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## DELHI HIGH COURT ON EMPLOYMENT AGREEMENTS

The Delhi High Court (**HC**) in the *Lily Packers* case<sup>1</sup> clarified on the enforceability of lock-in periods in employment contracts. The HC also confirmed that disputes arising from these restrictions, including lock-in periods, can be subject to arbitration when an arbitration clause is included in the employment agreement.

### Brief Facts

Lily Packers (**LP**), a company specializing in corrugated packaging manufacturing and trading, entered into separate service employment agreements (**Agreements**) with each of its employees (**Employees**).

Each Agreement included a clause stipulating a three-year lock-in period for the Employees, who did not comply with the same as below:

- Vaishnavi Vijay Umak, employed as Fashion Designer with LP, worked for one year and two months before going on leave and never returning.
- Meetkumar Patel, who worked as Autocad Design Engineer, resigned after one year and six months.
- Rahul Sharma, employed as General Supply Chain Manager, resigned without notice after only a few months, citing mental health concerns related to work stress.

In response to these premature departures, LP invoked the arbitration under the Agreements.

When the Employees refused to participate in arbitration, LP filed petitions with the HC under Section 11(6) of the Arbitration and Conciliation Act, 1996 (**Act**), requesting it to appoint an arbitrator.

### Contention of the Parties

LP contended that:

- The lock-in periods were necessary to protect its investments in employee training and to ensure stability for the organization.

The employees argued that:

- The lock-in periods were void and unenforceable as they violated their fundamental rights to life and employment as guaranteed by Articles 19 and 21 of the Constitution of India (**Constitution**). Imposing a mandatory three-year service period was an unreasonable restriction on their freedom to choose their employment.
- The disputes were not arbitrable because they violated fundamental rights. They relied on the Supreme Court decision in *Lombardi Engineering* case<sup>2</sup> (**Lombardi**) where the court struck down an arbitration clause that required the party initiating arbitration to make a pre-deposit of a percentage of their claim. This pre-deposit requirement was deemed to be an illegal barrier to accessing legal remedies and a violation of Article 14 of the Constitution.

### HC's Judgement and Reasoning

In three separate rulings, the HC confirmed the appointment of a sole arbitrator to address the disputes between LP and the Employees.

<sup>1</sup> *Lily Packers Private Limited v. Vaishnavi Vijay Umak and connected matters*, 2024 LiveLaw (Del) 777.

<sup>2</sup> *Lombardi Engineering Limited v. Uttarakhand Jal Vidyut Nigam Limited*, (2023) SCC OnLine SC 1422.

Drawing upon precedents,<sup>3</sup> it distinguished between covenants that apply during the employment term and those that apply after termination.<sup>4</sup>

It stated:<sup>5</sup>

- Reasonable covenants in force during the employment term are valid and do not violate fundamental rights. Specifically, a lock-in period is not a violation of fundamental rights as it simply requires the employee to fulfil the agreed-upon term of service.
- The lock-in period in the Agreements were a result of negotiations between the parties, who voluntarily agreed to the terms and conditions of employment.
- Lock-in periods are commonplace, particularly at executive levels, and provide stability and continuity for organizations by reducing employee attrition.

The court distinguished the *Lombardi* from the current case. It observed that the pre-deposit requirement in *Lombardi* constituted a barrier to pursuing legal remedies. In contrast, the lock-in period in the Agreements did not prevent access to legal remedies.<sup>6</sup>

It emphasized that the disputes in the current case fell within the scope of the Agreements, making them arbitrable under the Act.

It also clarified that its observations on the validity of lock-in periods would not bind the appointed arbitrator, who must independently evaluate the specific facts and circumstances of each case.<sup>7</sup>

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<sup>3</sup> *Niranjan Shankar Golikari v. Century Spinning and Manufacturing Co*, 1967 SCCOnline SC 418, and *Percept D'Mark (India) (P) Ltd. v. Zabeer Khan & Anr*, (2006) 4 SCC 227.

<sup>4</sup> Paragraphs 64, 65 and 67 of the Judgement.

<sup>5</sup> *Ibid*.

<sup>6</sup> Paragraph 76 of the Judgement.

<sup>7</sup> Paragraph 84 of the Judgement.