These Two Applications Are Filed By The vs Green ((1895) 2 Q.B.315) And Submitted ... on 10 July, 2012

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Bench: R.Subbiah

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 10.07.2012

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THE HON'BLE MR. JUSTICE R.SUBBIAH

Original Application Nos.356 and 357 of 2012
and Application No.2352 of 2012 in
Civil Suit No.292 of 2012

ORDER

These two applications are filed by the applicant/plaintiff to pass an order of interim injunction restraining the respondent/defendant from directly or in its capacity as sub-contractor to any of the competitors of the applicant, taking orders from any of the customers of the applicant and also from disclosing any confidential information, including knowhow, trade secrets, business and commercial information, which has been furnished to the respondent by the applicant, to any third parties.

2. The case of the applicant, in brief, is as follows:

> The applicant/plaintiff is a leading global OEM (Original Equipment Manufacturer) and has been supplying cement plant machinery, spare parts and services to various customers in India and globally for the past 128 years. The applicant and its sister concerns supply the cement and mineral industries globally with everything ranging from engineering, single machines and complete processing plants, to maintenance, support services and operation of processing facilities and they have developed a vast global pool of specialised engineering resources that is unique to the cement industry. Continuous research is the cornerstone of the applicant's growth, with special

emphasis on use of alternative fuels, reducing emissions and waste, improving heat recovery, decreasing power consumption, minimising water consumption, increasing plant capacity, availability and operating efficiently and minimising safety risks. The applicant, being a part of an international conglomerate, its Research and Developmental activities take place globally in various centres of excellence. The conglomerate's Dania test centre in Denmark is the cement industry's largest with laboratories and pilot testing facilities for global projects, including a broad range of emissions and environmental solutions for new and existing plants. The customer base of the applicant is wide ranging and includes reputed players in the cement industry, such as Madras Cements Ltd., Chettinad Cements, Binani Cements Ltd., JK Lakshmi Cements, ACC Limited, Ambuja Cements, Rain Cements, Dalmia Cements, Ultratech Cements Ltd., etc.

3. It is the further case of the applicant that in the course of its above detailed business activities, the applicant had developed the respondent as a vendor for manufacturing heat resistant castings, such as dip tubes/casted central tubes, kiln outlet sector, Inlet sectors etc., for the cement industry and supplying the same to the customers of the applicant. These castings were to be manufactured by the respondent strictly in accordance with the specifications and requirements of the applicant. Apart from this, the respondent were also manufacturing various connected ancillaries such as grizzly bars, parts of cast central tube, namely, hanger elements, top elements, etc. Several proprietary information and material belonging to the applicant, such as technical and manufacturing drawings, material specifications and documents containing knowhow, created specifically by the applicant were furnished to the respondent. The respondent's mandate was to use these drawings/prototypes to manufacture the final product, after approval of the model by the applicant, and to supply the same to the applicant for final supply to the end-user.

4. It is the further case of the applicant that to protect the confidentiality and secrecy associated with the applicant's trade secrets due to their innovativeness and high commercial significance, the applicant had entered into a Non-Disclosure Agreement dated 22.05.2006 with the respondent. Subsequent to the execution of non-disclosure agreement, the applicant passed on several vital proprietary information including technical drawings, trade secrets, quality requirements and means/ways to achieve the required quality for the part/product and information pertaining to its customers, to the respondent. The respondent started manufacturing different parts for the cement industry based on the primary contract between the applicant and its customers. While so, after two years, the applicant came to know of a serious violation of the agreement dated 22.05.2006 as well as breach of fiduciary duty on the part of the respondent. In November, 2008, the applicant came to know that the respondent had directly taken an order from a customer of the applicant, namely, Madras Cements and had written to the respondent in this regard vide letter dated 12.11.2008. The respondent's Managing Director Mr.V.Veluswamy had come to the applicant's office and given an undertaking not to continue such conduct. Though the applicant took the undertaking of the respondent as a positive assurance from their part, they stopped giving any further orders for execution to the respondent; but did not formally terminate its contractual arrangement with the respondent. But the respondent, by taking undue advantage of the information given to them by the applicant, has directly approached most of the applicant's existing customers such as Madras

