Rightsizing and Outsourcing: The Legal Implications

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HAC POPPEN

The traditional role of personnel or industrial relations managers has undergone a sea change. Today, when we talk of the new role of HR professionals, most people have in mind the role HR professionals have to play in right-sizing [a euphemism for down sizing] and contracting out jobs which were hitherto done departmentally through regular or casual workmen directly employed by employers.

Through this paper, I would like to draw the attention of this august body of HR professionals to the legal implications some of our labour laws have on our attempts at right sizing and contracting out of jobs to make our industries more globally competitive. However, this right sizing and out sourcing is often done without a clear understanding of the concerned labour enactments. The following acts have a direct implication in this regard.

HAC Poppen is Professor, Rajagiri School of Management, Kochi

1. Industrial Disputes Act, 1947 [on right sizing]
2. Contract Labour [R&A] Act, 1970 [on contracting out]
3. ESI Act, 1948 [on contracting out]
4. EPF Act, 1952 [on contracting out]
5. Workmen's Compensation Act, 1923 [on contracting out]
6. Minimum Wages Act, 1948 [on contracting out]
7. Inter-State Migrant Workers Act, 1979 [on contracting out]
8. Factories Act, 1948/Plantation Act 1951/Motor Transport Act, 1961 [on contracting out]

Aspects of Industrial Disputes Act, 1947 having implications on right sizing and outsourcing

Workmen's right to object to contracting out or right sizing:

a. As per section 2(k) of the I.D. Act, categories of employees in industry falling under the definition of 'workmen' as per section 2(s) can raise a dispute objecting to outsourcing of jobs or downsizing of the current workforce in industry.

b. According to section 9(A) read with item 10 of schedule IV and section 33(1), any "rationalization, standardization, or improvement of plant or technique which is likely to lead to retrenchment of workmen" will require prior notice of 21 days and obtaining the consent or agreement of the workmen or alternatively getting their dispute resolved through adjudication by labour courts or tribunals.

c. According to section 2(ra), 25(T), 25(U), schedule V (item 6), "abolition of work of a regular nature being done by workmen, and to give such work to contractors as a measure of breaking a strike" amounts to unfair labour practice which can attract the penalty of imprisonment up to six months or fine up to rupees one thousand or both.

d. According to section 25(N), 25(O), and 25(K), establishments which have an average workmen, strength [during the 12 months preceding the date of retrenchment] of 100 or more will need to obtain prior permission from the government before effecting any retrenchment or reduction of their workforce or closing of any unit if the establishment falls under the category of "Factory" or "Mine" or "Plantation".

e. According to section 25(H), any employer who restarts operation after retrenching his workmen has an obligation to give preference in re-employment to such workmen [even to those retrenched workmen who had not qualified for receiving retrenchment compensation by not putting in the qualifying attendance of 240 days as per section 25(B)].

Note:

i. However, if the workmen depart under an agreed VRS scheme, they shall not be eligible to claim re-employment.

ii. Such VRS scheme should ensure payment of compensation higher than the compensation of 15 days wages prescribed under section 25(F).

iii. Government is contemplating raising of the statutory compensation under section 25(F) from 15 days to 45 days per year of service and dispense with the requirement of obtaining prior permission for retrenchment from government for establishments employing less than 1000/500 workmen.

iv. If such enhancement of compensation under section 25(F) is carried out, future VRS schemes will have to offer compensations higher than the statutory rate to obviate the departed workmen's right to claim re-employment under section 25(H).

v. According to section 2(s), all employees in an industry would be entitled to the protective umbrella and benefits under the Industrial Disputes Act and it excludes only the following two categories of employees:

   a. All managerial category employees

   b. All supervisory category personnel if they are drawing wages above Rs. 1,600/month

It must be noted that engineers/technicians/ scientists who are branded as supervisors/officers without any subordinate to be supervised would continue to fall within the definition of "workman" under the I.D. Act and can raise disputes under the I.D. Act.

Aspects of the Contract Labour [R&A] Act, 1970 having implications on outsourcing

a. As per section 2(i) of the Contract Labour Act, all contract employees in an establishment will come under the purview of the act and it excludes only the following three categories:

   1. Employees of contractors in managerial or administrative capacity.

   2. Employees in supervisory [with some subordinates to supervise] capacity drawing Rs. 5,000/month or more.

   3. Out workers of contractors if such workers are not working in premises owned or under the control of the principal employer [if they are on principal employer's premises or his hired premises, they will not stand excluded].

b. As per section 7, any employer proposing to employ total of more than 20 contract workmen [all Contractors' workmen put together] will need to obtain a prior registration from the labour department and limit the number of contract workmen to the maximum number for which he has paid the registration fee as per rule 26.

c. As per section 12, if a principal employer wishes to give any job to a contractor where the contractor will have to deploy more than 20 workmen on the job and the job is to be carried out on the premises of the principal employer or in premises controlled by the principal employer, he can do so only after ensuring that such a contractor has applied and obtained a license certificate after paying the fees prescribed under the rules 26 to 32 and renews such license every year.

d. As per rule 25(2)(iv), the principal employer shall ensure that the contract workmen are being paid wages not less than the statutory minimum wages [if there is any such notification and witness and certify that the contractor is making full payment].

e. As per rule 25(2)(v), if workmen are doing jobs of same or similar nature as done by regular workmen in the establishment, such contract workmen are eligible to claim wages payable to such regular workmen.

f. As per section 16 to 21 and rule 40 to 62, the principal employer shall ensure that the contractor extends to his workmen the various welfare benefits prescribed and if the contractor fails to do so, the principal employer is duty bound to extend the same and he can in turn recover the cost from the contractor.

g. As per section 10(1), the government can after examining the circumstances prescribed under section 10(2) prohibit the employment of contract labour and on such prohibition no contract labour should be employed on the jobs prohibited from the date of such prohibition.

