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Employee Non-Competition Covenants: No Place for Blue Pencils

The recent decision of the Court of Appeal for Ontario in *Veolia ES Industrial Services Inc v Brulé*[1] deals with the interpretation and enforceability of a non-compete clause in an employment agreement and the scope of an employee's fiduciary duties to a former employer.

The parties entered into a three-year employment agreement on January 1, 2004, which was subject to the employer's right to terminate the employment for cause or without cause upon payment of the compensation to which the employee was entitled until the end of the term. The employee also had the right to terminate the employment agreement by giving the employer 180 days notice.

A non-competition covenant was included in the employment agreement and provided that Brulé employee was restricted from competing with the employer's core business for a period which would be either: (1) two years following termination for cause or as a result of the agreement's three-year term expiring; or (2) two years commencing January 1, 2007 following termination without cause or as a result of the employee's resignation in accordance with the agreement.

Brulé gave the employer notice of resignation on July 7, 2004, following which the employer asked him not come into work, but

[1] 2012 ONCA 173 ("Veolia").

continued to pay him until one or two weeks prior to the expiration of the 180 day notice period. Upon leaving, the employee asked a colleague to assemble a binder with information about recent municipal tenders and bids put in by the company and others. When he left the company, Brulé took this binder and a list of the company's employees.

Following his departure, Brulé started his own company in the business of rehabilitating water mains, which was related but not identical to the employer's business of rehabilitating sewers . In the fall of 2005, Brulé's new company needed work and decided to submit a bid on a public tender for sewer rehabilitation. They succeeded and were awarded the tender over the former employer Veolia who had submitted the next-lowest bid . The employer sued for the gross profits claimed to have been lost as a result of not being awarded the tender.

At trial, the judge rendered the non-compete clause in the employment agreement enforceable by severing the words "commencing on January 1, 2007" in accordance with the blue-pencil severance test articulated by the Supreme Court of Canada in *KRG Insurance Brokers (Western) Inc v Shafron*.[2] The trial judge noted that severing this phrase produced the result that the parties intended, which was to have a two-year non-competition covenant.

The trial judge found that Brulé breached the non-competition covenant by bidding on the tender for the sewer work. Furthermore, he found that the employee breached his fiduciary duties to Veolia by breaching the non-competition covenant, by leaving the company with the binder of information regarding prior bids and by failing to disclose to Veolia that his company was submitting a bid in respect of the municipal tender for sewer rehabilitation work.

The Court of Appeal for Ontario overturned the trial judge's decision. The court rejected the application of the blue-pencil severance test to remove the words "commencing on January 1, 2007" from the non-competition covenant and concluded that,

[2] [2009] 1 SCR 157 ("Shafron").

without the deletion of the disputed words, the restrictive covenant was unreasonable and unenforceable as the obligation commenced two years after the employee ceased to be employed.

Based on the Supreme Court of Canada's decision in *Shafron* the Court of Appeal noted that blue-pencil severance is only available in respect of trivial or technical parts of a restrictive covenant that the parties would unquestionably have agreed to sever without varying any other terms of the contract or otherwise changing the bargain. The words "commencing January 1, 2007" were not trivial as they pertained to the duration of the restriction. Furthermore, there was evidence that the parties would not have agreed to sever these words without varying the terms of the contract or changing their bargain.

The Court referred to the drafting lawyer's memorandum which explained to Brulé that upon termination without cause the company would pay his salary until the end of the three-year term. In light of this fact, the Court noted that it was logical for the non-competition obligation to commence on January 1, 2007, being the day after the term of the agreement expired. Removing this part of the clause would have left Brulé free to compete during a period in respect of which he may have been paid by Veolia. As a result, the Court found it highly unlikely that the parties would unquestionably have agreed to sever the words "commencing January 1, 2007" without varying any other terms of the contract.

Interestingly, the Court did not distinguish between the two sub-clauses of the non-competition provision which contained the disputed words, "commencing January 1, 2007". The first sub-clause applied in the event that the employee was terminated without cause, while the second sub-clause applied if the employee terminated the agreement. The Court could have removed the disputed words only from the second sub-clause. The effect would have been to establish that if the employee terminated the employment (as was the case on the facts) the non-competition obligation commenced on the effective date of his resignation. This would arguably have been a reasonable interpretation the parties' intentions with respect to the non-competition covenant.

Having ruled that the non-competition covenant was unenforceable, the Court went on to consider whether the employee breached his fiduciary duties to the former employer. The Court affirmed that certain fiduciary duties of an employee survive the employment relationship, but ruled that after the employment ends, a fiduciary is free to compete with his former employer, provided that he does not do so unfairly. Unfair competition includes soliciting the employer's customers or employees, taking advantage of a business opportunity that was developed during the employment, and using or disclosing the employer's confidential information in competing.

In this case, the Court found that Brulé did not breach his fiduciary duties because he did not compete unfairly with his former employer. With respect to the binder that he took when he left Veolia, the Court found that the employee did not use the information contained in the binder in making his bid for the disputed tender. Mere possession of the information did not make the competition unfair. Furthermore, the Court ruled that the information in the binder was neither confidential nor sensitive as municipal tenders and bids are publicly issued. Lastly, the Court ruled that the employee did not breach his fiduciary duties by failing to disclose to the employer that he was bidding on the tender for sewer rehabilitation. A former fiduciary who is free to compete is not required to tell his former employer that he is about to do so.

This decision reminds us of the importance of meticulous drafting and careful deliberation of all the possible interpretations of a prospective non-competition clause in an employment agreement. As restrictive covenants are *prima facie* unenforceable, the onus falls on the employer, being the party seeking to enforce the restrictive covenant, to show that the covenant is reasonable. A poorly drafted non-competition clause will prejudice the employer's ability to demonstrate that the covenant is reasonable and that it should be enforced.

Although the doctrine of severance is potentially available to resolve an ambiguous term in a restrictive covenant, the *Veolia* decision confirms that the doctrine is only available in rare cases where the portion being removed is trivial and not central to the main purport of the restrictive covenant. Anything pertaining to

the duration or location of the non-competition obligation is not likely to be trivial, as these are essential elements of a non-competition covenant.

Finally, this decision confirms that an employer can rely on the continuing fiduciary duties of a former employee in the absence of a non-competition clause. However, fiduciary duties only protect employers against unfair competition by the employee, which includes solicitation of the employer's customers and employees, appropriation of business opportunities developed during the employment relationship, and use or disclosure of the employer's confidential information in competing.

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