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### SELECT PUBLICATIONS

- |   |     |   |
|---|-----|---|
| ◆ Benchmarking the Best CSR Practices by SMEs in India                        | 250 | J.S. Sodhi, N.K Nair                        |
| ◆ Global Economic Crisis : Back to Keynes?                                    | 275 | J.S. Sodhi, N.K Nair                        |
| ◆ Quality of Growth; Approaches to Inclusive                                  | 350 | J.S. Sodhi, N.K Nair                        |
| ◆ Corporate Social Responsibility by SME's                                    | 150 | J.S. Sodhi                                  |
| ◆ Skilling Women in the Informal Sector                                       | 325 | M.S. Ramanujam<br>J.S. Sodhi                |
| ◆ Perspectives of Corporate Social Responsibility                             | 150 | J.S. Sodhi                                  |
| ◆ Economics, Lawlessness and Justice in India                                 | 310 | J.S. Sodhi, N.K Nair                        |
| ◆ Management of Values and Ethics in Corporate Governance                     | 125 | J.S. Sodhi                                  |
| ◆ Making Globalization Work   | 250 | J.S. Sodhi                                  |
| ◆ Development and Nationhood: An India Perspective                            | 350 | J.S. Sodhi                                  |
| ◆ Tata Steel: Becoming World Class  | 310 | S.N. Pandey<br>Jai B.P. Sinha<br>J.S. Sodhi |
| ◆ Development as Freedom: An India Perspective                                | 350 | J.S. Sodhi                                  |
| ◆ Management of Contract Labour in India                                      | 350 | M.S. Ramanujam<br>J.S. Sodhi                |
| ◆ Developing a Culture of High Performance                                    | 325 | Rama J. Joshi<br>J.S. Sodhi                 |
| ◆ Technology Transfer, Labour Relations & Human Resources Management in India | 300 | J.S. Sodhi<br>Pravin Sinha                  |

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The Indian Journal of Industrial Relations

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# THE INDIAN JOURNAL OF INDUSTRIAL RELATIONS

## A REVIEW OF ECONOMIC & SOCIAL DEVELOPMENT

Special Issue on

Labor Law Reforms In India

Guest-Editor

Lord Meghnad Desai



Vol. 50

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JULY 2014

# The Indian Journal of Industrial Relations

A Review of Economic & Social Development

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**The Indian Journal of Industrial Relations: A Review of Economic & Social Development (IJIR)** is devoted to dissemination of knowledge for effective management of human resources and harmonious industrial relations. A quarterly in English, the journal enjoys high academic reputation in India and elsewhere and is widely subscribed by government institutions, universities and private sector organizations. A refereed journal, its readership consists of academia, policy makers, practicing managers and student community.

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## About the Guest - Editor



Lord Meghnad Desai is an Indian-born, naturalized British economist and Labor politician. He has been awarded the Padma Bhushan, the third highest civilian award in the Republic of India, in 2008

He secured a master's degree from University of Mumbai, after which he won a scholarship to University of Pennsylvania in 1960. He completed his PhD at Pennsylvania in 1963.

He worked as Associate Specialist in the Department of Agricultural Economics, University of California, Berkeley, California. He then became a lecturer at the London School of Economics in 1965. At LSE, he taught econometrics, macroeconomics, Marxian economics and development economics over the years.

He wrote his first book Marxian Economic Theory in 1973 followed by Applied Econometrics in 1976 and Marxian Economics in 1979. He wrote Testing Monetarism, a critique of monetarism, in 1981. Desai has written extensively publishing over 200 articles in academic journals and had a regular column in the British radical weekly Tribune during 1985–

1994, in the Indian business daily Business Standard (1995–2001) and in Indian Express and Financial Express. During 1984–1991, he was co-editor of the Journal of Applied Econometrics. A selection of his academic papers was published in two volumes as The Selected Essays of Meghnad Desai in 1995. Lord Desai published Rethinking Islamism: Ideology of the New Terror (2006), The Route to All Evil: The Political Economy of Ezra Pound (2007), a novel Dead on Time, (2009) and The Rediscovery of India (2009). Besides the book on Marx's Revenge: The Resurgence of Capitalism and the Death of Statist (2002) he also published a biography of Indian film star Dilip Kumar titled Nehru's Hero: Dilip Kumar in the life of India (Roli, 2004).

He was Chairman British Labor Party during 1986–1992 and was made a life peer as Baron Desai, of St Clement Danes in the City of Westminster, in April 1991.

In 2003, he retired as Director of the Centre for the Study of Global Governance, which he founded in 1992 at the London School of Economics (LSE), where he is now Professor Emeritus. He was Chairman of the Trustee's Board for Training for Life, Chairman of the Management Board of City Roads and on the Board of Tribune magazine. Lord Desai was also a founding member of the Development Studies Institute (DESTIN) at the LSE in 1990. Lord Desai is Chairman of the Official Monetary and Financial Institutions Forum (OMFIF) Advisory Board,

# The Indian Journal of Industrial Relations

## A Review of Economic & Social Development

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VOLUME 50

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### Contents

#### Articles

Reforming Labor Laws	<i>Meghnad Desai</i>	1
Labor Law Reform in India: Insights from Tangled Legacy of Sidney & Beatrice Webb	<i>Bruce E. Kaufman</i>	2
Rethinking Labor Law Reforms	<i>Arun Maira</i>	24
Transition to Labor Law Reform: State-Level Initiatives & Informal Sector Labor Relations	<i>Hemal Shah</i>	33
Labor Market Flexibility & Trajectories of Development: Lessons from Brazil, India & China	<i>Anil Verma &amp; Ana Virginia Moreira Gomes</i>	51
Quo Vadis, Industrial Relations Disputes Resolution...?	<i>Jerome Joseph</i>	75
Reforming the Industrial Dispute & Trade Union Acts	<i>Tushar Poddar</i>	89
Labour Law Reform in India	<i>J.S. Sodhi</i>	100
Indian Industrial Relations Law: Case for Reform	<i>Debi S. Saini</i>	118
Legal Reforms for the Self-Employed: Three Urban Cases	<i>Martha Alter Chen, Roopa Madhav &amp; Kamala Sankaran</i>	133
Turnover Intentions among Indian Software Professionals	<i>Gloryson R B Chalil &amp; L Prasad</i>	151

**Powerful Leadership & Excellence in  
Public Enterprises**

*V N Srivastava*     **165**

**Strategy & Structural Dimensions – A  
Comparative Study of Four Industries**

*Bindu Gupta &  
Ajay Singh*     **180**



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## Guest-Editor's Foreword

# Reforming Labor Laws

**Meghnad Desai**

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India has for several decades now got itself into a situation of denial and delay in the matter of reforming the labor laws. The laws were passed some before independence and some after on the mistaken analogy of a developed industrialized country with a majority of its workforce in large factories. Socialist thought, reformist as well as revolutionary, had the industrial worker at its centre. The capitalist system was supposed to be sustained by exploitation of the worker—the proletariat – and hence regulation of the employer-worker relationship took prime place in reform legislation.

India has a slim minority employed in the organized sector, barely 5 % of its total work force. Yet the rights of this tiny minority are guarded by a phalanx of laws and regulations which has had the effect of retarding manufacturing growth in India. The principal legislations concern the ability to hire workers on non-permanent contracts, and, as that is difficult, the even more difficult task of terminating their employment on any grounds whatsoever. Firms find it difficult to liquidate themselves as that may cause unemployment of their workers. To this may be added over a hundred an-

nual inspections and enforcement of regulations which add to the transactions costs of doing business in the manufacturing sector.

India's Asian neighbors, Bangladesh, Malaysia, Indonesia, to say nothing of China or South Korea, have overcome these problems and managed to develop a thriving manufacturing sector. In India, the manufacturing sector remains stagnant at around 16 % and has relatively small size units which are engaged in medium and high tech industries. Many Indian manufacturers employ contract labor which has few rights and can be sacked on expiration of contract. This is healthy neither for the workers nor for employer-employee relationships. Our Asian neighbors have large factories with hundreds of employees manufacturing low tech products which have a large export market. India lags behind in this area.

Our journal has explored the topic of Informal Labor Markets in a special issue previously. This special issue tackles the urgent question of reform of labor laws. I welcome this initiative and congratulate all the contributors and Professor Sodhi and the editor for their excellent effort.

**By Invitation**

## **Labor Law Reform in India: Insights from Tangled Legacy of Sidney & Beatrice Webb**

**Bruce E. Kaufman**

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*Sidney and Beatrice Webb, co-founders of the industrial relations field and early pioneers of Fabian Socialism significantly influenced Jawaharlal Nehru and India's post-Independence model of economic development. Part of this model was a protectionist regime of labor law which has now come under increasing criticism as a structural impediment to growth. This article reviews the ideas of the Webbs and uses them as a prism for evaluating the case for labor law reform and the direction it should take. The article advances a three-prong conclusion: the Webbs' program for labor market regulation remains sound in principle but the specifics in India need substantial adjustment; the most important way to generate higher employment growth is not from labor market deregulation but continued liberalization of product markets and encouragement of entrepreneurship; and the most critical pro-growth reform is more efficient and honest institutional-regulatory governance.*

**Bruce E. Kaufman** is Professor, Department of Economics, Georgia State University, Atlanta GA USA Department of Employment Relations & Human Resources, Griffith University, Brisbane QLD AU. E-mail: bkaufman@gsu.edu

### **Introduction**

India posted an impressive growth record after economic liberalization in 1991. A slow-down during the world financial crisis of 2008-2010 was expected but so too was a rebound once the crisis passed. The crisis is now four years over but the growth recovery for India is disappointingly anemic. A number of analysts inside and outside the country conclude growth is obstructed by structural problems. Illustratively, IMF Report (2014:19) concludes, "There is consensus that structural reforms are going to be the lynchpin of an eventual rebound in growth". Five key areas of structural reform are listed: (1) power and natural resources, (2) agriculture, (3) health and education, (4) investment climate, and (5) labor regulation.

The IMF report is tactful and frames these structural problems, not as government failures of the past, but as agenda items for swift legislative action going forward.

