SMHI LEGAL NOTES
STEINBERG MORTON HOPE & ISRAEL LLP
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Volume 18 Summer 2009

Non-Competition Clauses

Contracts are an everyday part of our lives. A contract may involve something as simple as the purchase of an item at the mall to something as complex as the financial arrangements for a joint venture. As long as the parties to the agreement are not contracting to do something illegal or against public policy, individuals and businesses are free to make the legal arrangements that best suit their needs.

The Restrictive Covenant
It is only in exceptional circumstances that the courts will interfere with a legal agreement. One such exception is when a contract includes an unreasonably restrictive non-competition covenant, which the common law refers to as a covenant in restraint of trade. Employment relationships as well as agreements for the purchase and sale of a business are the most likely contracts to include such restrictive covenants. In the former case, a departing employee will be precluded from competing with the former employer. In the latter, the person selling the business will agree not to compete with the new owner of the business.

In 1894, the British House of Lords concluded that a clause in restraint of trade was contrary to public policy because it interfered with individual liberty of action. They also said that the exercise of trade should be encouraged and should be free. These twin notions continue to be sound public policy in 2009. For these reasons, the law presumes that a restrictive covenant is unenforceable unless it can be shown to be reasonable by the persons seeking to enforce it.

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Reasonable vs Unreasonable
To determine whether a restrictive covenant is reasonable, the terms of the covenant must be unambiguous. The court must be able to clearly determine what the covenant specifically intends.

If the court concludes that a restrictive covenant is unreasonable it will either strike down the covenant altogether or it may in certain circumstances alter the terms of the original contract by applying the doctrine of severance.

Severance
Where severance is possible, the illegal portion of the covenant will be dealt with in one of two ways: "blue-pencil" severance or "notional" severance.

Blue-Pencil Severance
The Supreme Court of Canada has described "blue-pencil" severance as being possible only " if the judge can strike out, by drawing a line through, the portion of the contract they want to remove, leaving the portions that are not tainted by illegality, without affecting the meaning of the part remaining." The parts struck out, however, must be trivial and not part of the main purport of the restrictive covenant.

Notional Severance
In the case of "notional" severance, the court will "read down" the illegal provision. For instance if the parties' contract calls for the payment of an illegal interest rate and it is clear that the parties did not intend anything illegal, the court can read down the interest rate to the legal statutory maximum.

Shafron vs KRG
In a recent Supreme Court of Canada case involving an employment contract, the principles of restraint of trade, restrictive covenants and severance were considered.

The Facts
Morley Shafron owned a Vancouver-based insurance agency business. In 1987, he sold the business to KRG Insurance Brokers Inc. He continued to be employed in the business and entered into a three-year employment contract. The employ-

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ment contract included a non-competition clause indicating that upon leaving his employment for any reason, other than termination without cause by KRG Insurance, he would not be involved directly or indirectly in the insurance business within the *Metropolitan City of Vancouver*. In other words, he would not leave KRG to go and open or work for a competing insurance business.

Every three years, until 2000, the parties continued to enter into a new employment contract, which contained a similar non-competition clause. In January 2001, Morley left KRG and began working for the Shaw Insurance Agency in Richmond, British Columbia. KRG commenced a legal action against Morley claiming he was in breach of the non-competition clause.

The Lower Courts

At trial, the judge dismissed KRG's action partly on the basis that the non-competition clause, specifically the term "*Metropolitan City of Vancouver*," was neither clear nor certain. The judge found that the term was ambiguous because there was no legal or judicial definition of *"Metropolitan City of Vancouver"* and, in any event, the provision was unreasonable.

The BC Court of Appeal agreed that the term "*Metropolitan City of Vancouver*" was ambiguous, however that Court felt it was possible to remedy the ambiguity. The Court applied the doctrine of "notional" severance to construe the term as applying to the City of Vancouver and municipalities contiguous to it, including Richmond. Defining the term in this manner, the Court was able to find the non-competition clause to be reasonable and enforceable.

The Supreme Court of Canada

The highest court in the land disagreed with the BC Court of Appeal and instead found the trial judge's view of the situation to be the correct one.

The Supreme Court of Canada began by stating that the doctrine of "notional" severance could not be used in cases involving a restrictive covenant in an employment contract. In order to apply "notional" severance, it must be obvious what the limits of illegality are, what the courts have referred to as the "bright-line" (i.e. the maximum legal rate of interest of 60% per year) and it must also be clear that the parties did not intend to cross that line.

