IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2013-404-845
[2013] NZHC 428

BETWEEN	HEALTH CLUB BRANDS LIMITED Plaintiff
AND	COLVEN BOTANY LIMITED First Defendant
AND	COLVEN THREE KINGS LIMITED Second Defendant
AND	COLVEN WESTGATE LIMITED Third Defendant
AND	STUART ANTHONY HOLDER Fourth Defendant

Hearing: 26 February 2013

Counsel: P Rice & N Batts for plaintiff
J K Goodall & M Lenihan for defendants

Judgment: 7 March 2013

JUDGMENT OF WINKELMANN J

This judgment was delivered by me on 7 March 2013 at 2.00 pm pursuant to Rule 11.5 of the High Court Rules.

Registrar/ Deputy Registrar

Solicitors
Haigh Lyon, Auckland
Stewart Germann Law Office, Auckland

Counsel
Phillip Rice, Auckland
J K Goodall, Auckland

[1] The plaintiff in this proceeding, Health Club Brands Ltd, operates a franchise of gyms across Auckland, trading under the name "Club Physical". The first, second and third defendants in these proceedings, Colven Botany Ltd, Colven Three Kings Ltd and Colven Westgate Ltd (the franchisee defendants), were each parties to franchise agreements granting them the right to operate Club Physical gyms in Botany, Three Kings and Westgate respectively. They purchased the businesses from previous franchisees, purchasing the Botany franchise in November 2009, the Three Kings franchise in December 2010, and the Westgate franchise in June 2011. The fourth defendant, Mr Stuart Holder, is the sole director of the franchisee defendants, and is a guarantor of their obligations under the franchise agreements.

[2] On 8 February 2013 the franchisee defendants issued notices terminating each of the franchise agreements. The stipulated grounds of cancellation included that they had been induced to enter into the agreements by a misrepresentation that Health Club Brands intended to honour its obligations under the agreements, and that it had breached its ongoing assistance obligations as set out in those agreements. The notices of termination concluded with advice that the franchisees would each discontinue the use of the Club Physical name as soon as practicable.

[3] Following termination, the gyms were immediately rebranded as "Jolt Fitness", and continue to trade under that new name.

[4] Health Club Brands claims that the franchisee defendants' actions amounted to repudiation of the franchise agreements. It accepted that repudiation and itself purported to cancel. Health Club Brands now applies for an interim injunction restraining all defendants from conducting or being interested in any health and fitness business within a distance of five kilometres from the premises formerly operated by them as a Club Physical gym. Health Club Brands relies upon a restraint of trade clause in each of the franchise agreements to support its application. If granted, these injunctions will close down the three Jolt Fitness businesses.

[5] The defendants oppose the application on the basis that they have a good arguable defence that the restraints of trade are unenforceable on three grounds:

(a) Because crucial elements of the restraint of trade clauses were not completed by the parties, the agreements do not operate to restrain the defendants as contended.

(b) To the extent that the restraints do impose obligations upon the defendants, those obligations should not be enforced because they are unreasonable.

(c) In any case, Health Club Brands is in breach of the franchise agreements, releasing the defendants from any contractual obligations which remain unperformed at the date of cancellation.

[6] Finally, the defendants submit that the balance of convenience and overall justice of the case favours the defendants given the consequences of such an injunction.

[7] Since termination, Health Club Brands has been contacting members of the three Jolt Fitness gyms in an attempt to persuade them to revert to Club Physical memberships. Health Club Brands is able to do so because it has access to a database of member names, phone numbers and email addresses which it uploaded from the three gyms prior to termination. The defendants have applied for interim injunctions restraining Health Club Brands from further accessing either its electronic or hard copy membership lists, and from contacting those members. The application is brought on the basis that these member details are the confidential information of the franchisee defendants.

[8] Health Club Brands opposes the defendants' cross-application. It says that member details are the property of Health Club Brands, or at least became so on termination.

Interim injunction principles

[9] The principles governing an application for an interim injunction are not at issue. The Court must first consider whether the plaintiff has established that there is a serious question to be tried. In answering that question the Court must consider:[1]

> ...first, what each of the parties claims the facts to be; second, what are the issues between the parties on these facts; third, what is the law applicable to those issues, and, fourth, is there a tenable resolution of the issues of fact and law on which the plaintiff may be able to succeed at the trial: see *Shotover Gorge Jet Boats Ltd v Marine Enterprises* Ltd [1984] 2 NZLR 154, 157.

