

# ANALYSIS



## Restraint of Trade in Hong Kong

The approach of the common law to restraint of trade is an example of commercial reality being incrementally determined by 'public policy' issues. The conflict in these public policy issues has been an element in the development of English (and Hong Kong) law since the 'classic' economic theories of Adam Smith provided the framework for and against English theories of freedom of contract in the nineteenth century.<sup>1</sup> One important question, of particular relevance to the 1997 transition period and the development of Hong Kong law, arises from recent Hong Kong decisions on restraint of trade: what is the public interest underlying the courts' decisions in this area of the law, and by extension how do judges choose among competing public interests when required to make such decisions?

This article examines the issue of public policy in and restraint of trade by contrasting the underlying influence of the English medieval theological doctrine of the sacred duty to work, and the resulting abhorrence of the idea of restraint of trade, with three Hong Kong cases on restraint of trade that emphasise the flexibility of the judges' interpretation of public policy issues. The existing model of restraint of trade case law thus indicates a trend towards a general doctrine of inequality of bargaining power that could be described as a sixth category of public policy decisions appearing in Hong Kong.<sup>2</sup> The judges are creating a new head of public policy based on the unconscionability of a bargain and the inequality of the bargaining power of the parties to the contract, and making a commercial practice expedient which formerly was in Lord Macnaghten's words 'mischievous to commerce.'<sup>3</sup>

### The traditional English medieval influence

St Thomas Aquinas' divine divisions of work as the consequence of a divine providence meant that every member of society had 'a duty to serve God in the estate or degree in which he found himself.'<sup>4</sup> Two consequences emerged from the Church's medieval view of a person's allotted place in society: there was a

<sup>1</sup> For a detailed discussion of the 'classical age' of the political economist and the English law of contract, see P S Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford: Clarendon Press, 1979), pp 292–448.

<sup>2</sup> The five categories of public policy heads currently recognised are objects which are: illegal; injurious to good government; interference with the proper working of the machinery of justice; injurious to morality and marriage; and economically against the public interest. A sixth head may in fact be emerging from Hong Kong cases on restraint of trade.

<sup>3</sup> *Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co Ltd* [1894] AC 535, 566.

<sup>4</sup> *Summa Contra Gentiles* III, C44 quoted in A W B Simpson, *A History of the Common Law of Contract* (Oxford: Clarendon Press, 1975), p 520.

duty to work and the medieval legal system made it a criminal offence to move out of such an ordained economic status. The rigidity of the Church's system of the social order, and the recognition of the duty of individuals to work in the trade to which their social status placed them, resulted in the complex logic that any restraint of trade clause enforced idleness and poverty. In Hong Kong the approach of the common law to restraint of trade continues to display the essentially medieval Christian influence on the doctrine, although expressed in the secular language of commercial necessity and public interest.

*Partial and general restraint of trade*

The sixteenth-century cases on restraint of trade thus rested upon the notion of a duty to work, and upheld a rigorous Church tradition emphasising the rigidity of the social system.<sup>5</sup> The more 'modern' approach was developed by Coke CJ in *Rogers v Parrey* (1614)<sup>6</sup> in which Coke distinguished on the particular facts of the case between the restriction of the use of particular property and a general restriction on the use of property. In reply to comments that enforcing the defendant's promise not to exercise or to permit the trade of joiner to be exercised on the adjacent property would prevent the defendant from exercising his trade, Coke CJ held that this particular promise was for 'a time certain and in a place certain, but that no general restraint there is here.'<sup>7</sup>

The distinction drawn by Coke CJ between partial and general restraints of trade survived until 1894 when *Nordenfelt*<sup>8</sup> recast the question in terms of the reasonableness of the covenant against restraint of trade. The basic principle, however, established in the fourteenth-century canon of Christian medieval theological doctrine remains a characteristic influence in English and Hong Kong common law — agreements in restraint of trade are prime facie void.

