

Locutus

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

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Welcome to Locutus

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

Recent Cases -

In late 2006 there was a spate of cases concerning the misuse of confidential information (usually customer information) by former employees, and the enforceability of restraint of trade clauses. *Mid-City Skin Cancer & Laser Centre v Zahedi-Anarak* is of significant interest as it considers in some considerable detail whether the implied duty of confidentiality constitutes an asset of a business and whether the right to enforce such an obligation is capable of assignment. The Court refused to consider itself bound in regards to the latter by the judgement of Finkelstein J in *TS & B Retail Systems Pty Ltd v 3fold Resources Pty Ltd* (2003) 57 IPR 530 where his Honour found that confidential information could not be assigned as it is not property.

The second case reported in this newsletter deals with the construction of a clause pertaining to the right of termination found in many franchise agreements. It also considers the particulars that need to be provided in a Breach Notice in respect of a breach of a franchise agreement.

Mid-City Skin Cancer & Laser Centre v Zahedi-Anarak [2006] NSWSC 844.

Issues:

1. Ownership of medical records, pathology reports, and booking sheets.
2. Obligations of confidentiality of medical practitioner working in another's practice.

3. Ability to assign the contractual obligation of confidentiality to a purchaser of business assets.

This judgement explores the above issues in the context of a corporatised medical practice.

Short Summary of Facts.

Dr Zahedi-Anarak worked in a corporatised medical practice for some years. No written contract was entered into by the parties except a short form contract in which he did no more than acknowledge that he was not an employee of the practice.

The clinic was sold in 2001. The assets sold included goodwill, all medical and pathology records, and all other business records relating to the clinic. The agreement contained the usual warranties. Dr Zahedi-Anarak left the clinic with 95 pathology reports plus patient information and booking sheets. After leaving the clinic he commenced contacting former patients.

Ownership of booking sheets: the Court referred to *Health Services for men Pty Ltd v D'Souza & Others* (2000) NSWCA 56; (2000) 48 NSWLR 448 on the issue whether property in these documents had been alienated by their transfer to the doctor. Held no gift, no sale and no contract effecting a transfer of title in the documents.

Ownership in pathology reports: the Court held that the property in these report was vested in the patient with the clinic and the referring doctor having rights as bailees. Because Dr Zahedi-Anarak's position with the clinic was analogous to that of an employee it was the clinic that had a better title to these records.

Obligations of confidentiality of medical practitioner working in another's practice.

On this issue the fact that the clinic displayed a sign in reception stating that patients 'are the patients of the practice' played a significant part in the Court's determination whether there existed an implied obligation of confidence. The Court proceeded from the basis that any treating doctor is under a duty not to voluntarily disclose information which the doctor has gained in his professional capacity. It also acknowledged that the clinic itself owed a similar duty to each patient.

In the case of the pathology reports they were held to constitute customer lists as each bore the patients name and telephone number.

The Court concluded that Dr Zahedi-Anarak was bound by an implied contractual obligation to maintain

the confidentiality of the patient information. It also considered whether he was bound by an equitable duty re the use of this information. The Court stressed the need to identify the alleged confidential information with specificity. Found that he was bound to use this information only for the purposes of the clinic.

Breach of implied duty ?

The Court held that compiling the list of patients and contacting them or arranging to contact them was a breach of the implied duty of fidelity.

Standing of the Plaintiff to bring action/Assignability of Obligation of Confidentiality.

As there had been no dealings between the plaintiff and Dr Zahedi-Anarak, it would only have had standing to sue for breach if the benefit of the implied contractual term had been assigned to it.

As there was no written document dealing with the assignment of the legal chose in action, there was no effective assignment at law.

Was there an equitable assignment? The Court held that there was as the expression “*all right, title and interest of the Vendor*” in the business in the Sale Contract included in the Court’s opinion the benefit of the contractual covenants from the people working in the clinic. In addition, the Court held that the said benefit constituted an asset of the business.

Importantly, it the Court held that it is possible to assign a right to have information kept confidential. The Court reviewed a large number of cases bearing on this issue. In particular the Court refused to follow the judgement of Finkelstein J in *TS & B Retail Systems Pty Ltd v 3fold Resources Pty Ltd* (2003) 57 IPR 530 where his Honour found that confidential information could not be assigned as it is not property. The Court drew a distinction between the argument put to Finkelstein J to the effect that there had been an assignment of the actual confidential information and the argument in this case that there had been an assignment of a chose in action only. The Court was not prepared to venture into a consideration of whether confidential information is property.

