[2025] 6 S.C.R. 240 : 2025 INSC 691

Vijaya Bank & Anr.
v.
Prashant B Narnaware

(Civil Appeal No. 11708 of 2016)

14 May 2025

[Pamidighantam Sri Narasimha and Joymalya Bagchi,* JJ.]

Issue for Consideration

Matter pertains to whether clause 11(k) of the appointment letter that employee to work for minimum three years and in default to pay Rs 2 lakhs as liquidated damages on leaving employment amounts to restraint of trade u/s.27 of the Contract Act and/or opposed to public policy; and the correctness of order passed by the High Court quashing clause 11(k) of the appointment letter and thus, directing the bank to refund the said sum to the respondent-employee.

Headnotes†

Contract Act, 1872 – s.27 – Agreement in restraint of trade void – Restrictive covenant in the clause of the appointment letter that employee to work for minimum three years and in default to pay Rs 2 lakhs as liquidated damages on leaving employment – Respondent-employee tendered resignation before completion of three years and paid the sum under protest – Writ petition by the respondent seeking quashing of the clause of the appointment letter – High Court quashed the clause of the appointment letter and thus, directed the bank to refund the said sum to the respondent – Correctness:

Held: Restrictive covenant in clause of the appointment letter does not amount to restraint of trade nor is it opposed to public policy – Validity of restrictive covenant in an employment agreement in regard to restraint in exercise of lawful profession, trade or business has to be tested on the touchstone of s.27 – Restrictive covenant operating during the subsistence of an employment contract does not put a clog on the freedom of a contracting party to trade or employment – Object of the restrictive covenant was in furtherance of the employment contract and not to restrain future employment – Hence, it cannot be said to be violative of s.27 – From the prism of employer-employee relationship, technological

* Author

advancements impacting nature and character of work, re-skilling and preservation of scarce specialized workforce in a free market are emerging heads in the public policy domain which need to be factored when terms of employment contract is tested on the anvil of public policy – Public sector undertakings like the appellant-bank needed to compete with efficient private players operating in the same field – Ensuring retention of efficient and experienced staff contributing to managerial skills was one of the tools inalienable to the interest of such undertakings – This prompted the appellant-bank to incorporate a minimum service tenure for employees, to reduce attrition and improve efficiency – Restrictive covenant prescribing minimum term not unconscionable, unfair or unreasonable and thereby in contravention of public policy – Respondent was serving in a senior middle managerial grade having lucrative pay package, quantum of liquidated damages not so high as to render the possibility of resignation illusory – High Court failed to consider the restrictive covenant in its proper perspective **–** Constitution of India – Arts.14, 19**.** [Paras 12, 15-16, 24-27, 31, 32, 35, 36]

Contract – Standard form employment contracts – Interpretation of – Legal principles – Discussed. [Para 21]

Case Law Cited

K.Y Venkatesh Kumar v. BEML Ltd., **Karnataka HC DB in W.A. No. 2736/2009 disposed on 09.12.2009;** *Niranjan Shankar Golikari v. Century Spinning and Manufacturing Co* **[1967] 2 SCR 378 : 1967 SCC OnLine SC 72;** *Superintendence Company (P) Ltd. v. Krishan Murgai* **[1980] 3 SCR 1278 : (1981) 2 SCC 246;** *Central Inland Water Transport Corporation Ltd. v. Brojo Nath Ganguly* **[1986] 2 SCR 278 : (1986) 3 SCC 156;** *Haryana Financial Corporation v. Jagdamba Oil Mills* **[2002] 1 SCR 621 : (2002) 3 SCC 496 – referred to.**

List of Acts

Constitution of India; Contract Act, 1872.

List of Keywords

Restrictive covenant; Liquidated damages; Resignation before completion of 3 years; Restraint of trade; Clog on the freedom to trade or employment; Restrain future employment; Opposed to public policy; Legal principles relating to interpretation of standard

form employment contracts; Terms of employment contract; Scarce specialized workforce; Public good and policy; Deregulated free-market; Minimum service tenure for employees; Expensive recruitment process; Appointment letter; Public sector undertakings; Senior middle managerial grade.

