



## Research Paper

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# Restraint-of-Trade Payments in South African Financial Service Companies

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A research project submitted to the Gordon Institute of Business Science,  
University of Pretoria, in partial fulfilment of the requirements of the degree of  
Master of Business Administration.

**Keneiloe Moumakoe**

**Student Number: 20143380**

Contact Details: +27 82 821 6932

Email: [keneiloe@homemail.co.za](mailto:keneiloe@homemail.co.za)

[keneiloem@mweb.co.za](mailto:keneiloem@mweb.co.za)

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## **ABSTRACT**

**Orientation:** The topic of restraint of trade has attracted attention, with significant renewed interest in light of the role it is said to play in contributing to the executive's career moves and the protection it offers companies. At the heart of the issue is the perceived unfairness of the contract between the employee signing the contract and the company restraining the employee.

**Research purpose:** The purpose of this study was to describe aspects the restraint of trade within the South African financial services industry.

**Motivation for the study:** The motivation for the study was the development of a deeper understanding of restraint of trade, within the South African context, as the concept became prevalent over the past years with many questions remaining unanswered.

**Research design approach and method:** The research was a qualitative, content study.

**Main findings/results:** The primary finding was that, despite the wide use of such contracts they are not clearly understood, they are still perceived as unfair and are seen as a tool to curb career development.

**Practical managerial implications:** The results suggest that the use of such contracts maybe popular but they are flawed, even though elements such as the period of the contracts and the quantum of payments are known the legal clarity and misunderstanding of these contracts is still an issue.

**Contribution/value add:** The study provides context to Restraint-Of-Trade within a South African framework. It further provides key insight into the perception, misalignment of these contracts to the overall understanding and the aim they are meant to achieve.

**Key words:** restraint of trade, executives, financial services, South Africa.

## DECLARATION

I, Keneiloe Ziphora Moumakoe, declare that this dissertation is my own unaided work. Any assistance that I have received has been duly acknowledged in the dissertation. It is submitted in partial fulfilment of the requirements for the degree of Master in Business Administration at the Gordon Institute of Business Science, University of Pretoria. It has not been submitted before for any degree or examination at this or any other University.

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Keneiloe Moumakoe

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7<sup>th</sup> November 2012

## ACKNOWLEDGEMENTS

The successful completion of this study depended greatly on the support of many individuals to whom I wish to express my sincerest gratitude:

- To GOD All Mighty who strengthens us every day;
- To my supervisor, Dr Mark Bussin, for his support and guidance throughout the course of this research; you have made this all possible for me;
- To Enoch Mchiza, thank you for your assistance and for sharing your knowledge;
- To all my family, friends and colleagues, for their support;
- To the faculty of GIBS and the GIBS community , for allowing me a chance to complete my studies;
- To those who participated in the research, and shared their insight on the subject matter; and
- To all the respondents of the semi-structured interviews and for their contribution to this study;

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## 1) Introduction to the Research Problem

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### 1.1) Title

“Restraint of trade payments in South African financial services companies”.

### 1.2) Research Problem

Executives, especially CEO’s differ fundamentally from general workers as they are tasked with more responsibilities, such as the huge responsibility of delivering on shareholder’s value expectation and driving the performance and sustainability of the company. Thus they are required to be highly skilled, and are required to possess the capabilities to utilise core competencies to the best advantage of the organisation. As a result, companies feel the need to restrain such talent for a period of time.

Paying former executives to refrain from competing with their former employers, which is the essence of most restraint of trade agreements, is common practice in corporate South Africa. According to Burmeister, CEO of Landelahni Recruitment Group (Business Times Live, 2012), "A restraint of trade agreement is part of the employment contract that the employee signs when he first joins the firm. It provides a stipulated time period during which the employee, usually a senior executive, agrees either not to take up a position with the employer's competition or not to do any kind of business with the employer's clients".

As in many countries the relationship between the employer and employee in South Africa is regulated by obligations and rights and is entrenched in common law, custom and practice, contracts, and legislation.

In many situations these restraint of trade come about as a result of competition. Companies work hard to build up profit margins and along the period those selfsame profits are put to shame by the sudden profit margins of another company, a competitor.

The competitor's sudden turnaround could be attributed to product innovations, clever marketing, good strategic alignment or possibly providence. However in some instances the company's superior performance is ascribed to the employment of an employee who divulged certain trade secrets and other confidential business information to the new company, giving it a competitive edge. This raises the question: How should a company go about to protecting its secrets and what information constitutes a trade secret? Thus companies' restraining a person through restraint of trade contracts is a topic that requires further investigation.

Until recently these restraint of trade payments were vague and were seen as a method to provide some level of tax-benefit (non-taxable lump sum) to the recipient; however it still remains a valuable mechanism for employers to protect genuine business interests. The debate as to whether restraint of trade agreements are enforceable has raged for many years and has become an area that remains clouded in mystery and as a result has many associated misconception. Questions have arisen regarding the contents of such agreement, the value-add around these agreements and the payments stipulated in these agreements (Deloitte & Touché Legal 2004).

Recently reported by Business Times Live (2012), former Absa CEO Booyesen took six months "special leave" worth R3-million after his successor Ramos took over in March 2009. Booyesen then received R19.1-million in August 2009 as a termination benefit and restraint of trade payment, binding him for a year to September 2010.

With the above in mind, the relevance of understanding the restraint of trade payments, the determinants of such payments and the quantum thus of, is of high importance.

### **1.3) Research Objectives**

The present research study aims to answer the following fundamental questions:

- How relevant are the restraint of trade agreements?
- What perception do executives have of Restraint-of-Trade payments?
- In aiming to answer the above questions, the following are the main objectives of the present research:
  - To investigate the determinants of the restraint-of-Trade payment values in the financial services industry in South Africa
  - To determine and analyse the quantum of the restraint of trade payments and
  - To determine the perception of executives regarding restraint of trade payments



#### **1.4) Research Aim**

Many articles on restraint of trade payments have been written by US-based scholars; these look specifically at golden parachutes and are based on the seminal 1985 paper by Lambert and Larcker (1985) on this phenomenon.

Stapledon (2005) also undertook a study on the restraint of trade payments focusing on the public policy analysis and good practice guidelines.

The aim of the present study is to determine how restraint of trade payments are determined, and the perceptions of executives regarding restraint of trade payments in the financial industry in South Africa.

It is important to understand the restraint of trade environment in the South African perspective or context is relevant in that it draws focus to the manner in which South African financial services companies have been understood this measure.

The other important factor to consider is that South Africa has joined the BRIC group of countries and has renewed its membership with the United Nations Security Council; this indicates the clear signal of South Africa's growing importance in the international landscape especially as a platform for capitalising on African opportunities (Business Day, 2011). Thus South Africa has a responsibility to ensure that relevance is seen in every opportunity sphere, from strategic knowledge to sustainable experience which should be understood by other developed countries.

The South African context appears to be growing in importance as investors

look to South Africa as a means to enter Africa. Given the importance of the South African financial services industry in facilitating increasing capital flows into Africa, it would be worthwhile to develop an understanding of the factors that play a role.

The misconceptions and misunderstanding of the restraint of trade agreements, warrants for some study.

Although the present research paper focuses on financial services company, many companies grapple with this aspect. Restraint of trade contracts are not new, but the conclusion of similar agreements with non-executives isn't standard practice.

The practice of some employers requiring all employees to sign restraint of trade agreements is a difficult action, as not all employees have access to or are involved in areas of the employer's business which require protection by way of a restraint of trade (Finweek, 2004).

With limited academic contributions to the body of knowledge around restraint of trade payments information available in South Africa, there exists an opportunity, and a need to,

- Further develop the understanding of the determinants of such payments;
- Show the level of understanding and
- Show the perception of executives around such payments.

In light of the above an opportunity is explored to make an understanding of the restraint of trade payments in employment contracts in an inimitable and imperative context.

Chapter 2 reviews the relevant literature and research on the topic and is presented in order to provide greater context to the research problem.

## 2) Literature Review

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### 2.1) Introduction to the Literature Review

The primary purpose of this study is to analyse, and understand the restraint of trade contractual payments in financial services organisations in South Africa. This chapter sets out the literature pertaining to the respective research constructs and will indicate how the various constructs relate to the research problem. The literature review will also provide insight into previous research conducted in the field as it relates to the specific constructs presented in this study.

The chapter is set out such that the literature begins with a review of the Financial Industry focusing mainly on the issues that have arisen following the financial crisis of 2008. The next step of the literature review focuses on the restraint of trade contract, definitions, and theories around the agreements in such contracts. This is followed up by a review of the restraint of trade payments, in order to provide further context to the present study. Finally, the literature presents an overview of restraint of trade within the South African context.

