
(1979) 07 DEL CK 0016
In the Delhi High Court
Case No : F.A.O. (O.S.) 86 of 1979

Krishan Murgai

APPELLANT

Vs

Superintendence Company of India (P) Ltd.

RESPONDENT

Date of Decision : 20-07-1979

Acts Referred:

Citation : AIR 1979 Delhi 232

Hon'ble Judges : V.S. Deshpande, C.J.; Harish Chandra, J

Bench : Division Bench

Advocate : G.L. Sanghi, S.C. Dhanda, D.N. Sawhney and V. Rao, for the Appellant; L.M. Singhvi N.D. Garg, L.K. Pandey and Rajiv Kumar Garg, for the Respondent

Judgement

1. "You cannot", they say, "have the cake and eat it too". But a plaintiff who obtains a temporary injunction against a defendant eats the cake even before getting it. It is obvious, Therefore, that temporary injunction, for instance, under Order Xxxix Rule 2 granted by the learned single Judge to the plaintiff respondent against the defendant appellant in this case can be justified only if it was, based on a good prima facie case made out by the plaintiff showing that in all probability the plaintiff was entitled to obtain ultimately the permanent" injunction sought by it as could appear, at this stage before going into evidence from the pleadings and the admitted documents. The appellant contends that no prima facie case was made out by the respondent and the temporary injunction should be vacated in the appeal. We must, Therefore, first see the facts and the pleadings, and the law applicable on such facts to know if a good prima facie case was made out to justify the grant of temporary injunction.

THE FACTS:

2. The plaintiff carries on business of inspecting merchandise with a view to assess their quality and claims that it has established reputation and goodwill in its business, developed its own technique for quality testing and control, and possesses trade secrets in the form of these techniques and clientele. The

plaintiff has been employing various persons as Manager and in other capacities in Calcutta, New Delhi and other places. The employees are put in posts of trust and confidence sharing the secrets of business and trade of the plaintiff.

3. The defendant was employed by the plaintiff on 27th March 1971. During his service the defendant appellant was given various positions including that of the Manager of the New Delhi branch of the plaintiff. The relevant terms in the appointment letter of the defendant are:

"9. that while in our employ, you will not be permitted to engage yourself in any part time job.

10. that you will not be permitted to join any firm of our competitors or run a business of your own in similar lines directly and/or indirectly, for a period of two years at the place of your last posting after you leave the company.

11. that no secrets of the company must be revealed to other parties and that you will not commit any sort of misdemeanors which may cause harm of any sort to the organisation."

The defendant accepted these terms. He served a probationary period and was confirmed. On 24th November, 1978 the plaintiff terminated the defendant's services with effect from 27th December, 1978."

4. After the termination of the service the defendant started carrying on business on lines identical with the business of the plaintiff under the name and style of "Superintendence of Surveillance Inspectorate of India" in New Delhi, which was similar to the name of the plaintiff, which is "Superintendence Company of India (P) Limited". The defendant was associating or joining with the competitors of the plaintiff's business. He was soliciting customers and business from the plaintiff's clientele and was also using and employing the technique of the plaintiff which he had learnt during his employment.

5. The plaintiff brought the suit for a permanent injunction to restrain the defendant from his activities on the ground that these activities were contrary to terms 10, 11 and 12 of his employment, As to term 10 the plaintiff is said to have made a rule that an employee after leaving plaintiff's service was not (to) engage in a similar business for two years.

6. Normally, the assessment whether a good prima facie case exists for granting temporary injunction is in the judicial discretion of the trial court and the court of appeal will not interfere if the judicial discretion is reasonably exercised. If, however, it appears that the fundamental condition for the grant of temporary injunction, namely a prima facie case, is itself not fulfilled ,then the court of appeal will have to interfere. On a careful consideration of the order under appeal and the learned arguments addressed by Shri G. L. Sanghi for the appellant, and Dr. L. M. Singhvi for the respondent we have been unable to find any prima facie case on the plaintiff's pleadings and the law applicable to it to sustain the temporary injunction.

7. Our reasons for this conclusion are as below: Section 27 of the Contract Act, 1872, reads as under:

"Every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void.

Explanation 1, - One who sells the good-will of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the good-will from him, carries on a like business therein, provided that such limits appear to the Court reasonable, regard being had to the nature of the business".

The key to the construction of S. 27 is to be found in the following observation in Pollock and Mulla on Indian Contract and Specific Relief Acts, Ninth Edition by Justice J. L. Kapur, at p. 271:

"Agreements in restraint of trade. -This section, like the last, unfortunately follows the New York draft Code, which has been the evil genius of this Act. The first paragraph is taken almost word for word from S. 833 of that production. The original draft of the Indian Law Commission did not contain any specific provision on the subject.

