

THE RIGID EMPLOYMENT PROTECTION LEGISLATIONS IN INDIA AND ITS IMPACT ON THE ECONOMY- IS FLEXICURITY A VIABLE SOLUTION?

Pallavi Arora*

ABSTRACT

The Indian labour market has been rendered inflexible by a voluminous body of Employment Protection Measures. In the guise of protecting the interests of the workers, the highly rigid labour laws actually work to the detriment of the employers and the overall economy. This paper, whose central premise, proposes the implementation of the policy of flexicurity, does so as a solution to the existent inflexible condition of the Indian labour market. To further this premise, the article comprehensively analyzes the adverse impact of the highly regulated labour market on the Indian business environment. Thereafter, the author examines the working of the flexicurity model and its successful implementation in Denmark. Finally, the article discusses whether or not the flexicurity model can be replicated in India's socio-political milieu.

INTRODUCTION

Post-independence, Pandit Nehru sought to make India the poster child for socialism among third world countries and hence actively pursued economic independence by scripting India's retreat from international trade.¹ But this golden hearted socialism soon succumbed to the license raj, red-tapism and nepotism. India receded into a cocoon of superficial self-sufficiency and became a land of a million controls.² Thereafter, the inevitable economic reforms of 1991 acted as a panacea to India's caged economy. Gradually, the State's over-regulative character diminished and India steadily marched along the lines of a market economy.³

The rigid labour laws of India, which allow for significant intervention and regulation by the State, were also modeled along the principles of socialism.⁴ But even though India promptly adopted the Liberalization-Privatization-Globalization policy in 1991, no efforts were made to alleviate the Indian labour market of its highly rigid Employment Protection Legislations.⁵

* V Year, B.A. LL.B. (Hons.), Dr.Ram Manohar Lohiya National Law University, Lucknow.

1 See J. Ahrens, *Prospects of Institutional and Policy Reforms in India: Toward the Model of a Developmental State*, Asian Development Review (1997).

2 *Id*

3 See K. Inoue, *Industrial Development Policy of India*, Occasional Paper Series No. 27: Institute of Developing Economies (1992).

4 See A.N. Sharma, *Flexibility, Employment and Labour Market Reforms in India*, Economic and Political Weekly (2006).

5 See T. Das, *The Impact of Research on Policymaking: The Case of Labour Market and External Sector Reforms in India*, Economic Research Network (2006).

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This article attempts to establish the adverse impact of the stringent labour laws on India's business environment and proposes the implementation of the flexicurity model as a viable alternative. Part I of the article examines the inflexible nature of the Employment Protection Legislations in India. Part II discusses the adverse impact of the rigid labour laws on the Indian business environment. Part III illustrates the ills associated with a policy rendered ineffective by labour market flexibility. As a solution, it analyses the concept of flexicurity by comprehensively evaluating its merits and demerits. Further, this Part shall also examine the practicality and the means of replicating the flexicurity model in India. The conclusion reemphasizes the need for implementing flexicurity in India, despite the financial costs associated with it.

I. THE EMPLOYMENT PROTECTION LEGISLATIONS IN INDIA

The term 'Employment Protection Measures' refers to measures that are adopted by a State to safeguard the interests of its labour class.⁶ These regulate the conditions for hiring and firing of employees; and may be grounded in legislation, collectively bargained conditions of employment, court rulings or even customary practice.⁷

According to a recent study by the World Bank, the Employment Protection Measures in India are among the most restrictive in the world.⁸ On the pretext of safeguarding the interests of workers, the rigid labour laws have in fact restricted labour mobility and fostered undue State intervention. Consequently, they work to the detriment of the industrial establishments and employers in general.⁹

Thus, the following sections seek to elucidate the over-regulative character of the Indian labour laws and the resultant predicament of employers, by examining the provisions of the Industrial Disputes Act (1947), the Contract Labour (Regulation and Abolition) Act (1970) and the Trade Union Act (1926). As a solution to the existent rigidity of the Indian labour market, the author shall examine the proposition of creating a flexible system that gives multiple options to the employers to enter into different types of contracts, subject to the market volatility.

A. THE INDUSTRIAL DISPUTES ACT, 1947

In pursuance of the Industrial Disputes Act, 1947¹⁰, an employer is expected to comply with a plethora of cumbersome formalities. This section previews a few such formalities resulting from the provisions of the IDA with respect to retrenchment, lay-off and closure of an industrial establishment. Further, the author shall also examine the

6 See *Employment Protection and Labour Market Performances*, OECD Employment Outlook (2000).

7 *Id.*

8 See *India Country Overview*, World Bank (2008).

9 See K. Basu, G.S. Fields & S. Debgupta, *Retrenchment, Labour Laws and Government Policy*, available at <http://siteresources.worldbank.org/INTDECSHRMSMA/Resources/india.pdf>.

10 Hereinafter IDA.

stance of the Indian judiciary on whether the conditions precedent to retrenchment, lay-off and closure are opposed to the Constitutional mandate.

a. Conditions precedent to retrenchment and lay-off

In order to initiate retrenchment or lay-off proceedings, an employer has to serve a notice on the employees as well as the appropriate government, indicating bona fide reasons to this effect.¹¹ Furthermore, applications for retrenchment or lay-off relating to non-seasonal industrial establishments (employing more than 100 workers) must also be approved by the appropriate authority.¹²

Studies by Nagraj point out that in order to retrench even a single workman, the employer is expected to seek the permission of the labour commissioner.¹³ According to Datta Chaudhari this acts as a formidable handicap, because in most cases the government does not grant the permission to retrench. Consequently, inflexibility in the free movement of labour as per demand and supply sets in.¹⁴

In view of this, employers have time and again questioned the constitutional validity of such provisions. The constant denial of permission by the government to retrench workers is perceived as a violation of an employer's fundamental right to carry on trade or business enshrined under Article 19 (1)(g). However even the Indian judiciary in a bid to appear pro-employee, has adopted a stance not conducive to the flexible redistribution of labour. In *Workmen Compensation for Meenakshi Mills Ltd. v. Meenakshi Mills Ltd.*,¹⁵ the Supreme Court held that the inflexible retrenchment provisions only place 'reasonable restrictions' on the employer's right to retrench workers and are therefore constitutionally valid. Thus, the Apex Court's decision serves to safeguard the welfare of the labour class even though it may potentially negatively impact the business interests of the employers.

Hence, undue state intervention in matters of retrenchment and lay-off, restrict the ability of firms to hire and fire employees according to their labour demand.

b. Conditions precedent to closure of an industrial establishment

When first introduced in 1947, the Industrial Disputes Act did not restrain employers from closing down unprofitable businesses.¹⁶ But the amendments of the Act in 1972 and 1976 sought to provide significantly greater protection to workers than the employers.¹⁷

11 For lay-off see 25C and § 25M IDA; for retrenchment see § 25N and § 25F IDA.

12 See §25 N(1)(b) IDA.

13 See R. Nagraj, *Labour Market in India-Current Concerns and Policy Responses*, Organization for Economic Co-Operation and Development (2007).

14 See M.D. Chaudhuri, *Labour Markets as Social Institutions in India*, Delhi School of Economics, CDE Working Paper No. 16 (1994).

15 1994 AIR 2696.

16 See K. Basu, G.S. Fields & S. Debgupta, *supra* note 9.

17 See A.N. Sharma, *supra* note 4.

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Therefore, in *Excel Wear etc. v. Union of India*¹⁸ the Supreme Court held that the rigid provisions in the IDA as regards closure (i.e. Section 25-O) violated Article 19(1) (g) of the Constitution, and was consequently severed from the Act.¹⁹

In order to fill the lacuna created by the Apex Court in the *Excel Wear* case, Section 25-O was amended by the Industrial Disputes (Amendment) Act, 1982. In the current amended version closure of an unprofitable venture is permitted, however employers employing 100 or more workers must give notice of a closure to workers or their representatives and to the government, 90 days prior to the date of intended closure. A prior approval of the government is also mandatory to perpetuate a valid closure.²⁰

Bhattacharjea in his thesis observes that the government invariably disallows the employers from closing down even financially unproductive industrial units, in an attempt to protect the workers.²¹ He further argues that despite the amended provisions, Section 25-O still makes compliance arduous for the employers leading to greater impediments in their business decisions.²²

This is reflected by the fact that even after the Amendment Act of 1982, the question of the constitutional validity of Section 25-O stood unresolved. The Calcutta and Karnataka High Court were of the opinion that the amended Section 25-O still violated Article 19(1)(g);²³ while the Delhi and Kerala High Court upheld its constitutional validity.²⁴ Finally, the controversy was put to rest once and for all by the Supreme Court in *M/s Orissa Textile and Steel Co. Ltd. v. State of Orissa and Ors.*²⁵ Much to the employers' dismay, the Supreme Court once again adopted a pro-worker stance and upheld the validity of the amended Section 25-O, along with its rigid compliance mechanisms. Thus in India, the government follows an ill-conceived policy of denying the closure of industrial establishments, regardless of their productivity. This consequently works to the disadvantage of the employers and negates the free operation of market forces.

