A lesson in restrictive covenants and new findings pertaining to a constructive wrongful dismissal claim

By Karen Moss
3PB Barristers

Quilter Private Client Advisers v Falconer and Continuum (Financial Services) LLP [2020] EWHC 3294 (QB)

1. In December 2020 Mr Justice Calver, sitting in the High Court, considered the matter of ***Quilter Private Client Advisers Ltd v Falconer and Continuum (Financial Services) LLP***. In broad terms, he found that a nine-month non-compete covenant was in restraint of trade and void, and also made interesting findings about affirmation in a constructive wrongful dismissal claim.

Facts and contractual terms

2. Ms Falconer was an FCA-regulated financial adviser, specialising in high-net-worth individuals and business owners, and began working for Quilter Private Client Advisers Ltd ("Quilter") in January 2019. She was employed for only six months as she resigned giving the required notice of 2 weeks, during her probationary period, because she was unhappy with the level of administrative support provided to her and the restrictions on the products she could recommend to the clients she was advising. She was also not getting on with her manager. She started to work for one of Quilter's competitors, Continuum (Financial Services) LLP ("Continuum") shortly after her resignation.

3. Ms Falconer's contract of employment with Quilter included a term purportedly preventing her dealing with or soliciting clients of Quilter for 12 months after the termination of her employment; and from working for a competitor for 9 months after leaving. The restrictions after termination were set out as follows:

Section 1: In order to protect the Confidential information and business connections of the Company to which they have access as a result of the Appointment, the Employee covenants (for itself and as trustee for Intrinsic) that they shall not for the following periods (less any period or periods spent on Garden leave immediately prior to Termination) after Termination howsoever arising save with the prior written consent of the Company (which shall not be unreasonably withheld or refused) directly or indirectly, either alone or jointly with or on behalf of any third party and whether on their own account or as principal, shareholder, director, employee, consultant:

a. for nine months following termination and in competition with the Company be employed or engaged in, assist or be interested in any undertaking which provides Services; ["the non-competition covenant"]

b. for twelve months following Termination, and in competition with the Company, solicit or otherwise endeavour to entice away from the Company … the business or custom of any Customer in relation to the supply of Services; ["the non-solicitation covenant"]

c. for twelve months following Termination, and in competition with the Company be concerned with the supply of Services to any customer; ["the no dealing covenant"]

Section 2: Each of the obligations in this clause is an entire, separate and independent restriction on the Employee, despite the fact that they may be contained in the same phrase and if any part is found to be invalid or unenforceable the remainder will remain valid and enforceable.

Section 3: None of the restrictions in clause Section 1 shall prevent the Employee from

…b. being engaged or concerned in any business concern insofar as the Employee's duties or work shall relate solely to geographical areas where the business concern is not in competition with Services; or

c. being engaged or concerned in any business concern, provided that the Employee's duties or work shall relate solely to services or activities of a kind with which the Employee was not concerned to a material extent in the 12 months before termination.

Section 4: While the restrictions are considered by the parties to be fair and reasonable in the circumstances, it is agreed that if any of them should be judged to be void or ineffective for any reason, but would be treated as valid and effective if part of the wording was deleted or the period or area was reduced in scope, they shall apply with such modifications as necessary to make them valid and effective…

Section 7: If the Employee is offered employment or a consultancy arrangement with a third party at any time during the Appointment or in the six months following Termination (howsoever arising), he will supply that third party with a full copy of this agreement and shall tell the Company the identity of that person as soon as possible after accepting the offer.

For the purposes of this clause:

"Customer" means any person, firm, company or entity in respect of which terms and conditions of business for the provision of financial advisory services have been in place between that person, firm, company or entity and the Company … during the 18 month period prior to Termination and in respect of which the Employee was materially concerned or had material personal contact at any time during such 18 month period prior to Termination;

"Services" means those parts of the business of the Company and/or Intrinsic with which the Employee was materially concerned at any time during the 12 months prior to Termination and, in particular, but not limited to, its business of the provision of Life, Pension and Investment services and Financial Advisory and Planning Services;

"Termination" means the termination of the Employee's Appointment with the Company howsoever caused.

