

GUIDANCE

RESTRAINT COVENANTS IN CONTRACTS OF EMPLOYMENT

RESTRAINTS

- × Not to set up any business on own account
- × Not to join competition/rival firm
- × Not to conduct any trade/business/occupation except that with the employer
- × Not to disclose trade secrets and confidential information

Restraint during employment

An agreement of service by which an employee binds himself, not to compete with his employer, directly or indirectly, is not in restraint of trade. However, it may also be subject to the doctrine of restraint of trade, if the restraints are such that one of the parties is so unilaterally fettered that the contract loses its character of a contract for the regulation and promotion of trade and acquires the predominant character of contract in restraint of trade.

Restraint after employment

A service covenant extending beyond the term of service is void. The negative covenant in a contract of employment placing a restraint on the employee that he shall not serve in any other competitor's firm for 2 years at the place of his last posting after the employee left the Company, would be void. A 'garden leave clause' operating after the termination of employment is also void. But a term restricting an employee from disclosing trade secrets and confidential information after ceasing employment can be enforced.

LEGAL PROVISIONS

Article 21 of the Constitution of India guarantees the freedom to livelihood and since it is a fundamental right it is held to be inviolable.

Section 27 of Indian Contract Act, 1872: Every Agreement by which anyone is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void. *Saving of agreement not to carry on business of which good-will is sold.*

Enforceability of restrictive covenant does not extend to :-

- × Business of employer other than the employee was employed in
- × Associated or subsidiary companies in which employee did not serve
- × Use of employee's own knowledge, skill or experience (even if acquired during the course of employment)

Restrictive covenant enforceable :-

- ✓ Protection of trade secrets, business connections and confidential information
- ✓ Protection against competition in cases of sale of goodwill/business
- ✓ Reasonable and consistent with the interest of the public

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