

POST EMPLOYMENT RESTRICTIVE COVENANTS- HOW MUCH ENFORCEABLE?

JUNE 2018

Our newsletter covers – Enforcement of Post Employment restrictive covenants including serving notice period, non-compete, non-solicitation etc.

The legislations governing several aspects of the employer-employee relationship are so complicated and ambiguous, that they yield in litigation rather than to provide clear way out. Moreover, the most important bone of contention w.r.t. protection of confidential information, non-disclosure and non-solicitation have not yet been addressed through legislation in India, thus warranting recourse to judicial interpretation and common law.

In an attempt to protect their interests, trade secrets, confidential information, every employer execute employment agreement and impose post employment restrictive covenants pertaining to manner in which the employees are required to serve the notice period, comply with the exit formality, non-solicitation, non-compete and others before finally exit from the employer.

However, to enforce post employment restrictive covenants had become a challenging task for the employers. In our June 2018 Newsletter, we seek to provide an overview of the steps to be adopted by the employer and how to address a conflict situation with its employees and to enforce post employment covenants.

Employer's- Legal Recourse & Future Course of Action

1. Pre- Conflict/Litigation- Course of Action:

At this stage, following documentation and course of action to be adopted to prevent/reduce any future conflict or issue with the present/future employees:

- a. **Execution of Employment Letter** which includes but not limited to exit mechanism; post-employment restriction and covenants; non-compete; non-solicitation; confidentiality obligation, IP protection. The post employment restrictive clause need to be draft with a balance keeping in view of Section 27 of Indian Contract Act and recent judicial approach. As Section 27 of the Indian Contract Act, prohibits any kind of unreasonable restraint on trade, employment and profession.*
- b. **Non-Circumvention & Non-Disclosure Agreement**- An Additional protection layer for securing the interest of the Company including confidentiality, non-solicitation, IP and data protection.*
- c. **Service Bond**- To include additional penalty clause for violation of IP; non-compete; non-solicitation; confidentiality; data; trade secret; client details.; post employment covenants; to join/engage any company or indulge in any competitive business only after no dues clearance and formal exit from the employer.*
- d. **Employee Handbook**- Beside general employment conditions it shall include but not limited to exit mechanism; imposing garden leave; post employment covenants; clearance of any investigation prior to exit from the Company.*

2. **Upon Breach of Terms of Employment:** *Separate Legal Notice to employee & new employer for breach of terms of conditions including but not limited to non-compete & non-solicitation. Also, a Cease & Desist Letter for tortious interference in business to new employer for “**using the ex-employee**” for violation of breach of terms including but not limited to non-compete; non-solicitation, data & IP.*
3. **Litigation:** *On the event of failure of the above-mentioned course of actions, the employer should initiate a litigation with keeping mind of the following points:*
 - a. *File a criminal/civil suit against the ex-employee depending upon the breach of terms and violations along with filing a police complaint depending upon the facts of the conflict;*
 - b. *File a criminal/civil suit against the new employer of ex-employee.*

*In general, a question is always raised by the companies/employers that- “**whether a suit or any action can be initiated against the new employer of the ex-employee of the Company, who had breached the terms of his employment & post employment covenant with the Company.**”*

On review of past decisions made by Supreme Court and other High Courts, in several adjudicated matters, new employer had been successfully sued in Court of Law, where the new employer is aware of the breach of terms & violations by its new employee (ex-employee of the Company). The new employer can be sued for tempting, luring and assisting ex-employee to breach a contractual obligation and shall be held liable for interference of contractual relationship between ex-employee & the Company.

Enforceability of Notice Period

*For serving notice period, in one of the case, **Chairman and Managing Director, India Airlines vs. Binod Kumar Sinha and ors., AIR 2001 SC 3988** hon'ble Supreme Court has held that – “An employee when joins service is subject to certain terms and conditions of service and he cannot quit the employment without giving requisite notice to the employer. But what should be the duration of a reasonable notice in such circumstances is a matter to be decided in each case depending upon the exigencies, needs or necessities and the essentiality of the service concerned.”*

Other decisions by hon'ble Supreme Court:

- 1. Thus, if an employee does not serve the notice period by working for the duration of the notice period, the employer may not have a decree from the court asking specific performance of the covenant to the effect that the employee would have to work for the notice period duration. But instead as a remedy to the employer, the court may grant damages for breach of contract.*
- 2. Since enforceability of the notice period is not an option available with the employers, and they may only claim damages in case of illegal termination of employment contract by the employee, it is pertinent to understand the extent of damages that can be claimed.*

*Moreover, in some of the earlier cases adjudicated at High Courts & Supreme Court, it has been held by the learned Courts that- “**A reasonable restriction on non-solicitation for carrying on business or employment with new employer by utilizing the list of clients/customer is valid.**”*

Compensation for Not Serving Notice Period

- 1. In relation to employee abruptly leaving the Company (without serving the notice period), Andhra Pradesh High Court in the matter of Satyam Computer Services Limited v. Ladella Ravichander, MANU/AP/0416/2011 held that- “such action by the employee did not cause any damage or loss to the Company and it would be unreasonable to acquire ₹ 2,00,000/- from employee. An amount of ₹ 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.”*
- 2. In one of the leading case, Union of India and Anr. vs. Tulsiram Patel and Ors., AIR 1985 SC 1416 w.r.t. compensation & enforceability of notice period, the hon'ble Supreme Court has held that- “Whether the contract of service is for a fixed period or not, if it contains a provision for its termination by notice, it can be so terminated. If there is no provision for giving a notice and the contract is not for a fixed period, the law implies an obligation to give a reasonable notice. Where no notice in the first case or no reasonable notice in the second case is given, the contract is wrongfully terminated and such wrongful termination will give rise to a claim for damages.”*

To prove tortious interference against the new employer, following points need to prove:

- a. A valid non-compete exists between former employer and employee;*
- b. The hiring employer had knowledge of the non-compete;*
- c. The hiring employer caused a breach of the non-compete by hiring the employee;*
- d. The hiring employer has no legal justification for causing the breach;*
- e. The former employer has realized the*

In addition to the above options, what steps can employer take in advance to protect against a breach by an employee?

- ✚ Review your standard contractual documentation to ensure that it operates as effectively as it can to protect your business.*
- ✚ Consider amending restrictive covenants to be sure (i) that they apply both during and after the employment and (ii) that they go no further than is reasonably necessary to protect your legitimate business interests. If they go further than is reasonably necessary, employer will not be able to enforce them.*
- ✚ Review confidentiality restrictions to ensure that they specifically protect the types of confidential information which are key to your business.*
- ✚ Consider whether to include within the contracts of employment of your senior employees an express duty of disclosure of matters which are averse to your interests. An express duty tends to be easier to enforce and will act as more of a deterrent to employees.*
- ✚ Check that your standard contracts of employment include a garden leave provision. A garden leave clause can give the employer the right to put an employee who is on notice of termination on garden leave and to prevent him from attending premises, contacting clients or undertaking any business activity.*
- ✚ Ensure that the contract makes clear that the length of any post-termination restrictive covenants inclusive of garden leave clause.*

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To know further details and other legal aspects of enforcement of restrictive post employment covenants and to get your employees to serve the notice period along with compliance of non-compete & non-solicitation or any clarification, please contact us at admin@equicorplegal.com/ +91 8448824659

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