The Court is not concerned with attempting to resolve conflicts of evidence in respect of facts which may determine the case, nor is it concerned with deciding difficult questions of law which "call for detailed argument and mature considerations".[2]

[10] Secondly, the Court must consider where the balance of convenience lies. In assessing the balance of convenience, regard may be had to the adequacy of damages should relief not be granted, the relative strength of each party's case and the impact of the decision on the rights of third parties.[3]

[11] These broad questions provide a framework for approaching these applications but are not exhaustive. They are questions under which considerations may be marshalled in order to help the Court determine where the overall justice of the matter lies.[4]

Health Club Brands' application for an interim injunction enforcing restraints of trade

Is there a serious question to be tried?

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1 *Klissers Farmhouse Bakeries Ltd v Harvest Bakeries Ltd* [1985] 2 NZLR 129 (CA) at 133.
2 *American Cyanamid Co v Ethicon Ltd* [1975] AC 396 (HL) at 407.
3 *Wellington International Airport Ltd v Air New Zealand Ltd* HC Wellington ClV-2007-485-1756, 30 July 2008 at [6] and [13].
4 *Klissers*, above n 1, at 142.

[12] It is convenient to begin by considering Health Club Brands' application for a interim injunction enforcing the restraint of trade provisions within each agreement. In doing so, it is first necessary to address whether Health Club Brands has established that there is a serious question to be tried that the restraint of trade clause within each agreement is enforceable. The issues to be addressed under this heading are:

(a) Did the parties agree to the form of the restraint Health Club Brands contends for? and, if so –

(b) Are the limits of the restraints reasonable? and

(c) Are the defendants discharged from any obligation to comply with the restraints by Health Club Brands' breach of contract?

(a) Did the parties agree to the form of the restraint Health Club Brands contends for?

[13] The relevant restraint of trade clauses are contained within a standard form franchise agreement provided by Health Club Brands. The wording of the relevant clause in the printed form is as follows:

AA RESTRAINT OF TRADE

1. *Restraint of Trade*

The Franchisee or if a company, its directors and shareholders or if a trust, its trustees (referred to collectively in this clause as "the Franchisee") shall not during any of the periods after the termination of this agreement at the Premises or within any distance from the Premises as specified below, conduct on their own account a business similar to the Business or be concerned or interested in, directly or indirectly, as agent, representative, consultant, employee, shareholder or director, of any firm or corporation conducting a business similar to the Business.

Period	*Distance*
2 years	

1 year

This clause shall be read as containing four separate and severable covenants between the Franchisee and the Franchisor restraining the Franchisee from being concerned in a business as outlined above, such covenants to operate in the following order of priority namely:

The covenants successively involving the combination of:

(a) the period of 2 years for the distance of;

(b) the period of 2 years for the distance of;

(c) the period of 1 year for the distance of;

(d) the period of 1 year for the distance of;

and no such covenant as to such restraint in respect of any particular combination of period and distance shall be invalid and unenforceable solely by reason of any covenants as to such restraint in respect of any other combinations of periods and distances being invalid or unenforceable.

[14] The second half of the clause (which, although not demarcated as a sub-clause, is logically distinct from the first half) describes how the first half of the clause is to be read. The direction as to how the clause is to be read and the direction regarding priority as between the four successive covenants are both clearly intended to operate in circumstances where there is a legal challenge to the reasonableness of the restraint. They are intended to facilitate the severance of any unreasonable aspect of the restraint so that a narrower restraint may still be enforced.

[15] In both the Westgate and Botany agreements, the clause appears in the form set out above. In neither has the additional detail contemplated by the clause been completed. However, in the Three Kings agreement there is a handwritten insertion in the first space that appears in the agreement, to the right of the page, under the heading "distance", as follows:

5 KM EXCLUDING ANY EXISTING CLUB PHYSICAL BRANCHS [sic].

This addition is initialled by the signatories to the agreement, but there is no other amendment or handwritten insertion in the clause. Even in the case of the Three Kings franchise agreement, therefore, the clause is only partially completed.

[16] Health Club Brands must link the injunction it seeks to the words of the restraint of trade. In this regard it stumbles at the first hurdle as it has failed to complete the restraint of trade clause as is contemplated in the agreement. This failure is complete in respect of the Westgate and Botany agreements. No time period has been stipulated, although the agreement clearly contemplates that one or other or perhaps both periods of time will be marked in the agreement. Nor are any distances indicated in the first or second half of the clause. There is thus no basis for arguing that a five-kilometre zone of restraint operates for these agreements.