Other analysts, however, are far more critical and say these problems have been allowed to fester and worsen because, rather than take liberalization the next step forward, Indian governments of the last decade have reverted to “the old recipe of social spending and industry mandates... and granting massive new entitlements” associated with “Nehru’s turn to Fabian Socialism” in India’s post-Independence era (Dalmia, 2014: 1-2). In a similar vein, the press in India is starting to wonder if the economic miracle is returning to the more anemic ‘Hindu rate of growth’ which Das (2006:2) explains, “had nothing to do with Hinduism and everything to do with the Fabian socialist policies of Prime Minister Jawaharlal Nehru”. A well-known American labor law professor, having recently returned from a trip to India, also puts the finger of blame for India’s growth problems on failure to jettison the “hopeless forms of Fabian Socialism that Jawaharlal Nehru, India’s first prime minister, brought into public life between 1950 and 1990” (Epstein, 2014: 2).

The failed policies associated with Nehru and Fabian Socialism provide a natural segue into the implications for labor law reform of the seminal writings of Sidney and Beatrice Webb, two of the founders of not only Fabian Socialism but also the field of industrial relations (Cole, 1943; Harrison, 2000; Kaufman, 2004). Many observers believe that Indian labor law is increasingly out of date, complex and burdensome and poses a structural impediment to sustained economic growth (VenkataRatnam, 2004; Hill, 2009; Saini, 2009; Krueger, 2013). But,

as cited above, a number of analysts also believe that the policies and practices historically associated with the industrial relations field, particularly as it came from Britain and Fabian Socialist writers such as the Webbs, are part of the source of the labor regulation muddle.

**Trade unions have two faces — a positive voice face and a negative monopoly face.**

This article tries to sort through parts of the Webbs’ writings with enduring value as guides for industrial relations and labor law reform and parts of which have been shown incorrect or harmful by historical experience. Analogous to the idea of Freeman & Medoff (1984) that trade unions have two faces — a positive voice face and a negative monopoly face, it is argued that the theory of the Webbs also has two faces, a positive industrial relations face and a negative Fabian Socialism face. The paper briefly identifies and delineates these two faces and then applies them to working-out useful principles for Indian labor law reform. Since much of the existing IR and labor law literature in India is descriptive and empirical, introducing a stronger conceptual element may be helpful for both the endeavors.

### **American & British Influences**

Industrial relations started in the late 19<sup>th</sup> and early 20<sup>th</sup> centuries as an Anglo-American project among reform-minded academics broadly linked to a social-institutional approach to economics, albeit



with a clear link to Germany and that country's tradition of historical economics and active social policy (Kaufman, 2004). Industrial relations was a response to the growing labor problem and attendant class-conflict in late 19<sup>th</sup> century industrializing countries and was positioned as a middle-way solution between laissez-faire orthodox economics and revolutionary Marxist-radical economics. These Western ideas on a middle way solution to the labor problem became a uniquely Indian third-way approach when integrated with the Gandhian philosophy of industrial harmony and self-government (Bose, 1956).

The concept of industrial relations and its formalization as a field of teaching and research in universities appeared first in the United States in the late 1910s under the leadership of Richard Ely and John Commons, institutional economists at the University of Wisconsin. The industrial relations term in early American usage was a short-hand for 'relations between employers and employees in industry and, hence, at its beginning industrial relations was conceived broadly as the study of the employment relationship and the labor problems which grow out of it. Illustrative of this broad focus, IR textbooks often used 'labor problems' in the title (e.g., *Labor Problems in American Industry*, Daughtery, 1933) and featured chapters on personnel management, trade unions, labor law, social insurance, and national labor policy.

In Britain, Sidney and Beatrice Webb are widely regarded as IR founders (Hyman, 1989; Ackers & Wilkinson,

2003). They also founded the London School of Economics (LSE) in 1895. Their seminal contributions, however, were not to launch the IR field itself – labor studies was not part of the early LSE curriculum and IR as a constituted field of study did not emerge in Britain until the late 1940s – but to initiate the study of organized labor as a legitimate topic of scholarly inquiry in England. The Webbs' most famous books are *History of Trade Unionism* (1894) and *Industrial Democracy* (1897). They also wrote on other labor topics, such as the poor laws and labor conditions of women, but labor law and personnel management were peripheral to their research agenda and remained so in the British IR field until the 1980s.

The subject of industrial relations in Britain started out, therefore, more union-centric than in the USA and also substantially to the left in the political spectrum (Hyman, 1989; Ackers & Wilkinson, 2003; Kaufman, 2014). The Webbs, and their intellectual successor G.D.H. Cole, were proponents of democratic socialism and, from experiences such as World War I and the Great Depression, became increasingly outspoken critics of capitalism. The democratic socialist and leftist Labor Party leaning of British industrial relations continued after World War II, albeit moderated by the Cold War chill of anti-communism, and found expression in the Atlee government's Fabian-inspired program of nationalization of key industries, industrial democracy through widespread industry-level collective bargaining, steeply graduated income and estate taxes, and extensive welfare state social

programs (Hinton, 1983). This economic growth model, attractive in theory and appealing to anti-capitalist sentiments widespread at the time, proved debilitating in practice and by the 1970s Britain declined to the unenviable status of 'poor man of Europe.'

As an organized area of teaching and research, the early field of industrial relations in India has in some visible ways more affinity to the American model than the British. For example, the organizing concept of labor problems for the study of industrial relations was widespread in America but not Britain and in India the term found frequent use (e.g., Agarwala, 1947; Mehrotra, 1965). Also, Indian writers followed the American model and included within industrial relations the full range of topics related to labor problems and the employment relationship, albeit with more emphasis on collective than individual relations (Seth, 1966). Giri's textbook is illustrative since it includes separate chapters for personnel management, labor law, social insurance, trade unions, and national labor policy. Also illustrative are early issues of *Indian Journal of Industrial Relations* which contain articles on all areas of the employment relationship, including labor law and management. By way of contrast, the range of topics in early issues of the *British Journal of Industrial Relations* is noticeably narrower.

America has one of the least regulated labor markets among advanced industrial countries and yet India has, by most accounts, much the opposite with a highly complex, bureaucratic, and protec-

**India has much the opposite with a highly complex, bureaucratic, and protective regime of labor law.**

tive regime of labor law (Debroy & Kaushek, 2005; Venkatta Ratnam & Verma, 2010). One has to conclude therefore, that while the American model may have to some perceptible degree influenced the formation of industrial relations in India as an academic field of study, its influence on the regime of IR institutions and labor laws actually put in place in India pales next to the influence of Great Britain (Kennedy, 1965). Not surprisingly, therefore, one of the imports from Britain – most visibly and influentially brought back by India's first Prime Minister — was the democratic socialist economic development model espoused by intellectuals and political leaders associated with the Fabian Society, British Labor Party, and other left-leaning groups (Narayan, 1964; Nanda, 1996).

Nehru spoke often and eloquently on his desire to steer India toward a democratic form of economic planning and market socialism which was positioned between American-style capitalism and Soviet style communism (Akbar, 1990). The exemplars of the period, from which he gained inspiration on his extensive foreign travels throughout Europe in the 1910s-1940s, were countries such as Britain, France and Sweden which moved toward nationalization of core industries, five year economic plans with state directed investment, national labor movements, social welfare states, state

bureaucratic regulation of business, steep income, wealth, and estate taxes, and an end-goal of 'euthanasia of capitalism.' American ambassador to India in the early 1960s, John Kenneth Galbraith, recalled that, "Nehru loved to reminisce about the world of R.H. Tawney, the Webbs and of Trinity College and Cambridge" (Nanda, 1996: 478). Unfortunately, India also followed in Britain's post-World War II footsteps and went down the socialist path to 'poor man of East Asia' by the late 1980s (Das, 2001; Drèze & Sen, 2013).

### Two Faces of the Webbs

The Webbs are co-founders of two different intellectual streams of thought. The first stream is a field of labor studies known as industrial relations with roots in historical-institutional economics and sociology and the second is a collectivist-oriented doctrine of evolutionary democratic socialism known as Fabian Socialism. Although the Webbs intend both parts to seamlessly fit together, they nonetheless have an identifiably separate presence in their work and the latter is considerably more radical and transformative than the former. A brief synopsis follows, labeled as their *industrial relations face* and *Fabian socialism face*, respectively.

*Industrial Relations Face:* A detailed review and exposition of the Webbs' theory of industrial relations is provided in Kaufman (2004; 2013) and Kaufman & Barry (2014). Provided here is only a brief summary as it pertains to consideration of labor law reform. A

more general exposition of the industrial relations theory of labor law is provided in Kaufman (2012a).

The Webbs, like Commons and other IR founders, were attracted to the study of labor as a way to discover methods to raise the condition of the working people, reduce class conflict, and make the work world more efficient, equitable, and democratic. They gained insight from Marx but rejected his theory of class struggle and proletarian revolution. The Webbs saw that the labor problem writ large, and individual labor problems writ plural, come from structural features of the capitalist employment relationship which can be contained and de-radicalized by institutional reform but never eliminated.

Central to their diagnosis are three interacting factors in a private property, competitive market, laissez-faire system. The first is that human labor is treated as a commodity to be traded on a buy-low/sell-high basis, putting workers in a de-humanized, insecure, and distrustful position which, in turn, undercuts productive efficiency, abuses human rights, and breeds conflict. The second is that the capitalist employment relationship contains an inherent inequality of bargaining power between employers and workers in both external and internal labor markets with consequent low wages, long hours, harsh conditions, sizable income inequality, and arbitrary treatment, arising from widespread surplus labor, involuntary unemployment, market and organizational failures, and employers' unrestricted private property rights. The third

is that in early capitalism the mass of workers are typically given little-to-no voice, representation, and due process rights inside firms, thus making the workplace an industrial autocracy — sometimes benevolent but often despotic — while in the polity at large capitalists and the rich dominate the government and set the rules of the game to keep labor politically and economically subordinated and exploited.

