Contracts in Restraint Of Trade in Malaysia

In Malaysia, all contracts of restraint of trade are void unless it falls within exception provided in S. 28 of CA 1950. Thus, in Malaysia, the legislature had purposely made the list of exceptions in restraint of trade simply exhaustive by including the three common law exceptions. The test of reasonableness that has been commonly used by English courts is not applicable in S. 28 of CA. On the other hand, in Singapore, a restrictive covenant clause may be held valid as long as it satisfies the reasonableness test.

In Malaysia, the first exception provided in S. 28 of CA is the sale of goodwill of business. It provides that "one who sells the goodwill of a business may agree with the buyer to refrain carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the goodwill from him, carries on a like business therein." This is further subject to a proviso that the limit must be reasonable. In a contract of sale of business, the restrictive covenant plays an equally important role to the vendor and purchaser. In the absence of restrictive covenant, a sale of goodwill of business could not be conducted because there is a possibility that the vendor may venture into the same business and compete with the purchases. Hence, a valid restrictive covenant is essential in creating a property right that is capable to be sold.

The second and last exceptions are related to the partnership agreements whereby the second exception deals with post-dissolution of partnership. The reasoning behind the second exception is the ex-partner may, on dissolution of the partnership, continue to conduct a similar business in competition with the previous firm and solicit the clients of the previous firm. Exception 2 of S. 28 of CA provides that "partners may, upon or in anticipation of a dissolution of the partnership, agree that some or all of them will not carry on a business similar to that of the partnership within such local limits." In order to give legal effects to the said exception, the whole partnership need not to be dissolved or terminated but it has to be proven that an agreement is made in anticipation of a dissolution of partnership, which may or may not happen.

In the case of Millennium Medicare Services v. Nagadevan Mahalingam , the defendant, a medical practitioner, entered into a partnership agreement to run health care centers. The agreement contained a clause that provided that as a partner, the defendant was prohibited from practicing as a medical practitioner within the radius of 15km from any of the plaintiff's branches within three years after he ceased to a partner of the plaintiff. The defendant resigned as a partner the next year and practiced in a clinic within 15kim from the branches. Then, the plaintiff applied for an injunction to restrain him from practicing within 15km and for damages. The issue arose was whether the clause falls within Exception 2 of S. 28 of CA. The judge found that the territory limit of 15km and duration of three years were reasonable. However, the restrictive covenant was held void because the appellant failed to prove that the agreement was entered in anticipation of the partnership practice being dissolved. Hence, it did not fall within the Exception 2 of S. 28 of CA.

Lastly, Exception 3 of S. 28 of CA provides that partners may agree that some one or all of them will not carry on any business, other than that of the partnership, during the continuance of

partnership. Restrictive clauses during the continuance of partnership are generally held valid.

On the other hand, Under the position of Singapore, the court will declare agreements which are in restraint of trade as prima facie invalid or void unless it can be shown that the scope of the restraint is reasonable and in the interests of the parties involved and in the public. The court will not simply uphold a bare covenant of restraint, hence there must be some kind of reasonable legitimate interests that the parties seek to protect.

All these will be subject to tests of reasonableness in order to ascertain whether a restriction is valid or otherwise. In the case of Man Financial (S) Pte Ltd v. Wong Bark Chuan David , the judge laid down a three-fold test where it contains three limbs and all these limbs must be satisfied. Firstly, is there a legitimate proprietary interest to be protected? Secondly, is the restrictive covenant reasonable in reference to the interests of the parties? Lastly, is the restrictive covenant reasonable in reference to the interests of the public?