Case Arising From

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 11708 of 2016

From the Judgment and Order dated 20.08.2014 of the High Court of Karnataka at Bangalore in WA No. 1159 of 2013

With

Civil Appeal No. 11499 of 2016

Appearances for Parties

Advs. for the Appellants:
S.R.Singh, Sr. Adv., Ms. Asha Gopalan Nair, Sushant Kumar Yadav, Prateek Yadav, Gaurav Lomes, Shashikant Pralhad Chaudhari, Rajesh Kr. Gautam, Likivi K Jakhalu, Deepanjal Choudhary, M/s. Mitter & Mitter Co.

Advs. for the Respondent:
Rahul Chitnis, Hersh Desai, Ms. Shwetal, Aditya Khanna, Chander Shekhar Ashri, Rajesh Kr. Gautam, Likivi K Jakhalu, Deepanjal Choudhary, M/s. Mitter & Mitter Co., Sanjay Kapur, Ms. Divya Singh Pundir, Arjun Bhatia, Ms. Shubhra Kapur, Ms. Mansi Kapur.

Judgment / Order of the Supreme Court

Judgment

Joymalya Bagchi, J.

CIVIL APPEAL NO. 11708 of 2016

1. Appellants have challenged judgment and order dated 20.08.2014 passed by the High Court quashing clause 11(k) of the appointment letter whereby the respondent-employee[1] was required to pay

1 Hereinafter, respondent.

liquidated damages of Rs. 2 lakhs in the event of leaving employment of the first appellant-bank[2] prior to three years and consequentially the appellant-bank was directed to refund the said sum to the respondent.

2. In 1999, respondent had joined the appellant-bank as a Probationary Assistant Manager. His service was confirmed in 2001. Thereafter, he was promoted to Middle Management Scale-II. In 2006, appellant-bank issued a recruitment notification for appointment of 349 officers in different grades. Clause 9 (w) of the recruitment notification reads as follows:-

> "*Selected candidates are required to execute an indemnity bond of Rs.2.00 Lakh (Rupees Two Lakh only) indemnifying that they will pay an amount of Rs.2.00 lakh to the Bank if they leave the service before completion of 3 years"*

3. Cognizant of the said condition, respondent applied to the post of Senior Manager-Cost Accountant at basic pay of Rs.18,240/- and was selected for the said post.

4. On 07.08.2007, respondent was issued an appointment letter. Clause 11(k) of the said letter reads as follows:-

> *"You are required to serve the Bank for a minimum period of 3 years from the date of joining the bank and should execute an indemnity bond for Rs.2.00 lakhs. The said amount has to be paid by you in case you resign from the services of the bank before completion of stipulated minimum period of 3 years. For this purpose, you have to bring a blank non-judicial stamp paper of Rs.100/- procured in the State of your posting."*

5. Accepting the aforesaid condition, respondent voluntarily resigned from his erstwhile post i.e. Manager, MMG-II and joined the post of Senior Manager, MMG-III on 28.09.2007. Respondent also executed an indemnity bond in terms of the aforesaid clause.

6. On 17.07.2009 i.e. before completion of three years from his date of joining, respondent tendered resignation for joining another Bank, namely, IDBI. His resignation was accepted and on 16.10.2009 respondent under protest in terms of the aforesaid condition paid the sum of Rs.2 lakhs to the appellant-bank.

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2 Hereinafter, appellant-bank.

7. Thereafter, respondent filed a writ petition before the High Court praying for quashing of clause 9 (w) of the recruitment notification and clause 11 (k) of the appointment letter alleging the same were in violation of Articles 14 and 19(1)(g) of the Constitution of India and Sections 23 and 27 of the Indian Contract Act, 1872.

8. Appellant-bank opposed the prayer. Learned Single Judge relied on the decision of a Division Bench of the High Court in *K.Y Venkatesh Kumar v. BEML Ltd.* [3] and allowed the writ petition. The order came to be upheld by the Division Bench.

9. Heard Mr. Rajesh Kr. Gautam, learned counsel for the appellants and Mr. Rahul Chitnis, learned counsel for the respondent.

10. The issue which falls for decision is whether clause 11 (k) of the appointment letter amounts to :-

    (i) restraint of trade under Section 27 of the Contract Act and/or

    (ii) opposed to public policy and thereby contrary to Section 23 of the Contract Act and violative of Articles 14 and 19 of the Constitution.