The Webbs point to many onerous and inequitable outcomes that arise from these defects in the capitalist employment relationship. Topping their list, however, are two. The first is persistent and widespread unemployment which puts the employer in a despotic ‘take it or leave it’ position and forces workers to accept shameful conditions and callous exploitation — outcomes orthodox economic theory either denies as a matter of logic or claims flexible wages automatically eliminate. The second is glaring social injustice when rich, powerful, and socially privileged elites use the government to rig the game so they can siphon large surplus income (economic rents) produced by a mass of common laborers working all year round in life-shortening sweatshop conditions.

Having diagnosed the cause of labor problems in capitalism, the Webbs offer a variety of solutions. They recognize the place to start an evaluation of labor policy is specification of the social objectives which policy is intended to achieve. They follow orthodox economics and make efficiency the first priority but argue for an enlarged conception of social efficiency.

An economic system is socially efficient when it best satisfies consumers’ wants but subject to covering all social costs of production. For labor, social cost includes minimum sustainable living expense for a worker and family, ability to acquire and maintain the human and social capital required for production, and provision of workplace conditions and treatment which cover socially recognized human and political rights. Non-labor social costs include infrastructure, environmental sustainability, and quality of life dis-amenities. These costs must be covered and incorporated into product prices or private cost of production is less than social cost, leading to a negative externality-type market failure.

The Webbs put-forth a two-prong labor policy program to promote social efficiency. The first prong is to improve wages, conditions, and treatment for workers in the lower part of the industrial pyramid. Doing so also keeps wages and labor conditions growing in line with productivity growth, thus maintaining macroeconomic demand/supply balance and social justice (Hobson, 1923; Commons, 1934). American writers call this part of the IR strategy ‘raising the plane of competition.’ To accomplish this goal, the Webbs propose establishment of a common rule that extends across the national labor market and requires all employers to provide a minimum standard of terms and conditions of work.

**Since social cost rises over time, so should the level of the minimum standard.**

This minimum is called the Social Protection Floor by the International Labor Organization (ILO). Since social cost rises over time, so should the level of the minimum standard.

Many employers and neoclassical economists oppose protective labor laws, or resist strengthening them, because they increase the price of labor, move firms up their labor demand curves, and reduce jobs (Wachter, 2012). However, what they fail to appreciate is that this loss of jobs promotes social efficiency by bringing private cost closer to social cost, thus ending an implicit social subsidy for consumers and firms – particularly the affluent elite who do most of the consumption (Kaufman, 2009). The parallel situation is loss of jobs when government decides to curb industrial pollution, say by putting an emissions' tax on firms.

The social cost common rule can be established through one or a combination of methods, all of which the Webbs promoted and were later made staple subjects in labor problems textbooks. A common rule, for example, can be established by industry-wide collective bargaining, protective labor laws such as minimum wages and maximum hours, social insurance such as unemployment compensation and old age pensions, or public sector funded jobs programs. Setting the common rule is challenging because social cost of labor varies by family size, urban vs. rural location, stage of economic development, and other such factors; nonetheless, many countries, including India, specify an official poverty line based on such contingencies so the task is not insuperable.

Also challenging is the contradictory role of trade unions in this process. On one hand, without a strong labor movement workers suffer from an inequality of bargaining power in labor markets and the government is inevitably dominated by business interests who block or greatly weaken protection for workers through labor law and social insurance. On the other hand, a strong labor movement inevitably leads to many counter-inefficiencies which frequently grow worse over time. In the labor market, the initial effect of unions is 'monopsony-reducing' as they level the playing field and promote social justice; however, over time they become 'monopoly-creating' as their continual push for 'more,' coupled with only patchwork organization across industries, gradually leads to inflated wages, productivity-sapping work practices, and a privileged labor aristocracy (Kaufman, 2012b). Likewise, in the political process unions have a tendency to shift from a broad-based voice of the working class to a narrow sectional interest group largely concerned with protecting their institutional power and member's vested perquisites.

The first prong of the Webb's labor strategy is to push up on the lower end of the industrial pyramid by using collective bargaining, legal enactment, and social insurance to establish and then gradually raise the plane of competition. The second prong is to push down on the top end of the pyramid through egalitarian social policies and progressive income, wealth, and inheritance taxes. The Webbs agree that people who make large contributions to production through

successful entrepreneurship, management, and technical skills deserve higher wages and income. In this respect the Webbs accept the marginal productivity theory doctrine. However, it is also their view that much of the income received by top-end groups in society takes the form of an economic rent, called surplus value by Marx and unearned income by J. S. Mill.

**Much of the income received by top-end groups in society takes the form of an economic rent.**

An economic rent is created when a resource owner receives a return higher than minimum supply price, such as in the case of a monopoly rent when a firm with market power charges a price higher than cost of production. From the Webb's perspective, and as also expounded by their Fabian colleague Hobson (1923), a significant portion of profit, interest, land rent, and high-end salaries – factor returns mostly accruing to socially privileged people in the top end of the income and wealth distributions – are a rent payment made possible by various natural and contrived scarcities and barriers to competition. Large CEO salaries, for example, are partly a payment for valuable leadership and business acumen but, also, a rent payment made possible by family connections, political patronage, or cronyism with the board of directors. Similarly, the high salaries of doctors, professors, and government officials are partly a return on human capital investment and hard work but, for many, also a rent payment

for being born into a socially advantage family with the money, social connection, caste, and skin color to first get into elite private schools and universities and then high-end professions and corporations.

The nature of an economic rent is that it can be taxed away without reducing supply or distorting incentives. Since rent is an unearned income, and because it also provides the affluent and powerful with large sums of money to twist the political process to preserve and strengthen their privileged position, the Webbs were strongly in favor of enacting steeply progressive income, wealth, and inheritance taxes. They were also strongly in favor of social policies that break down artificial barriers to competition and social mobility, such as contained in preferential laws, institutional rules, and social norms favoring men over women, upper class over lower class, and light-skinned over dark-skinned. Equally favored were policies that opened the door to equal opportunity, such as quality universal public education and health care and civil service rules for government employment.

### **Fabian Socialism Face**

Part of the Webbs' claim to founders' status is that they were among the first writers to articulate these principles in such a thorough and penetrating way. If this part of the Webbs' thought is all that had influenced Nehru, the post-Independence history of India would be considerably different. However, the influence of the Webbs, Hobson, Tawney, Besant,

and other Fabians in Nehru and India was not primarily through the case they developed for industrial relations but, rather, the case they built for transition of the national economy from free market capitalism to democratic socialism and industrial planning (Narayan, 1964; Akbar, 1990; Das, 2001).

Surveying the history of 19<sup>th</sup> century England, Sidney Webb in his chapter in the *Fabian Essays in Socialism* (Shaw, 1889: 46-47) tells readers of the “hopeless failure of an almost complete industrial individualism...[with] unrestrained private property... [and] subjection to a political oligarchy”. Like Marx, Webb thought the transition to socialism is inevitable and, indeed, states, “the economic history of the century is an almost continuous record of the progress of Socialism” (ibid.). But unlike Marx, Webb sees no need for class struggle and revolution. He and Beatrice were convinced that the wage-earning class was coming to realize the superiority of planned socialism over anarchic capitalism. They also thought, with the gradual democratization of the national government driven by popular pressure and extension of suffrage, political control of the state was shifting from the oligarchy of capital and land owners who dominated Parliament and most benefited from laissez-faire capitalism to the mass of wage-earners who most benefit from socialism. He concludes his chapter, therefore, with this forecast: “private ownership of the instruments of production is irreconcilable with the common weal...[It] keeps the many workers permanently poor... in order to make

a few idlers rich...[and] will inevitably go the way of feudalism which it superseded” (Shaw, 1889: 81-82). Part of the reason the Webbs founded the LSE was to train administrators and managers to staff the future socialist state planning apparatus.

Many socialists are frustratingly vague about the transformation from capitalism to socialism and the institutional structure and performance of a socialist economy. The Webbs are exceptions and devote an entire book, *A Constitution for the Socialist Commonwealth of Great Britain* (1920), to this purpose. With the wage-earning class exercising democratic control of the government, a process of nationalization of industry is initiated, starting with core or ‘commanding heights’ sectors (e.g., steel, banking, transport, communication) with gradual but not complete extension to other sectors. Planning boards are created for each industry to make strategic investment, production, and pricing decisions and exercise supervisory oversight of publically-appointed management. Private property for individuals is protected but private ownership of industry is gradually extinguished through a mix of confiscation, fair market value compensation, and steep profits tax. The end result is the “transformation of profit-making enterprise into public service” (Ibid: 334) with greater efficiency achieved by replacing capitalist monopoly, waste, and boom-bust cycles with public price regulation, scientific enterprise administration, and coordinated planning of production and investment.

## **Implications for Labor Law Reform**

**Nehru and the National Congress Party gradually implemented a democratic socialist planned economy model for India which in broad outline matched the Fabian prescription.**

Nehru and the National Congress Party gradually implemented a democratic socialist planned economy model for India which in broad outline matched the Fabian prescription and post-war governance regimes in Britain, France, and other European countries, albeit with numerous Indian adaptations for its status as an Asian developing nation and non-aligned country in the Cold War. The initial growth results were encouraging but then faltered in the 1970s and 1980s amidst rising crises with inflation, balance of payments deficits, and mounting labor strikes (Bhattacharjee, 2001; Nankervis, Cooke, Chatterjee & Warner, 2013: Ch.4).

Many other countries experienced similar problems. In reaction, British voters in 1979 and American voters in 1980 decided to shift toward neo-liberalism by electing Thatcher and Reagan. Although the score card for both leaders is mixed, two trends are clear. The first is the growth rate of both economies staged a considerable rebound until punctured by the world financial crisis of 2008-2010, fueled in part by liberalization of product and financial markets and expansion of small-medium entrepreneurial-driven firms. The second is that both countries also reshaped their labor law regimes

through a two-pronged strategy which rolled-back union power and collective bargaining and substituted expansion of minimum employment standards through specific labor law additions. The UK, for example, adopted a national minimum wage and various European Union directives on work hours and workplace information-sharing while the USA adopted guaranteed family and medical leave for women workers and discrimination protection for handicapped workers. Although neo-liberalism is typically associated with deregulation, it is particularly evident in the case of Britain (less so the USA) that breadth of labor market regulation actually increased, partly to fill the void left by receding collective bargaining and partly to protect the vulnerable from a market-induced race to the bottom by setting-up a strengthened floor of minimum employment standards à la the Webbs (Mitchell, Gahan, Stewart, Cooney, & Marshall, 2010).

