

March 2008

Law at work



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Taylor Wessing Immigration Breakfast Briefing

If points mean prizes, will *your* business be a winner?

Taylor Wessing invites you to a breakfast update on 24 April 2008 about the radical new points-based immigration laws that will affect **all** UK employers. More details to follow in next month's Law at Work.

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Features

Restrictive covenants – Time to act?

The latest case law on restrictive covenants and confidentiality suggests more likelihood of success in protecting business interests than ever before.

We have become used to being contacted by HR professionals in fits of rage about senior employees who have gone off to their company's most hated rival taking some of their team and some valuable information with them. Whilst the first reaction is to flay those employees within an inch of their lives, our experience is that there tends to be a reluctance to go beyond the odd nasty letter. This even happened in one case we dealt with where there had been an amicable negotiated exit with a compromise agreement. During those negotiations the individual had emailed himself some vital sales data from his company computer to his home computer. Not exactly a difficult trail to track you might think. Despite the fact that the company had the choice of pursuing him for breach of his compromise agreement without needing to take the route of an injunction, even then the Managing Director was not keen to go further than demanding undertakings from him that he would not pass the information to competitors.

Reluctance

So why this reluctance? Three main reasons in our view – cost, adverse publicity and risk.

There is no doubt that going down the injunction route is a costly process and should not be undergone lightly. However, it is not just this but the combination of the risk factor that has been putting companies off. Judicial opinion in the past has been generally in favour of the freedom of the market place and it has become a fairly standard piece of advice to give that non-competes in particular are notoriously unenforceable unless there is some highly confidential information to protect which can't be protected in any other way. Also non-solicitation/non-dealing covenants have been difficult to enforce for a different reason – namely the problem of getting enough evidence to show that the ex employee had acted out of turn. This was not even factoring in the problems of scrutinising the clause itself and risking the view being taken that on the wording it was too wide to be enforceable.

Perceived change in judicial approach

Although it can't all be said to have changed overnight, the spate of recent cases does seem to suggest that companies ought to consider being a little braver in their approach towards their senior employees who fall foul of their restrictions and confidentiality obligations. This is because it seems that judicial opinion at the moment appears to be swinging in favour of allowing companies to protect their business interests provided, of course, that they are reasonable. This is particularly if you are the type of company who has gone to some considerable lengths to restrict the dissemination of sensitive material, you have valuable client contacts with specific arrangements and/or you have rival businesses who could get a real leg up in the market place if passed the right information.

Non-competition

Recently a six month non-compete was upheld in relation to an HR manager. The reason was that he had been in charge of training the sales force on the company database and so had more knowledge of the system (which contained confidential client details) than anyone else. The company (Intercall) managed to convince the High Court that a confidentiality provision was not enough. This was reinforced by the HR manager's own argument that he could not remember a lot of the information – the Court found that if he could not remember it this meant there was a real danger of accidental disclosure of confidential information, so the injunction was granted!

12 month covenants for non-dealing and non-solicitation of key employees have also been upheld in the last year together with other non-compete covenants for longer periods, the longest being for three years – clearly this last one was a very unusual and unique case (RDF Media) relating to a very senior employee with complete knowledge of all aspects of the business.

But beware!

The RDF case was also important in establishing the fact that there is a fine line to tread between making efforts to protect your legitimate interests and going too far. Even if an employee is on garden leave and therefore not involved in the day to day running of the business, this did not mean that an employer can act in whatever way it likes towards an employee. Whilst employers could not, luckily, be prohibited from thinking negative and unworthy thoughts about an employee who is leaving, equally an employer could not, for example, vilify an employee in the press. If an employer goes too far, then this would not be "reasonable and proper conduct" and may result in damaging the relationship of trust and confidence between the parties. If that happened, it may not be possible to rely on covenants in any event.

