

Lean and Mean via Lay-Offs

Managing a company is a difficult and enormous task. A paramount apprehension of any investor, domestic or foreign, relates to the management of labour, a fear which is compounded by the complexities in the plethora of India's employment laws. Priti Suri of PSA, Legal Counsellors examines just what employers should be prepared for in case of lay-offs.



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India's emergence and moment as a powerhouse of opportunities has arrived. The country offers a prosperous environment for both manufacturers and service providers and a large market with resources to buy the finished products and services. Therefore, it is not surprising that multinational corporations are making a beeline towards India and that mergers and acquisitions activity is at an all time high. However, entry into a new market inevitably brings its own set of problems, including managing an industrial unit, which is no mean task. A paramount apprehension of any investor, domestic or foreign, relates to the management of labour, a fear which is compounded by the complexities in the plethora of employment laws. This article describes a key concern – lay-offs – both for the employer and the employee and focuses on the mechanism of compensation and related judicial interpretations.

Circumstances of lay-offs

The primary legislation that governs the investigation and settlement of industrial disputes is the *Industrial Disputes Act, 1947* (the ID Act). Any dispute referred for adjudication under the ID Act must relate to the terms and conditions of employment of a "workman" who, under Section 2(s) of the ID Act, is a person employed in an industry to perform skilled, unskilled, technical or operational jobs but which excludes white-collar employees.

The ID Act recognizes that business exigencies may compel an employer to temporarily discharge labour. Such a temporary discharge of labour is lay-off. Section 2(kkk) of the ID Act provides the situations under which an employer can lay-off his employees

and states that "lay-off means the failure, refusal or inability of an employer on account of shortage of coal, power or raw materials or the accumulation of stocks or the breakdown of machinery or natural calamity or for any other connected reason to give employment to a workman..." The critical aspect is the failure, refusal, or inability of an employer to provide work to an employee for the reasons enumerated in the definition which, effectively, means that lay-off is not connected with the performance of an employee. By incorporating "any other connected reason", the legislature has limited the scope of the definition to only those conditions connected with the reasons provided in the definition.

The courts have given varied interpretations to "any other connected reason". In *Hope Textiles Limited vs. State of Madhya Pradesh*, the Court

held that, "a financial stringency is not a cause for which 'lay-off' could be imposed." Conversely, in *SAE Mazdoor Union vs. Labor Commissioner*, the Court stated that, "the application for a lay-off, on account of 'lack of adequate orders' to run the industry would fall within the scope of 'connected reasons', and the continuance of production, would only lead to accumulation of stocks..." Thus, the courts examine the merits of each case to determine if the reason for lay-off falls within the ambit of the application.

The explanation appended to Section 2(kkk) introduces a fiction in the definition and provides that if a workman comes for work and is not assigned work within two hours, he will be deemed to be laid-off for the entire day. However, if a workman, who has been asked to appear for the second half of the day, presents himself and is given a task, he shall be considered laid-off for the first half of the day. But, if the employer is still unable to allocate any work in the second shift, the workman shall be entitled to full basic salary for that part of the day. Therefore, the definition provides that lay-off can take place at any time during the course of a working day.

The ID Act does not specifically grant an automatic right to the employer to lay-off the workmen in the specified circumstances. In order to establish an employer's right to lay-off, it is essential to rely on either the contractual employment terms or the Standing Orders formulated pursuant to the *Industrial Employment (Standing Orders) Act, 1946*, in which the employers define applicable conditions of employment in their establishment. Prior to laying-off any employee, an employer must take prior permission from the relevant authorities. In lay-off, the employer-employee relationship

is not terminated but is kept in abeyance or temporary suspension. An employer is under an obligation to re-appoint all the laid-off workmen as soon as normal working recommence and, thereafter, workmen are entitled to receive full salaries. However, it is important that an employer should not, under the garb of lay-off, continue to keep his employees under temporary suspension and deny their full salaries even though the ID Act does not specify the period for which lay-off can continue.

A lay-off for a short period is treated as compulsory leave, either with or without salary, while in a lay-off for an indefinite period, the employment can be terminated upon giving due notice or salary in lieu thereof.

Pre-conditions and quantum for compensation

Chapter 5A of the ID Act outlines the procedure for lay-off which applies only to those industrial units which employ an average of more than 50 workmen per working day in the previous month. The provisions of the chapter do not apply to industries which function seasonally. Thus, liability to pay any compensation for lay-off does not arise if less than 50 workmen work in an establishment.

An employee is entitled to compensation for lay-off provided he was in "continuous service" for 240 days within a period of 12 months from the day of lay-off. While calculating continuous service, breaks due to sickness, sanctioned leave, accident, legal strike, lockout and termination of work not due to the employee's fault are taken into account. Effectively, this implies a workman should be considered in continuous service not only on the days when he actually worked but also on the days on which he could not work due to his own inability to perform (due to illness or for being absent from work) or days on which he had been prevented from working by the employer (due to lockout or stoppage of work).

Lay-off compensation is a statutory right and failure to pay entitles the workman to take legal recourse to recover such amounts. To be entitled to lay-off compensation, it is essential that a workman present himself for work at the factory, at the designated time, on every working day during normal working hours. It is obligatory upon the employer to maintain attendance registers so that the employees can mark their presence. Whenever a workman is laid-off, he is entitled to receive compensation for all the days during which he is laid-off except for weekly holidays. The quantum of lay-off compensation is 50% of the basic wages and dearness allowance payable to a workman if he had not been laid-off. Dearness allowance is an all-cash payment paid to an employee to meet the rising cost of living.