[17] The situation is different in respect of the Three Kings agreement which contains the handwritten insertion "five kilometres excluding any existing Club Physical branchs" (sic). Again however, the relevant period is not circled or otherwise highlighted as applicable and, again, the four successive covenants are not completed.

[18] Health Club Brands argues that the clause within the Three Kings agreement should be read as imposing a five-kilometre restraint of trade for a period of two years, as the handwriting visually aligns with the printed "2 years". Alternatively, it is argued that Health Club Brands can elect which period it seeks to enforce. Although counsel for the defendants point to obscurity in the meaning of the words "EXCLUDING ANY EXISTING CLUB PHYSICAL BRANCHS", Health Club Brands responds that this was intended to ensure that the five-kilometre restraint would not prevent the franchisee from operating any other Club Physical franchise that it owned within the five kilometres.

[19] Given the alignment of the handwritten insertion to the printed "2 years", I accept that it is an arguable construction of the clause that a five kilometre restraint of trade was to apply for a period of two years, (excluding from the effect of restraint any other Club Physical gym operated by the second and fourth defendants within that zone). Although the parties did not complete the four covenants listed at the bottom of the clause, a respectable argument can also be made that the clause is effective without this, since that part of the clause does not purport to create obligations but is rather, as discussed, designed to operate in the face of challenge to the enforceability of the restraint. There is, then, a serious question to be tried that a

five-kilometre restraint of trade was intended to apply in respect of the Three Kings franchise.

[20] This is not, however, the end of the matter. A further argument was made to the effect that Health Club Brands must at least be able to insist upon enforcing that part of the restraint which relates to the premises. Health Club Brands is on much stronger ground with this argument. Notwithstanding the parties' failure to complete all of the detail in the clause relevant to the "distance" aspect of the restraint, on the face of it the clause records the parties' agreement that following termination the defendants would not conduct a health and fitness business from the premises. If the references to distance are removed from the first part of the clause, it reads as follows:

> [The defendants] … shall not during any of the periods after the termination of this agreement at the Premises … conduct on their own account a business similar to the Business …

The periods, in terms of the agreement, are one year and two years.

[21] Also relevant are the provisions of clause Q in each agreement, which provide, in part, that:

> On the expiry or termination of this agreement for any reason, the Franchisee will immediately:
>
> (a) cease carrying on the Business;
>
> …
>
> (j) assign any lease, sub-lease, licence or sub-licence of the Premises to the Franchisor or a party nominated by the Franchisor;
>
> …
>
> (l) appoint the Franchisor as its attorney to allow the Franchisor to complete any or all of the above acts to ensure the Franchisee complies with its obligations;
>
> (m) allow the Franchisor or its representative to enter the Premises to complete any act or take all reasonable steps necessary to ensure the landlord consents to the Franchisor's right to enter the Premises;
>
> (n) co-operate with the Franchisor to ensure a smooth transition so as not to disrupt the customers of the Business.

...

[22] This provision was not initially relied upon by Health Club Brands as a ground for seeking the injunction, and I assume it is for this reason that neither party has put any of the lease documents in evidence. Nevertheless, it seems likely that the leases are assignable; after all, rights of assignment appear in most leases, and these leases were presumably assigned to the franchisee defendants when they purchased each franchise business. The evidence filed by Health Club Brands in support of the application for injunction is contained in affidavits sworn by its director, Mr Paul Richards. Mr Richards says that if the injunctions are granted Health Club Brands intends to seek an assignment to it of these leases.

[23] Even were it not for the restraint of trade clauses, therefore, Health Club Brands could rely on clause Q to compel the defendants to cease trading from the premises. This clause also supports the construction of the restraint of trade clauses contended for by Health Club Brands – that is, that the parties did agree that the defendants would cease operating a gym business from the premises on termination of the agreement. I am therefore satisfied that it is arguable that those restraints prevent the defendants from operating a health and fitness business from the three premises.

(b) Are the limits of the restraints reasonable?

[24] The next issue is whether the limits of the restraints are reasonable. Restraints of trade are contrary to public policy and are therefore prima facie void. But where the restraint is no wider than the circumstances of the case reasonably require, and provided there is a legitimate interest to be protected by it, the covenant is enforceable. The onus is upon the parties seeking to enforce the restricted provision to show that the restriction is no wider than the circumstances reasonably require.[5]

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5 *Blackler v New Zealand Rugby Football League* [1968] NZLR 547 (CA); *Brown v Brown* [1980] 1 NZLR 486 (CA).

