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Restraint of Trade Clause: Safety or Complacency

A restraint of trade clause is a contractual provision often used in employment agreements. Its purpose is to restrict an employee from engaging in a similar business or profession that would compete with your company, for a specific period of time and/or within a specific geographical area after the contract ends.

The fundamental tension with this clause is that it operates as an exception to the public policy that favours open competition and an individual's right to work. For a restraint of trade clause to be enforceable, it must be reasonable and protect a legitimate business interest. Our courts apply a public policy test that balances an employer's right to protect its business against an employee's constitutional right to choose a trade and earn a living.

The Legal Tension

The law generally favours competition and disfavors restrictions on a person's ability to earn a living. A restraint of trade clause is, by its very nature, a restriction on these freedoms.

The validity of a restraint clause has to be weighed against two competing public policy considerations:

- The principle of sanctity of contract: Agreements freely entered into must be honoured.
- The right to freedom of trade: Section 22 of the Constitution guarantees every citizen the right to choose their trade, occupation, or profession freely.

The starting point is that restraints of trade are *prima facie* unenforceable because they are contrary to section 22. The employer bears the onus of proving that the restraint is reasonable (sensible and necessary) and therefore enforceable.



The Validity Test

For a restraint to be valid and be enforced, the employer must prove three things:

1. **A Legitimate Protectable Interest:** The employer must have a real commercial interest worth protecting, such as trade secrets, confidential information (e.g. customer lists, pricing strategies).
2. **Reasonable Scope:** The restriction must not be broad, with respect to three specific elements:
 - o Duration (Time): 6-12 months is often reasonable for mid-level to senior employees, while 24 months or more is usually considered unreasonable. A shorter period (3-6 months) is acceptable in most cases.
 - o Geographic Area: The restricted area must be limited to the territory where the employer actually does business and the employee worked. A national restriction for a business operating only in one province is generally unenforceable.
 - o **Scope of Activity:** The restraint must be specific. It should only prevent the employee from working for direct competitors or soliciting specific clients, not from working in their entire industry or profession.
3. **Not Contrary to the Public Interest:** The restraint must not harm the public by eliminating healthy competition and an employee's constitutional right to choose a trade and earn a living.

The protectable interest and scope of the restraint must be specified, a vague clause will automatically fail and cannot be validated by a court (*contra proferentem* rule).

Where the scope would necessarily prohibit the employee from earning an income, the employer's protectable interest is deemed secondary to the employees right to earn a living.

Key Elements for Enforceability

To be enforceable, a restraint of trade clause must be reasonable in 3 areas:

Element	Description	Unreasonable
Duration	The period of the restriction. Reasonable depends on the industry/seniority level/access to information. (e.g. tech industry, 6-12 months is reasonable; manufacturing, 2 years might be acceptable).	A 5-year non-compete for a hairdresser or a 3-year non-compete for a software developer.
Geographic Scope	The physical area where the restriction applies. This should be limited to the area where the employer actually does business or where the employee worked.	A nationwide or province restriction for a sales representative whose territory was only a single city.



Element	Description	Unreasonable
Activity Scope	The type of work or business that is prohibited. It should be limited to direct competitors and the specific role the employee performed.	A clause that prohibits an employee from working in "any capacity" (from CEO to receptionist) for "any company that repairs cars", rather than a direct competitor in the same specialised field.

With each of these elements, the employer must show:

- **Legitimate Interest:** Does the employer have a valid reason to protect its business for - that period, in that specific area, from that activity/knowledge?
- **Proportionality:** Is the duration, geographic area, and activity restriction necessary to protect that interest (no alternative/less restrictive means to achieve the same result)?
- **The Employee's Hardship:** The court will balance the employer's need against the employee's constitutional right to choose their trade and earn a living. If enforcing the restraint would make the employee economically inactive or unproductive, it may be deemed unreasonable.
- **Seniority and Role:** A reasonable restraint is much more likely to be enforceable against: a skilled expert with product design knowledge; senior executive with valuable strategic information or a key account manager with significant customer relationships, than against a junior employee with minimal autonomy or client access.