**Freedom of contract and the doctrine of the harmony of interests**

The distinction between partial and general restraints of trade played an important role in the extension (by the common law) of the economics of freedom of contract into contracts in restraint of trade. *Rogers v Parrey*<sup>9</sup> is an

<sup>5</sup> Simpson, *ibid*, quotes Thomas Becon's catechism of 1531 as an example of medieval thought on politics and economics: 'The subject is called to God to obey, and to be in subjection to his superior and every one of them is bound by the commandment of God to live in their vocation. The lawyer in pleading and defending poor men's causes, the shoe-maker in making shoes, the tailor in making garments ... and so forth in all persons, in whatsoever state God has called them. Every man in his vocation ought to labour and by no means be idle.'

<sup>6</sup> 2 Burst 136, Cro Jab 326. The facts of the case were that the defendant (a joiner) owned an adjacent property. While leasing property from the plaintiff, the defendant had been paid ten pounds not to exercise or permit the trade of joiner in the adjacent property for 21 years. The defendant subleased to a joiner in breach of the 21 year covenant, and the plaintiff successfully bought an action for breach of promise.

<sup>7</sup> *Ibid*, p 329 (Cro Jab), per Coke CJ.

<sup>8</sup> Note 3 above.

<sup>9</sup> Note 6 above.

example of the seventeenth century's common law approach to the conflict between restraint of trade and the principles of freedom of contract, establishing that it may in fact be in the interest of an individual to be able to make legally enforceable contracts *not* to carry on their own business at a certain time or place, particularly when they wished to sell the goodwill of a business.<sup>10</sup> The issue of restraint of trade thus became subsumed by doctrines of public policy, ultimately shifting away from the interests of the parties to those of the public with the high point of the enforceability of restraint of trade clauses reached at the end of the nineteenth century with *Nordenfelt*.

The House of Lords ruled that the primary requirement as to enforceability was the reasonableness of the covenant, and was technically echoing the view of Tindal CJ in 1831 when he summed up the approach of the common law: 'Contracts in restraint of trade are in themselves, if nothing more appears to show them reasonable, bad in the eye of the law.'<sup>11</sup> However, the decision suggests that the nineteenth-century English courts had adopted a new approach to commercial organisations which were deemed to be the best judges of whether the agreement containing the covenant was in their best commercial interests. Furthermore, in *Nordenfelt* the courts adopted 'in a somewhat new form, the old economic theory of the harmony of interests'<sup>12</sup> when considering the question of the public interest. What is meant by the 'old economic theory of the harmony of interests' is the eighteenth-century solution to the moral questions of the private rights and the public good (raised by obvious inequalities of great wealth and poverty and the institution of property itself).

The sympathy of the late nineteenth-century English judges for freedom of contract<sup>13</sup> extended philosophically from the nineteenth-century decisions based on the public's economic interest in the enforceability of restraint of trade clauses in contracts between vendor and purchaser of the *Nordenfelt* type into cases with more overtly political public policy implications. By 1942 an economist commented that the courts could discover new freedoms for business to charge whatever prices it saw fit, to hold the public to ransom without interference from the courts, and to combine with each other using their own workers and the workers of any other industry who belonged to the same union.<sup>14</sup>

<sup>10</sup> This approach was further developed in the case of *Mitchel v Reynolds* (1711) 1 P Wms 181, 24 ER 347, one of the 'modern' authorities on the enforceability of partial restraint of trade clauses.

<sup>11</sup> *Homer v Graves* (1831) 7 Bing 735, 744.

<sup>12</sup> Atiyah (note 1 above), p 699.

<sup>13</sup> Atiyah (note 1 above, p 699) suggests that the courts assisted in the destruction of freedom of trade by their pursuit of freedom of trade, reflecting public opinion and judicial sympathy with the doctrine of freedom of contract.

<sup>14</sup> See *Crofter Hand Woven Harris Tweed Co Ltd v Veitch* [1941] AC 435 and the comments of W Arthur Lewis quoted in Atiyah (note 1 above), p 701.

Since 1945, 'public opinion' has swung the other way and, assuming that the judges 'represent' public opinion (rather than creating it themselves), the decision of the House of Lords in *Esso Petroleum Co Ltd v Harpers Garage (Stourport) Ltd*<sup>15</sup> was the culmination of such a change in attitude. Statutory intervention such as the Fair Trading Act of 1973, and the Restrictive Practices Act of 1976 (discussed below), designed to prevent excessive freedom of trade from damaging the consumer, was the further high point of the legislative expression of public opinion. The next section examines how Hong Kong has resolved the tension between the freedom of trade and freedom of contract in contrast to developments in the United Kingdom.