Franchising

Aura Enterprises Pty Limited v Frontline Retail Pty Ltd [2006] NSWSC 902

The Court had to consider a number of issues including:

1. the extent of particularity and detail that a notice of termination must contain in respect of the relevant obligation and inconsistent state of affairs said to constitute the breach.

The Court held that a notice will sufficiently specify a breach if from its terms a reasonable recipient, who has knowledge of the terms of the contract, would, taking into account the surrounding circumstances, be able to identify the obligation and the manner in which it is alleged to have been breached – for which purpose reference to the relevant provision of the franchise agreement may in some cases suffice, but reference to facts describing how the breach is said to have occurred may sometimes also be necessary.

2. Clause 9 of the franchise agreement allowed for the giving of a notice of default in certain specified circumstances including - *“If and whenever there shall be a breach of any of the covenants and conditions herein contained and such breach continues for 14 days after service by the franchisor of a notice on the franchisee requiring him to remedy the same.”*

The franchisee argued that before the defendant could serve a valid Notice of Default pursuant to Clause 9 of the franchise agreement for a prospective termination pursuant to Clause 9.2, the defendant had to firstly serve the notice contemplated by Clause 9.2 and the breach must continue for 14 days after service of that notice. Only then, could a valid clause 9 notice be served.

The Court rejected that argument and held:

49 At first sight, the suggestion that a franchisee should be entitled to two notices to remedy before being in default so as to authorise termination is a surprising one. It is, to say the least, uncommon for a defaulting party to be entitled to two periods of grace or notice. Such a result would be so uncommercial and extraordinary that it is unlikely to have been intended. Clause 9 admits of an alternative construction, which is much more likely to have been intended, particularly given the apparent familiarity of the draftsman with the Code, including in particular reg 21.

50 The first sentence of cl 9 is a general provision, governing all terminations. Under it, the franchisor can terminate if a termination event listed in cl 9 has occurred, so long as it has given the requisite notice (which must comply with the requirements of the first sentence, and also comply with the requirements of the second sentence in those cases to which it applies). One of the listed termination events is a breach of covenant which continues for 14 days after notice to remedy has been given: sub-cl 9.2. Where the termination event involves a breach of the agreement, the reason for termination will be the breach continuing for (at least) 14 days after

notice to remedy.

51 Further, because a sub-cl 9.2 event is one of those specified in the second sentence of cl 9, such an event will authorise termination only if Aura has been informed what is required to be done to remedy the breach and allowed a reasonable time to do so. The second sentence of cl 9 refers to “the breach”, as does sub-cl 9.2, and not to “the event” or “the default”. The matters specified in sub-cl 9.1 and following sometimes but not invariably involve “breaches”, but all are “events”. Thus the second sentence of cl 9 governs a list of termination events, some of which involve “breaches”, but some of which do not. While this gives occasion to pause before concluding that “breach” in that sentence is a reference to the same “breach” as in, for example, sub-cl 9.2, nonetheless the better view is that it is. If it were otherwise, the reference to “breach” in the second sentence would have to be read as a reference to the failure to remedy the original breach of covenant within 14 days, but it is not possible to remedy such a breach - a failure to remedy the original breach within 14 days is incapable of remedy, because the time cannot be retrieved. Accordingly, at least in the context of sub-cl 9.2, the breach referred to in the second sentence of cl 9 is the same breach as that referred to in sub-cl 9.2, rather than the whole event constituted by sub-cl 9.2.

52 It follows that before Frontline can terminate under cl 9, pursuant to sub-cl 9.2 for breach of covenant, three conditions must be satisfied. The first is that Aura has been given notice to remedy and the breach has continued for 14 days thereafter [sub-cl 9.2]. The second is that Aura has been informed what is required to be done to remedy the breach and allowed a reasonable time to remedy it [cl 9, second sentence]. The third is that Aura has been given reasonable notice of the intention to terminate, stating the reasons for the proposed termination.

53 However, there is nothing that requires these three conditions to be satisfied consecutively, as opposed to concurrently, nor that there be separate notices to satisfy each of them. In my opinion, it is not essential that separate notices be served, first under sub-cl 9.2, and subsequently under the introductory part of cl 9, before the franchisor is entitled to terminate for breach of covenant. The same notice can require the breach to be remedied, specify what is required to be done to do so, allow a reasonable time to do so (provided that that reasonable time is not less than 14 days), and state that reason for the proposed termination, namely the breach continuing for (at least) 14 days after service of notice to remedy. The franchisee is not entitled to two notices to remedy and two periods of grace. The same notice can satisfy the requirements of the second sentence of cl 9, as well as the requirements of sub-cl 9.2.

And finally...

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