The New York draftsmen were of opinion that contract in restraint of trade have been allowed by modern decisions to a very dangerous extent, and deliberately tried to narrow the Common Lawthe Indian law has stereotyped that doctrine in a narrower form than even the old authorities would justify. The exception is also taken with slight variation from the New York draft Code."

8. Section 27 of the Contract Act is in absolute terms. It does not say that only unreasonable restraint of trade is void and reasonable restraint of trade is valid. The scheme of the old Contract Act was to enunciate the rule in S. 27 and also lay down in the statute itself the exceptions to the rule. The first exception regarding the sale of goodwill of the business is annexed to S. 27 itself. Three more exceptions to the rule were also a part of the Chapter on Partnership in the unamended Contract Act, which later became the Indian Partnership Act, 1932. These exceptions are contained in Ss. 11 (2), 36 (2) and 54 of the said Act. It will be seen that the framers of the Contract Act wanted to state the complete law as to the general rule that restraint of trade is void and also the exceptions based on reasonableness to such a rule. It is to be noted that the contract between the master and servant was not the subject-matter of any of the exceptions. If the rule is subject to the stated exceptions only, the ordinary interpretation of these statutory provisions would be that no other exceptions are to be engrafted upon these statutory rules stated in S. 27.

9. The Courts in India have approached the construction of S. 27 in the following manner: (A) If a contract of service is valid and the performance of the contract by the employee requires that during the period of service he must not engage in any other work and must not divulge to any person the trade secrets of the

employer then under such an agreement, even in the absence of a negative covenant prohibiting the employee from doing so, the employee would be prohibited by law from doing so. For, these acts are inconsistent with the performance of the contract, which would amount to a breach of contract. This conclusion can be based on the contract itself even without invoking S. 27; (B) But any restraint imposed by the employer on the employee would prima, facie be illegal and void as being directly hit by S. 27 if it is to operate after the expiry of the period of service contract.

10. In *Niranjan Shankar Golikari Vs. The Century Spinning and Mfg. Co. Ltd.*, , Shelat, J, reviewed the whole law on the subject and arrived at the following conclusion:

"The Court takes a far stricter view of covenants between master and servant than it does of similar covenants between vendor and purchaser or in partnership agreements, (The agreement between vendor and purchaser and between partners are the exceptions to the rule in S. 27 stated above). An employer, for instance, is not entitled to protect himself against competition on the part of an employee after the employment has ceased....."(Page 384)

"The Courts however have drawn a distinction between restraints applicable during the term of the contract of employment and those that apply after its cessation." (Page 385)

"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 S. 27 of the Contract Act. In *Brahmaputra Tea Co. Ltd. v. Scarth*, (1885) 11 Cal 545, the condition under which the convenante was partially restrained from competing after the term of his engagement was over with his former employer was held to be bad....."(Page 387)

10-A. This distinction is based on the development of law in England. Formerly all restraint of trade was thought to be bad, but when the restraint was reasonable it was upheld. Master and servant contracts were treated in the same way as commercial contracts. Lord Macnaughten in *torsten Nordenfelt v. The Maxim Nordenfelt Guns & Ammunition Co. Ltd.* 1894 Ac 535 first made this distinction in the following words;

"To a certain extent, different considerations must apply in cases of apprenticeship and cases of that sort, on the one hand, and cases of the sale of a business or dissolution of partnership on the other. A man is bound an apprentice because he wishes to learn a trade and to practice it. A may sell because he is getting too old for the strain and worry of business, or because he wishes for some other reason to retire from business altogether. Then there is obviously more freedom of contract between buyer and seller than between master and servant or between an employer and a person seeking employment."

As observed by Pollock and Mulla (page 275), in 1913 the House of Lords in *Mason v. Provident Clothing & Supply Co. Ltd.* 1913 Ac 724, accepted the statement of law of Lord Macnaughten and developed two propositions:

(1) All covenants in restraint of trade partial as well as general are prima facie void and they cannot be enforced unless the test of reasonableness propounded by Lord Macnaughten is satisfied.

(2) A distinction was made between contracts of service and contracts of sale of a business.