### Hong Kong's freedom of trade versus freedom of contract

The categories of restraint of trade covenants can be divided into three distinct types of agreements. First, agreements between traders or by employees or professionals as to their business methods such as agreeing the sale price of goods, wages, hours of work, terms of employment, and discounts on services. Second, the vendor/purchaser agreements in which the vendor of a business undertakes not to compete with the purchaser of its goodwill. Third, agreements by an employee not to set up a rival business terminating the contract of employment and not to join a rival business in direct competition with the employer. Each of the three distinct types of covenants in restraint of trade will be dealt with separately, highlighting the economic interests protected in each case in terms of public policy, and examining the available common law principles in Hong Kong that form the substratum of the public policy issues addressed by the judges.

#### *Cartels, monopolies, and restrictive practices*

There is no Hong Kong legislation or administrative control over the area of economic competition, monopolies, and restrictive practices other than the application of common law principles in the interest of 'public policy.' The current Hong Kong debate focuses on restrictive practices involving supermarkets, banking, telecommunications and broadcasting, gas supply, and financial services. The Consumer Council has produced reports on banking<sup>16</sup> and supermarkets<sup>17</sup> for public discussion, raising questions that consumers have the right to investigate Hong Kong's competitive environment and current market practices and to promote fair competition in the interests of consumers. Until

<sup>15</sup> [1968] AC 300, [1967] 1 All ER 699. The House of Lords held that, despite being exclusive 'solus' agreements, these agreements were in fact within the restraint of trade doctrine. The agreement for four and a half years was thought to be reasonable and therefore in the interests of the public and valid. However the 21 year agreement was thought to be unreasonable and contrary to public interest.

<sup>16</sup> Consumer Council, *Report on the Banking Industry* (November 1994).

<sup>17</sup> Consumer Council, *Report on the Supermarket Industry* (November 1994).

legislation is introduced, possibly as a result of pre-1997 discussions on fair competition and the public, the existing common law principles described below form the basis for Hong Kong public policy on this issue. By contrast the Restrictive Trade Practices Act of 1976 ('RPTA') in the UK, for example, provides that agreements relating to goods and services are *presumed* to be against the public interest unless it can be shown that they provide one or more benefits which outweigh any detriment to the public interest.<sup>18</sup>

As to agreements regarding hours of work and terms of employment, Hong Kong-style restraint of trade agreements of this nature are limited to the regulation of the professions and their self-regulating governing bodies such as the Law Society, the Bar Council, or the Hong Kong Society of Accountants charged with the duty of the admission of their own professional members and the setting of the 'appropriate' professional standards.

Other than the restrictive practices encouraged by and protected by the legislation relating to the Hong Kong professions, public policy on this type of restraint of trade is not currently an issue for discussion in Hong Kong.

#### *Vendor/purchaser agreements*

The second type of covenant in restraint of trade concerns the purchaser of a business who purchases the goodwill from the vendor and requires a covenant from the vendor not to compete. Traditionally this type of vendor's covenant has been regarded as being in the economic interests of the parties concerned and therefore reasonable if the covenant covers only the subject matter of the sale itself, that is, the *goodwill* of the particular business. *Nordenfelt* is still the classic statement of the law on this subject, and Lord Macnaghten's test must therefore be examined closely:

The true view at the present time I think, is this: The public have an interest in every person carrying on his trade freely: so has the individual. All interference with individual liberty of action in trading and all restraints of trade of themselves, if there is nothing more, are contrary to public policy, and therefore void. That is the general rule. But there are exceptions: restraints of trade and interference with individual liberty of action may be justified by the special circumstances of a particular case. It is a sufficient justification, *and indeed it is the only justification, if the restriction is reasonable* — reasonable that is in reference to the interests of the parties concerned and reasonable in reference to the interests of the public, so framed and so guarded as to afford adequate protection to the party in whose favour it is imposed while at the same time it is in no way injurious to the public.<sup>19</sup>

<sup>18</sup> s 43, RTPA.

<sup>19</sup> Lord Macnaghten, [1894] AC 535, 565 (HC) (emphasis supplied).

