HUNTER-LIBERATORE-LAW

Much Ado About Nothing

Looking At Non-Compete Clauses in Ontario Employment Law

a) Background

In this article we consider the impact of the prohibition of employment-related non-compete agreements in Ontario. The prohibition was introduced through amendments to the Ontario *Employment Standards Act, 2000* ("ESA") effective October 25, 2021. As of now, Ontario is the only common law province in Canada that has made non-compete agreements illegal in employment contracts. A summary of the changes can be found here.

The ESA defines a non-compete as "an agreement, or any part of an agreement, between an employer and employee that prohibits the employee from engaging in any business, work, occupation, profession, project or other activity that is in competition with the employer's business, after the employment relationship between the employee and the employer ends." Currently, there are no express restrictions on non-solicit agreements. The non-compete restrictions also do not apply to C-Suite executive positions.

b) New Developments

- **Parekh et al v. Schecter et al**

In early 2022, the Courts were able to interpret the new ESA restriction on non-competes for the first time. The Courts found that the new amendments would **not** be retroactive, but would only apply to employment agreements signed after the amendments came into effect.

In this case, the Plaintiff bought a dental practice in 2020 and decided to retain a few employees including the Defendant who was a dentist. He had entered into an employment agreement that contained a non-compete provision prior to the Plaintiff acquiring the practice. The provision read:

> *Non-Competition. The Associate shall not during the Term of this Agreement and for two (2) years thereafter, either directly or indirectly, whether as a proprietor, partner, shareholder, employee, associate or otherwise, carry on or be engaged in the practice of dentistry anywhere within a five (5) kilometer radius of the Premises*

The following year, the Defendant left the practice and began working in dentistry within a 5km radius of his previous employer.

The Defendant argued that the new amendments to the *ESA* made the non-compete illegal and thus void. They argued the provision applied retroactively "by necessary implication."

The Court considered the intent of the Legislature and the deliberate decision to include an effective date. The Court concluded that the amendments were not applicable to the contract as it was entered into prior to October 25, 2021. However, this did not end the Court's inquiry as it was then necessary to consider whether the non-compete was enforceable under the common Justice Sharma said:

> *At most, and in respect of this case, the new ESA provisions confirms the public policy against restraint of trade, which has already been accepted in the common law.*

Ultimately the Court found, despite the somewhat restrictive clause, the non-compete was enforceable.

- **M & P Drug Mart Inc. v. Norton**

The employee in this case, Norton, began working for Hometown IDA pharmacy as a pharmacist in 1980. IDA was later purchased by M & P Drug Mart Inc in 2014. At this time, Norton, entered into an employment agreement with M & P that contained a non-compete provision. The non-compete clause reads:

> *The Employee agrees that during the Employee's employment with the Company and during the one year period following the termination of the Employee's employment with the Company, for any reason whatsoever, the Employee shall not carry on, or be engaged in, concerned with, or interested in, directly or indirectly, any undertaking involving any business the same as, similar to or competitive with the business within a fifteen (15) kilometre radius of the business located at 10 Main Street East, Huntsville, Ontario P1H 2C9.* [the address is Hometown IDA]

In 2020, following his resignation with M & P, Norton began working as a pharmacist at Campus Trail Pharmacy, which was under 3 km from his previous employer. The employer alleged that Norton breached the non-compete provision in his employment contract. At trial Justice Bale found the non-compete to be unenforceable since it was overly broad and ambiguous. This decision was appealed.

At the Ontario Court of Appeal, Justice Zarnett reiterated the logic in *Parekh et al v. Schecter et al.*

> *These events occurred prior to the coming into force in December 2021 of the Working for Workers Act, 2021, S.O. 2021, c. 35 (the "WWA"), which prohibits employers from obtaining a non-competition agreement from an employee, subject to certain narrow exceptions. The parties' rights were therefore governed by the common law principles that treat such a covenant as unenforceable, even if freely entered into, unless it is reasonable as between the parties and with respect to the public interest.*

Having agreed that the new prohibition did not apply, the Court of Appeal set out the framework of analysis for the enforceability of non-competes in Ontario. In summary, the framework is as follows:

- The general rule is that, on public policy grounds, a provision in a contract that restrains a vendor of a business from competing with the purchaser, or an employee upon leaving employment from competing with the employer, is prima facie unenforceable.
- The exception to the general rule is that the provision will be upheld if it is reasonable in reference to the interests of the parties and the public, judged in light of the circumstances at the time the covenant is made.
- In order to determine whether a non-competition agreement is reasonable, the extent of the activity sought to be prohibited, the geographic coverage of the restriction, and its duration are all relevant.
- A non-competition covenant in an employment agreement that restricts the post-termination activities of an employee is subject to more rigorous scrutiny than a non-competition covenant in a sales agreement that restricts the post-sale activities of the vendor.
- The party seeking to enforce the restrictive covenant has the onus of demonstrating that it is reasonable as between the parties; the party seeking to avoid enforcement has the onus of showing the covenant is unreasonable with respect to the public interest.
- In order to withstand scrutiny, a covenant must be clear as to activity, time, and geography. A covenant that is ambiguous on any of these matters is prima facie unenforceable.
- The court is not permitted "to rewrite a restrictive covenant in an employment contract in order to reflect its own view of what the parties' consensus ad idem might have been or what the court thinks is reasonable in the circumstances".

