



## HR Broadcast – Internal Promotions and Restrictive Covenants

Consider this scenario; as a manager or owner of a business you are keen to promote from within as the business expands. You might employ somebody who has been with you for 10 or 15 years, has done a really good job and has helped the business develop, and you now want to make them a senior manager or perhaps even a director.

They are now in a position where they could cause your business damage if they were subsequently to leave and set up in competition or perhaps even take customers with them.

One way to limit the risk is to persuade that employee to now enter into “restrictive covenants”, limiting activities should they leave. This would cover such things as the period of time before which a competitor business could be established and a geographical area.

When contracts of employment are prepared for senior managers they very commonly include such restrictive covenants. However, a problem arises when an employee is promoted and their existing contract of employment reflects an altogether more junior position where such things as competition and taking away customers would have been highly unlikely.

Some employees in this situation will be more than happy to accept the promotion but much more reluctant to agree to give up employment rights should they leave the business. It is a common legal argument that for an employee

to give up such rights and therefore vary his existing contract of employment, he must receive some kind of ‘payment’ for that contract variation for the variation to be binding. This payment is known as ‘consideration’ and it does not need to be in the form of cash.

Timing is critically important; in a recent case the employer carried out reviews and appraisals of all staff and a particular employee received a pay increase. Shortly afterwards he was invited to sign a contract of employment reflecting that pay increase, but also requiring him to sign up to additional restrictive covenants.

He did sign the new contract, but subsequently left the employment and argued that he was not bound by the new restrictive covenants because he had received no consideration, the salary increase being made before he was offered the contract of employment. This last point is perhaps a little curious but the evidence before the court was that if the employee had not signed the new contract he would have been dismissed, therefore continued employment was of value.

There has undoubtedly been a trend over the last two or three years for the courts to find a way to defeat this kind of argument, presumably on the basis that the employee knew exactly what he or she was doing and was happy to accept the good parts of a revised contract, such as a salary increase but would perhaps unsurprisingly try to avoid the



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negative parts, such as more demanding covenants.

So, in this particular case, the High Court rejected the timing argument and in trying to identify the necessary 'consideration' concluded that the consideration could comprise the appraisal itself, the subsequent pay increase and the fact of continued employment.

Therefore the employee was bound by these new covenants, which seems entirely fair in the circumstances, because he was receiving benefits from the revised contract and he had actually signed the contract containing the revised restrictive covenants.

About two years ago there was also a case where employees had received an improved package of benefits linked to a promotion but did not sign the contract of employment. That itself raised the question why the employer had tolerated the situation. On leaving these employees also argued that there had been no consideration and that they were not bound by the new covenants. Again the court rejected that argument. The court found that the employees had enjoyed some of the benefits, such as health and medical benefits and they could not pick and choose which parts of the contract they wished to accept. If they accepted part of the new contract they accepted all of it.

The lesson that comes from this kind of case is that while the courts seem sympathetic to employers when contemplating promotions

from within it is very important to look at the existing contract of employment and see whether this need to reviewing and updating to go with the new more senior status.

It should then be made clear to the employee that a promotion or salary increase is conditional upon him or her signing up to a new contract containing new restrictive covenants and agreeing to be bound by those. No signature on a new contract, no promotion.