### **2.1.1) Financial Services Industry**

Since 1994 the financial services industry has experienced significant expansion into African countries as indicated by Khumalo (2008). Furthermore, South Africa facilitates more than a third (36%) of all direct foreign investment into sub-Saharan Africa (Asiedu, 2006). Thus the financial services industry plays an important role, especially in the South Africa context.

In describing the impact of the global financial crisis on the South African financial services industry, the South African Reserve Bank (2011) has indicated that prudent financial regulation and risk management along with limited exposure to highly leveraged securitisation instruments have played a role in sheltering the industry from the negative effects of the crisis.

Regulatory and governance frameworks such as King II have been reasonably effective in providing stability through the financial crisis. As shown by International Monetary fund, South African financial services industry has been able to absorb shock of the crisis, despite reaching the highest level of household indebtedness, capital and reserve cushions (International Monetary Fund, 2008).

Academic and business literature on payments in relation to restraint of trade payments within South African financial services companies is limited. A recent study identified noticeable structural changes in the way executives in the banking industry are paid indicating a move towards greater use of incentives (Olivier, 2008).

The understanding of the misaligned or the gap of financial payments is important as it is seen as a cause or contributor of the financial crisis and has been shown by a panel of corporate banking and law scholars, local financial services executives and bank regulators. The level of importance has also been consistently cited as shown by Aronson (2010).

The focus has shifted greatly from merely compensating executives to the quantum of restraint of trade payments paid to executives and attention has geared towards restraint of trade payments as evidenced in recent headlines such as “Questions arise when parting is such sweet sorrow” (Business Times Live, 2012).

Numerous studies focus on the underlying philosophies, structures, and practices that shape remuneration rather than the level of payment received upon the exit of executives, when a restraint of trade agreement exists.

## **2.2) Restraint of Trade Contracts**

### **2.2.1) Definition**

According to a PriceWaterHouse Coopers report (2011) a restraint of trade contract is a one in which a party (the employer) agrees with any other party (the employee) to restrict his or her liberty in the future to carry on trade with other persons not party to the contract.

According to Luckman (2007) two distinctly different forms application of contracts in restraint of trade exist, namely:

- In employment contract sphere and
- In competition law sphere.

The competition restraint of trade are typically utilised in instances of the sale of a business where the buyer and the seller enter into a voluntary contractual arrangement, typically restraining the seller from operating a defined commercial activity within a confined geographical area, for a fixed period of time.

The form of contract herein referred to in this present research across the whole document, is the restraint of trade in the employment contract sphere.

Restraint of trade is defined by Lubbe & Lotz (2003), as an agreement by which someone is restricted in their freedom to carry on trade, to practice their profession, carry on trading or pursue a business or other economic activities of similar nature within a stipulated time period.

According to Du Plessis and Davis (1984) a restraint of trade agreement, is one where one or more party to the agreement contract is restrained from engaging in commercial activity.

Furthermore, Basson et al. (2001) qualified this definition by stating that a restraint of trade prohibits a former employee from exercising his or her trade for a specified period in a specified area after termination of the employment relationship.

## 2.2.2) Elements of a Restraint Of Trade Contract

As indicted by those who have defined the restraint of trade, the aim of restraint of trade contracts, is to place restrictive cuffs, either to protect intellectual property (IP), trade secrets, information, or to maintain a certain degree of control over competition. For many companies to achieve such results, employers have to ensure that the following components are contained in restraint of trade contract, especially in the employment context.

### **Territorial Restriction:**

The competition business sphere has changed, thus because of the increased technical and scientific knowledge used in business today, the emphasis on research and development, the new products and techniques constantly being developed, the nation-wide activities (even world-wide in some instances) of many business enterprises, and the resulting competition on a very broad front, the need for restrictive agreements to protect the interest of the employer becomes increasingly important.

According to Huttler (2010), many companies would rather place restriction at a level of territory which allows them the modern view that the reasonableness of the territorial restraint depends not so much on the geographical size of the territory as it does on the reasonableness of the restriction.



The permissible territorial coverage of a competitive restraint of trade contract is limited to that area in which the employer could suffer economic harm from through the employee's activities.

### **Activity Restriction:**

The activity restriction places a trade restriction on an employee, where the activities are similar to the nature of the activities that the employee was engaged in during the course of his employment. (Huttler, 2010)

This is a restraint which prohibits the employee from obtaining employment with a competitor of the employer in any capacity.

It is the most common restriction, especially in Corporate South Africa. In many companies it does not stand alone; it has another element added to it – restriction time period, where a period of restriction is stipulated.

### **Time Restrictions:**

Huttler (2010) also brings in an interesting view where he states that for many companies to restraint over time gives the hypothetical leverage to slow down competition. The permissible length of time of the restraint is depended upon the interest that the employer is seeking to protect.

Where the Restraint-Of-Trade agreement is being imposed for the purpose of protecting the employer's trade secrets, the scope of trade secret protection should be justifiable. The actual length of protection depends, however, upon one's success in keeping a secret, and it is subject to being lost by

independent discovery of the information and other fair means of acquiring the trade secret.

At issue here, is what, then, would constitute a reasonable period of time for a trade secret which will be of continuing value and give a competitive advantage to its owner as long as no one else has legitimately acquired it.

These factors amongst others are imperative in defining and outlining the terms that will eventually impact on the restraint of trade payments.

### **2.2.3) Theories around Restraint Of Trade Employment Contracts**

There are three major underlying theories that are found to play a major contributing role in the structure and definition of restraint of trade contracts, namely the Market Theory, the Individualistic Theory and the Utilitarian Theory.

Adams and Brownsword (2004) show that Individualistic Theory in line with the Market Theory focuses on the voluntary choices of parties to enter markets, choose their fellow contractors and conclude binding contracts on their own terms. This constitutes the broad notion of freedom of contract and incorporates the value of freedom of trade.

The Market Theory affirms the notion that bargains freely entered into should be upheld.

Both the Individualistic and Market Theories support the principle of the

sanctity of a contract. However covenants in restraint of trade agreements further bring the principle of freedom of trade sharply into focus, as they stipulate the curtailment of economic activity which has to be approached with a degree of caution.

In following Pretorius (2009), a utilitarian perspective can be used to determine whether an employee's mobility restrictions are beneficial from a public policy perspective. Utilitarianism typically takes an ends-based, rather than means-based view to evaluate the morality of an outcome, with the goal of producing the greatest amount of happiness for the greatest number of people. Generally, Utilitarian Theory applies a cost–benefit analysis not only of the interests of individual parties but also of the overall outcomes for society. Thus, to determine the ethics of mobility restrictions the weight of the benefit gained by employers, employees, and greater society through permitting the enforcement of each type of restriction versus the cost incurred by employers, employees, and greater society should be ascertained and analysed. Where the benefits outweigh the costs, ensuring the greatest good, then there is an ethical basis for permitting mobility restrictions under utilitarian analysis.

The above theories have made it easier to judge their ethical elements, practicality and enforceability of restraint of trade contracts.

#### **2.2.4) Enforceability of Restraint Of Trade in South Africa**

Deloitte & Touché Legal (2004), share that the debate of whether restraint of trade agreements are enforceable or not, has raged for many years, and has left many open questions. This area of the law often remains unclear, and a number of misconceptions have arisen as a result. The following are some of the common misconceptions that currently exist in respect of restraints of trade:

- Restraint of trade agreements are no longer enforceable in view of Section 22 of the Constitution (Section 22 provides that every citizen has the right to choose his trade, occupation or profession freely).
- A restraint is enforceable only if the employee is paid a restraint payment.
- Unclear or unfair clauses in an employment agreement protecting the employer's confidential information, trade secrets, intellectual property and preventing an employee from soliciting customers or fellow employees are also seen as restraints of trade (Constitution of the Republic of South Africa, 2006).

Restraint of trade agreements remain a valuable mechanism utilised by employers to protect their business interests.

For quite some time the courts in South Africa adopted conflicting approaches when the validity of restraints of trade in employment contracts was challenged by one of the parties to the contract. Some courts preferred to

follow the English approach based on the freedom to trade, whereas others preferred the Roman-Dutch principle that values the sanctity of contract.

The general rule in English law is that all restraints of trade in contracts are at first appearance unenforceable. They will be enforced only if they are reasonable with reference to the interests of the parties, and the public interest.

Prior to 1984, South African law followed the English Law regarding restraints of trade, namely, that all restraints of trade were viewed as contrary to public policy and therefore *ab initio* void.

