The economic costs of restraint of trade agreements: modest lessons for South Africa from Germany and other selected jurisdictions

Musiiwa Mahangwahaya*

Mahangwahaya M. Attorneys Incorporated,
Louis Trichardt, South Africa
Email: mahangwahayamusiwa@gmail.com
*Corresponding author

Lonias Ndlovu

School of Law,
University of Venda,
Thohoyandou, South Africa
Email: lonias.ndlovu@univen.ac.za

Abstract: This paper considers the current legal position in South African labour law where employees subject to a restraint of trade agreement are not paid anything during the restraint's subsistence and face financial difficulties. When employees sign restraint of trade agreements, they undertake to surrender their ability to earn a living and not take advantage of other employment or commercial opportunities for a specific period, without getting any financial compensation as a means of survival during the subsistence of the period of restraint. After a detailed exposition of Germany's legal position and references to other similar jurisdictions, we recommend that South Africa learn from Germany and consider introducing mandatory compensation for employees who may find themselves rendered economically inactive by restraint of trade agreements.

Keywords: restraint of trade; compensation; freedom of trade; South Africa; Germany.

Reference to this paper should be made as follows: Mahangwahaya, M. and Ndlovu, L. (2021) 'The economic costs of restraint of trade agreements: modest lessons for South Africa from Germany and other selected jurisdictions', *Int. J. Private Law*, Vol. 10, No. 1, pp.47–64.

Biographical notes: Musiiwa Mahangwahaya graduated with his LLB in May 2017 and Master of Laws (LLM) in May 2019 from the School of Law, University of Venda, South Africa. His LLM dissertation was on the subject of the concurrent enforceability of restraint of trade agreements and garden leave in South African Labour Law. He served articles as a Candidate Attorney with Sonto Chawane Incorporated in Pretoria from February 2019 to February 2021. Musiiwa was admitted as an Attorney of the High Court of South Africa in May 2021. Currently, he is the Managing Director of Mahangwahaya M. Attorneys Incorporated, a Louis Trichardt-based law firm specialising in personal injury claims, family law, commercial law and labour law.

Lonias Ndlovu is currently the Dean of the School of Law at the University of Venda, South Africa. He previously worked at the South African universities of Fort Hare, Zululand and North-West, as a Lecturer, Senior Lecturer, and Associate Professor. He obtained his LLB in 2003 and LLM in 2005 from the University of Fort Hare and LLD in 2014 from the University of South Africa. His teaching and research interests generally lie in intellectual property law, intellectual property and public health, human rights and access to medicines, commercial law, and international trade law. He used to run a limited commercial law practice and regularly consults for government departments, international organisations and NGOs on intellectual property and public health. He supervised Musiwa Mahangwahaya's LLM dissertation.

1 Introduction

This paper compares the regulation of restraint of trade agreements in South Africa and Germany and the thematic lessons South Africa may learn. Although Germany's law does not apply in South African courts, the Constitution of the Republic of South Africa (hereafter Constitution)[1] urges courts to consider international law[2] and foreign law. In this context, the law of Germany is an example of this 'foreign law'. Germany applies Roman-Dutch law (civil law), which largely influenced the South African legal system's development.[3] The South African legal system is a mixture of Roman-Dutch and English Common law.[4]

In this paper, it is crucial to point out right from the onset that Germany's membership in the European Union (EU) implies an interplay between German restraint of trade rules and EU competition rules. Such interplay may amount to an incompatibility problem between EU competition law rules and the Common law restraint of trade doctrine.[5] The relevant EU laws implicated are Article 101 Treaty on the Functioning of the EU [TFEU] as implemented by EU Regulation 1/2003.[6] However, a detailed discussion of the interplay between German restraint of trade rules and EU competition rules is beyond this paper's scope.

The Constitution of the Republic of South Africa encourages courts to consider foreign and international law when interpreting the Bill of Rights.[7] Therefore, in the South African context, the legislature, courts, and the legal profession often adopt a comparative legal approach in developing, interpreting, and applying the law. The Labour Relations Act stipulates that South Africa should execute obligations binding on the Republic as a member state of the International Labour Organization.[8] Very importantly, South African courts often seek guidance from foreign judicial precedents.[9]

Landis and Grossett define restraint of trade as a form of an employment contract that imposes restrictions on an employee not to "work in competition with the employer by doing work for another employer or starting businesses in competition with the employer on leaving the employer's employ."[10] A similar definition was offered in *Petrofina (Great Britain) Ltd v Martin*[11], where a restraint of trade was defined as a contractual agreement between employer and employee imposing certain limitations on the employee's future activities or employment should they leave the employment.[12] In a restraint of trade agreement, the employee is restrained from using or making available trade secrets and trade connections to the former employer's direct competitors for a

specified time in a defined geographical area upon the employment contract's termination.

In South Africa, restraint of trade agreements have become prevalent in most current employment contracts. Some employers misuse restraint of trade agreements as a mechanism to discourage employees from fair competition.[13] Some restriction periods are more extended than necessary to protect the employer's legitimate interests and make employees economically inactive for inordinately long periods,[14] thus restraining them from taking advantage of the available employment opportunities upon leaving employment.[15] Unpaid restraint of trade agreements are open to abuse, and this paper endeavours to mitigate such abuses.

Three main issues have mostly pre-occupied South African courts concerning restraint of trade agreements. The first one is the absence of a legally prescribed maximum period of restraint. The discretion to determine the reasonableness of a period of restraint is left mainly to the presiding officer, who will endeavour to establish such reasonableness based on each case's facts.[16] Interestingly, in Germany, the maximum period of restriction set by law is two years.[17] The second related concern in the South African context is that the law seems to pay scant attention to the severity of the restraint's financial distress on former employees. In contrast, employers must pay former employees in Germany for rendering them jobless for the period the restraint subsisted.[18]

Thirdly, South African law does not acknowledge the realities of the parties' inequality in terms of bargaining powers in such agreements. Unpaid restraint of trade agreements tend to benefit employers by protecting their business interests and curbing competition. Therefore, unpaid restraint of trade agreements negatively affect former employees since they cannot work or open competing business enterprises while such restraints subsist.