4. Before Ms Falconer left the employment of Quilter, she scanned a substantial amount of Quilter's client documentation onto her personal laptop. Although Quilter knew Ms Falconer had started to work for Continuum a week or two after she started, it was four and a half months later when Quilter applied for injunctive relief. Quilter's witnesses admitted that they were not concerned about Ms Falconer working for a competitor *per se,* but were more concerned about her solicitation of their clients. In defence of the action for breach of restrictive covenants against her, Ms Falconer claimed that the terms were not enforceable due to her constructive dismissal.

The enforceability of the restrictive covenants

The non-compete clause

5. Calver J found that Ms Falconer had breached her contract of employment in a number of ways due to her breach of fidelity, confidentiality and various express clauses. He then turned to the restrictive covenants. Quilter did prove that they had legitimate business interests requiring protection (special trade connections and business secrets), but the covenants were found to be wider than was reasonably necessary for the protection of those business interests. The following were relevant factors in that decision:

   5.1 Quilter was found not to have adduced a great deal of evidence about the *necessity* of the non-compete restriction.

   5.2 The length of notice (during the probationary period) of 2 weeks was an indication that the length of restriction was unreasonable – the shorter the notice period, the less important to the company the employee's services would appear to be and the perceived need for protection is diminished.

   5.3 The length of the restriction was the same during the probationary period as thereafter, when Ms Falconer would have had little time to build relationships with clients. The evidence suggested that such a relationship would take a year to build; whereas Ms

Falconer had only been in employment with Quilter for 6 months and was purportedly restricted for 9 months from working for a competitor.

5.4 There was little evidence about why it was necessary for employees to be prevented from working for a competitor for as long as 9 months.

5.5 Employees who were more senior than Ms Falconer within Quilter had the same (or in one case less onerous) restrictions – this suggests that the restrictions for the more junior employee were wider than reasonably necessary.

5.6 The legitimate business interests of Quilter could have been protected by an appropriately worded non-dealing covenant relating to its customers; whereas the non-competition covenant prevented Ms Falconer from doing business with new clients who had nothing to do with Quilter. There was no substantive evidence from Quilter that non-dealing covenants were difficult to enforce – it was easy to identify the clients Ms Falconer dealt with during her Quilter employment.

5.7 Because Quilter is a nation-wide business, the geographical carve-out had little practical effect. It would have prevented Ms Falconer from working for a competitor all over the country.

5.8 Non-compete clauses were not industry-standard.

5.9 The witnesses for Quilter stated that the fact Ms Falconer was working for a competitor did not concern them, in itself. That suggests that preventing her from so doing went beyond what was a necessary protection.

6. All of the above should be considered by practitioners when drafting covenants and/or advising and/or drafting witness statements in proceedings concerning the enforceability of restrictive covenants. The delay of almost five months before action was taken by Quilter also confirmed the view that Quilter considered the non-dealing clauses to be more important that the non-compete clause. It is clear that Quilter did not discharge their evidential burden in a number of respects in this case.

Public interest of the non-compete clause

7. There was, in addition, an interesting argument put in relation to the public interest. Quilter had a regulatory obligation to act in the best interests of the client. Non-competition and non-dealing clauses act as a fetter on clients' ability to instruct the adviser of their choice: that is not in their best interests, and hence arguably lead to a breach of the client best interests' rule. If a client would like to continue to instruct a departing adviser, it was argued not to be in the public interest to prevent them from doing so through the enforcement of a non-competition or non-dealing covenant. It was suggested that to the extent that there is a conflict between a firm seeking to enforce a covenant and the interests of a client, that conflict must be resolved in favour of the client.

8. Calver J stated that he was not entirely persuaded by this but stated that:

> "*it was necessary to balance the public interest in the protection of the goodwill (in terms of customer connections) and the trade secrets of businesses of this type against the public policy that financial services advisers should be free to act in the best interests of the client by in particular, being able to join a competitor who offers the client a market wide offering of financial products rather than being forced to remain at a current employer who only offers those clients a restricted "in house" offering of financial products. But if the restrictions are found to be reasonable as between the parties by reference to the first of these considerations, then it is likely in my judgment that it will outweigh the latter consideration: after all, the client can always choose to engage a different financial services provider who does offer a full market service, regardless of the position of the individual financial adviser.*

9. In the absence of full argument on the point, Calver J left the point open, so it is still an argument which can be made in cases concerning comparable industries in future.