In 1984 the Appellate Division in the *Magna Alloys* case ruled that the English approach was not suitable to South Africa and that a valid contract overrides the right and freedom to trade. Restraints of trade are therefore deemed *prima facie* valid and enforceable, unless they are contrary to public policy, in which case they will not be enforced. (Deloitte & Touché Legal, 2004)

As a result of the *Magna Alloys* ruling decision, restraints of trade are contracts are therefore at first appearance deemed enforceable.

Several judgments after the advent of the Constitution merely confirmed the common law principles pertaining to restraint of trade agreements and held that these agreements were not in conflict with constitutional principles. In *Magna Alloys* the Appellate Division held that a contract in restraint of trade is enforceable as any other contract freely entered into, unless it is against public policy (Calitz, 2011).

In South Africa, restraints of trade in employment contracts are prima facie valid and enforceable, provided they are not contrary to public policy, which is defined as follows:

- The principles, often unwritten, on which social laws are based.
- The principle that injury to the public good is a basis for denying the legality of a contract or other transaction.

According to by Grossett and Landis (2006), although public policy requires that agreements freely entered into should be honoured, it also requires, generally, that everyone should be free to seek fulfilment in business and their profession. An unreasonable restriction of a person's freedom to trade, as concluded in the Magna Alloys judgment, would be contrary to public policy should therefore not be enforced.

A number of subsequent court cases have expanded on the Magna Alloys case, with the result that guidelines have been established to test the enforceability of restraints of trade. These tests are as follows:

- Is there a legitimate interest of the employer that deserves protection at the termination of the employment agreement?
- If so, is that legitimate interest being prejudiced by the employee?
- If the legitimate interest is being prejudiced, does the interest of the employer weigh up, both qualitatively and quantitatively; against the interest of the employee not to be economically inactive and unproductive
- Is the ambit of the restraint of trade (in respect of its nature, area and duration) justifiably necessary to protect the interests of the employer?

(Deloitte & Touché Legal, 2004).

As in many countries the factors that constitute the relationship between the employer and employee in South Africa are regulated by obligations and rights with sources in common law, custom and practice, contracts, and legislation.

Corporate governance guidelines advice boards of directors to ensure that the contract permits the company to terminate the executive's employment in a variety of situations, include agreed termination payments in advance (e.g. liquidated damages clauses); other terminations when determining payments; and that they should avoid making excessive payments in situations where the reason for the termination is that the executive has failed to perform (Shellan, 2007).

#### **2.2.4.1) Enforceability Approaches to Restraint Of Trade in Employment Contracts**

Courts in South Africa have used conflicting approaches when relating to issues regarding the validity and enforcement of restraints of trade in employment contracts.

According to a legal paper by Pretorius (2009), other courts were satisfied that the Roman-Dutch principle that valued the sanctity of contracts reflected the proper position in South Africa in respect of the validity of restraints of trade.

At common law, all contracts that are seriously concluded by persons with the necessary contractual capacity are valid and enforceable. Thus the principle of sanctity of contract is expressed in the maxim *pacta servanda sunt*. It is through this, that the principle has found its way into South African law through the works of various Roman-Dutch jurists. Grotius considered this to be one of the basic principles of natural law.

### **The Traditional Restraint Doctrine**

The traditional restraint doctrine, which the courts favored under the influence of English law, essentially was that covenants in restraint of trade were *prima facie* void and unenforceable, unless the covenantee could prove that the restraint was not contrary to public interest (Pretorius, 2009).

### **The Common Law**

The common law, reinstated by *Magna Alloys*, emphasized sanctity of contract and regarded such covenants as entirely valid unless inimical to the public interest, in which event they would be unenforceable.

Pretorius (2009) states that the main point of contention regarding the common law approach is that public interest, is a fairly vague and amorphous notion and that more concrete guidelines regarding the enforcement of a restraint are required. It is also uncertain to what extent reasonableness plays



a role in determining the enforceability of such a contract.

A further consideration is that a restraint that is reasonable *inter partes* (between the parties concerned) could still be detrimental to the interests of the public. In actuality then, the traditional approach strongly influenced the manner in which courts set about resolving these matters in terms of the common law, which is created on precedents – there is no seeking of comfort.

## **The Constitution**

The constitutional approach focuses on the entrenched right in question and then enquires as to whether the limitation of the right is reasonable and justified in the circumstances. Freedom to engage in economic activity was initially entrenched as a constitutional right in Section 26 of the interim Constitution, in 1993, and then section 22 of the Constitution of the Republic of South Africa, 1996. The constitution states that a restraint is invalid for offending Section 22 of the Constitution unless the limitation of this right is reasonable and justified in the circumstances (Section 36).

## **The Three doctrines together**

Common law addresses the issue of restraint of trade more directly. Restraint disputes curtail from contractual obligations, therefore procedural and substantive issues peculiar to the law of contracts which may arise while the

central question still remains whether a contractual undertaking should be enforced in the circumstances or not.

The application of the traditional doctrine is still very much evident in the way in which restraint matters are adjudicated, in South African courts.

On a broader level, there is the enquiry which relates to the balancing of the values of freedom of trade and sanctity of contract in the specific circumstances and the common law approach is in line with the Constitution and actually gives concrete expression to the constitutional approach, while the former, although seemingly conceptually different, in practice applies the very same criterion of reasonableness *inter partes* that was integral to the traditional doctrine.

With the above, it seems then that even in the modern constitutional age, the South African law on restraint still owes much to the English law, without which it certainly would have been the poorer.

Based on the above, the enforceability of restraint of trade contracts as well as the nature of contracts, the variable and the factors that determine the payments, call for analysis and research.

### **2.3) the Nature of Restraint Of Trade Payments**

In many countries publicly listed companies are subject to much regulation of payments to senior executives and directors. In South Africa, regulation takes

the form of mandatory disclosure of all forms of remuneration received by key senior/executive personnel.

King III further provides advisory guidelines or principles which companies can choose to adopt or not, with a requirement to explain “if not, why not” should the company choose to not adopt the practices recommended and the JSE has made provision for such.

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### **2.3.1) The Restraint Of Trade Payment Clause: Compensation**

For many years, companies have placed a payment tag to restraint of trade agreements.

The payment is based on the fact that the employee may suffer hardship due to the restraint of trade being exercised.

While the cost of such a clause may appear high, the cost of not having a restraint of trade agreement in place may be higher.

### **2.3.2) The Restraint-Of-Trade Payments other than Parachute Payments**

Studies done by Yermack (2006) and Bebchuk and Fried (2004) examined termination payments other than golden parachutes, which were performed in the early 2000's. The study performed by David Yermack's examines the termination payments made to a sample of 179 *Fortune 500* CEOs who left

their firms during the period 1996 to 2002. It is here that David Yermack found that only 24 per cent of the CEOs in his sample received some or all of their termination payment in the form of liquidated damages (an amount agreed at the time the CEO started in this role).

### **2.3.3) Restraint Of Trade Payments and Termination Payments**

In many other countries like South Africa, few studies have been done on restraint of trade payments; Stapledon's (2005) study of termination payments to Australian executives was noted as the first such analysis of its kind, despite existing concern over remuneration of company executives. His study presented empirical findings based on the termination payments made to 40 executives of listed companies over the period 1999 to 2004 aside from a comprehensive survey of the academic literature, public policy analysis, and good practice guidelines relating to termination payments.

In his study Stapledon notes the average termination payment and show the median payment. From that study it is clear that the headline figure reported as a termination payment in the media does not discriminate between the actual termination payment and other accumulated payments legally. Stapledon (2005) has questioned whether liquidated damages clauses are the best way to deal with terminations, as the executive can be paid what is described as 'a lifetime income' via a termination payment, only to be re-employed within a short timeframe

Due to the limited amount of information on this subject, this present research will lean towards Stapledon's structure as it contains analysis and formulas,

methods as well as conceptual understanding of how these payments were calculated.

Often when these kinds of payments are made, they are seen to signify the end of the employment relationship between the executive and the company.

According to Stapledon, regulations of termination and restraint of trade payments have to balance the competing interests of an executive and the company outcome, especially where the termination is not due to misconduct. Although in the South African context the regulation is more around the contract and its enforceability, these payments seem to be made with two elements that are common with Stapledon's method of calculation.

The restraint of trade contracts contain the time period factor and the remuneration factor or the compensation factor.