18 (1978) 4 SCC 224.

19 The Supreme Court struck down the pre-amendment § 25-O on the following grounds: *First*, according to sub-section (2) of the pre-amendment § 25-O, the appropriate Government was not obligated to provide any justification as regards an order that denied the closure of an establishment (*See* ¶ 25 and 26). *Second*, there was no provision for appeal, review or revision of the order even after sometime (*See* ¶ 27). *Third*, on account of the first two factors, the pre-amendment § 25-O compelled the employers to pay minimum wages and to manage the undertaking, even when they did not find it financially practicable to do so. (*See* ¶ 26, 27 and 30).

20 *See* Section 25-O, Industrial Disputes (Amendment) Act. 1982.

21 *See* A. Bhattacharjea, *Labour Market Regulation and Industrial Performance in India: A Critical Review of the Empirical Evidence*, 39(2) Indian Journal of Labour Economics (2006).

22 *Id*

23 *Maulis of India v. State of West Bengal*, (1989) 2 LLJ 400; *Union of India v. Stumpp Schedule Somappa Ltd.*, (1989) 2 LLJ 4.

24 *DCM Ltd. v. Lieutenant Governor*, AIR 1989 Del 193; *Laxmi Starch v. Kundra Factory Workers Union*, (1992) Lab IC 1337 (Ker).

25 2002 LLR 225.

It is further submitted that Section 9 A of the Act has also been a cause of concern for the employers. It lays down necessary pre-conditions for a change in employee service rules, whereby employees should be given at least 21 days notice before modifying their wages, hours of work and rest intervals. In the opinion of Anant this constrains industrial restructuring, technological upgrading and causes problems when employees have to be redeployed quickly in order to meet certain time bound targets.²⁶

The foregoing discussion regarding the rigid provisions of the IDA highlights how the labour policies in India demonstrate a unilateral tilt towards employees. As against this, the principle assertion of the author is that instead of a partisan approach, India would do better to adopt a balanced policy framework that is mutually favorable to both the employees as well as the employer.

B. THE CONTRACT LABOUR (REGULATION AND ABOLITION) ACT, 1970

Contract labour refers to ‘workers engaged through an intermediary and is based on a triangular relationship between the user enterprises, the contractor (including the sub contractor) and the workers’.²⁷ The law governing contract labour in India is the Contract Labour (Regulation and Abolition) Act, 1970, and its related Rules of 1971.

The judiciary has acknowledged the significance of the Contract Labour Act by describing it as “a piece of social legislation for the welfare of labourers whose conditions of service are not at all satisfactory and the Act should therefore be literally construed”.²⁸ The Act has considerably contributed in securing the interests of contract labourers who are generally engaged in hazardous occupations²⁹ and often denied minimum wages as well as employment security.³⁰

However contract labour as a concept is significantly beneficial from the perspective of the employers, as it allows firms to induce flexibility in their labour structure by outsourcing certain works to a contractor or a staffing agency.³¹ But due to, the recurrent judgments of the Supreme Court in 1960 and again in 1972, a number of restrictions have been placed on the use of contract labour by the employers in India. For instance, a firm cannot engage contract labour if the work is perennial, part of the core operations, involves a large number of workers or is normally done by regular workers.³² Such

26 See T.C. Anant et al, *Labour Markets in India: Issues and Perspectives*, in *LABOUR MARKETS IN ASIA: ISSUES AND PERSPECTIVES*, (J. Felipe & R. Hasan eds., 2006).

27 See *Contract Labour in India*, Ministry of Labour, available at <http://labour.nic.in/annrep/files2k1/lab10.pdf>.

28 *Lionel Edward Ltd v. Labour Enforcemnt Officer*, 1977 Lab IC 1037 (Cal).

29 See *Contract Labour in India*, Ministry of Labour, available at <http://labour.nic.in/dglw/Session41ofILC.doc>.

30 See H.L. Kumar, *Labour and Industrial Law* 509 (2d. ed. 2004).

31 See M. Rajeev, *Contract Labour Act in India: A Pragmatic View*, IGIDR Proceedings/ Project Report Series, PP 062 (2009).

32 *Standard Vacuum Refinery Company v. Their Workmen*, (1960) 3 SCR 466 ¶ 11; *Vegoils Pvt. Ltd. v. Its Workmen*, (1971) 2 SCC 724 ¶ 26.

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limitations reduce the use of contract labour by firms, thereby augmenting the inflexibility of the labour market.

Furthermore, there also remains the issue of whether those workers who have served thus far on contract basis, must be regularized (or instead be retrenched), when the court determines that the jobs they have been doing constitute regular employment. In *Air India Statutory Corporation Ltd. & Ors v. United Labour Union & others*³³ it was held that it is mandatory for a firm to regularize the contract labour engaged in regular employment. Such a stipulation acted as a deterrent to the use of contract labour, adding to the rigidity of the labour market. Therefore, the Supreme Court overturned this position in the *Steel Authority of India Ltd. v. Union of Waterfront Workers & others*³⁴ by holding that a principal employer is not under any obligation as such, to absorb the contract labour working in the concerned premises.

It is worth mentioning that the judgment in the SAIL case definitely takes into consideration the broader interests of the employers. But nevertheless, it remains to be seen whether the appropriate authority will follow this judgment in letter and spirit or whether it will succumb to the vaulting pressure from the trade unions that calls for the absorption of contract labour.

C. THE TRADE UNION ACT, 1926

A trade union is defined as ‘an organized association of workmen formed for the protection and promotion of their common interests, especially with regard to wages, hours and working conditions’.³⁵ In India, trade unions are registered under the Trade Union Act, 1926,³⁶ which traces its origin to the labour unrests dating back to 1877.³⁷ Accordingly, trade unions in India can avail themselves of different privileges and are obligated to various liabilities under the Trade Union Act.³⁸

Economists like Wilkinson and Campbell acknowledge the contribution of trade unions in encouraging firms to adopt a ‘high road to growth’.³⁹ According to Blanchflower and Oswald, trade unions also avert the ‘race to the bottom’ syndrome, by ensuring a minimum floor of labour standards.⁴⁰

But over intervention by trade unions in India has earned them the title of ‘market distorting agents’.⁴¹ First, trade unions curtail the free operation of market forces leading to

33 (1997) 9 SCC 377.

34 [2001] 7 SCC 1 ¶ 89 and 125(3).

35 See THE NEW INTERNATIONAL WEBSTER’S DICTIONARY OF THE ENGLISH LANGUAGE 1330 (Encyclopedia ed. 2003).

36 For ‘Registration of Trade Unions’ see Chapter II, § 3 to § 14 Trade Union Act, 1926.

37 See K.D. SRIVASTAVA, LAW RELATING TO TRADE UNIONS IN INDIA (2d ed. 1982).

38 For ‘Rights and Liabilities of Registered Trade Unions’ see Chapter II, § 3 to § 14 Trade Union Act, 1926.

39 See A.N. Sharma, *supra* note 4.

40 *Id*

41 See P.L. MALIK, INDUSTRIAL LAW 2878 (21st ed. 2008).

an increase in transaction costs which in turn, results in an alteration of the 'market price'.⁴² This curtails market investments and creates a breeding ground for unemployment.⁴³

Second, trade unions in consonance with the law allow for outsiders to be office bearers and members of unions.⁴⁴ So workers who are not directly employed under a particular employer also may stand against that employer in the event of any dispute. According to Nath a provision to this effect does not exist in the laws of other countries.⁴⁵

Third, Nath points out that while countries like UK and Japan follow a democratic way of electing the office bearers of their trade unions through a process of secret ballot, laws in India follow a different strategy.⁴⁶ Election through secret ballot is not essential⁴⁷ and unions also do not hold any strike ballot before any strike.⁴⁸

It is further argued that recurrent strikes in India are not just on account of the facilitative nature of the law. In fact, the IDA attempts to restrain strikes by mandating that employees can resort to strike only after giving a 6 week prior notice to the employers or else it would be deemed 'illegal'.⁴⁹ Further, the 'right to strike'⁵⁰ has not been recognized as a fundamental right in India, but remains a statutory right, subject to reasonable restrictions.⁵¹ Thus, even the courts have restricted the right to strike and relegated it to the status of only a legal right. Nevertheless, India's business environment has been plagued by recurring 'illegal strikes', which have culminated in grave losses to various business establishments.⁵² According to Nath the annual loss of persons per day due to strikes in India is said to be the second highest in the world.⁵³

For instance in 2011, close to 700 pilots of Air India refused to fly. Consequently, 90% of their domestic flights were grounded, resulting in a loss of almost Rs. 100 crore every week to the national carrier.⁵⁴ Jet Airways also faced significant labour unrest in

42 See A.N. Sharma, *supra* note 4.

43 *Id.*44 § 22(2) of the Trade Union Act, 1926 stipulates that 'all office-bearers of a registered Trade Union, except not more than one-third of the total number of the office-bearers or five, whichever is less, shall be persons actually engaged or employed in the establishment or industry with which the Trade Union is connected'. Thus, outsiders can be office bearers up to one third of total office bearers or five whichever is less. See also P.R.N. Sinha, et.al, INDUSTRIAL RELATIONS, TRADE UNIONS AND LABOUR LEGISLATION (2009).

