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Recent decision highlights need for precision in seller restrictive covenants in Canadian M&A transactions

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Key Takeaways

- The decision emphasizes the need for precise drafting of non-competition and non-solicitation clauses in Canadian mergers and acquisitions transactions.
- The Court deemed the non-solicitation clause unenforceable due to ambiguity related to customer definitions after employment, highlighting the need for clear limitations.
- Canadian courts will scrutinize restrictive covenants for reasonableness, rejecting those deemed unreasonable.

A recent decision by the Alberta Court of King's Bench, *Intellimedia Limited Partnership v. Jawad*, 2026 ABKB 247, illustrates the importance of carefully drafting seller non-competition and non-solicitation clauses in the context of Canadian mergers and acquisitions transactions.

In this case, the Court found a non-solicitation clause to be unenforceable due to ambiguity because it applied to persons who "are" customers (and other classes of related persons) of the buyer without limiting the restriction to those who had that status during the seller's employment. This language made it impossible for the seller to know, post departure, who fell within the restricted class. This decision also demonstrates both the possibility and limits of using severance to save overbroad non-competition and non-solicitation clauses.

Background

The decision addresses restrictive covenants entered into in connection with the sale of a Canadian software business pursuant to an asset purchase agreement (the APA). As part of the transaction, Mr. Jawad, a co-founder and CEO of the company, was hired as the purchaser's CEO pursuant to an employment agreement. He later left that position.

The purchaser asserted that Mr. Jawad breached the non-compete and non-solicitation clauses included in the APA through his work creating a software product that would directly compete with the acquired business. The purchaser therefore sought an injunction to enforce the terms of the APA to restrain him from competing with the purchaser, from inducing its customers and others to cease doing business with or purchasing products from

it, and from soliciting any of its employees and independent contractors.

Non-solicitation clause was unenforceable for ambiguity

The non-solicitation clause contained in the APA provided that, from the APA's closing date until five years following the termination of the employment agreement, Mr. Jawad would not

i. "solicit the business of any Person who is a customer of Buyer for services materially similar to those offered by Buyer;

ii. solicit the business of any Person who is a customer of Buyer for services materially similar to those offered by Buyer;

iii. cause, induce or attempt to cause or induce any customer, supplier, licensee, licensor, employee, contractor, referral source, or other business relation of Buyer to cease doing business with Buyer or to purchase products or services materially similar to those offered by Buyer;

iv. solicit any employee or independent contractor of Buyer or in any way interfere with the relationship between Buyer and any of its employees or independent contractors; or

v. solicit any employee or contractor of Buyer for the purpose of having such employee or contractor employed or in any other way engaged by another Person with whom a Seller Party may be affiliated or otherwise associated;

provided, however, that [Jawad] may engage in such acts with the prior written approval of Buyer or pursuant to the terms of the [Employment Agreement] on behalf of Buyer and its Affiliates."

The Court explained that, in order for a non-solicitation restrictive covenant to be unambiguous and enforceable, its meaning must be ascertainable and it must be possible to predict when it is being breached. The restriction must be narrowed to a "reasonably knowable group of people."

The Court concluded that the purchaser had not established a strong *prima facie* case to enforce the non-solicitation clause. The restriction purported to apply to customers and other persons with connections to the purchaser, using the present tense, and without limiting them to those with whom the purchaser had a connection during Mr. Jawad's employment. After his employment ended, Mr. Jawad could never know whether a particular person became a customer, supplier, licensee, licensor, employee, contractor or referral source. This created an ambiguity and an unreasonable overreach because the clause was not limited to a reasonably knowable group of people. The Court also noted that the references to the purchaser's "business relations" created an additional ambiguity.

This was fatal to the non-solicitation clause in its entirety. Furthermore, in the Court's view, it could not likely be saved through a blue-pencil or notional severance, even though the APA expressly contemplated severance.

'Blue pencil' severance available to save non-compete clause

The non-compete clause's core restriction was in respect of "the creation or licensing of education software products (for educational institutions (K-12)) that directly compete with

any software products of the Seller." It applied from the APA's closing date until five years following the termination of the employment agreement.

The Court concluded that, in the circumstances, there was a strong *prima facie* case that the non-compete clause was reasonable and enforceable. On the last point, the Court considered whether the non-compete clause had an unreasonably broad geographical scope. Under Canadian law, the reasonableness of the geographic scope of a restrictive covenant is judged by the geographical scope of the business that was sold. The Court observed that, in this case, the non-compete clause covered jurisdictions outside of Alberta, but there was limited evidence that the acquired business engaged in business outside of Alberta.

While the enforceability of the non-compete appears not to have been strongly contested, the Court observed that, even if the non-compete clause was unreasonably broad, there was a strong *prima facie* case that the clause could be saved as reasonable. Its overbreadth could be addressed by applying "blue pencil" severance to delete the geographical jurisdictions other than Alberta. As previously noted, this type of severance was expressly contemplated in the APA.

The Court accordingly granted an injunction targeting certain business activities involving competition with the acquired company, thereby specifically enforcing the non-compete clause. The purchaser was not, however, entitled to an injunction in relation to the non-solicitation clause.

Conclusion

This decision underscores that Canadian courts will closely scrutinize non-competition and non-solicitation covenants — even those entered into in the M&A context, as opposed to the employment context — for reasonableness, and will decline to enforce restrictive covenants that are found to be unreasonable.

In this case, the non-solicitation language found to be unenforceable is similar to form language often encountered in M&A restrictive covenants, and *Intellimedia* provides important guidance that should be taken into account by Canadian practitioners. Specifically, practitioners should ensure non-solicitation clauses expressly limit the restricted class to customers and business relations as of the date of the restricted person's departure (or a defined lookback period), rather than using open-ended present-tense formulations that could capture persons who acquire that status after departure.

The Court's reasons also show how severance can and cannot be used to save an otherwise overbroad restrictive covenant clause. The Court expressed a willingness to apply severance to save the non-compete clause as reasonable by deleting the geographical jurisdictions other than Alberta to limit the clause's geographical scope. On the other hand, severance was unlikely to save the non-solicitation clause, because the ambiguity at issue ran throughout the entire clause.

Intellimedia supports the inclusion by buy-side M&A lawyers of express "blue pencil" severance language in restrictive covenant agreements, as well as careful drafting of covenants to facilitate "blue pencilling" if a court deems it necessary. It is important to note that while *Intellimedia* and other decisions have applied "blue pencil" severance to restrictive covenants entered into in the M&A context, Canadian courts are generally not willing to apply it to restrictive covenants entered into in the employment context.