Although South African jurisprudence in relation to restraint of trade agreements has some similarities with its counterpart in Germany, there are several important distinctions. German law differs from South African law in several respects. Most prominently is the prescribed duration of a restraint of trade after the termination of an employment agreement. Additionally, in terms of German law, the validity of a restraint of trade agreement, among other things, depends on whether the parties agreed on specific monthly monetary compensation.[19] Finally, unlike its German counterpart, South African law does not burden employers with the costs of rendering former employees economically inactive.[20]

This paper aims to address the abuse of unpaid restraint of trade agreements by advancing arguments for law reform that will culminate in South African law being developed to the extent of obligating employers to compensate former employees during the subsistence of restraints. The Common law doctrine of restraint of trade should be developed and harmonised to protect employers' and employees' legitimate interests effectively.

To effectively address the above aim, the paper commences with a brief outline of similarities and differences between the pertinent South African and German law on the subject. It thereafter proceeds to evaluate the points of difference between the two jurisdictions. The paper further explores the notion of obligatory financial compensation in restraint of trade agreements in Germany and opines on the concept's relevance to South Africa, alongside a discussion of other jurisdictions that deal with the

compensation question differently. After an expository account of the legal position in Germany and other cognate jurisdictions, the paper closes with an outline of lessons South African may learn and proposes that South Africa must consider compensating employees during restraint of trade periods, taking a leaf from Germany.

2 Enforcing restraint of trade agreements: similarities between the two jurisdictions

In both Germany and South Africa, the legal position is that restraint of trade agreements are *prima facie* valid and enforceable unless the party who wishes to avoid enforceability can prove that the restraint agreement is not aimed at protecting the legitimate business interests of the employer and is contrary to public policy.[21] Therefore, a restraint of trade agreement may not be enforced if an employee proves that the agreement does not protect the employer's legitimate business interests.[22]

In both jurisdictions, the applicable law acknowledges that the employer's legitimate commercial interests must be protected against exploitation.[23] Similarly, both jurisdictions confer the freedom of trade on employees, which includes the right to choose one's profession freely and make a living through the chosen career.[24] Restraint of trade agreements may only be enforced if they are reasonable *inter partes* (between employer and employee).[25]

In Germany, post-restraint of trade is imposed by a written employment agreement.[26] Although there is no legislative requirement that a restraint of trade agreement should be in writing under the South African law, courts enforce written restraint of trade agreements.[27] In light of the above, after the termination of the employment contract, an employer has no right to prevent a former employee from competing or being employed by direct commercial competitors unless a valid written restraint of trade agreement exists.[28]

In both jurisdictions, restraint of trade agreements restraining employees from trading outside the geographical area in which they materially served employment duties before the termination of an employment agreement are regarded as unreasonable and, therefore, unenforceable.[29] Thus, the geographical area of restriction should be limited to places where employers carried out the business before the employment contract termination and the area in which employees carried material employment duties.

Restraint of trade agreements are premised upon assuming equal bargaining power between parties in an employment relationship.[30] The time is ripe for South Africa and Germany to consider the realities of unequal bargaining power between employers and employees. There is no equality of bargaining power between employers and employees in restraint of trade agreements because employers control employees' economic freedom.[31] Employers utilise employees' known desperation for employment as a weakness and thus compromise the equal bargaining position *inter partes*.[32] In a bid to establish equal bargaining power between parties in restraint of trade agreements, the German legislature passed legislation making it obligatory for employers to pay employees for preventing them from earning a living during the subsistence of restraint of trade agreements.[33] Additionally, the legislation in question restricts the period of restraint to not more than two years.[34]

The following section sets out the differences in how restraint of trade agreements are enforced in Germany and South Africa regarding the preceding discussion. It is apparent

from the next section of this paper that there are specific lessons that South Africa may learn from Germany.

3 Enforcing of restraint of trade agreements: differences between the two jurisdictions

In Germany, restraint of trade law is codified.[35] Rules guiding restraint of trade agreements are laid down in statutes.[36] However, in South Africa, restraint of trade agreements are regulated by the Common law. There is no statutory provision in South Africa regulating the enforceability of restraint of trade agreements. Therefore, South African courts are guided by the Common law in their adjudication of restraint of trade disputes; hence, a reliable body of case law on the subject has steadily evolved.[37]

In terms of German jurisprudence, the maximum period of trade restriction is limited to two years.[38] Thus, any restraint of trade agreement preventing former employees from competing, freely exercising their profession, or being employed by former employers' direct commercial rivals after more than two years post-employment is unreasonable and unenforceable.[39]

However, there is no set maximum term applicable to the enforceability of restraint of trade agreements in South Africa. Thus, an employer may propose a restraint of trade period exceeding three years, and desperate employees in a weak bargaining position may sign such agreements. The above may be the case considering the high unemployment rate in South Africa, which stood at 32.6% in the first quarter of 2021 (15.0 million people without jobs).[40] South African courts determine the reasonableness of a restraint of trade period based on the facts of each case.[41] While it is laudable for South African courts to consider the facts of each case, we submit that South Africa can learn from Germany and consider setting a maximum reasonable restriction period. Restraint of trade agreements that prevent former employees from competing, freely exercising their profession, or being employed by their former employers' direct commercial competitors for more than two years seems unreasonable because restraint of trade agreements has the effect of depriving former employees of their rights to earn a living.

In Germany, employers must pay former employees for rendering them jobless during the restraint of trade period.[42] Such compensation is payable in monthly instalments, and it includes a consideration of contractual employment benefits.[43] Accordingly, German jurisprudence considers that people under unpaid restraint of trade may be under severe financial distress. Thus, a restraint of trade agreement is null and void and unenforceable if it does not include former employees' compensation.[44]

In contradistinction, South African jurisprudence does not consider the economic suffering that employees endure during the restraint period's subsistence. We submit that such a position is unconscionable, considering that former employees have everyday bills to pay. One may argue that unpaid restraint of trade agreements bring suffering to former employees and their families. There is a probable and not remote possibility that employers may abuse the restraint of trade agreements to avoid genuine competition.

The differences between the two jurisdictions are eye-opening, and it will be worthwhile to analyse the points of difference closely. Such further analysis is rendered immediately below.