Here, substance over form is the determining factor. What matters is whether the knowledge and insight gained in a role could realistically be used to help a competitor.

Legitimate Interests an Employer Can Protect

- **Trade Secrets & Exclusive Information:** Proprietary processes, customer lists, pricing strategies, and secret formulas (e.g. the Coca-Cola recipe).
- **Confidential Business Information:** Information that is not a legally protected "trade secret" (e.g. patent) but is still valuable, not generally known in the industry, compiled or created by the company (e.g. sales strategy, client profile analysis).
- **Goodwill & Customer Relationships:** Longstanding customer relationships that can be considered partners or high value clients that the company has built over time.

When an employer seeks to enforce a restraint clause, they don't have to prove the information was a trade secret or exclusive; they just have to prove it was confidential business information that was compiled or created, that gives them a competitive advantage.

Substance over form is the determining factor. What matters is whether the knowledge, insight or relationship could realistically be used to help a competitor who would not ordinarily have access to it.



Categories of Employees

Restraint of trade clauses are not applied to all employees, an employee's role and knowledge must pose a genuine risk to the employer's legitimate business interests. Employers cannot use restraints simply to eliminate fair competition or to stop an employee from using their general skills and experience.

A restraint is most likely to be justified for employees who fall into the following categories:

Employee Category	Why	Practical Example
Access to Trade Secrets or Confidential Information	These employees know information that is proprietary to the business and gives it a competitive edge, e.g. pricing models, marketing strategies, supplier arrangements, or software code.	A technological expert at an outdoor advertising company restrained from sharing sensitive information that could allow a competitor to undercut pricing.
Key Account Managers & Sales Staff with Strong Customer Relationships	These employees build deep, personal relationships with clients. The goodwill the employer has invested in these relationships is what is protected by recognising that clients might follow the employee to a new job.	A Key Account Manager for a major retailer restrained because they were the primary point of contact for high-value clients.
Senior Executives and Strategic Staff	Individuals in senior roles are exposed to the company's long-term strategy, future plans, and non-public commercial data. Their knowledge goes beyond general skills and is considered a protectable interest.	A senior executive in telecoms restrained from joining a competitor because they had insight into commercially sensitive strategy deemed to have lasting value.

The question is not their job title, but the risk they pose. If the employee has access to valuable confidential information or holds the keys to valuable client relationships, a restraint of trade clause is a legal mechanism to protect your company's legitimate interests.

An appropriate alternative for senior and strategic personnel is garden leave. This clause allows an employer to send an employee home during their notice period while keeping them on payroll. The notice period varies and can be up to 6 months for senior executives. The employee remains an employee, receives their full salary and benefits, and must remain contactable and available to the employer, but they do not perform their regular duties.

By paying the employee to stay at home during their notice period, the employer effectively removes them from the market, safeguards confidential information, and ensures that any competitive advantage the employee might bring to a rival is significantly diminished.

The difference from restraint of trade is that during garden leave, an employee is still employed. A restraint of trade only takes effect after employment has officially ended.

Conclusion

Successful companies understand that the best way to protect against the loss of talent is to create an environment where those employees never want to leave in the first place. This can



be achieved by shifting resources toward financial incentives (e.g. ESOP's – Employee, Share Ownership Policies), career development, a supportive culture, and genuine wellness support.

When employees do leave for greener pastures, it is hopefully due to a compelling opportunity elsewhere rather than poor treatment. An exit with a well-managed handover and a signed settlement agreement is almost always preferable to a contested legal battle. Litigation to keep former employees from competing is expensive, uncertain, and can damage your employer brand.

Your employees are your greatest asset, but when they leave, they can become your greatest competitive threat. Do not wait for a key account manager to join a rival. Contact **Cyclopedic Consulting** for a confidential consultation. Let us help you build a comprehensive strategy that keeps your best people engaged and, when necessary, protects everything you have built.



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