

Client Alert

Strategic Options for Optimising Labour Costs

As the Indian economy begins the challenging and arduous journey to recover from the economic shock of the COVID-19 pandemic, many companies have witnessed a sharp contraction in demand, sales and revenues. The lockdown, which was nationwide till mid-May, and is now being selectively imposed in some parts of the country as cases spike, has hampered economic activity. The present consensus of GDP growth this fiscal year is a contraction of around 4.5%. The prevailing economic environment and the uncertain business climate in the months ahead have led many companies to evaluate their options for reducing costs. One such option is for companies to optimise their labour costs and rationalise their workforce.

Labour laws in India are strict, complex, and labour friendly. This Client Alert presents some of the options that employers can evaluate when they consider optimising their labour costs.

Indian laws classify an employee as a 'workman' (blue-collar) or a 'non-workman' (white-collar). Indian labour laws make a distinction between employees based on this classification. The service conditions of a workman are subject to far greater statutory protection than that of a non-workman. The terms of employment of non-workmen are governed mainly by their employment contracts and the policies of the company.

The below-mentioned labour cost-reduction approaches can be considered by companies operating in India. However, each of them has to be detailed and implemented depending on the circumstances and in accordance with the procedures prescribed under the law.

1) Salary reduction

Salary reductions may be done by an employer through a direct reduction in the employee's salary, or by reducing or removing variable components, benefits, perquisites that constitute the employee's cost to the company.

A change in the contractually agreed salary of an employee in India requires compliance to be made under the applicable laws (for a workman) and the consent of the employee (for a non-workman). For a workman, a salary cut would amount to a change in his service

conditions, and before implementing the same, the due process of the law is required to be followed. For a non-workman, the employer and employee may enter into a mutual agreement to this effect.

If a company wants to reduce benefits that do not form a part of the employment contract, but are provided for under the company policies/handbook, it will have to amend its policies after conducting discussions with employees and/or union(s) (if any), obtaining their feedback, and properly communicating the changes to all affected employees.

Taking into account the sharp downturn in business because of the COVID-19 pandemic, in certain industries (like aviation, tourism, hospitality etc.), employers and employees have agreed on a standardised pay cut across the board. Having stated that, salary cuts in India in wake of COVID-19 and/or during the lockdown have been subject to several central and state government notifications, which have been challenged under various petitions filed before High Courts and the Supreme Court of India.

The Supreme Court of India, in the matter of *Ficus Pax Private Limited vs. Union of India & Ors.* (W.P. (C) Diary No. 10983/2020), passed an interim order directing that commercial and industrial establishments that are willing, may negotiate the terms and enter into settlements with their employees regarding salary payments for the lockdown period (during which said establishments were closed) as applicable in the respective jurisdictions. Prior to the said interim order, the Supreme Court had directed the appropriate governments not to take any coercive action against private companies that were unable to pay full salary to their employees during the lockdown.

Further, companies may consider the option of 'no work no pay' and enter into specific settlement agreements to this effect with employees.

Therefore, with respect to salary cuts, specific legal advice should be taken on a case-to-case basis.

2) Deferment of salary

Deferment of payment of salaries to employees can be an effective measure to reduce the immediate liability of employers. In wake of COVID-19, many companies across many sectors have decided to defer a certain percentage of their employees' compensation package, which includes deferring promotions and bonuses as well for a short duration.

Such measures provide a temporary means for employers to manage their cash flow. However, in order to effect such a change/deferment, there should be transparency and clear communication and from the management to the employees.

It is also important to note that salary deferments are subject to Indian social security and tax laws.

3) Leave with or without pay

Some employers consider the option of granting leave without pay as a cost-reduction measure.

In the Indian context, just as leave cannot be claimed as a right by an employee, an employer also has no power to send an employee on forced leave without pay.

Under Indian laws, employers cannot force paid or unpaid leaves on their employees, unless the employees agree to such an arrangement voluntarily. For employees qualifying as workmen, under the applicable laws, the enforcement of paid leaves on the employees may amount to change in their service conditions, requiring compliance with the required procedures prescribed under said laws.

After the outbreak of the COVID-19 pandemic, the central as well as various state governments have issued notifications stating that where the lockdown has been implemented and commercial and industrial establishments are closed pursuant to the lockdown, the absence of employees from work should not be adjusted towards paid or un-paid leaves.