These payments may be offered to employees who hold office on a permanent basis for a number of years and Stapledon analysed the time period, the payment made and the relationship as referenced and guided by the Corporation Act 2001. It is in this guidance by this document that the restraint of trade payments were made based on the aspect that it was calculated by reference to years (the number of years the employee was in office) and average annual remuneration, leading to the formula:

Total remuneration x relevant period

The above guideline is used internationally in calculating termination payments. The relevant period is the time that the person held office in the company, while total remuneration means the person's total remuneration received from the company and from related bodies corporate in the last three years of the relevant period. Most companies assume that three years, is a reasonable restraint period because there are tangible and intangible aspects to consider in such restraint.

The present research aims to shed light on current practice through both the empirical analysis of executive's service agreements regarding restraint of trade agreements and payments.

#### **2.3.4) South African Context**

This present research will briefly explore the broad issue of restraint of trade payments and focus more specifically on the financial services companies.

The literature pertaining to the restraint of trade payments is particularly limited within the South African context.

## 2.4) Conclusion from the Literature Review

The literature review provided an overview of the key aspects that shape the field of restraint of trade agreements. In particular, the Market Theory, and the Individualism Theory were shown as theories amongst other theories that have been hypothesised as alternative theories underpinning the restraint of trade contracts.

Numerous factors were identified as key considerations in the restraint of trade contracts. These include the territory restraint, time restraint, the activity restraint and the extent to which monitoring exists within the industry. Furthermore, increased competition appears to have led to an emphasis on the territory restraint, in restraint of trade contracts.

The financial services industry is a dynamic industry with a unique remuneration proposition.

There appears to be compelling arguments and conflicting results when we look at the doctrines around the enforceability of the restraint of trade. The research does, however, support the case for greater regulation of restraint of trade contracts, which should also be applied to the payment of such contracts as a means to provide greater stability and sustainability in the employment structures.

Greater regulation could have a negative impact on the relationship. Executives have the obligation to run a business in line with prescribed and required corporate governance, the responsibility of safeguarding and safekeeping the interests and confidential property of the business and the rights of employees insofar as freedom to trade is concerned, is it any wonder

that executives and companies are troubled how to 'get it right.' Perhaps the simple answer is finding a balance between the right to trade and be employed, the value payment linked to it and the preservation of the cornerstones of the business (Landis and Grossett, 2006).

By exploring the literature, the importance of understanding the factors that could be determinants of restraint of trade is better understood.

Even though there has been widespread interest in the concept of the restraint of trade contracts and the enforceability, very little attention has been focussed on explaining the quantum of restraint of trade payments and the perception around the payments.

The present research aims to research on the quantum of restraint of trade payments and the perception of executives of such payments.

The following chapter presents the main research questions that provide the direction for the present research study.



### **3) Chapter 3: Research Propositions and Questions**

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#### **3.1) Introduction to Research Questions and Proposition**

The research proposition and questions arose from the challenges and factors noted in the literature review and thus provided direction for the research methodology discussed in Chapter 4. As indicated by the literature reviewed, despite the amount of knowledge and advancement stemming from these developed economies, there is diminutive understanding of the determinants and factors surrounding the Restraint-of-Trade Payments.

#### **3.2) Research Questions**

The study also has two fundamental research questions:

##### **3.2.1) Research Question 1**

Is there evidence of the significance of restraint of trade payments in executive's employment contracts, in the financial services companies in South Africa?

##### **3.2.2) Research Question 2**

Is there evidence of the level of perceptions of executives of restraint of trade payments within financial services companies in South Africa?

### **3.3) Research Propositions**

1. The determinants of the restraint of trade payment paid to executives in financial service companies in South Africa.
2. Determination and analysis of the quantum of restraint of trade payments in the financial services industry in South Africa
3. Executive's perception of restraint of trade payments in the financial sector.

### **3.4. Summary of Research Questions**

Summarising the above, Research Question 1 aims to discover the determinants of the restraint of trade payments by examining factors that make up these payments to see if they are positioned well in these contracts.

Research Question 2 aims to show, make sense of, and analyse the quantum of payments made in financial services in the context of South Africa.

Research Question 3 investigates the perception of executives, of restraint of trade payments and their (employees) understanding to these payments in relation to the understanding of the companies that make such payments.

## 4) Chapter 4: Research Methodology

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### 4.1) Choice of Methodology

The research design was based on a qualitative methodology using non-probability sampling, which is convenient and purposive in nature. Qualitative research is “a technique that seeks to describe, decode, translate phenomenon” (Cooper & Schindler, 2006). The focus is on words and observations, such as stories, visual portrayals, meaningful characterisation, interpretations and other expressive description (Zikmund, 2003). The element of descriptiveness and exploration will surface. Zikmund (2003) indicates that the major purpose of descriptive research is to describe characteristics of a phenomenon. The present study aimed to ascertain the aspects or determinants of restraint of payments, the value add and the quantum of such payments in the financial sectors. Zikmund (2003) also states that descriptive studies are conducted when there is some previous understanding of the research problem. Descriptive studies seek to determine answers to questions such as who, what, when, where, and how (Zikmund, 2003).

The research questions in this study were aimed at investigating, senior executive’s perceptions of restraint of trade payments. Saunders, Lewis and Thornhill (2003) define the exploratory approach as a valuable means of finding new insights and asking questions. Saunders (2003) mention three ways of conducting exploratory research, namely: review of the literature,

talking to subject matter experts, and conducting interviews. As indicated, the research was exploratory and was aimed at expanding on existing literature.

The objectives of the study were achieved using a qualitative, empirical, analytical research methodology, which was more suitable because the study aimed to provide an in-depth description of a group of people through analysing responses received from semi-structured interviews. This method was used in order to understand how the research participants understand and experience the use of restraint of trade agreements. According to Mouton (2009), the participatory nature of the design minimises suspicion and distrust of the study with a concomitant increase in trust and credibility.

The present study answers the following questions:

- How significant are the restraint of trade payments in executive's employment contracts?
- And what perception do executives have of restraint of trade payments?

#### **4.2) Universe and Unit of Analysis**

**Unit of analysis:** In order to support the research propositions stated above, the unit of analysis for this study was executives at a financial service company that is listed on the JSE.

**Universe:** The universe is limited to financial services companies that are listed on the JSE.

### 4.3) Population

The population consisted of all executives who:

- Work for a South African financial institution
- Who have experienced a Restraint-of-Trade contract in their employment life
- Who have general understanding of the term
- Who reside in South Africa

The participants included a span of seniority level such as chief executives, deputy executives, heads of departments and senior professional employees.

With regards to the financial companies, the company population in the study includes all listed financial services companies. Due to de-listing and listing, the total number of financial services companies changes periodically. The below table indicates the population group.

**Table 1: Population group**

Absa	Liberty Holdings
African Bank	Mercantile Bank
Barnard Jacobs Mellet	Metropolitan
Brait	Momentum
Brimstone	Nedbank Group
Capitec Bank	Old Mutual
Clientele Life	Peregrine
Coronation Fund Managers	PSG
Discovery Group	Remgro
FirstRand Group	RMB Holdings
Glenrand MIB	Sanlam
HCI	Santam
Investec	Sasfin
JSE	Standard Bank
Kagiso Islamic Equity	Zurich

#### **4.4) Sampling Method & Size of Sample**

A non-probability sampling technique was used, which is described by Zikmund (2003) as a sampling technique in which units of the sample are selected on the basis of convenience. For the purpose of the present research, convenience and purposeful sampling was utilised to include people who were most conveniently available (Zikmund, 2003).

Semi-structured interviews were conducted with a total of 17 participants. Initially there were 19 participants and 2 asked to be removed. The selection criteria was based on the researcher's own judgement and ensured a balanced response from the various elements of the sampling frame.

The respondents needed to meet the criteria set out above for the population. The questionnaire interviews were conducted at the financial institution in South Africa due to ease of access and ease of obtaining permission to conduct the interview.

The researcher was referred to the participants by her contacts, her supervisor and HR managers of financial companies at the time the study was undertaken. The researcher was permitted to conduct the study in partial fulfilment of the requirements of her academic qualification. The participants' permission to participate in the study was also requested through a formal letter attached to the questionnaire and they consented to take part in the study. At the beginning of each semi-structured interview, the researcher reconfirmed the anonymity of the participants and requested permission to

record the interviews and discussions. Not all participants agreed to the interviews being recorded.

There is a need to accommodate disadvantage aspects; the variability and bias of estimates cannot be measured or controlled and projecting data beyond the sample is inappropriate (Zikmund, 2003).

## **4.5) Data Gathering and Research Instrument**

### **4.5.1) Research Instrument**

- A desktop method of obtaining information and
- A detailed interview questionnaire was used for the present study. The interview questionnaire was informed by the factors and variables previously highlighted in the literature review.