Cements, Chettinad Cements, etc., with price quotation for supply of casted central tubes/dip tubes and other castings in accordance with the applicant's technical drawings, specifications, technical knowhow and entered into contracts with them for supply of casted central tubes and dip tubes and other castings, which is in gross violation of the terms of the Non-Disclosure Agreement. Hence, the applicant issued a legal notice dated 11.11.2011 asking the respondent to furnish a list of its customers/clients with whom it had shared the applicant's confidential information. The respondent sent an evasive reply to this notice. Thereafter, the applicant issued another legal notice dated 25.01.2012 and for which, the respondent sent a reply conceding that it has directly approached Madras Cements, a leading customer of the applicant. Though the applicant issued another legal notice to refrain them from taking any order from the customers of the applicant, there was no response from them till date. Due to the respondent's conduct, the applicant has suffered a loss of sales in dip tubes alone to its existing customers, ranging about Rs.10 to 12 crores. Hence, the plaintiff filed the suit along with the said applications.

5. This Court, by order dated 25.04.2012, granted an order of interim injunction in O.A.No.356 of 2012 and ordered notice to the respondent in O.A.No.357 of 2012.

6. On appearance, the respondent has filed a counter as well as Application No.2352 of 2012 to vacate the interim injunction granted in O.A.No.356 of 2012, stating that the relief sought for by the applicant is contrary to law as it restricts the respondent's fundamental rights to trade apart from seeking to restrict the competition and, therefore, ought to be rejected in limini. The further relief sought for to restrain the respondent from disclosing any confidential information of the applicant to any third party is without any basis. The relief sought for by the applicant/plaintiff is for the enforcement of the Non-Disclosure Agreement dated 22.05.2006 which is void since the agreement is contrary to section 27 of the Contracts act. Clause 6 of the agreement says that the respondent is restricted from quoting directly to the applicant's customers. The Non-Disclosure Agreement does not provide a list of the applicant's alleged customers which the applicant has now sought to attach with the Judge's summons.

7. It has been further averred by the respondent that the respondent is a small scale unit started in the year 2000 and is in the business of jobbing foundry works which manufactures castings and other parts based on individual customer specifications and drawings. The respondent manufactures around 340 items of equipment of its own based on the respondent's own research and development and have developed its own standards. The respondent is in the business of the manufacture of heat resistant castings such as dip tubes, central tubes and immersion tubes for almost 12 years. They have been supplying the products directly and indirectly to the cement companies both as a sub-contractor as well as a direct vendor. Even before the non-disclosure agreement dated 22.05.2006, the respondent was supplying to M/s.India Cements Limited. In fact, the applicant approached the respondent to act as its sub-contractor because it was aware of their experience with the cement industry. The arrangement between the applicant would be for a period of 5 years, but the applicant did not proceed with the arrangement beyond January 2009 since the applicant has terminated the agreement by their letter dated 06.01.2009, whereby it requested the respondent to return all the applicant's patterns since it had started its own foundry division. It is also reiterated that in any case, there has not been any violation of the trade secrets of the applicant.

The respondent has duly returned all the information, material and drawings including the patterns to the applicant. The respondent had always been manufacturing and supplying for various industries including the cement industry even prior to the agreement with the applicant. It is vehemently denied that there has been any violation of the agreement dated 22.05.2006 or any alleged breach of fiduciary duty by the respondent. In short, it is the contention of the respondent that the relief sought for by the applicant would amount to restrict the respondent's fundamental rights and is contrary to section 27 of the Contract Act and as such, the prayers cannot be allowed. Thus, he prayed for the dismissal of the applications.

