FOLEY'S LIST

OBTAINING INJUNCTIONS AGAINST USE OF CONFIDENTIAL INFORMATION, SOLICITING CLIENTS AND COMPETING: S 1324 & S.183 CORPORATIONS ACT

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Glen Pauline
Barrister
E glen.pauline@vicbar.com.au
M 0411 707 487

1. I recently appeared in the Supreme Court to obtain injunctions restraining the misuse of confidential information by two former employees. They resigned as employees and resigned as directors of the company in order to set up a new company to compete. They had both been employees since around mid 2019. They had both signed employment contracts containing express confidential information and restraint clauses applying during and post their employment. They had both been directors of the company for about 3 years as well as being shareholders of the company for that time. They both had responsibility for dealing with customers including developing key relationships and proactively building the customer base in the area on behalf of the employer as well as scheduling jobs and managing the various employees needed to complete the jobs.

2. After deciding to resign they sought to negotiate an exit involving the sale of their shares in the company. However negotiations broke down without any agreed valuation of their shares. They then resigned from their employment immediately. They were still current shareholders of the employer company. They were still party to a shareholders agreement which contained express provisions relating to confidential information and restraints of trade.

3. In the 30 minutes or so that I have today I will talk about:

    a. the causes of action that are relevant to this kind of case;
    b. the restraints and confidential information obligations in the Employment Agreements and Shareholders Agreement;

c. the summons seeking injunctions and the importance of describing precisely the orders sought particularly in relation to clients and confidential information sought to be protected;
d. I will describe some of the evidence relied on to bring proceedings and seek injunctive relief preventing the use of confidential information for the purposes of soliciting clients in order to compete with the former employer; and
e. If time permits I will also mention some case law relating to protecting employer confidential information and client connection, and the balance of convenience and inadequacy of damages.

4. Let's get started. In the statement of claim it was alleged that the defendants were in breach of their contractual fiduciary and statutory duties and obligations by commencing a competing business. The evidence was that the defendants through their corporate entities were competing via a new company they had incorporated and held shares in. They had in fact held shares in that company for several months prior to resigning from their employment. This evidenced an intent to prepare to compete with the employer in breach of their employment duties and the shareholder agreement. Within a few weeks they had commenced to provide competing services via the new company in blatant breach of the prohibition on having a direct or indirect interest in a competing business. This also was a direct breach of the clause of the employment contract requiring them not to carry on or be interested in or associated with or otherwise involved in any business activity that was competitive with the employer for a period of 12 months or alternatively 6 months or alternatively 3 months after the conclusion of their employment.

5. Both the employment contracts and the shareholders agreement contained clauses relating to **confidential information**. The *employment contract* defined **confidential information** relevantly to include information or material proprietary to the employer or any of its related entities, information that was imparted in confidence to the employees by the employer, and any such information relating to the employer's clients or customers. In the *shareholders agreement* **confidential information was defined** to mean any and all technical and non-technical information that is confidential to a party not in the public domain and includes all data details business information contracts customer lists forecasts sales and merchandising information marketing plans documents agreements techniques commercial knowledge in whatever form however stored regardless of whether the information is designated conspicuously as confidential.

6. The defendants were bound by employment contracts containing express terms requiring them not to disclose without written consent confidential information or any information concerning the business transactions or affairs of the employer or any related body corporate, not to use or attempt to use confidential information in any manner which may cause or be calculated to cause injury or loss to the employer, not to use the confidential information other than for purposes of performing the services under the employment agreement; and they were required by their employment contracts to use their best endeavours to safeguard the security of the confidential information and advise immediately if they became aware of any breach of confidentiality; and return all confidential information immediately upon the request of the employer. These were described as the "*safeguarding obligations*".