Ultimately, the Court of Appeal agreed with the lower courts. The provision was too broad as it restricted activities beyond working as a pharmacist for a competitor. It was also ambiguous as to what activity was restricted and the Court could not revise the covenant to make it reasonable.

- **Dymon Storage Corporation v. Nicholas Caragianis**

Dymon Storage Corporation, the Plaintiff, builds self-storage units in Ottawa and the Greater Toronto Area. Bliss Edwards resigned from Dymon and began working at a competitor, Smartstop. Dymon alleged that Edwards breached the non-compete provision in her employment contract and shared confidential information.

The non-compete clause restricted Edwards from working in any business that would compete with Dymon, for 10 years throughout Canada. Again, since the clause was entered into before October 25, 2021, the new amendments were not applicable, and Justice Koehnen engaged in the common law analysis. Deeming the clause unreasonable and thus unenforceable, he considered the significant geographical scope - even though Dymon only operated in the Ottawa and Greater Toronto Area - and the lengthy 10-year duration.

This case also offers an interesting discussion on the distinction between know-how and confidentiality. For information to be considered confidential, it must have the "necessary quality of confidence". It must be specific in nature. The court identified the following considerations in determining whether information has the quality of confidence, including:

a. The extent to which the information is known outside the business;

b. The extent to which it is known by employees and others involved in the business;

c. Measures taken to guard the secrecy of the information;

d. The value of the information to the holder of the secret and to its competitors'

e. The effort or money expended in developing the information;

f. The ease or difficulty with which the information can be properly acquired or duplicated by others; and

g. Whether the holder and taker of the secret treat the information as secret.

The above was contrasted to "know-how" which the Court described as follows:

> Where information derives from a professional's experience, knowledge, practice, or skill; or is commonly known within an industry, it is not confidential to another party. Put differently, information is not confidential when it derives from a professional's techniques that are known in the field and could easily be duplicated by one with rudimentary skills in the trade.

The Court concluded that there was insufficient specific evidence that confidential information had been shared and declined to issue an order on that issue.

c) What's in a name?

Shakespeare said that 'a rose by any other name would smell as sweet.' Likewise, a non-solicitation agreement that has the same effect as non-competition clause will be interpreted as such. Like non-competes, non-solicits are unenforceable unless the party seeking enforcement can demonstrate that they are reasonable and necessary to protect business interests. Traditionally, non-solicits have been easier to enforce than non-competes because a well-crafted clause is less restrictive and focuses on the relationship between customers and the departing employee. While challenges to non-solicits as "non-competes in disguise" are not new, we anticipate that with the introduction of the legislative prohibition on non-competes, these arguments will be pursued with increased vigour. For contracts entered into after October 25, 2021, reasonableness will not be a consideration if it can be established that a non-solicit is really a non-compete, and therefore prohibited under the ESA.

- **Giacomodonato v PearTree Securities Inc.**

The Plaintiff was employed in the roles of President and Co-Head of Banking with the Defendant, PearTree. The Plaintiff alleged he was wrongfully dismissed and that he was underpaid from $3.194 million to $3.927 million. The employer denied this and counterclaimed that Plaintiff breached both the non-solicit and non-compete clauses. After finding the non-compete clause to be overly broad, the Court went on to consider the non-solicit. The portion of the clause in issue read as follows:

> *You…agree that during the term of your employment and for a period of 24 months after the cessation of your employment for any reason, you shall not… directly or indirectly, solicit… any customers or suppliers (which includes issuers, brokers and other intermediaries) of Peartree to secure engagements to underwrite securities offerings or otherwise obtain allocations of securities under those offerings for the purpose of gifting arrangements or other tax structured products.*

The provision was found to be "a camouflaged non-competition clause designed to eliminate competition." The evidence was that the clause restricted the Plaintiff from contacting issuers regarding any "flow-through offering", not just charitable flow-through products. As PearTree did not facilitate traditional flow-through offerings, the Court found that the non-solicit was even more restrictive than the non-compete. This clause is a perfect example of when a non-solicit is too restrictive and essentially becomes a non-compete.

d) Conclusion

The inclusion of the prohibition on non-competes in the ESA has not changed the Courts' approach to considering the enforceability of restrictive covenants, including non-competes. Courts maintain that restrictive covenants of any kind are *prima facie* unenforceable unless proven reasonable. Courts continue to consider the geographical coverage, temporal scope, and ambiguity as well balancing the public interest in not unduly restricting competition and protecting the ability of individuals to earn a living against the proprietary interests of employers.

Non-compete clauses have always been hard to enforce. Now that they are illegal in Ontario other than for select executive employees, we can expect added scrutiny of non-solicits. Any restrictive covenant should be drafted clearly, keeping the restrictions a reasonable as possible to protect the employer's interests.