

Update

Employment Law

November 7, 2008

Supreme Court of Canada Rules on the Duties of Departing Employees:

No General Duty Not to Compete \$1.5 Million Awarded for a Manager's Breach of a Duty of Good Faith

The Supreme Court of Canada recently issued a ruling that clarifies the duties applicable to departing employees. In *RBC Dominion Securities Inc. v. Merrill Lynch Canada Inc.* (released October 9, 2008), the Supreme Court held that:

- absent a contractual non-competition agreement, departing employees are free to compete against their former employer immediately upon resignation;
- employees are under a duty to give reasonable notice of resignation and may be liable to their former employer for damages arising from a breach of that duty; and
- managers who organize a mass departure of employees breach their implied duty of good faith, including a duty to retain employees under their supervision, and may be liable for substantial damages – in this case \$1.5 million – as a result of such breach.

The Facts

A branch manager in RBC Dominion Securities' small Cranbrooke office orchestrated the mass departure of almost all of the investment advisors and assistants working under his supervision in order to join a competitor, Merrill Lynch. The employees did not give

RBC Dominion Securities advance notice of their resignation. None of the employees had non-competition or non-solicitation clauses in their employment agreements. In the weeks preceding the mass exodus, the employees surreptitiously copied RBC Dominion Securities' client records and transferred them to Merrill Lynch. As a result of their actions, the RBC Dominion Securities office was effectively hollowed out and all but collapsed: it lost approximately 85% of the client accounts serviced by the departing employees.

The Supreme Court of Canada summarized RBC Dominion Securities' lawsuit as containing the following claims:

- *against its former employees*: breach of fiduciary duty; breach of an implied contractual term not to compete unfairly upon leaving employment; breach of an implied contractual term to give reasonable notice of termination/resignation; and an action for misuse of confidential information.
- *against Merrill Lynch and its manager*: breach of duty in tort for inducing RBC Dominion Securities staff to terminate their contracts of employment and to breach their contractual obligations not to compete unfairly.
- *against all defendants*: conspiracy and conversion, primarily related to the removal and copying of RBC Dominion Securities' proprietary and confidential information.

The Supreme Court of Canada Awards Damages of over \$1.5 million

RBC Dominion Securities was substantially successful and the Supreme Court of Canada upheld damages as follows:

- The RBC Dominion Securities manager who orchestrated the mass exodus was determined to have breached the implied duty of good faith owed by him – as with all employees – to his then-current employer. In this case, his duty was to retain employees who worked under his supervision. Damages of \$1.5 million were awarded on account of proven loss of profits.

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- The departing employees were determined to have breached the implied duty to give their employer reasonable notice of resignation, which in this case was held to be 2.5 weeks. A total of \$40,000 was awarded, based upon on the profits that these investment advisors would have contributed during the 2.5 week notice of resignation period.

Note that the appellate court had previously ordered punitive damages against Merrill Lynch in the amount of \$250,000, the managers in the amount of \$10,000 each, and the individual investment advisors in the amount of \$5,000 each. These awards, which were based on the misappropriation of confidential information, were not the subject of further appeal to the Supreme Court of Canada.

In making its decision, the Supreme Court of Canada confirmed that, absent a non-competition or non-solicitation clause in an employment contract, no such duties will be implied into an employment relationship. Accordingly, the Court rejected the claim for damages against the individual investment advisors based upon a breach of the “implied duty of unfair competition”. The Court held, however, that departing employees might be liable for specific wrongs such as improper use of confidential information during the notice period.

The Practical Result

This decision illustrates the need to put into place, at the time of hiring, enforceable written non-competition and non-solicitation agreements to guard against direct competition from a departing employee immediately upon resignation, which can be very damaging to a former employer’s business. Care should be taken, however, to include only reasonable and necessary non-competition and non-solicitation clauses that are catered to the particular business, failing which these clauses can be found to be unenforceable.

In addition, departing employees should recognize that their duties preclude the copying, removal, or use of the employer’s proprietary or confidential information other than for the purposes of the employer. Any confidential or proprietary information should be returned immediately to the employer. A misuse of information of this nature by either the departing employee or the new employer could result in substantial punitive

damages. As noted above, the court awarded \$250,000 in punitive damages against the new employer, Merrill Lynch, in addition to lesser awards of \$5,000 each against the departing employees and \$10,000 each against the managers.

This decision provides some protection for employers in that it confirms that all employees, whether or not they are fiduciaries, are under a duty of good faith while employed and that the recruitment of fellow employees to leave and join a competing business may breach that duty. Such breach can result in substantial damages being awarded against the “ringleader” employee.

Finally, the decision confirms that all employees are under an implied duty to provide their employer with reasonable notice of resignation, and that damages can arise from a failure to provide that notice. The damages do not include, however, losses arising from unfair competition.

If you have any questions with respect to the foregoing, please do not hesitate to contact:

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