Payment of compensation is not a condition precedent for lay-off.

An employee is only entitled to receive compensation but, unlike retrenchment, there is no stipulation about the timing of the payment. The Bombay High Court in *KT Rolling Mills vs. MR Meher* held that "compensation for lay-off cannot, therefore, be awarded in advance of actual lay-off and on grounds of social justice." Further, to require an employer to pay compensation prior to laying-off is neither possible nor feasible as it may defeat the purpose of lay-off especially during extreme urgency.

The provisos to Section 25C of the ID Act, which prescribes payment of compensation, states that an employer is entitled to pay compensation for lay-off beyond 45 days, whether the period is continuous for a week or not, unless there is an agreement to the contrary. The second proviso gives an option to the employer: If the period of lay-off exceeds 45 days, the employer can either continue to pay compensation for subsequent periods as prescribed in the section or choose to retrench the employee in accordance with the relevant procedure.

In adjudicating cases of lay-off compensation, the courts usually do not intervene or step into the shoes of the management to enquire whether the employer could have avoided the lay-off unless the workmen plead *mala fide*. In *Tatanagar Foundry Company Limited vs. Its Workmen*, Supreme Court held that courts have the right to intervene if the workmen plead mala fide intentions of the management for their lay-off.

Employee disentitled to compensation

Section 25E of the ID Act states that an employee is barred from claiming any compensation if a workman refuses to accept alternate employment or defaults in presenting himself for work. Another condition whereby an employer is not liable to pay compensation is if lay-off is due to a strike or "go slow" by the employees.

If an employer offers an alternate job in the same factory from where the employee is laid-off or in another location in the same city, town, village or in a radius of five miles from the current place of employment and the employee refuses to accept the alternate employment offered to him, he shall not be entitled to lay-off compensation. However, the employer must ensure that the job offered does not require any special skill or prior experience and that the employee being laid-off can perform it. Further, it should not reduce the status, benefit and salaries of an employee. But, in *JK Cotton Spinning and Weaving Mills vs. Its Workmen*, the court held that, "the term 'alternative' could only mean 'other jobs' and it had no reference to nature of employment".

According to section 25E of the ID Act, failure to present himself at least once a day during normal working hours also disentitle an

employee to claim lay-off compensation. In *Zandu Pharmaceutical Works Limited vs. RN Kulkarni*, the Bombay High Court held that “if [a] laid-off workman fails to report for the work even once a day, the employer is absolved from the liability of paying the lay-off compensation”.

The employer is absolved of his responsibility to pay compensation if certain key employees strike or slow down the production in another part of an establishment in a manner which would compel the employer to shut down the factory. In *Zandu Pharmaceuticals*, it was held that workmen laid-off because of a strike by other workmen in the same establishment were not entitled to lay-off compensation. Similarly, in *Management of India Radiators Limited vs. PO, Second LC* it was stated that if the workmen adopt the tactic of slowing down the production to pressurize the management to accept their demands, the workmen shall not be entitled to any compensation for lay-off.

Conclusion

Managing an industry is a difficult and enormous task. Situations may arise when the management must resort to stringent actions,

so it is pertinent to safeguard its interests from undue liabilities. Precautionary and preventive steps taken in the initial stages of establishing a business can reduce the exposure to liability and serious problems. Lay-off provisions in the Standing Orders must be unambiguous, or the courts will rely upon the lay-off provisions of the ID Act. The Standing Orders should define the grounds for lay-off in as much detail as possible and cover varied ground, including conditions that may quantify the time of prior notice given to the employees and the duration of payment of the compensation. If management elects not to describe processes in the Standing Orders, the employment contract must contain provisions enabling the employer to lay-off in accordance with law in certain situations.

Although India has much to offer in the industrial sector, labour is a major deterrent which, at times, keeps the investors at bay. The Indian legal system has socialist leanings with courts usually adopting the principles of social justice. India's strength and potential in the service industry is well-known but, in order to compete with China and other Asian economies in manufacturing, the government will have to shed its protectionist policies. As India marches on to become a powerhouse, it is imperative that



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the government implements reform in labour laws and integrates that reform with the economic reforms process. Financial success coupled with cost-effective customer service and an adherence to delivery schedules have emerged as key criteria for the evaluation of the success of companies. For Indian companies to progress further and become truly global, labour reforms must become a priority agenda for the legislature.

About the author

Priti Suri is the proprietor of PSA, Legal Counsellors. She has more than two decades of experience on three continents in diverse areas of international commercial law, mergers and acquisitions, joint ventures,

technology transfers, and arbitration and litigation. After earning an LL.M. in the United States, she took part in the ABA's International Legal Exchange programme and worked at law firms in the US. Based in Paris in the early 1990s, she returned to India in February 1997 to set up the practice in New Delhi. She continues to represent several clients in a broad spectrum of industry ranging from automobiles, defence, energy, information technology, infrastructure, pharmaceuticals and telecommunications. Suri has also authored and edited two books, Open Source and the Law (the first book on the subject in India) and FDI Notifications: An Anthology, both published by LexisNexis Butterworths, India.

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