Note:

1. Even though the government is encouraging outsourcing, no changes have been made in the statutory impediments to large-scale outsourcing.

2. Government will have to stop looking at the problem from the angle of "perennial or non-perennial jobs" and look at it from the point of "core and peripheral jobs" while taking decisions on prohibitions, to give greater flexibility in manpower deployment and outsourcing.

Aspects of the ESI Act, 1948 having Implications on Outsourcing or Contracting out jobs

a. As per section 2(9)(Invariant-I) of the ESI Act, the principal employer is bound to ensure the coverage of contract workers under the ESI scheme if any one of the following conditions is attracted.

- If contract workers are deployed on jobs inside the premises of the principal employer.
- Employed outside his premises, but the work of the contract workers is supervised by the principal employer's officers or agents.

b. As per sections 40 and 41, the principal employer shall ensure that the ESI contribution of all contract workers are collected and remitted on a monthly basis and submit all relevant returns pertaining to such labour to the ESI authorities.

Aspects of the EPF Act, 1952 having Implications on Outsourcing or Contracting out Jobs

a. As per section 2(1) of the Act and paragraph 30 of the EPF scheme, the principal employer is obliged to ensure coverage of all contract workers deployed by him: (i) inside his premises and (ii) outside his premises is such contract job has connection with the work of the establishment.

b. Principal employer should, therefore, ensure that the contractors furnish to him the required wage particulars on a monthly basis, so as to enable him to make the correct remittances on a monthly basis and submit the necessary returns within the prescribed time limits.

c. Alternatively, he can ask the contractors employing more than 20 workmen to obtain a separate EPF code and ask them to make direct remittance to EPF authorities and submit copies of the contractor's remittance particulars to the principal employer for production before the inspection authorities when they demand proof of contractor's independent compliance.

Aspects of the Workmen Compensation Act, 1923 having Implications on Outsourcing

a. As per sections 2(a) and 12 of the Workmen's Compensation Act, the principal employer is obliged to pay compensation for injury as well as occupational diseases suffered by contract workmen in the following contingencies:

- The workmen are not covered under the ESI scheme
- The workmen were employed on one of the jobs listed under section 2(n) read with schedule Invariant-I of the Act.

b. As per section 12(2), if the principal employer had to pay any compensation to any contract workman he can sue the contractor.

Aspects of the Minimum Wages Act, 1948 having Implications on Outsourcing

a. As per section 2(e) and 12 of the Act, the principal employer has an obligation to ensure that the contractor pays his workmen wages not below the notified minimum wage.

b. As per section 3, the government can notify various kinds of employments under schedule I and prescribe the rate of minimum wages for such activities.

c. Hence, principal employer should take note of the different rates prescribed for the different scheduled jobs [schedule I] and ensure that the contractors make payments according to the prescribed rates with applicable D.A.

d. The Supreme Court has passed a dictum that any employer who cannot pay the notified minimum wages has no right to carry on the business and should shut down his operations.

Aspects of the Inter-state Migrant Workmen Act, 1979 on Out-Sourcing

a. Section 2(1) of the act defines the term "Inter-state Migrant Workmen" to mean 'any person who is recruited by or through a contractor in one state under an agreement or other arrangement for employment in an establishment in another state, whether with or without the knowledge of the principal employer in relation to such establishment'.

b. As per section 4, any principal employer engaging five or more 'inter-state migrant' workmen in his establishment needs to get a registration certificate from the labour authorities and contractors engaged by him will need to obtain a license under section 8.

c. As per section 18, principal employer shall ensure that the contractor meets his obligations under sections 12 to 17.

Coverage of Contract Workers under Factories Act, Plantation Act, and Motor Transport Workers Act

a. Definition of the term "worker" under Factories Act, 1948 [section 2(1)], under Plantations Act, 1951 [section 2(k)] and under Motor Transport Workers Act, 1961 [section 2(h)] contemplates inclusion of contract workers also.

b. Accordingly, the principal employer contracting out jobs to be performed inside his establishment is required to ensure that the welfare/safety/working hours provisions under these Acts are extended to the contract workers also.

While it is increasingly being admitted that our labour laws are too rigid and need to be liberalized to make our industries globally competitive, no concrete measures have so far been initiated to scrap or modify the outdated labour enactments. Until such bold measures are forthcoming from the executive and legislative arms of the government, the judiciary will be compelled to view the actions of the employers based on the existing legal provisions. It is therefore imperative that all HR professionals continue to keep in mind the legal provisions while making strategic decisions on right sizing or outsourcing their manpower requirements.