The interview questionnaire comprised of two parts:

- The first part (part A), positioned the research to the respondents and included instructions for more access to information. It also included a statement that participation is voluntary and that participants could withdraw at any time without penalty. All data was kept confidential and respondents remained anonymous.
- The second part (part B) comprised a series of questions to investigate the perception of executives around the restraint of trade payments.



#### **4.5.2) Data Gathering**

Data was gathered using a desktop method of collection. This provided insight into the determinants and the quantum of payments. The interviews were conducted, where information was collected via a questionnaire. Interviews were conducted at the respondents' location, which required the researcher to travel to the respondent's location (Zikmund, 2003).

#### **4.6) Data Collection and Analysis**

For research analysis, content analysis method was used to analyse data. Content analysis is a research technique for systematically analysing written communication or data.

Creswell (2008) indicates that a successful content analysis requires knowing the audience. Content analysis is a diagnostic tool; it is a means not an end.

#### **Content Analysis can be performed in the following manner:**

The researcher defines the content to be analysed. The second step is to define the audience.

- A suitable time frame is then chosen. This is a period to be measured.
- The counting happens and it is then followed by thorough analysis where the researcher applies the numbers to goals and determines success or failure.

#### 4.7) Research Limitations

- The sample taken was restricted to only 15 financial institutions and executives in South Africa
- Convenience sampling was utilised to select participants for the interview, hence no inferences can be made to the population
- The sample was restricted to the Gauteng geographical area
- The time frame for the project was limited to 2012 and therefore changes to interview results are anticipated as executives leave the market to participate in business.

A methodology is a guiding tool that provides direction for the research as it is undertaken to address the research questions. The results of the present study are presented in Chapter 5.

## **Chapter 5: Research Results**

### **5.) Introduction**

Chapter 5 presents a broad analysis of the descriptive statistics used in the present study, as well as a presentation of the results relating to the three main research questions stated in the previously.

#### **5.1) Qualitative Method**

##### **5.1.1) Description of sample**

In total, 17 executives participated in the semi-structured interviews for the purpose of this present study. Participants were in different senior positions and had relevant experience and knowledge of restraint of trade agreements in financial companies.

##### **5.1.2) Management Seniority Distribution**

The study focused on executives at different designates. Table 2 shows the different positions held by the participants. There are only three categories of seniority; middle management, senior Management and executive management.

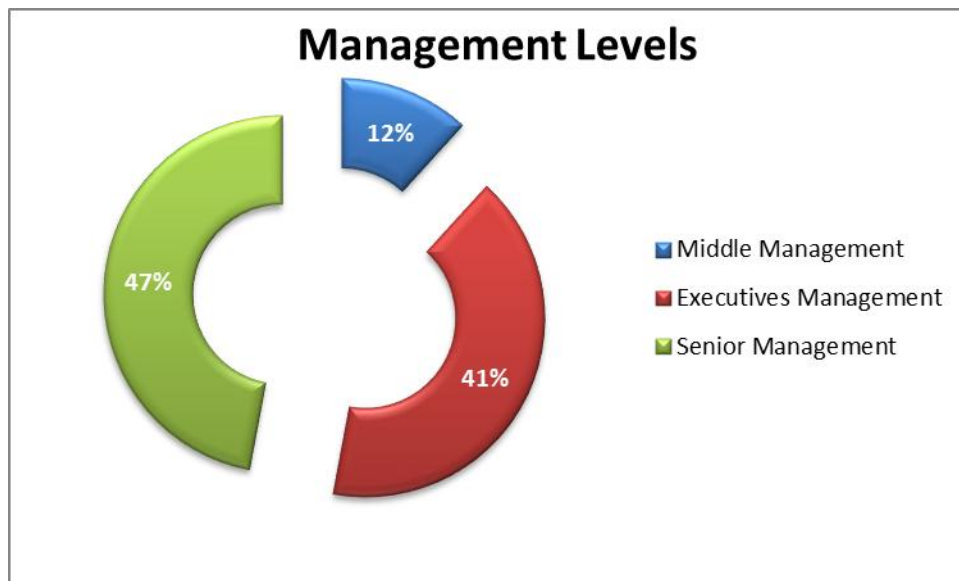
**Table 2: Sample Groups' Level of Seniority**

<b>Designation</b>	<b>Management Level</b>	<b>Number of Respondents</b>
Executive Human Resources Manager	Executive	4
Senior Human Resource Manager	Senior	2
Consultant	Senior	1
Project Manager	Middle	1
Chief Procurement Officer	Senior	1
Corporate Administrator	Middle	1
Corporate Lawyer	Executive	1
Account Development Manager	Senior	1
Managing Director	Senior	3
Directors	Executives	2

### **Level of Seniority**

As per Figure.1 below, the majority of the respondents were Senior Managers (47%), followed by Executive Managers (41%) and the remaining respondents were Middle Managers (12%).

**Figure 1: Distribution of Seniority**



## 5.2) Presentation of Interview Findings

Initially 19 respondents participated, however 2 participants retracted their questionnaires and their interview answers, leaving 17 participants. Many respondents asked to remain anonymous. To ensure that all respondents remained anonymous, each was each given a representative code where the first executive interviewed received the coded KR 1.

### 5.2.1) Question 1: What is your designation?

This question aimed to establish the respondents' position at work in order to ensure that they met the relevant criterion of holding an executive position, in order to participate in the present study. As seen from Table 2 and Figure 1, illustrates that the respondents met the criterion.

### **5.2.2) Question 2: Do you understand the term of contract, restraint of trade?**

The purpose of this question was to test whether the participants understood the concept of restraint of trade and to learn about respondents underlying assumptions, regarding the purpose and use of such contracts. 16 of 17 (16/17) respondents indicated that they did understand the concept, while 1 respondents (1/17) indicated a lack of an understanding. The 16 respondents illustrated their understanding of the concept through the following responses:

“A tool to control competition”;

“A method to curb trading of company secrets, used by employers”;

“A restriction of freedom of employment to preserve the trusted fundamental resources of the company and to protect intellectual property”.

From the above findings, it can thus be assumed that the majority of the respondents understood the term and are aware of its reasons of existence.

### **5.2.3) Question 3: Have you ever signed a restraint of trade clause in your employment tenure?**

This question was aimed at determining respondents' exposure to restraint of trade contracts, the nature of these contracts and the associated payments. Although many executives understand the term, some respondents indicated that they have never been exposed to the actual contract itself and thus their knowledge is based on external information available. This had an effect on

the further understanding of the contract, and the quantum. Of the 17 respondents, the majority, 14 respondents (14/17) had signed a restraint of trade contract at least once in their employment tenure.

When asked if they understood what they had signed and what it meant to their career at the time, many of the respondents explained that the contracts were not very clear and were often positively skewed towards the employer's interests. Older contracts dating years back did not stipulate an amount, quantum or any benefits and the term of restraint was almost indefinite or more than twelve months. These contracts only changed when the relevant legislation was amended. Most respondents who were subject to an active restraint of trade contracts proclaim that they know the period of restraint and know the quantum.

2 (2/17) respondents understood the term, but had never signed such a contract in their employment tenure.

#### **5.2.4) Question 4: What is/was the period on your restraint of trade contract?**

Table 3 below sets out the time period which the participants were restrained.

**Table 3: Periods of restraint as contained in restraint of trade contracts of respondents**

Period of Restraint		RESPONDENT																Count		
												K	K	K	K	K	K	K		
		KR	KR	KR	KR	KR	KR	KR	KR	R	R	R	R	R	R	R	R	R	R	R
		1	2	3	4	5	6	7	8	9	0	1	2	3	4	5	6	7		
0	Not Applicable																X	X	X	3
1	6 Months													X	X	X				3
2	1 Year								X	X	X	X								4
3	2 Years and above	X	X	X	X	X	X	X												7

This question helped to pave way for Question 5. If the period is known, it can investigate how the period was determined and if there was a model for the periods set. Periods of restraint varied between respondents, which could be related to their different positions/designations. Seven group executive managers had agreed to a period of restraint of two years and longer; senior management were subject to a period of between six months and one year, whilst middle managers had agreed to a restraint period of at least six months but less than one year. For those respondents who had never signed a restraint of trade contract, this question was not pertinent.

It can be concluded that, the period of restraint varies and increases in accordance with the level of seniority.



