



Fiduciary Obligations of Former Employees in the Oil & Gas Industry

By Brian Thiessen and Frank Durnford

We are often asked to consider whether the competitive activities of certain former employees of companies in the oil and gas industry may be restricted due to the fiduciary duties owed by these employees to their former employers. This memorandum sets forth an overview of the legal issues that are applicable in respect of both the duties owed by these employees to their former employer and the potential remedies available to their employers to restrict their competitive acts.

I. SUMMARY

It is established law in Canada that certain employees, normally upper echelon managers and directors of an organization, owe their employer a fiduciary obligation over and above their implied duty of good faith and fidelity as a regular employee. Former employees that were given the authority to make decisions in the best interest of their employers and, indeed, who were charged with the responsibility to do so, cannot actively solicit the business of their former employer.

All employees owe a duty not to disclose confidential information. Examples of confidential information that have been found by the courts to be included in this fiduciary duty in the oil and gas industry include (but would not be limited to): unpublicized well information (such as tight well information), specific confidential plays, developed seismograph information or proprietary seismic, detailed subsurface studies and private environmental assessments. A former employee in the oil and gas industry is free to use his knowledge of the industry and available resources and opportunities when competing with a former employer. However, he may not use information garnered as the result of a particular corporate venture or exercise which is not generally known to the public, or any other trade secrets of the employer.

Where a former employee so breaches his fiduciary duty, the former employer may claim damages for the amount of the wrongful gain garnered as a result of the breach. Further, an employer may claim injunctive relief to prevent further breaches of the duty owed.

II. DISCUSSION

A. Fiduciary Obligations Owed By Former Employees

All employees have a duty to their employer to serve their employer honestly and faithfully. This is a fundamental term of the employment relationship.

As the Court stated in *Tree Savers International Ltd. v. Savoy*¹:

An employee has a basic common law obligation to render faithful and loyal service to his employer during his employment. As a general rule, an employee may leave his employment and lawfully compete against his former employer, taking with him knowledge gained in his former employment, but he may not take or use against his employer any of his employer's trade secrets, confidential information or customer lists, whether during or after his employment. **If he was top or senior management or a key employee he owes a fiduciary duty to his employer, which not only encompasses the ordinary duties of an employee but is an enlarged, more exacting duty which endures after termination.**

Fiduciary obligations go beyond the fundamental duties of an employee. *Black's Law Dictionary* defines a "fiduciary relationship" as follows:

a relationship in which one person is under a duty to act for the benefit of another on matters within the scope of the relationship.

Canadian courts continue to use the test espoused by Wilson J. in her dissent in *Frame v. Smith*², in determining whether a fiduciary relationship exists. According to Wilson J., the following indicia must be present:

1. a scope for the exercise of some discretion or power;
2. a unilateral ability to exercise that power or discretion so as to affect the beneficiary's interests; and
3. a peculiar vulnerability to the exercise of the discretion of some power.

The Supreme Court of Canada's decision in *Canadian Aero Service Ltd. v. O'Malley*³, made it clear that fiduciary obligations can extend beyond directors of a company to other senior management employees.

Laskin J. outlined the principles to be considered in assessing whether an employee owes a fiduciary obligation to a former employer:

The general standards of loyalty, good faith and avoidance of a conflict of duty and self interest to which the conduct of a director or senior officer must conform must be tested in each case by many factors which it would be reckless to attempt to enumerate exhaustively. Among them are the factor of the position or office held, the nature of the corporate opportunity, its ripeness, its specificness [sic], and the director's or managerial officer's relation to it, the amount of knowledge possessed, the circumstances in which it was obtained and whether it was special or, indeed, even private, the factor of time in the continuation of the fiduciary duty when the alleged breach occurs after termination of the relationship with the company, and the circumstances under which the relationship was terminated, this is whether by retirement, or resignation or discharge.

Despite the extension to senior management employees, courts still look for indicia of power or the ability to affect the legal or practical interests of the company before they find a fiduciary obligation. As set out in *R.W. Hamilton Ltd. v. Aeroquip Corp.*⁴, an officer or manager cannot be "saddled" with a fiduciary duty

¹ (1991), 81 Alta. L.R. (2d) 325 (Q.B.) at 328 [*Tree Savers*].

² [1987] 2 S.C.R. 99.

³ [1974] S.C.R. 592 [*Canadian Aero*].