45 See S. Nath, *Labour Policy and Economic Reforms in India*, in B. DEBROY & P.D.S KAUSHIK, REFORMING THE LABOUR MARKET (2006).

46 *Id.*

47 See S. Nath, *Labour Policy and Economic Reforms in India*, in B. DEBROY & P.D.S KAUSHIK, REFORMING THE LABOUR MARKET (2006).

48 See S. Nath, *supra* note 45.

49 Syndicate Bank v. K. Umesh Nayak, 1994 SCC (5) 572.

50 See § 2(q)(n2) IDA.

51 All India Bank Employees Association v. IT, 1962 SCR (3) 269.

52 See M. Sill & R.C. Datta, *Contemporary Issues in Labour Law Reform in India: An Overview*, Tata Institute of Social Sciences, Mumbai, Discussion Paper No. 5/2007 (2007).

53 *Id.*

54 *Delhi High Court Issues Contempt Notice to Air India Pilots*, NDTV, May 3, 2011, available at <http://www.ndtv.com/article/india/air-india-strike-hits-100-crore-mark-still-no-breakthrough-103050>.

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2008, when they laid-off nearly 1000 employees as a cost cutting measure in response to the rising fuel prices around the globe. Thereafter, not only did the Jet employees go on strike but also amassed enough political clout to be reinstated the very next day.⁵⁵ Therefore, it is fair to conclude that the collective bargaining machinery in India certainly restricts productivity and heightens the inflexibility of the labour market.

II. THE ADVERSE IMPACT OF THE RIGID EMPLOYMENT PROTECTION LEGISLATIONS ON THE INDIAN BUSINESS ENVIRONMENT

The following sections seek to establish how the inflexible labour laws in India, not only hurt the interests of the employers, but also work to the detriment of employees as well as the overall economy.

A. EFFECTS ON THE BUSINESS ESTABLISHMENTS

Studies by Papola and Datta Chaudhari have revealed that on account of the rigid Employment Protection Legislations in India, companies find it difficult to adjust the excessive supply of labour.⁵⁶ They argue that firms are forced to maintain a bloated workforce even on encountering adverse business conditions. This increases their labour costs and leaves very few resources for re-investment in new lines of activity.⁵⁷ Hence, in order to escape the rigors of rigid Employment Protection Measures, Indian companies are compelled to enforce a number of regressive policies. According to Mathur, employers have devised alternative ways to reduce the workforce despite the “restrictive” provisions in place.⁵⁸ Some policies to this effect are:

a. Excessive use of contract labour

If an employer knows well in advance that it is impossible to get the Government’s permission to lay-off or retrench a permanent employee, then he would avoid getting into such a rigid commitment. Alternatively, he would choose to substitute the permanent worker with machines, contract labour or casual workers.⁵⁹ The employer may also contract out work to small enterprises which are not covered by the stringent regulations.⁶⁰

Studies by Goswami have illustrated how the rigid labour laws have resulted in the increasing use of contract labour in the powerloom industry as well as in the already

55 *Government Examining if Sacking Flouted Law*, The Times of India, October 17, 2008, available at http://articles.timesofindia.indiatimes.com/2008-10-17/india/27934412_1_labour-laws-labour-ministry-labour-commissioner.

56 See K. Basu, G.S. Fields & S. Debgupta, *supra* note 9.

57 See T.S. Papola, *Structural Adjustment, Labour Market Flexibility and Employment*, 37(1) The Indian Journal of Labour Economics, NEW Delhi(1994).

58 See A. Mathur, *INDUSTRIAL RESTRUCTURING AND UNION POWER: MICRO-ECONOMIC DIMENSIONS OF ECONOMIC RESTRUCTURING AND INDUSTRIAL RELATIONS IN INDIA*, ILO, GENEVA (1991).

59 See M.D. Chaudhuri, *supra* note 14.

60 *Id*

capital intensive fertilizer and chemical industry.⁶¹ Empirical evidence also indicates that the percentage of contract workers to total workers in the manufacturing sector as a whole increased from about 12 per cent in 1990 to about 23 per cent in 2002.⁶² In states like Andhra Pradesh, the increase was phenomenal – it rose from 40 per cent in 1990 to about 62 per cent in 2002.⁶³ Thus, contract labour has been one of the principal methods used by the employers to gain flexibility in the labour market.

Empirical evidence has revealed that the extraordinary rise in the use of contract labour due to the rigid labour laws has been accompanied by their blatant abuse by industrial establishments. Roy has stated that in a significant number of cases where contract labour has been adopted, the workers have suffered as they have been deprived of their dues.⁶⁴ This is illustrated by the recent instances of agitation by contract workers in the Hyundai Motors case (May 2007) and the NTPC-Simhadri case (January 2007).⁶⁵ In the aforesaid cases, disconcerted contract workers had been demanding an increase in their pay scales but since the management failed to address their needs, they eventually resorted to a strike.

Thus, it can be concluded that a misuse of contract labour in India has a two-fold effect. First, by contracting out the work designed to be performed by a permanent employee, the possibility of labour specialization or firm specific knowledge in the work so contracted out, is surrendered by the firm.⁶⁶ Due to the lack of labour specialization vis-à-vis its permanent employees, a firm cannot achieve economies of scale, thereby hindering the firm's productivity.⁶⁷ Second, as pointed out by Papola and Sharma, a blinded policy of contract labour weakens the collective bargaining machinery of the labour market which in turn leads to an increase in employer militancy.⁶⁸

b. Use of lock outs

Employers have also tried to evade the effect of the rigid labour laws by resorting to lock-outs. Nath argues that though the incidence of lock-outs has decreased since 1985, compared to other countries, India has shown a greater loss of person days.⁶⁹ According to the Economic Survey (2005-2006) the number of lock-outs in the year 2005 stood at the high figure of 185.⁷⁰

61 See Goswami, *Sickness and Growth of India's Textile Industry: Analysis and Policy Options*, 25(31) Economic and Political Weekly(1990).

62 See A.N. Sharma, *supra* note 4.

63 *Id.*

64 See R. Dutta, *Employment Dynamics in Indian Industry: Adjustment Lags and the Impact of Job Security Regulations*, 73 Journal Of Development Economics (2004).

65 See M Sill & R.C. Datta, *supra* note 52.

66 See A.N. Sharma, *supra* note 4.

67 *Id.*

68 See T.S. Papola & A.N. Sharma, *Labour: Down and Out?*, Seminar (2005).

69 See S. Nath, *supra* note 45.

70 Ministry of Finance, *Economic Survey 2005-06*, Government of India, New Delhi (2006).

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A case in point is the Murphy Electronics Company (Mumbai). The said company fearing that the Government would not grant permission to close down one of its plants, decided to use lockouts and promoted inter-union rivalries to further this cause as a tactic to get rid of workers. During the period of lockout, the management made arrangements to carry on production of its products by small sub-contractors.⁷¹ The result was that out of the 2,500 workers only 497 remained and this strategy helped the management to get the plant declared a sick unit by the Board of Industrial and Financial Reconstruction (BIFR) in 1988.⁷²

c. Other strategies and their effects

In order to combat the legislative rigidities, companies often adopt a strategy of capital deepening which involves a pure substitution of capital for labour.⁷³ Other strategies entail the use of golden handshakes, voluntary retirement schemes, resorting to corruption and setting up production in states where the labour class is not yet organized.⁷⁴

The adoption of such informal routes to dismiss employees has proved detrimental to the interests of the workers. Studies by Papola and Sharma in 2005 indicate that the rigid labour laws have led to forced arrangements between local and plant level unions and employers, which have, in turn, adversely affected the welfare of the workers.⁷⁵ For example, the fear of losing jobs through informal means has impelled unions to accept relocation, downsizing, productivity linked wages, a freeze in allowances and benefits, voluntary suspension of trade union rights for a specific period etc.

