Locutus

The newsletter of intellectual property law, statutory deceptive conduct and franchising law.

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Welcome to Locutus — July 2007

Locutus is a newsletter of current news, recent cases, and practice decisions. It is authored by Carmen Champion Barrister-at-Law.

Recent Cases -

Franchising

The need to take infinite care in drafting breach notices.

J F KEIR PTY LTD V PRIORITY MANAGEMENT SYSTEMS PTY LTD (ADMINISTRATORS APPOINTED) [2007] NSWSC 789 (24 July 2007)

AJ Rein accepted the following propositions in respect of the exercise of a power by a franchisor:

(i) must act reasonably and honestly: *Renard Constructions (ME) Pty Limited v Minister for Public Works* (1992) 26 NSWLR 234, *Alcatel Australia v Scarcella* (1998) 44 NSWLR 349

(ii) which must be considered objectively: *Renard*, supra at 258, 261 and 268, *Burger King Corporation v Hungry Jacks Pty Limited* (2001) NSWCA 187 at [189];

(iii) not simply relying on information provided by third parties: *Burger King*, supra at [177], or 'wilfully shutting (ones) eyes' or refraining from making inquiries, but exercising the degree of 'caution and diligence to be expected of an honest person of ordinary prudence': *Mid Density Developments Pty Limited v Rockdale Municipal Council* (1993) 44 FCR 290 at 298, *Russell v Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (2007) NSWSC 104 at [115]. The defendant had submitted that it could rely on complaints received from 3rd parties without investigation those complaints;

(iv) It will be a breach of the duty if the defendant is acting for some ulterior motive: *Burger King*, supra at [142]–[185], *Mangrove Mountain Quarry Pty Limited v Barlow* (2007) NSWSC 492;

(v) any action by the defendant must recognise and have regard to the legitimate interests of both parties in the enjoyment of the fruits of the contract: *Overlook v Foxtel* (2002) ACR 90-143; and

(vi) avoiding action rendering the plaintiffs interests under the agreement 'nugatory, worthless, or... seriously undermined': Byrne v Australian Airlines Ltd (1995) 185 CLR 410.

The breach notice alleged a number of breaches which the franchisor well knew he had no proper basis for making. Further, when he made those allegations he did so in a form that gave no proper particulars of the alleged breaches and when particulars were sought he gave no answer in breach of a requirement to do so: *Aura Enterprises Pty Ltd v Frontline Retail Pty Ltd* (2006) 202 FLR 435; [2006] NSWSC 902.

In regard to a claim that the franchisee has misrepresented itself the Court held that the franchisor had failed to seek clarification of how it was said the franchisee had misrepresented itself to a third party and further failed to seek any explanation from the franchisee on this, nor did it give any convincing explanation as to why it had not done so.

The Court also made the point that Sparks (the principal of the franchisor) through his significant shareholding and directorship of two of the franchises and ownership of the defendant as franchisor was in a position of obvious conflict.

The Court concluded that the First Notice was not given as the result of a bona fide belief that the franchisee was in breach of the franchise agreement but for reasons connected to Mr Spark's interests in the North Sydney franchisee and matters extraneous to PMS's legitimate interests as franchisor.

Contravention of the Franchising Code renders franchise agreement unenforceable for statutory illegality.

KETCHELL v MASTER OF EDUCATION SERVICES PTY LTD [2007] NSWCA 161 (19 July 2007)

In the proceedings below it was found that the franchisor did not comply with Clause 11(1) of the Franchising Code (provides that the franchisor must not enter into a Franchise Agreement without receiving from the franchisee a written statement stating that they have read and have had a reasonable opportunity to understand the disclosure document and the Code).

Associate Judge Malpass found that though this breach was tantamount to a finding of a contravention of s51AD of the Trade Practices Act 1974 (Cth) (the Act), it did not render the receipt of the non-refundable payment illegal. He held that the matter was covered by the decision in *The Cheesecake Shop v A & A Shah Enterprises* [2004] NSWSC 625,

The issue was whether a contravention of Clause 11(1)(a), and resulting contravention of Clause 11(1)(c), rendered the contract unenforceable for statutory illegality.

