

Application of the Doctrine of Restraint of Trade in Employment Contracts: A Dichotomy between English Law and Indian/Bangladeshi Law and Its Potential in Outsourcing Contracts

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Abstract: *The doctrine of restraint is no more confined to the entrenched words of the sections of the Contract Act, 1872. It has travelled beyond by encompassing the reasonableness doctrine within it. However, the development is still in its rudimentary state in context of Bangladesh as very few cases are dealt with by the Bangladeshi Courts on this issue. As a result, we do not have enough legal premises to make an in-depth analysis of the applicability of the doctrine in our perspective. However, the Grameenphone Ltd vs Chairman case in the First Labor Court has opened a new dimension on this issue through anatomizing an outsourcing contract. It has provoked us to think again of the application of restraint of trade doctrine in employment contracts. But before delving into the matter with a research methodology, we need to know more about it since the texts on the issue of outsourcing are still nascent. The aim of the article is to introduce to the reader the developments of the doctrine of restraint of trade and contextualize it in Bangladesh's context.*

1. Introduction

Freedom of trade is a recognized fundamental right in our Constitution (The Constitution of the People's Republic of Bangladesh). The framers embodied the right in article 40 of the Constitution, Part III, under the title of "Freedom of profession or occupation". Nobody has the right to restrain any person from carrying on his own business, trade, or profession. The Contract Act 1872 respects such right of a person to trade freely. On the other hand, the law also recognizes a person's ability to contract. It is said that every competent person under law is free to enter into a contract with any other person.

The conflict arises when a person enters into a contract to restrain another from performing their lawful trade, business or profession. The two parties have applied their right to enter into a contract with an object of restraint but have voluntarily given up their fundamental right of freedom of trade, business, profession or occupation. The state has an active interest in the continuance of trade, commerce and profession, as it satisfies the needs of consumers, prevents

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monopoly, preserves a competitive environment, and increases revenue to the government fund. This means that freedom of trade is also a public policy. The question then stands: can a court respect such a contract that is voluntarily entered into by competent parties but violates public policy?

The first part of this discussion will involve the Common Law approach of treating a restraint covenant in employment. In the second part we will discuss the aspects of Indian laws, Which our court follows as well, comparing it with the Common Law approach. Then we will go on discussing the developing jurisprudence in this scenario.

2. The Common Law Approach

Common Law Approach gives a non-exhaustive list to the application of the doctrine of restraint of trade. It is because the approach involves the doctrine of “reasonableness” which makes the contract flexible and adaptive to the contemporary world. The Courts in England would rather go over the cases on a ‘case-to-case’ basis to rule out the contracts made in restraint of trade which is not reasonable in an objective standard.

The approach did not exist in the era of Queen Elizabeth, but came into existence later on, keeping in mind the progress of society. The reason why the current approach was not appreciated in Queen Elizabeth’s era is the fear that allowing such restraint in contract may allow monopoly to develop.¹ However, it was noticed that these covenants were essential to carry on business as well. For example, we can take an example of the sale of goodwill², where the essence of the whole contract gets vitiated when such restrictive covenant is not allowed.

One of the oldest case examples in *Mitchel v Reynolds* illustrates this fact. It recognizes that the restrictive covenant must be useful to both parties, otherwise, a contract that is one-sided in its terms must be set aside. It goes on as:

“[W]herever a sufficient consideration appears [to make it a proper and useful contract, and such as cannot be set aside without injury to a fair contractor, it ought to be maintained; but with this constant diversity, viz, namely where the restraint is general not to exercise a trade throughout the kingdom and where it is limited to a particular place; for the former of these must be void, being of no benefit to either party and only oppressive”³

¹ Furmston MP, Cheshire GC and Stuart FCH, ‘Contracts Void at Common Law on Grounds of Public Policy’, *Cheshire, Fifoot and Furmston’s Law of Contract* (Oxford University Press 2012)

² J Beatson, A Burrows and J Cartwright, ‘Common Law and Statutory Control of Anti-Competitive Agreements’, *Anson’s Law of contract* (29th edn, Oxford University Press 2010)

³ *Mitchel v Reynolds* [1711] 1 PWms 181.

However, the most important principle on this doctrine was laid down in *Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co. Ltd*⁴. It has not only affirmed *Mitchel v Reynolds*, but also recognized the contract oppressive to either party as void contract.⁵ But more importantly, the case has laid down a test for considering whether a contract is valid or void by following two steps. The judgement of Lord Macnaghten delineates two layers for testing reasonableness. They are:

1. The restriction is reasonable in reference to the interests of the concerned parties. The covenant must be useful for the benefit of both the covenantee and the covenantor. If it is one-sided, the agreement will be void.
2. The restriction is reasonable in reference to the interests of the public. Sanctity of contract, though highly respected by the Courts, turns futile before the interests of the people. The Court will always weigh the interests of the people more than the interests of the parties. However, Court will as far as possible respect the contract entered by the parties and then look to the public interests as far as possible.