7. The Defendants were also bound by **three restraint clauses** in their employment contracts:

    a. First a **non-solicitation clause** applying during employment and for one year post termination prohibiting them within Australia on their own account or on behalf of any other person directly or indirectly soliciting or interfering with or endeavouring to induce the custom of a person firm company or entity that had been a client of the employer in the 12 months prior to the end of their employment.
    b. Second, a **reduce dealings clause** prohibiting during employment and post termination for *12 months and six months and three months* in the restraint area being *Australia and Victoria and within 200 kilometres of a Victorian country town* by any means directly or indirectly attempting in any manner to **persuade a client to cease dealings with or reduce dealings** with the employer which the client had customarily had or contemplated having with the employer.
    c. Third, a **competition restraint** requiring them during employment and post termination for the same periods and in the same restraint area, by any means directly or indirectly carrying on advising providing services to or engaging or being engaged concerned or interested in, or associated with or otherwise involved in, any business activity that is competitive with any business carried on by the employer.

8. The employment contracts contained clauses in which the defendants acknowledged that the solicitation clause operates independently and is necessary to protect the employers reasonable and legitimate business interests. The defendants in their employment contracts also acknowledged that the

employer will be entitled to injunctive relief and other equitable relief to prevent or cure any breach or threatened breach of those clauses.

9. In addition to breaches of the restraint clauses of the employment contract and **breaches of their fiduciary duties to the employer as directors and employees**, it was alleged and they were in contravention of section 183 of the *Corporations Act* duties not to **(both during and after cessation of employment)**:

    a. **improperly use information obtained as an employee to gain an advantage for themselves or someone else; or**
    b. **cause detriment to the corporation.**

10. In a recent decision of Derrington J *Smart EV Solutions v Guy* [2023] FCA 1580, it was said that the Confidential Information protected by section 183 arguably extends broadly to "knowledge of facts".1 His Honour also said that the use of confidential information improperly to entice customers and divert business opportunities is in contravention of section 183.2

11. Section 1324 of the *Corporations Act* was relied upon in seeking the injunctions including on an interim basis. Sub-section (1) provides relevantly that where a person has engaged, is engaging or is proposing to engage in, conduct that constitutes a contravention, an attempt, aiding abetting counselling or procuring, or being directly or indirectly knowingly concerned in or party to such contravention, the Court may grant an injunction on terms it things fit including restraining conduct and requiring the person to do an act or thing.

12. Sub-section (4) provides the power to grant an interim injunction, and sub-section (5) provides the power to grant an injunction by consent whether or not it is satisfied that sub-section (1) applies. Further, sub-section (6) and (7) allow the Court to exercise its power to grant both prohibitory and mandatory injunctions regardless of whether or not it appears they intend to continue to engage in the conduct (or refuse to do an act or thing), and regardless of whether there is imminent danger of substantial damage to any person from such continued conduct or refusal.

[1] See *Smart EV Solutions v Guy* [2023] FCA 1580, Derrington J at [71].
[2] See *Smart EV Solutions v Guy* [2023] FCA 1580, Derrington J at [73].

Summonses

13. The Plaintiffs applied for interlocutory injunctive relief restraining the Defendants from conduct in breach of confidential information clauses in the Employment Agreements and Shareholders Agreement, directors and employees fiduciary duties, and section 183 of the *Corporations Act* 2001. They sought orders enforcing the provisions of the Shareholder Agreement with respect to the disclosure of confidential information, the return or destruction of confidential information.

14. The schedule to the summons contained the broad descriptions of **confidential information** taken from the combined wording of the Employment Agreements and the Shareholders Agreement. In essence, the definitions were broad and typical and included reference to:

    *"information or material proprietary to" the employer, including "all data…figures, financials, costings…processes, formulae, know-how, trade secrets… **business information**…intellectual property rights, contracts, customer lists, documents, agreements, commercial knowledge and other proprietary information in whatever form and however stored and regardless of whether the information is designated conspicuously or otherwise as confidential;*

15. Also included was *information designated in writing as confidential during the employment; information imparted in confidence; and any such information relating to the employer's clients or customers*.

16. The summons also sought orders requiring the Defendants to swear an affidavit specifying all persons to whom they have disclosed Confidential Information including by providing relevant details.

17. The schedule to the Summons also described the regime for return or destruction of confidential information directions sought by way of order, including delivery of hard copy and electronic information to the Plaintiff's solicitors, and deletion of the electronic files and production to the Plaintiffs solicitors of logs or records to evidence the permanent deletion and/or destruction of the files.