4 Evaluating the differences between South African and German law

4.1 Inequality of the parties' bargaining powers in restraint of trade agreements

In terms of the principle of freedom of contract, parties to a restraint of trade agreement are free to make and enforce whatever legal terms (bargains) they wish against each other.[45] The principle of freedom of contracts binds parties who freely entered into contracts to honour the terms of their contracts.[46] Thus, courts ordinarily do not reshape or interfere with agreements voluntarily entered into by the parties.[47] The principle of freedom of contract also draws its support from the doctrine of the sanctity of contracts (*pacta sunt servanda*).[48] However, if an employee can raise a defence that they entered into a restraint of trade agreement under undue influence or without free will, such agreement may not be enforceable.[49] In terms of the principle of freedom of contract, parties in a contract who negotiated terms of their undertaking with equal bargaining power are bound to perform per their agreement.[50]

Bargaining power is the ability to negotiate, influence, or dictate an agreement's terms and conditions.[51] Parties with equal bargaining power must agree to the material terms of the contract.[52] In South African and German law, restraint of trade rules are premised on the assumption that employers and employees have equal bargaining power.[53] An agreement is unreasonable and unenforceable if one party exploits the need, carelessness, or inexperience of another.[54] The law should protect employees in a weaker bargaining position against stronger employers who take advantage of employees' desperation and need to secure employment.

It is worth reiterating that in South Africa, unpaid restraint of trade agreements are enforced based on the assumption that there is equal bargaining power between employers and employees.[55] In the light of the above, restraint of trade agreements are *prima facie* valid and enforceable unless the employee can discharge the onus of proof by adducing evidence that proves that the agreement in question is unreasonable and inimical public interest.[56] The imbalance of bargaining power between employers and employees is a factor that should be considered together with other factors in determining public interest.[57] In other words, the inequality of bargaining power can negatively affect the enforceability of restraint of trade agreements.[58] Factors that should be taken into consideration in determining whether a restraint of trade agreement was entered into with equal bargaining power or free will are the following:[59]

- the experience and skills or lack of experience and skills of the employee
- the demand in the labour market for the employee's skills
- whether there is a high rate of unemployment
- the state of the economy and the unemployment rate
- personal circumstances such as family responsibilities that would place pressure on an employee in finding a job in a certain area
- the age of the employee (young people and people above 50 may find it more difficult to find employment).[60]

These factors may be regarded as equivalent to economic duress created by "illegitimate commercial pressure exerted on a party to a contract, which induces him/her to conclude the contract and amounts to a coercion of the will, which vitiates consent."[61]

The unequal bargaining power between employers and employees is primarily driven by the high unemployment levels in South Africa.[62] This dire unemployment situation has further been exacerbated by the COVID-19 pandemic, which has resulted in many job losses, especially in the tourism and informal sectors.[63] Many South Africans are in desperate need of employment. They have no bargaining alternatives available to them because they are economically dependent on employers for employment.[64] They are in a vulnerable position of taking employment without negotiating employment terms.[65] Employers take advantage of the employees' desperation for employment and impose whatever employment contractual terms they wish without due regard to the impact of such terms on employees. Because of the high rate of unemployment, job seekers are in a take-it-or-leave-it situation.[66]

Parties to contractual agreements rarely enjoy equality of bargaining power.[67] Lord Justice Dillon observed that when a person wants to enter into a loan agreement, he urgently needs money and is inevitably in a weak bargaining position compared to a person from whom money is borrowed.[68] Lord Justice Dillon expressed the view that such a person is not in an equal bargaining position to negotiate terms of the loan with the lender; he will then take it or leave it.[69] Thus, in any contract entered into in circumstances of inequality of bargaining power between parties, courts should be reasonable in interfering with such agreements and prevent strong parties from exercising rights emanating from harsh bargains against the weak.[70]

A standard form contract prepared in advance in favour of employers is presented to job seekers to sign.[71] If the job seeker is dissatisfied with a particular term, employers cannot negotiate employment terms.[72] An employer will inform the job seeker to sign an agreement or remain jobless since many people wish to take the vacant position.[73] The job seeker succumbs and signs the contract to avoid the financial strain associated with joblessness.[74] In the circumstances described above, the employee's freedom of choice and enjoyment of equal bargaining power is equivalent to a fairy-tale.[75]

In a bid to balance the bargaining power, German jurisprudence imposes employers' obligation to compensate employees for agreeing to a restraint of trade deal.[76] An unpaid restraint of trade agreement is a one-sided deal that seeks to benefit only the employer to the employee's detriment.[77] Under the restraint of trade agreements, employees are prevented from opening competing business enterprises and working for the former employers' commercial competitors.[78] South African courts should be vigilant in dealing with the realities of unequal bargaining power between employers and employees. Employees are economically dependent on big corporates for employment.[79] These big companies exploit desperate individuals seeking employment by introducing harsh restraint of trade terms in employment contracts to maximise profits.[80]

It is unreasonable to impose the burden of proof on employees in a weaker bargaining position to employers.[81] Where employees are vulnerable due to their weaker bargaining power, employers must prove that the restraint of trade agreement in question is reasonable and enforceable.[82] The law should be developed and reformed to impose the burden of compensating former employees on employers to balance the bargaining position. Unpaid restraint of trade agreements seek to benefit employers by protecting their business interests and curbing competition. The reality of unequal bargaining power

between employers and employees cannot be swept under the carpet. It is unreasonable to assume that all restraint of trade agreements are *prima facie* valid and enforceable in light of the economic pressure employees are subjected to.

The reality of unequal bargaining power between employers and employees is aptly acknowledged by German law, which obligates employers to pay employees for preventing them from earning a living during the subsistence of a restraint of trade agreement. The period of restriction should not exceed two years.[83] In terms of English law, if an employee "willingly, though foolishly, accepts a bargain that includes oppressive terms, or where the stronger party exercises its rights under the contract in a manner that is harsh or unfair", then there is a possibility of courts pronouncing such agreements as unreasonable and unenforceable.[84]

The English Common law rules relating to restraint of trade agreements were developed, taking employees' unequal bargaining position into account.[85] In *Nordenfelt v Maxim Nordenfelt Guns & Ammunition*,[86] Lord MacNaghten emphasised that there is no equal bargaining power between employers and employees as opposed to a sale agreement between a buyer and seller.[87] Similarly, in *Mason v Provident Clothing Co Ltd*,[88] the court held that employers have more bargaining power than desperate employees seeking employment.[89]

South Africa must now come to terms with the reality that the bargaining power is uneven, and employees require protection from their ignorance in restraint of trade contexts.