What Macnaghten's test did was to find a balance, or a point in between the interests of the parties— which is essential for both the parties to survive their business or trade as opposed to undermining it.

3. Restrictive Covenant In Employment Contract

Let us now consider the application of the doctrine in employment contracts. The employer agrees to employ a candidate. In return, the employee agrees to restrict himself in terms of time, space and purpose/capacity to work in another employer's firm/company. Therefore, the covenant is restrictive in nature in relation to the employee's business. Hence it falls within the scope of the doctrine of restraint of trade. If the covenant were scrutinized by the Courts in earlier times (for example, in Elizabethan era), it would be rendered void. The picture, however, is not the same today.

Modern business is built upon specialization of work, with employers providing training to the employees to specialize them for their job and increase their efficiency. The employer has an interest in protecting these trade secrets and confidential information, because if they are not protected, no business firms will dare to provide training or special information to the employees. Additionally, the employees come in touch with the customers in the course of employment and create a bond with them, which the employer has invested in. If the employee is allowed to take away the customers the employer's firm has a good relationship

⁴ *Nordenfelt v Maxim Nordenfelt Guns and Ammunition Co Ltd* [1894] AC 535

⁵ *Ibid*

with, a lack of trust between the employer and employee should arise, leading to a fall in the employment rate.

Thinking reversely, the employee too has an interest, although indirect, in the restrictive covenants.⁶ In return for the restraint upon them, they are assuring the employers that they will not carry away with the trade secrets or confidential information, nor will they solicit their customers. This trust allows them to receive training and the benefit of receiving necessary information from the employer's firm to deal with the customers or to utilize the tools or machinery used in the firm.

Therefore, the key is to balance the interests of the employer and the employee in scrutinizing an employment contract. To balance the interests Courts often take help of reasonability doctrine. Reasonability does not imply a blanket rule and it differs from case to case. However, there are multiple factors that the Courts consider in holding whether the restriction is reasonable or not. We can take a few examples.

3.1. Whether the Employer Has a Legitimate Interest

The legitimate interests of the employer are those which the employer wants to save in order to protect the distinctiveness of products or even to survive in the market. However, legitimate interests do not include the interest to prevent competition. Instead, legitimate interests include- trade secrets, confidential information of customers, goodwill of the business or relationship with the customers. These interests are in the jurisprudential sense, 'proprietary interests' of the employer. If they are lost, the firm may collapse or drop out of the market. Therefore, it is reasonable to protect such interests through restrictive covenants by the employer. Nonetheless, if the restriction imposed by the covenant does not cover any legitimate interest, such portion of the covenant will be void.

*Herbert Morris Ltd vs Saxelby*⁷ can be a good example to illustrate the fact. The employee, Saxelby, was an engineer specialized in a field of work who used to work for a hoisting machinery manufacturing company. There was a restraint covenant in his contract that prevented him from working in any similar business for 7 years after leaving. This restraint did not cover the jobs he did for the company but also restricted him from doing jobs in the general field of engineering. It was held that the restrictive covenant was void pro tanto because the employer company did not have any proprietary interest in other fields of engineering which can be acquired by the employee through his own efforts. Additionally, such restrictions will put the employee to idleness or force him to

⁶ *Herbert Morris v Saxelby* [1916] 1 AC 688 (AC)

⁷ *Ibid*

seek employment from the former firm, as it is the engineering profession which he lives on. However, if the employer has legitimate interest in the employee's working skill, then it will be considered as a valid restraint.

A recent example can be drawn from the case of *Hanover Insurance Brokers Ltd*⁸. This case involved a brokerage named Hanover Insurance Brokers. Hanover Insurance Brokers was a subsidiary of a company named Hanover Associates. In the contract deed, there was a 'non-soliciting clause' that prevents the covenantor from soliciting clients from their former firm. Three directors who worked only for Hanover Insurance Brokers left and set up their own firm. They were accused of soliciting the clients of their former firm. Their objection was that the covenant was too wide and therefore void. The Court held that the covenant was void as to the restriction against soliciting clients from Hanover Associates and its subsidiaries except Hanover Insurance Brokerage. In other words, only the restriction against soliciting clients from their former firm, was held valid.

3.2. Whether the Restraint is Limited to Time, Space, and Subject-matter

For a restraint to be reasonable, it must be limited to time, space and subject matter. If the restraint is not limited to time, space and subject matter, it will become absolute. The problem with imposing absolute restraint is that it confines the employee to sheer idleness and prevents him from utilizing his self-earned skills. Again, time and space are also important factors in examining the validity of a restrictive covenant. A restraint as to time itself must be reasonable. Because a restraint exceeding a limited time limit will result in preventing competition with other firms. But an employer is not entitled in law to protection against competition. Therefore, such restriction for an unreasonable amount of time is void. The same theory goes for space too.