A report of the Task Force of the Planning Commission in 2001 further indicates that due to the aforementioned reasons, foreign investors who are keen on investing in labour intensive countries like India are deterred from doing so.⁷⁶ The report explains that during 1991-94, the flow of foreign investments to India has gone up perceptibly, but the preferred avenue for this investment has been the financial sector, rather than manufacturing industries.⁷⁷ The fear of not being able to correct mistakes or to alter production plans in response to market signals, due to the imposed inflexibilities in labor-use is a serious deterrent to foreign investments in India.⁷⁸

71 See K. Basu, G.S. Fields & S. Debgupta, *supra* note 9.

72 *Id*

73 See A. Ghose, *Employment in Organised Manufacturing in India*, 37(2) Indian Journal of Labour Economics (1994).

74 See K. Basu, G.S. Fields & S. Debgupta, *supra* note 9.

75 See T.S. Papola and A.N. Sharma, *supra* note 68.

76 See Planning Commission, *Report of the Task Force for Employment Opportunities*, Government of India (2001). See also A. Agarawal, *The Influence of Labour Markets on FDI: Some Empirical Explorations in Export Oriented and DomesticMarket seeking FDI across Indian States* (2007), available at <http://www.hss.iitb.ac.in/ties07/paper/ts4/psE/2.pdf>.

77 *Id*

78 See M.D. Chaudhuri, *supra* note 14.

B. GROWTH RATE OF EMPLOYMENT IN THE ORGANIZED SECTOR

India is currently the fourth largest economy in the world,⁷⁹ having recorded a growth rate of 8.6% in GDP for the financial year 2010-2011.⁸⁰ But on account of the rigid labour laws, India's economic prowess has not been complimented by a proportional growth in employment. Employment as a whole, which had experienced a steady growth of around 2% from 1961 to 1990, declined sharply to 1.5% during 1990-92 and further to around 1% during 1993-2000.⁸¹

In addition, the slow growth rate of employment in the organized sector, which faced the full brunt of the rigid labour laws, is also worth considering. Between 1995-96 and 2000-01, about 1.1 million workers, or 15% of workers in the organized manufacturing sector across major states and industry groups, lost their jobs. In fact, employment in the organized sector grew at 1.2% p.a. during 1983-1994, but this rate dipped to 0.53% between 1994 and 2000.⁸²

Studies by the ILO-ARTEP (1993) have analyzed the reasons behind the slow growth rate of employment in the organized manufacturing sector in India.⁸³ Some reasons to this effect were the increase in real wages⁸⁴ as well as structural and technological changes. But primarily they attributed the deceleration in employment growth to the inflexible labour laws.⁸⁵ A study of the Indian labour market by Ahluwalia in 1992 explained that the legal provisions surrounding job security and institutional factors such as the pressure of trade unions made the adjustment of the workforce difficult for enterprises, and hence discouraged the organized sector enterprises from expanding employment.⁸⁶

Ahluwalia's reasoning was reaffirmed by Nagaraj. In his thesis in 2004, he observed that firms in the organized sector are compelled to consider their future labour needs while devising their current employment policies.⁸⁷ Therefore, a company would be reluctant to hire additional workers during an economic upturn if it anticipates significant

79 See *Report for Selected Countries and Subjects*, World Economic Outlook Database, International Monetary Fund (2011).

80 *Advance Estimate for 2010- 2011*, Central Statistics Organization, Ministry of Finance (2010).

81 See A.N. Sharma, *supra* note 4.

82 *Id.*

83 See ILO, *India: Employment, Poverty and Labour Policies*, ILO-ARTEP (1993).

84 See *supra* note 35. 'Real wages' is defined as '*wages evaluated in terms of the purchasing power (i.e. wages that have been adjusted for inflation) as contrasted with nominal wages, evaluated in money*'. According to Fallon and Lucas (1991) and Ahluwalia (1992) an increase in the real wages is inversely proportional to the growth rate of employment in the manufacturing sector. The faster growth rate of industrial wages relative to consumer prices, abetted by job security provisions resulted in a significant long term reduction in employment during the period 1959-60 to 1985- 86; See A.N. Sharma, *supra* note 4.

85 See ILO, *supra* note 83.

86 See J. AHLUWALIA, *PRODUCTIVITY AND GROWTH IN INDIAN MANUFACTURING* (1992).

87 See R.NAGARAJ, *EMPLOYMENT AND WAGES IN MANUFACTURING INDUSTRIES IN INDIA: TRENDS, HYPOTHESIS AND EVIDENCE*, INDIRA GANDHI INSTITUTE OF DEVELOPMENT RESEARCH, MUMBAI (1993).

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costs in reducing its work force during a subsequent downturn.⁸⁸ This in effect decelerates the growth of employment in the organized sector. Sharma endorses Nagraj's viewpoint and argues that excessive institutional intervention make wages 'sticky'⁸⁹ which impacts the freedom of the employers to adjust the quantities of resources allocated to wages leading to further reluctance in increasing employment. Hence, in order to protect the existing employees, the potential employees (and even retrenched workers) remain unemployed or enter the unorganized sector with no social security or political power.⁹⁰

AN Sharma further brought to light the plight of unemployed workmen who turn to the unorganized sector. He rightly argues that employers in the organized sector would flatly refuse to employ workers from the unorganized sector. This is because employers know well in advance that at a later stage the government will refuse any application to retrench or lay-off the said workmen from the unorganized sector. Thus, the employers adopt an over-cautious approach by employing lesser workmen than their actual labour demand. Consequently, there is a visible segmentation of the market between the insiders (workers with a protected job) and outsiders (workers employed in the unorganized sector or black economy).⁹¹ The Employment Protection Legislations clearly discourage the outsiders from entering the labour market and thereby, spur unemployment.⁹²

Another study by Sundaram and Tendulkar in 2002, particularly analyzed the employment trend in the factory manufacturing sector.⁹³ The organized factory segment registered a higher annual average growth rate (in terms of output) i.e. 7.9% in the 1980s as compared to 4.6% during the previous decade. However, they argue that on account of the rigid labour laws, the faster growth rate of the 1980s was associated with a virtual stagnation in factory sector employment and the decade was widely described as one of "jobless growth" in the factory-manufacturing segment.

Thus, Debroy rightly argues that India's comparative advantage of enormous labour abundance would be more adequately utilized if wages in the organized sector were controlled by market forces instead of being regulated by the inflexible labour legislations.⁹⁴ In fact, Falon and Lucas have maintained that in the absence of any stringent

88 *Id*

89 *See supra* note 35. ('Sticky wages' refers to the proposition that, "some wages adjust slowly in response to labour market surpluses or shortages. In particular, sticky wages are prime reason behind the positive slope of the short-run aggregate supply curve. 'Sticky wages' may also be called inflexible or rigid wages").

90 *See* A.N. Sharma, *supra* note 4.

91 *See* A.N. Sharma, *supra* note 4.

92 *See* A. Barone, *Employment Protection Legislation: A Critical Review of the Literature* (2001), available at <http://www.csifin.it>.

93 *See* K. Sundaram & S. Tendulkar, *The Working Poor in India: Employment- Poverty Linkages and Employment Policy Options*, ILO, Geneva, Discussion Paper 4 (2002).

94 *See* B. Debroy, *Why We Need Law Reform* (2001), available at <http://www.indiaseminar.com/2001/497/497%20bibek%0debroy.htm>.

job security regulations, the employment rate in the organized manufacturing sector would have been 17.5% higher.⁹⁵

A survey by Besley and Burgess in 2002, examined the negative impact of ‘pro-worker’ laws enacted by states like Gujarat, Maharashtra, Orissa and West Bengal.⁹⁶ The study conclusively established how such anti-establishment policies had resulted in plummeting returns from the registered-manufacturing sector. On the other hand, the states with ‘pro-employer’ legislations (i.e. Andhra Pradesh, Madhya Pradesh, Rajasthan, Tamil Nadu, Karnataka and Kerala) had reaped the benefits of industrial deregulation. Moreover, the said observation is not just peculiar to India, but is equally applicable on the global plane.⁹⁷ For example, the higher unemployment in Europe vis-à-vis North America is often attributed to its rigid labour institutions.⁹⁸

In a nutshell, each of the aforementioned studies and surveys provide empirical evidence to substantiate the negative consequences of the highly stringent labour laws in India.

III. SHOULD INDIA ADOPT LABOUR MARKET FLEXIBILITY?

The foregoing discussion has established that rigid Employment Protection Legislations are counter-productive to the interests of the employers, the employees and the economy at large. The next question is whether India should adopt ‘labour market flexibility’, thereby giving the employers an unbridled discretion as regards the hiring and firing their employees. The following sections preview the pros and cons of an excessively flexible labour market policy.