⁴ (1988), 65 O.R. (2d) 345 (Ont. H.C.) at 353.

unless, "the position occupied contains the power and the ability to direct and guide the affairs of the company". An employee's title may or may not match the reality of the situation. The Court went on to write:

Not all managerial positions should lead to the imposition of the very high duty of a trustee lest the law commit a high proportion of employees in this Province to slavery. Employers are protected from the faithless actions of top management by the law of trusts and, failing that, in respect of lower level employees by certain elementary rules of decency that will prevent theft of confidential information and customer lists. Beyond this the law dare not go, preferring that the business community rely on contractual arrangements.

It is likely, then, that anyone formerly holding a senior executive position will owe a fiduciary duty to their former employer even beyond the employment relationship.

B. Breach of Fiduciary Duty

In *CRC-Evans Canada Ltd. v. Pettifer*⁵, both employees were found to have breached their fiduciary duties to their employer. The Court concluded:

These men were trusted employees. They acted in a fashion that betrayed the duty that was owed by them to their employer. CRC-Evans expected them to make decisions in the best interest of their employer. They were given the authority to do so. They were charged with the responsibility to do so. They did not. While both were employed by the Plaintiff, they planned to incorporate a competing business. They planned to go after customers normally serviced by CRC-Evans. They planned to bid on projects that one of them bid for the employer. Information directly involved with this bid was provided to [the service manager] from [the sales manager].

Generally speaking, charging a fiduciary with the authority and responsibility to act in the best interests of their employer and to continue to do so for a time after the employment relationship has terminated does not result in an endless list of prohibitions. Indeed, much of the law focuses on two areas: non-solicitation and confidentiality.

(i) Non-solicitation

Where a former employee is held to be fiduciary, direct solicitation of former customers, employees and suppliers is prohibited. As the court stated in *Anderson, Smyth & Kelly Customs Brokers Ltd. v. World Wide Customers Brokers Ltd.*⁶:

Direct solicitation of the former employer's clients by the departing or departed employee is not acceptable where the employee is a fiduciary of the employer. Having been vested with a high degree of trust and confidence, the indicia of a fiduciary relationship, a key employee is not then at liberty to betray the trust by soliciting the employer's clients for his own account or for someone else to his indirect benefit. To suggest otherwise would be to weaken the strong sense of duty and obligation which the term fiduciary connotes.

Outside a specific non-solicit covenant, the fiduciary duty not to solicit customers extends for a reasonable time period. In that case the Court deemed that period to be between 15-18 months. The decision is also significant because it emphasizes the movement of the law away from the use of formal relationships as

⁵ [1997] A.J. No. 20 (Q.B.); aff'd [1998] A.J. No. 629 (C.A.).

⁶ (1996), 7 W.W.R. 736 (Alta. C.A.).

determinative of a fiduciary duty towards a greater reliance upon the substance of the relationship between the parties.

It is important to distinguish between actively soliciting past partners and clients and simply accepting business from them. In *Christie (W.J.) & Co. v. Greer and Sussex Realty and Insurance Company*⁷, the Manitoba Court of Appeal found that a fiduciary employee is entitled to accept business from a former client but direct solicitation of that business is not permissible. This case was cited with approval in *Alberta in Clarke v. Rossburger*⁸.

Similarly, in *Sanford Evans List Brokerage v. Trauzzi*,⁹ the Court held:

As an overriding proposition, departing employees have an absolute right to go into direct competition with their former employer and make use of the skills and general knowledge they accumulated during their period of employment. Competition per se by a departing fiduciary is not prohibited; only unfair competition is precluded. Thus, a departing fiduciary may advertise to the general public. If the former employer's customers are notified during the course of the general advertising campaign, there is no breach, provided there is no misuse of confidential information such as trade secrets or customer lists.

What constitutes direct solicitation is a question of fact. The courts have frequently drawn a distinction between general solicitation of customers, which is permitted, and targeting specific customers, which is not. The courts have also allowed fiduciaries to return calls from customers responding to general announcements.¹⁰ Where, however, an industry is very small and all the customers are well known, a fiduciary cannot respond to a contact initiated by his former employer's customer if the contact is in response to a general announcement.¹¹

*Jordan Inc. v. Jordan Engineering Inc.*¹² describes the scope of a former employee's non-solicitation duty as follows:

As well, if a departing fiduciary attracts customers or other employees by virtue of her qualifications or experience, this will not breach the fiduciary duty; however, if she affirmatively solicits customers or employees, relying on relationships developed during her time with the corporation, she will be in breach of her fiduciary obligations.