RESTRAINT OF TRADE

11. Section 27 of the Contract Act provides every agreement which restrains a person from exercising a lawful profession, trade or business of any kind is to that extent void. A sole exception is carved out in the proviso with regard to sale of goodwill of a business, in which case the seller may be restrained from carrying on similar business within a reasonable local limit.

12. Though the Contract Act does not profess to be a complete code, Act is exhaustive with regard to the subject matter contained therein. That is to say, validity of a restrictive covenant in an agreement including an employment agreement in regard to restraint in exercise of lawful profession, trade or business has to be tested on the touchstone of Section 27 of the Contract Act.

13. Whether Section 27 operates as a bar to a restrictive covenant during the subsistence of an employment contract fell for decision

3 Karnataka HC DB in W.A. No. 2736/2009 disposed on 09.12.2009.

in *Niranjan Shankar Golikari v. Century Spinning and Manufacturing Co.*[4] After an illuminating discussion on the subject, the Bench made a distinction between restrictive covenants operating during the subsistence of an employment contract and those operating after its termination. The Bench held as follows:-

> "**17.** The result of the above discussion is that considerations against restrictive covenants are different in cases where the restriction is to apply during the period after the termination of the contract than those in cases where it is to operate during the period of the contract. Negative covenants operative during the period of the contract of employment when the employee is bound to serve his employer exclusively are generally not regarded as restraint of trade and therefore do not fall under Section 27 of the Contract Act. A negative covenant that the employee would not engage himself in a trade or business or would not get himself employed by any other master for whom he would perform similar or substantially similar duties is not therefore a restraint of trade unless the contract as aforesaid is unconscionable or excessively harsh or unreasonable or one-sided.."

14. This view was reiterated in the concurrent opinion of A.P. Sen, J. in *Superintendence Company (P) Ltd. v. Krishan Murgai.*[5] Endorsing the ratio in *Golikari* (supra) with regard to validity of restrictive covenants during the subsistence of a contract, A.P. Sen, J. held:-

> **"18.** Agreements of service, containing a negative covenant preventing the employee from working elsewhere during the term covered by the agreement, are not void under Section 27 of the Contract Act, on the ground that they are in restraint of trade. Such agreements are enforceable. The reason is obvious. The doctrine of restraint of trade never applies during the continuance of a contract of employment; it applies only when the contract comes to an end. While during the period of employment, the courts undoubtedly would not grant any specific performance of a contract of

4 1967 SCC OnLine SC 72

5 (1981) 2 SCC 246

personal service, nevertheless Section 57 of the Specific Relief Act clearly provides for the grant of an injunction to restrain the breach of such a covenant, as it is not in restraint of, but in furtherance of trade.

19. In Niranjan Shankar Golikari case this Court drew a distinction between a restriction in a contract of employment which is operative during the period of employment and one which is to operate after the termination of employment. After referring to certain English cases where such distinction had been drawn, the Court observed:

"A similar distinction has also been drawn by courts in India and a restraint by which a person binds himself during the term of his agreement directly or indirectly not to take service with any other employer or be engaged by a third party has been held not to be void and not against Section 27 of the Contract Act."

15. In view of these authoritative pronouncements, it can be safely concluded law is well settled that a restrictive covenant operating during the subsistence of an employment contract does not put a clog on the freedom of a contracting party to trade or employment.

16. A plain reading of clause 11 (k) shows restraint was imposed on the respondent to work for a minimum term i.e. three years and in default to pay liquidated damages of Rs. 2 Lakhs. The clause sought to impose a restriction on the respondent's option to resign and thereby perpetuated the employment contract for a specified term. The object of the restrictive covenant was in furtherance of the employment contract and not to restrain future employment. Hence, it cannot be said to be violative of Section 27 of the Contract Act.

OPPOSED TO PUBLIC POLICY

17. Let us now examine whether the clause is opposed to public policy.

18. Mr. Chitnis has vehemently argued the clause is part of a standard form contract and his client was compelled to sign on dotted lines. If he did not do so, he would have to forsake career advancement. The terms of the contract were imposed on him through an unequal bargaining mechanism. Clause 11 (k) being an unreasonable, onerous and ex-proportionate measure resulting in unjust enrichment for

the appellant-bank is opposed to public policy. At the time of his resignation respondent was compelled to comply with the illegal condition and had done so under protest. In these circumstances, he cannot be precluded from challenging the condition as violative of fundamental rights and public policy.