A. ADVANTAGES OF LABOUR MARKET FLEXIBILITY

The Employment Protection Index⁹⁹ indicates that countries like the United States of America and the United Kingdom have fuelled their labour markets with flexibility, as a part of the New Deal Package.¹⁰⁰ A study by Klapper indicates that the Chinese labour market is 3.33 times more flexible than that of India.¹⁰¹ The benefits arising out of such a policy are manifested by a lower unemployment rate in the United States

95 See P. Fallon & R. Lucas, *The Impact of Changes in Job Security Regulations in India and Zimbabwe*, 5(3) World Bank Economic Review (1991).

96 See T. Besley & R. Burgess, *Can Labour Regulation Hinder Economic Performance? Evidence from India*, Journal of Economic Literature (2002).

97 *Id.*; Djankov et. al (2002).

98 See Nickell (1997).

99 See *Employment Protection Regulation and Labour Market Performance*, OECD Employment Outlook, Chapter 4 (2004).

100 See *The Social Security (Flexible New Deal) Regulations 2009*, Secretary of State for Work and Pensions, SI 2009 No.480 (2009).

101 See Klapper, Leora, L. Laeven & R. Rajan, *Barriers to Entrepreneurship*, University of Chicago, Chicago, Working Paper (2005).

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America and the United Kingdom (i.e. 12.7% and 21.4% respectively), as compared to France (41.6%) and Germany (51.8%) in 2004 (which have still retained rigid labour market institutions).¹⁰²

B. DISADVANTAGES OF LABOUR MARKET FLEXIBILITY

Needless to say, that 'labour market flexibility' is beneficial in addressing the issue of unemployment. But if there are no legal safeguards vis-à-vis the implementation of a flexible 'hire and fire' policy, then it becomes amenable to abuse by the employers. Rossen cites the example of USA to explain that with a flexible 'hire and fire' policy, the employers may lay-off their employees on a short notice, without providing any immediate financial support or other unemployment benefits like an active assistance in searching for a new job. This in turn would hinder the job and income security of the workers.¹⁰³

For example, in 1995, the Chinese government drastically downsized many State Owned Enterprises.¹⁰⁴ Consequently, the number of persons that were laid-off increased from 3 million in 1993 to 17.24 million in 1998.¹⁰⁵ Between 1998 and 2002 another 25 million employees were laid off.¹⁰⁶ In spite of the mass lay-offs, the Chinese labour laws failed to provide any post-termination security to the employees. The resultant dissent from the Chinese trade unions was also suppressed by the Communist Party of China.¹⁰⁷ Thus, 'labour market flexibility' can serve as a double edged sword, in the absence of any supplementary social security measures.

C. AN ANALYSIS OF THE FLEXICURITY POLICY

Hence, it is asserted that a highly regulated labour market and a blinded policy of flexible 'hire and fire', represent two extreme ends of a continuum. If on one hand, the State must not arbitrarily deny the employers their right to retrench workers; then on the other hand, even the employers must not misuse the 'hire and fire' policy to the detriment of the working class. Hence, a workable strategy for India would be a hybrid of a Liberal Market Economy (and USA) and a highly Coordinated Market Economy (like India). To this effect, the following sections discuss the concept of flexicurity, which is modeled along the lines of a Negotiated Economy, and works on the central premise of harmonizing the interests of the employers and the employees.

102 *Id*

103 See H. Rosen, *Trade Adjustment Assistance: The More We Change the More it Stays the Same*, in C. FRED BERGSTEN AND THE WORLD ECONOMY 79-113 (M. Mussa ed., 2006).

104 J. Giles et. al, *What is China's True Unemployment Rate*, CHINA ECO. REV. (2004).

105 See J. Xue & W. Zhong, *Unemployment, Poverty and Income Disparity in Urban China*, 17 ASIAN ECO. J. (2003).

106 *Id*

107 *Id*

a. Origin of “flexicurity”

It is still disputed whether flexicurity originated in Denmark or the Netherlands. Some scholars like Van Oorschot are of the opinion that the concept was propounded by the Dutch sociologist Hans Adriaansens in the mid 1900’s in connection with the Dutch Flexibility and Security Act.¹⁰⁸ The others contend that flexicurity originated in Denmark, after the negotiations between Danish employers and trade unions paved the way for the September Compromise (1899) and the Basic Agreement (1960).¹⁰⁹ The policy was formally adopted by the Danes in 1994.¹¹⁰ Madsen rightly points out that flexicurity is not a political blueprint or a rational policy design but the outcome of gradual processes over time as well as political struggles and compromises.¹¹¹

Taking a cue from the Danish flexicurity model, the European Commission has also tried to promote flexicurity among its member States. Initiatives to this effect include the Spring Summit (2006), Lisbon Strategy for Growth and Jobs (2007), Mission for flexicurity (2008), European Economic Recovery Plan (2008) and the Euro Plus Pact (2011). Furthermore, the Jobs Strategy (2006) prepared by the OECD and the Employment Sector’s Decent Works Programme conducted by the ILO, have also called for an active implementation of flexicurity.

b. Definition of “flexicurity”

The concept of flexicurity guarantees a certain degree of flexibility to the employer, which is complemented by a proportionate degree of security to the working class. According to Wilthagen and Tross:

Flexicurity is (1) a degree of job, employment, income and ‘combination’ security that facilitates the labour market careers and biographies of workers with a relatively weak position and allows for enduring and high quality labour market participation and social inclusion, while at the same time providing (2) a degree of numerical (both external and internal), functional and wage flexibility that allows for labour markets’ (and individual companies’) timely and adequate adjustment to changing conditions in order to enhance competitiveness and productivity.¹¹²

108 See *Balancing Work and Welfare: Activation and Flexicurity Policies in the Netherlands*, 13(1) International Journal of Social Welfare (2004).

109 *Id.*; The September Compromise (1899) refers to a series of negotiations that took place between the employers and the trade unions in Denmark to develop a Labour Market Constitution, with the underlining objective of creating a mutually beneficial state. In 1960, the said Constitution was revised and renamed the Basic Agreement. The Basic Agreement sought to curtail the unfettered autonomy in the hands of the labour class as well as the managerial prerogative to dismiss the employees arbitrarily.

110 See T. Wilthagen & F. Tros, *The Concept of Flexicurity: A New Approach to Regulating Employment and Labour Markets*, in *Flexicurity: Conceptual Issues and Political Implementation in Europe*, 10(2) European Review of Labour and Research (2004)

111 See K. Madsen, *The Danish Model of Flexicurity- A Paradise With Some Snakes*, European Foundation for the Improvement of Living and Working Conditions, Brussels (2002).

112 See T. Wilthagen and F. Tross, *supra* note 110.

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Thus, the underlining feature of flexicurity is a trade-off between flexibility to the employers and security to the employees. To safeguard the interests of both the employers and employees, there must be proportionality between the quantum of flexibility and security on three main parameters. First, in terms of depth i.e. the extent of flexibility and security. Second, with respect to scope, which relates to the groups that are covered through flexibility and security. And third via length, which refers to the aspect of time, i.e. whether flexibility and security occur simultaneously.¹¹³

It is imperative to note that different forms of flexibility and security exist in a labour market. It is the prerogative of every country to choose which form of flexibility and security is best suited to its labour market needs. Accordingly, every country should determine a suitable trade-off between the most adequate forms of flexibility and security. To take the discussion forward, let us consider the different kinds of flexibility and security that may exist in a labour market.

As per the OECD Jobs Study,¹¹⁴ four different forms of 'labour market flexibility'¹¹⁵ can be adopted by countries. They can be summarized as follows:

(1) External numerical flexibility allows firms to adjust the intake of labour from the external markets through relaxed hiring and firing regulations. (2) Internal numerical flexibility refers to the ability of firms to adjust the working hours of the employees. (3) Functional flexibility relates to the redeployment of the workforce within different sectors of an organization. (4) Financial flexibility refers to the wage differential between the employees on the basis of rate for the job system or assessment based pay system or individual performance wages.¹¹⁶

Similarly Wilthagen and Tross have enumerated the following forms of 'employee security':

(1) Job security is the security of being able to stay in the same job, which can be expressed via employment protection and/or tenure with the same employer. (2) Employment security refers to the security of staying employed, though not necessarily in the same job. (3) Income security relates to receiving a secured income in case of unemployment, sickness or accidents. (4) Combination security entails the possibilities available for combining working and private life, e.g. through retirement schemes, maternity leave, voluntary-sector unpaid work etc.¹¹⁷

113 *Id*

114 *See The OECD Jobs Study: Facts, Analysis, and Strategies*, OECD Employment Outlook (1994).

115 *See J. Atkinson, Flexibility, Uncertainty and Manpower Management*, Institute of Manpower Studies, Brighton, IMS Report No.89.

116 *See J. Berg & S. Cazes, Policymaking Gone Awry: Labour Market Regulations of the Doing Business Indicators*, Comparative Labour Law and Policy Journal (Summer 2008).