4.2 The obligation imposed on employers to financially compensate employees for rendering them idle (jobless) during restraint of trade period

In Germany, a restraint of trade agreement is null and void and unenforceable if it does not stipulate compensation for restraint of competition to employees.[90] In terms of Section 74 (b) (1) of the German Commercial Code, an employer who places an employee on restraint of trade must pay the latter half of the remuneration they were recently receiving.[91] Restraint of competition compensation is payable in monthly instalments.[92] On this basis, the discretion remains upon employees whether to agree to receive lower restraint of trade compensation or immediately compete with a former employer upon termination of the employment relationship.[93]

In terms of Section 74 (1) (b) of the Commercial Code, the compensation for a restraint of trade competition includes bonuses.[94] Moreover, in determining restraint of trade compensation, courts consider all compensation elements under the employment agreement, including a fixed monthly salary, 'commission payments', and other employment benefits.[95] "For variable compensation elements such as performance-related payments, the average amount payable during the last three years of employment are taken into account."[96] When considering employment agreement benefits, courts consider the company car, company house that an employee was using, and payments in kind.[97] As previously stated, restraint of trade agreements that do not include compensation are not binding and unenforceable in Germany.[98] Similarly, restraint of trade agreements that provide for insufficient compensation are not binding.[99] However, an employee has the discretion of accepting to comply with such a restraint of trade agreement, negotiate for fair, adequate compensation, or whether not to be bound at all.[100]

The reasonableness of restraint of trade agreements differs from case to case. A restraint of trade agreement, which prevents an employee from exercising their trade for a

short period and in a small geographical area, may justify a minimum compensation amount.[101] Similarly, an employer may offer higher restraint of trade compensation to make the broader scope of restriction reasonable.[102] However, it is worth emphasising that the employer's offer of high restraint of trade compensation should not be used to render employees economically inactive for an inordinately long period.[103] In other words, restriction periods should not be more extended than reasonably necessary to protect the employer's legitimate commercial interest.[104]

4.2.1 Deduction of other earnings from the restraint of trade compensation

In terms of Section 74 (c) of the Commercial Code,[105] a former employee who is subjected to a restraint of trade agreement may work elsewhere provided that it is not in violation of such restraint agreement.[106] If a former employee receives remuneration from the new employer not in breach of restraint of trade agreement, then such former employee should allow the former employer to deduct earnings from the competition compensation due to them.[107] Furthermore, an employee must inform the former employer about his earnings when he claims restraint of trade compensation.[108]

In terms of Section 74 (c) of the Commercial Code,[109] when employers make deductions to the compensation due to employees, they should not deduct social security contributions.[110] One may raise the lingering question of whether unemployment benefits are deducible from the restraint of trade compensation due to a former employee. A literary interpretation of Section 74 (c) of the Commercial Code clearly shows that unemployment benefits should not be deducted from employees' compensation.[111] The above stems from the fact that employees receive unemployment benefits for being unemployed. Courts held that unemployment benefits should be deducted from the restraint of trade compensation.[112] Although unemployment benefits are not earnings received by people currently working, the Federal Labour Court held that such benefits have the effect of substituting a salary. Therefore, they should be deducted from the restraint of trade compensation due to former employees.[113]

We consider other jurisdictions that follow the same system of paid restraint of trade agreements like Germany in the section immediately below. These other jurisdictions are chosen to make a further case for South Africa to consider restraint of trade compensation in the future.

4.3 Other jurisdictions in which monetary compensation is a formal requirement for the validity of restraint of trade agreements

There are many other countries following a payment practice similar to the Germanic one. Good examples are the Czech Republic, Italy, Poland, Spain, Finland, the Netherlands, France, Belgium, Hungary, and Denmark. Most countries in which the validity of restraint of trade agreements depend on financial consideration require that employees be entitled to 50% of their monthly remuneration during the restraint period. How employees should be financially compensated differs from jurisdiction to jurisdiction. In some jurisdictions, former employees subject to restraint of trade agreements must be paid a lump sum as financial compensation. In this case, one singular once-off payment is made. Other jurisdictions require that the compensation be paid monthly until the period of restriction lapses.

4.3.1 Some jurisdictions in which monetary compensation is paid monthly

In some countries, employees should be financially compensated, and this compensation should be at least half of their average monthly remuneration for each month that the trade restriction applies. In other countries, the payment is restricted to 25%. This compensation should be paid monthly to make former employees since restraint of trade agreements mainly render former employees jobless or economically inactive. Example countries include, among other things:

- The Czech Republic: In the Czech Republic, the legal requirement is that employees should be financially compensated. This compensation should amount to half (50%) of their average monthly remuneration for each month that the trade restriction applies.[114]
- Italy: Italian jurisprudence does not specify the level of consideration or mode of payment required for restraint of trade agreements.[115] However, Parties ordinarily prefer restraint of trade compensation to be paid monthly to prevent former employees from starving.[116]
- Poland: The Poland position is that a restraint of trade agreement is invalid if employees will be compensated at an amount lower than 25% of their average monthly remuneration for each month that the trade restriction applies, including other contractual benefits.[117]
- Spain: In Spain, financial compensation can be made in monthly instalments depending on the agreement between the parties.[118] The relevant law further permits parties to agree on one lump sum compensation paid either at the commencement or at the end of the trade period's restraint.[119]
- Finland: In Finland, the law only imposes a compensation obligation on employers if the restriction period exceeds six months.[120] The law requires that employees be entitled to 'fair compensation', and the facts of each case determine this. Case law mainly indicates that 'fair compensation' is between 50% and 100% of the employee's average monthly remuneration.[121] Regarding the payment mode, parties may agree that the compensation is paid monthly or as a lump sum.[122]
- The Netherlands: Although the law does not demand that employees be compensated, a court may award monetary compensation for the period of restriction.[123] In this regard, an employee may file a request for financial compensation.[124]

4.3.2 Some jurisdictions in which monetary compensation is paid as a lump sum

- Belgium: The Belgian position is that employers must pay employees a lump sum compensation equal to half (50 percentage) of their gross remuneration for the period of restriction.[125]
- Hungary: In Hungary, financial compensation is an essential element of the validity of restraint of trade agreements.[126] In a case where parties entered into a restraint of trade agreement before 1 July 2012, the legal position directs that such employees are entitled to 50% of their gross remuneration for the period of restriction.[127] However, the new Labour Code of Hungary provides that for restraint of trade

agreements entered into from 1 July 2012, employees are entitled to at least one-third financial compensation of the remuneration that has to be paid for the restriction period.[128] For example, if a former employee is restrained from competing with the former employer for six months, such an employee is entitled to at least two months' salary.