There are two aspects to Lord Macnaghten's test: is the restraint in the interest of the parties? If yes, then is it also in the interests of the general public? The difficulty, however, lies in deciding what constitutes the public's interest. Does this mean the liberty of the subject, or freedom of trade, freedom of contract, or general economic utility? One hundred years later in Hong Kong, *Nordenfelt* leaves a legacy of unanswered questions and a possible tautology inherent in Lord Macnaghten's test. What is in the interests of the parties may also, paradoxically, be in the public interest.

*The employer/employee restraint of trade*

The trilogy of Hong Kong cases, *Deacons (a firm) v Bridge*,<sup>20</sup> and cases against John Edwards<sup>21</sup> and Koo, Hoi, Yan and others<sup>22</sup> involving the solicitors Kao Lee and Yip, fall into the employer/employee category of restraint of trade clauses. The three cases concern a 'partner' retiring from a partnership of solicitors and focus on the test devised by Lord Macnaghten: what is *reasonable* in respect of the geographical scope and duration of a restraint of trade clause must both give adequate protection to the parties and in no way injure the public.

*Deacons (a firm) v Bridge*

Robin Bridge had been a full capital partner in the firm of Deacons for over eight years from April 1974 until December 1982. Upon leaving the firm, Bridge set up in competition as a solicitor in Hong Kong in breach of the partnership agreement he had entered into in 1974. The agreement contained a specific clause restricting a retiring partner from acting as a solicitor in Hong Kong for five years for any *client of the firm*, including anyone who had been a partner of the firm for the three years immediately before the partner retired. Deacons took out injunctions to prevent Bridge from, first, soliciting clients, second, inducing employees of the firm to break their contracts of employment with Deacons, and third, acting for clients of the firm in breach of the restrictive covenant in the partnership agreement. The appeal to the Privy Council was limited to the first and central issue of the *enforceability* of the restraint of trade clause against Bridge acting for clients of the firm, with the two subsidiary injunctions being dependent upon the enforceability of the restraint of trade clause.

The Privy Council characterised the case as a partnership agreement case and focused on the contents of the *entire* partnership agreement, in particular upon clause 8(a) of the agreement providing that 'the assets of the partnership including goodwill and all furniture, safes, boxes, equipment, fitting, stores and

<sup>20</sup> [1984] 1 AC 705.

<sup>21</sup> *Kao Lee & Yip (a firm) v Edwards* [1994] 1 HKLR 232.

<sup>22</sup> *Kao Lee & Yip (a firm) v Koo, Hoi, Yan* (1994) CA, Civ App No 20 of 1994.

books held or used for or in connection with the practice ... *belong to the partners in proportion to their respective shares.*<sup>23</sup>

Bridge argued that the consideration paid to him upon retirement for the goodwill of his share of business was inadequate and thus invalidated the restraint of trade clause. The Privy Council agreed that this was not a vendor/purchaser situation, where protection against competition by the vendor can be justified because *'it will enhance the price he receives for the business.'*<sup>24</sup> Rather the Privy Council held that this partnership agreement was closer to an employer/employee situation, and that while adequacy of consideration was indeed important, the adequacy of the consideration (and hence the reasonableness of the restraint of trade clause) must be considered in relation to the contract signed in 1974 and not upon retiring in 1982. Therefore, the restrictive covenant was held to be enforceable against Mr Bridge.

The reasoning of the Privy Council is an interesting example of the argument in favour of freedom of contract and was expressed specifically in terms of the economic interest of society as a whole. A new partner joining a firm is not normally in a position to pay the full market share for the goodwill of the business. The charging of new partners a *nominal sum* enables these partners to pay this nominal sum gradually over a period of time out of their share of the profits while deducting drawings for their current use. It is therefore both practical and reasonable that, upon retiring, only a nominal sum should be paid out for the retiring partner's share of the goodwill. How is making the covenant enforceable in the public interest? It encourages new blood into the profession and it benefits clients by securing continuity in the practice. The case therefore appears to fall directly within Lord Macnaghten's special circumstances of a particular case. However, it does not come within the usual employer/employee type of agreement, focusing instead on the adequacy of consideration for the goodwill of the business.