19. In *Central Inland Water Transport Corporation Ltd. v. Brojo Nath Ganguly,*[6] this Court dealt with interpretation of standard form employment contracts in the backdrop of unequal bargaining power of employees. The Bench opined if such contracts are unconscionable, unfair, unreasonable and injurious to public interest, they shall be deemed void in law being opposed to public policy. The Bench elucidated the proposition in the following words:-

> **"91.....**the majority of such contracts are in a standard or prescribed form or consist of a set of rules. They are not contracts between individuals containing terms meant for those individuals alone. Contracts in prescribed or standard forms or which embody a set of rules as part of the contract are entered into by the party with superior bargaining power with a large number of persons who have far less bargaining power or no bargaining power at all. Such contracts which affect a large number of persons or a group or groups of persons, if they are unconscionable, unfair and unreasonable, are injurious to the public interest. To say that such a contract is only voidable would be to compel each person with whom the party with superior bargaining power had contracted to go to court to have the contract adjudged voidable. This would only result in multiplicity of litigation which no court should encourage and would also not be in the public interest. Such a contract or such a clause in a contract ought, therefore, to be adjudged void. While the law of contracts in England is mostly judge-made, the law of contracts in India is enacted in a statute, namely, the Indian Contract Act, 1872. In order that such a contract should be void, it must fall under one of the relevant sections of the Indian Contract Act. The only relevant provision in the

6 (1986) 3 SCC 156

> Indian Contract Act which can apply is Section 23 when it states that "The consideration or object of an agreement is lawful, unless ... the court regards it as ... opposed to public policy."
>
> *(Emphasis supplied)*

20. It may not be out of place to note A.P. Sen, J., a member of the coram in *Brojo Nath* (supra) had expressed a similar view earlier in *Murgai* (supra):-

> "**59.** It is well settled that employee covenants should be carefully scrutinised because there is inequality of bargaining power between the parties; indeed no bargaining power may occur because the employee is presented with a standard form of contract to accept or reject. At the time of the agreement, the employee may have given little thought to the restriction because of his eagerness for a job; such contracts "tempt improvident persons, for the sake of present gain, to deprive themselves of the power to make future acquisitions, and expose them to imposition and oppression".

21. The legal principles relating to interpretation of standard form employment contracts may be summarized as follows:-

    (i) Standard form employment contracts *prima facie* evidence unequal bargaining power.

    (ii) Whenever the weaker party to such a contract pleads undue influence/coercion or alleges that the contract or any term thereof is opposed to public policy, the Court shall examine such plea keeping in mind the unequal status of the parties and the context in which the contractual obligations were created.

    (iii) The onus to prove that a restrictive covenant in an employment contract is not in restraint of lawful employment or is not opposed to public policy, is on the covenantee i.e. the employer and not on the employee.

22. This brings us to the issue as to what is public policy? In *Brojo Nath* (supra) the expression 'public policy' under the Contract Act was expounded as follows:-

> **"92.** The Indian Contract Act does not define the expression "public policy" or "opposed to public policy". From the very nature of things, the expressions "public policy", "opposed to public policy", or "contrary to public policy" are incapable of precise definition. Public policy, however, is not the policy of a particular government. It connotes some matter which concerns the public good and the public interest. The concept of what is for the public good or in the public interest or what would be injurious or harmful to the public good or the public interest has varied from time to time. As new concepts take the place of old, transactions which were once considered against public policy are now being upheld by the courts and similarly where there has been a well recognized head of public policy, the courts have not shirked from extending it to new transactions and changed circumstances and have at times not even flinched from inventing a new head of public policy.."

23. In *Golikari* (supra), the Bench noted the evolving nature of public policy in following words :-

> "**12.....**The attitude of the courts as regards public policy however has not been inflexible. Decisions on public policy have been subject to change and development with the change in trade and in economic thought and the general principle once applicable to agreements in restraints of trade have been considerably modified by later decisions. The rule now is that restraints whether general or partial may be good if they are reasonable. A restraint upon freedom of contract must be shown to be reasonably necessary for the purpose of freedom of trade. A restraint reasonably necessary for the protection of the covenantee must prevail unless some specific ground of public policy can be clearly established against it."

24. Generally speaking, public policy relates to matters involving public good and public interest. What is 'just, fair and reasonable' in the eyes of society varies with time. Civilizational advancements, growth of knowledge and evolving standards of human rights and dignity alter the contours of public good and policy.