Now, what about India? To an outside observer, it appears that India has only partially accomplished product and financial market liberalization and barely touched labor market liberalization. However, in the case of labor law the kind of reform that is needed is only partly liberalization — i.e., loosening regulatory/legal constraints to spur job-creation by reducing labor cost and promoting employment flexibility – and more in the direction of regulatory modernization and improved governance. This dimension of the subject is postponed, however, to later in the paper. The strategic point of entry into the labor law reform debate is, perhaps paradoxically, not in labor markets but product markets.



India needs to generate roughly twelve million new jobs each year to keep-up with labor force growth. Further, these jobs need to offer better wages and conditions to satisfy the rising quality of life expectations of the Indian people. One can reasonably argue about the degree of blame to be laid at the door of European socialist doctrines and their importation by Nehru and the Congress Party but, regarding the general argument that India still suffers from excessive government intervention and costly economic regulation, the evidence seems clear-cut. Indeed, this theme runs like a gold thread through books and policy reports on the growth prospects for the Indian economy (e.g., Drèze & Sen, 2013; Hope, Kochar, Noll & Srinivasan, 2013; World Economic Forum, 2014).

**Much of India remains mired in poverty and archaic business practices.**

India, as oft-observed, is a land of sharp contrasts and contradictions (Nilekani, 2009). On one hand, liberalization has spawned a rapidly growing IT sector and expanding number of world-competitive companies. On the other hand, much of India remains mired in poverty and archaic business practices. Although only an anecdotal account, mentioned earlier was law professor Richard Epstein's discussion of his first visit to India in early 2014 and in it he provides in microcosm the extent to which liberalization still remains a considerably incomplete project (Epstein, 2014). Rather than being able to buy a mobile

phone at one store with a credit card and relatively transparent and easy-to-complete contract, he had to travel around the choked streets of Mumbai to seven different stores to get photographs, purchase the phone, purchase the SIM card, on several occasions fill-out lengthy paperwork, and always pay with cash. In the short-run, this round-about process creates jobs for the taxi driver, shop keepers, and government officials but in the long-run it keeps India trapped in a low productivity third-world type economy with anemic job growth as other Asian countries gain competitiveness, move upstream into higher paying manufacturing, and increase export share at the expense of Indian companies (Drèze & Sen, 2013).

More comprehensive and authoritative evidence on sources of growth in GDP and employment is provided in several policy reports, such as the World Economic Forum's *Global Competitiveness Report 2013-2014* and World Bank's *Doing Business 2014*. Both reports paint a depressing picture of India's economy hobbled by institutional constraints and mal-governance. In terms of global competitiveness (World Economic Forum, 2014: Table 3), India ranks 60 out of 148 countries and is behind numerous other developing East Asian countries, including Singapore (2), Taiwan (12), Malaysia (24), China (29), Thailand (37), Indonesia (38), and Philippines (59). In terms of ease of doing business (World Bank 2014, Table 1.1), India ranks 134 out of 190. The anomaly of this poor performance on competitiveness and business creation is that when Indian people

emigrate to better governed and more market-friendly countries they achieve impressive success in entrepreneurship, occupational attainment, and family income.

Job creation is only another name for what economists call labor demand and economic theory teaches that the strength of labor demand is a direct function of the strength of product demand. Thus, adopt measures that increase Indian companies' product demand and their labor demand is certain to follow, albeit moderated by productivity growth. The message of this insight for the labor law reform debate in India is: put strategic emphasis where it counts the most, which is not in labor markets per se but on impediments to growth in product markets.

**Put strategic emphasis where it counts the most, which is not in labor markets per se but on impediments to growth in product markets.**

Two pieces of evidence support this proposition. First, the *Global Competitiveness Report* divides countries into five stages of economic development, starting at the low end with Factor Driven, in the middle with Efficiency Driven, and at the top with Innovation Driven. The report also notes that the key drivers of growth differ across stages of development; for example the best way for a Factor Driven country such as Cambodia to improve competitiveness is not necessarily the best way for an Innovation-Driven country such as Germany.

The report identifies twelve 'pillars of competitiveness' and ranks the most important for each development stage. The report places India in the low Factor Driven stage. At this stage, the report identifies four pillars as critical: Institutions, Infrastructure, Macroeconomic Environment, and Health and Education. If ranked only on these four competitiveness pillars, India falls from an overall position of 60 to 96. In other words, on the critical 'must do' ingredients for growth India is actually in a considerably worse position than suggested by its overall competitiveness ranking.

Labor Market Efficiency is also one of the twelve pillars in the competitiveness ranking. However, it is rated as a critical success ingredient only when countries get to the intermediate Efficiency Driven stage – which India has not reached. Further, with respect to labor market efficiency, and five other pillars considered critical for countries at the intermediate stage, India's ranking actually rises from 60 to 42. Hence, the evidence is fully consistent with the conclusion earlier reached by Venkata Ratman (2011): excessive and overly rigid labor regulation is *a* problem for India but not *the* problem.

Additional insight on why labor market over-regulation is not the strategic factor with respect to India's growth and job creation conundrum comes from reading the report's discussion of the first of the twelve pillars, Institutions. It states (World Economic Forum, 2014: 4-5),

"The institutional environment is determined by the legal and administrative

framework within which individuals, firms and government interact to generate wealth...[However,] the role of institutions goes beyond the legal framework. Government attitudes toward markets and freedoms and the efficiency of its operations are also very important: excessive bureaucracy and red tape, overregulation, corruption, dishonesty in dealing with public contracts, lack of transparency and trustworthiness, inability to provide appropriate services for the business sector, and political dependence of the judicial system impose significant economic costs to business and slow the process of economic development”.

This quotation highlights fundamental constraints on job creation in India because they obstruct the long-run productivity and competitiveness of the nation’s employers (more below). A debate on labor law reform, therefore, must be broadly framed to include these types of obstacles in product markets. Shortening the purchase process for a mobile phone from seven transactions to one is a concrete example.

The second piece of evidence comes from the report *IFC Jobs Study* by the International Finance Corporation (2014), a subsidiary of the World Bank. The report develops a conceptual framework for thinking about the factors that stimulate and impede job growth. The framework begins with the labor market and the forces shaping labor demand and labor supply. However, the report also concludes that a labor market focus by itself is greatly incomplete. Illustratively, the report analyzes responses from manag-

ers at over 45,000 enterprises in 106 developing countries to the question: “Which of the following elements [15 items in a list] of the business environment, if any, currently represents the biggest obstacle faced by this establishment?” Respondents listed the following items as the top seven: Access to finance, Access to electricity, Informality, Tax rate, Political instability, Inadequate educated workforce, and Corruption. Labor regulation was #14 on the list and was cited by only 3 percent of respondents.

What is the connection between this discussion and the Webbs? One can plausibly argue it reveals the fatal contradiction in their theory of political economy. The Webbs correctly identify in their industrial relations face that surplus labor and unemployment are the most serious causes of poverty, substandard labor conditions, and unequal bargaining power. However, they also propose in their Fabian Socialism face a growth model which creates these conditions by stifling entrepreneurship and capital investment. In fairness, when the Webbs formed their opinions on capitalism vs. socialism the record of capitalism had a number of serious blotches, including periods of deep economic crisis and mass unemployment. Their conversion to socialism was thus partly born of skepticism that capitalism could ever produce reasonably sustained and balanced growth. The most recent world financial crisis suggests their concerns are not to be cavalierly dismissed. Nonetheless, the record of the last sixty years – with the considerable help of economist J.M. Keynes and government demand management – suggests

the Webbs picked the wrong horse in the growth and prosperity race. Their policy program of slowly restricting and narrowing the economic space for market forces and entrepreneurial action appears, therefore, ill-advised and harmful to the interests of the working class which, paradoxically, they sought to promote. Unfortunately, on achieving independence India also bet on the socialist horse and seven decades later the pernicious effects in stifled product market performance are still reverberating into lackluster labor market performance.

### **Regulation & Performance of Labor Markets.**

The message of the previous section is that all of India's labor laws and regulations can be shredded and the positive effect on economic growth is likely second-order. But, at least in industrial relations, this scenario is not countenanced even if it were politically feasible. The reason is that industrial relations has from its beginning days maintained that capitalism functions best when labor law and social insurance are used to stabilize, balance, professionalize, and humanize labor markets and workplaces (Budd, 2004; Kaufman, 2004).

Diagrammatically, IR theory predicts the relationship between labor market regulation and economic performance is an inverted U (regulation on the horizontal axis from 0% to 100% and GDP/job growth on the vertical axis) so that optimal labor law is not zero but an interior point somewhere in the moderate middle (recalling IR = the 'middle way'). One

notes that proponents of neo-liberal free market economics, such as Professor Epstein, disagree with industrial relations proponents on this critical point. Epstein (2012:203) advances a close-to-zero position, stating, "Why not try competition across the board – which would lead to repeal of virtually every labor law that regulates wages and terms of employment, except perhaps with respect to health and safety?"

The IR answer to his 'why not?' question comes from the Webbs, Commons, Gandhi, and other proponents of a human conception of labor (Kaufman 2010, 2012a). That is, when labor is treated as a commodity in unprotected external and internal labor markets the results are likely to be closer to the predictions of Karl Marx than Milton Friedman. Reasons are because productivity sinks (from low morale, trust and cooperation), firms skimp on investments in human capital and human resource management, costs escalate from high turnover, conflict, and shirking, and workers look to militant unions and socialism for protection. Note may be made here that in this regard the IR argument for labor law is paradigmatically different from the standard neoclassical model. In the latter, a competitive labor market is the ideal and labor law is sanctioned only in the case of irremediable market failures; in the former, a competitive labor market is far from ideal as a basis for a high-performance employment relationship and labor law is required to create order and stability (Kaufman, 2010; 2012a). Thus, from an IR perspective, Fabian Socialism does not provide the optimal amount of labor regulation (to the

right of the inverted U) but neither does free market neo-liberalism (to the left of the inverted U).

