PRINCIPLES OF RESTRICTIVE COVENANTS AND THE RIGHTS OF AN EMPLOYEE IN THE WORKPLACE

Shoprite Checkers (Pty) Ltd v Kgatle [2023] ZAWCHC 159

1 Introduction

Indubitably, employees have been subjected to ill treatment and improper working conditions by their employers. Prior to South Africa attaining full democracy and adopting the Constitution of the Republic of South Africa, 1996 (the Constitution) as supreme law, and the passing of post-democratic labour legislation, employees suffered at the hands of their employers. Section 23 of the Constitution, dealing with labour relations, guarantees certain fundamental rights for employees in the workplace. Furthermore, the Labour Relations Act (66 of 1995), read together with the Basic Conditions of Employment Act (75 of 1997), has key provisions aimed at protecting and promoting the rights of employees in the workplace. Non-compete agreements, which can lawfully be introduced by an employer in a contract of employment, find difficult application, particularly because the South African government, especially the legislative branch, has travelled lengths to uphold and protect the rights of employees. In terms of the law, employers have the right to include non-compete agreements in the employment contract. The rationale for non-compete agreements is to prevent an employee from moving to a different employer in a similar trade or business to that of the employer after the employee's contract of employment is terminated either by the employee or the employer. The question that is most raised in disputes regarding the enforcement of non-compete agreements is whether the agreement violates the employee's right to work in an occupation of their choice. Another equally important consideration regarding non-compete agreements is whether such agreements unnecessarily limit the employee's chances of being economically active and of providing for themselves, and possibly dependants.

In this light, this case note reviews the judgment in *Shoprite Checkers (Pty) Ltd v Kgatle* ([2023] ZAWCHC 159). This case is significant in the South African context since it not only revisits some of the important principles of non-compete agreements, but does so having regard to the rights of employees. What is commendable in this case is the court's readiness to protect the rights of the employee in question. However, before analysing the case, it is essential to restate some of the legal principles of both contract law and employment law.

2 Principles of contract

The law of contract is based on several general notions, the first being privity of contract. Privity of contract simply means that an agreement between parties of a particular contract entitles them to bring lawsuits against each other, to the exclusion of third parties; accordingly, persons who are not parties to an employment contract do not have a say in the issues pertaining to the contractual relationship between the contracting parties. For instance, no third party may intervene in the affairs of an employment relationship that flow from the employment contract. Another equally important element of a contract is the *caveat subscriptor* principle. This principle states that whoever signs an agreement must be aware of what they sign and must equally be bound by the terms of the agreement that they have signed. Lastly, the principle of sanctity of contract needs consideration. This principle requires parties to honour their contractual obligations, failing which one can take the other to court on the basis of a breach of contract. A breach of contract refers to the failure by one or both parties to a contract to fulfil their contractual obligations. There are at least five common breaches of contract – namely, *mora debitoris*, *mora creditoris*, repudiation, positive malperformance and making performance impossible. Breaching a non-compete agreement can be classified as *obligatio non faciendi*. This type of breach of contract may fall under positive malperformance, in terms of which the debtor performs an act from which they are lawfully required to restrain themselves. Argued differently, a breach of a non-compete agreement may also be classified as repudiation, which in essence refers to a situation where a party to a contract, either through words or conduct, behaves in a manner indicating they no longer wish to be bound to the contract or a particular contractual term. Regardless of the classification of the breach, failing to comply with a non-compete contract or clause will result in a breach of contract, and subsequently be followed by the ordinary remedies for breach of contract.

3 Principles of employment law

At the dawn of democracy, South Africans in all spheres attained freedom. This freedom extended to the labour market, where employees now have rights such as the right to equal pay for equal work, the right to good working conditions and the right not to be unfairly dismissed, among others. Historically, workers in South Africa have been victims of slavery and unfair treatment. Thus, after the installation of democratic government in 1994, South Africa had to take legislative reforms to recognise and protect the rights and working conditions of employees. Generally, it is understood that an employer is in a position of authority and carries more bargaining power than do employees when negotiating terms of the employment contract. It is against this background and historical inadequacies that the courts seek to protect the rights of employees. Employees are sometimes viewed as receiving unfairly beneficial treatment when compared with the treatment to which employers are subjected. Where non-compete agreements are concerned, one's first thought may well be that an employer wants to ill-treat an employee by unfairly restricting the latter's freedom of occupation. This

reasoning is supported by several South African judgments in which the court, at the expense of an employer, refused to enforce non-compete agreements (see *Savvy Insurance Brokers (Pty) Ltd v Fourie* [2022] ZALCJHB 222; *Med 24-7 (Pty) Ltd v Kruger* [2022] ZAFSHC 79; *Forsure (Pty) Ltd v Puckle* [2022] ZALCJHB 221; and *DIY Superstores (Pty) Ltd v Kruger* ([2022] ZAFSHC 75) – all cases where the courts have dismissed an application for the enforcement of non-compete agreements).