117 *See T. Wilthagen and F. Tross, supra* note 110.

Thus, different countries adopt varying combinations of the aforementioned flexibilities and securities, to devise a flexicurity policy that is suitable to their labour market. For instance in Germany and Belgium, the emphasis is on more traditional forms of flexibility (i.e. working time flexibility and functional flexibility in internal labour markets), whereas the focus in both Denmark and the Netherlands is to a greater extent on numerical flexibility.¹¹⁸ The same goes for the security aspect, where Germany and Belgium still tend to focus on income and job security, Denmark has shifted focus to employment security.¹¹⁹

c. The working of the flexicurity model

In order to analyze the working of the flexicurity model, this section will first discuss the Danish approach towards flexicurity, followed by the steps taken by the European Commission in this regard.

The Danish labour market policy is an interesting “hybrid” between the flexible, free market states characterized by liberal hiring-and-firing rules and the generous Scandinavian welfare regimes of high social security.¹²⁰ Thus, the Danish flexicurity model, which is referred to as the ‘Golden Triangle’ is often cited by most scholars in labour market literature as being an extremely effective mechanism. The ‘Golden Triangle’ successfully combines three core elements, i.e. an easy access to hiring and firing, generous unemployment benefits and an active labour market policy.¹²¹

i. Easy access to hire and fire employees

Stiglitz has stated that free market outcomes are Pareto efficient¹²² and optimal.¹²³ Therefore, the Employment Protection Legislations in Denmark are structured along the lines of market fundamentalism.¹²⁴ Denmark has flexible and pro-employer provisions as regards the notice period and authorization before retrenchment, lay-off or closure. It

118 See T. Andersen & M. Svarer, *Flexicurity- The Danish Labour Market Model*, Paper Presented at the IMF Seminar on Flexicurity, Danish Central Bank(2006).

119 See P.K. Madsen, *Flexicurity: A New Perspective on Labour Markets and Welfare States in Europe*, Centre for Labour Market Research, CARMA Research Paper (2006).

120 See T. Bredgaard, F. Larsen & P.K. Madsen, *The Flexible Danish Labour Market—A Review*, CARMA Research Papers, Aalborg University, CARMA(2005).

121 *Id*

122 See N. BARR, *ECONOMICS OF THE WELFARE STATE* (2004). The ‘Pareto principle’ also known as the 80-20 rule, states that in most instances, roughly 80% of the effects come from 20% of the causes. The term ‘Pareto efficiency’ refers to a minimal notion of efficiency and does not necessarily result in a socially desirable distribution of resources. In other words, ‘Pareto efficiency’ makes no statement about equality, or the overall well-being of a society.

123 See J. STIGLITZ, *GLOBALIZATION AND ITS DISCONTENTS*, NEW YORK, NORTON (2002).

124 See A. HARGREAVES, *TEACHING IN THE KNOWLEDGE SOCIETY: EDUCATION IN THE AGE OF INSECURITY*, TEACHERS COLLEGE (2003). ‘Market fundamentalism’ denotes the belief in the ability of laissez-faire or free market economy policies to solve economic and social problems.

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also encourages non-regular forms of employment like part-time, fixed-time, casual and contract labour. But at the same time the provisions against wrongful dismissals are strict, thus guaranteeing employment protection to the employees. In other words the employers are in a position to exercise greater leverage in hiring and firing their employees, though not arbitrarily.¹²⁵

ii. Passive labour market policy

The high labour mobility achieved due to the flexible Employment Protection Legislations must be complimented by an efficient safety net. In view of this, the Danish Government implements passive labour market policies which seek to provide short-term income security and transition security to the unemployed workforce by granting generous unemployment benefits.¹²⁶

First, the Danish employees pay contributions to an unemployment insurance scheme, which is partly government funded but administered by private agencies in close relations with the trade unions. Hence, a worker would receive financial security out of the unemployment insurance fund on being fired, upto a period of 4 years.¹²⁷ Moreover, the employees who are ineligible for the unemployment insurance scheme are covered under a government funded social insurance policy. This ensures that no worker is financially abandoned by the government after being served a pink slip by the employers.¹²⁸

Second, the employers pay a lump sum amount to the employees on the termination of their job, based on the years of service. This is referred to as the severance or gratuity pay. Furthermore, according to the early retirement scheme, the Danish employers are expected to pay a lump sum or monthly payment to an employee who retires prior to his expected date of retirement.¹²⁹

iii. Active labour market policy

The third leg of flexicurity includes lifelong activation and retraining programs for the unemployed workforce. In pursuance of this policy, the government organizes long-term programs that hone and rationalize the skills of the unemployed workers. This enhances their qualification and enables them to bag the available jobs on sheer merit. Moreover, after undergoing the training, the workers can easily be redeployed within and among different sectors of an industrial establishment. A 'carrot and stick' approach

125 See CAMPBELL & A. JOHN, NATIONAL IDENTITY AND THE VARIETIES OF CAPITALISM: THE DANISH EXPERIENCE (2002).

126 See P.K. Madsen, *Flexicurity through Labour Market Policies and Institutions in Denmark*, in P.AUER & S.CAZES, EMPLOYMENT STABILITY IN AN AGE OF FLEXIBILITY (2003).

127 *Id*

128 *Id*

129 See T. Bredgaard & F. Larsen, *External and Internal Flexicurity: Comparing Denmark and Japan*, Comparative Labour Law and Policy Journal (2010).

is the defining feature of this policy, whereby any unemployed worker resisting participation in such activation programs would be flatly denied all unemployment benefits.¹³⁰

Per the Active Labour Market Policy, the Danish Government assists the unemployed workforce in searching for a job, through an efficient public employment service. The government also provides wage subsidies that encourage employers to hire the unemployed workers and promotes self-employment through credit access and tax breaks.¹³¹

In a nutshell, flexicurity enables the employers to lay-off or retrench workers as per their firm's demand for labour. Thereafter, an efficient safety-net ensures that the retrenched workers immediately receive unemployment benefits from the unemployment insurance fund or in the form of severance/ gratuity pay. Moreover, if an employee remains unemployed for a longer period of time, he is enrolled in the life-long skill development program and is assisted in job search by the government. Consequently, flexicurity proves to be a positive sum game for the employer, the workers as well as the overall economy.

The European Commission has also vociferously endorsed the flexicurity policy and made constant attempts to execute flexicurity across its Member States. To this effect, the European Commission has devised the basic guidelines called the "common principles of flexicurity",¹³² which serve as a barometer to prevent a lopsided implementation of flexicurity. The 'common principles of flexicurity' can be summarized as follows:

First, before implementing the policy of flexicurity each country must make ex-ante policy evaluations, to determine the long-term and societal consequences of the strategy as a whole, including its effect on institutional competitiveness. Second, each state must appropriately define the extent of flexibility and security with respect to trade-offs as well as the concrete arrangements and instruments involved in their respective flexicurity pathway. Third, the policy should be implemented through a transparent political process involving all relevant stakeholders and in an environment of trust between the public authorities and social partners. Therefore, flexicurity policies should aim to reduce the divide between the insiders and the outsiders. Fourth, flexicurity should be pursued with a view to contribute to sound and financially sustainable budgetary policies. They should also aim at a fair distribution of costs and benefits, especially between businesses, individuals and public budgets.

130 See T. Bredgaard & F. Larsen, *Flexicurity and Older Workers on the Danish Labour Market*, in *EMPLOYMENT POLICY FROM DIFFERENT ANGLES*, (T. Bredgaard & F. Larsen eds., 2005).

131 See R. Neilsen, *Flexicurity and the Lisbon Agenda: A Cross Disciplinary Reflection*, *COMMON MARKET L. REV.* (2010).

132 See *Towards Common Principles of Flexicurity: More and Better Jobs through Flexibility and Security*, Commission of the European Communities Brussels (2007).

d. Empirical evidence illustrating the success of the flexicurity policy

This section examines the success of the flexicurity policy through empirical evidence from Denmark, Netherlands.