**Little doubt exists that India needs a substantial overhaul of its labor law regime.**

Little doubt exists that India needs a substantial overhaul of its labor law regime. The basic framework was created in the late 1940s-early 1950s, but with substantial roots in British colonial statutes going back to the 1920s. Maintaining industrial peace was then the central goal, partly a reflection of British imperial interests but also the Gandhian emphasis on social harmony (Kennedy, 1965; Sundar, 2010). Not even the most presciently designed labor law system, however, can remain a good fit in the 2010s when designed more than a half-century earlier for a largely rural, hand-craft, and informal economy. Of course, Indian labor law has not been completely static over the decades and economic liberalization and globalization of product markets have increased the pressure for change. Also, labor law reform has been the subject of numerous commissions, reports, political speeches, and proposals to Parliament (Venkata Ratnam, 2004; Shah, 2013). To the frustration of actors in all parts of the IR system, however, direct government action has been exceedingly slow, particularly at the national level.

Where change in labor regulation has occurred, the movement is sometimes in the wrong direction. For example, the

labor law provision which critics cite as the impediment to growth (Das, 2006; Datta & Sil, 2007; Krueger, 2013) – the ban in the Industrial Disputes Act (1947) on terminating workers and closing establishments – has been revised over the years but by *lowering* the employment threshold so it covers not only large firms but numerous small-to-medium sized firms (firms with more than 100 employees). Even people committed to fully protecting workers' rights can see that this rule – coupled with equally restrictive business insolvency rules – imposes potentially severe financial risks and penalties on firms in a market system with fluctuating sales due to product life cycles, business cycles, and seasonal customer orders. Further, this rule undermines competitiveness and economic development by incenting investors and entrepreneurs to keep firm size below the 100 person floor, thus sacrificing economies of scale and modern production technology and exacerbating industrial dualism and a stunted manufacturing sector (Debroy, 2005; Kruger, 2013; Kumar, 2014). Companies also evade the rule by hiring more contract workers and closing down facilities through the subterfuge of a labor dispute lock-out.

Looking at the Indian labor law regime through the lens of the Webbs' industrial relations face, two structural problems look most important to reform. Recall, as context, the Webbs seek to promote social efficiency and justice by using legal enactment and trade unions to push-up on the lower end of the industrial pyramid and push-down on the top end. The first structural reform, there-

**The main corpus of Indian labor law applies to only about 7 percent of the labor force, limited mostly to people in the organized sector.**

fore, is of the 'push-up' nature, achieved by extending the basic protections of labor law to a much larger part of the workforce. This task is difficult because 60 percent of the Indian workforce is still in the agricultural sector and another large share are wage workers or self-employed in the informal sector (Hill, 2009; Venkatta Ratnam & Verma, 2010). But, in another reflection of extreme economic dualism, the main corpus of Indian labor law applies to only about 7 percent of the labor force, limited mostly to people in the organized sector (Shah, 2013). In the Indian context, 'organized sector' includes all public sector organizations and private sector non-agricultural enterprises with 10 or more employees.

The Webbs advocate that a common rule be established across all labor markets – including the market for day laborers, contract workers, and self-employed – which provides minimum wages, conditions, and treatment consonant with social costs and human rights. Nine out of ten people in the Indian workforce do not have this minimum guarantee and several hundred million live in abject poverty (Hill, 2009). Hence, the first-prong of labor law reform is to broaden the base of coverage. An example in this spirit, defects in implementation and administration notwithstanding (Shankar & Gaiha, 2013), is the Ma-

hatma Gandhi National Rural Employment Guarantee Act (MGNREGA) – a law passed in 2005 which guarantees 100 days of wage employment to rural households if adult members volunteer for unskilled manual labor on community projects. Also illustrative are various income supplement devices, such as for widows, disabled, and retired people, under the National Social Assistance Program (1995), although it so far provides benefits to only 21 million people (Subrahmanya, 2013).

**The first-prong of labor law reform is to broaden the base of coverage.**

The Webbs also counsel using legal enactment to push-down on the top of the industrial pyramid on the argument that a significant part of the high earnings of the affluent elite is economic rent siphoned from society through monopoly market barriers, government-created privileges, and closed family and social networks. Part of the success of the Indian economy over the last two decades is that it has created a new middle class, numbering approximately 50 million or 5 percent of the population. However, it has also spawned a tiny elite of super-rich whose share of the country's wealth has skyrocketed from 1.8 percent to 26 percent (Peeples, 2014). Some of the super-high income is a much deserved return to entrepreneurship and capital investment; however, another portion is from gaming the system. As part of liberalization, India also substantially reduced the progressivity of income tax

rates and eliminated an estate tax. Labor law (broadly defined), therefore, needs to counter this trend toward rent-seeking and inequality. One avenue is social initiatives to open-up access to high income parts of the job distribution, such as greater educational opportunities for society's poor and disadvantaged and greater legal enforcement of hiring, promotion and pay on the basis of merit rather than connection and caste (Bhandari, 2014). The other avenue is to impose higher effective tax rates on family income through base-broadening and better enforcement while shutting-off egregious sources of rent-skimming, such as the too-often corrupt process of awarding public contracts.

Finally, although nearly all commentators say touching trade union law is politically impossible, a Webbian perspective suggests that here too significant reform is needed. Currently trade unions represent perhaps as few as 3 percent of the workforce (Sundar, 2010), mostly in the small organized sector and often in public sector employments, and exact a considerable efficiency cost through restrictive employment practices, political infighting, and adversarial relations. Labor law reform should take politics and conflict out of union recognition and collective bargaining by institutionalizing recognition and bargaining procedures (Venkatta Ratnam, 2004); the same procedures would help shift trade unions from an entrenched protector of a narrow-based labor aristocracy to a broader-based but less adversarial and politicized workers' representative.

## Effective Implementation & Good Governance

Liberalization in the early 1990s opened-up the opportunities and incentives needed to fuel a growth surge but, as noted in the introduction, the surge may have faded. Observers can pick-out a variety of structural reforms, including labor reform, which will help put stronger wind into India's economic sails. None of these reforms are likely to make much difference, however, if not well implemented, administered, and governed. Here seems to emerge the critical weak spot in India's future and thus the key point for strategic attack (Nilekani, 2009; Debroy, Bhandari, 2013; World Economic Forum, 2014) Das (2006:1) remarks about India's growth surge, "what is most remarkable is that rather than rising with the help of the state, India is in many ways rising despite the state". He adds, "Although Indians blame ideology (and sometimes democracy) for their failings, the truth is that a mundane inability to implement policy – reflecting a bias for thought against action – may have been even more damaging" (ibid: 2). The same diagnosis is made by Nandan Nilekani (2009:457), founder of one of India's IT success stories, Infosys Technologies Ltd. "Implementation, sadly, has long been India's weak spot".

**Indian workforce is the most highly protected in East Asia.**

India currently has more than 45 national-level labor laws and five times that many at the state level (Debroy & Kaushek, 2005), making the Indian

workforce the most highly protected in East Asia (Basu, Fields & Debgupta, 2000). The reality, however, is starkly different. Due to substantial dualism, about 10 percent of the workforce enjoys too much labor protection while the other 90 percent enjoys too little. However, many Indians feel cynical and frustrated about the government's ability to redress this imbalance (Debroy & Bhandari, 2013; Transparency International, 2014), albeit with a bounce in hope that the new Modi government can do better.

Implementation and governance are separate but related dimensions of institutional performance. Implementation occurs after a labor law is passed; for example, firms need to make sure they are paying at least a minimum wage and government must monitor and enforce compliance. Governance is faithfully and efficiently executing the law and keeping it free of corruption. By some accounts, India currently has the worst-performing bureaucracy in East Asia and the nation ranks 94 on perceived corruption (Political & Economic Risk Consultancy Ltd, 2013; Transparency International, 2014). This nation-state problem is reflected in lax labor law implementation and corrupt governance. For example, labor inspectors are bribed, firms keep double sets of accounting and payroll records, union officers take kick-backs, and government program administrators embezzle funds. It is estimated that only 15 percent of the government's anti-poverty funds reached the poor in the mid-2000s ("Corruption in India, Cause of Instability & Inequalities," [poverties.org/corruption-in-india](http://poverties.org/corruption-in-india), 2014)

and the annual funds diverted through corruption are one-third larger than total government expenditure on health care ("Corruption – An Epidemic of Epic Scale in India," *Huffington Post India*, May 5, 2014).

The point to be emphasized, therefore, is that enacting new labor laws and modifying existing ones is only part of the labor law reform battle. Attention must also be given to the unglamorous but critical aspect of implementation. This insight is hardly new. American IR founder John Commons noted (Commons & Andrews, 1936: 448), "More important than the hasty enactment of additional laws is the adoption of methods of administration that will enforce them. It is easy for politicians or reformers or trade union officials to boast of new laws which they have secured for labor, and it is just as easy to overlook details or appropriations or competent officials." Translated into the inverse U-shaped diagram of optimal labor regulation (earlier cited), this consideration makes the theory more complicated because it is not only an issue of too much or too little regulation but, perhaps more importantly, better regulation.

The Webbs were quite mindful of the importance of efficient and honest labor regulation and, indeed, as earlier noted they founded the LSE in part to train high-class managers and administrators for the new socialist planned economy. The Webbs were optimistic for they thought England possessed one of the finest government bureaucracies in the world (Webb & Webb, 1920: 319). As it later proved, the Webbs were too optimistic on the possi-



bilities of socialist administration and here is another fatal flaw in their political economy. Commons (1921) judged the Webbs woefully naïve about the possibilities of administering a socialist state and concluded such a system was an impossibility in the USA because the American people are “administratively incompetent” (Commons, 1934: 846).