Also, don't forget basic principles – although the courts have more recently been prepared to look at the overall meaning behind covenants and not scrutinise every word, this does not mean that the courts have recently lost their marbles and are upholding previously totally unenforceable covenants. For example, the covenants must be no wider than necessary to protect the particular company's legitimate business interests in terms of period and the type of business or clients it covers. Even where there is highly confidential information to protect, it must be clearly distinguished from other types of information and preferably jealously guarded, in order to convince a court that it is worth protecting, particularly if going for a non-compete injunction rather than simply recovery of the information itself.

Now is the time to act

Whilst the courts seem to be in favour of businesses trying to protect their positions, now is the time to make sure that the restrictions in senior employees' contracts are as enforceable as they can be and that it is clear to those employees what the company is trying to protect. It should be made clear what is and what is not confidential and which clients are the most vital. Don't have a "one size fits all" policy because this is likely to come unstuck if wanting to rely on it and do seriously consider picking a case and pursuing it all the way if you genuinely believe a senior employee's conduct is unacceptable and damaging to the business. It is amazing the effect that this might have on the conduct of others who might be tempted to follow if granted!

By Laura Livingstone

A shorter version of this article will appear in Personnel Today

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Case law update

Are agency workers employees?

James v Greenwich Borough Council UKEAT/00006/06/ZT

Why care?

The latest Court of Appeal decision on whether a contract should be found between agency worker and end user in a triangular employment relationship situation.

The case

Ms James commenced working for the Council in 1997 and this ended in September 2004. She changed agencies at various points throughout this period. One of these points was in 2003 when she signed a temporary worker's agreement with an agency. The agency assumed responsibility for the payment of her remuneration and statutory deductions and contributions. According to the terms of this agreement Ms James contracted in the capacity of a self-employed worker in relation to each assignment undertaken by her. She was not obliged to consider any assignment offered to her by the agency and the terms stated that they constituted a contract of services between the agency and the temporary worker and did not give rise to a contract of employment between them or between the temporary worker and the client.

In August and September 2004, Ms James was absent due to sickness but did not notify the Council's team manager in her section of the reasons for absence. She did not receive sick pay from the Council. She did provide a medical certificate to the agency and informed her work colleague that she was ill and unable to attend work. While she was away the work she had previously undertaken was undertaken by another worker provided by the same agency.

Following the period of absence, she returned to work on 24 September 2004 to find another agency worker had arrived to cover the same shift. Ms James did not undertake any further work for the Council. She presented her claim for unfair dismissal against them a couple of months later. The agency was later joined as a respondent, although it was not contended that she was an employee of the agency.

The decision of both the tribunal and the EAT (chaired by Elias) was that she was not employed by the Council under a contract of service and could not therefore bring a claim for unfair dismissal. This was also despite the fact that the Council conceded that Ms James was subjected to a degree of control in that it had arranged all Ms James' instructions and working conditions and provided the materials used in her work. However, there was an absence of mutuality of obligation.

Various cases were stayed pending the outcome of this decision by the Court of Appeal.

The Court of Appeal considered that the two types of contracts - agency agreement and contract of employment – are not necessarily mutually exclusive and it is legally possible for a worker to have one kind of contract with an employment agency and another kind of contract with the end user to whom he renders services. It went on to state that it is for the fact-finding tribunal to assess carefully all evidence placed before it to determine whether a claimant could be an employee.

Dismissing the appeal, the Court of Appeal held that, although Ms James could not be described as a temporary worker, given the length of time she had worked for the Council, the tribunal had correctly applied the test of necessity in assessing whether a contract of employment should be implied between Ms James and the Council. In the absence of an express contract of employment, the Court of Appeal made clear that where the arrangements are genuine it will be a rare case where there will be evidence entitling the tribunal to imply a contract between worker and end user.

The court also expressed its approval of the guidance handed down by the EAT and made clear that Dacas should not be seen as authority for implying a contract with the end user simply because the worker has worked for the end user for a long period of time. Lord Justice Mummery, giving the lead judgment, made clear that whether or not a contract is implied should be decided on the basis of common law principles of implied contract. Labels are no substitute for legal analysis of the evidence.