In Denmark, a successful implementation of the ‘Golden triangle’ has reduced unemployment and fostered a general feeling of security among the population. In 1993 the unemployment rate in Denmark was over 12% but after the formal introduction of flexicurity in 1994, unemployment has consistently declined.¹³³ Statistics reported by the World Economic Outlook reveal that Denmark’s unemployment rate in 2011 stood at 4.1%.¹³⁴ Moreover, according to Eurostat the employment rate in Denmark in 2010 was 76.1% thereby surpassing the EU 2020 Headline Target of 75%.¹³⁵ A study by Bingley further reveals that worker turnover in Denmark is about 30% and no less than 25%.¹³⁶

In the Netherlands, flexicurity aims to strengthen the position of workers on temporary contracts by limiting the consecutive use of fixed term contracts to three (the next contract being open-ended). This was incorporated in the Flexicurity and Security Act (1999). Consequently Netherlands saw drastic reduction of unemployment and a strong job creation. According to the statistics in 2006, employment rates in the Netherlands are high (74.3%), though employment in full time equivalents is lower due to the high part time rate.¹³⁷ The Eurostat has reported that the level of unemployment in the Netherlands is among the lowest in the Eurozone (5.1% in 2011).¹³⁸

Studies by Aurer, the European Commission and Eichhorst and Konle – Seidl have further illustrated the successful implementation of flexicurity in Ireland, Austria and Spain respectively.¹³⁹

e. Criticism of the flexicurity policy

A holistic analysis of flexicurity reveals that its implementation has failed to produce the desired results in certain situations. It is worth mentioning that such minor hurdles in

133 See J. Hendeliowitz, *Danish Employment Policy National Target Setting, Regional Performance Management and Local Delivery*, Employment Region Copenhagen & Zealand, The Danish National Labour Market Authority, available at <http://www.oecd.org/dataoecd/13/53/40575308.pdf>.

134 See *World Economic Outlook*, IMF(2011).

135 See *Labour Force Survey*, Eurostat News Release (2011), available at http://epp.eurostat.ec.europa.eu/cache/ITY_PUBLIC/3-29062011-AP/EN/3-29062011-AP-EN.PDF

136 See P. Bingley et al., *Beyond ‘Manucentrism’-Some Fresh Facts about Job and Worker Flows*, Center for Labour Market and Social Research, Aarhus University, Working Paper 99-09 (2000).

137 See *supra* note 101.

138 *Euro Area Unemployment Rate 10.1%*, Eurostat News release (2011), available at http://epp.eurostat.ec.europa.eu/cache/ITY_PUBLIC/3-07012011-AP/EN/3-07012011-AP-EN.PDF.

139 See P. Aurer, *Flexibility and Security: Labour Market Policy in Austria, Denmark, Ireland and the Netherlands*, in *THE DYNAMICS OF FULL EMPLOYMENT*, (G.Schmid & B. Gazier eds., 2002).

the path of flexicurity can be surmounted through effective policy execution. Nevertheless, it is imperative to discuss the criticisms leveled against flexicurity.

First, the highly dynamic nature of the labour market, involving a large number of shifts between jobs, also implies a continuous testing of the productivity of employees. Thus, due to the inadequate restrictions on the employers from conducting mass lay-offs, workers are gradually expelled from the labour market if they fail to meet the productivity criteria set by their employers. Consequently, the number of workers placed on transfer income will increase. For instance in Denmark, over the 40-year period from 1960 to 1999, the number of full-time persons receiving some form of transfer income went from about 200,000 persons to over 800,000 persons (equivalent to about one quarter of the adults aged 15-66 years).¹⁴⁰

Second, Gaxier B argues that the policy of flexicurity will produce beneficial results only during a period of economic expansion, due to the high costs of funding the active and passive labour market policies. In the event of a change in the business cycle to an economic downturn, the cost of funding the flexicurity program would be difficult on account of the falling revenues. Consequently, the political pressure to cut the active programs would become overwhelming.¹⁴¹

Third, Veibrock and Clasen have relied on a number of evaluations to show examples of ‘creaming effects’, implying that the most resourceful among the unemployed are obtaining the best quality activation offers. Thus, the bias towards the stronger unemployed is in conflict with some of the declared political objectives of the active labour market policy.¹⁴²

D. CAN FLEXICURTY BE REPLICATED IN INDIA?

It is worth mentioning that a standard flexicurity model cannot be replicated across States as one-size-fits-all approach. There is great diversity in the social and value systems of different States, which is linked to their historical choices leading to their subsequent economic and social institutions. In view of this, the next section will argue against the replication of flexicurity in India. But the subsequent sections shall explain how India can devise a flexicurity pathway that addresses the pressing needs of the Indian labour market.

a. Problems in transferring the flexicurity policy in India

First, Schneider points out that the reforms proposed by the flexicurity model will only entail the formal economy and specifically exclude the informal sector.¹⁴³ In India

140 See T. Andersen & M. Svarer, *Flexicurity-The Danish Labour Market Model*, Paper Presented at the IMF Seminar on Flexicurity, Danish Central Bank (2006).

141 See B. Gaxier, *Flexicurity and Social Dialogue, European Ways*, Paper Presented at the DG EMPL Seminar (2006).

142 See Veibrock & Clasen, *Flexicurity a State-of-the-art-review*, Working Paper on Reconciliation of Work and Welfare in Europe, RECOWE Publication Dissemination and Dialogue Centre, Edinburgh (2009).

143 See F. SCHNEIDER, *SIZE AND MEASUREMENT OF THE INFORMAL ECONOMY IN 110 COUNTRIES AROUND THE WORLD* (2002).

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the informal sector comprises a staggering 93% of the total labour force.¹⁴⁴ Thus, funneling budgetary finances into a high-cost flexicurity policy is futile, as the majority of the labour class will remain unaffected by these reforms. India needs to channel funds towards public works and self employment programs to uplift the informal sector rather than directing them towards the flexicurity model, which if successful would cover only 7% of the total labour force.

Second, Eichhorst and Konle-Seidl are of the opinion that strict employment protection legislations as existent in India, are hard to abolish, and Auer and Cazes point to national employment systems as considerable sources of inertia.¹⁴⁵ Thus, suddenly introducing the flexicurity policy may have an adverse impact on the Indian labour market. Nevertheless, it is submitted that only because the current system is hard to abolish, that fact alone does not translate into flexicurity having an adverse impact on the Indian labour market.

Third, the flexicurity model is costly because of its need to finance spending on labour market programs and unemployment benefits through the state exchequer. Consequently, higher public spending on active and passive labour market policies will be hampered by the fear of increasing the deficit on the public budgets. Moreover, financing the flexicurity model will not only increase the tax burden but also widen the tax wedge, with an adverse impact on labour demand and supply. For instance, according to an economic survey conducted by the Danish Ministry of Finance, the tax burden in Denmark was as heavy as 46.9% of GDP in 2011.¹⁴⁶ In view of this, a developing country like India is unlikely to effectively implement the flexicurity policy.

b. India must devise its own flexicurity pathway

The previous section has conclusively established that a number of obstacles stand in the way of executing the flexicurity model in India. But nevertheless, implementing flexicurity still remains a better option when compared to the ills associated with the existent inflexible labour market policy. The need of the hour is to devise a flexicurity policy that corresponds to the prevalent socio-political conditions in India.

Paul Vandenberg in his paper titled “Is Asia Adopting Flexicurity? A Survey of Employment Policies in 6 Countries” argues that India must implement flexicurity. He cites the example of how Asian countries like Singapore and Malaysia have modeled their brand of flexicurity according to their national requirements.¹⁴⁷ In Singapore and

144 Ministry of Finance, *Economic Survey 2007-08*, Government of India, New Delhi (2008), available at <http://indiabudget.nic.in/es2007-08/esmain.htm>.

145 See Eichhorst, Werner R.Konle-Seidl, *The Interaction of Labor Market Regulation and Labor Market Policies in Welfare State Reform*, Bonn: IZA. Discussion Paper No. 1718 (2005).

146 See J. Zhou, *Danish for all? Balancing Flexibility with Security: The Flexicurity Model*, IMF Working Paper, European Department (2007).

147 See P.Vandenberg, *Is Asia Adopting Flexicurity? A Survey of Employment Policies in 6 Countries*, Economic and Labour Market Papers, ILO, Geneva (2008).

Malaysia, weak employment protection is traded with strong lifelong skill development strategies and adequate unemployment benefits.¹⁴⁸

Paul Vandenberg further illustrates how China and Korea have also undertaken a massive restructuring of their labour market on the lines of flexicurity since the past decade.¹⁴⁹ Currently, China and Korea are in a state of transition in implementing flexicurity. An effective implementation of flexicurity in these countries has resulted in strong labour market outcomes.¹⁵⁰

Taking a cue from other Asian countries, India also needs to relax the rigid Employment Protection Legislations and contemporaneously strengthen the social security network to safeguard the interests of the unemployed workforce. In view of this, the next section discusses various proposals that could be incorporated in India's flexicurity policy.

c. Defining the contours of India's flexicurity pathway

This section seeks to illustrate how India has already initiated programs that lay down the basic groundwork for creating a sound social security network. Thus, India stands at an advantage in implementing flexicurity in a holistic perspective. But these labour market programs in India are still in their infancy, resulting in a narrow coverage, inadequate financing and tardy implementation. Therefore, in order to implement flexicurity, India needs to strike the appropriate level of trade-off between flexibility and security, coupled with an efficient enforcement and adequate financing of the existent social security schemes.

i. Strengthening programs to uplift the informal sector

The presence of a large informal sector in India is not a hurdle to flexicurity. In fact public works that strengthen the informal sector should be incorporated in India's flexicurity policy. India has implemented a number of public works programs over the years to uplift the informal sector.¹⁵¹ The Mahatma Gandhi National Rural Employment Guarantee Scheme which was launched in 2006 is the most ambitious undertaking to date.

