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**How to protect the employer's interests after the termination of employment contracts –
aspects of labour law in general
Commission(s) in charge of the Session/Workshop:**

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INTRODUCTION

Post-termination restrictive covenants typically used in the employment contracts in India are in the form of non-compete clauses, confidentiality obligations, non-solicitation clauses and garden leave clauses.

Relying on the interpretation of applicable provisions contained in the Constitution of India and the Indian Contract Act, 1872, Indian judiciary has generally held that the right to livelihood of the employees must prevail in spite of an existing agreement between the employer and the employee. Consequently, the courts have upheld that non-compete provisions which extend beyond the term of the employment are not enforceable. Further, courts do not recognize 'reasonable' non-compete restrictions and have on several occasions held that all post-termination non-compete provisions are in the nature of a restraint on trade and therefore, unenforceable.

However, companies generally include such post-termination non-compete clauses in the employment contract since such clauses act as a deterrent to the employees.

1. Employment Law

1.1. Restrictive covenants

1.1.1. **Is the principle of A POST-TERMINATION RESTRICTIVE COVENANT known in your legal system? If yes, how can this principle be defined? Where does the principle have its origin? (Civil Code, case law, etc)**

Post-termination restrictive covenants like non-compete, non-solicit, confidentiality, etc. are ubiquitous in employment contracts in India.

The basic principle behind these clauses is to prevent the ex-employee from (i) creating competition to the employer using knowledge gathered while in employment; (ii) soliciting or dealing with customers of the business by using knowledge of those customers gained during his prior employment, etc.

The concerns of employers and employees relating to protection of confidential information, non-disclosure, non-compete and non-solicitation are yet to be addressed through a specific legislation in India. Hence, these principles have evolved over a period of time along with increased complexities in the work field and resultant increase in disputes related to payment terms, termination of service, breach of confidentiality, etc.

1.1.2. At what stage in the employment relationship between employee and employer are post-termination restrictive covenants agreed upon in your jurisdiction? Is there any relevant case law?

The post-termination restrictive covenants typically are agreed to at the time of commencement of the employment relationship, i.e. such covenants form part of the employment agreements executed between the employee and the employer prior to/at the time of commencement of the employment relationship.

1.1.3. Once the employment contract is signed, is there a general obligation of non-compete also in the absence of an express agreement after the termination of the employment? Are there specific statutory provisions or precedents referring to this? Could whistle blowing be regarded as a part of the employee's post-termination restrictive covenant?

As mentioned above in the introductory section, Indian courts have upheld that non-compete provisions which extend beyond the term of the employment are not enforceable. Further, Indian courts do not recognize 'reasonable' non-compete restrictions and have on several occasions held that all post-termination non-compete provisions are in the nature of a restraint on trade and therefore, unenforceable. As a result, general obligation of non-compete provisions do not exist in India post-termination of employment.

Barring the confidentiality obligations forming part of the employment agreements executed between the employee and the employer, there is no statutory framework governing whistle blowing in the private sector.

1.1.4. Which obligations regarding post termination restrictive covenants exist on the employer's side in the absence of an express agreement? Are there specific statutory provisions or precedents governing employer's duties after the termination of the employment in your jurisdiction?

As mentioned above, in the absence of an express agreement between the employer and the employee, it is clear that the general obligation of a non-compete provision is not in existence in India. However, an ex-employee will be under a general obligation to maintain secrecy of confidential information relating to the employee post-termination of his/her employment with the employee failing which the employer can initiate action against the ex-employee under the Indian Penal Code, 1860 ("IPC") and the Information Technology Act, 2000.

1.1.5. What kind of different restrictive covenants that may be available and can be agreed between employer and employee in your jurisdiction? (see the

examples in the introduction). Please describe how these can be defined and how they work in your jurisdiction.

Firstly, it is necessary to understand the legal system governing post termination restrictive covenants.

As per the Indian Contract Act, 1872 (“**Act**”), agreements that restrain a person from his right to take up any lawful profession, business and trade are void to that extent.¹ An agreement in restraint of trade is one in which one party agrees another party to restrict his liberty in the present or the future to carry on a specified trade or profession with other persons (not being parties to the contract) without the express permission of such other party in such a manner as he chooses. However, the Act provides an exception to the above and validates inclusion of such restrictive clauses in agreements relating to sale of goodwill wherein the purchaser of the goodwill of a business may agree with the seller to refrain himself from carrying on a similar business within specified local limits.