The other restrictive covenants

10. The other restrictive covenants were also found to be too wide. Quilter had failed to adduce any or any substantial evidence to justify the breadth of protection offered by the non-solicitation and non-dealing clauses. The 18-month back-stop described in the definition of "customer" in the contract was not supported by evidence. Calver J considered that the customer connection generated by an employee dealing with a customer once over 17 months before termination was likely to be stale and the evidence did not convince him otherwise. Quilter's clients were mostly subject to semi-annual reviews so the 18-month back-stop appeared to be unnecessary. The covenants would also have prevented Ms Falconer from dealing with family or friends as clients despite there being no legitimate business interest in preventing that.

The constructive dismissal claim

11. In relation to affirmation, Calver J cited Simler J (as she then was) in ***Cockram v Air Products Plc*** [2014] ICR 1065, when she upheld the principle that, at common law (unlike unfair dismissal under **s.95 Employment Rights Act 1996**), a party cannot affirm the contract for a limited period of time and then abrogate it on the expiry of that period of time. Therefore, an employee wishing to resign and successfully claim constructive dismissal would have to resign without notice. Simler J did, however, state that the law will look carefully at the facts before deciding whether there has really been an affirmation.

12. Calver J in ***Quilter*** stated:

> *"It is undoubtedly the case that if the employee decides to accept the repudiatory breach, he must do so unambiguously and with sufficient dispatch. If his purported acceptance is delayed, he runs the risk of a court finding that his action has not been sufficient to discharge the contract. However, in my judgment it is what happens during the delay which is the critical feature: provided the employee makes unambiguously clear his objection to what has been done by the employer, he is not necessarily to be taken to have affirmed the contract by giving a short period of notice, and continuing to work and draw pay for a limited period of time. To this extent, I would respectfully disagree with the observation of Simler J that at common law an employee wishing to resign and successfully claim constructive dismissal would necessarily have to resign without notice. It all depends upon the facts of the particular case whether the employee has nonetheless unambiguously accepted the repudiation of the employer and with sufficient dispatch. The length and circumstances of the delay require to be examined in each case."*

13. Ms Falconer failed to show that Quilter had committed a repudiatory breach of her contract and therefore she had not been constructively dismissed; but, interestingly, Calver J went on to observe that, on the particular facts of the ***Quilter*** case, he would not have found that Ms Falconer had affirmed the contract by giving two weeks' notice. Although she had delayed in accepting the alleged repudiatory breach, it was not put to EF that she had knowledge of her legal right to choose between treating herself as discharged under the contract or treating the contract as continuing and it appeared to Calver J that she did not know that she had this choice.

Implications

14. The ***Quilter v Falconer*** case demonstrates the importance of supporting the assertions commonly made by Claimants in restrictive covenant cases with substantial evidence, by the time these matters reach a final trial. Culver J confirmed that, when it comes to

restrictive covenants, one size does not fit all. Consideration must be given by employers, and practitioners drafting restrictive covenants, to what is necessary protection in relation to the particular employee concerned. The public interest element is also a relatively rarely used argument which is likely to be deployed again, where a conflict between the interests of a customer and the interests of the former employer arises.

15. The Department for Business, Energy and Industrial Strategy has recently issued a consultation paper[1] on measures to reform post-termination restrictive covenants. The ambit of the consultation is to consider two proposals: altering the law so that post-termination covenants are only enforceable if the employer continues to pay remuneration during the restricted period; and banning such covenants altogether. Given that restrictive covenants are now only enforceable if they go no further than is necessary to protect legitimate business interests, and, even then, only if they are also in the public interest, it will be interesting to see how this consultation progresses in the post-Brexit world of encouraging competition and entrepreneurial business; perhaps it will all be a simple matter of interpreting the public interest.

11 January 2020

Karen Moss

Barrister
3PB

0330 332 2633
karen.moss@3pb.co.uk

3pb.co.uk

[1] *Non-Compete Clauses - Consultation on measures to reform post-termination non-compete clauses in contracts of employment.* Closing date: 26 February 2021