An interesting example can be drawn by *Fitch v Dewes*⁹ case. Unlike the other covenants held as reasonable, it was exceptional. Because the Court held the covenant as valid even though the period for restriction was unlimited. The reason was that the area involved in the case was rural. The employee was in fact a solicitor's clerk. Because of living in a rural setting, there were only a limited number of clients. Moreover, these clients were also in contact with the clerk. Allowing the clerk to operate in the same capacity would be harmful for the employer's own business, because the employee knows the details about the clients which the employer must keep secret. That is why the Court holds such unlimited restriction as to time as valid.

⁸ *Hanover Insurance Brokers Ltd and Christchurch Insurance Brokers Ltd v Schapiro* [1994] IRLR 82

⁹ *Fitch v Dewes* [1921] 2 AC 158

In *Mason case*¹⁰ the Court examined the limitation as to locality. In this case, the employee was restrained from working in a similar business within 25 miles of London. It was held as void, because the employer did not have any legitimate interest in protecting beyond the periphery of London, where the business was situated. If the employee worked beyond London, the employer would be faced with no harm at all. Restricting him instead will put the employee into idleness, which goes against the public policy. Therefore, it becomes evident to us, that the primary factor determining the validity of a restrictive covenant in English law is determined by “reasonableness”. The restraint, if held as reasonable will be valid in law, even if it operates post-employment.

4. The Indian Approach

India, at that time when the Contract Act 1872 was enacted, was hardly an industrialized country. In fact, it was ruled under a feudal system where land used to be the primary tool for production of goods. The British rulers undertook the policy to industrialize India as quickly as possible. To this end, they had to free the market and guarantee the ease of making a contract. To realize the policy, a law had to be passed in order to make it simple for any competent person to enter into a contract with another. To that effect the colonial rulers passed the Contract Act 1872. The doctrine of restraint of trade in India is grounded upon this historical context.

The section discussed in the article was actually taken from New York Draft Code as has been mentioned by Pollock and Mulla¹¹. In opposite to the erstwhile common law principles, the Code narrowly accepted the application of restraint of trade by rendering all restraint of trade, whether partial or general, void. India, and today’s Bangladesh has been following the same principle. However, it was recommended by the Indian Law Commission’s 13th Report¹² on Contract Act 1872 to amend the Act adding the wording “reasonableness” to it. However, the legislators have not yet amended it and the Courts in India and Bangladesh has to follow the antiquated precedents where all restraint of trade are held void.

4.1. *Diversification from Common Law Principles*

The leading precedent in Common Law during the enactment of the section in Contract Act was *Mitchel v Reynolds*¹³. What we understand from this case is that to justify the validity of an agreement in restraint of trade, we are required to show the following ingredients:

¹⁰ *Mason v Provident Clothing and Supply Co* [1913] AC 724

¹¹ Pollock and Mulla, *Indian Contract and Specific Relief Acts* (4th edn, Sweet and Maxwell 1919)

¹² ‘Thirteenth Law Commission’ (*India*) <https://lawcommissionofindia.nic.in/report_thirteenth/> accessed 15 June 2023

¹³ Above n 3

- i. That the agreement was made with sufficient consideration so that:
 - a. it does not become oppressive to any of the party.
 - b. it becomes beneficial to both parties involved.
- ii. The agreement must be qualified as to time and place, otherwise the agreement will be void.

The Court put an extra emphasis on the judgement of consideration. They observed that it is the sufficiency of consideration that justifies the validity of the agreement in restraint of trade. At the same time, the judges were careful to scrutiny whether the agreement was itself restraint to a certain period of time, or a certain place, unless such limitation too creates a monopoly. In short, the Court ruled that a restraint agreement must not create a monopoly on entering business or limit the choice of vendors for obtaining the best product or service. Partial restraint will be held valid, if found reasonable, and any effort to create a monopoly will be disregarded. Additionally, sufficient consideration must be paid to ensure the agreement is not oppressive to any party and benefits both.

In contrast to the English principle established in this case, the Indian Law of Contract deviates from the position taken in *Mitchel v Reynolds*. The English Law had validated the agreement in restraint of trade limited as to time and space, made with due consideration. But section 27 of Contract Act 1872 does not have any mention of “partial” restraint. The question remained whether the section validates the restraint agreement that are partial and limited to time and space, or all the agreements in restraint of trade are void under the purview of section 27.

The same issue was dealt with in *Madhub Chunder*¹⁴ in 1874. It showed that the scope of allowing an agreement in restraint of trade in India is narrower than in English Law. In India, all agreements in restraint of trade will be held void due to the strict wording of the section and the deliberate omission of the word “absolute”. The Court observed that, if the legislators had intended to save partial restraint of trade, they would not have added an exception of allowing partial restraint of trade in case of sale of goodwill. It would have been unnecessary. More importantly, if we look at the next section, that is section 28 of Contract Act 1872, we can see that the legislators have used the word “absolutely” to define the periphery of the section. It is held that if the legislators had in mind to allow partial restraint of trade, then they would have put it in the section just like section 28. It can be inferred that the omission of the word “absolute” was deliberate, and the legislators did not want any sort of agreement in restraint of trade to be valid in Indian jurisdiction.

