takes time to locate a suitable replacement broker and a broker takes time to nurture*".

In respect of the non-solicitation restriction, while the court was prepared to take the position that it was in principle reasonable to have a non-solicitation of employees clause in order to protect Cantor's legitimate business interests, the court rejected Cantor's argument as there was no evidence to support in this particular

instance that 12 months was required to find and train replacement employees. As such, the court refused to enforce the non-solicitation clause as 12 months was unreasonably long.

Practical pointers

Takeaway points for those drafting such restrictions to consider include:

- **consider the use of garden leave as an additional (not substitute) form of protection - whilst this can be circumvented in Hong Kong in principle through an employee paying in lieu of notice, many employees will accept garden leave without dispute, thus providing a higher degree of protection and control over their activities without having to rely on the potential enforceability of restrictive covenants**
- **conduct regular audits of covenants - we frequently see companies trying to enforce restrictions that were imposed when an employee first joined years before, and which simply do not reflect their current seniority or role or which cannot be enforced when judged by the test of reasonableness at the time they were entered into**
- **adopt tailored restrictions for those at different levels of seniority and/or across different roles**
- **remember that appropriately drafted non-solicitation and non-dealing clauses are likely to be easier to enforce than a non-compete - ensure your set of restrictions provides an appropriate arsenal of protections, rather than relying only on a non-compete**
- **don't ask for too much in the hope the court will help you re-write the covenant...**
- **don't forget that other possible avenues of protection can be utilised, for example claims around misuse of confidential information ■**