8. Learned Senior Counsel appearing on behalf of the applicant would submit that the plaintiff is a leading global OEM and has been supplying cement plant machinery, spare parts and services to various customers in India. They have developed the respondent as a vendor for manufacturing heat resistant castings such as dip tubes/casted central tubes, etc. They have also furnished several proprietary information and material belonging to the applicant, such as technical and manufacturing drawings, material specifications and documents containing knowhow, to the respondent. For this purpose, a Non-Disclosure Agreement dated 22.05.2006 was entered into by the applicant with the respondent. Under Clauses 1 to 4 of the agreement, the defendant agrees that the confidential information would not be disclosed or made available by them directly or indirectly to any third parties without prior written consent of the applicant. Clauses 1 to 4 are non-competitive clauses. A reading of the said clauses would show that the information passed on to the respondent including access to the applicant's clients is only in fiduciary position of the respondent in its dealing as a sub-contractor. Clause 6 is a non-solicitation clause. Section 27 of the contracts Act does not prohibit any contractual obligation of non-solicitation, as any genuinely worded non-solicitation clause only meant to bring in fairness and transparency in business operations and thus, the agreement is not in restraint of trade. In this regard, the learned senior counsel for the applicant, by inviting the attention of this Court, to sections 36(1)(c) and 55 of the Partnership Act submitted that under section 36(1)(c), the solicitation by the outgoing partners to carry on competing business with the customers of firm before he ceased to be a partner is prohibited. Similarly, section 55(2), which deals about the rights of buyer and seller of goodwill, says that where the goodwill of a firm is sold after dissolution, a partner may carry on a business competing with that of the buyer and he may advertise such business, but he may not solicit the custom of persons who were dealing with the firm before its dissolution. Therefore, non-solicitation of the customers of the firm by the outgoing partner is recognised under law. Therefore, it cannot be said that under the provisions of section 27 of the Contract Act, the respondent's fundamental rights to trade is restricted since clause 6 of the agreement entered into between the parties prohibits the respondent from soliciting the applicant's customers.

9. The learned senior counsel for the applicant further submitted that clause 6 of the Agreement, which consists two parts, i.e. (i) during the period of agreement and (ii) for further period of five years from the date of termination under the provisions of the agreement, says that the vendor should not quote directly to the customers or not to engage in activities of competing nature which are detrimental to the interest of the applicant. Thus, the learned senior counsel submitted that the said provision does not restrict the right of the respondent to do trade and it only says that the respondent should not solicit the customers of the applicant, that too, only for a further period of

five years. Therefore, it is not violative of the provisions under section 27 of the Contract Act. In this regard, the learned senior counsel relied on the judgment reported in Robb .vs. Green ((1895) 2 Q.B.315) and submitted that the principle held in that case will be applicable to the case on hand, wherein the defendant, who was in service of the plaintiff, copied from the plaintiff's order book, at a time when, as he himself admitted, he thought nobody could see him, a list of the plaintiff's customers, not for the purpose of using it for the benefit of his master, but for the purpose of keeping it unknown to his master, and using it, as soon as he left the plaintiff's service, so as to get hold of the plaintiff's customers and induce them to transfer their custom to himself. On this background, the Queens Bench granted an injunction on an observation that in equity, the plaintiff was entitled to an injunction in respect of the breach of faith which he was committing and which he appeared likely to continue in future. In this regard, the learned counsel has also relied upon a judgment reported in Landmark Brickwork Ltd., .vs. William Sutcliffe ((2011) EWHC 1239 (QB) and John Richard Brady .vs. Chemical Process Equipments Pvt.Ltd., (AIR 1987 Del.372). Hence, the applicant is entitled to the reliefs as prayed for in the applications.