When the Webbs visited India in 1911, they were impressed with the quality of governance exhibited by Indians recruited into the Indian Civil Service, although on the voyage home Sidney Webb was moved to say, “Three months’ acquaintance has greatly increased our estimate of the Indians, and greatly lessened our admiration for, and our trust in, this Government of officials” (Jayal, 1987: 209). In rendering this negative verdict, however, Webb noted that “we have found the British officials more inaccurate and more disingenuous than the Indians” (ibid: 119). Braibanti (1963) claims the Indian government administration was among the dozen best performers in the 1950s; other observers, however, questioned at the time whether Nehru’s idealism and faith in people were matched by the administrative capacity of the Indian state and indicate that corruption was growing around him (the Gorwala report of 1951, cited in Akbar, 1990). These fears turned out to be justified and India has traveled a six decade path toward less efficient and honest administration. The USA featured rampant corruption and mal-administration in government in the 19<sup>th</sup> century and one of the keys to its successful development in the 20<sup>th</sup> century was reforming a diseased system from within. Here, it seems,

is a similar institutional challenge for India and of which labor reform is a part.

## Conclusion

The Webbs’ writings present a mixed picture with respect to Indian economic development and industrial relations policies. The industrial relations part continues to provide sound principles, such as a national minimum set at the social cost of labor. The Fabian Socialism part of their writings, however, has proved a recipe for sclerotic growth. This paper tried to untangle these diverse threads and work-out the implications for restructuring Indian labor law. Partly this exercise is useful because it stimulates thinking about the industrial relations field and, in particular, to what extent it has general principles and concepts useful for framing the reform debate and guiding it to a consensus program. Also, the debate on labor reform in India seems to follow along a fairly well-worn groove of analysis so perhaps bringing a different perspective to the matter à la the Webbs is useful for stirring new thinking and dialogue.

**India is long over-due for substantial modernization and rationalization of its labor law regime.**

India is long over-due for substantial modernization and rationalization of its labor law regime; a large cross-section of Indian people recognize this imperative; many books, papers and reports with detailed recommendations have been written on the subject; and yet frustratingly little happens. Possibly the Webbs

and the Fabian tradition make a contribution of a different kind for people who want change but are discouraged. The Fabian founders chose to name the organization after Roman emperor Fabius Maximus, renowned for his patience before launching an attack on the enemy. Even if the socialism part of the Fabian legacy is not helpful for the Indian IR field and labor law reform project, certainly helpful in a messy democracy is the patience and perseverance part.

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**By Invitation**

## **Rethinking Labor Law Reforms**

**Arun Maira**

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*Indian labor laws must be improved. The improvements required must emerge from a dialogue between representatives of employees and employers. The failure to make any significant improvements in the laws so far, in spite of demands for over twenty years from both employers and unions, suggests that the processes used so far to try to change the laws have not been able to produce the required outcome. The paper also outlines the India Backbone Implementation Network, a Planning Commission initiative, conceived along with the 12<sup>th</sup> Five Year Plan by the Steering Group for Manufacturing.*

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### **Introduction**

“If you don’t know where you are going, you will end up somewhere else”, warned Casey Stengel, a famous baseball player. India needs to create more jobs. For that, it needs to build a competitive manufacturing sector. The drumbeat of (mostly right-wing, free market) economists and employers asserting that India must change its labor laws to permit easier firing of workers is misdirecting the country from its goals.

Do we want a sustainably strong manufacturing sector, or do we merely want to change our labor laws? We must stay focused on our goals of a competitive manufacturing sector and more jobs and not get distracted by a rather shallow presumption that easier firing of workers will lead to growth of competitive manufacturing enterprises. Let us understand the relationship between these two objectives: one supposedly the means to the other.

At the outset, it must be admitted that change in Indian labor laws is overdue. Many are very old and must be up-dated to suit present conditions. There are too many laws and regulations, sometimes contradicting each other. And the laws

are not implemented properly, perhaps because many cannot be implemented in practice, or because the government machinery to implement them is inadequate. Not only are employers demanding improvements in labor laws, unions are too. We will return to the questions of what the thrust of changes should be and how to bring them about. First, let us examine what is required to grow India's manufacturing sector to create more employment.

### **Constraints on Growth**

Labor laws are not the principal constraint, or even amongst the top three or four constraints on the growth of India's manufacturing sector. Many surveys in the past few years, conducted by several industry associations, consulting organizations, and government commissions have revealed this. The principal constraint, for both large and small enterprises, is the quality of the business regulatory environment. India ranks towards the bottom of the World Bank's rankings of countries for ease of doing business and its position has been slipping. Implementation of business regulations is more corrupt, confused, and tardy in India than in other countries. This deters investments from abroad and from Indian investors too. It especially saps the productivity of small enterprises where the owner has to personally respond to the regulators when he is also the manager of the business to which he must give more attention. Since small enterprises are the largest creators of employment in the manufacturing sector (and account for a large share of its produc-

tion and exports too), political and bureaucratic capacities (which are constrained too) should be applied to address this number one constraint on the productivity and growth of manufacturing enterprises, and not be distracted towards lower order constraints such as the ostensible difficulties in firing workers.

The second, almost equally large impediment for the productivity and competitiveness of manufacturing enterprises in India is inadequate physical infrastructure for transportation and power supply. Indian IT enterprises are not handicapped by these shortcomings and so many have grown to be world-class competitors. However, manufacturing enterprises have to convert stuff and move stuff, and this requires energy and physical transportation. They are severely handicapped by the poor infrastructure: it adds to costs and delays and reduces their international competitiveness.

The third constraint is the availability of skilled manpower. Since the country's objective is to employ more people in manufacturing, and since skilled persons can also improve the productivity and competitiveness of enterprises they work in, this constraint must be relieved very vigorously. A national skills mission has been launched with impressive targets. It needs much more participation of employers for development of requisite skills: more about this later.

Large enterprises and MSMEs have different constraints. In fact, one of the greatest constraints on the growth of small enterprises in India is the availabil-

ity and cost of credit, whereas large enterprises do not have a problem obtaining loans from banks and at lower rates than MSMEs (though the cost may be higher than in other countries). The distinction between the needs of large enterprises and SMEs must be always remembered while devising strategies to grow India's manufacturing sector. Too much of attention of policy-makers is given to the views of large enterprises, who get the attention of policy-makers through powerful business associations and directly too, rather than the perspectives of SMEs.

**Some economists have pointed out that India's manufacturing sector has a 'missing middle'.**

MSMEs and larger enterprises have different issues with labor laws. Many MSMEs are in the informal sector. Many of those in the formal sector fall below the threshold limits of industrial relations' laws. They do not need more freedom to legally hire and fire: their contracts with employees are informal and flexible. It is the large enterprises who say they are impeded by laws that make it difficult for them, legally, to fire their employees. They have got around the restrictions by employing large numbers of contract workers, always at lower costs than permanent employees. Therefore, in practice, the labor laws have not come in the way of their hiring more people. So, if these enterprises have not grown and have not hired even more people, the constraint has not been the labor laws. Other constraints, mentioned before, have

restrained their competitiveness and growth.

Some economists have pointed out that India's manufacturing sector has a 'missing middle'. There are too many MSMEs, and some large companies, and too few in the middle. They point to a barrier that MSMEs do not wish to cross to become bigger. According to some of these economists, the barrier is the onerous restrictions on firing people once the enterprises become larger. However, as suggested here, this may not be as much of a restriction as it is made out to be. Other factors impede growth even more.

**Such an architecture has been mooted by the NMCC and MSME ministry. This would give incentives to MSMEs for a fixed number of years.**

The MSMEs themselves point out that the architecture of incentives to MSMEs induces them to stay small. Incentives are given to enterprises below a threshold size. Therefore, when they cross that threshold, they lose the support. So they would rather multiply numbers of small units, each of them getting the incentives, than grow a large one and lose them. An alternative architecture of schemes to assist MSMEs is required if the objective is to help them grow stronger and larger. Such an architecture has been mooted by the NMCC and MSME ministry. This would give incentives to MSMEs for a fixed number of years, during which they must make all efforts to improve their productivity and grow,

because they will lose the incentives thereafter. This will motivate small enterprises to learn and improve faster and cross into the zone of the presently 'missing middle'.

The strategy to grow Indian manufacturing enterprises must be to improve their competitiveness, rather than to provide them with protection against larger and stronger competitors. To improve their competitiveness, enterprises must be faster learning than others. The only resource in a manufacturing enterprise that has the ability to learn and improve its capability and productivity are its employees. The capability of all other resources—machines, buildings, materials—depreciates with time, inevitably. Far-sighted employers understand that employees are the only 'appreciating assets' of a manufacturing enterprise. Motivated and enabled employees can also improve the capability of the enterprise's manufacturing processes and the productivity of its machines.

### **People, Skills, Jobs**

India has the world's largest pool of young persons seeking jobs. Human beings are a trainable resource. Manufacturing enterprises in India, wanting to compete with enterprises in other countries should design their manufacturing systems to use more human beings and less capital. A manufacturing enterprise in India that has the ability to improve employee skills can count on a continuing supply of trainable people, and thus have a sustainable competitive advantage over enterprises elsewhere.

The Planning Commission asked Bain and Company to do an independent, objective evaluation of the co-relation of competitiveness of Indian manufacturing enterprises and their industrial relations' practices. Bain connected the economic performance (growth, profits) amongst Indian enterprises in several manufacturing sectors with their orientation towards employees. The study confirmed that enterprises in which employees were treated as 'appreciating assets' produced better economic results over the long run than their competitors who took a more short-term, 'cost' oriented view of employees.

**Enterprises in which employees were treated as 'appreciating assets' produced better economic results over the long run than their competitors.**

Economists who wish India well would want manufacturers in India to employ more people and pay them better too. More employment and more earnings will give a boost to economic growth. However, this win-win solution is not being realized because owners of enterprises are facing problems with employees. Employees do not have the requisite skills, they say. When employees are dissatisfied they can create industrial relations problems. Therefore the general response of employers, with a few notable exceptions, is either, use machines instead of people if they can afford them (the cost of capital is high in India, and SMEs cannot raise it easily) or, hire more temporary/contract workers, who do not



yet have the ability to organize themselves (though they are beginning to), and are easier to fire legally.