What to take away

Whilst employers can take comfort from the fact that it will be rare for the courts to imply a contract even if a worker has been working for the end user for some time, this case does emphasise the uncertainty created by lack of paperwork. Although not definitive, it would help to have paperwork in place making clear that the worker is not an employee of the end user.

Furthermore, employers should take steps in practice to reduce the risk of agency workers being found to be employees, for example try to engage different workers for shorter periods, not integrating them too much within the workforce and make clear that substitutes by the agency will be tolerated.

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Does homophobic banter discriminate against heterosexuals?

Mr S English v Thomas Sanderson Blinds Limited UKEAT/0556/07/LA

Why care?

The EAT confirmed that the Employment Equality (Sexual Orientation) Regulations 2003 (the "Sexual Orientation Regulations") do not prohibit homophobic banter against a heterosexual man who is known to be heterosexual.

The case

Mr English was engaged by the Respondent under an agency agreement between October 1996 and August 2005. In November 2005 he presented a claim in the Employment Tribunal complaining of harassment contrary to the Sexual Orientation Regulations.

The Claimant submitted that he had for many years been subjected to sexual innuendo by his work colleagues to the effect that he was homosexual. This course of conduct apparently originated from a manager who learnt that the Claimant had (a) attended a boarding school, and (b) lived in Brighton.

A preliminary issue arose about the fact that the Claimant was not homosexual, nor was he mistakenly or genuinely thought to be so by his "tormentors". The Respondent therefore contended that, as a matter of law, the Claimant's case did not fall within the scope of the legislation.

The Employment Tribunal accepted the Respondent's position and found that the Claimant was not protected by the Sexual Orientation Regulations in respect of this treatment.

The EAT upheld this decision. Although Mr English had been harassed based on his colleagues' view that he had some of (what they thought of as) the characteristics of a homosexual male, they did not believe him to be gay.

The argument then centred on whether the Sexual Orientation Regulations correctly implemented the EC Framework Directive. The Directive prohibits harassment "related to" the protected characteristic, whereas the Sexual Orientation Regulations prohibit harassment "on grounds of sexual orientation". An analogy was drawn with the position under the Sex Discrimination Act and the decision in *EOC v Secretary of State for Trade and Industry [2007] IRLR 327*. There it was found that the phrase "on grounds of her sex" was not sufficient implementation of the Directive in respect of sex discrimination.

It was submitted that the Sexual Orientation Regulations were wider than the framework within the Sex Discrimination Act because the Sex Discrimination Act speaks of treatment on the ground of "her" sex whereas the Sexual Orientation Regulations refer to "on the ground of sexual orientation". The EAT accepted that the phrase "on grounds of sexual orientation" is wider than "on grounds of her sex". They said that the formula in the Sexual Orientation Regulations extends to discrimination based on perception, association or instructions. Nevertheless, they were not persuaded that the Sexual Orientation Regulations actually properly implement the Directive by limiting the protection in this way.

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The EAT dismissed the appeal but granted leave to appeal to the Court of Appeal. Mr English is being supported by the EOC. It therefore appears likely that the matter will go to the Court of Appeal.

What to take away

As currently drafted, the Sexual Orientation Regulations do not protect a person who is known to be heterosexual but is nevertheless teased that he is homosexual (or vice versa). However, the EAT saw this as an unsatisfactory state of affairs which did not properly implement the EU Directive and permission has been granted to appeal to the Court of Appeal. It therefore seems possible that the Sexual Orientation Regulations may need to be amended in due course.

As the law presently stands, an employee subjected to this type of banter would have a constructive dismissal case. Presumably, it is the fact that Mr English was an agency employee that led to the necessity to plead the claim through the Sexual Orientation Regulations in the first place.