The reason for such strict nature of Contract Act 1872 in relation to restraint of trade lies in the historical background of India at that time. To mention it here

¹⁴ *Madhub Chunder v Rajcoomer Doss* (1874) 14 B.L.R. 76

again would be a mere restatement and unnecessary redundancy. In this regard, the observation of Kindersley J will be of greater use to explain the underlying rationale of the section. He categorically emphasized that “the goal of section 27 is to protect trade. That is why the legislators have been strict about nullifying all agreements in restraint of trade to that extent”.¹⁵

This principle was then reaffirmed in *Sheikh Kallu vs Ramsaran Bhagat*¹⁶. It was observed that the rule expressed in Section 27 of the Contract Act differs from the rule iterated in the case of *Nordenfelt*¹⁷ on the topic in an almost shocking way. In the same tone of Sir Richard Couch in *Madhub Chunder*¹⁸ case, Mukherjee J held that any agreement in restraint of trade, whether partial or absolute, qualified or unqualified will be void to that extent.

Interestingly, the Court did not restrict itself only in the position taken in *Madhub Chunder*¹⁹ but viewed the contention of the respondent as to reasonableness liberally. The Court also used the reasonability test taken in *Nordenfelt*²⁰ finding that the agreement of restraint of trade in this case is larger than necessary and therefore oppressive. The Court found that the agreement in *Sheikh Kallu*²¹ ranged from generation to generation and was unrestricted as to time and place. Therefore, the restraint must be unreasonable. Therefore, Indian courts have accepted the age-old strictness of Elizabethan era in holding agreements in restraints void, even if they are reasonable, despite the development of the common law principle in *Nordenfelt*.²²

4.2. Application of Section 27 in Employment Contract

The general rule enshrined in section 27 does not apply to employment contracts. In this case, the Courts have innovated an exception to the case in employment contracts through interpretation. It is true that the sort of covenant employed in the deed is a covenant for restraint of trade. But if this sort of covenant is not enforced, then the Court will have to nullify all other contracts of personal service too on the same ground²³.

¹⁵ Oakes & Co. v Jackson [1876] 1 Mad 134, 145

¹⁶ Sheikh Kallu vs Ramsaran Bhagat 1 Ind Cas 94

¹⁷ Nordenfelt v Maxim Nordenfelt Guns & Ammunition Co Ltd [1894] 1 AC 535

¹⁸ Above n 14

¹⁹ ibid

²⁰ Above n 17

²¹ Above n 16

²² Above n 17

²³ Charlesworth v MacDonald (1898) 23 ILR Bom. 103

In an employment contract for rendering personal service, the employer receives from the employee the consideration of working only under him for a fixed period of time. Within this time, he cannot work for anyone else. This is the nature of this sort of contract. Such a restraint is natural for the enforcement of contracts of this sort. The whole concept of employment contracts will be nullified if the restraint on the employee is not imposed while he is working for the employer. The court held such restraint as not being a restraint of trade at all. In *Charlesworth v MacDonald*²⁴ the court refused to nullify the restrictive covenant in the employment contract due to the fact that contracts of personal service for a fixed period do not fall within Section 27. Therefore, it seems that the validity of restraint covenant in employment contract is basically a judicial interpretation. The legislators indeed intended to bar restraints imposed for other reasons than rendering services to the employer.

Moreover, in this sort of employment contract there is a delegation of personal skills and knowledge and sharing of confidential information and trade secrets upon which the employer has his/her legitimate interest. Such contracts will become meaningless if the employer is disabled from restricting his employee from working otherwise.

Indian courts have handled restrictive covenants in employment contracts differently from English courts. English courts have embraced the test of reasonableness,²⁵ while Indian courts have held negative covenants to be in restraint of trade if enforced beyond the employment period. The judgement in *Gujarat Bottling Co Ltd v Coca Cola Co*²⁶ can be called into the discussion. In this case, the Court has accepted the principle that it will enforce the restrictive covenant included in the contract if such restriction is inserted for the promotion of trade. In other words, the restrictive covenants, if it is proved to be intended for promotion of trade itself, that debar a person from exercising his lawful trade, business or profession is exempted from the effect of section 27.

The Gujarat Bottling Co Ltd case clarified that section 27 applies only when a contract's restraint is construed as one-sided, not when it aims to promote trade. It points to the fact that the Court has acknowledged the intention of the legislators was not to annul contracts of services in India, but to promote trade, commerce and business in India while enacting section 27. In fact, section 27 remains there to restrict a person's freedom to enter into contracts which may have ill effects on the trade and commerce of the country.