18. There were also two orders sought in the summons relating to the post-termination employment restraints. The first sought to restrain the Defendants from soliciting, interfering with or endeavouring to induce the custom of any client of the First Plaintiff in the 12 months prior to termination of their employment agreement (as named in the Schedule) ("**the solicitation order**"). The second

sought to restrain the Defendants from attempting to persuade a client to cease dealing with or to reduce the dealings which the client has customarily had or contemplated having with the First Plaintiff (as named in the Schedule) ("**the reduce dealings order**").

19. Finally, the summons specifically named all 162 clients whom it was alleged the Defendants had a close connection with through their employment, in light of the relevant case law.

Prima facie case

20. The Plaintiffs alleged a strong prima facie case through disclosure and use of the employer's confidential information relating to its clients and the corporate opportunities to provide services to them, that were known to them only through their employment and directorships, for the purposes of soliciting clients and persuading them to cease or reduce dealings with the employer.

21. They had already commenced a competing business and already secured the custom of at least two of the Plaintiff's clients of the past one year and appeared to be seeking to provide services to a key client, and there was direct evidence that they had submitted a quotation to another client.

Balance of convenience

22. The balance of convenience3 favoured the granting of the orders sought, because there was a greater risk of injury or inconvenience to the Plaintiffs if the injunctions were not granted, than any risk of injury or inconvenience to the Defendants, who at least until determination at trial, would be able to continue to operate the new business in competition with the First Plaintiff (as no injunction was sought to stop them competing per se) but would need to do so without further disclosing or using the confidential information of the Plaintiffs or soliciting clients or persuading them to reduce dealings with the Plaintiff.

23. The evidence was that there was another 162 clients whose primary contact with the First Plaintiff had been the Defendants whilst they were employed by the First Plaintiff. The evidence was that those clients had together generated a monthly revenue of over $800,000 prior to the Defendants leaving, and the monthly revenue had dropped sharply in the two months since, to $350,000 and then

[3] *Patrick Stevedores Operations No 2 Pty Ltd* v *Maritime Union of Australia (No 3)* (1998) 195 CLR 1; see also *Australian Broadcasting Corporation v O'Neil* (2006) 227 CLR 57 at 81, 82 [65] per Gummow and Hayne JJ (see also [19], [65], [72]).

$150,000 in consecutive months, with such drop not being accounted for by any seasonal factors.

24. There was evidence of a recent comment by one of the Defendants, whilst still employed by the Plaintiff, that the other Defendant had "close contacts with the local councils" and other bodies that "would generate the daily business" (for the Plaintiff).

25. Another former employee of the Plaintiff, a relative of one of the Defendants, had been seen on the site of one of the Plaintiff's major clients, doing works of the same type carried on by him when he was employed by the First Plaintiff. The monthly revenue from that client had significantly dropped from more than $30,000 to $2,000.

26. The Plaintiff had calculated a total loss of revenue in the two months since the Defendants ceased their employment of over $100,000, with the prospect of much more loss to come.

Evidence of soliciting customers

27. There was an inference arising from the evidence, that the First and Third Plaintiffs may have directly or indirectly solicited, interfered with or endeavoured to induce the custom of one client arising from an email from that client to the Defendant whilst he was employed by the Plaintiff, the lack of any email response from him whilst employed by the Plaintiff, the confirmation from the client about a month later that she had directed the work to him and he would shortly be working for a new company.

28. A further inference arose in relation to another client where the job had been booked with the Plaintiff initially, until the Plaintiff sent its current schedule of rates to the client at the client's request. This suggested the Defendants were competing with the Plaintiff on price, using the knowledge they had of the Plaintiff's rates, in "endeavouring to induce" the clients. The strong inference was that this client in fact was induced, and either directly or indirectly, persuaded to cease dealing with or reduce dealings with the Plaintiff.

