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SC validates PSU bond clause; legal experts say private sector unlikely to be impacted

Synopsis

The Supreme Court has validated Vijaya Bank's employment clause, mandating officers to serve three years or pay ₹2 lakh for early resignation. The court emphasized that this is reasonable for PSUs due to their extensive recruitment processes. Experts believe this ruling primarily impacts public sector undertakings and is unlikely to significantly alter private sector employment agreements.



In a significant ruling that clarifies the employment contracts in public sector undertakings (PSUs), the Supreme Court has upheld the validity of [Vijaya Bank](#)'s employment clause that required officers to serve a minimum of three years or pay two lakh rupees as liquidated damages in case of premature resignation.

The division bench of Justice Pamidighantam Sri Narasimha and Justice Joymalya Bagchi, while ruling in favour of the Vijaya Bank, observed that the stance of the bank is neither unjust nor unreasonable.

"The appellant-bank (Vijaya Bank) is a public sector undertaking and cannot resort to private or ad-hoc appointments through private contracts," observed the Apex Court in its order of May 14. "An untimely resignation would require the Bank to undertake a prolix and expensive recruitment process involving open advertisement, fair and competitive procedure lest the appointment fall foul of the constitutional mandate under Articles 14 and 16," it further added.

The case may clarify the position of law in the case of public sector undertakings, but legal experts are of the view that it is unlikely to have any [impact on private sector employment agreements](#).

Apeksha Mattoo, Partner - Labour & Employment Law Practice at the law firm Trilegal, said bearing in mind past precedent, employees working in the private sector have not been required to make payments in case of premature cessation of employment which breaches an employment bond unless the employer had borne any expenses for specialized training of such employee, and the bond specifies the quantum of the liquidated damages that are

SECTIONS

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damages incurred by the employer (in monetary terms).

“This is because the public sector undertakings cannot deviate from the set procedures, so the cost of replacing an employee is fairly high. (PSUs) have an elaborate and detailed recruitment process, which is time-consuming, and such companies incur higher costs given that there is a loss of continuance of the role,” she added.

In this case, a former probationary assistant manager at Vijaya Bank had accepted the promotion to a senior manager in 2007 under the new terms that included the clause which required a minimum three-year service tenure or payment of two lakh rupees if the officer resigned earlier. However, in 2009, he resigned to join **IDBI Bank** and paid the amount in protest. He subsequently challenged the clause, alleging it was unconstitutional and against public policy. The High Court had ruled in his favour, terming the clause coercive and disproportionate. Later, the public sector lender had challenged the ruling.

Pooja Tidke, Joint Managing Partner, Parinam Law Associates, said the judgment emphasises the need to evaluate restrictive covenants through the lens of reasonableness, keeping in mind the nature of the challenges that surround the covenantee in present-day market conditions. “In this particular case, the fact that the covenantee was a public sector undertaking and would be required to go through an elaborate recruitment process owing to the employee’s pre-mature resignation weighed in its favour,” adds Tidke.

The Supreme Court also dismissed the argument that the clause was opposed to public policy, noting that public sector banks, post-liberalisation, operate in a competitive environment and must retain skilled manpower to maintain efficiency. It observed that attrition due to premature resignations imposes significant costs on PSUs, including the need for fresh recruitments through expensive and time-consuming public processes.

Debjani Aich, Partner and part of the Employment Practice Group at the law firm IndusLaw, said the Vijaya Bank case and the Hon’ble Supreme Court’s judgement are not a new position in law, as employment bonds have been quite common in India, including in the private sector.

“This case reinforces the differentiation between an employment bond and a post-termination non-compete restriction on an employee,” said Aich.

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