Enforceability of post-employment restrictions
By Michael P. Fitzgibbon, Partner, Borden Ladner Gervais LLP

The natural consequence of increased competition on a local and global level, a shrinking talent pool and ease of mobility of workers is that employees are in the driver's seat so far as their careers are concerned (see Hira, Nadira A., *You Raised Them, Now Manage Them* (Fortune, May 28, 2007) 38 and also Dychtwald, K., Erikson, T.J. and Morison, R., *Workforce Crisis – How to Beat the Coming Shortage of Skills and Talent* (Boston, Harvard Business School Press, 2006)). It is a "seller's" market so far as talent is concerned and Gen Yers, as a rule, are not averse to crossing the street in the hope that greener pastures await. Employers are making a significant investment in attracting, hiring, training and retaining employees and they are attempting to safeguard that investment by restricting, to varying degrees, the activities in which their workforce can engage post-employment.

The rubber hits the road when the employee departs and joins the competition or engages in activities that the employer believes are in breach of the terms of the restrictive covenant agreed to by the employee. The employer tries to enforce the agreement by way of, for example, an injunction and the court is called upon to scrutinize, among other things, the reasonableness of the agreement and, hence, its enforceability.

It is likely that, for the reasons mentioned, this type of litigation will become more common. Though the cases seem relatively consistent regarding the inquiry that the court will engage in when assessing the enforceability of these agreements, courts have, increasingly, placed these covenants under a microscope before enforcing them.

Reasonableness in all respects

Where the employer attempts to enforce a restrictive covenant, the threshold issue confronting the court will be whether the covenant is "reasonable." The leading Canadian case on point is *Elsley v. J.G. Collins Insurance Agencies Ltd.* [1978] 2 S.C.R. 916, where the court established a three-fold test for determining the enforceability of restrictive covenants:

1. The employer has a legitimate proprietary interest that it is entitled to protect;
2. The restraint is reasonable between the parties in terms of temporal length, geographical area, the nature of the activities prohibited and overall fairness; and
3. The restraint is reasonable with reference to the public interest.

The court was careful to note that reasonableness is to be determined having regard to the specific circumstances of each individual case. In other words, while other cases are of assistance in establishing general principles they are of little value in deciding whether the specific covenant is, itself, reasonable.

Accordingly, the court will presume that the covenant is *prima facie* void as being in restraint of trade and is contrary to public policy unless that presumption is rebutted by

the party seeking to enforce the covenant showing that it was both necessary and reasonable in all of the circumstances.

A recent decision showing the court's approach is that of Mr. Justice Frank Newbould of the Ontario Court of Justice in *Trapeze Software Inc. v. Bryans* (2007) CanLII 1882 (ON S.C.).

Trapeze Software Inc. brought a motion to enjoin certain former employees by way of interlocutory injunctions from being employed by a competitor of Trapeze for a period of one year from the time when each of the defendants left the employment of Trapeze. Trapeze sought to enforce the non-competition agreements signed by the defendants with Trapeze which provided that they would not be involved with a competitor of Trapeze for 12 months after they left the employment of Trapeze. Trapeze also asked for interlocutory injunctions:

- to enforce a non-solicitation clause under which each of the defendants agreed not to contact or solicit any Trapeze clients within 12 months of their leaving their employment with Trapeze; and
- to enjoin the misuse or disclosure of confidential information of Trapeze which each of the defendants acquired in the course of their employment with Trapeze.

Justice Newbould summarized the law in the area as follows:

- the general rule in most common law jurisdictions is that non-competition clauses in employment contracts are void as being a restraint on trade;
- for a restraint on trade to be valid it must be reasonable in the interests of the contracting parties and also reasonable in the public interest;
- there are competing interests at play here. While there is an important public interest in discouraging restraints on trade, and maintaining free and open competition unencumbered by the fetters of restrictive covenants there is also a need to enforce contracts, freely entered into, "by knowledgeable persons of equal bargaining power";
- the notion of "reasonableness" strikes an appropriate balance between these competing interests; and
- restrictive covenants must be reasonable in the following respects (a) whether the employer has a proprietary interested entitled to protection (b) whether the temporal or spatial features of the clause are too broad (c) whether the covenant is unenforceable as being against competition generally, and not limited to proscribing solicitation of clients of the former employee.

The court went on to consider these factors and, as a general comment, concluded that, in the circumstances, 12 months was reasonable. The non-competition clause ran into difficulty because of its geographic scope (Canada, the U.S., and anywhere else in the world where Trapeze marketed its products or services during the period of employment of the defendants). The clause went "too far" in protecting what otherwise was

acknowledged as a “legitimate business interest,” and was “unreasonable” and unenforceable.