- France: France also established a system of restraint of trade compensation.[129] Since 2002 the validity of restraint of trade agreements depends, among other things, on the employer's offer of financial compensation to former employees during the subsistence of the restriction period.[130] However, France's pertinent law does not set or prescribe a minimum restraint of trade financial compensation.[131] In practice, the Metal Industry Collective Bargaining Agreement provides for 60% of the average monthly total remuneration before the termination of the employment agreement as a minimum amount of compensation.[132] Thus any financial compensation below 60% to employees working within metal industry is invalid and unenforceable.[133] In a case where there is no relevant provision for restraint of trade financial compensation in the applicable collective bargaining agreement, and the contract of employment provides for unreasonably low compensation, the former employee may ask the court to assess the reasonableness of the granted compensation.[134]

Financial compensation of less than 15% of the monthly remuneration is unlikely to be found reasonable and valid.[135] 30% to 50% of gross monthly remuneration is likely to be considered reasonable financial compensation.[136] Restraint of trade financial compensation should be paid irrespective of the grounds for termination of the employment agreement.[137] The law in France does not a guide as to how the financial compensation may be paid.[138] Thus, it may be paid in one instalment upon the employment agreement's termination or in monthly instalments during the subsistence of the restraint of trade agreement.[139]

To the extent that French law does not provide any guidance on how financial compensation may be paid except in the context of collective agreements, and unlike in Germany where guidelines for the same exist, we submit that French law is unlikely to be helpful to South Africa in that specific regard, and German law may provide some guidance.

4.3.3 Some jurisdictions in which part of monetary compensation is paid as a lump sum and the rest monthly

- Denmark: Like all the jurisdictions, as mentioned above, financial compensation is an essential element of the validity of restraint of trade agreements in Denmark.[140] Employees are entitled to at least 50% of their average remuneration that they would have been paid if they continued working for employers for the term of restriction.[141] A lump sum of three months' salary is payable to employees upon the termination of the employment contract.[142] The remaining financial compensation is payable in monthly instalments until the period of restriction lapses.[143]

Given the identified perceived abuse of unpaid restraint of trade agreements by employers in South African as highlighted earlier in this paper, we recommend that South Africa considers what obtains in other jurisdictions briefly outlined here, and extracts some modest lessons from Germany about compensation, to improve the current law.

5 Possible lessons for South Africa from Germany

South Africa should learn from Germany and consider law reform that imposes employers' obligation to provide former employees' financial compensation. South African courts are conferred with the power to develop the Common law,[144] which informs the courts' current approach to restraint of trade disputes. The Constitution of the Republic of South Africa demands that when courts develop the Common law, they "must promote the spirit, purport, and objects of the Bills of Rights."[145] Further, Section 22 of South Africa's Constitution guarantees everyone the right to freely practice a trade and engage in useful commercial activities or the profession of their choice.[146] To actualise former employees' rights to practice their trades and engage in relevant professions freely, it is imperative that they not be hamstrung by the debilitating effects of unpaid restraint of trade periods.

Unpaid restraint periods interfere with employees' practice of their professions or engagement in commercial activities. Such restraint of trade agreements that limit former employees' ability to take up alternative employment with competitors or engage in commercial activities falling within the restraint's ambit without any compensation prospects are untenable in the new South Africa.

Therefore, South Africa needs to adopt a system of paid restraint of trade agreements to compensate former employees bound by restraint of trade to cover for the actual or potential loss of earning, as is Germany's case. This proposal for financial compensation should be one of the essential requirements for the validity of restraint of trade agreements in South Africa going into the future. Like the position in Germany, we submit that a former employee subject to a restraint of trade agreement in South African be eligible to receive 50% of the remuneration they were receiving before the termination of the employment agreement.[147] Unpaid restraint of trade agreements enable employers to abuse those agreements. We are of the considered view that if employers incur financial costs related to putting their former employees on restraint of trade agreements, it logically follows that employers will enter into these agreements with the sole motive of protecting their serious, legitimate commercial interests that are worthy of legal protection, and not for any other purpose.

It is submitted that if employers in South Africa are obligated to pay compensation to their employees during restraint periods, then such employers would not lightly enter into restraint of trade agreements. Most importantly, affected former employees will be able to pay their bills, maintain their families, and meet everyday bills, such as taking their children to school. We submit that it is unreasonable to prevent a person from working or opening an enterprise without considering how they will survive during the period of restriction. Therefore, unpaid restraint of trade agreements bring suffering to former employees and their families. Their continued existence in South Africa should be questioned, with the ultimate goal of jettisoning such restrictive agreements.

Uncompensated restraint of trade agreements limit employees' freedom of trade.[148] The Constitution confers protection to employees against unemployment (Section 22) and unfair labour practices (Section 23).[149] The violation of the above constitutional rights inevitably crystalises into the infringement of other constitutional rights such as the right to dignity, thus preventing affected parties (employees and their dependents) from having access to goods and services that are only enjoyed by those who have jobs and can pay for them.[150]

Taking a cue from Germany, restraint of trade agreements in South Africa should only be enforceable and binding between parties if the employer undertakes to compensate the former employee financially. Such compensation should be 50% of the average monthly remuneration for each month that the trade restriction applies. However, if a former employee receives remuneration from new employment not violating a restraint of trade agreement, then the former employer should deduct the monthly competition compensation.[151] For example, lets us assume that Dr. X, a medical doctor, was employed at a private hospital, despite a restraint of trade agreement with his former employer. Dr. X may work as a lecturer at a medical school. Suppose 50% of the remuneration that Dr. X earned from his previous employer is R50,000 and the monthly remuneration that he is earning at medical school is R30,000. In that case, the former employer may be entitled to deduct R30,000 from R50,000. Dr. X will be entitled to R20,000 monthly compensation from the previous employer and continue to earn his remuneration from his new job as a lecturer. Furthermore, the South African Revenue Services (SARS) should be entitled to tax the monthly competition compensation due to former employees.