Similarly, in *Re Berkey Photo (Canada) Ltd. v. Ohlig et al.*¹³, the Court stated that if a former employee did not solicit the former employer's employees, but rather, such employees decided of their own volition to leave the former employer to work for the new company, there is no breach of fiduciary duty.¹⁴

Although the breach of fiduciary duty must involve some affirmative action, case law suggests minimal efforts to solicit employees of the former employer may be enough. In *Canadian Patent Scaffolding Co. v.*

⁷ (1981), 9 Man. R. (2d) 269 (C.A.).

⁸ [1999] A.J. No. 1256 (Q.B.); aff'd [1999] A.J. No. 1168 (C.A.).

⁹ (2000), 50 C.C.E.L. (2d) 105 (Ont. S.C.) [*"Sanford Evans"*].

¹⁰ See generally *W.J. Christie v. Greer* (1981), 121 D.L.R. (3d) 472 (Man. C.A.) and *Metropolitan Commercial Carpet Centre Ltd. v. Donovan* (1989), 42 B.L.R. 306 (N.S.S.C.).

¹¹ *Di Florio v. Con Structural Steel Ltd.*, [2000] O.J. No. 340 (Ont. S.C.).

¹² [2004] O.J. No. 3260 (Ont. C.J.). Note that the facts of the case involved solicitation of clients by the former employee.

¹³ (1983), 43, O.R. (2d) 518 (Ont. H.C.).

¹⁴ See also *DCF Systems Ltd. v. Gellman* (1978), 41 C.P.P. (2d) 145 (Ont. H.C.).

*UMACS of Canada Inc.*¹⁵, the Court found solicitation in a case where a fiduciary former employee merely asked another employee of his former employer whether he would be interested in a new job. Once the employee responded in the affirmative, the Vice President of the new employer offered the job; the former employee had no further involvement in the recruitment. The Court granted an interim injunction restraining the former employee and the new employer from soliciting the former employer's employees.

(ii) Confidentiality and Non-competition

Tree Savers, supra, and *Sanford Evans, supra*, are clear in their support of fair competition by former employees who are fiduciaries. Indeed, in *Physique Health Club Ltd. v. Carlsen*¹⁶, the Alberta Court of Appeal found that "[c]ompetition with [an employer] after the employment relationship has ceased does not of itself constitute a breach of the fiduciary duty." Furthermore, the right to compete with a former employer extends to top management (see *Metropolitan Commercial Carpet Centre Ltd. v. Donovan* (1989), 91 N.S.R. (2d) 99 (N.S.S.C.)). While a former employee may benefit from any skill or general knowledge garnered during the course of his employment, the Alberta Court of Appeal affirmed that he cannot "use for his own benefit confidential information acquired in the course of his employment or information which is 'special or peculiar' to his ex-employer," lest he engage in unfair competition.

Laskin J. defined confidential information in *International Corona Resources Ltd. v. Lac Minerals Ltd.*¹⁷ as information that has "the necessary quality of confidence about it, namely, it must not be something which is public property and public knowledge." Similarly, trade secrets have been defined as

"any formula, pattern, device, or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it."¹⁸

In *Abode Properties Ltd. v. Schickedanz Bros. Ltd.*¹⁹, a case regarding a claim for breach of contract and breach of confidence, the Court found that two geotechnical and environmental assessments that were ordered by the Plaintiff company in anticipation of the purchase of a parcel of land for development were confidential as the reports were not available to the public and were the result of private testing. It follows, then, that any similar report or resource developed by a company for its use and benefit and any knowledge specific to the contents of those materials falls into the category of confidential information or trade secret. With respect to employees engaging in competition with their former employers, then, using such information amounts to unfair competition and constitutes a breach of the fiduciary duty.

Of particular importance to the oil and gas industry is the application of an employee's duties to landmen and geologists who have worked as corporate employees. In this regard, Morison states:

"trade secrets are the property of the employer and cannot be taken or used by the former employee for his own benefit... The geologist who has worked as a corporate employee in a certain area has acquired a

¹⁵ [1990] O.J. No. 112 (Ont. S.C.).

¹⁶ [1996] A.J. No. 1004 (C.A.).

¹⁷ (1989), 61 D.L.R. (4th) 14 (S.C.C.).

¹⁸ *R.L. Crain Ltd. v. R.W. Ashton & Ashton Press Mfg. Co.*, [1949] O.R. 303, as cited by I. Christie et al., *Employment Law in Canada*, 4th ed (Markham: LexisNexis Canada Inc., 2005) (looseleaf). Christie et al. also note that trade secrets may be industry specific, insofar as it is the custom or practice in the industry to regard a particular type of information as confidential and of commercial value.