In the case of a restrictive covenant, attempting to apply "notional" severance would amount to the court rewriting the covenant in a manner that it, and not the parties, subjectively considers reasonable. There is typically no such "brightline" when considering the reasonableness of the temporal or geographic limits of a non-competition clause. Therefore, it cannot be used in such cases.

In addition, if "notional" severance were used, some employers could impose an unreasonable restrictive covenant on the employee. The only negative to the employer in such a case would be that if the covenant was found to be unreasonable, the court would rewrite it.

The Court next considered whether "blue-pencil" severance could be applied. Based on the evidence presented at trial, the Court could find no evidence that Morley and KRG would have unquestionably agreed to remove the word "Metropolitan" without varying any other terms of the contract or otherwise changing the bargain. In other words, there was no evidence that it was merely a "trivial" addition to the clause. Therefore, "blue-pencil" severance could not be used to the correct the ambiguity.

Its arguments for severance being unsuccessful, KRG next suggested that the Court was in a position to rectify what it referred to as a mistaken description. Rectification will be used to restore what the parties' agreement actually was, were it not for the error in the written agreement. In this particular case, there was no evidence to indicate that the parties had ever agreed to a specific geographic area but mistakenly written down "Metropolitan". Therefore, this argument was not accepted either.

The end result was that because the non-competition clause was ambiguous and unreasonable, KRG could not rely on it to restrict Morley's current activities.

The Lessons

When entering into a contract it is important that the language used is clear and unambiguous. Any significant terms should have an accepted legal meaning or one should be spelled out. These lessons are particularly important when drafting restrictive covenants, since the general rule is that a restrictive covenant will not be upheld if it is unreasonable.

Our firm works in all areas of corporate commercial law. We would be pleased to assist you with your particular legal situation.

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The Best Interests of the Children are Paramount

Child custody cases are some of the most difficult cases the family court must deal with. When parents are unable to adequately decide on custody and access issues, the court will step in to decide on the arrangements.

In Ontario, custody issues are governed by either the Federal *Divorce Act* or the Provincial *Children's Law Reform Act*, depending on the circumstances. If the child, who is the subject of a custody case, is a child of marriage and the parents have begun divorce proceedings, the court looks to the *Divorce Act*. In all other situations (unmarried parents, separating parents who have not started divorce proceedings and third party applicants) the court relies on the *Children's Law Reform Act*. In both instances, the law is clear that the test for making decisions regarding custody and access is the *best interests of the child*.

While neither statute defines the test, both provide a list of criteria which should be taken into consideration in custody cases.

The *Divorce Act* states that the best interests of the child are to be "determined by reference to the conditions, means, needs and other circumstances of the child."

The *Children's Law Reform Act* directs the court to consider all the needs and circumstances of the child, including the following factors.

1. The child's relationship, including love, affection and emotional ties, with the person(s) applying for custody as well as the relationship with the extended family and those people the child will come into regular contract with, such as the applicant's new partner.

2. If they can be adequately determined, the court will be interested in the views and preferences of the child. However, it is not appropriate for young children to bear the onus of making custody decisions.

3. If, at the time of the application, the child has been living in a stable environment, that meets his or her needs, the court will be reluctant to disturb the status quo.

4. The applicant's ability and willingness to provide guidance, education, necessaries of life, as well as any special needs of the child are all important facts. In addition, the court wants to assure itself that the custodial parent will promote a relationship between the child and the non-custodial parent.

5. The court is also interested in the plans for the child's care and upbringing as proposed by the applicant.

6. The permanence and stability of the applicant's family unit is another important consideration since it is the court's desire to keep further upheaval in the child's life to a minimum.

7. Although blood ties are not as important as they once were, they remain a factor to be taken into account.

The answer to what is in the best interests of the children can be particularly difficult in cases involving allegations of parental alienation.

According to Professor Nicholas Bala, parental alienation may involve emotionally abusive "pathological alienation," caused by the conduct of an alienating parent and resulting in a child having negative beliefs and feelings that are not consistent with the child's actual experience with the rejected parent. In other cases, the child may be "justifiably estranged" due to conduct of the rejected parent, such as abuse or poor parenting.