6 Conclusions

This paper made a clear case for the abandonment of unpaid or uncompensated restraint of trade agreements in South African labour law. In the absence of a statutory enactment regulating restraint of trade agreements in South Africa, we recommend that South African courts develop the Common law to include compensation for workers who are rendered economically inactive by restraint of trade agreements. Many progressive jurisdictions acknowledge such compensation. South Africa as a keen member of the global community should consider learning from Germany and similarly placed jurisdictions and provide for employees' compensation during restraint periods, some of which may permanently disable an employee's ability to make a living. This idea sounds like one for the future but will certainly be welcome in the new South Africa grappling with high unemployment and related ills.

Acknowledgements

This paper is based on a revised and expanded version of a chapter extracted from the first author's LLM dissertation titled 'A critical analysis of the concurrent enforceability of restraint of trade agreements and garden leave in South African Labour law', submitted to the University of Venda, Thohoyandou, South Africa.

Notes

1 Constitution of the Republic of South Africa 1996.

2 Constitution of the Republic of South Africa 1996, Sec 39 (1) (b).

3 Van den Bergh, R. (2012) 'The remarkable survival of Roman-Dutch law', *Fundamina: A Journal of Legal History*, Vol. 18, No. 1, p.73, p.74, p.89. See also Lokin, J.H.A. (2008) 'Harmonisation in Roman, Roman-Dutch and South African law', *Fundamina: A Journal of*

Legal History, Vol. 14, No. 1, p.34. Farlam, I. (2003) 'Some reflections on the study of South African legal history', *Fundamina: A Journal of Legal History*, Vol. 9, No. 1, p.3.

4 Ackermann, L.W.H. (2006) 'Constitutional comparativism in South Africa', *South African Law Journal*, Vol. 123, No. 3, p.500.

5 Lucey, M.C. (2012) 'Europeanisation and the restraint of trade doctrine', *Legal Studies*, Vol. 32, No. 4, pp.623–641.

6 Ibid at p.624.

7 Constitution of the Republic of South Africa 1996, Sec 39 (1).

8 Labour Relations Act 66 of 1995, Sec 1 (b).

9 *Vodacom (Pty) Ltd v Motsa and Another* (J 74/16) [2016] ZALCJHB 53. See also *Basson v Chilwan and Others* (332/1991) [1993] ZASCA 61, para 46, *Den Braven SA (Pty) Ltd v Pillay and Another* (2899/2008) [2008] ZAKZHC 22, para 37.

10 Landis, H. and Grossett, L. (2006) 'Restraint of trade: what effect does it have today?', *Management Today*, Vol. 22, No. 8, p.55.

11 *Petrofina (Great Britain) Ltd v Martin* (1966) 1 Ch. 146.

12 Ibid.

13 *Montego Pet Nutrition (Pty) Ltd v Bouwer and Another* (16575/15) [2016] ZAGPPHC 791, para 25.

14 Kemp, K. (2005) 'The significance of consideration paid for post-employment restraints in England and Germany', *Stellenbosch Law Review*, Vol. 2, No. 1, p.258. See also Kohn, L. (2008) 'Restraint of trade agreements', *Without Prejudice*, Vol. 1, No. 1, p.6.

15 Ibid

16 *EOH Mthombo (Pty) Ltd v Bheekie-Odhav* (C177/12) [2012] ZALCCT 10, para 17.

17 Handelsgesetzbuch of 1897 (HGB) English translated by: M Pelzer/EA Voigt 'German Commercial Code' (2003) Sec 74 (a) 1.

18 Handelsgesetzbuch [German Commercial Code] Sec 74 (2).

19 Kemp, p.264.

20 Russell, L. (2018) 'Multi-country survey on covenants not to compete', *Greenberg Traurig and Association of Corporate Counsel*, p.1. See also *Magna Alloys and Research (SA) Pty Ltd v Ellis* 1984 (4) SA 874 (A), 893A, 898C-D.

21 *Magna Alloys and Research (SA) Pty Ltd v Ellis* 1984 (4) SA 874 (A) 875 H-I. See also Van Jaarsveld, M. (2003) 'The validity of a restraint of trade in an employment contract', *South African Mercantile Law Journal*, Vol. 15, No. 1, p.336. Kemp, p.263. Handelsgesetzbuch [German Commercial Code] Sect. 74 (a) (1). Judgment BAG 1st August 1995 – AP HGB § 74 a Nr. 5.

22 Pretorius, C.J. (2009) 'Covenants in restraint of trade: a synthesis of traditional, Common law and constitutional approaches', *Obiter*, Vol. 30, p.157. See also Bredin, P. et al. (2016) *Post-Contractual Restrictions on Competition in Employment Relationships in the UK, France and Germany*, No. 5 [online] https://www.hengeler.com/fileadmin/news/BF_Letter/15_Labour_Law_2016_12.pdf (accessed 23 May 2018).

23 Landis and Grossett, p.57. See also Judgment BAG 1st August 1995 – AP HGB § 74 a Nr. 5; Mario, E. (2006) 'Non-competition clauses in labour contracts – Germany', *XIVth Meeting of European Labour Court Judges*, Court de Cassation, Paris, 4 September, p.4; also, Bredin, p.6, p.7.

24 *Fidelity Guards Holdings (Pty) Ltd v Pearman* 1997 (4) All SA 658G. See also *Laser Junction (Pty) Ltd v Fick* 38 ILJ 2675 (KZD) (28 September 2017), para 28; *One Capital Sponsor Services (Pty) Ltd and Another v Chellan and Others* (J1572/17) [2017] ZALCJHB 340 (18 September 2017), para 23; *Den Braven SA (Pty) Limited v Pillay and Another*, para 36; *EOH Mthombo (Pty) Ltd v Prelence Bheekie-ODHAV (C177/12) [2012] ZALCCT 10*, para 28; *Handelsvertreterentscheidung*; judgment of 7th February 1990; BVerfG 81,242; Constitution of the Republic of South Africa 1996, Section 22; Grundgesetz of 1949,

Section 12 (GG) [German Constitution] Translated by C. Tomuschat, D.P. Currie, D.P. Kommers et al. (2018).