[25] Mr Richards says that there is a concern that if the defendants are allowed to continue trading in competition with Club Physical, it will be impossible for a Club Physical franchisee to re-establish itself in the area due to the limited demand for health and fitness gyms. The fact of there being a limited demand for gyms was reflected in the franchise agreements, which granted the franchisee the exclusive right to operate a franchise within the specified area of five kilometres from the premises.[6] Therefore, although it is Health Club Brands' intention to re-establish clubs in the areas of Botany, Three Kings and Westgate, this will only be viable if the defendants are restrained from operating in those areas for the agreed restraint of trade period. It is therefore submitted for Health Club Brands that an injunction covering an area of five kilometres from each premises for a period of two years is reasonable in scope.

[26] It is clear that a franchisor may have a legitimate interest in protecting the goodwill developed through use of its business model by means of a restraint of trade. As was said by William Young J in *Washworld Corporation (Leases) Ltd v Reid* at 385:[7]

> In terms of the public interest, I see no particular general difficulty with a restraint, at least if it is properly limited. In my view, a franchisor who has gone to the difficulty and expense of developing a successful business model is entitled to protect its investment in that business model by prohibiting franchisees from exploiting it for their own advantage and in competition with the franchisor and other franchisees.

[27] The defendants did not seek to argue that the five-kilometre restraint originally sought by Health Club Brands in its application was unreasonable. They do, however, challenge the reasonableness of a restraint which would only prevent them from conducting a health and fitness business from the premises, arguing that such a restraint can have no legitimate business objective. Because it allows the

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6 This exclusive right was subject to the following: "if in the reasonable opinion of the Franchisor, the specific demographics of the Area allow for another Club Physical site within the Area then the Franchisee shall be granted the right of first refusal if the Franchisor is satisfied that the Franchisee has the necessary financial and managerial resources to operate another outlet. If the Franchisor is not satisfied the Franchisor shall be entitled to operate or grant a third party the right to operate another outlet within the Area."

7 *Washworld Corporation (Leases) Ltd v Reid* (1998) 8 TCLR 372 (HC) at 385.

defendants to simply open a similar business next door, it can only be viewed, they say, as an obstacle to the defendants' business, and not as a legitimate mechanism for protecting the goodwill built up in the franchise model.

[28] Although the defendants are no longer using the "Club Physical" brand, I consider that there is a respectable argument that by operating from the existing premises they continue to trade on the goodwill built up through access to the "Club Physical" business model. Health Club Brands has a legitimate interest in ensuring the transfer of that goodwill to an incoming franchisee. That can only be achieved if the defendants are prevented from exploiting the goodwill in competition with the new franchisees. Thus, I consider there is a serious question to be tried that the restraints are reasonable in scope.

(c) Are the defendants discharged from any obligation to comply with the restraints by Health Club Brands' breach of contract?

[29] The defendants' next argument as to enforceability is that any restraint that would otherwise be enforceable is discharged through Health Club Brands' breach of the franchise agreements. The defendants rely upon observations of Fisher J in *Pirtek (New Zealand) Ltd v Mega Fluid Solutions Ltd*[8] that it might be difficult for a franchisor to repudiate a contract and yet at the same time seek to enforce a restraint of trade clause within it. In reply, Health Club Brands relies upon a decision, *Safety Step (New Zealand) Ltd v Safety Step Auckland Ltd*,[9] which it says is authority for the proposition that cancellation of a franchise agreement under the Contractual Remedies Act 1979 ("the Act") does not affect enforceability of restraint of trade provisions intended to operate after termination of the franchise agreement.

[30] The facts in *Safety Step* have significant similarities to the present proceeding. A group of franchisees purported to cancel franchise agreements for non-performance, and then set up in competition with the franchisor. The franchisor applied for an injunction to restrain the defendants from operating businesses in

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8 *Pirtek (New Zealand) Ltd v Mega Fluid Solutions Ltd* HC Hamilton CP5/03, 7 March 2003.

9 *Safety Step (New Zealand) Ltd v Safety Step Auckland Ltd* HC Auckland CP466/01, 14 September 2001 at [45]-[53].

competition with it, relying upon the restraint of trade clauses in the agreements. The defendants argued that because the franchise agreements had been cancelled, neither side was obliged to perform the contract further, and it followed that the defendants were not bound by the restraint of trade provisions. They relied upon the provisions of s 8(3)(a) of the Act which provides:

> (3) Subject to this Act, when a contract is cancelled the following provisions shall apply:
>
> (a) So far as the contract remains unperformed at the time of the cancellation, no party shall be obliged or entitled to perform it further:
>
> ...