Justice Newbould then went on to consider the non-solicitation covenant, which he also found to be unenforceable. In reaching that conclusion, he relied on the recent Court of Appeal case of *IT/NET Inc v. Cameron* (2006) CanLII 912 (ON C.A.), where the following non-solicitation clause was found to be unenforceable in the circumstances:

> 4.2 he/she will not attempt to solicit business from any IT/NET clients or prospects without the written consent of IT/NET. The intent of this clause is to reasonably protect the goodwill of IT/NET while at the same time not unduly limiting the ability of the Subcontractor to continue in the practice of his/her profession.

Goudge J.A., for the court, stated:

> However, clause 4 goes considerably beyond what is needed to protect this proprietary interest. The language of clause 4.2 prevents the contractor from soliciting business from any IT/NET client or prospect, not just from the client where the contractor has been placed. This prohibition applies whether or not the contractor knows that the target of his solicitation is an IT/NET client or prospect or whether he has any prior relationship with that client or prospect due to his work for IT/NET.

Justice Newbould noted that the provision before him did not contain a geographic limitation and this was also problematic from an enforceability perspective.

As he said, “as with the non-competition clause, Trapeze has failed to satisfy me that it has a strong *prima facie* case that the non-solicitation clause as drafted in this case is reasonably required or valid.” This recent case emphasizes that employers must not only be thoughtful when drafting restrictive covenants but also when selecting the covenant to use.

Conclusion

While employers are increasingly using restrictive covenants to protect their corporate assets and investments, courts appear to be adopting a more probing approach when determining their enforceability. A number of principles are worth emphasizing.

1. Employers must have a proprietary interest entitled to protection. Though this might be a relatively low standard, it is nonetheless the threshold question from which all others flow and emphasizes that a restrictive covenant must go no further than is reasonably necessary to protect the employer’s legitimate proprietary interests *Tank Lining Corp. v. Dunlop Industrial Ltd.* (1982), 40 O.R. (2d) 219 (C.A.).

2. A restrictive covenant's duration, geographic reach and scope of activities restricted must also be reasonable and not go beyond what is required for the legitimate protection of the employer's interests. A clause that is over-reaching or which goes beyond the absolute minimum level of protection that is required to protect the otherwise legitimate business interest will not be enforced. In other words, a non-competition provision will not be enforced where a non-solicitation provision would have provided sufficient protection.
3. Generally speaking, though this may not be the case in all provinces (*ACS Public Sector Solutions Inc. v. Courthouse Technologies Ltd.* , (2005) BCCA 605 (CanLII) and *KRG Insurance Brokers (Western) Inc. v. Shafron*, (2007) BCCA 79 (CanLII) however *Canadian American Financial Corp. (Canada) Ltd. v. King* (1989), 36 B.C.L.R. (2d) 257 (C.A.)), a court will not "read down" or "blue-pencil" an unreasonable restrictive covenant, nor will the court re-write an unreasonably broad restrictive covenant so as to make it enforceable (*Maguire v. Northland Drug Co.* , [1935] S.C.R. 412, *Globex Foreign Exchange Corp. v. Kelcher*, 2005 ABCA 419 (CanLII), *Transport North American Express Inc. v. New Solutions Financial Corp.* [2004] 1 S.C.R. 249, *Community Credit Union Ltd. v. Ast*, (2007) ABQB 46 (CanLII)).
4. While there is no substitute to "getting it right" from the outset, and though there are conflicting cases on the point, there *might* be some advantages to drafting a "ladder-type" restrictive covenant providing a series of scenarios where the failure of one scenario drops the enforcement to the next lesser term. An Alberta court recently found that it could, when faced with such a provision, narrow the scope of the covenant to what it believed was reasonable as a means of giving effect to the objective intentions of the parties; *Community Credit Union Ltd. v. Ast* (2007) ABQB 46 (CanLII)

Saying the deck is stacked against employers in these cases would be an overstatement, given that courts will and do enforce these clause in appropriate circumstances. It is probably fairer to say that courts continue to view these restrictions with some trepidation and continue to hold the party seeking to enforce them to a high standard of reasonableness.

Michael P. Fitzgibbon *is a partner at the national law firm of Borden Ladner Gervais LLP, where he practices management-side labour and employment law. He runs the labour law blog Thoughts from a Management Lawyer.*