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Non-Competition Agreements and Restraint of Trade

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Generally speaking, contracts that restrain trade (sometimes known as non-competition clauses) are, *prima facie*, void on the grounds of public policy but courts have long recognised the competing interests of those who wish to uphold contracts freely entered into by parties of equal bargaining power and society's interest in preventing contracts that unduly restrict the free market and create monopolies.¹

Like all areas of the law, courts have attempted to balance these competing interests by requiring that restrictive covenants be reasonable to the parties and reasonable with respect to the interests of the public. These clauses must adequately protect the person who grants the covenant and must be in no way injurious to the public.²

In *Tank Lining Corp. v. Dunlop Industries Ltd*, the Ontario Court of Appeal outlined a convenient test to determine the legitimacy of restrictive covenants:

Is the covenant under review in restraint of trade?

Is the restraint one which is against public policy and, therefore, void? It must fall within recognised exceptions such as restraints attached to mortgages or leases of real property; otherwise it is void.

Can the restraint be justified as reasonable in the interests of the parties?

Can it also be justified as reasonable with reference to the interests of the public?³

It has been held that there is no restriction of trade where the covenant only ties the parties during the continuance of the contract and where any negative ties are incidental and normal to the positive commercial arrangements of the parties.⁴

The person seeking to uphold a non-competition agreement must demonstrate that the

¹ *Burnside & Co. Law v Holmes*, 2003 CarswellMan 338 at para. 12 (Man. Q.B.) online: Westlaw-eCarswell <<http://www.ecarswell.westlaw.com>> and *Winnipeg Livestock Sales Ltd. v. Plewman* (2001), 192 D.L.R. (4th) 525 at para. 15.

² *Nordenfelt v. Maxim Nordenfelt Guns & Ammunition Co.*, [1894] A.C. 535 at 565, Macnaghten L.J. (H.L.). This reasoning was adopted by the Supreme Court of Canada when they analysed an employment related restrictive covenant. See *Elsley v. J.G. Collins Ins. Agencies Ltd.*, [1978] 2 S.C.R. 916 at 925.

³ *Tank Lining Corp. v. Dunlop Industries Ltd.* (1982), 140 D.L.R. (3d) 659 at para 13(Ont. C.A.)[hereinafter "*Tank*"].

⁴ *Esso Petroleum Co. v. Harper's Garage (Stourport) Ltd.*, [1968] A. C. 269 at 328 (H.L.).

covenant is reasonable as between the parties. The party seeking to attack the covenant must show that it is not reasonably in the public interest.⁵ It is also important to remember that all questions of reasonableness are determined in each case after considering the facts.⁶ There are no hard and fast rules.

To be unreasonable to the parties, the covenant's restrictions must be more than adequate to protect the enforcer's interests. Courts are loath to overturn business contracts entered into freely where both parties are of equal bargaining power.⁷ Inversely, courts are more quick to overturn restrictive covenants in employment contracts because of the obvious power differential.⁸ The covenant's geographical and temporal limitations are not overly broad and reasonably attempt to protect the interest of the contract's enforcer. Similarly, restrictive covenants in shopping malls that prohibit overlapping spheres of business are enforceable⁹ in order to create a community of interest that furthers the business of all the parties.

The public interest step is more nebulous. Any restrictive covenant that injures the public in some way, particularly those that breach the *Competition Act*,¹⁰ may be contrary to the public interest.¹¹ Restraint, by itself, is not necessarily bad. Business people should be allowed to contract relatively freely. The Court in *Tank* suggested that "[t]he cessation of business might, for example, deprive the nation or a region of an essential industry, an important source of wealth and employment or vital technology" would be a violation of the public interest.¹² It includes economic or social effects but should not be limited to them.

⁵ *Tank*, *supra* note 3 at para. 18.

⁶ *Doerner et al. v. Bliss & Laughlin Industries Inc. et al.*, [1980] 2 S.C.R. 865 at 873.

⁷ *Tank*, *supra* note 3 at para. 20.

⁸ *Button v. Jones*, 2001 Carswell Ont 1785 at para. 10 (Ont. S.C.J.) online: Westlaw-eCarswell <<http://www.ecarswell.westlaw.com>>

⁹ *Spike v. Rocca Group Ltd.* (1980), 23 Nfld & P.E.I.R. 493 (P.E.I.S.C.).

¹⁰ R.S.C 1985, c. C-34.

¹¹ *Tank*, *supra* note 3 at para 40.

¹² *Ibid.*, at para. 46.