4) Adjustment of working hours and reducing overtime hours

A company can consider increasing the working hours of its employees, capping them to the legally allowed working hours i.e. 48 hours per week. For companies that have their standard working hours as 40 hours per week (i.e. 8 hours per day for 5 days per week), necessary amendments can be made in their working hours' policy. Increase in working hours of employees can help companies save on the overtime payments.

The above is relevant for manufacturing entities. As a part of the efforts of the Indian government to overcome the economic crisis and its 'ease doing business' initiatives, several state governments viz. Madhya Pradesh, Rajasthan, Gujarat, Punjab, Himachal Pradesh etc. have passed state amendments to the Factories Act, 1948 (during the lockdown period) to increase the maximum number of working hours per day from 8 to

12, and the maximum working hours per week from 48 to 72. This is a short-term relaxation.

5) Hiring of temporary employees or independent consultants

A company can cut its costs by hiring temporary employees or independent consultants instead of hiring employees on a full-time basis. Working with temporary employees or independent consultants can benefit a company in saving on additional employment costs that it has to incur in the case of permanent employees. However, the engagement of temporary employees and/or independent consultants is subject to several considerations such as nature of job, duration of engagement, nature of control exercised by the company, etc.

As many migrants and other workers (mainly in the workman category) have returned to their home states, some industrial and other establishments are a shortage of manpower while resuming their operations. In such a situation, it would be a prudent strategy to hire employees on a temporary basis depending upon the need and economic exigencies of the company.

6) Lay-off

Lay-off refers to the inability of an employer to provide employment to its workmen on account of a shortage of power, raw materials, accumulation of stocks, break-down of machinery, natural calamity, or any connected reason beyond the control of the management. Besides the temporary discharge from employment, a lay-off does not put an end to the employer-workman relationship during the period of lay-off. Lay-offs are carried out with the expectation that within a reasonable period of time, the establishment would resume its ordinary course of business/ operations, and the employees who have been laid-off will be reinstated to their full rights as normal employees.

A workman who is laid-off is entitled to compensation equivalent to fifty percent (50%) of the total basic wages and dearness allowance for the period of lay-off. Further, with respect to workmen, law prescribes processes and payments for lay-off with respect to certain categories of establishments such as factories, mines and plantations.

It is recommended for commercial establishments that a right to lay-off employees should be specifically agreed to in the employment contracts and/or policies of the company, providing powers to the management to lay-off employees, reasons or grounds for lay-off, compensation to be paid in case such lay-off is undertaken, etc.

7) Retrenchment

Retrenchment is akin to downsizing. In India, the Industrial Disputes Act, 1947 (the 'ID Act') is the governing legislation for retrenchment. It takes a wider view of termination of employees as against the ordinary meaning of the term retrenchment.

For employees qualifying as workmen, the due process required under the applicable laws as well as requirements under their employment contracts have to be followed for their retrenchment.

While effecting retrenchment of workmen, as per the ID Act, the employer is required to pay retrenchment compensation at the rate of fifteen (15) days' wages for every completed year of employment to be calculated at the last drawn salary of the respective workmen.

In conclusion, employers in India have several options to reduce their labour costs in order to manage their cash flows as they cope with the business challenges created by the COVID-19 pandemic. Options should be carefully evaluated and experienced legal advice should be taken. Due process of law should be followed, and the consent of employees should be obtained, wherever possible, in order to effectively implement the chosen cost reduction strategy while mitigating the risk of subsequent legal challenges.

About Chadha & Co.

Chadha & Co. is a leading corporate and commercial law firm based in New Delhi, India. The Firm has a specialised inbound practice in advising domestic and foreign corporations doing business in India on all Indian laws and regulations that are relevant to their business.

Contact

Savita Sarna | Manila Sarkaria | Natasha Sahni | Lesley Rajan

Chadha & Co.
Advocates & Legal Consultants
S – 327, Greater Kailash II
New Delhi – 110 048
India

Tel: +91 11 4163 9294, +91 11 4383 0000
Fax: +91 11 4163 9295
Email: ssarna@chadha-co.com
Web: www.chadha-co.com

This update is not a legal service and does not provide legal representation or advice to any recipient. This update is published by Chadha & Co. for the purposes of providing general information and should not be construed as legal advice or an attempt to solicit business in any manner whatsoever. Should further information or analysis be required of any subject matter contained in this publication, please contact Chadha & Co.