These cases show that the courts consider employees to be the weaker partners in the employment relationship.

In cases such as *Dust A Side Partnership v Ludik* ([2014] ZALCJHB 97), the court, though finding that the employee had breached a non-compete clause, was hesitant to order specific performance. This is particularly because of the financial hardship the employee could suffer if ordered to leave employment with the new employer. In other cases, such as *AJ Charnaud & Company (Pty) Ltd v Van der Merwe* ([2020] ZALCJHB 1) and *SA Kalk and GIPS (Edms) Bpk v Krog* ([2017] ZALCCT 30), the court found that the applicant (employer) had failed to prove the existence of a restraint-of-trade agreement.

Considering the above, the courts evidently remain hesitant to enforce non-compete agreements, especially where enforcement will result in a failure to protect the rights and interests of an ex-employee. Again, one has to bear in mind that the employee is the weaker party in the employment relationship.

4 Non-compete agreements

Non-compete agreements, commonly known as restraint-of-trade contracts, operate in employment relationships or sale-of-business contracts. For instance, where parties enter into a contract of employment, they may agree that, after the termination of their employment relationship, the employee will not take up employment with a different employer operating in the same industry or field of business. Similarly, in sale-of-business contracts, a current business owner selling their business may undertake not to compete with a new owner by agreeing not to operate in the same trade or industry. There are several factors that courts look into when dealing with the enforcement of non-compete agreements.

In one of the leading cases, the court said:

> "A contractual restraint curtailing the freedom of a former employee to do the work for which he is qualified will be held to be unreasonable, contrary to the public interest and therefore unenforceable on grounds of public policy if the ex-employee (the covenantor) proves that at the time enforcement is sought, the restraint is directed solely to the restriction of fair competition with the ex-employer (the covenantee); and that the restraint is not at that time reasonably necessary for the legitimate protection of the covenantee's protectable proprietary interests, being his goodwill in the form of trade connection, and his trade secrets. If it appears that such a protectable interest then exists and that the restraint is in terms wider than is then reasonably necessary for the protection thereof, the Court may enforce any part of the restraint that nevertheless appears to remain reasonably necessary for that purpose." (*Magna Alloys and Research v Ellis* (1984 (4) SA 874 (A))

In other words, a non-compete agreement will not be enforceable where it is meant simply to prevent healthy competition. There should be justifiable reasons for restricting a person's freedom to trade or run a business. The test known as the Basson test was formulated in the case of *Basson v Chilwan* (1993 (3) SA 742 (A)) as follows:

> "a. Is there an interest of the one party, which is deserving of protection at the termination of the agreement?
> b. Is such interest being prejudiced by the other party?
> c. If so, does such interest so weigh up qualitatively and quantitatively against the interest of the latter party that the latter should not be economically inactive and unproductive?
> d. Is there another facet of public policy having nothing to do with the relationship between the parties but which requires that the restraint should either be maintained or rejected?" (*Basson v Chilwan supra* 7761 I–J)

In terms of the principles laid down in the *Magna Alloys* case, an employer bears a reverse onus to prove that there are indeed interests worthy of protection by a non-compete agreement, and it is not simply meant to prevent fair competition.

Furthermore, in the case of *Louw and Co (Pty) Ltd v Richter* ([2010] ZANCHC 54), the court said:

> "Covenants in restraint of trade are valid. Like all other contractual stipulations, however, they are unenforceable when, and to the extent that, their enforcement would be contrary to public policy. It is against public policy to enforce a covenant which is unreasonable, one which unreasonably restricts the covenantor's freedom to trade or to work. In so far as it has that effect, the covenant will not therefore be enforced. Whether it is indeed unreasonable must be determined with reference to the circumstances of the case. Such circumstances are not limited to those that existed when the parties entered into the covenant. Account must also be taken of what has happened since then and, in particular, of the situation prevailing at the time enforcement is sought." (*Louw and Co (Pty) Ltd v Richter supra* 243B–D)

Thus, the enforcement of non-compete agreements must be judged against the principles of reasonableness and the principles of public policy.