As pointed out by Younger L. J. in *Attwood v. Lamont*, (1920) 3 Kb 571, the House of Lords in *Mason's* case developed this distinction leading to the following points: (1) the burden of proof is on the plaintiff wanting to enforce the restrictive covenant to show that it is reasonable for the protection of his interest (2) the restraint must be reasonable not only in the interests of the covenantor but in the interests of both the contracting parties. In *Herbert Morris Ltd. v. Saxelby*, (1916) 1 Ac 688, Lord Parker observed that "the Court no longer considers the adequacy of the consideration in any particular case." That is to say, covenant in restraint of trade cannot be justified merely because it is for adequate consideration; and (3) An employer is not entitled by a covenant taken from the employee to protect himself after the employment has ceased against his former servant's competition per se, although a purchaser of goodwill is entitled to protect himself against such competition on the part of the vendor. There are at least two reasons given for this distinction. An employer may not, after his servant has left his employment, prevent him from using his own skill and knowledge in his trade or profession, even if acquired when in the employer's service. That skill and knowledge are only placed at the employer's disposal during the employment. They have not been made a subject of sale after that employment has ceased. On the other hand, when a purchaser takes over the goodwill of a business, if he is to have all its advantages it must in his hands be immune from its former owner exercising his special knowledge to the buyer's detriment.

11. Restraints imposed on the carrying on of the business after the expiry of the period of service contract by a covenant between the employer and the employee were held to be unreasonable and, Therefore, void in *Herbert Morris Ltd. v. Saxelby*, (1916) 1 Ac 688, as also in *Mason v. Provident Clothing & Supply Co. Ltd.* 1913 Ac 724.

12. The invalidity of restraint of trade imposed on an employee after the termination of the period of his employment has been consistently affirmed by the Indian decisions on a construction of S. 27 of the Contract Act. A few of them are *Oakes & Co. v. Jackson*, (1876) 1 Mad 134, *Pragji Soorji v. Pranjiwan Tooljaram*, (1903) 5 Bom Lr 878, *Burn & Co. v. McDonald*, (1909) 36 Cal 354, and *Lalbhai Dalpatbhai and Co. Vs. Chittaranjan Chandulal Pandya*, .

13. The Indian Contract Act is exhaustive as far as it goes and cannot be

controlled by the English decisions based on common law. No Indian decision seems to have held any restraint of trade imposed on the employee by the employer coming into force after the expiry of the contract of service against the employee as valid. The question of it being reasonable or not can hardly arise in view of the absolute prohibition of such restraint imposed by S. 27. On the other hand, the provisions of the Act are also based on the English common law and in so far as the Act codifies only the common law the English decisions may help in the exposition of the provisions of the Act. Section 27 as stated earlier, is intended to narrow the scope of the common law in allowing contracts in restraint of trade. This is why all such contracts have been declared to be void with certain specific exceptions stated in the statute. Those English decisions, which relate to exceptions to the rule against restraint of trade which go beyond the exceptions in the Indian statute are not, Therefore, relevant and applicable to the construction of the Indian Contract Act.

14. However, English decisions regarding the reasonableness of contracts imposing restraints of trade have been referred to. It may be useful, Therefore, to briefly consider even if the English decisions based on the common law were to be relevant in India whether the restraints imposed by the parties in the contract in this case would be valid as being reasonable. Only three grounds as justifying restraints placed on the freedom of an employee to carry on business similar to that of the employer after the termination of the employment on the ground that such restraint is reasonable have been upheld by the English decisions. Each of these three grounds as applicable to the facts of the present case is considered below:

(1) Protection of a proprietary or quasi-proprietary or commercial interest of the employer.

(2) Protection of the trade secrets of the employer; and

(3) Protection of the trade connection of the employer.

(1) Protection of a proprietary or quasi-proprietary or commercial interest of the employer.

15. What is the meaning of interest in this connection? Freedom from ordinary trade competition is not considered to be an interest which can be protected by the employer by such a covenant (G. H. Tritely - The Law of Contract, Fourth Edition, page 298). An interest to be enforceable must be based on common law, some previous contract other than the impugned one or a statute. The restrictive covenant in the present case is not based on any of them.

(2) Trade Secrets:

16. A trade secret is some secret process of manufacture. For example, the Coca-Cola formula which the Coca-Cola firm refused to disclose in India is a trade secret. In the pleading by the plaintiff there is no reference to any such trade secret. The nature of the employment of the defendant itself rules out the

possession of a trade secret by him. The defendant was a short service commissioned officer in the Army without any technical qualification. He was employed to do work which was not technical in its nature. No pleading is made by the plaintiff to show that any science or technology was involved in the work of the defendant. The plaintiff has not even said in the plaint that any training was given to the defendant. Of course, merely because the employee receives training, he is not prevented from using his own skill and knowledge derived from such training in his own interest after the end of the employment. An agreement by a firm binding the apprentice to serve it for a certain number of years on the ground that the firm has spent time and money in training the apprentice was held to be void by A. N. Ray, J. (as he then was) in *Shree Gopal Paper Mills Ltd. Vs. Surendra K. Ganeshdas Malhotra*, . It was categorically held that restriction beyond the period of employment would also not be valid.