²⁴ *ibid*

²⁵ 'Void Agreements' (*Patna Law College*) <<https://patnalawcollege.ac.in/econtent/Void%20Agreements%20by%20Prabhat%20Kumar.pdf>> accessed 15 June 2023

²⁶ *Gujarat Bottling Co Ltd v Coca Cola Co* (1995) 5 SCC 545

Having said that, it needs to be mentioned that employment contracts become subject to section 27 under certain circumstances. The Court, although has not completely accepted the reasonability test as the English law, has limitedly applied the test to restraint of trade in employment contract as long as the contract subsists. That is, the Court can render an employment contract void on the grounds of restraint of trade (section 27) if it deems the terms of the contract to be unreasonable. However, unlike English Law, Indian Courts do not enforce restrictive covenants after the termination of contract even if the terms are reasonable. In other words, section 27 applies to all agreements of restraint after the termination of the contract and nullifies those through the application of the same.

It seems that nullity of agreements in restraint of trade in relation to employment contract is the general rule, enforceability being the exception. Because restraints in the employment contract are only enforceable if it fulfils certain criteria of reasonability before the court. Such reasonability will only be tested if the restraint applies during the subsistence period of the contract. For example, in *Gopal Paper Mills Ltd*²⁷ the Court refused to enforce the negative covenant because the contract was wholly one-sided. The employee was devoid of the power to terminate the same under any circumstance. The Court found the terms of the contract as giving excessive power in the hands of the employer, and thus it was considered a one-sided and unconscionable contract.

In an obiter in *Brahmaputra Tea Co Ltd*²⁸, in line with *Charlesworth v MacDonald*, the Court observed that an agreement of service which aims at serving a person exclusively for a definite period is a lawful agreement. Because such an exclusive service is essential for the fulfilment of such a contract. The Court also emphasized the importance of considering if a negative covenant is crucial for the employer's protection. It found the restraint in question necessary for safeguarding the employer's interests, making it enforceable.

*Niranjan Shankar Golikari*²⁹ is a landmark case while considering the application of restraint of trade. It is the first case where the Court has explicitly accepted the test of reasonability regarding negative covenants operative during the employment course. It has reaffirmed the principle taken in *Brahmaputra Tea*³⁰ by allowing restraint covenant during the employment period. But more importantly, the Court has commented that all restraints, whether general or partial, may be

²⁷ *Gopal Paper Mills Ltd v Surendra K. Ganesh Das Malhotra* [1962] 1 AIR Cal 61

²⁸ *Brahmaputra Tea Co Ltd v Scarth* [1885] 1 ILR Cal 545

²⁹ *Niranjan Shankar Golikari v Century Spinning & Manufacturing Co Ltd* [1967] 2 SCR 378

³⁰ Above n 24

valid if they are proved to be reasonable.³¹ It can be argued that the Court here has given more emphasis on freedom of trade over freedom of contract.

But in doing so, it has contradicted and deviated from the general position taken in Indian jurisdiction as we have seen in *Madhub Chunder*³², and *Sheikh Kallu*³³ where it was held that a restraint, whether general or partial, is void under a textual interpretation of section 27. On the contrary, the Court has gone far enough to allow both general and partial restraint if they are deemed reasonable. The Court said in this case that it can issue a limited injunction during employment, ensuring it's reasonable and necessary for the employer's protection. In order to be a reasonable restriction, the injunction itself must be restricted as to time, nature of employment and area. However, the position taken in *Niranjan Shankar Golikari* was not followed later.

In *Krishan Murgai*³⁴ the Court has stuck to the textual interpretation and followed the decision made in *Madhub Chunder*³⁵ case and *Sheikh Kallu*³⁶. It was reiterated that a restraint of trade whether qualified or general is void under section 27. However, the Court has recognized that a restrictive covenant is enforceable if that is operative during the employment period and not beyond that. At the same time, it held all restraints post-employment as void as that falls within restraint of trade as envisaged by section 27 of the Contract Act 1872. But it did not overrule the reasonability principle taken in *Niranjan Shankar Golikari*³⁷ case.

The Court, in recent times, has been liberal in handling cases of agreement in restraint of trade if it is operative during the employment course. However, the Court has widened the scope of allowing negative covenants operative during the employment period by validating all such covenants if proven reasonable and necessary for the interests of the employer and not against public policy through the *Niranjan Shankar*³⁸ case. But in the *Krishan Murgai*³⁹ case, the Court has annulled all post-employment restraint as restraint of trade, even if it is reasonable.

31 *ibid*

32 Above n 14

33 Above n 16

34 *Superintendence Company of India v Krishan Murgai* [1980] AIR 1717

35 Above n 13

36 Above n 16

37 Above n 25

38 *ibid*

39 Above n 27

4.3. *Dealing With Post-employment Restraints*

The Courts in India have always viewed restraint covenants applicable after the termination of contract as a restraint of trade hence nullified them. The Courts will hardly scrutiny the reasonability of the terms of the negative covenant applicable post-employment unlike the restrictive covenants operative during the employment period. Reasonability is one of the determining factors for a restrictive covenant while only an employment contract subsists. But the same covenants operative after the termination of the contract are always held as void by the Indian Courts no matter how reasonable the conditions appear to be.