[31] Randerson J rejected that argument on several grounds, including that compliance with a restraint of trade obligation does not involve performance of an obligation under the contract, but rather amounts to the observance of a negative obligation.

[32] Although ultimately an issue for trial, it seems difficult to contend that compliance with a restraint of trade clause is not undertaken in performance of the contract. If it is not, what compels compliance? Therefore, contrary to the views of Randerson J, I accept that it is an arguable proposition that were the defendants able to establish breach of the contract by the franchisor which justified cancellation under s 7 of the Act, they would not be bound to further perform the provisions of the restraint of trade.

[33] It is of course possible to contract out of the provisions of the Act;[10] parties may agree that obligations will survive termination, even termination for breach. However, I note that the clause in question simply provides that it is to apply after "termination of the contract". This is to be contrasted with the wording of clause Q, which is expressed to apply after "termination for any reason". Nevertheless there may be good arguments for construing the restraint of trade clauses as applying after termination for breach by the franchisee, plainly, the circumstance in which there

[10] Contractual Remedies Act 1979, s 5.

would be the most need for a restraint. But arguments that it should be construed to apply after termination for breach by the franchisor are far less clear.

[34] The point we reach therefore is that if, at the substantive hearing of these proceedings, Health Club Brands is successful in contending that the three restraint of trade clauses contain sufficient detail to create enforceable obligations, and if Health Club Brands discharges the onus upon it to establish that the restraints of trade are reasonable and therefore should be enforced, the defendants will need to show that they have nevertheless been discharged from those obligations by breaches on the part of Health Club Brands justifying termination. If the defendants cannot show that, then they will have unlawfully repudiated the contract, the restraint of trades clauses will apply, and the defendants will be exposed to both permanent injunction orders and a claim for damages by Health Club Brands for breach of contract.

[35] The defendants' case as presented at the hearing of the injunction application is that the franchisor breached the obligation contained in the franchise agreements at clause H4:

> To provide ongoing business development assistance and advice in relation to the operation of the Club Physical Franchise including a site visit to the Premises at least four times in each financial year.

[36] The allegations made in Mr Holder's affidavit in relation to these matters are factually disputed, and it is not possible to resolve those disputes in the course of this interim injunction hearing. It is, however, necessary to form a view as to the strengths of the respective cases. Mr Holder alleges that Mr Richards refused to provide "ongoing business development assistance and advice in relation to the operation of the Club Physical Franchises" in several respects. First, Mr Holder contends that Mr Richards refused to evaluate the group's pricing in light of intense competition from other low-cost gyms starting up in the Auckland region, and even forced Mr Holder to shut down initiatives he had introduced to became more competitive. At the same time, Mr Richards' own Club Physical gyms were undercutting prices across the rest of the group, which created confusion in the market place about the Club Physical offering and undermined the defendants' attempts to gain new members.

[37] Mr Richards denies having taken an inconsistent approach to pricing and says that Mr Holder's concern with price grew out of his inexperience in the industry. He says that gyms such as Club Physical simply cannot compete with low-cost gyms which typically achieve low costs through low or zero staffing levels.

[38] Secondly, Mr Holder complains of poor marketing systems. Mr Holder alleges that Mr Richards refused to review his approach to marketing and instigated a number of marketing campaigns which tended to lose rather than build market share. Instances cited include an advertising campaign depicting aliens shooting overweight people with the slogan "get the fat people first". Mr Holder says that his members considered this advertisement offensive, and it nearly lost him a significant corporate account at Botany. Mr Richards denies that he refused to engage on marketing issues and says the marketing campaigns referred to by Mr Holder are "cliff edge" marketing, designed to evoke a comedic response amongst the general public. He says that Club Physical complied with its obligation to market, with the normal monthly spend for marketing being between $25,000 to $30,000.

[39] Thirdly, Mr Holder says that attendance at fitness classes provided by the franchisor, and charged separately to the franchise fee, was very low. Classes are a significant part of what attracts members to gyms, and Club Physical was running between 50-60 fitness classes across Mr Holder's three gyms. Mr Holder says that attendance at classes was falling because Health Club Brands did not refresh the nature of the classes. This meant that the defendants' gyms lost customers to their low-cost competitors. In reply, Mr Richards speculates that part of the difficulty the defendants had in this regard was that Mr Holder's wife was responsible for the "Group X classes" in the defendants' gyms and did not understand the dynamics of the class.

