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Feature

Restrictive Covenants in the Commercial Context

Alberta Court of Appeal uses blue pencil to save non-compete

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A recent decision by the Alberta Court of Appeal, *City Wide Towing and Recovery Service Ltd. v. Poole*, 2020 ABCA 305, revisits whether a court can sever or restrict overly-broad provisions within restrictive covenants (known as "notional" severance and "blue-pencil" severance) in order to save them. This case also holds that the doctrine of severance has broader application in the commercial setting than the employment setting.

At issue in this case was the enforceability of a non-competition clause agreed to by Devon Poole as part of the sale of his business, Capital Towing ("Capital"), to City Wide Towing and Recovery Service Ltd. ("City Wide"). After the sale closed, Poole resigned from City Wide's employ and began employment with DRM Recovery Ltd.("DRM"), an alleged competitor of City Wide. This prompted City Wide to bring an action and application for injunction against Poole and DRM for breach of the restrictions in the commercial agreement that Poole entered into as part of the commercial sale.

The Chambers Judge granted the injunction application and issued an order (the "Order"), which was the subject of the appeal before the Court of Appeal. The Court of Appeal held that the analysis of the Chamber Judge leading to the Order was incorrect:

> In the present case, the chambers judge analyzed the geographical scope of the non-competition agreement by looking not at the activities of the business sold by Poole (i.e., Capital), but rather the business of City Wide. In concluding the geographical scope was reasonable, she noted that City Wide "had customers or carried on business in the particular provinces" and "had stated an intention to expand and develop the businesses in those provinces": AR, F4/36-38. This was the wrong focus. The chambers judge should instead have determined the area in which Capital carried on business at the time it was sold by Poole to City Wide.

The central question on appeal was thus whether a restrictive covenant that is entered into as part of the sale of a business, and which is *prima facie* unenforceable as overbroad in geographical scope, may be saved by severing the overbreadth from the rest of the agreement. The majority of the Court of Appeal answered the question in the affirmative. In doing so, the majority distinguished the rigorous application of the doctrine of severability in the employment context (e.g., in employment agreements) from that of the commercial context (e.g., in sale business agreements). Typically in an employment agreement, an overbroad restrictive covenant will be wholly unenforceable rather than narrowed in scope.

The Court's application of severance resulted in the majority amending the non-compete area in the Order to apply only to Alberta instead of Alberta, British Columbia, and Saskatchewan (as originally drafted). The majority of the Court said:

> We conclude that Shafron does not speak to blue pencil severance of restrictive covenants in commercial contracts and therefore does not preclude its application in the present case. Moreover, blue pencil severance is supported in this case by the English authorities, ACS Public Sector, and a number of decisions of first instance, including Sterling Fence Co. Ltd. v Steelguard Fence Ltd., 1992 CarswellBC 1771

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(BCSC); Restauronics Services Ltd. v Forster, 2001 BCSC 922, rev'd in part on other grounds in 2004 BCCA 130; and GDL Solutions Inc. v Walker, 2012 ONSC 4378.

Writing in dissent about the policy concerns arising from the majority's decision, Justice Slatter referenced the Supreme Court of Canada decision in *Shafron*, in which the Court's concern that permitting severance is an invitation to employers to draft overly broad restrictive covenants with the prospect that the court will only sever the unreasonable parts or read down the covenant to what the court considers reasonable. It bears repeating that the majority held that *Shafron* was inapplicable to commercial contracts.

This decision serves as a cautionary reminder that employers should carefully review and draft employment-related restrictive covenants to protect legitimate interests. It is also a helpful authority to provide greater latitude when enforcing restrictive covenants in the commercial setting where the court will more readily accept there is a balance of power between the parties (and less reason for judicial intervention).

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