Employers train their employees, and employees may gather special knowledge in regards of their field through working under the employer's agency. The employer has the right to protect such special knowledge, trade secrets and confidential information that are not available in the public domain⁴⁰. That is why negative covenants operating during employment are held valid before the Court.

Contrarily, post-employment negative covenants are held void as being in restraint of trade. Because, after the termination of the employment, the employee becomes free from discharging the duties imposed on him through the contract of personal service. Since the contract itself is dissolved, the restriction that inevitably followed from the contract loses its enforceability. Because such enforcement will necessarily prevent the employer from competition with other employment agencies. But protection from competition is not recognized by law as a legitimate interest of the employer⁴¹. The philosophical foundation of the doctrine of restraint of trade rests on the fact that any sort of restraint through an agreement causing prevention of competition in the market or creating a monopoly is a restraint of trade and should be held void.

One of the first cases that came up with the issue is *Brahmaputra Tea Co Ltd v Scarth*.⁴² The Court held that the condition by which the respondent was bound not to serve otherwise during the term of the employment was a valid restriction. But at the same time, the same restriction that was imposed after the termination of the contract (post-employment) was held void as being in restraint of trade. The fact that the restraint was partial and not absolute did not prevent the Court from holding the restraint void. Reasonability or limitedness of the scope of restraint shall hardly play a role in annulling the negative covenant imposed after the contract is over.

The case also differentiated the Indian position from the position held by Common Law. English law is familiar with contracts that reasonably limit

⁴⁰ American Express Bank Ltd. vs Ms. Priya Puri (2006) III LLJ 540 Del

⁴¹ Above n 25

⁴² 11 ILR Cal. 545

individuals from competing with former employers after their agreements end. If those are imposed for reasonable causes, English law enforces them. But with a clear reading of the section in Contract Law 1872, we shall not see such a practice finding a place as an exception to the general prohibition imposed by section 27. Such an omission indicates that the legislators did not intend to give legal effect to the practice in India.⁴³ The Court confirmed several principles taken in Common Law jurisdiction, such as *Kores Manufacturing Co Ltd*⁴⁴, which held that after the employee's employment has ended, the employer is not allowed to take any measures to prevent them from engaging in competitive behavior. This sets up the issue of whether the employer is preventing competition in the market as one of the key factors in determining a covenant in restraint of trade.

It seems that the Court actually pointed to the restraint applicable during the term of employment, and such restraints are not considered as restraint of trade in Indian jurisdiction. The ground of such reasonable restraint during employment period was derived from the English case of *Fitch v Dewes*⁴⁵ where it had been mentioned as a public policy to allow an employer to employ such employee through whom he can efficiently carry on his business and fearlessly instruct them in his trade and share the secrets with him without the fear of his becoming a competitor. During employment, employers have a legitimate interest in restraining employees to prevent competition. However, post-employment, such restrictions are viewed as restraints of trade. The question remains: does such an interest to prevent competition dissolves with the end of the contract, even if such post-employment restraint is imposed for a reasonable period? The Court has not yet come up with an answer.

However, the Court had agreed that injunction could be imposed on the employee only during the employment period, but the injunction must be restricted as to time, place and nature of employment. The reason being the distinction between 'restraint during employment' and 'restraint of trade'; where reasonable restraint during employment has not been considered at all as restraint of trade.

The landmark case dealing with post-employment restraint is *Krishan Murgai case*⁴⁶. The Court, in this case, tried to define what is meant by the expression "restraint of trade". It maintains that a contract that restricts a party's future freedom to do his trade, business, or profession in the way and with the people he chooses is known as a contract in restraint of trade. Hence, the contract which objects to a restraint of trade will be void, prima facie. However, it only becomes so until proven that such restrictions are unjustified regarding the circumstances from the parties' perspectives.

⁴³ Above n 14.

⁴⁴ *Kores Manufacturing Co Ltd v Kolak Manufacturing Co Ltd* [1959] 1 Ch. 108,

⁴⁵ Above n 9

⁴⁶ Above n 34

The Court opined that once it has been proved that such restraint is a restraint of trade, the Court will not accept the defense of reasonableness or the restraint being of partial character. In other words, the Court evaluates reasonability, considering the employer's legitimate interest, fair conditions for the employee's livelihood, and limits on time, space, and locality.⁴⁷ But it has strictly confirmed the position that the Court will not look favorably if the restriction is imposed on the employee after the termination of the contract in order to prevent competition. Such restriction definitely falls within the definition of restraint of trade.