[40] Finally, the defendants say that site visits were supposed to be carried out by Mr Richards at least four times every year. However, Mr Holder claims that Mr Richards only visited the Botany gym once after being "hounded", and only stayed for 30 minutes. Mr Richards never visited the other two gyms. Although Mr Holder accepts that other representatives from Health Club Brands visited the gyms, he says it was implicit that the support would be provided by Mr Richards.

Mr Holder claims to have been enticed to enter into the contract as a result of Mr Richards holding himself out as having significant experience in the New Zealand fitness industry. Mr Richards gave various assurances to Mr Holder prior to his investment that he would "provide hands on assistance … in the operation of the business and that [he] would get a high level of support".

[41] To corroborate his account that Mr Richards did not provide ongoing assistance and business development, Mr Holder attached three letters to his affidavit from other people who had previously held Club Physical franchises. The contents of these letters are summarised as follows:

(a) A former owner of the Club Physical Women franchise in Auckland Central Business District details a "lack of support" from Mr Richards despite issues being raised in respect of pricing and a decline in attendance at gym classes. She also describes the adverse impact on her business of the "cliff edge" style of advertising that Club Physical pursued, including one advertising campaign which was directed at "cankles", which was offensive to her core market.

(b) A former owner of the Club Physical franchise at Karangahape Road describes being forced to sell the franchise because it was a failure. He refers to disputes with Mr Richards regarding marketing strategies, which he says failed to target his gym's market, and he further claims that he never received "any hands on help" from Mr Richards.

(c) A former owner of the Westgate franchise says "what struck my husband and I at the time was the lack of support structure provided by the franchisor".

[42] The defendants argue they were entitled to cancel the franchise agreements under the Act because there was a breach of essential terms (duty to assist) and/or the effect of the breach was substantial (lack of assistance leading to near insolvency of franchisee defendants). Mr Holder explains in his affidavit that Mr Richards'

insistence on an inflexible pricing structure which did not enable the defendants to meet the market in terms of price, whilst employing a flexible pricing structure in his own gyms, combined with stale exercise classes and misdirected advertising campaigns, were driving the gyms to the point of insolvency. In those circumstances, his financial situation meant that he had to take immediate action and terminate the franchises.

[43] Having reviewed the evidence, I am satisfied that the defendants' case that breaches of contract by Health Club Brands justified cancellation is poorly supported. Mr Holder's evidence is, in significant part, confused and contradictory. He complains that, despite promises of assistance and support being made, Mr Richards did not visit the clubs or provide them with any direct assistance or training, and that he offered a "total lack of support". But in his affidavit he also states that there were in fact monthly marketing meetings, that he had numerous meetings with Mr Richards in which he raised pricing issues with him, and that Mr Richards caused disruption by "continuing to exert influence over the gym" through Health Club Brands' sales manager, Ms Miles (who is also Mr Richards' sister-in-law). He says that Ms Miles visited the Three Kings gym nearly every day. The extent of the influence exerted was so great that Mr Holder advised the Three Kings' staff not to discuss in-house matters with Ms Miles or Mr Richards, and asked staff to sign confidentiality agreements. In light of this evidence, and even had Mr Richards not responded to the allegations made in Mr Holder's affidavit, it would be difficult to conclude that Health Club Brands had failed to offer "ongoing business development assistance and advice". Mr Holder may not have liked the business development assistance and advice, but it seems he received it.

[44] The "propensity" type evidence from previous franchisees might have been relevant if it tended to corroborate evidence that Health Club Brands was not performing its obligations as franchisors. But Mr Holder's evidence does not give any such account. His complaints seem to be principally about pricing and marketing. The franchisee defendants did not contract for any control over pricing or marketing. Rather, they contracted to conform with the franchise system at all times, including co-operating with the marketing strategy, and consulting and obtaining prior approval from the franchisor regarding any changes in membership

options or prices. Although the defendants may feel, with the benefit of hindsight, that they obtained a poor commercial bargain from Health Club Brands, that does not of itself confer a right to cancel.

[45] The defendants also face the difficulty that the three franchises were bought over a period of almost two years. As the tenor of Mr Holder's evidence is that the franchise was dysfunctional throughout, his decision to purchase two further franchises some time after the initial purchase of the Botany gym appears inconsistent with his allegations of breach of contract.

[46] To sum up on this point, there is a serious question to be tried:

(a) That the franchise agreements contained a provision restraining the defendants from operating a health and fitness business from the relevant business premises following termination, probably for a period of two years. In respect of the Three Kings franchise, there is also an arguable case that a five-kilometre restraint of trade applies.