MNREGA guarantees by law each rural household 100 days of manual work annually at the statutory minimum wage of ₹120 per day in 2009 prices.¹⁵² Thus, an average rural household working the entire 100 days would increase its income by at least \$146 annually. An interesting feature of the program is that if work cannot be offered in 15 days from the time of application, then the applicant is paid an unemployment

148 *Id*

149 *Id*

150 *Id*

151 *See* Maharashtra Employment Guarantee Scheme(1970); National Rural Employment Program(1980), Jawahar Rojgar Yojna(1989); Employment Assurance Scheme(1993), Unorganized Workers' Social Security Act(2008).

152 http://nrega.nic.in/circular/WageRate_1jan2011.pdf.

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allowance. The Central Government's outlay for the scheme is 40,000 crore in the financial year 2010-2011.¹⁵³ The scheme currently covers 625 districts across the country and according to the United Nation's Global Assessment Report 41 million households were employed in the MNREGA worksites in 2010-2011.¹⁵⁴

The major criticism leveled against the adoption flexicurity in India, is that it fails to address the needs of the informal sector that employs 93% of the total Indian workforce. But this clearly stands negated if MNREGA is incorporated within India's flexicurity policy. Thus, India needs to further strengthen the implementation of MNREGA by tackling the issues of corruption, transparency and lack of awareness.

ii. Flexible laws governing the organized sector

It is worth mentioning that though the formal labour force constitutes only 7% of India's total workforce, in absolute terms it is still rather large, comprising of over 30 million workers. That is more than the entire workforce of Korea or the total workforces of Malaysia, Sri Lanka and Singapore combined.¹⁵⁵ Thus, there is a need to create flexible labour laws and enhance the social security for the unemployed workforce in the formal sector as well.

Part I and II of the article have conclusively established the need to do away with the highly regulative labour laws and reduce State intervention in labour market governance. Thus, India's labour laws must provide greater leverage to the employers in hiring and firing their employees.

Moreover, at present, there are 47 Central laws and 200 State laws on labour regulation in India.¹⁵⁶ Hence, an employer is expected to maintain a separate register for every piece of legislation and file individual annual returns per the guidelines of every Act. Eventually, most businessmen evade the high cost of procedural compliance either by bribing the inspector or paying the paltry fine imposed by the court. In view of this, the 2nd National Labour Commission, proposed the creation of an umbrella legislation (i.e. a Uniform Labour Code), enforceable across India.¹⁵⁷ Such a code has however not been brought into force.

iii. Passive Labour Market Policies

India has already implemented wide ranging schemes that provide unemployment benefits to the organized workforce. But these programs are rendered ineffective as a

153 See <http://www.nrega.nic.in/netnrega/home.aspx>.

154 *Global Assessment Report on Disaster Risk Reduction- Revealing Risk, Redefining Development-International Strategy for Disaster Reduction*, United Nations Organization (2011).

155 See P.Vandenberg, *supra* note 147.

156 See Debroy, *supra* note 94.

157 See *Second National Commission on Labour Report*, Ministry of Labour and Employment, Government of India (2002), available at http://labour.nic.in/lcomm2/nlc_report.htm.

result of their insignificant coverage, slack implementation and inadequate financing. Thus, India must incorporate these schemes in its flexicurity program thereby strengthening their implementation. It is imperative to discuss some governmental initiatives in this regard.

First, the Industrial Disputes Act, 1947 and the Payment of Gratuity Act, 1972 have made provisions for the payment of a severance and gratuity amount to employees, for 15 days of wages per year of service.¹⁵⁸

Second, India had allocated \$73.5 million for incorporating an unemployment allowance in 2005 to its long standing Employees State Insurance Scheme. The allowance covers loss of employment due to retrenchment, closure or disability due to non-work related accidents. When initiated in 2005, the scheme covered 8.4 million workers, which represent a meager 2% of the total workforce. Thus, currently it is a relatively small program; nonetheless the inclusion of unemployment under the ESI is marked improvement and may be the basis for further expansion in the future.¹⁵⁹

iv. Active Labour Market Policies

India has also initiated a number of lifelong skill development programs; nevertheless due to their small coverage and sluggish execution, they have failed to produce any significant results. Some schemes in this regard are discussed below:

First, India has undertaken a number of skills training initiatives. For instance, the government created the National Renewal Fund (1991), which was replaced by the Plan Scheme for Counseling, Retraining and Redeployment (CRR) in 2000. Other skill development schemes include the Centers of Excellence Scheme, the Skills Development Initiative and the Apprenticeship Training Scheme.¹⁶⁰

Second, India operates a National Employment Service with a network of nearly 1000 'employment exchanges'. The Employment Exchanges (Compulsory Notification of Vacancies) Act, 1959, made it mandatory for the public sector and for private enterprises with 25 workers or more to register their vacancies at the nearest exchange.¹⁶¹ But the failure of the scheme is reflected by a study conducted by Chandra in 2006, which indicates that in the private sector, many employers opt for non-compliance because enforcement is weak and penalties low.¹⁶² As a result of these trends, the number of vacancies registered with the public exchanges fell by half between 1991 and 2002, while the number of placements dropped by 44%.¹⁶³

158 See § 25 F (b) IDA.

159 See P.Vandenberg, *supra* note 147.

160 *Id*

161 See P. Vandenberg, *supra* note 147.

162 See A. Chandra, *The Role of Training in Promoting the Objectives of the National Renewal Fund*, in NATIONAL RENEWAL FUND: A LOOK AHEAD (M.L.Nandrajog ed.,1999).

163 *Id*

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Third, a number of initiatives have been undertaken by the government to encourage self-employment. Initiatives to this effect include the Prime Minister's Rozgar Yojna and the Rural Employment Generation Program.¹⁶⁴ It is imperative to reiterate that though these schemes provide the basic framework for future expansion, as of now they are still in their infancy. Thus, the government needs to be conscious of the need to make these services more relevant when incorporating them in the flexicurity agenda.

v. The financial aspect of India's flexicurity policy

The high budgetary cost associated with the lifelong learning strategies and providing unemployment benefits is often seen as an impediment in implementing flexicurity in India. It is true that if India implements flexicurity it will require a more efficient, and sometimes greater, use of public and private resources, but this should pay off in terms of more jobs and higher labour productivity.

In this regard, while defining the 'common principles of flexicurity', the European Commission has rightly pointed out that the financial cost of flexicurity should always be assessed against the budgetary benefits stemming from enhanced labour market dynamism, higher employment and productivity.¹⁶⁵ The European Commission maintains that flexicurity increases labour market participation. Consequently, long-term reliance on social security benefits decrease and thereafter administrative costs can be reduced. Bassani and Duval relied on data from the OECD Member States and concluded that a 10% increase in the Active and Passive Labour Market Policy spending per unemployed person reduces by 0.4% the unemployment rate.¹⁶⁶

Taking a cue from countries like Denmark and Netherlands, India must also devise ways of mutual risk management by distributing the budgetary costs of flexicurity between businesses, individuals and public budgets. Withagen suggests that a significant proportion of the on-the-job-training costs as well as the unemployment benefits can be borne by the employers and the workers. In addition, public policies may channel the financial burden towards individuals, e.g. through tax deductions.¹⁶⁷

IV. CONCLUSION

It is high time that the Indian government walks the tightrope of balance between flexibility to the employers and security to the employees. After all, both the entrepreneur and labour are pivotal factors of production. Weighing the scales in equilibrium through flexicurity holds the key, or else one of the two factions would stand aggrieved.

164 See P. Vandenberg, *supra* note 147.

165 See *supra* note 132.

166 See Bassani & Duval, *Employment Patterns in OECD Countries: Reassessing the Role of Policies and Institutions*, 35 OECD WP (2006).

167 See T. Withagen & M. Houwerzijl, *Reconciling Labour Market Flexibility and Social Cohesion: A Methodological Tool Proposed by the Council of Europe*, Paper Presented at Forum, Council of Europe (2005).

Admittedly, transplanting the flexicurity model into the socio-political setup of India maybe a daunting task for the government, but nevertheless it is imperative to implement it. Eventually, the success of flexicurity in India would depend upon the government's willingness to implement labour reforms and the existence of mutual trust between the social partners and the State. In this regard, Abraham Lincoln had once said:

To secure to each labourer the whole product of labour, or as nearly as possible, is a tricky object of any good government.