Article 19 (g) of the Constitution of India clearly provides every citizen the right to practice any profession, trade or business.

For any restrictive covenant to fall within the ambit of Section 27 of the Act, the agreement has to be in restraint of trade, and unlike the law of UK, the Act, does not distinguish between partial and total restraint of trade; if the clause amounts to a restraint post termination of the agreement, then the same is void.

While it is a settled position of law that restrictive agreements bind current employees in lawful employment of the employer throughout the duration of the contract², the position of law regarding validity of such restraints on employees after termination of contract is more contentious and adjudicated before courts. Recently, it was held by the Supreme Court that “a restrictive covenant extending beyond the term of the contract is void and not enforceable”³.

The different kinds of restrictive covenants that are usually agreed upon between the employer and the employee in India, include, non-compete, non-solicit, confidentiality and non-disclosure, training bonds, garden leave, etc., which are discussed in the detail below.

Non-compete: As mentioned above, agreements that restrain a person from his right to take up any lawful profession, business and trade are void under the Act.

¹ Section 27 of the Act: "Agreement in restraint of trade, void" – Every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void.

² Superintendence Co. of India Pvt. Ltd. v. Krishan Murgai, AIR 1980 SC 1717.

³ Percept D'Mark (India) Pvt. Ltd. v. Zaheer Khan & Anr, AIR 2006 SC 3426.

An Agreement in restraint of trade is defined as one in which one party agrees with another party to restrict his liberty in the present or the future to carry on a specified trade or profession with other persons (not being parties to the contract) without the express permission of such other party in such a manner as he chooses.

Further, Article 19 (g) of the Constitution of India clearly provides every citizen the right to practice any profession, trade or business.

For any restrictive covenant to fall within the ambit of Section 27 of the Act, the agreement has to be in restraint of trade.

In the case of *Wipro Ltd. v. Beckman Coulter International SA*, it was held that “negative covenants between employer and employee contracts pertaining to the period post termination and restricting an employee’s right to seek employment and/or to do business in the same field as the employer would be in restraint of trade and, therefore, a stipulation to this effect in the contract would be void”⁴.

Thus, it is a settled position of law that the non-compete restriction is valid only during the term of employment.

Non-solicit: Under a non-solicit covenant, an employee agrees not to solicit the employees or clients of the employer for his own benefit during or after his employment with the employer. Unlike non-compete covenants, non-solicit covenants have been enforced in certain cases and enforceability of such a covenant would be dependent upon the facts of each case.

In case of *Embee Software Pvt. Ltd. v. Samir Kumar Shaw*⁵, the Calcutta High Court held that ‘acts of soliciting takes such active form that it induces the customers of the former employer to break their contract with the former employer and enter into a contract with the former employee, or prevents other persons from entering into contracts with the former employer’ cannot be permitted.

To conclude, non-solicit covenants may be enforced (post-employment) in cases where the employees have actually pursued to poach employees and customers of the ex-employer and such action on the part of such ex-employee has resulted in discontinuance of contracts by such employees and customers with the employer company. Further, bargaining power of both the parties will be the major factor that will decide enforceability of such contracts.

4 2006 (3) ARBLR 118 (Delhi)

5 AIR 2012 Cal 141.

Therefore, non-solicitation of employee clauses are generally weak covenants per se and easy to circumvent.

Confidentiality and non-disclosure: Under this covenant, the employee agrees to not discuss or disclose the confidential information of the employer or its clients to any person or business unrelated to the employer, unless such disclosure has been mandated under the law. Such covenants are enforceable in India.

In *Diljeet Titus v. Mr. Alfred A. Adebare and Others*, the Delhi High Court barred the defendant from using the information taken away illegally⁶.

As mentioned above, the IPC under section 381 (theft by clerk or servant), section 403 (dishonest misappropriation of property), section 405 (criminal breach of trust), section 408 (criminal breach of trust by a clerk or servant) provides adequate protection in case of breach of confidentiality terms by an ex-employee. In such cases, action against the ex-employee can be initiated by the ex-employer under the IPC.

In *Abhinav Gupta v. State of Haryana*, it was discovered that the employee had transferred or downloaded various confidential information of Company A into his personal e-mail. Screenshots of the mail id of the accused was produced which showed that such information was passed on to a competitor company where he took up employment. Thus, the Court was of the view that such act amounted to hacking under Section 66 of the Information Technology Act, 2000; cheating and dishonestly inducing of property under Section 420 of the IPC and also amounted to criminal breach of trust under Section 406 of the IPC⁷.