10. Per contra, the learned Senior Counsel for the respondent/defendant submitted that the defendant is doing business from the year 2000. The respondent is supplying castings and casting components to various customers in industries such as cement, steel, fertilizer, etc., and they entered into an agreement with the applicant in the year 2006. The learned senior counsel further submitted that the respondent are not sub-contractors. The agreement is on principle to principle basis. In this regard, the learned senior counsel relied on a letter dated 06.01.2009 and submitted that after January, 2009, there was no transaction between themselves and the applicant. The applicant had started their own foundry at Arakkonam and they requested the respondent to return all the applicant's patterns. In this regard, the learned senior counsel also relied on the minutes of the meeting and submitted that the applicant made an inspection and taken back all the patterns from the respondent and after 2009, virtually, there is no business transaction with the applicant. In this regard, the learned senior counsel, by relying upon the judgments reported in Niranjan Shankar Golikari .vs. The Century Spinning and Mfg.Co.Ltd., (AIR 1967 SC 1098), M/s.Gujarat Bottling Co.Ltd., .vs. Coca Cola Co.and others (AIR 1995 SC 2372), Superintendence Company of India (P) Ltd., .vs. Sh.Krishnan Murgai (AIR 1980 SC 1717) and Percept D'Mart (India) Pvt.Ltd., .vs. Zaheer Khan and another (AIR 2006 SC 3426) submitted that clause 6 of the agreement is void in nature. After the agreement period is over, the applicant cannot enforce the covenants in the contract to restrain the defendant from doing business with any persons including the customers of the applicant. In short, it is the submission of the learned senior counsel for the respondent that after the contractual period, negative covenant of the agreement cannot be enforced since the post contract restriction is not legally valid. Further more, the said clause is against the provisions of section 27 of the Contract Act. Therefore, the applications are liable to be dismissed.

11. This Court has paid anxious consideration on the submissions made by both parties and perused the materials available on record.

12. Though the learned senior counsel appearing on either side have made elaborate arguments by inviting the attention of this Court to various documents, the core question that has to be considered in this case is, Whether clause 6 of the agreement is a non-solicitation clause and if it is enforced

Whether the same would amount to violative of the provisions under section 27 of the Contract Act ? and whether a negative covenant can be enforced after the expiry of the agreement period ?

13. The factual aspects found in this case would show that the applicant/plaintiff, who is a leading global OEM and is supplying cement plant machinery, entered into a Non-Disclosure Agreement with the respondent and developed the respondent as a vendor for manufacturing heat resistant castings such as dip sectors etc., for the cement industry and supplying the same to the customers of the applicant. Clauses 1 to 4 of the Agreement are non-competitive clauses, which are restraining the respondent from disclosing confidential information supplied by the applicant to any third party directly or indirectly without the consent of the applicant. Clause 6 prohibits the respondent from quoting directly to the customers of the applicant and from engaging the activities of competitive nature during the period of agreement as well as for a period of five years from the date of termination of the agreement. The main issue is only with regard to the enforcement of clause 6. So, it would be appropriate to extract clause 6 and it reads as follows:

> "During the period of this agreement and for further period of 5 years from the date of termination under the provisions of the agreement, VENDOR covenants not to quote directly to customers or not to engage in activities of competing nature which are detrimental to the interest of FLS".

clauses 1 to 4, the non-competitive clauses read as follows:

> "1. All date, drawing, and technical information, whether oral or written ("Confidential Information") which is disclosed or made available to VENDOR or its employees by FLS either directly or indirectly, in writing or orally, will be treated by VENDOR as being strictly confidential and will not be disclosed or made available by VENDOR directly or indirectly to any third party without prior written consent of FLS.
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> 2. VENDOR shall take all necessary steps to preserve the strict confidentiality of all such Confidential Information and agrees that the same shall be made available only to those of its officers and employees as shall have a need to know the same for the purpose set forth herein.
>
> 3. VENDOR will ensure that its employees or agents who may come in contact with such Confidential Information will abide by the provisions of this Agreement.
>
> 4. VENDOR agrees that it will neither confirm nor deny to any third party that any drawings or Information furnished to VENDOR by some other source are identical with or similar to the Confidential Information furnished hereunder".