25 *Den Braven SA (Pty) Ltd v Pillay and Another*, para 36. See also Burgerliches Gesetzbuch [Civil Code] Section 241 (2); Bredin et al., p.7.

26 Handelsgesetzbuch [German Commercial Code] Section 74 (i).

27 Frahm-Arp, L. (2018) 'Multi-country survey on covenants not to compete', *Greenberg Traurig and Association of Corporate Counsel*, p.92.

28 Constitution of the Republic of South Africa 1996, Sec 22. See also *Absa Insurance and Financial Advisors (Pty) Ltd v Jonker and Another*, *Absa Insurance and Financial Advisers (Pty) Ltd v Jonker and Another* (741/17, C742/17) [2017] ZALCCT 57 (17 November 2017), para 23; Handelsgesetzbuch [German Commercial Code] 74 (i); Bredin et al., p.1.

29 Von Einem, D. (2018) 'Multi-country survey on covenants not to compete', *Association of Corporate Counsel*, p.33. See also Scouble, N.C. (1963) 'Restraint of trade on employees', *The Rhodesia and Nyasaland Law Journal*, Vol. 3, No. 1, pp.196–197.

30 Calitz, K. (2011) 'Restraint of trade agreements in employment contracts: time for Pacta Sunt Servanda to bow out?', *Stellenbosch Law Review*, Vol. 22, p.66. See also Angelo and Ellinger, p.484.

31 Angelo and Ellinger, p.484, p.489. See also Sharrock, R. (2014) 'Relative bargaining strength and illegality uniting reformed church, De Doorns v President of the Republic of South Africa 2013 (5) SA 205 (WCC): cases', *Obiter*, Vol. 35, No. 1, pp.140–141. Hawthorne, L. (1995) 'The principle of equality in the law of contract', *Tydskrif vir Hedendaagse Romeins – Hollandse Reg*., Vol. 58, No. 157, p.157, p.170.

32 Ibid.

33 Handelsgesetzbuch [German Commercial Code] Sec 74 (2).

34 Handelsgesetzbuch [German Commercial Code] Sec 74 (a) (1).

35 Handelsgesetzbuch [German Commercial Code]. See also Burgerliches Gesetzbuch [Civil Code]; Grundgesetz [Constitution].

36 Ibid.

37 *Afrox Healthcare BP (Cape) v Strydom* 2002 6 SA 21 (SCA); *ARB Eletrical Wholesalers (Pty) Limited v Ashley* (D683/17) [2017] ZALCD 20 (13 October 2017); *Aramex South Africa (Pty) Limited v Van Schalkwyk and Another* (C516/2017) [2017] ZALCCT 44 (4 October 2017); *Canon KwaZulu-Natal (Pty) Ltd t/a Canon Office Automation v Booth* (2005) 3 SA 205 (N); *D & E Trading (Pty) Ltd v Hilton Village Centre CC & Others* (1342/13) [2013] ZAKZPHC 12 (19 March 2013); *Den Braven S.A. (Pty) Limited v Pillay and Another* (2899/2008) [2008] ZAKZHC; 22; *Dickinson Holdings Group (Pty) Ltd and Others v Du Plessis and Another* 2007 (1) All SA 583; *Everfresh Market Virginia (Pty) Ltd v Shoprite Checkers (Pty) Ltd* 2012 (3) BCLR 219 (CC); *Experian South Africa (Pty) Ltd v Haynes and Another* 2013 (1) SA 135; *Metcash Trading Africa (Pty) Ltd v Pauls* (4861/2005) [2005] ZAFSHC 153 (8 December 2005); *Montego Pet Nutrition (Pty) Ltd v Bouwer and Another* (16575/15) [2016] ZAGPPHC 79; *Mozart Ice Creams Classic Franchises (Pty) Ltd v Davidoff and Another* (2009) 30 ILJ 1750 (C); *Vodacom (Pty) Ltd v Motsa and Another* (J 74/16) [2016] ZALCJHB 53.

38 Handelsgesetzbuch [German Commercial Code] Sec 74 (a) 1.

39 Ibid.

40 See Statics South Africa (2021) *Quarterly Labour Force Survey (QLFS) – Q1:2021* [online] https://www.statssa.gov.za/publications/P0211/Media%20release%20QLFS%20Q1%202021.pdf (accessed 12 September 2021).

41 *EOH Mthombo (Pty) Ltd v Bheekie-Odhav* (C177/12) [2012] ZALCCT 10, para 17.

42 Handelsgesetzbuch [German Commercial Code] Sec 74 (2).

43 Handelsgesetzbuch [German Commercial Code] Sec 74 (b). See also Bredin et al., p.8; Von Einem, p.3.

44 Ibid.

45 Calitz, p.50. See also Bhana, D. and Pieterse, M. (2005) 'Toward a reconciliation of contract law and constitutional values: Brisley and Afrox revisited', *South African Law Journal*, p.866. Hutchison and Pretorius (2012) *The Law of Contract in South Africa*, 2nd ed., p.21, Oxford University Press, Cape Town.

46 Ibid.

47 Ibid.

48 Bhana, D. and Pieterse, M. (2005) 'Toward a reconciliation of contract law and constitutional values: Brisley and Afrox Revisited', *South African Law Journal*, Vol. 122, No. 4, p.866.

49 *Medscheme Holdings (Pty) Limited & Another v Bhamjee* 2005 (5) SA 339 (SCA), para 18.

50 Hutchison and Pretorius.

51 Beale, H. (1986) 'Inequality of Bargaining Power', Oxford Journal of Legal Studies vol.6, pp.123, 125. See also Sharrock p.140.

52 Ibid.

53 Angelo and Ellinger, p.484.

54 Burgerliches Gesetzbuch [Civil Code].

55 Calitz, p.66. See also *Knox D'Arcy v Shaw* 1996 2 SA 651 (W) 659; *Den Braven SA (Pty) Ltd v Pillay and Another*, para 27.