The case did not, however, fall within the usual type of employer/employee relationship where the prime consideration applicable is the hostility expressed towards restraint of trade since the fourteenth century's medieval theological doctrine on the subject took such a firm hold on the common law judges. Nevertheless *Deacons* illustrates the point at which the interest of the public coincides with the interests of the parties on public policy considerations concerning economic rights and the protection of freedom of contract in the commercial world. The two cases involving the firm of solicitors Kao Lee & Yip by contrast illustrate the emergence of a new head of public policy in Hong Kong law, the unconscionability of a bargain in relation to the inequality of the parties' bargaining power.

<sup>23</sup> Note 20 above, p 709 (emphasis supplied). This is the argument used to justify the line of cases following *Mitchel v Reynolds* (1711) 1 P Wms 181, [1558-1774] All ER Rep 20, 24 ER 347, and culminating in *Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd* (note 15 above).

<sup>24</sup> Note 20 above, p 711.

*Kao Lee & Yip v John Edwards*<sup>25</sup>

In the case of Mr John Edwards, a salaried partner in the firm Kao Lee & Yip since 1989, the partnership agreement contained a restrictive covenant similar to the restrictive covenant in *Deacon*. There was, however, one important exception. In the restrictive covenant in *Deacons*, a partner was restricted from practising in Hong Kong. In the Kao Lee & Yip partnership agreement the restriction was world-wide. The plaintiff argued that the covenant was merely designed to protect their goodwill, and that such protection is within their legitimate interests (provided that it is reasonable). The defendant argued that since there was a lack of equal bargaining power between the equity partners and the salaried partners there was no mutuality of benefit on the contract as evidenced in the *Deacons* agreement. The reality of Mr Edwards' position was that of employee; as a salaried partner he had no interest in the goodwill or assets of the partnership, nor did he share in the risks and benefits of the partnership. He was held out as a 'partner' of the firm but in fact his benefits were limited to a salary increase and a bonus payable at the discretion of Mr Kao and Mr Yip, the equity partners.

The plaintiff agreed that goodwill was the only legitimate interest to be protected but argued that the covenant was impliedly restricted to Hong Kong, and would indeed be reasonable if so restricted. The court, however, decided that the clause was worldwide, and thus unreasonable, and refused to substitute a lesser period for the five year restriction included in the covenant between the parties (despite the fact that, as will be shown below, in theory a court can sever the offending words if thereby the clause can be saved). The Court of Appeal upheld the decision of Jones J, and commented that 'it seems to us that the 5 year restraint is aimed at stifling competition, deterring the defendant from leaving the firm, rather than the protection of the firm's goodwill.'<sup>26</sup>

*The question of severance in Hong Kong*

The question of severance was not specifically addressed but it is important to note that the general rule laid down in *Pickering and Ilfracombe Ry*<sup>27</sup> in 1868 is still good law in Hong Kong as in England. The general rule is that 'where you cannot sever the illegal from the legal part of a covenant, the contract is altogether void; but where you can sever them, whether the illegality be created by statute or by the common law, you may reject the bad part and retain the good.'<sup>28</sup>

There are two well-known principles relating to this general rule. First, the courts will not re-write an existing contract if it alters its essential nature.

<sup>25</sup> Note 21 above.

<sup>26</sup> Note 21 above, p 16 per Litton JA.

<sup>27</sup> (1868) LR 3 CP 235.

<sup>28</sup> *Ibid*, p 250.



Second, the courts will not sever the unenforceable parts of a contract unless it accords with public policy to do so. The Court of Appeal found in Mr Edwards' restrictive covenant that it was *not* in the interests of public policy to sever or 'blue-pencil' the offending parts of the clause. There is a clear distinction between the vendor/purchaser covenant typified by *Goldsohl v Goldman*<sup>29</sup> in which the offending words could be severed, and the employer/employee relationship in which it is against the interests of one of the parties and hence not in the interests of public policy to do so. It is a pity that the Hong Kong Court of Appeal did not consider the 'modern' approach to severance and restraint of trade clauses in this context.

