

Don't Give Up On Restrictive Covenants



If revising your employment and independent contractor agreements is on the “to do” list for 2023, the recent case of [*Quick Pass Master Tutorial School Ltd. v Zhao, 2022 BCSC 1846*](#) is a good reminder to review any restrictive covenants in those agreements. The law in this area is always evolving and restrictive covenants can be difficult to enforce without careful drafting. However, as this case shows, B.C. courts are still willing to enforce properly drafted and reasonable covenants.

In the employment context, most decisions dealing with alleged breaches of restrictive covenants concern applications for interlocutory injunctions, with the issues never proceeding to a full trial on the merits. The dispute between these two parties first came before the BC Supreme Court in 2018, when Quick Pass Master Tutorial School Ltd. (“Quick Pass”) sought an interlocutory injunction against Mr. Zhao to prohibit him from competing with it, from soliciting its students, and from using its confidential information. In May 2018, the BC Supreme Court granted an interlocutory injunction regarding the non-competition covenant. This recent decision arises following a full trial on the issues.

Background

Quick Pass provides real-estate related tutorial programs in the Lower Mainland. Its target demographic is Mandarin speakers. In 2017, Quick Pass hired Mr. Zhao, a Mandarin-speaking real estate agent, to teach real estate tutorials for a two-year term. Mr. Zhao signed two agreements upon hiring: 1) an independent contractor agreement, and 2) a non-competition agreement. The independent contractor agreement included a “Confidential and Proprietary Information Agreement.”

The non-solicitation clause in the independent contractor agreement stated that:

“During the term of the Contractor’s active employment with the Company, and for two (2) years thereafter, the Contractor will not divert or attempt to divert from the Company any business the Company had enjoyed, solicited, or attempted to solicit, from its customers, prior to termination or expiration, as the case may be.”

The non-competition agreement included the following terms:

“4. The Contractor agrees with and for the benefit of the Company that during and for a period of eighteen (18) months from the date of termination of the Independent Contractor Agreement (whether such termination is occasioned by the Company, by the Contractor, or by mutual agreement), the Contractor will not, for any reason,

directly or indirectly, either as an individual or as a partner or joint venture or as an employee, sales representative, principal, consultant, agent, shareholder, officer or director for any person, firm, association, organization, syndicate, company or corporation or in any other manner whatsoever: carry on, be engaged in, be concerned with, be interested in, advise, lend money to, guarantee the debts or obligations of, or permit his or her name or any part of it to be used or employed by, any person, business, firm, association, syndicate, company, organization or corporation concerned with or engaged or interested in a business which is the same as, or competitive with, the business of the Company, in Vancouver, Burnaby, and Richmond, British Columbia.

5. The Contractor shall not profit from, directly or indirectly, nor engage in the business of pre-licensing real estate training, and real estate educating in a manner which is the same as, or competitive with, the business of the Company during and for a period of eighteen (18) months following termination of the Independent Contractor Agreement.”

In September 2017, Mr. Zhao incorporated his own real estate tutorial school. He subsequently advised Quick Pass that he was quitting and opening his own school in Burnaby, which is a city specifically named in the non-competition agreement. He began advertising his school on WeChat (a popular social media platform amongst the Mandarin-speaking community), on various websites, by email, and in a weekly newspaper. Quick Pass argued that he was using their confidential and proprietary materials in his new school.

At trial, Quick Pass sought damages for breach of the non-competition, non-solicitation and confidentiality agreements, and sought a permanent injunction enjoining Mr. Zhao from using or disseminating teacher materials he developed while working as a contractor for Quick Pass.

The Court’s Decision

The BC Supreme Court found that the non-competition clause was enforceable, but that the non-solicitation clause was not. In reaching this decision, it applied the following general principles concerning restrictive covenants:

- Restrictive covenants are presumptively unenforceable as a restraint of trade;
- Courts will apply a higher level of scrutiny to restrictive covenants in the employment context, and the degree of scrutiny applied will reflect the parties’ relative bargaining power; and
- The party seeking to enforce the covenant has to establish that:
 - there is a proprietary interest worthy of protection;
 - it cannot be adequately protected by a less restrictive measure; and
 - the covenant is reasonable in terms of the activity being restricted, the geographical area of the restriction and the duration of the restriction.

The court held that given the similar degree of bargaining power between the parties, this was not a case warranting a higher level of scrutiny. Notably, Mr. Zhao had negotiated an additional \$15 per hour in express consideration for the restrictions in the non-competition agreement (which was an almost 43% increase in his compensation).

Mr. Zhao argued that the non-competition clause was unenforceable on the basis that terms like “concerned with,” “interested in,” and “business which is the same as, or competitive with” were ambiguous, and that the clause was overly broad. The Court disagreed, noting that Quick Pass’ business was defined earlier in the independent contractor agreement, and that both the geographic scope (Vancouver, Burnaby and

Richmond) and temporal scope (18 months) were reasonable in the circumstances.

In comparison, the court held that the two-year non-solicitation clause was unenforceable because it was broader than necessary to protect Quick Pass' proprietary interests. In particular, it purported to restrict Mr. Zhao from soliciting anyone, regardless of whether he had any prior dealings with the person. The court also explained that even if it had found that the clause was enforceable, it would have concluded that Mr. Zhao did not breach the clause. The court commented that a general advertisement about a new business and location, which does not reference a former employer's name, does not breach a non-solicitation agreement.

The court acknowledged that assessing damages was difficult in this case, but that there was evidence that Quick Pass' student enrolments and income had significantly declined in the six-month period following the opening of Mr. Zhao's competing business. It also found that Mr. Zhao had appropriated work product he created while employed by Quick Pass. The court ultimately decided to award Quick Pass damages of \$50,000 for Mr. Zhao's breach of the non-competition clause and the confidentiality clause. The court declined to grant the permanent injunction sought by Quick Pass with respect to its teaching materials, on the basis that granting such a remedy would be a "herculean task" not warranted in the case.

Key Takeaways for Employers

- Careful and thoughtful drafting is important. Make sure that these clauses are specific and tailored to the business and the individual being restricted. In this case, the clause drafted with more thought and precision (the non-competition clause) was the one that the court upheld.
- Make sure the covenant is only as broad as necessary. In this case, Quick Pass sought to restrict solicitation of all of its customers, regardless of whether or not they were customers when Mr. Zhao worked at Quick Pass or customers with whom he had interacted during his engagement.
- This case does not mean that courts will always be willing to uphold an 18-month non-competition covenant, which is significant. In deciding to enforce the non-competition clause against Mr. Zhao, the court attached particular importance to the parties' equal bargaining positions and the fact that Mr. Zhao had received meaningful and specific consideration in exchange for agreeing to the significant restrictions. In many (if not most) employment relationships, the employer will have a meaningfully stronger bargaining position, which will be a factor in the scrutiny applied by a court in assessing any associated restrictive covenants.
- In certain cases, employers may want to consider providing employees with specific consideration in exchange for agreeing to significant restrictive covenants, and documenting this consideration in the applicable employment agreement, independent contractor agreement, or restrictive covenant agreement.

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