NON-COMPETITION CLAUSE: LESS IS BETTER THAN MORE

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In a recent judgement of the Superior Court of the province of Quebec, district of Montreal, bearing number 500-05-056150-004, dated July 12, 2001, Honorable Justice Pierre J. Dalphond refused to issue an order of permanent injunction against nVidia Corporation and one of its employees, Mr. Dany Lepage, for what the Plaintiffs, Graphiques Matrox Inc. and Systèmes Électroniques Matrox Ltée, considered to be unfair competition practices. The two Plaintiffs (Matrox Group) are two Canadian companies located in Montreal. They specialise in the conception, development and sale of digital technologies. nVidia is a Delaware company having its principal place of business in Santa Clara, California. It operates a business in direct competition with the Matrox Group.

The case on the merits raises many issues, but one is of particular interest for the purpose of this article. Matrox Group claimed that nVidia was inducing its management level employees to terminate their employment contract and was using confidential information which belonged to the Matrox Group with the intention to disrupt their business.

An interim injunction had been issued enjoining nVidia, its agents, directors, officers and employees not to induce or encourage, directly or indirectly, any employees of Matrox Graphics Inc. or of Systèmes Électroniques Matrox Ltée or former employees to breach any of their obligations under their confidentiality and/or non-competition agreements with Matrox Graphics Inc. or Systèmes Électroniques Matrox Ltée. The court had refused to enjoin nVidia from soliciting any employee or ex-employee of the Plaintiffs, even though the court was specifically requested to issue an order in that regard.

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The court on the merits found that there was no doubt that in our society, where freedom of speech, including commercial speech, is constitutionally protected and where competition is seen as a garanty of economic and social progress, any employer looking for manpower has the right to speak of the job opportunities it can offer, including in newspapers, radio and TV medias and on the Internet. An employer looking for candidates can also at informal or formal meetings show an interest for a given person, even if this person has a job with a third party. It can also make telephone calls to any person that it considers qualified, even if this person works for somebody else or to use the services of "head-hunters" to do so.

Whether the solicitation by an employer is done at large or individually, it does not have to be channelled towards persons not having a job for the solicitation to be legal. There is also no doubt that an employer who is looking for new employees has the right to consider all the offers received in answer to its solicitations, including those offers coming from employees already working for another employer. To forbid the consideration of candidates already having an employment would limit the possible mobility of employees and would appear to be against public order.

The court considered that the non-competition agreement, if it exists and if it is valid, only binds the parties that have signed it and not third parties. A third party however cannot induce an employee to breach his obligations under an employment contract. An order in that regard could only have been issued if the court considered that nVidia induced and encouraged the employees of the Plaintiffs to breach valid non-competition undertakings.

The existence of a valid non-competition clause is essential to any conclusion to the effect that a third party has participated in a breach of contract, before a court can issue a permanent injunction in that regard. Such an exercise can only be made on an individual basis. No order can be issued at large.

Non-competition undertakings, even though consented to freely by the parties to an agreement, have always been subject to the judicial control under the Common Law of Great Britain and Canada, based on the fact that public order favours free competition, freedom of business or freedom of employment. Courts will refuse to give effect to such clauses when they are unreasonable under the circumstances. The will of the parties is therefore not sovereign in such matters. The civil law of the province of Quebec recognises expressly that contracts cannot be contrary to public order (article 1411, Civil Code of Quebec) and the economic framework of Quebec is the same as in the rest of Canada and similar as the one prevailing in the United Kingdom; therefore, the courts applying the Quebec civil law have not hesitated to

refer to British jurisprudence when asked to decide as to the validity of non-competition clauses.

Non-competition clauses can be found in many different types of contracts: sale of a business agreements, transfer of shares agreements, franchise agreements, distribution agreements, partnership agreements, employment contracts, etc.. Even if the concepts applied in these different types of contracts are similar, it is well established that the attitude of the courts will vary according to the nature of the contract where the restriction lies. In an employment contract, if the non-competition clause is for an indefinite period of time, the clause will be considered as restricting the freedom of employment and the mobility of the employee, it will therefor be considered as restricting unduly the freedom of the person.