*Kao Lee & Yip (a firm) v the six 'equity partners'*

The second *Kao Lee and Yip (a firm)*<sup>30</sup> case involved six defendants who had signed a partnership agreement setting out the rights of 'the founding partners' and the 'equity partners.' The equity partners were in a distinctly inferior position in that the founding partners had the right *inter alia* to choose the partnership name, to set aside up to 50 per cent of the total profits of the partnership for any financial year for distribution according to their own discretion, to increase or to reduce the share of profits of the equity partners, and to admit new partners without the consent of the equity partners. Perhaps more significantly the founding partners could oust the equity partners by twelve months' notice, but not vice versa, and equity partners alone were restricted from engaging in any other trade or business. The Court of Appeal was not criticising the founding partners' arrangements, but noted that the arrangement was clearly one-sided, and thus material to the question of the enforceability of the restrictive covenant in restraint of trade (modelled once again on the *Deacons* clause).

Unlike Mr Edwards, whose partnership agreement had been called a 'Salaried Partnership Agreement,' and which Mr Edwards had signed *qua* salaried partner, here the six defendants had a partnership agreement intended to cover the rights of both 'equity' and 'founding' partners. The Court of Appeal examined the restrictive covenants against poaching of clients and poaching of employees from the perspective of the protection of some legitimate interests of the plaintiff, Kao Lee & Yip. However, even if restraints against poaching either the firm's *clients* or its *employees* could be shown to be reasonably necessary for the protection of some legitimate interest of the plaintiffs, they are unenforceable if shown (by the defendants) to be against the public interest.

The offending employment and client poaching clauses will now be examined separately to assess the public policy issues raised by the Court of Appeal.

<sup>29</sup> [1914] 2 Ch D 603.

<sup>30</sup> Note 22 above.

*The employee poaching clauses*

The following is an extract from the 'salaried partnership agreement' of Kao Lee & Yip entered into by the six defendants upon joining the firm as 'equity partners' and quoted in the Court of Appeal judgment:<sup>31</sup>

- 16b. Upon any partner ('the outgoing partner') ceasing to be a partner of the partnership for any cause whatsoever, the outgoing partner shall not for the space of 5 years directly or indirectly: ...
- ii employ or engage any person who shall have been an employee of the partnership (which expression includes the partnership practice of *Kao, Lee and Yip* carried on before a period of 3 years immediately the date of such cessation.

The Court of Appeal pointed out that this was not a clause prohibiting enticement or solicitation of employees by a former partner of the firm, but was a restraint against employment of former employees of the firm under any circumstances. Thus it was a naked restraint against legitimate competition and limits quite unjustifiably 'the extent to which the person subject to the restraint can legitimately compete in the labour market against those seeking to enforce it against him.'<sup>32</sup> The court relied on the line of argument established in *Kores Manufacturing Co v Kolok*<sup>33</sup> (and later endorsed by Lord Reid in *Esso Petroleum*).<sup>34</sup> In *Kores Manufacturing* the parties had agreed that neither would employ any man who had left the service of the other. However, although this might be in the interest of the contracting parties, it could well be against the public interest to interfere with the freedom of the employees. The law would not therefore countenance such an agreement by enforcing it. Unfortunately, the difficult question as to whether employees constitute an asset of the business and therefore a legitimate interest of the employer capable of being protected from enticement or solicitation did not have to be pursued further by the Court of Appeal since the 'employee restraint' in question did not contain the words 'solicit' or 'entice,' but was a restraint against employment under any circumstances.

The obvious difficulty raised by the two conflicting English decisions on 'enticing' or 'soliciting' employees from an employer in *Ingham v ABC Contract Services Ltd*<sup>35</sup> (in which the employees were considered to be an asset of the employer who therefore had a legitimate interest in protecting them from poaching), and *Hanover Insurance Brokers Ltd v Schapiro*<sup>36</sup> (in which it was held

<sup>31</sup> Note 22 above, per Godfrey JA.

<sup>32</sup> *Ibid.*

<sup>33</sup> [1957] 1 WLR 1012.

<sup>34</sup> Note 15 above.

<sup>35</sup> (English) Court of Appeal (unreported), 12 November 1993.