(b) That those restraints are reasonable because they are designed to protect Health Club Brand's legitimate interest in the goodwill developed through association with the "Club Physical" brand.

(c) That although the restraints would not survive termination by breach on the part of Health Club Brands, the defendants' termination of the agreements was unjustified and a repudiation of the agreements. The restraints remain enforceable.

Balance of convenience

[47] As stated at paragraph [10] above, relevant considerations in terms of the balance of convenience include the adequacy of damages should an injunction be granted, the effect on third parties of either the grant or the non-grant of an injunction, and the relative strength of the parties' cases.

[48] Health Club Brands argues that damages will not be an adequate remedy if the plaintiff ultimately succeeds because it will have lost the opportunity to retain members' loyalty to the Club Physical brand through the restraint of trade provisions. The damage to Health Club Brands' goodwill through this loss of presence in the Botany, Three Kings and Westgate areas will be substantial yet difficult to quantify. It will not only result in the loss of franchise fees, but will diminish the value of the brand to potential new members and new franchisees, as the franchise will be reduced from nine gyms to six. It is argued that an injunction granted at the time of trial will be practically worthless because by that time the defendants will have established loyalty to the new brand "Jolt Fitness" in the same premises. At that point in time an injunction would simply cause further disruption to members and further brand damage.

[49] It is also argued that it is significant that there is no evidence that the defendants are in a position to pay a damages award. On Mr Holder's evidence, the defendants are in financial difficulty. Conversely, if an injunction is granted and the defendants ultimately succeed in establishing a right to trade from the premises, they can be adequately compensated in damages. Evidence has been provided that the Richards' Residential Trust has substantial assets and could therefore meet an award of damages. This does not seem to be disputed by the defendants. Moreover, since Health Club Brands seeks to take over the leases of the premises and intends, as Mr Rice submitted, to offer jobs to existing staff who were employed at the gyms at the time of termination, some of the loss caused to the defendants by the injunction will be ameliorated.

[50] The defendants argue that the balance of convenience favours them, identifying the following relevant factors:

(a) The grant of an injunction will terminate the defendants' business with catastrophic effect. The fourth defendant would lose his $2.1 million capital investment in the business, and the first three defendants would be rendered insolvent.

(b) Rent of approximately $55,000 a month will continue to accrue. Each of the first three defendants is named as a tenant, and Mr Holder is a guarantor. Two leases run until 2017, and one until 2022.

(c) 40 permanent staff and 20 contracting staff would lose their jobs. The total weekly wage outgoings are approximately $20,000 and most staff will be entitled to four weeks' wages for termination.

(d) Gym members will lose their access to the gym, and the defendants would have to refund about $90,000 in pre-paid gym fees.

(e) A number of businesses which sub-lease space at the three gyms will be detrimentally affected by the gym businesses shifting.

(f) The defendants would have no income to meet outstanding debts to suppliers totalling approximately $90,000.

(g) Damages are an adequate remedy for Health Club Brands. The defendants have filed undertakings as to damages along with an undertaking to deposit funds equivalent to 5% of their gross monthly turnover into the trust account of their solicitor, representing franchise fees otherwise payable. They are also offering reciprocal membership rights which were available prior to cancellation.

[51] It is true that granting the injunctions sought is likely to have a catastrophic effect on the defendants' businesses. Nevertheless I have concluded that the overall justice of this case favours the grant of an injunction restraining the defendants from operating gym businesses from any of the business premises, and further, in the case of the Three Kings gym, within five kilometres of the business premises, until further order of the Court. In reaching that conclusion, I have taken the following into consideration:

(a) Health Club Brands has a strongly arguable claim that it has enforceable contractual provisions which restrain the defendants from

operating a gym business at each of the three business premises. In respect of the Three Kings franchise, there is also a serious question as to whether there is a five-kilometre restraint of trade operating, although that argument has to be assessed as being less clear cut.

(b) Conversely, the defendants' claim that breaches by Health Club Brands of the franchise agreement entitled them to cancel the franchise agreements must be assessed as weak. Even on the defendants' own evidence, there is little to support its argument that Health Club Brands did not provide ongoing assistance, and indeed much to support Health Club Brands' argument that it did.

(c) Even if Health Club Brands cannot rely upon its restraint of trade clause, it can nevertheless seek to enforce the provisions of clause Q, requiring the assignment of the lease of each of the premises, thus achieving the same outcome.