Held:

(1) If the legislature prohibits the making of a contract, the making of the contract does not give rise to an enforceable right or obligation: *Trade Practices Commission v Milreis* Pty Ltd (1977) 29 FLR 144 at 158 per Brennan J, citing *Chai Sau Yin v Liew Kwee Sam* [1962] AC 304 at 311). This statement was recently approved by the High Court in *SST Consulting Services Pty Ltd v Rieson* (2006) 225 CLR 516 at 532[49], 546[102]). What is prohibited under cl 11 is not just conduct but the contract itself and the recovery of money under it (contrast *Hurst v Vestcorp Ltd* (1988) 12 NSWLR 394 at 442-43).

(2) The governing principle in this case is that disobedience of the Code is disobedience of the Act.

(2) Section 51AD read with Clause 11 directly prohibited the contract in question and the recovery of the monies claimed. There is nothing in the *Trade Practices Act 1974* that expressly or implicitly negated the application of the common law rule.

Confidential Information

DEL CASALE & ORS. V. ARTEDOMUS (AUST) PTY. LIMITED [2007] NSWCA 172 (18 JULY 2007)

The first and second appellants had been directors and employees of the respondent company, an importer of stone and ceramic products for the building industry. The respondent sold in Australia a particularly popular type of modica stone, which it obtained from the Ragusa region in Italy and marketed under the name "Isernia". The respondent had been the sole importer of modica stone into Australia. The source of Isernia and the fact that it was modica stone could not be easily ascertained, and the respondent made efforts to conceal this information by giving it only to a few people in the organisation, including the first two appellants.

The first two appellants terminated their employment with the respondent company, and subsequently the first appellant in an agreement for the sale of shares in the respondent contracted not to compete with it for three years and to keep confidential any "commercially sensitive information" he had learnt whilst in the employment of the respondent. Earlier, the first appellant had set up Stone Arc, the third appellant. Both the first and second appellants then used their knowledge that Isernia was modica stone to find a supplier of modica stone to be imported and sold by Stone Arc

The primary judge found the claim of breach of confidence made out.

Artedomus relied among other things upon the provisions of s.183 of the *Corporations Act 2001 (Cwth).*

The following are some of the issues considered by the NSW Court of Appeal:

1. Was the relevant information confidential to the extent that it would be protected after cessation of employment and/or directorship, without express contractual restraint? The majority held that generally questions concerning an employee's obligation of confidentiality **after** employment has come to an end, in the absence of an express contract dealing with the matter, are best dealt with as part of the general law concerning confidentiality of information>

2. Was it proved that Mr. Del Casale and/or Mr. Savini used that information in breach of confidence? It is clear that information may be confidential, even if it is known to persons other than the person claiming confidentiality: it may be sufficient that the information is not freely available, particularly if it is not freely available to competitors of the employer. Refers with approval to the list of matters listed in *Wright v. Gasweld*, as expanded by R. Dean, *The Law of Trade Secrets and Personal Secrets,* (2002) 2nd Ed., at 190. Identify one futher factor of importance, namely the extent to which the particular information can be readily isolated from the employee's general know-how which the employee is entitled to use after the end of employment.

See also:

1. *Orica Investments Pty Ltd v William McCartney* [2007] NSWSC 645 re the misuse of pricing information.

2. *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* [2007] HCA 22 (24 May 2007) re whether property acquired through misuse of information by a fiduciary should be treated as trust property.

Preliminary Discovery

Keshi Pty Ltd v Firefly Press (Australia) Pty Ltd [2007] FCA 982

Alleged breach of copyright in charts used in literacy teaching. The question was whether the applicant had

sufficient information under O 15A r 6(b) of the Federal Court Rules.

Digital Agenda Amendment Act 2000/ US Free Trade Agreement Implementation Act 2004

The operation of amendments to Part IX of the Copyright Act (relating to moral rights for performers, and enacted as part of the US Free Trade Agreement Implementation Act 2004) was dependent on the WIPO Performances and Phonograms Treaty coming into force. Those amendments are now operative.

The new rights include the right of attribution of performership; the right not to have performership falsely attributed; and the right of integrity of performership.

These moral rights only subsist in respect of live performances (including, for example, live radio broadcasts) and sound recordings of live performances where the performance or recording was made after the commencement of the amendments.

And finally...