### **5.2.5) Question 5: How was the period determined?**

The purpose of this question was to establish the relationship between the period on the contract and the employment position and ascertain how these periods are set. The majority (12/17) of the respondents explained that there is no fixed model to assist employers in determining the period, except for the fact that it has to take into consideration the public interest policy. The majority indicated that the period was based on the number of years they had been employed with the company, the value obtained and the intellectual property which the employee has accessed since joining the company. KR 4 pointed out that his contract was on a “years of escalation” basis, meaning the more years he spent with the company, the longer the restraint period extended.

1 respondent (KR 5) indicated that his period of restraint applied throughout his employment and only be removed when he moved to a different sector or different industry. The remaining respondents were not affected by this question as they had never signed a restraint of trade contract.

### **5.2.6) Question 6: What is/was the value (The restraint of trade payment), Please provide an estimate of the value?**

Table 4 below sets out the total values of the restraints for each participant.

**Table 4: Payment Value Table**

Value/Payment	RESPONDENT																	Count			
	K	K								K	K	K	K	K	K	K	K	K			
	R	R	KR	KR	KR	KR	KR	KR	R	R	R	R	R	R	R	R	R	R	R	R	R
	1	2	3	4	5	6	7	8	9	0	1	2	3	4	5	6	7				
0 Not Applicable																		X	X	X	3
1 No value, contract void					X																1
2 R200k – R500k								X	X	X	X	X	X	X							7
3 R500k – R1m	X	X	X	X		X	X														6
4 R1m and above																					0

This question aims to follow on the question of how these payments around the contracts are made. It aims to build on the information that the payment is not just a set value; there are other determinants within this value.

The senior managers all had a value attached to their restraint of trade contract, ranging from R200, 000.00 to R500, 000.00. The executive manager’s payments were set at R500, 000.00 to R1m. The respondents again alluded to experience, level of responsibility and position within the company as elements that contribute to determining the value.

**5.2.7) Question 7: What are the determinants of the payment (Quantum: What is it made up of)?**

This question aimed to determine the quantum of restraint of trade contracts. The Table below shows how the respondents described the quantum related to their contracts.

2 respondents (KR 4 and KR 8) both have negotiated the payments upon their termination and an effective restraint period. The payments of KR 10 and KR 12 were based on their basic salaries. The remaining respondents (12/17) fell in the bracket of the Incentive quantum. KR 12 also fell within this bracket as his contract stipulates basic salary, percentage of company benefits and a fixed portion that is based on a performance bonus.

Table 5 below sets out the determinants of the restraint of trade payments.

**Table 5: Determinants of restraint of trade payments**

THEME	Responses to the Question: What are the determinants of the payment (Quantum: What is it made up of)?
<b>Not Applicable</b>	<p>“There was no restraint in place”. (KR 15, KR 16 &amp; KR 17)</p> <p>“It was not well structured and thus illegally enforced. As a result there was no value of payment”. (KR 5)</p>
<b>Negotiated</b>	<p>The contract value was negotiated between the employee and the employer and was agreed upon once the employee and the employer were satisfied with the contents.</p>
<b>Basic Salary</b>	<p>The payment was the equivalent of a set number of months’ salary for example, if restrained for six months, then the employee will receive six months’ worth of their basic salary.</p>
<b>Incentives</b>	<p>The quantum included :</p> <p>Share profits;</p> <p>Performance bonus and</p> <p>Percentage of the company benefits</p>

**5.2.8 Question 8: What are your perceptions around the restraint of trade as an employee?**

In trying to establish the perception of management of the restraint of trade contracts, Question 8 was asked with options to guide the respondents. Table 6 shows the options selected by the respondents in sharing their perceptions. They elaborated on their perceptions by selecting “other” and provided the following perspectives:

- “It is a tool to destabilize the career path of an individual after leaving the company.”
- “It does not work; it destroys the career of the ex-employee.”

- “The company tries to control competition and employee is paid not to work for that period.”
- “It protects company secrets”
- “It controls your career but you are paid for that. The company does not win anyway.”
- “It locks a person down, it is career limiting during that period unnecessarily. There is a shortage of skill set, although the job market is perceived to be intrusive or insensitive as it is saturated. How does the employee enter the market again?”
- “It does not work; one employee cannot make such a huge impact when talking to the competition.”

**Table 6: Perceptions around the restraint of trade contracts**

Perceptions	RESPONDENT																	Count		
	KR 1	KR 2	KR 3	KR 4	KR 5	KR 6	KR 7	K R 8	K R 9	K R 0	K R 1	K R 2	K R 3	K R 4	K R 5	K R 6	K R 7			
1 It is unfair					X		X			X			X			X	X			6
2 It is a tool with which detrimentally affects the career path of an individual						X									X					2
3 It sets a measure that limits uncontrollable elements that add to competition									X											1
4 It does protect the employer and the employee				X										X						2
5 It is fairly good	X	X	X					X			X	X								6

This table shows a wide dispersion of views ranging from “unfair to good.”

## 6.) Conclusion

This chapter set out the interview results as they were presented. The results were analysed using content analysis and key themes were identified. Where appropriate, the results were presented verbatim. The researcher concluded that based on the results presented, the research questions were adequately answered.

The results of Research Question 1 indicate that there is some level of significance of restraint of trade contracts and payments in executives' employment contracts. The results of Research Question 6 and 7 indicate a relationship between the period of contract and level of seniority. The results also show that the quantum is made up of known elements. The results suggest some degree of improvement.

Finally, the results of Research Questions 8 indicate the perception of the executives in of restraint of trade contracts and that they perceive the contracts to be limiting if not unfair.

In the next chapter, the researcher will interpret, analyse and provide clarity on the results of the semi-structured interviews and link these with the literature review. The chapter will also include an interpretation of the key findings.

## **Chapter 6: Interpretation of Results**

### **6. Introduction**

This chapter aims to give a brief interpretation of the data collected and the results, as discussed in the previous chapter. The objective of the present study was to investigate restraint of trade contracts, in terms of their value add, the quantum and the perception of senior executives.

#### **6.0) Interpretation of Results**

The data was analysed by means of content analysis. Each of the Research Questions asked will be discussed below.

#### **6.1) Respondents Contour**

##### **6.1.1) Interview Question1 (What is your designation)**

The population group consisted of executives from different companies in the financial sector. The interviews were conducted with employees from different levels, middle management, senior management (Head of Divisions), executive management (Managing Directors and Chief Executives), who met the requirements.

The criteria for participation in the present study were:

The (population) respondents were executives who:

- Work for a South African financial institution;
- Who may or may not have entered into a restraint of trade contract in their working life;



- Who have general understanding of the term; and
- Who reside in South Africa.

The designation question ensured selection of relevant participants. One could have expected the participation of more senior employees.

## **6.2) Respondents awareness and understanding of restraint of trade**

### **6.2.1) Interview Question 2: (Do you understand the term of contract restraint of trade)**

It was imperative to determine whether the respondents understood the construct by asking a general question on the subject and using interpretative methods to derive meaning from their responses. This confirmed respondents understanding of the concept, and elicited respondents' definition thereof.

Whilst many definitions exist around the term, and amongst other written literatures, Lubbe and Lotz (2003) define the term restraint of trade agreement, as an agreement by which someone is restricted in their freedom to carry on trade, their profession, business or other economic activities of a similar nature within a stipulated time period.

Of the 17 respondents, only 1 responded was unable to define the term and 16 of the respondents understood the term and its implications, which are centralised around the restriction of freedom to trade (control) in employment, over a period of time.

### **6.3) Nature of the restraint of trade contract**

#### **6.3.1) Interview Question 3: (Have you ever signed a restraint of trade contracts clause in your employment tenure)**

One respondent could not relate to the term nor could he define it. The respondent had never come across such a contract; whilst 2 (12%) of the respondents understood the term of contract, restraint of trade, but had never been exposed to such a contract. Of the 17 respondent only 82% (14/17) had been exposed to such contracts, some of which were current.

In South Africa, restraints of trade in employment contracts are valid and enforceable, subject to the contract not being contrary to public policy as defined in Chapter 2.

According to Grossett and Landis (2006), although public policy requires that agreements freely entered into should be honoured, it also requires, generally, that everyone should be free to seek fulfilment in business and in their professions.

The respondents indicated that although they were aware of such contracts, they did not fully understand what they were signing and indicated that the following elements were cause of concern:

- The terminology used in the contracts was unclear;
- The restraint period curbed employee careers, thought they had a financial protection (which is the value of the restraint);
- Some contracts did not contain any restraint payment;
- The contracts were almost always in favour of the employer; and

- The contract sometimes did not stipulate the restraint payment or the period.

Many respondents found themselves signing due to the need for employment and the financial and social needs surrounding their lives.

