

JOURNAL FOR LAW STUDENTS AND RESEARCHERS

CURRENT LEGAL POSITION OF NON-COMPETITION AND NON-SOLICITATION AGREEMENTS IN INDIA

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INTRODUCTION

Non-competition and non-solicitation clauses are the restrictive covenants in contracts. A non-compete agreement restricts a former employee from competing against a former employer for a specified amount of time. They are covenants which prohibit the employee from joining any other competing business during and/or after the contract of employment. For instance, if an employee worked with a company for 10 long years and had mastered the art of developing a certain software or product during the course of employment and if he's now willing to start his own firm, but he's prohibited from doing it because of a clause, that particular clause is called as a non-competition clause. On the other hand, a non-solicitation clause prevents an employee or a former employee from indulging in business with the company's employees or customers against the interest of the company. A non-solicitation clause bars a former employee from inducing the customers and employees of the former employer to his own benefit. For example, an employee agrees not to solicit the employees or clients of the company for his own benefit during or after his employment.

These non-compete and non-solicitation agreements as mentioned in the earlier paragraph are the restrictive covenants in contracts. The companies (employers) defend themselves saying that such agreements are necessary to protect their trade secrets, confidential information etc. When we look at Indian Contract Act of 1872, nothing is explicitly mentioned about these restrictive covenants. The law outlined under Section 27 of the Indian Contract Act says that "every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void". But, with the change in times and with an increase in the competition levels, non-competition, confidentiality and non-solicitation agreements came into picture. A large number of companies are using these clauses in the employment agreements because of the growing competition.

This essay seeks to analyze to what extent the non-competition agreements and non-solicitation agreements are valid. It deals with the judicial developments to these restrictive covenants in India.

This research is based on the secondary method of research. The information has been taken from previous works such as research papers and articles.

COMPARATIVE STUDY

The validity and enforceability of the non-compete clauses and the non-solicitation clauses differ from country to country. In foreign judiciary subject to certain limitations and reasonable boundness, the non-compete agreements are declared to be enforceable to the reasonable extent.

WITH RESPECT TO USA:

In USA, unlike the law stated under Section 27 of the Indian Contract Act which says all agreements in restraint of trade are void, the Courts in most of the American jurisdictions apply the test of reasonableness in determining the enforceability of non-compete agreements which are also similar to the law in England. The test of reasonableness depends on the duration of the restriction, the geographical scope of the restriction and the substantial nature of the activity being restricted. The Courts in USA use blue pencil doctrine where they delete the offending terms in the agreement and render the non-compete clause enforceable¹. They also use reformative approach where they rewrite the term of duration they find excessive so as to make the non-compete clause enforceable.

WITH RESPECT TO UK:

In general, the courts in the U.K. are not in favour of enforcing restrictive covenants operating beyond the termination of employment unless there's a valid and reasonable say. The chaos-free thing with respect to the enforcement of restrictive covenants in U.K. is incorporation of garden leave clauses in the employment contracts. Keeping the employee employed and payrolled but excused from job duties for the entire non-compete period is a 'garden leave'. In fact, enforcement of such clauses is easier than enforcement of restrictive covenants.

JUDICIAL PRONOUNCEMENTS

Coming to the legal scenario, Indian courts have consistently refused to enforce post termination non-competition clauses in employment contracts as "restraint of trade" is not permissible under Section 27 of the Indian Contract Act, 1872, and have held them void. But, considering the developed social, legal and technological circumstances, the courts have started considering the non-competition and non-solicitation agreements. In a landmark case

¹ Ujjwal Ashok, "Validity and Enforceability of Non-Compete clauses under Indian Law", https://blog.ipleaders.in/non-compete/#_ftn14, 10th November, 2017

of *Niranjan Shankar Golikari v. The Century Spinning and Manufacturing Company Limited*², the Supreme Court of India observed that restraints or negative covenants in the appointment or contracts may be valid if they are reasonable. It was held that where an employee has agreed to work for an employer for a specified period of time but resigns from the employment prior to the completion of such specified period, in breach of the terms of the contract, a non-compete clause operating during the term of the contract may be enforceable for the remaining unserved period.