17. The business of the plaintiff as described in the plaint as far as it was entrusted to the defendant did not seem to involve imparting of any secret information by the plaintiff to the defendant. As was observed in *Herbert Morris Ltd. v. Saxelby* (supra) the so-called secret is nothing more than a special method of organisation adopted in the business (Cheshire and Fifoot - *Law of Contract*, Ninth Edition, page 379). To establish that the employer has an interest in protecting his trade secrets he must plead and show that such secrets include secret formulae or processes, or lists of information or know-how of the kind which could be regarded as a proprietary interest of the employer as imparted to the employee. (Trietel - *The Law of Contract*, Fourth Edn., p. 300). In *Herbert Morris* case (supra), Lord Parker made the following observation regarding the nature of the trade secrets which the employer in that case alleged to have been imparted to the employee:

"Mr. Walter boldly argued that the expression trade secrets ought to be extended so as to include everything which Mr. Morris claimed to be peculiar to the plaintiffs" method of carrying on their business.

I will assume that the matters referred to by Mr. Walter are in fact peculiar to the plaintiffs" business, though I can hardly regard Mr. Morris"s uncorroborated evidence as very satisfactory proof that the practices in question were unknown to other firms. Still, the manner in which Sargent, J. dealt with this part of the case appears to me to be unanswerable. Though the defendant had access to the E Charts, the L sheets, the drawings of special machines, the cost index and other documents were far too detailed for the defendant to carry away the contents thereof in his head. All that he could carry away was the general method and character of the scheme of organisation practiced by the plaintiff company. Such scheme and method can hardly be regarded as a trade secret. The same applies to the plaintiff company"s system of standardizing mechanical apparatus capable of being used in more than one class of machine. The nearest approach that I can find in the evidence to anything in the nature of a trade secret is the mention of certain formulae, said to be based on the plaintiffs"

experience, and to be more trustworthy than Molesworth's formulae for similar purposes.

During the course of the argument your Lordships asked for but failed to obtain these formulae, and Therefore, I am unable to judge whether they are such that the defendant could carry them in his memory. I Therefore cannot attach any great importance to them. It would be a point of some difficulty whether the possession by an employee of a single trade secret would justify a restraint as wide as that in the present case, but under the circumstances I do not consider that this point really arises." (pp. 711-712).

It is true that the above observation was made taking into account the evidence given in that case, and that at this stage evidence had not been taken in the case before us. Nevertheless, we think it was the duty of the plaintiff to have disclosed some facts in the pleadings to show that any trade secret as such was imparted to the employee by the employer.

(3) Protection of trade connections:

18. In the course of employment an employee is bound to get acquainted with the customers of the employer and to know the customers. But this is not a ground to validate a covenant restraining the employee from starting a business in competition with the ex-employer and attracting the customers whom the employee had known while serving the employer. It is not the mere contact or acquaintance with the customers of the employer during the period of service which disentitles the employee after the period of service from having business dealings with the customers of the former employer. It is necessary for the employer to show that during the employment the employee had acquired influence over the employer's clients or customers. As was observed by Lord Parker in Herbert Morris case (supra), "Wherever such covenants have been upheld it has been on the ground, not that the servant or apprentice would, by reason of his employment or training, obtain the skill and knowledge necessary to equip him as a possible competitor in the trade, but that he might obtain such personal knowledge of and influence over the customers of his employer, or such an acquaintance with his employer's trade secrets as would enable him, if competition were allowed, to take advantage of his employer's trade connection or utilize information confidentially obtained." The employee in that case was Manager of the London Branch of the plaintiff's business as also Sales Manager of another Branch. With the exceptions of these jobs he worked as an Engineer. If the employee could have been shown to have had influence over the customers of the employer when the employee came to know them, the case could have been made out for restraining the employee from dealing with these customers.

19. Cheshire and Fifoot on the Law of Contract, Ninth Edition, page 380 have laid down the following tests of finding out whether the employee had opportunity to develop influence over the customers of the employer during the period of

service:

"A restraint is not valid unless the nature of the employment is such that customers will either learn to rely upon the skill or judgment of the servant or will deal with him directly and personally to the virtual exclusion of the master, with the result that he will probably gain their custom if he sets up business on his own account."

