

Non-Compete Clauses In M&A Deals Presumed Lawful By Supreme Court Of Canada



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In a September 12, 2013, decision, the Supreme Court of Canada has enforced the restrictive covenants flowing from the sale of a business for a 10-year period post-closing.¹ The decision is particularly noteworthy as it indicates a different approach from that adopted by the Ontario Court of Appeal in a similar case earlier this year.² While the Ontario Court of Appeal began with the principle that covenants in restraint of trade are *prima facie* unenforceable and then closely scrutinized the drafting of restrictive covenants founded in the sale of a business, the Supreme Court of Canada presumed them to be lawful requiring interpretation consistent with the intention of the parties and the obligations to which the covenants give rise, unless it is shown they are contrary to public policy. The Supreme Court of Canada's approach should provide commercial parties with comfort on how their agreements will be interpreted and enforced judicially, should this become necessary.

The particular case at issue arose out of the sale of the assets of a crane rental business in Quebec for \$26 million. The partners in that business agreed to both a non-competition and a non-solicitation covenant. The non-competition clause precluded the partners from involvement with another business in the crane rental industry within the province of Quebec for five years from the date on which their employment ceased. The non-solicitation clause operated for the same five year post-termination of employment period and precluded the partners from both soliciting and either doing business or attempting to do business in any manner whatsoever on behalf of a crane rental business with both the customers of the business sold and customers of the purchaser's business. The non-solicitation clause also contained an open-ended non-solicitation of employees and consultants of the business sold and the purchaser's business.

The partners initially were retained as consultants for a six-month transitional period following the closing. Thereafter, one of the partners, Mr. Payette, was employed as operations manager for a further period four years. A few months after his dismissal, Mr. Payette entered into an agreement resolving the termination of his employment. At the time he signed the agreement, Mr. Payette sought and then received approval from his former employer to accept employment in a non-competitive

industry. Approximately, three months later, Mr. Payette actually began employment as operations manager with a competitive crane rental business in Quebec. His former employer quickly obtained an interlocutory injunction until trial requiring compliance with the restrictive covenants that were part of the sale.

At trial, the court dismissed the application for a permanent injunction authorizing Mr. Payette to compete with his former employer. The Quebec Court of Appeal set aside this decision and ordered a permanent injunction requiring compliance with the non-competition and non-solicitation clauses. The Supreme Court of Canada dismissed the appeal and affirmed the decision of the Quebec Court of Appeal.

Important findings from the Supreme Court of Canada's decision include the following:

- The reason why the covenant was entered into is the first step in the analysis to determine whether the covenant is properly linked to a contract for the sale of a business or a contract of employment. In this case, the restrictive covenants properly were viewed within the context of the sale, not employment, because this is the reason why the parties entered into them.
- In a commercial context, a non-competition covenant will be reasonable and lawful, provided it is limited in term, territory and the activities to which it applies are necessary to protect the legitimate interests of the party in whose favour it is granted. To determine validity, factors to be considered include: sale price, nature of the business's activities, the parties experience and expertise, and legal and other professional advice.
- Territorial limitations in non-solicitation clauses are unnecessary and obsolete in the context of the modern economy.

The Supreme Court of Canada's approach is a welcome one for the purchasers of business who seek to protect the value of those businesses following closing and the end of their relationships with the former principals of the vendor.

Footnotes

¹*Payette v. Guay Inc.*, 2013 SCC 45 (CanLII).

²*Martin v. ConCreate USL Limited Partnership*, 2013 ONCA 72 (CanLII).