In CLAAS Medical Centre Pte Ltd v. Ng Boon Ching , the respondent ran an aesthetic medicine clinic and had a business which distributed aesthetic laser and intense pulsed light machine. Six doctors and the respondent incorporated the appellant and acquired the respondent's business. They entered into a shareholder agreement that contained a restrictive clause which prohibited the parties from "being engaged and/or interested in any trade and/or business carried on within Singapore" that was similar to the "Business" of the Company and/or the practice of "Aesthetic Medicine" for the period remaining as shareholders and up to three years after cessation of shareholdings. Later, the respondent sold all his shares in appellant and resigned. He then set up his own aesthetic medical practice. The restriction is imposed on a sale of a business, hence there is a clear proprietary interest to be protected and not contrary to public policy. The next question the court considered is whether the clause is reasonable in the interest of the parties. The court was of the view that the clause was a blanket restriction on every type of aesthetic medicine, which was far more than reasonably necessary to protect the goodwill sold by respondent. The clause did not satisfy all three limbs, and therefore was held unreasonable.

Another case that illustrates the application of the reasonable test is the case of Centre for Creative Leadership (CCL) Pte Ltd v Byrne Roger Peter and others. The plaintiff was a company providing leadership training program. The first and third defendants were employees of the plaintiff. Their employment agreement with the plaintiff contained a restraint of trade covenant, which was a non-compete covenant. Later, both of them resigned and join another company, Roffey Park. One of the plaintiff's main clients sought tenders from the plaintiff, Roffey Park and another company. However, the plaintiff did not obtain any bid while Roffey Park obtained one of the bids. The plaintiff claimed that Mr. Byrne and Mr Jenkins have been providing and designing programs for the client as an employee of the plaintiff. Hence, the plaintiff sued the first and third defendant for breaching the non-compete covenant. In regards to whether the non-compete covenant was enforceable; the court successfully identified two main interests to be protected which are trade secrets and trade connection. It was found that Mr. Jenkins and Mr. Byrne did have influence over the plaintiff's client, rendering it a legitimate interest to be protected. However, the second and third limbs of the test were not satisfied because the geographical scope, time span and scope of the activities were unreasonable wide with reference to the interest of the parties.

Conclusion

As have seen from the above discussion, the laws governing restraint of trade in Malaysia is definitely stricter as compared to Singapore. The position of restraint of trade contracts in Malaysia can be concluded as all contracts in restraint of trade are void pro tanto unless it falls within statutory exceptions. On the other hand, the position in Singapore is all contracts in restraint of trade are prima facie void unless it satisfies the test of reasonableness. It is clear that reasonableness and fairness are never the basis to validate restrictive covenants in Malaysia. S. 28 of Contracts Act 1950 is a rigid rule that renders all restraints void, whether it is general restraints, partial restraints or narrow restraints. However, Malaysian courts do not have any discretionary power but to declare all contracts in restraint of trade void.

We are of the view that Malaysia should take a looser approach regarding to restraint of trade. The Law of Commission of India advocates for amendment to S. 27 of Indian Contracts Act which is in pari materia with S. 28 of Contracts Act 1950 to allow reasonable restraint on trade. Similar view was echoed by the Supreme Court of India in the case of Percept D'Mark (India) Pvt Ltd v. Zaheer Khan & Anor . The judge wrote, "... somewhere there must be a line between those contracts which are in restraint of trade and whose reasonableness can, therefore, be considered by the Courts which merely regulated the normal commercial relations between the parties and are, therefore, free from doctrine ...".

A more liberal approach of interpretation on restraint of trade has been taken by Malaysian courts by distinguishing restraint of trade and restrictive of trade as can be seen in the case of The Hua Khiow Steamship Co Ltd v. Chop Guan Hin. The judge wrote that, "… This does not mean that every contract made by a trader whereby in the carrying on of his trade or business he limits the scope of his trading by his conduct is void, and it is perhaps a little difficult to state in general terms of the precise difference between a contract which restrains the exercise of trade and a contract which limits the manner in which that trade is to be carried on…" All in all, we are of the view that contracts in restraint of trade should be given loose and liberal interpretation in order to avoid a blanket ban on all contracts in restraint of trade which are in the course of ordinary commercial relations.