Is Your Business Protected When Employees Leave?

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One of your top-producing employees leaves your organization and, while you're naturally worried about finding a good replacement, the non-competition agreement he or she signed means you won't have to worry about the ex-employee taking business from you.

Or will you? Unless the non-competition or non-solicitation agreement was carefully drafted with the employee's role in mind, there's a good chance the agreement is unenforceable and that your business may be more vulnerable than you think.

Recent case brings clarity

A recent Ontario Court of Appeal decision H.L. Staebler v. Allan 2008 ONCA 576 brings some important clarity to the law regarding non-solicitation and non-competition agreements for departing employees. Here is what happened in that case.

Two employees worked for H. L. Staebler Company Limited selling commercial insurance. On October 15, 2003, the employees resigned and immediately began working in a similar capacity for a competitor. Both employees had written employment contracts with Staebler, which contained a non-competition clause.
Within two weeks of their departure, approximately 118 clients had moved their business from Staebler to the new employer. Staebler sued the employees for, among other things, breach of the non-competition clause. The employees' new employer was also named as a defendant.

The non-competition clause in question read as follows:

"In the event of termination of your employment with the Company, you undertake that you will not, for a period of 2 consecutive years following such termination, conduct business with any clients or customers of H.L. Staebler Company Limited that were handled or serviced by you at the date of your termination."

While the trial judge found this non-competition clause to be enforceable and awarded Staebler $2 million in damages the Court of Appeal disagreed and overturned the decision and the awarding of damages.

Focus on non-solicitation, not non-competition

The Court of Appeal stated that a non-competition agreement will only be enforceable in exceptional circumstances and that none of these exceptional circumstances arose in the Staebler case. Even though this particular clause was limited to conducting business with clients or customers, the court still found this to be a non-competition agreement, and not a non-solicitation agreement, as the clause referred broadly to "conducting business" not "soliciting business".

In this case, the court found the non-competition clause unreasonable in several respects.

 Too wide a scope. The clause contained no geographic limit on the activities it sought to restrict. The employees would be

restrained from doing business with their former clients “even if they relocated to the far reaches of Ontario or, for that matter, elsewhere in Canada.”

 No limit on type of business. The clause did not in any way restrict the type of business that could be done, including work that in no way competed with Staebler. The court found that the absence of a geographical limit combined with a blanket prohibition on “conducting business” rendered the non-competition clause overbroad and unenforceable.

 Less intrusive means available. The court found that a less intrusive client non-solicitation clause would have adequately protected the employer’s interests in this case for a number of reasons.

First, there was an imbalance in bargaining power between the employees and Staebler when the employment contracts were negotiated. Second, the employees were commercial insurance salespeople not managers, directors or key employees and did not owe a fiduciary duty to Staebler. Finally, it was the industry norm for salespeople to have close relationships with their clients, and these relationships were not exclusive as other Staebler employees served the clients in various capacities.

All of these factors favoured a non-solicitation agreement instead of a non-competition agreement. In fact, Staebler had different agreements with other salespeople in which salespeople could solicit clients and customers and conduct business with Staebler clients so long as they did so outside of a 50-mile radius of the Waterloo region.

Make sure you’re protected

With the many restrictions that courts place on enforcing non-solicitation and non-competition clauses, it’s essential for organizations to move beyond boilerplate language in their employment contracts as a means of protecting their interests. If your business is potentially vulnerable from the departure of one or more key employees, be sure to get the legal advice you need to ensure your interests are properly protected and that any contract language is enforceable.

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