<sup>36</sup> (English) Court of Appeal (unreported), 12 August 1993.

that the staff are not assets like apples, pears, or stock in trade) remain unresolved in Hong Kong employment law. Perhaps this particular 'unruly horse' of public policy, to use Lord Pearce's metaphor in *Esso Petroleum*,<sup>37</sup> illustrates that there is no separation between what is reasonable on the grounds of public policy and what is reasonable as between the parties. However, in the Hong Kong context the question of reasonableness in the *Nordenfjelt* test does not appear to encompass the wider issues either by virtue of restrictive practices legislation or by investigation from the court itself. It seems to bring us back full circle to the doctrine of the harmony of interests and the nineteenth-century philosophical approach to freedom of contract. In addition to the 'unruly horse' of public policy and the unspoken conflict of the harmony of interests debate, the Court of Appeal then turned to the question of the poaching of clients by the defendants against whom the plaintiff sought to enforce the restrictive covenant.

#### *Poaching of clients*

The following is an extract from the partnership agreement signed by the six defendant 'equity partners' in the firm of Kao Lee & Yip:

- 16(b) ... the outgoing partner shall not for the space of 5 years from the date of such cessation directly or indirectly:
- i solicit legal business from or do any work or act normally done by solicitors, for any person or firm or corporation who or which shall have been on client of the partnership (which expression includes the partnership practice of Kao, Lee & Yip being carried on before the commencement date) within a period of 3 years immediately preceding the date of such cessation PROVIDED always that the foregoing restrictions shall not apply to anything at any time done by the outgoing partner professionally for himself or for any member of his family or for the personal representatives or trustees of any such member.<sup>38</sup>

The Court of Appeal considered that this restraint of trade went far further than necessary to protect the plaintiffs' legitimate interests, and focused on two specific questions first put by Lord Reid in the *Esso Petroleum* case:<sup>39</sup> first, what were the plaintiffs' legitimate interests? In the case of a firm of solicitors, *Deacons* illustrates that the clients are thought to be a legitimate asset — a part of the firm's valuable goodwill that the firm can legitimately protect. Second, are the restraints more than adequate for the purpose of protecting those

<sup>37</sup> Note 15 above, p 724 per Lord Pearce.

<sup>38</sup> Note 22 above, per Godfrey JA.

<sup>39</sup> *Ibid*, p 709.

legitimate interests or do they go further than is reasonably necessary? There is a wide spectrum of infinite shades or variety of relationships in the restraint of trade cases, and on the facts of these particular equity partners the partnership agreement was closer to the employer/employee relationship than the mutuality of dealing reflected in the partnership arrangement found in *Deacons*. Thus the court would be slow to find harsh provisions fair or reasonable if clearly one-sided and in the interests of the stronger party.

### Conclusion

The Court of Appeal's approach in the case of *Kao Lee & Yip* and the six equity partners described above underlines an apparent trend in Hong Kong law towards a general doctrine of inequality of bargaining power. It is an interesting development in the overlap of equity's jurisdiction to relieve the unconscionable and unfair terms imposed upon the weaker party (as demonstrated clearly in *Multiservice Bookbinding v Marden*)<sup>40</sup> and the common law's jurisdiction to declare a contract unenforceable as being in restraint of trade. The overlapping of these two jurisdictions was emphasised in *Panayiotou v Sony Music Entertainment (UK) Ltd.*<sup>41</sup> The entertainer George Michael claimed that his contracts with Sony Music were void because they were in restraint of trade, and thus unenforceable. In the circumstances the claim was unsuccessful. However, the argument has been accepted and canvassed successfully in *Macaulay v A Schroeder Music Publishing Co Ltd*<sup>42</sup> in which Lord Diplock looked at the reasoning of nineteenth-century judges and at the lip-service paid to current economic theories of Bentham and laissez-faire economic philosophy, but found that they struck down a bargain if they thought it to be unconscionable as between the parties. Lord Diplock was saying nothing inconsistent with the public policy principle laid down in *Esso Petroleum* (clearly identified as freedom of trade). However, the two lines of authority are not, as yet, treated as a single homogenous jurisdiction. Nevertheless, this apparent development towards a homogeneity of jurisdiction is an important identifiable trend in Hong Kong law, and should be more clearly articulated to assist in defining the social and political objectives of Hong Kong law.

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<sup>40</sup> [1979] 1 Ch D 84.

<sup>41</sup> [1994] Ch 142, [1994] 2 WLR 241, [1994] 1 All ER 755.

<sup>42</sup> [1974] AC 1308, 1315 per Lord Diplock.

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