ALBERTA COURT OF APPEAL USES BLUE PENCIL TO SAVE NON-COMPETE

Posted on September 5, 2020

Categories: Insights, Publications

In *City Wide Towing and Recovery Service Ltd v Poole*,[1] a majority of Alberta's Court of Appeal applied a seldom-used legal doctrine in order to save a non-competition covenant from being struck down.

Background

The employee, Devon Poole, was the former owner of Capital Towing, a vehicle towing business operating in and around Edmonton, Alberta. In 2017, he sold the assets of Capital Towing to City Wide Towing and Recovery Service Ltd. ("**City Wide**") for $700,000, though $35,000 was conditional on Mr. Poole remaining employed with City Wide for a fixed-term of two years.

In connection with the sale, Mr. Poole entered into a Non-Competition Agreement that prohibited him from competing with City Wide for a period of five years (from the date of the sale) in British Columbia, Alberta, Saskatchewan or any other location within Canada where City Wide and its affiliates carried on business.

In 2018, Mr. Poole resigned from his employment with City Wide in order to take up employment with an alleged competitor, DRM Recovery Ltd. ("**DRM**"). Shortly thereafter, City Wide brought an action against Mr. Poole and DRM for breach of the Non-Competition Agreement, among other things. City Wide also brought an application for an interim injunction, which was granted by the chambers judge. Mr. Poole and DRM subsequently appealed the chambers judge's decision to the Court of Appeal.

Court of Appeal's Decision

On appeal, Mr. Poole and DRM argued that the restricted covenants were unenforceable as overbroad and in restraint of trade. In particular, they argued that the non-competition covenant should have been limited to the territory where Capital Towing carried on business at the time of the sale, i.e., in and around Edmonton. In their view, the non-competition covenant was overbroad because Capital Towing was not conducting business outside of Alberta at the time of the sale.

The Court of Appeal agreed with Mr. Poole and DRM that when a restricted covenant is entered into in connection with a commercial transaction, the reasonableness of the covenant must be judged with reference

to the scope of the business sold rather than the business of the purchaser. In this case, the chambers judge had erred by analyzing the geographic scope of the non-competition covenant with reference to the business of the purchaser (i.e., City Wide and its affiliates) as opposed to the business sold (i.e., Capital Towing).

Because Capital Towing was not conducting business in British Columbia, Saskatchewan or any other location within Canada (outside of Alberta) at the time of the sale, the Court of Appeal held that the non-competition covenant was geographically overbroad and therefore unreasonable.

However, this did not end the analysis. City Wide argued that if the non-competition covenant was geographically overbroad, the covenant could be read down or "blue penciled" by the court in order to delete references to British Columbia, Saskatchewan and "any other location within Canada". City Wide relied on the following clause in the Non-Competition Agreement in order to give the Court of Appeal the power to read the covenant down:

[S]hould a court determine that any provision or portion of any provision of this Agreement is not reasonable or valid, the parties hereto agree that such provision should be interpreted and enforced to the maximum extent which the court deems reasonable or valid and the parties agree to request that the court apply notional severance to give effect to the restrictions in this Agreement to the fullest extent deemed reasonable or valid by the court. In particular, if such court determines that the duration of the Non-Disclosure Period and/or the Restriction Period and/or the scope of the Non-Compete Area is unreasonable, the parties agree to reduce such duration and/or scope to such extent as may be necessary to ensure that the covenants in this Agreement are reasonable in the circumstances, as determined by the court.

A majority of the Court of Appeal agreed with City Wide. It its view, the non-competition covenant should be read down in order to make it reasonable (rather than striking down the entire covenant simply because part of it was overbroad). In the result, the majority held that the non-competition covenant remained enforceable to the extent that it applied to Alberta only.

Takeaways for Employers

The Canadian courts have consistently afforded greater latitude to non-competition covenants negotiated in the context of a commercial transaction.[2] However, the courts have traditionally resisted blue penciling such covenants on the basis that the parties drafting a contract have an obligation to ensure that restricted covenants are no wider than is reasonable. Parties should not be encouraged to draft the widest possible restrictive covenant, and then rely on the courts to revise the covenant so as to make it reasonable.

For employers, the majority's approach in *City Wide Towing and Recovery Service Ltd v Poole* is a pragmatic and welcome departure from the traditional approach. However, the majority was careful to note that their

analysis only applied to covenants negotiated between sellers and purchasers in commercial transactions. In this regard, the majority confirmed that courts "should not come to the assistance of an employer who has drafted an overly broad restrictive covenant" in light of the inherent power imbalance that exists between employer and employee.

by Paul Boshyk and Gordana Ivanovic

[1] 2020 ABCA 305.[ps2id id='1' target='/]
[2] Payette v Guay Inc., 2013 SCC 45.[ps2id id='2' target='/]

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.