25. From the prism of employer-employee relationship, technological advancements impacting nature and character of work, re-skilling and preservation of scarce specialized workforce in a free market are emerging heads in the public policy domain which need to be factored when terms of an employment contract is tested on the anvil of public policy.

26. Since the last decade of 20th century, India witnessed an era of liberalization. Golden days of monopolistic public sector behemoths were gone. Public sector undertakings like the appellant-bank needed to compete with efficient private players operating in the same field. To survive in an atmosphere of deregulated free-market, public sector undertakings were required to review and reset policies which increased efficiency and rationalized administrative overheads. Ensuring retention of an efficient and experienced staff contributing to managerial skills was one of the tools inalienable to the interest of such undertakings including the appellant-bank.

27. This prompted the appellant-bank to incorporate a minimum service tenure for employees, to reduce attrition and improve efficiency. Viewed from this perspective, the restrictive covenant prescribing a minimum term cannot be said to be unconscionable, unfair or unreasonable and thereby in contravention of public policy.

28. The other aspect involves imposition of liquidated damages to the tune of Rs.2 Lakhs in the event of pre-mature resignation. Mr. Chitnis has strenuously argued the quantum is disproportionate and causes unjust enrichment to the employer. We are unable to agree with this submission. In their pleadings before the High Court the appellant-bank has clarified the financial hardship which it would suffer due to untimely recruitment drives owing to pre-mature resignations. The Bank pleaded as follows:-

> "The Indemnity Bond obtained by the Bank was done so with a view to secure the interests of the Bank and to place adequate safeguards against premature resignations-tendered by employees. In the usual course, appointments are into service of the Bank after a detailed and elaborate process of recruitment and the Banks interest would be seriously prejudiced in the event premature resignations are tendered which would render the entire recruitment

> process redundant. That apart the Bank would also suffer the consequences of the loss in continuance of the said post which would necessitate alternative arrangements and restructuring to ensure smooth functioning of day to day business activities. That apart, the bank would have to initiate a fresh process of recruitment which would be time consuming and also expensive."

29. The stance of the appellant-bank is neither unjust nor unreasonable. The appellant-bank is a public sector undertaking and cannot resort to private or ad-hoc appointments through private contracts. An untimely resignation would require the Bank to undertake a prolix and expensive recruitment process involving open advertisement, fair competitive procedure lest the appointment falls foul of the constitutional mandate under Articles 14 and 16.

30. Keeping these exigencies in mind, the appellant-bank had incorporated the liquidated damage clause in the appointment contract.

31. Respondent was serving in a senior middle managerial grade having a lucrative pay package. Judged from that perspective, the quantum of liquidated damages was not so high as to render the possibility of resignation illusory. In fact, the appellant had paid the said quantum and resigned from the post.

32. The High Court failed to consider the restrictive covenant in its proper perspective in the factual matrix of the case and mechanically relied on *BEML* (supra) to set aside the covenant as barred by law.

33. In *BEML* (supra), a coordinate Bench of the High Court was considering a restrictive covenant which not only imposed a minimum term of employment but also a clog on future employability.

34. That apart, in *BEML* (supra) the issue of financial loss suffered by the public sector undertaking owing to time consuming and expensive recruitment drives due to pre-mature resignations had not fallen for consideration. It is trite judgments cannot be read as statutes and have to be applied keeping in mind the factual matrix peculiar to each case.[7]

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7 Haryana Financial Corporation v. Jagdamba Oil Mills (2002) 3 SCC 496

35. In light of the aforesaid discussion, we are of the view the restrictive covenant in clause 11(k) of the appointment letter does not amount to restraint of trade nor is it opposed to public policy.

36. Consequently, the appeal is allowed. Impugned judgment and order of the High Court is set aside.

CIVIL APPEAL NO.11499 of 2016

37. Similar issue with regard to validity of clause 11(k) in the appointment letter fell for consideration in Civil Appeal No. 11708 of 2016. High Court dismissed the appellant-employee's challenge. In view of the order passed in the aforesaid appeal, we find no reason to interfere with the order of the High Court.

The appeal is dismissed.

Result of the case: Civil Appeal No. 11708 allowed.
Civil Appeal No. 11499 dismissed.

†*Headnotes prepared by:* Nidhi Jain