29. The prima facie case was strengthened by the evidence relating to another client. The first evidence of any contact between the client and the Defendants since they had ceased employment with the Plaintiff, was an email from the client to the Defendant at his email address of the new competing company. It could be inferred that the Defendant had directly or indirectly taken steps prior to that date,

to solicit, interfere with or endeavour to induce the custom of that client, by providing him with his new email address.

30. The client had forwarded the email chain to the Plaintiff which was direct proof of the Defendants taking a previous corporate opportunity offered to the Plaintiff while the Defendants were employed by the Plaintiff. The email chain included the quotation by them for the job after they had commenced their competing business.

31. This was unequivocal evidence of a direct attempt to solicit the custom of the client in breach of the non-solicitation restraints and reduce dealings restraints. It was clear that the corporate opportunity was previously the First Plaintiff's while it employed the First Defendant, and that its confidential information as to its client had been used by the First Defendant which may cause injury or loss to the First Plaintiff.

32. The competition restraint had also been breached within three months being the minimum enforceable period, and within the minimum geographical area of the clause. Hence, by reason of the Defendants involvement in the competing company, providing or seeking to provide competing services to those clients within the minimum time period and geographical area, there was a prima facie case of breach of the competition restraint (if enforceable).

Case law re **customer connection** as a legitimate interest of an employer

33. The key issue in the proceeding was of course the extent to which the Plaintiff could seek to protect its client base from the Defendants. Time does not permit me to describe the relevant case law principles which are well established and restated in *Wallis Nominees (Computing) Pty Ltd v Pickett*[4], by the Court of Appeal relating to protection of an employer's legitimate interest in its **customer connection** save that the Court concluded:
    a. "**Two key points** emerge from these formulations. First, that an employee must be in a **position to gain trust and confidence so as to be relied on in a client's affairs**. Secondly, that the relationship between employee and client is such that there is a **possibility that if the employee leaves the business of the employer he or she may carry away the client's business** with them.

[4] (2013) 45 VR 657 [21]–[26], [50], [52]–[54] (Warren CJ and Davies AJA, Redlich JA agreeing) (citations omitted).

34. In this proceeding the evidence relied upon included that the Defendants and their families were based in the local regional Victorian area, hence the Defendants were "locals" and they had been able to establish the local client base and operate the business in the roles of Operations Manager. Their responsibility included dealing with customers, scheduling jobs and managing drivers and employees to complete actual jobs. The Third Defendant's role was to "source work" and included "chasing jobs" and he "***had close contacts with the local councils, other authorities and private clients that would generate the general daily business*** for the Plaintiff". The **Plaintiff had encouraged them to develop key relationships with customers** and proactively build the customer base in the area on behalf of the Plaintiff".

35. There was particular evidence of dealings between the First Defendant and direct contact with a client, across two years, since 2022, and the relation of ***influence*** he had with that client whilst an employee of the Plaintiff. Together with evidence of his dealings with the other clients, there was clear and cogent evidence upon which the Court could rely to conclude that the Plaintiff needed to protect its legitimate interest in its **customer connections** from the actions of the Defendants.

36. There is authority for the proposition that an employer is entitled to protection against the use of personal knowledge and ***influence*** over its customers, which the employee might acquire in the course of his or her employment, so as to **undermine** its customer connections. It is against the possibility of its business connection being adversely affected by the use of that personal knowledge and ***influence*** that the employer is entitled to be protected.5

37. The Plaintiff in my recent case did not have long term contracts for the routine maintenance work and was vulnerable to losing significant ongoing maintenance work if individual customers were encouraged to direct their work elsewhere. Hence, the need for orders to protect the Plaintiff's legitimate interests from damage, was clear.

38. A recent reported case of an injunction made to restrain misuse of confidential information in similar circumstances involving a former employee and director

[5] See *International Cleaning Services (Australia) Pty Ltd v Dmytrenko* [2020] SASC 222, Stanley J at [49].

and shareholder, is *Smart EV Solutions v Guy* [2023] FCA 1580.6 At [33] Derrington J said:

> "courts of equity are astute to protect confidential information from misuse: see *Commonwealth v John Fairfax & Sons Ltd* (1980) 147 CLR 39, 50; *Boardman v Phipps* [1967] 2 AC 46, 127-128. That is particularly so where the information in question has been utilised by former employees or directors **in pursuit of business opportunities** in apparent contravention of their duties".