5 Facts

The first respondent (the employee) received a bursary from the applicant to complete his honours degree at the University of Stellenbosch. He then worked as a trainee for the applicant in its logistics section, and was promoted to the position of Design Planner on 1 July 2021. At this point, he signed an employment contract that contained two covenants relating to confidentiality and restraint of trade, respectively. The employee subsequently resigned, claiming that there were no opportunities for promotion with the applicant, that he was underpaid, and that he lacked a clear professional path. His resignation was motivated by these factors. He indicated that, with effect from 3 April 2023, he would be taking up employment with the second respondent, a significant and direct competitor of the applicant. This was notwithstanding that the restraint of trade forbade

the first respondent from working for any company that marketed and distributed identical goods to those of the applicant through the retail chain.

The applicant thus brought an urgent application to enforce the confidentiality agreement and trade-restraint undertaking. The second respondent, one of the largest retail chain stores, is in direct competition with the trade carried out by the applicant, and sells, among other things, the same pharmaceutical and household products as the applicant. The first respondent's employment with the applicant was extended to 2 May 2023 because (a) the applicant undertook to pay his remuneration for April 2023 and (b) the second respondent was prepared to keep his position open for him, pending the outcome of the interdict application by the applicant. The application also agreed to re-appoint the first respondent to his old position if the restraint were enforced.

6 Legal counsel's arguments

The applicant argued that the first respondent was legally bound by the terms of their contract. This is because the applicant contributed to the first respondent's education, and trusted him with sensitive information. Therefore, it was contended, his agreements with the applicant must be upheld.

The applicant claimed that if the first respondent wished to prove that application of the restraint in these circumstances was against public policy, he had to provide a sufficient factual basis on the papers. The applicant claimed that all of the first respondent's defences were technical and in need of more legal and factual support. This was claimed to be the case, among other things, owing to the first respondent's admission that the applicant had granted him access to its private information, which needed to be protected. This is the reason the first respondent reiterated his confidentiality commitment to the applicant, both before the application was launched and during the application process.

The first respondent's main defence was that the restraint should not be implemented for public policy considerations. He argued that even if the second respondent had access to the applicant's trade secrets and confidential information, it would not stand to earn anything from it. This is one reason that enforcing restraints may be against public policy.

The first respondent averred that it would be unfair, unreasonable and not in the public interest to enforce the restraint against him because: (a) he had given an undertaking that he would keep the applicant's information confidential and not share it with the second respondent; (b) his undertaking was sufficient protection for the applicant; (c) the enforcement of the restraint was unreasonable; (d) the confidential information he may have been exposed to was of no commercial benefit to the second respondent and, (e) taking into account the first respondent's interests in comparison to the applicant's, both qualitatively and quantitatively, it did not justify applying the restraint to his disadvantage.

The applicant claimed that the first respondent had received a promotion to a managerial position. He was therefore obliged to sign both covenants –

the restraint and the confidential undertaking – on which the petitioner had relied.

The first respondent made the following arguments as to why his restraint should not be enforced: He left the applicant for a number of reasons, including: (a) his youth; (b) the short amount of time he had worked there; (c) the fact that he was not a senior employee; and (d) his dissatisfaction with his job and the circumstances surrounding it. According to the applicant, the first respondent needed to make good on his promise.

According to the applicant, the first respondent must honour his undertaking, since the applicant had promoted him and given him access to confidential information.

7 Court's findings

The court concluded that it had unquestionably been shown that the first respondent intended to work in the same field as the second respondent, which is a direct rival of the applicant with similar expansionist goals and tactics, making the enforcement of the restraint (it was argued) in the public interest. Therefore, whether to enforce the restraint was the main question in this application.

The court considered the fact that the applicant remained ready to accept a withdrawal of the first respondent's resignation, and to retain his position. Thus, the court concluded that it was necessary to enforce the restraint on the basis of public policy in both a qualitative and quantitative sense. The balance between upholding constitutional principles regarding the restraint agreement and trade freedom was also taken into consideration by the court. The court held that the rule of law and legality norms were to be observed.

Furthermore, it was in the public interest that the applicant be encouraged to promote the first respondent into a position of trust. The applicant's reasons for the terms of the restraint were not rendered against public policy by the first respondent's allegations that he did not possess the knowledge. This was because the applicant required the first respondent to sign the restraint covenant when he was promoted.

Moreover, according to the court, the contract concluded between the applicant and the first respondent undoubtedly served an acceptable employment purpose for the benefit of both parties at the time that the applicant promoted the first respondent. The enforceability of contracts is essential both for commerce and fair employment practices.

As far as the principles of public policy are concerned, the court was not convinced that the restraint covenant was contrary to the principles of public policy in the circumstances of the case. The basis of this reasoning was that the first respondent, having been fully informed, elected voluntarily to consent to the terms of the restraint covenant; the first respondent expressly agreed and accepted that he understood what he agreed to in his employment contract and restraint covenant.

