Posted on: July 1, 2010

# REVISITING THE RESTRICTIVE COVENANT

**July 2010**

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*Richards Buell Sutton Employment Law Newsletter, July 2010*

The Supreme Court of Canada released its decision in *Shafron v. KRG Insurance Brokers Inc.*, in January 2009. At issue in that case was the validity of a restrictive covenant purporting to restrain the employee Shafron from competing with his former employer for a period of 3 years, within the "Metropolitan City of Vancouver". While the case turned on the ambiguity of this geographical descriptor, Canada's top court took the opportunity to set out legal principles that come into play when an employer seeks to enforce such a covenant.

Our courts, as a matter of public policy, do not like restrictive covenants. In *Shafron*, Mr. Justice Rothstein for the court cited the "general rule" that restrictive covenants, being restraints of trade, are contrary to public policy and therefore void. For these reasons, the law effectively presumes such clauses to be "unreasonable" and they will be enforced only where the employer can establish reasonableness. What is reasonable will depend on consideration of the length and geographical scope of the covenant, the nature of the restricted activity and the other surrounding circumstances. An "ambiguous" covenant will never be considered reasonable.

In the past, some courts have preferred to hold parties to their agreement, or at least a watered down version of their agreement, by "severing" the content of restrictive covenants found to be unreasonable. In *Shafron*, the Supreme Court of Canada addressed this tendency, clarifying the law of severance and arguably putting a clamp on this sort of judicial intervention.

**Ruling in *Shafron***

The B.C. Court of Appeal had found the phrase "Metropolitan City of Vancouver" ambiguous, but was prepared to give it life. The Court of Appeal ruled that a certain interpretation of the phrase was likely in the reasonable contemplation of the parties, and the covenant could be enforced accordingly.

At the Supreme Court of Canada, the covenant was again found ambiguous, but struck down. The Court refused to save the ambiguous phrase through the doctrine of severance, because:

- the general rule is that unreasonable restrictive covenants in employment contracts are unenforceable;
- "blue-pencil severance", where the court ignores the offensive language as if drawing a line through it, will be allowed only sparingly, and only where the content is clearly severable, trivial and "not part of the main purport of the restrictive covenant";
- "notional severance", or the reading down of a clause to make it reasonable, has no place in the interpretation and enforcement of restrictive covenants, because there is no "bright line" to make it clear where the line is to be drawn between reasonableness and unreasonableness (and because such severance simply amounts to the court re-writing the covenant for the parties according to what the court thinks is reasonable).

In *Shafron,* the Supreme Court of Canada highlighted an established doctrine of law to the effect that restrictive covenants in the employment context call for greater scrutiny than similar covenants in agreements for the purchase of a business. The distinction is based on the fact that the seller of a business is typically selling the "good will" of the business and will be expected not to compete in order to preserve that good will for the purchaser. The distinction makes sense also because there is usually an imbalance of bargaining power between an employer and an employee which does not exist between parties to the sale of a business.

**Recent Cases in British Columbia**

Restrictive covenants often come under judicial scrutiny for the first time when the employer seeks an injunction against a departed employee. In *McMillan Tucker McKay v. Pyper*, a law firm sought an injunction against a departed lawyer who had signed an agreement that he would not practice law within five miles of this former law firm in Cloverdale for a period of three years. To entitle itself to the injunction, the law firm was required to show, amongst other things, that it had a strong *prima facie* case that the restrictive covenant at issue was enforceable or, in other words, that it was reasonable. To make that determination, the chambers judge noted that the critical issue was whether the spatial and temporal limits were reasonable (there was no issue of ambiguity). The court cited the statement in *Shafron* that restrictive covenants in employment contracts must be distinguished from those in agreements for the sale of a business. To assess "reasonableness", the court looked to the following factors:

1. Does the employer have a proprietary interest entitled to protection?
2. Are the time and spatial restrictions reasonable?
3. Are the restrictions clear and certain, or overly broad and therefore against the public interest?

The court decided that neither the three year term, nor the five mile restriction, were reasonable, expressing much concern about the lawyer being prevented from practicing at all in the area where he had practiced for the last six years. Mr. Justice Pearlman wrote "the public interest is not served by restrictions on the right of qualified professional persons to practice their profession at the location of their choice. The court also noted that there was some power imbalance, in that the Plaintiff was an articling student who had never practiced in British Columbia when he signed the agreement at issue years earlier.

In another recent case, *F & G Delivery Ltd. v. MacKenzie,* a freight delivery company sought an injunction against a former employee who had taken a position with a competitor. Six years earlier, upon his hire, the employee had signed a restrictive covenant. In it, he had agreed not to solicit business from any client or potential client for two years, or engage himself in similar business activity for one year (within a geographical area unfortunately not explained in the decision). He also agreed not to cause employees of F & G to leave F & G for a period of three years. The Court would not grant the injunction. The court found the customer solicitation clause and the employee hiring clause "much broader than necessary to protect any legitimate proprietary interest" of the former employer. (Relief based on the employee's agreement not to work at all in a similar business for one year was not pursued, probably because it clearly was a non-starter).

It should be noted that neither of the two cases cited above were final rulings on the enforceability of the covenants at issue. Those issues await trial, should that be necessary. But these are clear rulings that the covenants at issue, on their face, are not reasonable.

**Going Forward**

*Shafron* will be important going forward in a number of respects. Arguably *Shafron* will make restrictive covenants more difficult to enforce. Certainly the decision has put judges and litigants on alert that saving restrictive covenants through judicial re-writing of ambiguous phrases is not likely to fly. It has also made clear that the doctrine of severance has extremely limited application. For employers, the basic rules surrounding restrictive covenants remain the same. First, there must be absolutely no ambiguity about when and where the activity is restricted, or about what activity is restricted. Second, a "less is more" approach is really the only approach – asking for too much will bring no protection at all.