39. At [35] Derrington J referred to the situation where information that is confidential in nature is made explicit by the imposition of confidentiality **in contracts between the employee and the company**, and said the Court is permitted in assessing the balance of convenience, to consider whether the respondent was:

*"warned or had notice of the rights that it is alleged to have infringed, such that it can be said to have embarked on the conduct the subject of the application with its **"eyes wide open"**.*

40. That was the case here by reason of the Employment Agreements and Shareholders Agreement.

Legal principles – restraints

41. Time does not permit me to discuss the principles of enforceability of restraint clauses, however I make the following comments.

42. There is authority, Derrington J *Smart EV Solutions v Guy*, that where an **employee's role in the business includes business development**, this prima facie supports a reasonable non-solicitation clause that covers all existing clients as being reasonable.7

43. Recently, in *Avant Group v Kiddle* [2023] FCA 685, Wheelahan J at [101] said that where the parties had in contemplation that the employee might during the term of employment, have access to **information identifying all the plaintiff's clients**, and **would be involved in business development**, and **exposed to the plaintiff's confidential information that identified the clients and their contact details**, and the **pricing structure and business strategies** of the employer, it is arguable

[6] See Derrington J at [33], [35], [36], [67], [68], [69], [71], [72], [73]-[76], [80].
[7] Ibid at [102].

that these activities would also have fostered connections between the employee and persons who referred business to the employer on a regular or ongoing basis. In such circumstances, employers may be entitled to protection, by reasonable post-employment restraints, not only against the unfair use of customer connections, but ***also against the use of confidential information*** which is otherwise difficult to protect.8

Identification of clients to be protected

44. In *Crowe Horwath Pty Ltd v Loone* [2016] VSC 582 McDonald J held at [14] the plaintiff had a genuine interest in protecting its client base.9

45. McDonald J referred to *Birdanco Nominees Pty Ltd v Money* (2012) 36 VR 341; 219 IR 276 at [5] which is authority for the proposition that a *restraint clause that is limited to the provision of services to those particular clients that, by virtue of the employment and the opportunity to establish a continuing relationship*, is *precisely the kind of connection which the authorities make clear, the employer is entitled, within reasonable limits, to protect*.10

46. In *Crowe Horwath* the interlocutory injunction was made with reference to the clients listed in an exhibit to the plaintiff's affidavit material.

Damages inadequate

47. *In Avant Group v Kiddle* [2023] FCA 685 (Wheelahan J) at [7] said that in applications for interlocutory injunctions to enforce restraint clauses, the inadequacy of damages as a final remedy informs the balance of convenience. Damages may be inadequate because once **client relationships** are severed, they may be difficult to repair, and an award of damages, although possible, may not be the most suitable remedy.

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[8] *See Avant Group v Kiddle* [2023] FCA 685, Wheelahan J at [101].

[9] McDonald J at [14] citing *Lindner v Murdock's Garage* (1950) 83 CLR 628 at 636, cited with approval in *Birdanco Nominees Pty Ltd v Money* (2012) 36 VR 341; 219 IR 276 at [5], [75]-[76].
[10] *Birdanco Nominees Pty Ltd v Money* (2012) 36 VR 341; 219 IR 276 at [5] cited by McDonald J in *Crowe Horwath Pty Ltd v Loone* [2016] VSC 582 at [16].

48. *In Smart EV Solutions v Guy* [2023] FCA 1580, Derrington J at [81] said damages will be an inadequate remedy for a number of reasons, including the difficulty of detection of breaches of the obligations, establishing causation between any **loss of business with customers** and any actions of the ex-employee and the difficulty of the calculation of the quantum of damages arising from the loss of business.

Conclusion

49. Happily for the Plaintiffs in my recent case the Defendants **consented** until further order of the Court, to the injunctions and other orders sought with some minor modifications. The Plaintiffs gave the usual undertaking as to damages.