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The importance of evidence in the absence of clear bonus documentation

Mr David Kahn ("DK") v Dunlop Haywards (DHL) Limited ("DHL") [2007] EWHC 2659 (QC)

Why care?

The High Court found in favour of an employee whose evidence was stronger in determining the position on bonus in the absence of a formal written agreement.

The case

DHL is a property consultancy firm and DK was employed as Managing Director from 2001 until 2004, after which time he switched to fee earning work. When in a fee earning role, DK was very successful in referring a lot of work to other departments, mainly the valuation department, which generated repeat business for DHL. DHL operated a company wide bonus scheme and a separate departmental bonus scheme. These schemes incorporated arrangements to reward departments (and individuals) for cross-referral of work.

Due to the change in the company's corporate structure (i.e. various acquisitions and mergers involving parts of the business that DK had worked in), there was concern that DK would leave the organisation, and DHL did not want to risk losing DK because he was a valuable asset. DK was highly respected in the property scene and generated a significant amount of business.

DK therefore entered into discussions with DHL about negotiating special bonus terms for himself, which in particular recognised the large amount of his successful referral work to other departments.

The terms of the special bonus scheme for DK were not recorded in a formal written agreement between the parties.

The essential issue was whether DK negotiated and agreed a special bonus arrangement which (1) exempted him from the normal 70/30 split between him and the valuation department (i.e. the department to which he referred work) and (2) enabled him to continue receiving bonuses calculated by reference to that special arrangement in relation to repeat business carried out by the valuation department for clients he had originally introduced. DK claimed that he was owed just short of £500,000 which was due to him in respect of bonuses for 2005 and 2006.

DHL disputed that it owed any money to DK under the special bonus arrangement and accused DK of dishonesty. DHL also argued that, commercially speaking, DK's interpretation as to what was agreed must be incorrect, as his bonus would have exceeded DHL's profit.

In the absence of any formal documentation, the court examined a chain of various emails and discussions, looking at the factual matrix to interpret the agreement between parties. The court found DK's evidence more convincing and held that the contract for the special bonus was completed at the moment a DHL executive accepted a very detailed email from DK which set out what he understood was verbally agreed between the parties.

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The court found the detail included in DK's email record of the conversations that took place between him and DHL on the special bonus arrangement could not have been fabricated by him, and must have been supported by the existence of an actual conversation between him and DHL executives. The court pointed out that it would have been useful to hear evidence from the two senior DHL executives who were involved in these conversations with DK – these individuals had left the company and had not provided evidence.

The court found that the special bonus agreement was supported by an acknowledged need to reflect DK facilitating and maintaining repeat work, and also by the fact that DHL recognised that client loyalty to DHL was dependant on loyalty to DK, and DK could have taken these clients after his three month non-compete expired.

The court dismissed DHL's arguments that internally this may have affected bonuses of people doing the referral work (DK now being entitled to the profit instead of it being split), holding that this was an internal matter, and that these people would probably have rather have had a share of work than none at all.

What to take away

This demonstrates the importance for employers in having clear unified documentation, signed by both parties to support any agreement on bonus. In this case, the lack of such formal documentation did not prevent the court from finding an effective agreement in the employee's favour. The employer had seemingly agreed to special bonus terms without fully appreciating the generosity, or that there was a substantial difference as to what both parties believed had been agreed.

The arguments pointing to the lack of commercial sense put forward by the employer did not have any impact on the decision.

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Setting up in competition and confidentiality

Crowson Fabrics Limited v (1) Paul Ryder (2) Warren Stimson (3) Concept Textiles Limited [2007] EWHC 2942 [CH]

Why care?

The High Court refused to grant a springboard injunction but it did provide useful observations on potential relief, setting up in competition and confidential information.

The case

Paul Ryder and Warren Stimson were former employees of Crowson Fabrics Limited ("Crowson"), one of the leading producers, designers and suppliers of home furnishings. At the relevant time Mr Ryder was Product & Distribution Director but was not a legal director of Crowson. Mr Stimson was the UK & Export Sales Manager.