¹⁹ (1999) 254 A.R. 91 (Q.B.).

great deal of knowledge about ... conditions, formations and production characteristics of that certain area. All of this he surely could continue to use. **As opposed to this, however, he cannot take with him seismograph information which has been developed by the corporation, detailed subsurface studies or unpublicized well information.**²⁰

A former employee in the oil and gas industry, then, is free to use his general knowledge of the industry and the available resources and opportunities when competing with a former employer. Where that knowledge has been garnered as a result of a particular corporate venture or exercise, that is not known to the public, it cannot be used in the new position.

(iii) Further examples of breaches of the fiduciary duty

A review of the Alberta case law indicates that the following actions would likely be found to constitute a breach of fiduciary duty:

- targeting/soliciting past clients and partnerships without allowing for a “cooling off period”. In doing this, the fiduciary employee takes the reputation that he built with the employer and immediately flips it to a new company, thereby misappropriating the employer’s good will;
- utilizing price information if it can be proven that the employee took customer lists, inside knowledge or confidential price lists (as opposed to using information widely known among sales people or general knowledge gained in the industry). Notably, memorization of lists in some cases has been held to be tantamount to physical appropriation: see *Quantum Management Services Ltd. v. Hann et al.*, [1989] O.J. No. 542;
- negotiating to become involved with a competitor or key customer at the time still employed with the employer (i.e. personal interest conflicting with employer’s interest);
- taking advantage of an opportunity that came to the employee’s attention because of his unique position of fiduciary to his employer;
- using knowledge about appropriate workers, the standard mark-ups employed by the Company for product and labour costs, the jobs that would have to be bid and the jobs that would not have to go out to bid; and
- disclosing or using confidential information such as proprietary seismic, specific confidential plays, detailed subsurface studies, unpublicized well information, or other trade secrets that have been prepared and developed by their employer.

²⁰ “Conflicts of Interest in the Oil and Gas Industry” (1963), 8 Rocky Mountain Mineral Law Institute 219, cited with approval in *Chevron Standard Ltd. v. Home Oil Co.*, [1982] W.W.R. 427 (Alta. C.A.), leave to appeal denied: 67 C.P.R. (2d) 16 (S.C.C.). In that case, a senior and management level geologist changed jobs just as his former employer was embarking on an exploration opportunity. The Court found that the former employee relied solely on his own experience and knowledge and public information to lead his new employer to success in the same venture.

It should be noted that in *RBC Dominion Securities Inc. v. Merrill Lynch Canada Inc.*,²¹ a recent decision of the British Columbia Court of Appeal, the Court carved out a narrow exception for former employees in a regulated industry. In that case, investment advisors were found to be entitled to write down the contact information of their own "book of clients" to take with them to their new job. The Court found that in such a regulated industry seamless service is essential to the client and that a client is entitled to know, immediately upon an advisor leaving one firm for another, the location the advisor has gone so the client may decide where to take his business. RBC Dominion, who lost most of its employees in the events surrounding this case, is appealing to the Supreme Court of Canada. For now it seems that, in regulated industries at least, client lists likely do not "belong" to the employer.

A good summary of the established law is provided in the Ontario case of *Gertz v. Meda Ltd.*, [2002] O.J. No. 24 (S.C.):

[. . .] A mere employee is quite entitled, following termination of his employment to immediately engage in competition with his former employer and solicit the customers of his former employer, and to use the knowledge and skills which he acquired in his former service, including knowledge and skill obtained from the previous master in teaching his business: *Alberts v. Mountjoy* (1977), 16 O.R. (2d) 682 (Ont. H.C.). "Top management", however, owes a fiduciary duty which is much larger and more exacting, and is similar to that owed to a corporate employer by its directors. That duty includes loyalty, good faith and the avoidance of a conflict of duty and self-interest: *Canadian Aero Service Ltd. v. O'Malley*, [1974] S.C.R. 592.

Accordingly, in light of the case law reviewed above, as fiduciaries of their previous employer, former senior executives are permitted to attract partnerships and business opportunities of their former employer by virtue of their qualifications or experience, however, former senior executives may not affirmatively solicit their former employer's business opportunities, relying on relationships developed during the tenure of their employment with the former employer. To do so would constitute a breach of their fiduciary obligations.