Such tactical manoeuvres are diametrically opposed to the strategy to make India a globally competitive manufacturing hub. There is little incentive to train temporary/contract workers, so skill development is constrained when India is crying for more skill development. Moreover, contract workers are paid much less than others, leading to industrial relations disputes. Thus employers' relationships with people in their enterprises are becoming fraught. With this trend, manufacturing may be in a downward spiral, at a time when, for improvement in competitiveness of Indian manufacturing enterprises, people (and more of them) must be at the heart of enterprises' strategies.

To build a globally competitive manufacturing sector, India must expand the scope of its vocational skills program. More technically skilled workers are required of course. Even more than that perhaps, employers in the garments and other labor-intensive sectors say they need good supervisors who can manage work and people well. Productivity improvements and skill development happen on the shop floor and good supervisors are critical for these.

Above all, the country needs very good systems' and people managers who will improve competitiveness of manufacturing enterprises by managing the interplay of the many systems that interact to create faster learning enterprises.

These systems include material flows, information flows, processes for quality, productivity improvement, and very importantly, the human side of the enterprise.

**Manufacturing management must become an attractive vocation for India's best engineers.**

India's massive vocational skills program must address the need for better manufacturing managers too. 'Manufacturing management' must become an attractive vocation for India's best engineers, whereas they have been gravitating to the IT industry, building its international competitiveness, at the cost of India's manufacturing sector. Churning out more skilled workers can be a socio-economic fix that will back-fire if these skilled workers do not find jobs. To create jobs, the competitiveness of Indian manufacturing enterprises must be rapidly improved. To improve the enterprises' competitiveness, better manufacturing managers with skills to nurture human assets and manage complex systems will be required in much larger numbers than what India is generating at present.

It is not surprising that countries such as Germany, Japan, and Sweden, which have maintained (and even increased) the competitiveness of their manufacturing sectors, even as wages increased and their currencies became stronger, have a long term orientation towards human assets. In these countries, there is much greater commitment to the continuity of

employees in service. To them, 'flexibility' in employment is the ability of employees, supported by employers to learn new capabilities, rather than the flexibility of employers to quickly dispense with employees' services.

For India to reach its goal, of creating 100 million additional jobs in manufacturing, which it must, owners and managers of manufacturing enterprises in India must treat human beings as their core asset and not a problem to be avoided.

### **What about Labor Laws?**

We return now to the question of labor law reform. Labor laws must be examined by keeping in mind the goal we want to achieve. Which is to grow India's manufacturing sector and employment in it. Whatever reforms are to be made in the labor laws must be assessed with this goal in mind and must support the strategy required to reach it.

**Relations between employers and employees must become co-operative, not confrontational.**

The strategy has to be to build rapid learning enterprises with employees at their heart. Relations between employers and employees must become co-operative, not confrontational. Together, enlightened employers and responsible unions must establish processes that will build trust within enterprises. Together, they can determine what changes in labor laws are required. Industrial relations

will be damaged if Government forces any changes in labor laws that are not founded on an understanding between unions and employers about what changes are required to ensure fairness to employees and enable faster learning and improvement of competitiveness in enterprises. It is not politically feasible for Government to change the laws without the support of both unions and employers. The lesson from France is instructive. The productivity and growth of France's manufacturing enterprises have been hampered by rigid labor laws. Last year, the French government changed the laws without too much contention. The minister-in-charge explained that the Government was able to make the changes because the unions and employers, following the German example of cooperation, came to an agreement about the changes required which they put to the Government to implement.

The World Bank's annual World Development Report, 2013 focused on 'Jobs'. The need to create good quality jobs has become a major challenge for policy-makers in many countries, including developed ones where youth unemployment is over 25%. The Report points towards approaches that policy-makers should adopt to create jobs. It says: "A careful review of labor policies in developing countries yields a mixed picture. Most studies find that impacts are modest—certainly more modest than the intensity of the debate would suggest. Across firm sizes and country levels of development, labor policies and regulations are not among the top three constraints that formal private enterprises face."

“There is no consensus on what the content of labor policies should be. Views are polarized, reflecting differences in fundamental beliefs. To some, labor market regulations and collective bargaining are sources of inefficiency that reduce output and employment, while protecting insiders at the expense of everyone else.....To others, these policies provide necessary protection to workers against the power of employers and the vagaries of the market.”

The Report says, “The challenge is to set labor policies on a plateau—a range where regulations and institutions can at least partially address labor market imperfections without reducing efficiency.”

The ‘plateau’ is a coherent combination of regulations, processes, and orientations amongst the stakeholders—employers, workers and their representatives, and regulators. The plateau (or the edge) between too rigid regulations and too little regulation, and between sclerotic institutions and no legitimate institutions, has to be found in each country, within each region, and even within enterprises. Within the same country and the same national labor laws, some regions and some enterprises have more harmonious human relations and thereby more competitive enterprises.

The discovery of the plateau requires deliberations amongst the stakeholders at regional, state, and enterprise levels. Changes in labor laws may be necessary, and in India some changes are required. However, the discovery of what these

changes will emerge from the stakeholder engagements that will address the composite of processes, orientations, and regulations. The changes required in laws cannot and must not be debated in isolation of these grounded, multi-stakeholder engagements. Reforms in processes are critical; not merely reforms in laws.

### Improving Trust & Co-operation

Indian labor laws must be improved, as mentioned before. However, the improvements required must emerge from a dialogue between representatives of employees and employers. We must find our own ‘plateau’. The failure to make any significant improvements in the laws so far, in spite of demands for over twenty years, from both employers and unions, that something should be done suggests that the processes used so far to try to change the laws have not been able to produce the outcome required.

**The tripartite Government-led process (the Indian Labor Conference) has not been able to overcome the trust deficit between unions and employers.**

The India Backbone Implementation Network (a Planning Commission supported initiative, about which more will be said later) has examined several processes that have been applied so far. The examination revealed that the tripartite Government-led process (the Indian Labor Conference) has not been able to overcome the trust deficit between unions and employers. Agreements supposedly

reached at its meetings are not followed through. On the other hand, bi-lateral processes, such as those facilitated by the ILO, do enable better dialogue. But they are not able to convert discussions into enforceable decisions because Government seems a reluctant participant in them.

The India Backbone Implementation Network was conceived along with the 12<sup>th</sup> Five Year Plan by the Steering Group for Manufacturing. The Group had agreed, at the outset, that a plan to create 100 million additional jobs in the manufacturing sector, by improving the competitiveness of enterprises and accelerating the growth of the sector (which has been languishing at below 16% of GDP) will not be sufficient. The root causes for the country's failure to implement its previous plans to grow manufacturing must be analyzed and addressed too. The root causes for slow implementation, it was found, were (1) unresolved contentions amongst stakeholders on a variety of issues (land requirements, environment clearances, industrial relations, etc) and (2) confusion in implementation of solutions even when there was agreement. For these reasons, infrastructure is not being built fast enough, projects are stuck, skills are not being developed adequately, etc.

The Planning Commission set about finding ways to convert contention into collaboration, confusion into coordination, and thereby convert intentions into implementation. Processes and techniques for this were searched for in countries that have good track records for building

sustainably strong manufacturing sectors by cooperation amongst stakeholders. The India Backbone Implementation Network (IbIn) was created to promote the use of such approaches in India to accelerate the growth of employment in India's manufacturing sector.

IbIn has brought national unions and employers' federations together to consider some fundamental questions for cooperation:

- Do 'we' seriously want to improve industrial relations?
- What is required to be done by us 'together' to enable improvement of industrial relations?
- Are we willing to try a better method to achieve our objective?

Several meetings have been held amongst the stakeholders. There is agreement that both unions and employers want better industrial relations, and for this the trust deficit between them must be reduced. This will require a greater willingness to listen to each other and co-create solutions. Both sides have agreed that they must follow a systematic 'IbIn' process which will move along two tracks:

1. Resolve issues that have not been resolved so far, systematically, with a better process (For the record here: the principal, urgent issue in large enterprises is contract labor, and for MSMEs it is social security. The right of employees to form unions is the other important issue.)

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2. Pay explicit attention to the quality of the process of dialogue, and strengthen it to increase trust and create a stronger platform for the stakeholders' dialogue for solutions

The second objective, the building of a strong platform for purposeful dialogue, is essential to achieve the first objective. A strong platform will produce several benefits:

- The root causes of poor productivity and competitiveness of manufacturing enterprises will be analyzed, and can then be addressed
- Better practices for addressing these root causes and improving industrial relations will be discerned and disseminated
- There will be agreement on what changes are required in the content and in the implementation of labor

laws to improve competitiveness of manufacturing enterprises, grow the manufacturing sector, and increase employment

An understanding of what changes should be made in the labor laws will be an outcome of a process of cooperation between unions and employers' federation. Attempts to force a change in labor laws to enable easier firing of employees, which is being demanded by some employers and some economists, will decrease trust which is insufficient amongst employees and employers, when there is need to increase trust.

A stronger platform for dialogue is required. Using this platform the stakeholders in India can discover the 'plateau'—the combination of practices, processes, and laws—that the World Bank report on Jobs has analyzed as the policy solution for accelerating growth of employment in manufacturing in all countries.

