RESTRICTIVE COVENANTS

Geoff Hope

Restrictive covenants are a common tool used in employment contracts to protect the trade secrets, business connections and other proprietary information of the employer. These covenants typically take the form of either a non-competition clause or a non-solicitation clause, or some combination of the two. These covenants purport to limit the freedom of an employee to exploit his or her skill, connections and know-how outside the employment relationship, both during the term of employment and after the employment ends. While many employers are under the assumption that restrictive covenants are adequate to protect their interests when an employee leaves, the enforceability of these clauses is sometimes questionable.

Any restrictive covenant in an employment contract is considered to be a restraint of trade that can only be justified and enforceable if it is reasonable in reference to the interests of both the parties concerned and the public. The traditional considerations in deciding whether a restrictive covenant is reasonable in an employee/employer relationship is identified by the Supreme Court of Canada in *Elsley* v. *Collins*. Basically, the party seeking to enforce the covenant must have a proprietary or legitimate interest entitled to protection, the temporal and spatial features of the covenant must be reasonable and not overly broad, and the covenant must not prevent competition generally unless it is reasonably required for the protection of the employer in the circumstances.

The more straightforward of these factors to consider in assessing the enforceability of restrictive covenants are the temporal and spatial features (i.e. how long the covenant purports to restrict the employee and what geographic area it applies to). These factors can be assessed on the simple basis of reasonableness in the circumstances. For example, if the employer operates its business exclusively in northern Alberta and the departing employee has only worked there for 5 months, it would obviously be unreasonable to restrict the employee from working in the industry anywhere in North America for 5 years after termination. But while the temporal and spatial features of a clause are relatively simple to analyze, deciding whether the employer has a proprietary interest to protect and whether the clause is appropriate to protect that interest are

2000, 10235 - 101 Street
Edmonton, AB T5J 3G1
PH: 780.423.3003

1900, 350 - 7th. Avenue S.W.
Calgary, AB T2P 3N9
PH: 403.260.8500

203, 5102 - 50th Avenue
Yellowknife, NT X1A 3S8
PH: 867.920.4542

www.fieldlaw.com

both issues that complicate the enforceability issue for restrictive covenants.

Non-Solicitation Clauses

The intent of a non-solicitation clause is to prevent a departing employee from exploiting his knowledge of the former employer's customers in order to lure them away from doing business with that former employer. Such clauses are not as onerous as non-competition clauses, because they are simply geared to protecting the employer's client or customer base, rather than preventing the former employee from being in the same business at all. Typically, an employer will have a clear proprietary interest in its customer lists and business goodwill. Therefore, assuming that the temporal and spatial limits of the clause are not unreasonable, a non-solicitation clause protecting these proprietary interests of the employer will generally be enforceable against the departing employee.

Non-Competition Clauses

As illustrated by the recent decision of the Ontario Court of Appeal in *Lyons* v. *Multari*, non-competition clauses in the employment context are becoming more difficult to enforce, mainly because it is difficult for employers to establish a proprietary interest that such a stringent clause is needed to protect. The Courts generally frown upon any employer who is simply attempting to reduce competition by keeping a former employee out of the business after his employment terminates. The only proprietary interests that the majority of businesses will have are their business contacts, goodwill, and customer lists, and all that is generally required to protect those interests is a non-solicitation clause. Generally speaking, the courts will not enforce a non-competition clause if a non-solicitation clause would adequately protect the employer's interests.

A non-competition clause will only begin to be justifiable in certain fact situations. For example, where the employee is dealing with crucial trade secrets that could seriously undermine the employer's business, the employer would obviously have a legitimate interest in stopping that individual from using that information to compete. A more common example of a situation that might justify a non-competition clause is where the departing employee was so entrenched in the company that customers perceive him or her as the personification of the company itself.

As a general rule then, if an employer can adequately protect its interests with a non-solicitation clause without resorting to a non-competition clause, they will often be better off simply relying on a well-drafted version of the former rather than gambling on the ultimate enforceability of the latter.