In another case of *Percept D'Mark (India) Pvt. Ltd. v. Zaheer Khan and Anr*³, Zaheer Khan entered into an agreement with the appellant for promotion advertisement for 3 years. After 3 years, he entered into agreement with the second respondent. The appellant filed a petition for interim order and injunction against Zaheer Khan. The Court held that the clause does not restrict Zaheer Khan from entering into any contract with third party. If negative covenant under the clause mentioned is sought to be enforced beyond the term then it is unlawful restriction on Zaheer Khan's freedom to enter into fiduciary relationship with persons of his choice. It was also held that any compulsion on him to forcefully enter into fresh contract with appellant would be restraint of trade and void under Section 27 of Contract Act. The Supreme Court further went on to observe that the doctrine of restraint of trade is not confined only to contracts of employment, but is also applicable to all other contracts.

There are certain non-solicitation clauses which do not amount to restraint of trade, business or profession and would not be subject to Section 27 of the Contract Act. This was held in *Wipro Limited v. Beckman Coulter International S.A.*⁴ In this case, the petitioner worked as a sole and exclusive canvassing distributor for respondent for 17 years. The respondent decided to undertake direct operations in India and issued an advertisement seeking employment from people and giving preference to candidates having experience in that field. The petitioner alleged that advertisement was in violation of non solicitation clause and approached court for prohibiting solicitation and claiming damages. The court held that the restriction was not on the employees and the non-solicitation clause by itself did not put any restriction on employees. Also, the non-solicitation clause did not amount to a restraint of trade, business or profession and under Section 27 of the Indian Contract Act, 1872. And thus the agreement was held not in restraint of trade. The key points laid down in this judgment are:

² AIR1967SC1098

³ AIR2006SC3426

⁴ 2006(3)ARBLR118(Delhi)

- Restrictive covenants during the subsistence of a contract would not normally be regarded as being in restraint of trade, business or profession unless the same are unconscionable or wholly one-sided.
- Post-termination restrictive covenants restricting an employee's right to seek employment and to do business in the same field as the employer would be in restraint of trade and therefore void.

There's another landmark case *Pepsi Foods Ltd. and Ors. v. Bharat Coca-Cola Holdings Pvt. Ltd. and Ors*⁵, in which it was held that the "post termination restraint" on an employee is in violation of Section 27 of the Indian Contract Act, 1872.

In other landmark case *Embee Software Private Ltd. v. Samir Kumar Shaw & Ors*⁶, the question arose whether the respondents would allow soliciting the clients of the plaintiff so as to induce them to break their contract or their legal relationship with plaintiff or prevent them from entering into a contractual relationship with plaintiff. But, the court held that inducing a person to break a contract with another or preventing a person from entering into a contract with another was a tort. If the act of soliciting took such a turn that it induced customers of plaintiff to break their contract with plaintiff, such acts will not be permitted. Also, in the case of *FL Smidth Pvt. Ltd. v. Secan Invescast (India) Pvt. Ltd*⁷, the court held that the negative covenant of the agreement can be enforced only during the period of contract and that the same cannot be enforced after the expiry of the agreement period. It says that approaching customers of a previous employer does not amount to solicitation until orders are placed by such customers based on such approach.

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CONCLUSION

The current legal position with respect to the non-compete and non-solicitation agreements in India is clear on one point, that is, the courts through various judicial pronouncements have upheld that non-compete clauses operating after the termination of the service of the employee are not enforceable in India. Though they are valid and enforceable in other countries, they are not valid in India. But the recent judgments show that the judiciary is tending to validate the non-compete clauses/agreements only when they are reasonable. Here, the term 'reasonable' means whatever a normal person would do using common sense and knowledge, under the given circumstances.

The post term restrictive covenants have been held invalid through the judicial pronouncements. The employer cannot protect himself against the competition on part of an

⁵1999VAD(Delhi)93

⁶ AIR 2012 Cal 141

⁷ 2013(1)CTC886

employee even after his employment came to an end. Though Section 27 of the Indian Contract Act says that all agreements in restraint of trade are void, the recent judicial pronouncements lead to a conclusion that reasonable restraint is permitted and does not render the contract void ab initio.

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