-

## **6.4) The Restraint Period**

### **6.4.1) Interview Question 4: (What is/was the period on your restraint of trade contracts)**

Activity restraint is the most popular way to restrain employees in many corporates (Huttler, 2010), where the employee is restrained from trading in the same activities and in the same industry as his previous employment. This term does not often stand alone in these contracts it is correlated with time to it, which is the restriction time period.

Huttler (2010) states that restraint over time, provides companies with the hypothetical leverage to slow down competition. In many cases enforceable length of the time restraint is dependent upon the interest (intellectual property) that the employer is seeking to protect.

The actual length of protection however depends, however, upon one's success in keeping a secret, and it is subject to being lost by independent discovery or other fair means of acquiring the trade secret.

The results regarding the time period of restraint were reported in Chapter 5, showing a period of restraint that is commensurate with seniority. Executives' were restrained for a period of 2 years or more. Senior Managers were restrained for a period of 6 months to one year, whilst middle management was restrained for at least six months but less than one year.

Some respondents indicated that their period of restraint was incremental (escalation basis). The number of years of employment would inform the length of the restraint period.

Some respondents felt that the restraint period is the one factor amongst others in the contract that has a much greater negative impact on their mobility to re-enter the ever changing and fast paced job market.

Based on the results it seems as if employers are not necessarily focusing on the short term competition, but rather the long term. However they continue to ignore the impact of technology, new skills, core capabilities and core competencies that are in play everyday,

A reasonable duration of restraint period would seem to be acceptable at a level of minimum six months and reasonable maximum of two to three years.

## **6.5) Factors determining period**

### **6.5.1) Interview Question 5: (How was the period determined?)**

12 respondents ((12/17=71%) were unable to confirm that a model was used to determine the period of restraint, or if any guidelines were adhered to. 1 respondent indicated that his period of restraint was indefinite. The contract,

stipulated restrictions of both activity and territory within the same industry. 1 respondent was a party to a contract according to which the restraint period increased in accordance with the number of the respondents was employed by the company. The other 3 respondents could not participate in this question as they had never entered into such an agreement, although they displayed a general grasp of the concept.

The restraint of trade contracts often stipulate compensation for the relevant restraint.

These restraint payments are offered to employees who will hold office on a permanent basis for a number of years. Stapledon (2005) states restraint of trade payments are calculated according to the number of years the employee was in office.

According to Stapledon most companies assume that three years or more, is a relevant restraint period, tangible and intangible aspects gained over time (experience) need to be considered.

Amongst other guidelines to determining a reasonable period of restraint, employers should consider the fast moving market and the period that causes employees skills to be obsolete, making it very difficult for these employees to re-enter the labour market.

## **6.6) Value of the restraint of trade contract**

### **6.6.1) Interview Question 6: What is/was the value (the restraint of trade payment) Please provide an estimate of the value**

Respondents knew what the value of their contracts were, but could not base it on any formula. The value of such contracts varied.

Respondents in executives roles had a much higher value stipulated in their contracts (R500, 000.00 to R1m), and senior managers payments ranged between R200, 000.00 and R500, 000.00. It is also evident that the number of years within a company and experience do play a contributing role in calculating the payment and how it should be treated.

According to Bebchuk and Fried (2004) in their paper about executive Pays and Corporate governance, they show that corporate governance guidelines offer advice to boards and company on how to treat termination of executive's employment in a variety of situations with reference to misconduct; agreed termination payments, current and in future (by liquidated damages clauses, for example), and distinguish between terminations for misconduct ('for cause') and for other reasons. They also state that companies should avoid making excessive payments.

According to Stapledon, termination and restraint of trade payments have to balance the competing interests of an executive and the company outcome, especially when the termination is not due to misconduct.

Based on the above we can infer that the level of responsibility and the position held also play a significant role in determining the period and the

value payment. It is pertinent to look at the full breakdown or the components of such payments in order to consider how best to understand the calculations.

The next question aimed to investigate how different companies, within the same sector/ industry determine restraint payments.

## **6.7) Quantum factors**

### **6.7.1) Interview Question 7: What are the determinants of the payment (Quantum- What is it made up of?)**

Often when payments are negotiated the one party often sacrifices to an extent depending on what is at stake.

2 (2/17 = 12%) of the respondents were fortunate enough to have been in a position to negotiate their restraint payments with their employers, before signing their contracts. Another 12% of the respondents indicated that their payments were based on their salary, where they would be paid the equivalent of current salary during the restraint period. 1 respondent signed a contract that did not stipulate a value, whilst some respondents had no exposure to such a contract could not part take in this question. The other respondent's payments were in what we termed the "Incentive Quantum".

Their payments were structured according to their incentives:

- Performance bonuses;
- Share options;
- Share of profits; and
- Percentage of company benefits such as medical aid during the restraint period.

In a study conducted by Stapledon, he notes the average termination payment, shows the median payment. In this analysis it is shown that the figure reported by in the media as a termination payment does not discriminate between the actual termination payment and other accumulated payments. Stapledon (2005) examined whether liquidated damages clauses are the best way to deal with terminations, as the executive may be paid what is described as “a lifetime income” via a termination payment, only to be re-employed within a short timeframe.

A treatment of share-based payments in termination payments has to be considered as these shares vest immediately or according to the original vesting schedule.

The results of the present study do not indicate how companies treat share options, termination payments and restraint periods. In relation to the share option the assumption is that they are paid over time as responsibly as possible.

It seems that payments in South Africa are calculated making reference to is the literature written by Stapledon on the below model of payment.

Total remuneration x relevant period

3

Stapledon shows how some of these payments are made and distinguishes between actual termination payments and other liquid clause payments.



## **6.8) Perceptions on restraint of trade**

### **6.8.1) Interview Question 8: What are your perceptions around the restraint of trade as an employee**

The primary stakeholders in restraint of trade contracts are the employee and the employer, secondary to what they aim to achieve and the law tools around them.

The understanding and perceptions of the employees regarding restraint play a vital role as they have an impact on the willingness to sign and the restraint of trade agreement.

The respondents' perceptions of a restraint of trade agreement are that it is used to contain secrets and gain a competitive advantage, but also that it is not reasonable and in many ways, detrimental to employees.

Respondents perceive these contracts to be unfair in that they hinder employee's career progression.

Respondents also felt that it does a single person cannot cause that much competition in an industry that has access to so much skill sets, core competencies, core capabilities, strategies and knowledge to play and sustain the company in the market space.

The other perception around the restraint of trade contracts is that it locks down an employee unnecessarily when the job market is perceived to be insensitive as it is saturated.

Respondents also highlighted their understanding of contract protecting interests of the employers by mainly protecting the company against detrimental competition and safeguarding intellectual property and trade method.

Basson *et al* (2001) qualifies restraint of trade where they state that an employee is prohibited from exercising his or her trade for a specified period in a specified area after termination of the employment relationship.

Many literatures align with the employers' motive, however not much is written on the employees' perspective to further elaborate on what the respondents perceive or understand about Restraint-Of-Trade contracts.

## **6.9) Limitations**

In this study the below have been categorized as limitations:

The study was confined to financial companies in South Africa and as such the results may not be transferable to other organisations, which could enhance the value of the research.

While 19 participants were identified and 2 withdrew, leaving 17 participants who participated in the study and while this was acceptable in terms of the academic requirements as this was a qualitative research study; the sample was not large enough to make generalisations.

The participants were all in management positions, excluding those who may not be at management level but may have substantial amount of years of general experience and knowledge of restraint of trade contracts relating to, for example intellectual property.

Thus, there is a need to exercise caution when considering transferability of the findings to other contexts.

The study was limited by geographic means as it only focused on executives in the Gauteng area due to accessibility. This eliminates ever determining if geographical aspects also play a role in such contracts or restraint of trade payments.

Overall, it is important that the findings be assessed within the context of financial companies in South Africa, and the global environment at the time when the data was gathered.

## **6.10) Conclusion**

The researcher found that the majority of the respondents had an understanding of the term “restraint of trade” within the context of the financial companies in South Africa. However one of the respondents indicated not being aware of the nature and existence of such contracts.

Based on the responses received, it is clear that the restraint of trade contracts are not well received by employees. The researcher was able to identify the following perceptions as put forth by the majority of the respondents regarding a restraint of trade contract:

- It is career limiting;
- It is unfair; and
- It is employer focused.

The study has met the research objectives by demonstrating the overall awareness amongst employees of the nature of such contracts, the quantum and the stipulations contained therein.

The overall results were compared on a question to question basis, highlighting the important issues of the study.