Although Mr Crowson was its Chairman and sole shareholder, and was still involved in decision making, the three key day-to-day managers of the business were Mr Worrall (the Managing Director), Mr Ryder and Mr Stimson.

Despite both employees having brief terms of employment, neither had either restrictions or even brief confidentiality provisions. Mr Ryder gave his 12 weeks' contractual notice and Mr Stimson gave his four weeks'.

Up until the end of the notice period, the employees incorporated the rival business Concept Textiles Limited ("Concept"), acquired substantial leasehold premises, set up a computer and email system and emailed clients saying they were setting up a rival fabric company offering great prices. In spite of these steps, it was alleged that these acts were no more than merely preparatory. They indicated that they were entitled to organise a state of affairs to set up a rival business since there were no express covenants preventing them from doing so.

Furthermore, they took and copied Concept documents belonging to Crowson with a view to using them as an illegitimate springboard to compete. Despite this blatant action, it was contended that all of the material was available in the public domain and in any event was part of the employees' own gathered knowledge and experience.

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Importantly, the court found that Mr Ryder not only had a duty of fidelity towards Crowson but also that he owed a fiduciary duty. Although employees do not generally owe fiduciary duties, employees can have higher duties. In Mr Ryder's case he was entrusted with senior tasks and strategy discussions, whereas Mr Stimson was not.

It was not difficult to determine that the defendants were in breach of their duties of fidelity, and Mr Ryder was also in breach of his fiduciary duty. Not only did they set about creating a rival business in breach of those duties, but also they used the confidential information as an illegitimate springboard and solicited the business of agents and some customers. They also diverted some business opportunities to themselves.

Regarding setting up of competition, it is often said that the test is whether or not the actions done were merely preparatory for the future activity or went beyond that. The court made clear that the key point is to identify that which is legitimate and that which breaches an employee's obligations, not centring simply on whether activities are preparatory.

Despite the defendants admitting taking huge amounts of information, it was recognised that this information could be obtained from the public domain and/or had been retained as part of their experience. However, Crowson was permitted to stop illegitimate use of the information.

Even taking this into account, the court had grave doubts about the worth and enforceability of a springboard injunction in this case since this type of injunction would not prevent the employees from using the information if it can be shown to have been part of their memory. The benefit of having an injunction for such a short period here, i.e. less than six months, was also questioned.

Unfortunately for Crowson, it was not possible to produce evidence at this stage to state that they had suffered any particular loss and therefore the court considered that it may be worth seeking an account of profits which would not be dependant on loss. The problem with this, however, would be that the profits must flow from the breach of fiduciary duty and not, for example, the wrongdoers' own efforts necessarily. This, therefore, might be difficult to determine.

It was instead suggested by the court that the parties might like to consider whether the appropriate relief would be to grant damages in lieu of an injunction measured "by reference to what would be a reasonable price the Defendants ought to pay for using the Claimant's documents as a short cut to setting up their business."

What to take away

Even in such a blatant case of breach, it is possible that the courts will not grant a springboard injunction since it may be difficult to police and too much time may have gone by. It may be worth trying to determine what other possible remedies could be sought, especially if it is difficult to determine actual loss.

The main point, however, is that it is important to have express covenants wherever necessary since this case is a good example of how difficult it can be to succeed even in relation to blatant taking of confidential information without the benefit of an express covenant.

This case also demonstrates that senior employees can have fiduciary duties in addition to the duty of fidelity even if they are not legal directors.

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Hot topics

Women undergoing IVF treatment are not "pregnant"

The ECJ has held that women undergoing IVF treatment but who have not yet had the fertilised eggs implanted into their womb are not "pregnant" and are therefore not protected from dismissal by the Pregnant Workers Directive (92/85). The ECJ considered the objective of the Pregnant Workers Directive in *Mayr v Bäckerei und Konditorei Gerhard Flöckner OHG C-506/06* and it was decided that although protection should start from the earliest possible date in a pregnancy, women undergoing IVF treatment are not pregnant for the purposes of the Directive until the fertilised ova have been implanted. Such women are therefore not protected from dismissal by the Pregnant Workers Directive.