56 *Roffey v Catteral, Edwards & Goudre (Pty) Ltd* 1977 (4) SA 494 (N), 505 E-F.

57 *Afrox Healthcare BP (Cape) v Strydom* 2002 6 SA 21 (SCA). See also *Barkhuizen v Napier* (2007) (5) SA 323 (CC), para 59.

58 Ibid.

59 Calitz, p.65.

60 Ibid.

61 Ibid.

62 *SA Unemployment Rate Jumps to 29%, The Worst Since 2008* [online] https://www.fin24.com/Economy/just-in-sa-unemployment-rate-jumps-to-29-the-worst-since-2008-20190730 (accessed 30 July 2019).

63 van Eck, S. (2020) 'COVID-19 and labour law: South Africa', *13 Italian Journal Italian Labour Law e-Journal Special Issue*, Vol. 13, No. 1, p.2.

64 Sharrock, p.141.

65 Hawthorne, p.170.

66 Naude and Lubbe, p.368. See also *Barkhuizen v Napier*, para 135.

67 *Alec Lobb (Garages) Ltd v Total Oil (Great Britain) Ltd* [1985] 1 W.L.R. 183.

68 Ibid.

69 Ibid.

70 Ibid.

71 Naude and Lubbe, p.368. See also *Barkhuizen v Napier*, para 135.

72 Ibid.

73 Ibid.

74 Cassim, p.528. See also Glover, G. (2006) 'Developing a test for economic duress in the South African law of contract: a comparative perspective', *South African Law Journal*, Vol. 123, No. 2, pp.287–288.

75 Ibid.

76 Handelsgesetzbuch [German Commercial Code] Sec 74 (2).

77 Ibid.

78 Landis and Grossett, p.57.

79 Angelo and Ellinger, p.458.

80 Ibid.

81 *Biografic (Pty) Ltd v Wilson* 1974 2 SA 342 (R) 346. See also Van Heerden, H.J.O. and Neethling, J. (1995) *Unlawful Competition*, p.25, Lexisnexis Butterworths, Durban.

82 Beale, p.123, p.125.

83 Handelsgesetzbuch [German Commercial Code] Sec 74 (a) 1.

84 Angelo and Ellinger, p.460.

85 Ibid. See *Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co* 1894 AC 535, 566.

86 *Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co, Ltd*.

87 Ibid.

88 1913 AC 724.

89 *Mason v Provident Clothing Co Ltd*.

90 Handelsgesetzbuch [German Commercial Code] Sec 74 (2).

91 Handelsgesetzbuch [German Commercial Code].

92 Bredin et al., p.8. See also Von Einem, p.3.

93 Mario, p.3.

94 Handelsgesetzbuch [German Commercial Code] Sec 74 (1).

95 Bredin et al., p.9.

96 Ibid.

97 Ibid.

98 Handelsgesetzbuch [German Commercial Code] Sec 74 (1).

99 Bredin et al., p.9.

100 Ibid.

101 Ibid.

102 Bredin et al., p.7.

103 Ibid.

104 Ibid.

105 Handelsgesetzbuch [German Commercial Code].

106 Ibid.

107 Handelsgesetzbuch [German Commercial Code] Sec 74 (c) (2).

108 Ibid.

109 Ibid.

110 Handelsgesetzbuch [German Commercial Code] Sec 74.

111 Handelsgesetzbuch [German Commercial Code].

112 Ibid.

113 Handelsgesetzbuch [German Commercial Code] Sec 74 (c).

114 Sochorová, P. (2013) *A Global Guide to 'Restrictive Covenants'*, p.10, Mayer Brown Practices International LLP, London.

115 Contributed by Studio Legale Associato Quorum (2013) *A Global Guide to 'Restrictive Covenants'*, p.64, Mayer Brown Practices International LLP, London.

116 Napoli, C. et al. (2018) 'Multi-country survey on covenants not to compete', *Greenberg Traurig and Association of Corporate Counsel*, p.48.

117 Pałubicki, R. (2013) *Partners a Global Guide to 'Restrictive Covenants'*, p.76, Mayer Brown Practices International LLP, London.

118 Barrena, L. (2013) *A Global Guide to 'Restrictive Covenants'*, p.86, Mayer Brown Practices International LLP, London.

119 Ibid.

120 Havia, S. (2013) *A Global Guide to 'Restrictive Covenants'*, p.24, Mayer Brown Practices International LLP, London.

121 Ibid.

122 Ibid.

123 De Wind, E. and Van Doorne, N.V. (2013) *A Global Guide to 'Restrictive Covenants'*, p.70, p.71, Mayer Brown Practices International LLP, London.

124 Ibid.

125 Baltazar, S. (2013) *A Global Guide to 'Restrictive Covenants'*, p.6, Mayer Brown Practices International LLP, London.

126 Szemán, P. (2013) *A Global Guide to 'Restrictive Covenants'*, p.47, Mayer Brown Practices International LLP, London.

127 Ibid.

128 Ibid.

129 Bredin et al., p.9.

130 Ibid.

131 Ibid.

132 Ibid.

133 Ibid.

134 Ibid.

135 Ibid.

136 Lambert, L.D. (2013) *A Global Guide to 'Restrictive Covenants'*, p.30, Mayer Brown Practices International LLP, London.

137 Ibid.

138 Ibid.

139 Ibid.

140 Amsinck, H. and Reumert, K. (2013) *A Global Guide to 'Restrictive Covenants'*, Mayer Brown Practices International LLP, London.

141 Ibid.

142 Ibid.

143 Ibid.

144 Constitution of the Republic of South Africa 1996 Sec 39 (2). See also *Canon KwaZulu-Natal (Pty) Ltd t/a Canon Office Automation v Booth* 209G.

145 Constitution of the Republic of South Africa 1996 Sec 39 (2).

146 Constitution of the Republic of South Africa 1996.

147 Handelsgesetzbuch [German Commercial Code] Sec 74 (1).

148 *Fidelity Guards Holdings (Pty) Ltd v Pearman* 658G.

149 *Laser Junction (Pty) Ltd v Fick*, para 28.

150 Ibid.

151 Handelsgesetzbuch [German Commercial Code] Sec 74 (c) (2).