In the following chapter the researcher will discuss the results and provide a summary, together with conclusions and recommendations.

## **Chapter 7: Conclusion and Recommendation**

### **7.1) Introduction**

Chapter 7 contains the summary of the research objectives, the major findings of the research, and contributions of the research to the existing body of knowledge. Recommendations and suggestions for future research are identified and then followed by a conclusion.

#### **7.1.1) Motivation and aim of study**

The aim of this study was to determine how restraint of trade payments are determined, and the perception of executives regarding these payments in the financial industry in South Africa.

South Africa is growing in importance in the international landscape especially as a platform for capitalising on African opportunities (Business Day, 2011). Thus it is wise to project the use of acceptable practices with reference to employment.

In reading many newspaper articles and reading about executives and recent payments made to South African executives, the misconceptions and some level of misunderstanding of the restraint of trade agreement warranted for some study, and that became my point of interest.

Although the research paper focuses on financial services companies, many companies grapple with the concept of restraint of trade as these are commonly utilised in employing executives.

### **7.1.2) Value add of study**

The value add of this study is the findings that the literature review indicates that the restraint of trade contract is a useful tool and the employees have a negative perception of its application. The present study will enable employers to understand employees' perceptions of these contracts.

This study has confirmed that traditional benefits, that competition can be curbed, that restraints are acceptable despite the relevancy of period, term or payment is to be questioned. The study has also confirmed that perceived understanding of the actual intention of the contract can play a role in the perception of employees.

The present research has confirmed that employees would like to see a different approach to structuring restraint of trade

## **7.2) Key Findings**

### **7.2.1) Empirical Findings**

The following are the key findings of the present study:

The present study was able to access employees' perceptions, views and feelings on how the restraint of trade contracts. Although the sample consisted of only 17 participating employees, the research results indicated a consistent perception of there being such unfairness. These findings are also in line with previous researches conducted.

To answer the secondary research objectives, the researcher performed content analysis to identify the stipulations contained in such a contract, impact and how they are determined. With regard to rewards and the period of restraint it was concluded that these are set by the employer as he deemed fit. It was thus the responsibility of the employee to accept or to reject the offer.

The researcher found that whilst the respondents were aware of what rewards (if any) a restraint of trade contracts entailed, they were unable to articulate the primary structure of the contracts, This finding indicates that there is a need for continued education or awareness campaigns regarding the nature of Restraint-Of-Trade contracts.

An interesting observation from the findings is that whilst other factors were in play. The most worrying was the time period factor which could be set

anything from six months to indefinite and an escalation year method could be used to restraint an employee. These findings do not necessarily speak to the previous research on the subject but are positively skewed towards inequality of term in these contracts.

The findings also showed that although it is possible to suggest that the number of years of employment have an indirect effect on the restraint payment and that experience also contributes to determining the value payment, it is not physically provable.

Perception of employees may mean that employees are crying out that there is need for a shift of mind-set in terms of employer preferences of these contracts over the years. Whilst the research has revealed that competitive remuneration levels and flexible remuneration packages are top in terms of rankings, it was interesting to note that perceived “lack of fairness” in these contracts was mentioned by most of the respondents as a key factor to consider.

### **7.3) Recommendations**

This research has highlighted employees’ perceptions, views and feelings about the effectiveness of the restraint of trade contract as a way of gaining competitive advantage. The research has also revealed that there is a need for on-going communication, education and simple clarity on the purpose of the contracts, the importance of such contract and transparency on what it aims to achieve. This will facilitate increased awareness of the contract and



will also assist in ensuring that the right objectives intended by implementing this contract, are met.

It is further recommended that a standard model be used to determine the correct restraint period, at different organisational levels, which may include methods of calculation.

The employees may sign these restraint of trade contracts because it is a prerequisite to have. It is recommended that issues relating to period and payment disparities in these contracts be reviewed on an on-going basis; make the contracts flexible by allowing a fair discussion around period and payment. It should allow that ad hoc adjustments are considered to deal with any incorrect perceptions.

A robust process of how these should be structured is needed.

#### **7.4) Suggestions for future study**

There is no evidence that the findings of the present study on the perceptions of employees around the issue of restraint of trade contracts would be the same when using for a larger sample size.

There is a need to conduct further research to ascertain whether, gender, education level or employee band would have an impact on the structure of these contracts.

In the present study, a qualitative, semi-structured interview process was used to obtain data and content analysis was applied. A follow-up study using a quantitative method could be conducted to ascertain whether the findings indicated in the current research would be the same.

Another recommendation is that companies should ensure that the contracts are simple and easy to analyse and understanding.

## **7.5) Conclusion**

Companies' benchmark, their performance, they perform market analysis, they look at industry averages and often the competitor's sudden turnaround is attributed to product innovations, clever marketing, good strategic alignment or possibly providence. However in some instance the competitor's increased performance is ascribed to the employment of one of another company's former employees who has divulged certain trade secrets and other confidential business information to the current employer, hereby creating a competitive edge. This has led to the use of restraint of trade contracts, which may include compensation for such restraints.

The study was aimed at exploring employees' experiences, and perceptions regarding restraint of trade contracts. It did so by engaging a group of executives, senior managers and middle managers in financial services companies.

A questionnaire was used to gather data, which was obtained (qualitative research) and content analysis was applied further. The findings revealed reasonable correspondence with several studies that engaged different research populations such as the research conducted by Stapledon. The study also tried to answer the quantum question, though there were no significant conclusion one could draw from the quantum question and the restraint period.

It is safe to conclude that although the concept of restraint of trade is understood by employees, the actual aim of what these contracts aim to achieve, is not understood by both the employer and the employee yet.

However the study does not show whether we can or cannot assume a standard application method for the factors and contents of these contracts.

## 8) Appendix 1: Questionnaire

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### QUESTIONNAIRE CONSENT LETTER

#### TOPIC OF RESEARCH \_"RESTRAINT-OF-TRADE PAYMENTS IN EMPLOYMENT CONTRACTS"

I am a GIBS (Gordon Institute of Business School) MBA student and I am conducting research on Restraint-Of-Trade Payments in Financial Services in South Africa. I am trying to acquire more information about the subject of Restraint of Trade Payments in employment contracts of executives in financial service companies in South Africa. The interview and or completion of the questionnaire will further assist to understand how the payments are made and the quantum of Restraint-Of-Trades within the financial services companies.

*Please kindly note that your participation is voluntary and you may withdraw at any time without any penalty. All data will be kept confidential and no names will be mentioned.*

Hope the above is in order and for any queries please kindly feel free to contact me or my supervisor. Our details are provided below.

Researcher Name: Keneiloe Moumakoe      Research Supervisor: Dr. Mark Bussin

Email: [keneiloe@homemail.co.za](mailto:keneiloe@homemail.co.za)/[keneiloem@mweb.co.za](mailto:keneiloem@mweb.co.za)

Email:[drbussin@mweb.co.za](mailto:drbussin@mweb.co.za)

Phone: +27 82 821 6932

Phone: +2782 901 0055

Signature of Participant: \_\_\_\_\_

Date: \_\_\_\_\_

Signature of Researcher: \_\_\_\_\_

Date: \_\_\_\_\_

## QUESTIONNAIRE ON RESTRAINT –OF-TRADE PAYMENTS IN EMPLOYMENT CONTRACTS

1. What is your designation?

.....  
.....

2. Do you understand the term of contract, Restraint-of-Trade?

YES		NO		MAYBE	
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If Yes, share your  
understanding.....

.....  
.....  
.....  
.....  
.....

3. Have you ever signed a Restraint-Of-Trade clause in your employment  
tenure?

YES		NO	
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4. What is/was the period on your Restraint-Of-Trade contract?

6 months		1 year		2 yrs. and above	
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5. How was the period determined?

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6. What is/was the value (The Restraint-Of-Trade payment), Please provide an estimate of the value?

R		R		R 1m and	
200,000.00		500,000.00		above	
–		– R 1m			
R500,000.00					

7. What are the determinants of the payment (Quantum: What is it made up of)?.....

.....

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8. What are your perceptions around the Restraint-Of-Trade as an employee?

- It is unfair
- It is a tool used to deteriorate the career path of an individual
- It sets a measure that limits uncontrollable elements that add to competition
- It does protect the employer alongside the employee
- It is fairly good
- Other.....

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Thank you for participating, this will assist to further build on the Research regarding Restraint-Of-Trade Payments.

Date: \_\_\_\_\_

Researcher Name: ...Keneiloe Moumakoe

Email: keneiloe@homemail.co.za

Phone: +27 82 821 6932

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