5. The Way Forward

5.1. Non-compete Clause: The Infosys Case

The recent case of *Infosys*⁴⁸ has drawn the attention of the people to the doctrine of restraint of trade again. Infosys included a non-compete clause in the contract, barring the employee from joining competing firms or their subsidiaries for six months after contract termination. The clause also prevented the employee from accepting job offers from customers they had worked with in the preceding twelve months before termination. The case is still in proceeding. The Court had ruled in favor of the employee annulling the non-compete covenant as being in restraint of trade. Thus, it reapplied the principle held in *Krishan Murgai*.⁴⁹

However, it can be argued that the employer does not lose all his interests with the termination of the employment contract. As we have seen in *Niranjan Shankar Golikari*⁵⁰ that employee was restrained from getting employed otherwise because considerable trade secret, confidential information and training was provided to him in the course of business in the former company. If he was allowed to employ himself in a new company, it would prejudice the freedom of trade of the complainant company. The Court noted that a covenant reasonable for conducting business should not be deemed a restraint of trade, as the Court said:

“Both the Trial Court and the High Court have found, and in our view, rightly, that the negative covenant in the present case restricted as it is to the period of employment and to work similar or substantially similar to the one

⁴⁷AMLEGALS, ‘Restrictive Covenants of Employment & Contract Act - Contract of Employment - India’ (*Restrictive Covenants Of Employment & Contract Act - Contract of Employment - India*, 3 January 2019) <<https://www.mondaq.com/india/contract-of-employment/768944/restrictive-covenants-of-employment--contract-act>> accessed 15 June 2023

⁴⁸ Surana P and Surana, ‘The Baffling Case of Infosys Non-Compete Clause: A Critical Analysis’ (*SURANA SURANA*) <<https://suranaandsurana.com/2022/09/09/the-baffling-case-of-infosys-non-compete-clause-a-critical-analysis/>> accessed 15 June 2023

⁴⁹ Above n 34

⁵⁰ Above n 29

carried on by the appellant when he was in the employ of the respondent company was reasonable and necessary for the protection of the company's interests and not such...as the court would refuse to enforce. There is therefore no validity in the contention that the negative covenant contained in clause 17 amounted to a restraint of trade and was therefore against public policy.”

So, the company should be allowed to enforce such clauses. In the Court's view a covenant preventing an employee from engaging in similar trade or employment is not a restraint of trade, unless the contract is deemed unconscionable, excessively harsh, unreasonable, or one-sided. However, it should be also maintained that such covenant does not badly affect the right to employment of the employee. It should also be mentioned that the purpose of imposing a restriction is not confined to preventing competition. The most important aspect of post-employment restraint is to protect the firm's trade secrets and confidential information and its connection with the customers.

The employment agency does not lose this interest even after the employee leaves the firm. When an employee leaves the company, he may take with him the company's trade secret and confidential information that is not in the public domain. Again, it takes years for the company to build up its relationship with the customers. It is the credit of the employer to employ and provide necessary training to the employee by dint of which the employee becomes capable of establishing a relationship with the employer. Hence, the interest here is legitimate. If this interest is not protected, the employer will not find the assurance to train his employer or delegate knowledge to him to run the business.

But a non-compete clause inherently gives the employee a right to prevent competition. Objections against imposing non-compete covenant by this way often roots to the fact that such restraint limited to trade secrets and confidential information can also be imposed through various other clauses without prejudicing the right to seek employment of the employees. A non-solicitation clause is one of the examples. Through this clause, the employer agency prevents the employee, post-employment, from soliciting its other employees or customers to enter into business or a trade relationship with the new firm that the ex-employee has joined, against the interest of the former employer. The Court in India has held such a non-solicitation clause as valid and not dictated under the doctrine of restraint of trade in *Wipro Limited v Beckman Coulter International*⁵¹.

Another way of imposing a restraint to protect the same legitimate interest of the employer is by using “non-disclosure restrictions”. This sort of covenant strictly applies to prevent the employee, after his termination of employment, from disclosing any trade, secret, business connections, and confidential information to any person, other than those related to the employer company.

⁵¹ (2006) 3 ARBLR Del 118

5.2. Outsourcing Contracts: The Grameenphone Case

Outsourcing contracts is a place where the application of restraint of trade may come handy. An outsourcing contract is generally more complex than the traditional contracts of employment. To understand how the doctrine of restraint of trade can be applied in an outsourcing contract, we need to first understand what an outsourcing contract is, and how it works. This leads us to the second segment of this section: The Grameenphone case, where the Court has magnificently elucidated the mechanisms of an outsourcing contract.

In *Grameenphone Ltd vs Chairman, First Labour Court, Dhaka, and Others*⁵² a number of drivers who were employed by the Respondent, Smart Services, used to provide services for the Grameenphone company, the Petitioner. But the Petitioner denied that the Respondent drivers were their workers, and they did not even pay them any salaries. The contention arose in the case of the drivers, Respondents no. 3, whether they were workers under the Petitioner. The Petitioner said that the drivers worked for Respondent no. 4, Smart Services Ltd. and/or Jamsons International. They emphasized that the services of the drivers had been procured through a contract between them and Smart Services Ltd. They added that Smart Services Ltd. are merely contractors, as opposed to “recruiters” and they even issued appointment letters in favor of the respondent drivers for rendering services for the petitioner as “outsourced” workers. They also mentioned that Respondents no. 3 were even a party to the contract, and the contract was signed between the petitioner itself and Respondent no. 4.