It is the submission of the learned senior counsel for the applicant that the respondent, by directly quoting the customers of the applicant, has violated the said clauses of the agreement, and as such, the respondent should be restrained by way of granting interim injunction.

14. Per contra, it it is the submission of the respondent that the post-contract restriction contained in clause 6 is not legally valid and is against the provisions of section 27 of the Contract Act because it restrains the right to trade by a person, whereas, according to the applicant, clause 6 of the agreement cannot be construed as a post contract restriction and on the other hand, it is only a clause imposing non-solicitation and it prevents the respondent from soliciting only with the customers of the applicant and not preventing the respondent from doing business. So, the respondent can always do business with the others except the customers of the applicant for a period of five years from the date of expiry of the agreement dated 22.05.2006. Therefore, clause 6 cannot be construed as a clause restring the right to trade.

15. It is the further contention of the applicant that clause 6 prohibits the respondent from quoting the prices to the customers of the applicant only for a period of five years from the date of termination of the agreement. Therefore, at any cost, it cannot be construed that the said clause is in violative of the provisions under section 27 of the Contracts Act. In this regard, the learned senior counsel for the applicant invited the attention of this Court to sections 36(1)(c) and 55 of the Partnership Act and submitted that section 36(1)(c) which recognised the rights of outgoing partner to carry on competing business, says that the outgoing partner may not solicit the custom of persons who were dealing with the firm before he ceased to be a partner. Section 55 also recognised the rights to buyer and seller of goodwill and it says that a partner may not solicit the custom of persons who were dealing with the firm before its dissolution. Therefore, prohibiting the person from doing solicitation to the customers of the applicant under the clauses of agreement, that too, for a particular period, is not against law and it cannot be said that the same is restraint of trade. In this regard, the learned senior counsel for the applicant has also relied upon the judgment reported in (1895) 2 Q.B.15 (supra), wherein the relevant paragraphs are extracted hereunder:

> "In this case the defendant, while he was in the service of the plaintiff, copied from the plaintiff's order-book, at a time when, as he himself admitted, he thought nobody could see him, a list of the plaintiff's customers, not for the purpose of using it for the benefit of his master, but for the purpose of keeping it unknown to his master, and using it, as soon as he left the plaintiff's service, so as to get hold of the plaintiff's customers and induce them to transfer their custom to himself. The question is whether such conduct was not what any person of ordinary honesty would look upon as dishonest conduct towards his employer and a dereliction from the duty which the defendant owed to his employer to act towards him with good faith. I think the judge was perfectly justified in holding that such conduct was a breach of the trust reposed in the defendant as the servant of the plaintiff in his business. The question arises whether such conduct is a breach of contract. That depends upon the question whether in a contract of service the Court can imply a stipulation that the servant will act with good faith towards his master. In this case it is said that the contract of service was in writing; but there is nothing in the express terms of the contract that contradicts such an implication. I think that in a contract of service the Court must imply such a stipulation as I have mentioned, because it is a thing which must necessarily have been in view of both parties when they entered into the contract. It is impossible to suppose that a master would have put a servant into a confidential

> position of this kind, unless he though that the servant would be bound to use good faith towards him; or that the servant would not know, when he entered into that position, that the master would rely on his observance of good faith in the confidential relation between them. Where the Court sees that there is a matter of this kind which both parties must necessarily have had in their minds when entering into a contract, that is precisely the case in which it ought to imply a stipulation. We have the authority of Bowen L.J. In the case of Lamb v.Evans that there is such an implication in a contract of service. He said in that case, after stating that there is no distinction between law and equity as regards the law of principal and agent: "The common law, it is true, treats the matter from the point of view of an implied contract, and assumes that there is a promise to do that which is part of the bargain, or which can be fairly implied as part of the good faith which is necessary to make the bargain effectual. What is an implied contract or an implied promise in law ? It is that promise which the law implies and authorizes us to infer in order to give the transaction that effect which the parties must have intended it to have, and without which it would be futile". Therefore, I think the learned Judge in the Court below was quite right in making the implication he did, and holding that there was a breach of that implied contract which entitled him to award damages to the plaintiff. Then with regard to the injunction, I think it is quite clear that in equity the plaintiff was entitled to an injunction against the defendant in respect of the breach of faith which he was committing, and which he appeared likely to continue in future. For these reasons I think the judgment must be affirmed".