Thus, it can be noted that unauthorized disclosure of confidential information is adequately protected and enforceable in India.

Training Bonds: The training bonds specify the minimum period for which the employee shall serve the employer though such clauses may not be enforceable in the Indian context. However, the employer can seek compensation, limited to the expenses incurred for training. However, the compensation awarded would be reasonable.

In *Satyam Computer Services Limited v. Ladella Ravichander*, the company sought to recover liquidated damages of Rs. 2,00,000.00 from the employee who abruptly left the organization. It was held that such action did not cause any damage or loss

⁶ 2006 (32) PTC 609 (Del)

⁷ 2008 CriLJ 4356

to the company and it would be unreasonable to acquire such amount. An amount of Rs. 1,00,000 was fixed by the court as reasonable damages taking into consideration the period of work and the fact that no actual loss was caused to the company.

In *Toshnial Brothers (Pvt.) Ltd. v. E. Eswarprasad & Ors.*, an employee working as Sales Engineer in breach of his undertaking left his services within 14 months as against the contractually agreed period of 3 years. The employer is required to establish that the employee was the beneficiary of special favour or concession or training at the cost and expense wholly or in part of the employer and there had been a breach of the undertaking by the beneficiary of the same⁸.

Garden Leave: The effect of a garden leave clause is to prohibit the ex-employee from taking up any employment during a limited period (ranging from one to three months) on the cessation of employment with the employer. Such clauses are usually being viewed as restraint in trade, etc. under section 27 of the Act and hence, not enforceable.

In case of *VFS Global Services Private Limited v. Mr. Suprit Roy*, the Bombay High Court held that the garden leave clause is in restraint of trade and hence, hit by Section 27.

1.1.6. What are the conditions for a valid post termination restrictive covenant in your jurisdiction? (e.g. prerequisites like minimum age, minimum salary, minimum employment period; way of termination of employment, etc.). Please describe the conditions applicable and how these work in your jurisdiction.

As mentioned above, concerns of employers and employees relating to protection of confidential information, non-disclosure, non-compete and non-solicitation are yet to be addressed through legislation in India; requiring recourse to common law and judicial decisions. Hence, there are no pre-requisites like age, qualification, experience, designation, etc. for enforcing such covenants and it will be dependent upon the facts of each case and the nature of restriction.

1.1.7. What is the potential scope of a post termination restrictive covenant in your jurisdiction? (e.g. taking into consideration time, geographical scope, content, interest, activities; etc.). Please describe how that works in your jurisdiction and what pitfalls have to be observed for both employers and employees.

⁸ 1997 LLR 500

As mentioned above, a post termination restrictive covenant in India can be held valid only during the term of employment or if related to disclosure of confidential information of the employer's business or non-solicitation of the employer's clients for a reasonable time period post termination of the employment. Also, the buyer of goodwill of a business shall be subject to the restrictive covenants imposed by the seller.

Barring these limited circumstances, a post-termination restrictive covenant is non-enforceable and invalid in India.

Hence, employers need to carefully analyze the outcome of the inclusion of these restrictive covenants in the employment agreements.

An employee on the other hand, must ensure that he does not disclose any confidential information relating to the business of his ex-employer which may cause him financial loss. In such a case, the ex-employee would be held liable and would have to indemnify the employer. Also he must not solicit with any his ex-employer's clients for a reasonable period of time as mentioned in his employment agreement. Although he has every right to leave his employment even when he is under a training bond, he must not cause his employer to incur losses in his business.

1.1.8. What are the possible sanctions against the employee in the event of a breach of a post termination restrictive covenant? Describe how that works in your jurisdiction and provide for practical information about the dos and don'ts.

In case of a breach of post-termination restrictive covenant which is valid in the eyes of law, the employer can file a civil suit before a Civil Court of appropriate jurisdiction. Also, the employer can file a civil suit seeking injunction/specific performance of contract as well as damages.

1.1.9. What are the possible sanctions against the new employer in the event of a breach of a post termination restrictive covenant by the employee of the former employer? Is it a matter of unfair competition in your jurisdiction?

There are no possible legal sanctions in India available against the new employer in the event of a breach of a post-termination restrictive covenant by the employee of the former employer.

The liability lies on the employee to ensure that when he leaves a particular enterprise and joins a rival enterprise, the confidential information or the business security of the enterprise is not compromised. The employee also has to adhere to

the non-solicitation clause if it is imposed on him through the employment contract.