The High Court held that the drivers were actually the employees of Respondent no. 4 (Smart Services Ltd/Jamsons International), and not of the Petitioner Grameenphone Ltd. The drivers received salaries and other benefits from Smart Services/Jamson International without complaining for several years. Therefore, they cannot say all of a sudden that they were not the employees of Smart Services Ltd. but of Grameenphone Ltd. Grameenphone did not issue them any approval letter as an employee, rather they were merely the user of the services. Grameenphone paid service charges to Smart Services/Jamson International, not to the drivers. They do not have to deal with the drivers but only deal with only their services.

Tarikul Hakim J has clearly explained the outsourcing process. It is a procedure whereby the person receiving the service enters into an agreement with a contractor or service provider who then hires individuals to provide the service. There is no employment agreement between the service recipient and the service provider in such a circumstance. There is a contract in place between the service recipient and the contractor, and the service recipient pays the contractor

⁵² [2018] 10 SCOB (HCD)

compensation for the services. If the service recipient is dissatisfied with the service provided by the individuals hired by the contractor, he or she may sue the contractor for breach of the terms and conditions of the agreement.

Why is this case important?

While analyzing restraint of trade in the case of traditional employment agreements, we can see that the service recipients usually hold the power to impose the restrictive covenant on the service renderers. It is because in such a case, the employer and the service recipient are the same entity. Similarly, the service renderer solely holds the title of 'employee' of that employer. But this is not the case in an outsourcing contract. Because the service recipient is not the employer of the service renderer in an outsourcing contract scenario. Instead, it is actually third-party. The main employment contract takes place between the service renderer (the drivers in Grameenphone) and the contractor agency (Smart Services/Jamson International). The contractor can only control employment terms and the service recipient, like Grameenphone does not have a hand in it. Because, unlike a traditional employment contract, there is no contract between the service renderer and the service recipient. That is why, we saw in the Grameenphone case, the drivers were unable to be integrated as permanent workers.

Similarly, it follows that Grameenphone is not able to control the employment of the drivers since the drivers are not their workers at all. In absence of a contract between the service recipient and service renderer, by dint of which the rights of the employees are generally controlled, how will it be possible to impose restrictive covenants like 'restraint of trade'? This leads us to our hypothetical question: How can the Court manage to allow the restraint in this form of service contracts (outsourcing)?

Unlike general contracts of service, here both contract of service and contract for service come into play. Since the employee renders service to the service recipient company, there is an active risk of breach of trade secret and confidentiality. Hence, the service recipient has an interest in restraining the employee. But a problem will arise because the service renderer is not under any actual contract with him. In this scenario, two sorts of solutions can be given.

Firstly, the Court has to imply a contract between the service renderer and the service recipient in order to deal with such situations. The nature of the work is absolutely the same as it would be if they were in an employment contract with the service recipient. But no such direct contract is made with the workers, instead with the contractors. It does not mean that the employees are working voluntarily. There is of course a contract, but the nature of it is very complex. Only because there is no visible contract does not mean that they are voluntary workers. Hence it

can be said that there is an implied contract because of which the service renderer works for the service recipient company. However, this approach of implying a contract is of course highly artificial.

Secondly, the service recipient can contract with the contractor under the condition that the service renderer will not disclose or otherwise use any vital information gained while providing services to him. This approach is not artificial. But unlike the previous solution, if the contract is not signed with the given conditions it will leave the service recipient remediless. Whereas in the first instance, restrictive covenant can be enforced without such extra conditions inserted in the contract with the contractor agency. But since it is still a developing jurisprudence, further instances should be dealt with and more contents have to be developed.

6. Conclusion

The problem regarding the issue of restraint of trade regarding employment contracts is presently centered around the question of restraint after the termination of employment. In common law jurisdiction, a restraint applicable after the termination of contract, if implied reasonably, is held valid. This is not the case in India or Bangladesh. All restraints post-employment is held void here as being in restraint of trade. The Courts here have accepted the narrow meaning of section 27. However, it can be said that there is still hope for protecting the legitimate interests of the employer by usage of non-solicitation clause and non-disclosure clause in the contract. But the position as to the use of non-compete clause is very strict in India and similarly in Bangladesh because the right of the employee to seek employment elsewhere is highly regarded.

On the other hand, in case of outsourcing contracts, it can be said that the service renderer should be deemed free to contract at times otherwise than under active employment under the contractor, not the employer. And the contractor should be given the scope to enforce the negative covenant under the contract to prevent the service renderer to leak confidential information or trade secret under a contract between himself and the contractor of the employee.