The court concluded that it is evident that the parties to the contract and clause in question possessed equal bargaining power, and they must have understood what they agreed to.

For these reasons, the court granted the interim and final relief contended for by the applicant against the first respondent and costs in addition thereto. Thus, the restraint-of-trade agreement was enforced against the employee.

8 Analysis

Parties to an employment contract essentially enter into such a contract freely and voluntarily. There is therefore an obligation on the parties to abide by the terms of such an employment contract. Whether an undertaking not to compete with your employer's business is included by way of an ancillary agreement or it forms part of the employment contract as a clause, parties need to honour the provisions of such restrictive covenants. Failure to do so without justifiable reasons allows an employer to apply for an interdict and any other applicable remedies for breach of a restrictive covenant. The court correctly interdicted the first respondent from continuing to breach the restrictive covenant.

Post-democracy and with the adoption of the Constitution, it has become customary for courts to consider public policy when adjudicating disputes arising from private agreements. Although the employment contract is a private formulation between employer and employee, whenever there is a dispute arising out of such a contract, the court considers the broader interests of society. In the case under review, the court has properly done this by decisively holding that the enforcement of a restraint-of-trade clause is not contrary to public interests. This pronouncement by the court is crucial considering that public interests and policy are key considerations in determining the legality of non-compete agreements. Failure to prove that a non-compete agreement is against public policy will result in the court enforcing such restraint clause or agreement.

The first respondent objected to the enforcement of the restrictive covenant. Ordinarily, the restraint denier is required to provide reasons why a restrictive covenant should not be enforced. However, counsel for the first respondent did not adequately set out the grounds on which he relied in challenging the enforcement of the restrictive covenant. The grounds raised – namely, (a) the youth of the first respondent; (b) the short amount of time he had worked there; (c) the fact that he was not a senior employee; and (d) his dissatisfaction with his job and the circumstances surrounding it – were not sufficient to deny the restrictive covenant. These grounds could be ancillary grounds but could not be said to be the main grounds for having the restrictive covenant set aside. A display of facts and evidence proving the unreasonableness of the restrictive covenant could have enhanced the first respondent's arguments. Furthermore, the argument that the enforcement of the restrictive covenant would be contrary to public policy should have been adequately debated. Simply arguing that a restraint is contrary to public policy without substantiated evidence is futile, as in the case under review.

At face value, restrictive covenants may seem unnecessary to prevent an ex-employee from pursuing the career or occupation of their choice.

However, a proper analysis of a non-compete agreement suggests that there is sometimes a need to protect an employer's business interests, especially where the employer has interests worthy of protection (*Basson v Chilwan supra*). Both the employer and the employee have commercial and monetary interests, and both need protection. The employer and the employee each need first to establish their interests and to provide evidence justifying the protection of such interests. The employer has commercial interests and desires to protect its business-related assets such as trade secrets, whereas the employee intends to earn a salary through finding new or different employment. Failure to establish commercial and monetary interests and the need for protection of same will result in either the employer or the employee being denied protection of such commercial or monetary interests.

9 Concluding remarks

Employees must not enter into employment contracts and non-compete agreements in haste. Owing to the nature of contracts, and surrounding principles such as sanctity of contract and the *caveat subscriptor* rule, employees risk being held to non-compete agreements they have signed.

Although not expressly apparent from the judgment, employers should also exercise caution when drafting employment contracts and restraint-of-trade agreements, and should pay attention to whether such restraint agreements are included as a clause in the contract of employment or whether they are intended to operate ancillary to the employment contract. Furthermore, a careful consideration must precede any amendments to a contract of employment generally, or restraint-of-trade agreement specifically, since such changes could potentially and materially affect the conditions of employment. Needless to say, employment contracts and restraint clauses should be properly designed. The conduct of both employer and employee after drafting a non-compete agreement, as well as at the time of enforcement of such an agreement, will be considered by the courts when dealing with disputes in relation to such agreements.

What is unique and commendable about the case under review is the court's willingness to protect the interests of the employer. Although not the first case in which the interests of the employer have been found to outweigh those of the employee, it is commendable that courts continue to consider an employer's interests worthy of protection, contrary to popular belief that an employee's rights outweigh those of an employer. One cannot credibly argue against the fact that employees as a category have suffered severely at the hands of employers, and therefore require some protection. Thus, judicial officers must interpret and apply legal principles, both from statute and the common law, in a manner that recognises and promotes the rights of employees. However, this does not take away an employer's rights and

the protection that should be afforded to an employer in exercising and enforcing its rights.

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