However, since the dismissal of a female worker for being pregnant or for a reason essentially based on their pregnancy amounts to direct sex discrimination, the dismissal of a woman, if related to her IVF treatment, will amount to discrimination on the ground of sex contrary to the EC Equal Treatment Directive (76/207).

Advocate General's opinion on annual leave during sick leave

In *Schultz-Hoff v Deutsche Rentenversicherung Bund C-350/06* the Advocate General has said that leave not taken by a worker because of illness during the leave year must be granted at a later date. Similarly, if a person has already had their employment terminated, a payment in lieu of that leave must be made. The Advocate General considers that, since the absence is beyond the worker's control, a period of illness is equivalent to a period of service. The Advocate General's opinion is now available in English and was handed down on the same day as *Stringer & Others v Her Majesty's Revenue & Customs C-520/06* which concerns similar issues.

SGP: employees offer to compromise claims does not invalidate step 1 letter

The EAT has held that letters raising multiple grievances in relation to an employer's conduct, which also contain an offer to settle with the employer, can amount to a step one statement of grievance under the Statutory Grievance Procedure (SGP). In *Ward v University of Essex UKEAT/0391/07* the EAT held that, since the essential characteristic of a grievance letter is that the employer is put on notice of what the employee's complaint is, the letter could stand as a valid grievance because the employer in this case could be in no doubt as to the nature of the dispute. *Palihakkara v British Telecommunications Plc UKEAT/0185/06* was relied upon by the EAT as authority for the proposition that an employee's underlying grievance becomes live again, once a compromise agreement is void.

Expired disciplinary warnings may be relied upon

The Court of Appeal has held recently in *Airbus UK Limited v Mr M G Webb [2008] EDCA Civ.49* that an employer may sometimes take expired disciplinary warnings into account when deciding to dismiss an employee. This decision overturned the decision in the Employment Tribunal and the EAT on the same case and suggests that, in certain circumstances, it may be fair to rely on expired disciplinary warnings when making a disciplinary decision. The case concerned Mr Webb and four other staff members who were all guilty of gross misconduct. Mr Webb's four colleagues, with totally clean disciplinary records, were subjected to a final written warning. Mr Webb, however, was summarily dismissed. In this case, the Court of Appeal considered the most important factor in the outcome of the case to be the fact that Mr Webb could legitimately have been dismissed for gross misconduct based solely on the incident in question. In respect of the other four employees, who were not dismissed, the starting point was that they would and should have been dismissed for gross misconduct but the fact they had a totally clean disciplinary record was taken into account as a mitigating factor. The *Diosynth* case was distinguished because in that case the fact of having received prior warnings was stated to have tipped the balance in favour of dismissal.

This case does not permit employers to routinely take into account expired disciplinary warnings. The safest course of action will still be to discount any disciplinary warning which is previously expired. However, the case may be helpful for an employer who has a number of employees alleged to have committed the same disciplinary offence, where one appears to be a repeat offender and the others have an unblemished record.

Temporary and Agency Workers (Equal Treatment) Bill passed at second reading

The Temporary and Agency Workers (Equal Treatment) Bill, which aims to give agency workers the rights to the same terms and conditions as permanent staff, has passed its second reading and has been committed to a Public Bill Committee. But although 147 MPs voted in favour and only 11 against, it appears the Government does not support it. Further, according to Personnel Today, the Confederation of British Industry (CBI) claims the Bill will diminish labour market flexibility and the British Chambers of Commerce, the Federation of Small Businesses and the Institute of Directors also do not understand how its introduction will help temporary staff get the same rights. As such it is yet to be seen whether the Bill will proceed through the next stage.

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