It is true that the defendant being the Manager of the plaintiff's business in the New Delhi Branch had full opportunity of knowing customers of the plaintiff. But what was the nature of the defendant's work? Practically nothing is known about it. The various words used by the plaintiff describing its business are totally inadequate to give us any idea of it. When two persons come in a contractual relationship and one of the contracting parties is in a dominating position he can be said to have influence over the other partner; if he takes undue advantage of such things then the contract would be voidable as being induced by undue influence under S. 27 of the Contract Act. The provisions of S. 27 can give us a good idea as to when one contracting party can be said to wield influence over the other partner. The illustrations to the section also further clarify the meaning of influence. By these criteria a person who holds the real or apparent authority over the other or who is in a position to dominate the will of the other or who deals with a person who is temporarily, or permanently affected by reason of age, illness or mental or bodily distress is said to have an influence over the other. There is no pleading nor any document to show that the defendant had, any such influence over the customers of the plaintiff. An inference can also be drawn from the nature of the work as to whether influence can be exercised by one party to the contract over the other. For instance, a legal adviser or a medical adviser or a person who lends money to another who is in distress are examples of persons being in a position to influence the other partner to the contract.

20. In *Fitch v. Dewes*, (1921) 2 Ac 158, a managing clerk of a solicitor, himself qualified as a solicitor, managed his master's business for many years. It was shown that he on his own dealt with many of the customers of his master. When he left the service of the master he was injected from dealing with the customers of his previous master. In our view, a solicitor is a particularly good example of a person who has influence over his clients. The reason is that the solicitor alone possesses the knowledge of law, while the client is a layman. The client is, Therefore, completely under the influence of the legal advisor. It is not shown that the work of the defendant involved any such advice or instruction or service to the clients of the plaintiff as is rendered by a lawyer or a doctor, so that the clients of the plaintiff could have been under the influence of the defendant. We are not satisfied, Therefore, that the acquaintance and knowledge of the clients of the plaintiff by the defendant during the service was such as to amount to the defendant having influence over its clients.

21. If the law applicable to the facts of the present case set out above is correct,

then the view of law taken in the order under appeal does not, with respect, seem to be in accordance with it. This will be apparent by the perusal of the following extracts from the order:

1. "Under the S. 27 of the Contract Act to determine whether the agreement is void, one has to determine whether the restraint is reasonable. If the restraint is reasonable the agreement will not be, void. The negative covenant has been enforced from time to time. Injunctions are granted u/s 42 of the Specific Relief Act, 1963 to enforce negative agreement, express or implied". With respect, all post-service restrictive covenants are prima facie void. The only exceptions are those given in the statute or those developed by the English case law stated above.

2. "It is well known that if the covenant is unreasonable the same is void and unenforceable, In case the covenant is reasonable the same can be enforced.....In case before the Supreme Court (Niranjan Shankar Golikari Vs. The Century Spinning and Mfg. Co. Ltd.,), the injunction was issued on the ground that it was restricted as to the time, the nature of employment and as to area and cannot, Therefore, be said to be too wide or unreasonable or unnecessary".

22. With respect, it may be pointed out that the injunction upheld in the Supreme Court case related to the negative covenant operating during the period of service. The court has repeatedly emphasised that Section 27 does not apply to a negative covenant operating during the period of service. The Supreme Court has not upheld in that case any restrictive covenant which prevented the employee from carrying on a similar business or working with a rival employer after the period of service. The injunction operating after the period of service was confined to the divulgence of trade secrets only. In the present case no such trade secrets, have been shown to have been imparted to the defendant.

3. "Clause 10 of the agreement is not unreasonable and is not contrary to any law. It does not appear to be hit by Section 23 or 27 of the Contract Act. It is not against public policy. It is also not a restraint on trade for an unreasonable period or place."

23. Clause 10 bars the defendant from doing a business similar to that of the ex-employer for a period of two years after leaving the service. This is directly contrary to Section 27 of the Contract Act.

24. Incidentally it may be observed that clause 10 applies only after the employee "leaves" the company. The learned single Judge has construed this to include the termination of the employment by the employer. It would appear that the difference between resignation from a job and the termination of the service is well established in service law. The two are not the same. An employee leaves the service on his volition. The employer terminates his services without his consent and against his will. We, Therefore, think that the word "leave" does not include termination of the services by the employer. If so, clause 10 would not

apply at all and the very basis of the injunction sought disappears. As for clause 11 if any secrets as having been passed on to the defendant had been pleaded by the plaintiff and the facts pleaded could have shown that they were trade secrets the plaintiff would have been entitled to a temporary injunction against the defendant ordering the defendant not to divulge these trade secrets. Since the meaning of the pleadings and of the law applicable is totally different in our view as compared to the view of the learned single Judge, we are constrained to interfere with the order under appeal.

25. The appeal is allowed and the temporary injunction is vacated. There will be no order as to costs.

26. Appeal allowed.