In a case decided earlier this year, the court had to rule on possible parental alienation in conjunction with a non-custodial father's application for sole custody of his daughters, ages 14, 11 and 9. The parties' relationship had been a difficult one from the start and ultimately ended in divorce. Despite the father's desire and willingness to be involved in his children's lives, the mother began putting up roadblocks immediately following the birth of the first child. At no time did she ever encourage the children to have a relationship with their father, even when all were living under the same roof. He was not allowed to be alone with the children, and in fact the mother began to leave the children with her parents.

Following the parties' separation the mother often refused the father access, even when court ordered. By the time the oldest daughter was 6, she refused to speak to her father. Although the two younger children were initially affectionate, they worried that their mother might find out. At one point the mother began to regularly call the police to make the exchange for the father's access. She also moved with the children on a regular basis so to get further and further away from the father.

The court concluded that the three girls had been alienated from their father over a long period because the mother was unable to accept that it was in their best interests to have a relationship with him. The court went on to find that the mother's unrelenting behaviour toward the children was tantamount to emotional abuse. As a result of her behaviour, the wish of the two older children, that they stay with their mother, was found not to be their own and therefore were not taken into account. For these reasons, the best interests of the children

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Changes Are Coming

Several years ago, the McGuinty government asked former Associate Chief Justice Coulter Osborne to head up the *Civil Justice Reform Project*. Mr. Justice Osborne's mandate was to review and recommend ways to make the civil justice system more accessible and affordable for Ontarians.

Mr. Justice Osborne made recommendations for changes in a number of areas, including:

- Judicial resources
- Small claims court
- Unrepresented litigants
- Discovery
- Trial management
- Costs of litigation

Based on Mr. Justice Osborne's recommendations, input from various members of the legal community and from the public, the government has agreed to implement a number of major reforms to the rules of Ontario's civil courts. These changes, which take effect on January 1, 2010, include:

- The monetary jurisdiction of the Small Claims Court being increased from $10,000 to $25,000.
- The Simplified Procedure Rules being available for cases with a monetary limit of $100,000, double the previous limit.
- Within the Simplified Procedure, each party will be allowed up to two hours of pre-trial oral discovery. In regular procedure, each party will be limited to a total of seven hours of pre-trial Examination for Discovery, unless the parties consent or the court orders otherwise.
- The new rules are designed to encourage parties to bring motions for summary judgement, since it will now be less likely that costs will be awarded against the party that loses the motion.
- The civil courts will be subject to the general principle of proportionality, meaning the time and expense devoted to any case must reflect what is at stake in the proceedings.

As the January 1st deadline approaches, more information about the changes will become available.

Buying a Cottage

Although the economy is in some difficulty, if you are in the market for a cottage there are deals to be had.

Buying a cottage is different from buying a house. There are issues that may arise in the context of buying a cottage that are rarely seen with a residential home, including: the description of the land; access to the land; drinking water; septic system and zoning.

When buying a cottage, it is important to have a lawyer review the agreement of purchase and sale before it is signed. Our firm works in this area of real estate. We would be pleased to assist you.

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required an order for the father to have sole custody. In addition, the mother was to have no access to the children save and except for the purpose of court ordered counselling.

While this result may seem harsh, this case demonstrates that in decisions involving children, the court's only concern is to determine the living and access arrangements that will be in the child's best interests.

Steinberg Morton Hope & Israel LLP

5255 Yonge Street - Suite 1100
Toronto, Ontario M2N 6P4

T: 416 225-2777 F: 416 225-7112
www.smhilaw.com

LAWYERS

Irwin Steinberg
isteinberg@smhilaw.com

James C. Morton
jmorton@smhilaw.com

Jack W. Hope
jhope@smhilaw.com

David M. Israel
disrael@smhilaw.com

Michael E. Cass
mcass@smhilaw.com

M. Michael Title
mtitle@smhilaw.com

Shelley Brian Brown
sbrown@smhilaw.com

Taras Kulish
tkulish@smhilaw.com

Antonin I. Pribetic
apribetic@smhilaw.com

David A. Brooker
dbrooker@smhilaw.com

Corey D. Steinberg
csteinberg@smhilaw.com

Haleh Soltani
hsoltani@smhilaw.com

Olga Kanevsky
okanevsky@smhilaw.com

Victor A. Nikitine
vnikitine@smhilaw.com

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