Having said that, there may be a possibility where the prospective employer may be dragged into litigation, by taking the position that the new employer is encouraging and assisting the employee to breach his obligations towards the previous employer.

In order to avoid such scenarios, it is also helpful to obtain a representation from the new employee (whether under an employment contract or otherwise) that the employee has not and will not breach any obligations towards his previous employer, as a result of joining the employment of the new employer.

1.1.10. When an employer has invested money in an employee's training, is there any possibility for the employer to get a refund from the employee, in case of breach of the post termination restrictive covenant, and under which conditions?

The amount of damages to be paid to the employer on account of losses incurred by him due to an employee's violation of the employment bond/training bond should be reasonably calculated and decided by the Courts. The reasonable amount of compensation to be awarded to the employer will be based upon the training cost involved, the actual loss incurred by the employer, the time period for which the employee had served the employer and other facts of the case.

In the case of *Fertilizers and Chemical Travancore Limited vs. Ajay Kumar and Others*, the Kerala High Court held that the employer will definitely incur loss when a trainee breaks the conditions of the bond and walks off. The employer is deprived of the expected service of the competent person for which fresh selection and training may become necessary. Breach of a bond by a trainee is therefore an aspect involving damages to the employer. Only the question of quantum of damages then remains to be decided⁹.

In the case of *Sicpa India Limited v Shri Manas Pratim Deb*, the plaintiff had incurred expenses of INR 67,595 towards imparting training to the defendant for which an employment bond was executed under which the defendant had agreed to serve the plaintiff company for a period of three years or to make a payment of INR 200,000. The employee left the employment within a period of two years. To enforce the agreement the employer went to the court, which awarded a sum of INR 22,532 as compensation for breach of contract by the employee. It is crucial to note that though the bond stipulates a payment of INR 200,000 as

⁹ 1990 LLR 771

compensation for breach of contract, the judge had considered the total expenses incurred by the employer and the employee's period of service while deciding the compensation amount. Since the defendant had already completed two years of service out of the agreed three years period, the judge divided the total expenses of INR 67,595 incurred by the plaintiff into three equal parts for the three years period and awarded a sum of INR 22,532 as reasonable compensation for leaving the employment one year before the agreed time period.¹⁰

1.1.11. What are the possibilities of lawsuit for the employee in case of the employer's disadvantageous actions during a period covered by a restrictive covenant (e.g. the employer prevents the employee from finding a new job by spreading out rumours)?

The employee can file a criminal suit under Section 499 and Section 500 of the IPC against the employer on charges of defamation.

1.2. Garden Leave

1.2.1. Does the concept of "garden leave" exist in your jurisdiction? How does it work, what is the scope and what are the prerequisites?

Although such clauses find place in some of the employment contracts in India, such clauses are usually being viewed as restraint in trade, etc. under section 27 of the Act. As discussed in the case of VFS Global Services Private Limited, the garden leave clauses are treated as restraints of trade and are hit by Section 27 of the Act.

The courts in the country have not appreciated the inclusion of the clause of garden leave by employers in their employment agreements as it has been considered to violate the fundamental right to profess any lawful trade, business or profession.

This clause in an employment agreement does not seem to protect the employer when it comes to Court of law; as they are considered to be agreement in restraint of trade under Section 27 of the Contract Act and does not allow the person to pursue any lawful trade, business or profession in the light of Article 19 (1) (g) of the Constitution of India.

1.2.2. Talking about garden leave provisions: do employees – or certain types of employees – have a right to be "actively employed" in your jurisdiction, e.g. so that a garden leave provision would not – or not be fully – be enforceable

¹⁰ MANU/DE/6654/2011

for an employer and the employee would have a “right” to continue working until the end of the employment? What is the respective legal framework in your jurisdiction?

Being hit by section 27 of the Act, garden leave clauses are not enforceable in India and hence, the employee has the right to be actively employed.

1.3. Are there any other specific means to protect the employer’s interest at the end of an employment contract in your jurisdiction? Please explain in detail and provide for practical guidance.

As explained above, an employer has every right to file a suit against his employee if he suffers loss in his business on account of employee’s disclosure of confidential information relating to his business, or his solicitation of employer’s clients with a specified time period as mentioned in the employment agreement.

The employer may file such a case against the employee before the Civil Court having the appropriate jurisdiction to seek injunction, specific performance and reasonable damages.

The Court shall award reasonable amount of damages to the employer depending upon the amount of loss incurred and facts of each case.