(d) The loss suffered by Health Club Brands might ultimately be capable of being adequately compensated for in damages. But there is no evidence provided by the defendants to suggest that they have any means to meet a substantial damages award. On Mr Holder's evidence, the franchisee defendants are in financial difficulty.

(e) The proposed arrangement whereby 5% of gross takings be paid into the trust account of the defendants' solicitor also provides little comfort. Such an amount would no doubt represent only a part of any award of damages if Health Club Brands succeeds in its claim. Moreover, such an arrangement would be difficult to enforce. It would likely require entering into complex arrangements to ensure that 5% of the gross proceeds was properly calculated and paid.

(f) If ultimately the defendants are able to establish that clause Q and the restraints of trade are not enforceable against them, they can enforce

Health Club Brands' undertaking as to damages, which I assess as having substantial value.

(g) Other franchisees will be damaged by the actions of the defendants, as the value of the business model they pay franchise fees for will be diminished by the reduction in number of Club Physical gyms.

(h) Although the defendants point to other third parties who will be harmed if an injunction is granted, Health Club Brands has stated that it will seek an assignment of each of the leases of the business premises, and will also seek to employ those staff at the three gyms who were Club Physical staff immediately prior to the termination. If the defendants maintain that Health Club Brands has no right to an assignment it may be that some interim arrangement can be reached between the parties to preserve the position pending final resolution of this proceeding.

[52] There will undoubtedly be harsh consequences for the defendants which flow from the issue of this injunction. However, given the relative strength of each party's case, this consideration does not outweigh those which tend to support the grant of an injunction.

Defendants' application for interim injunction restraining use of customer details

[53] The defendants seek an injunction restraining Health Club Brands from accessing contact details of the franchisee defendants' gym members, and from contacting them. Mr Holder's evidence is that prior to cancellation, all members' names, phone numbers and email addresses for each gym were uploaded to a computer system operated by Health Club Brands. Health Club Brands therefore had full access to all of those details as they existed at that point in time, and has been phoning, texting and emailing Jolt Fitness members, attempting to persuade them to change back to Club Physical. Mr Holder says that he regards that customer information as the property of Health Club Brands. He takes this attitude because

the agreements for sale and purchase of the Three Kings and Westgate gyms expressly included "membership base" as an intangible asset acquired on purchase, and the sale and purchase agreement for Botany expressly included "membership contact" details as an intangible asset acquired on purchase. The defendants contrast this with the fact that the franchise agreements, they say, do not have any provision which bears upon the ownership of the client database. The balance of convenience favours the defendants because harm is being caused to their business by the contact being made. At least one communication from Health Club Brands to a Jolt Fitness gym member has included a statement that the franchisee defendants have breached the Fair Trading Act 1986.

[54] The defendants in my view do not reach the threshold of establishing that there is a serious question to be tried that the use by Health Club Brands of the customer details is a misuse of the defendants' property or confidential information. This is because clause Q contemplates that on termination "for any reason" the franchisee will immediately cease carrying on the business at the premises, co-operate in the assignment of the lease to Health Club Brands and will co-operate with Health Club Brands to ensure a smooth transition so as not to disrupt the customers of the business. This plainly contemplates that Health Club Brands will simply step into the shoes of the franchisee defendants and carry on the business with the existing customers. To do this, Health Club Brands would need access to the client details and it would have to be free to contact them. Moreover, the franchisee defendants accept an obligation to co-operate with Health Club Brands to ensure a smooth transition so that the customers of the business are not disrupted.

[55] Given these provisions, the defendants' argument faces very considerable hurdles to the extent that I am satisfied an injunction should not issue.

[56] For this reason the defendants' application is declined.

Result

[57] Health Club Brands' application for an interim injunction restraining the defendants from operating a health and fitness business is granted, but on modified terms to those sought as follows:

(a) In respect of the Three Kings franchise, the second and fourth defendants are restrained from trading at, and within five kilometres of, the Three Kings premises formerly operated as a Club Physical gym until further order of the Court.

(b) In respect of the Botany and Westgate franchises the first, third and fourth defendants are restrained from trading at the Botany and Westgate premises formerly operated as Club Physical gyms until further order of the Court.

[58] The defendants' cross-application to restrain Heath Club Brands from accessing contact details of the franchisee defendants' gym members, and from contacting those members, is declined.

[59] I ask the registry to list this proceeding before me for a telephone conference to decide how it is to be managed through to trial. Costs are reserved.

Winkelmann J