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NEWS

Company pays for employee breach of duty

We are commonly asked about the rights and obligations of both the employer and employee when someone who has had access to confidential information moves to a competitor. While typically the focus is upon the parties to the employment relationship, a recent Supreme Court case brings into focus the potential liability a new employer can suffer.

Here, partner Selina Nutley and lawyer Sarah Sherman explain how the Court ordered the new employer (Dreamtime Supply Company) to account for profits it received over two years to the tune of \$1.18 million after an employee breached its contract with a former employer (Steadfast ICT Security).

THE CLAIMS

Steadfast claimed two of its former employees, along with a former director, Mr Peak, copied confidential information and transferred commercial arrangements to Dreamtime whilst still employed at Steadfast.

Steadfast obtained a forensic computer analysis showing Mr Peak downloaded over 7,500 files from Steadfast's IT system, including client details, proposals and reseller agreements.

Mr Peak was also said to have destroyed files and data on Steadfast's Google Workspaces account, including quotes, proposals, emails archives and employee timesheets on departing his employment.

Mr Peak was accused of breaching the restraints in his employment contract and his fiduciary duties as a former director to act with honesty, care and skill, and in Steadfast's best interest.

Steadfast claimed it suffered a loss of clients, customers or suppliers, loss of income from those sources, and reputational damage.

Not only did Steadfast commence proceedings against Mr Peak and the other two employees, it also named Dreamtime as a defendant. Steadfast said Dreamtime had participated in the employee's plans to transfer business away from Steadfast and had knowingly:

- obtained the clients, customers and/or suppliers of Steadfast
 - obtained and used Steadfast's confidential information and intellectual property
 - profited at Steadfast's expense
 - had the use and benefit of the employees' services in breach of their contracts of employment.
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DECISION

At trial, Steadfast produced evidence, such as copies of correspondence, to support that a director of Dreamtime was aware of Mr Peak's plans, and that the plans would be a breach of his obligations to Steadfast. Steadfast could also prove up to eight of the lost clients were transferred directly to Dreamtime.

The Court upheld Mr Peak's restraint on the basis it was proportionate to his salary and his role as director, but said the restraints imposed on the other two employees were unreasonable and therefore unenforceable.

The Court said in knowingly receiving the benefit of Mr Peak's and Dreamtime's directors' scheme to transfer business away from Steadfast, Dreamtime participated in Mr Peak's breaches of his employment contract with Steadfast, including the restraint and other provisions relating to confidential information and intellectual property. Dreamtime was also a participant in Mr Peak's breaches of his fiduciary duties arising out of his role as director of the company.

The Court calculated Dreamtime had received \$1.18 million in profit as a result of the conduct, quantified by reference to contracts performed for entities with which Steadfast had a previous relationship, and it was ordered to pay that amount to Steadfast.

A WARNING FOR EMPLOYERS

This case serves as a warning for employers to exercise caution in accepting information from incoming employees that may cause the employee to be in breach of any duties owed to their former employer, including fiduciary duties or restraint of trade.

In particular, an employer should generally avoid accepting client details and contracts produced by the former employer unless the incoming employee can prove entitlement to the information. If an employer knowingly assists an incoming employee to breach those obligations, any profits earned may have to be repaid to the former employer.

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