In the province of Quebec, article 2089 of the Civil Code states the following:

> "The parties may stipulate in writing and in express terms that, even after the termination of the contract, the employee may neither compete with his employer nor participate in any capacity whatsoever in an enterprise which would then compete with him.
>
> Such a stipulation shall be limited, however, as to time, place and type of employment, to whatever is necessary for the protection of the legitimate interests of the employer.
>
> The burden of proof that the stipulation is valid is on the employer."

It follows from this article that there are conditions of form which need to be met: the necessity of a written agreement that must specifically deal with non-competition; the stipulation needs to be limited as to time, place and type of employment. There are also conditions of substance which need to be met: the non-competition clause must be necessary for the protection of the legitimate interests of the employer. The burden of proving that a non-competition clause is valid is transferred to the employer.

Article 2089 came into force with the new Civil Code in 1994. The jurisprudence prior to that date has to be considered with caution. Prior to 1994, the employee had the burden of proving the invalidity of the non-competition clause.

This process is similar to the one applicable under the Canadian Charter of Rights and the Quebec Charter of Rights, wherein the burden of proof lies with the party seeking to maintain a restriction of rights to demonstrate that

the restriction is reasonable and justified under the circumstances. A non-competition clause in an employment contract is a restriction of personal freedom.

The court went on to analyse the non-competition obligations imposed on the Defendant Lepage. The court found that, as far as the conditions of form were concerned, these had not been satisfied since the restrictions as to the type of work were too broad, the territory was not expressly described and the duration was ambiguous, because it made reference to different durations letting the court to decide which duration it considered reasonable under the circumstances.

As for the substantive conditions, the Court held that the only legitimate interest of the employer which was alleged was the protection of its trade secrets. Is the protection of trade secrets sufficient to justify the prohibition to work for a competitor? The Plaintiffs suggest that it is, since the employment of one of its ex-employees implies inevitably the disclosure of trade secrets. The Court was not impressed by this argument. With respect to Mr. Lepage, no proof was made of an inevitable risk of disclosure of trade secrets following his employment by nVidia.

The evidence revealed that the manufacturers of personal computers want new products on the market place approximately every six months and that their suppliers, such as nVidia or the Plaintiffs, constantly need to improve the solutions they offer. The Plaintiffs, in their own statement of claim, state that the product life cycle is short and is likely to remain short and that the timely research and development of new products is therefore essential; success depends on large part on achieving "design win", which entails having existing and future products chosen by personal computers OEMs.

According to the court, a prohibition to work for nVidia for a period of eighteen months or even twelve months seemed excessive under the circumstances. The court also found excessive the fact that the clause would apply whatever were the reasons for the termination of the employment contract, which would include dismissal due to lack of work with the Plaintiffs or the abandonment of the project on which the employee was working. The court found even more excessive the prohibition to work for nVidia even in areas where nVidia is not in competition with the Plaintiffs.

In such circumstances, the non-competition clause was declared null because it was imprecise with respect to its length, too broad with respect to the prohibited activities and unreasonable with respect to the interests which the Plaintiffs could legitimately protect. Such a declaration did not leave the Plaintiffs without any protection. The obligations of loyalty under the Civil

Code still apply and could be sufficient to adequately protect the legitimate interests of the Plaintiffs relating to trade secrets.

This is one of the first cases decided under new Article 2089 of the Civil Code of Quebec, where the shift of the burden of proof on the shoulders of the employer has worked in favour of the employee. Employers wishing to impose non-competition obligations on their employees once they terminate their employment must be careful in the drafting of the non-competition clause. By imposing obligations which are too broad or not precisely defined, the employer may find itself with a clause which is invalid. The court will not rewrite the clause. It will only declare it invalid. It is therefore recommended to have a non-competition clause which focuses on the important and essential aspects of what the employer wishes to protect. It is better to aim for less and have a valid non-competition clause that to aim for more and be caught with a clause which is invalid.