C. Damages for Breach of Fiduciary Duty

The Court in *Firemaster Oilfield Services Ltd. v. Safety Boss (Canada)(1993) Ltd.*²² cites the Supreme Court of Canada's decision in *Canadian Aero*, *supra* as authority for the proposition that fiduciaries must answer for their default according to their gain. On this basis, where a breach of fiduciary duty can be established, the wronged party can apply for a remedy declaring trust "property" to be owned by it and/or an account of all gain made through the breach. However, this does not mean that the Plaintiff does not have to prove that the amount gained by the Defendant is a wrongful gain consequent to the breach of fiduciary duty.

D. Injunctive Relief

In the context of trying to enforce restrictive covenants or trying to enforce fiduciary duties not to solicit key customers, the test for injunctive relief is fairly strict. The three pronged test is as follows:

1. strong *prima facie* case to be tried;
2. irreparable harm if the injunction is not granted; and

²¹ (2007) BCCA 22.

²² (2001), 4 W.W.R. 256 (Q.B.).

3. on a balance of convenience, more prejudice to the employer as opposed to the employee by not granting the injunction.

(i) Strong Prima Facie Case

Instead of having to demonstrate that there is simply a serious issue to be tried, an employer must demonstrate that it has a "strong prima facie" case. This is due to the fact that if the injunction is successful, the employer effectively obtains a full remedy before trial: See *R.J.V. Gas Field Services Ltd. v. Baxandall*, [2003] A.J. No. 731 (C.A.); see also *Windship Aviation Ltd. v. deMeulles*, [2002] A.J. No. 952 (Q.B.).

(ii) Irreparable Harm

Further, the employer must demonstrate that monetary damages are insufficient to compensate it for the breach. Irreparable harm might be demonstrated where disclosure of a trade secret has occurred (as in *Windship*, supra), however, most cases indicate that outside of particular circumstances, an employer can be adequately compensated by damages: see *Noise Solutions Inc. v. Commercial Insulation Contracting Ltd.*, [1998] A.J. No. 883 (C.A.).

(iii) Balance of Convenience

Even where a fiduciary obligation exists, courts are hesitant to grant injunctions on the basis that it would unduly restrain an employee from competing with his former employer: see *Vue Weekly v. See Magazine Inc. (Receiver of)*, [1995] A.J. No. 993 (C.A.) at paragraph 20. In the absence of a situation where trade secrets are being disclosed or where it can be proven that former employees are actively targeting key customers of the employer, it is rare that an injunction will be ordered.

In addition, for the applicant on an injunction to succeed, it must give an undertaking as to damages. If it is determined in the end that no breach has occurred, the applicant is liable for all damages the respondent suffers as a result of the injunction having been in place.

While the employee in *Firemaster*, supra was not held to be a fiduciary employee, the court did find that the sales employee had not provided his employer with sufficient notice of his resignation. All employees (whether fiduciary or not) owe their employer the duty of loyalty and fidelity, including the duty to give reasonable notice of resignation. In *Firemaster*, supra Cusson was a 13-year employee and was the only salesman in the Calgary region. On that basis, the Court found that his employer could have reasonably expected more than two weeks' notice to move someone else into his position. Ultimately, the Court had awarded Firemaster the equivalent of three months' notice as an appropriate period of notice for Firemaster to adapt to the loss of its salesman. One of the factors the Court considered was whether Firemaster had a large sales force throughout the province such that another senior salesman could be transferred to Cusson's former position.

III. CONCLUSION

For the most part, former senior executives are free to engage in fair competition with former employers (absent a contractual agreement to the contrary), but they will be bound by fiduciary obligations not to actively solicit clients, suppliers and employees of their former employer. Where specific knowledge has

been garnered as a result of a particular corporate venture or exercise, that is not known to the public, it cannot be used in the new position.

In Alberta, the extent of the duty owed by such employees will also likely prohibit them from:

1. targeting/soliciting past business partners;
2. using pricing information that is linked directly to customers and their individual information or to specific projects and bidding processes;
3. using confidential information such as proprietary seismic, unpublicized well information, detailed subsurface studies, specific confidential plays, private environmental assessments or other trade secrets of the employer;
4. negotiating new employment with a competitor while still employed with the employer; and
5. taking advantage of opportunities that are available by virtue of the position with the employer.

An employer may sue for breach if such a transgression occurs, claiming as damages the wrongful gains garnered by the prohibited actions. Injunctive relief is also available, allowing an employer to potentially put an end to the prohibited behaviour.