16. This judgment was followed in the other cases relied upon by the learned senior counsel for the applicant. But I find that, as submitted by the learned senior counsel for the respondent, the contract entered into the parties on 22.05.2006, came to an end on 21.05.2011. It is the submission of the respondent that clause 6 could be enforced only during the existence of the agreement and not beyond the agreement. Moreover, in the instant case, from January 2009, there was no transaction between the respondent and the applicant because the applicant started its own factory at Arakkonam. At this stage, it would be appropriate to see the judgment relied on by the respondent. In AIR 1995 SC 2372 (supra), the Hon'ble Supreme Court of India has held as follows:

> "35. Similarly, in Superintendence Company of India (P) Ltd., .vs. Krishan Murgai (MANU/SC/0457/1980) A.P.Sen J., in his concurring judgment, has said that "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".

36. Shri Shanti Bhushan has submitted that these observations must be confined only to contracts of employment and that this principle does not apply to other contracts. We are unable to agree. We find no rational basis for confining this principle to a contract for employment and excluding its application to other contracts. The underlying principle governing contracts in restraint of trade is the same and as a matter of fact that courts take a more restricted and less favourable view in respect of a covenant entered into between an employer and an employee as compared to a covenant between a vendor and a purchaser or partnership agreements. We may refer to the following

observations of Lord Pearce in Esso Petroleum Co.Ltd., .vs. Harper's Garage (Stourport) Ltd., (1968) AC 269).

When a contract only ties the parties during the continuance of the contract, and the negative ties are only those which are incidental and normal to the positive commercial arrangements at which the contract aims, even though those ties exclude all dealing with others, there is no restraint of trade within the meaning of the doctrine and no question of reasonableness arises. If, however, the contract ties the trading activities of either party after its determination, it is a restraint of trade, and the question of reasonableness arises.(p.328)"

17. A reading of the above decision would show that the negative covenant in agreement could be enforced only during the pendency of the contract and not beyond the expiry of the agreement period. Therefore, I am of the opinion, as contended by the learned counsel for the respondent that there cannot be any post-contract restriction. Under such circumstances, the judgment relied upon by the learned senior counsel for the applicant based on the judgment rendered by the Queens Bench cannot be accepted. Therefore, I am of the opinion that even if clause 6 is only a non-solicitation clause, the same cannot be enforced after expiry of the agreement. In the instant case, the agreement had expired on 21.05.2011. Thereafter, the applicant has no legal right to enforce clause 6. In AIR 1967 SC 1098 (supra), the Hon'ble Apex Court has held that negative covenants operative during period of contract do not fall under section 27 of the Contract Act and it reads as follows:

"20. 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 as in the case of W.H.Milsted & Son, Ltd. (1927) W.N.233. 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 ofemployment and to work similar or substantially similar to the one carried on by the appellant when he was in the employment 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 therefore against public policy".

In view of the dictum laid down in the said judgment, I am of the opinion that the negative covenant of the agreement can be enforced only during the period of contract and the same cannot be enforced after the expiry of agreement period. Hence, even a non-solicitation clause cannot be enforced after the expiry of agreement period. Under such circumstances, I am of the opinion that the reliefs sought for by the applicant are not maintainable and the applications are liable to be dismissed since in the instant case, the contract period of five years was over by 21.05.2011 itself.

Accordingly, O.A.Nos.356 and 357 of 2012 are dismissed and A.No.2352 of 2012 is allowed.

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