**By Invitation**

## **Transition to Labor Law Reform: State-Level Initiatives & Informal Sector Labor Relations**

**Hemal Shah**

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*The 1991 economic reforms in India quadrupled growth, but kept good quality jobs stagnant. About 93 percent of the workforce is employed in the informal sector, holding back India's growth potential. If India is to realize its full growth potential, reforming the heavily regulated labor market is indispensable. However, resistance from vested interests in an inflexible market and lack of political capital in New Delhi has contributed to more than six decades of impasse. This paper accounts for interests of all stakeholders in addressing this issue. The paper identifies best practices that individual states have undertaken to simplify labor laws to ease doing business and address the lack of skilled labor. It also identifies smaller reforms to extend security coverage to informal workers.*

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### **Restrictive, Archaic, Convoluted Labor Laws**

For India to transition to a modern economy – from agriculture to industry, informal to formal sector, and shift to urbanization – she must realize her true growth potential by focusing on the creation of good quality jobs and infrastructure. One of the key enablers is the modernization of the labor market, which is regulated by extremely restrictive laws. This forces businesses to remain small, and in turn operate in the informal sector. About 450 million informal employees who make up 93 percent of the total workforce stand to benefit from reforms to labor laws and improve business productivity.

Informal or unorganized sector workers, by definition, are those employed in enterprises that use power and employ fewer than 10 people or do not use power and employ fewer than 20 people (Debroy & Bhandari, 2008). Common occupations include small farmers, fishermen, beedi packers/bonded laborers, migrant workers, contract and casual laborers (Planning Commission, 2001). Informal workers are often characterized as low-skilled,

poorly paid and seldom covered by social security provisions. This paper uses the terms 'informal' and 'unorganized' interchangeably.

**Indian labor legislation is convoluted, archaic and restrictive in nature.**

Indian labor legislation is convoluted, archaic, and restrictive in nature. About 50 Central laws overlap with 150 State regulations. The clauses of the Industrial Disputes Act (IDA) of 1947, one of the major regulations, were conceived under the British Raj. In 1976, the introduction of Chapter V-B to IDA decreed that firms employing 300+ people should seek government permission to effect lay-offs, retrenchments and closures. This was further restricted to firms with 100+ workers in 1982, making hiring or firing new workers extremely difficult even if they are inefficient (Sharma, 2006). The Trade Unions Act is as old as 1926 and Workmen's Compensation Act from 1923.

The 1970 Contract Labor Act allows firms to employ contract workers for tasks of permanent nature but the arbitrariness of the law allows the government to ban contract use if similar establishments use regular workers for that same task (Bhagwati & Panagariya, 2013). The 1948 Factories Act limits the maximum hours of work per week to 48, requires paid holiday for each 20 days of work, bans the employment of women for more than nine hours a day, among other things (Bhagwati & Panagariya, 2013).

## Adverse Effects

Stringent labor regulations affect industrial development, thereby economic growth and jobs. Firms are disincentivized from expanding and harnessing the economies of scale and forced to remain informal. The World Bank's (2013a) World Development Report focusing on labor issues directly links larger, formal sector firms to a range of positive factors. Surveying businesses in 102 countries, the report found that larger firms (with more than 100 workers) are likely to be more productive.

For instance, value added per worker in India's informal manufacturing sector is on average about one-tenth that in the formal manufacturing sector (Sharma, 2009). The World Bank report also found that larger, formal sector firms innovate more, and compete in export markets, especially in the presence of foreign competitors. They are also likely to pay higher wages and control for worker characteristics like age or education through a wage premium. However, India misses out on capitalizing on such economies of scale. For example, about 84 percent of manufacturing firms in India are micro and small firms, employing less than 49 people. A miniscule 6 percent of ("medium size") firms employ between 50 and 199 people. Only 11 percent employ over 200 people ("large size"); in China large sized firms account for 52 percent (Hasan & Jandoc, 2012).

On the other hand, economic growth in India has not brought about sufficient jobs. For instance, overall employment,

which experienced a steady annual growth of around 2 percent from 1961-90 (when average growth was about 3.5 percent) declined sharply to 1.5 percent during 1990-91. Employment further declined to around 1 percent during 1993-00, when growth rose to an average of 6 percent (World Bank, 2013b). This situation improved in 2000-2005 when India's GDP growth rate averaged at 7 percent, and employment went up by 1.6 percent (World Bank, 2013b). But as a u-turn, in 2005-2010 when growth averaged higher at 8 percent and employment dropped by 5.4 percent (World Bank, 2013b).

Even if employment increased slowly over the years, the rate of good jobs creation was going the opposite direction. While the formal sector grew slowly at 1.2 percent annually in 1983-94, this rate fell to 0.53 percent in 1994-2000 (Sharma, 2006). Overall, employment in India increased by 92.7 million during 2000-2005 but a mere 2.2 million during 2005-2010 (Mahambare & Nadkarni, 2011). Even then, the quality of jobs added to the economy was dismal. The small increase in aggregate employment of 2.2 million during the high economic growth, but low job growth period of 2005-2010 was due to a massive increase in informal or casual jobs.

Fallon & Lucas (1991) argued that employment in formal manufacturing firms would have been 17.5 percent higher in the absence of job security regulations. But not only has the share of informal workers gone up to 93 percent today, the share of informal jobs in for-

mal sector companies is also on an upward trajectory (Papola & Sahu, 2012). In fact, India has been the main driver of increase in informal employment in all of South Asia (Iyer & Vijay, 2013). The immediate reasons for a burgeoning informal economy are increased taxes and social security contribution burdens, intensity of regulations, and low quality of public sector services (Schneider, 2002).

### **Urgent Need**

**India is amongst the most difficult places to do business.**

India is amongst the most difficult places to do business. The World Bank's Doing Business index shows India falling down three places to 134th this year, the worst performing country in South Asia after Bhutan and Afghanistan. Starting a business and enforcing contracts are amongst the major problems (World Bank, 2014). The World Economic Forum's 2014 Global Competitiveness Index ranks restrictive labor regulations as among the top problems for businesses to operate in India. Addressing this could help India make the transition from a factor-driven economy to an efficiency- and innovation- driven economy (Schwab, 2013).

Growth of India's manufacturing sector record is also waning. In the 1970s, the share of manufacturing to GDP was around 12 percent. After barely rising over the years, this share fell again to 14.6 percent in 2012-2013, the lowest in 20 years. To meet the goals of the



National Manufacturing Policy (NMP) – boosting the share of manufacturing to GDP to 25 percent and adding 100 million jobs – strong labor law reforms are needed now to put India on the path to create around 110 million jobs by 2025 (Goldman Sachs, 2014). With more than 10 million Indians entering the job market annually, the stakes to reform sooner rather than later will be particularly high in the coming decade to exploit the opportunities from the demographic dividend.

**Strong labor law reforms are needed now to put India on the path to create around 110 million jobs by 2025.**

### **Current Organization of Labor Legislation**

The Centre failed to make a case for flexible labor markets due to strong trade union resistance (and political party affiliations) and problems with re-drafting amendments. To curtail this, there is a tendency on the Centre's part to pass the buck on to States (Debroy, 2012). India's labor legislation is a subject in the Concurrent List, which means that both the Centre and the State could enact laws pertaining to the relevant category. There are:

- Labor laws enacted and enforced by the Central government
- Labor laws enacted by Centre but enforced by both Central and State governments

- Labor laws enacted by the Centre but enforced by the State government
- Labor laws enacted and enforced by the various State governments which apply to respective States (Ministry of Labor and Employment, 2011).

The following items related to labor appear under the Seventh Schedule (Article 246) of the Constitution, under the Concurrent List, allowing State governments to amend some Central statutes, and also add new statutes to a certain extent:

22. Trade unions; industrial and labor disputes
23. Social security and social insurance; employment and unemployment
24. Welfare of labor including conditions of work, provident funds, employers' liability, workmen's compensation, invalidity and old age pensions and maternity benefits

This paper identifies the most ideal reform scenarios in order of importance but also rates their difficulty level.

### **Most Difficult Scenario**

While India needs a major overhaul in labor legislation, the IDA of 1947 warrants reform most urgently. Bhagwati & Panagariya (2013) highlight some of the pressing changes required that include tightening the definition of retrenchment and deferring disputes to independent authorities to deliver time-bound justice as opposed to labor courts and tribunals. Section 9A should be amended to give

the employer more flexibility to reassign workers to similar but alternative tasks at short notice should the need arise. The IDA also prohibits strikes only by public utility services without notice, but such restrictions should also be extended to other industrial establishments to discourage “wildcat strikes.” And perhaps the most crucial reform of all is to Chapter V-B that restricts laying off workers in a factory with 100 or more workers (Bhagwati & Panagariya, 2013). Besides India, Pakistan and Sri Lanka are the only countries that require approval by public administration before undertaking any dismissal (Iyer & Vijay, 2013). The Contract Labour Act and Factories Act also need to relax their caps on restrictions.

However, the Labour Ministry in New Delhi rejects any idea of reform on the pretext it would only apply to the 7 percent in the formal sector anyway. On the contrary, the discussion should be about how to bring the 93% under the system and balance flexibility and security. Furthermore, almost all major Indian political parties have a trade union wing. “This means political parties (more so in a coalition) are reluctant to legislate on labor flexibility, since this would antagonize their own trade union wings” (Debroy, 2012). For instance, in February 2012 and 2013, millions of trade union members organized a national strike (All India Bandh) to demand permanent jobs and elimination of contract labor preventing any change in status quo. However, the dismal showing of the 2014 Lok Sabha elections marked a clear defeat for the left-wing political parties – especially the bloc of commu-

nist parties whose hold was reduced to the lowest ever vote share of 4.4 percent – and a decisive victory for the centre-right Bharatiya Janata Party (BJP), making way for some reform discussion.

### **Moderately Difficult Scenario**

India is becoming more federal in nature. The number of states has been on the rise in India: from 14 states in 1957, India federalized to 29 in 2014. This is just one of the reasons to devolve more power to India’s 29 chief ministers, rather than concentrating it in New Delhi. In addition to a majority in number, it also makes sense to move labor law items completely from the Concurrent to the State list (by amending the Seventh Schedule, Article 246, of the Constitution) for several reasons:

First, the current arrangement of shared responsibility encourages inaction, non-accountability, and free-riding. On the one hand, it keeps the Centre tight-fisted and avoid rocking the boat, and on the other hand States remain complacent, contributing to the decades-long impasse.

Second, performance-driven states are punished and complacent ones rewarded. For instance, states like Andhra Pradesh, Gujarat, Karnataka, Madhya Pradesh, and Maharashtra, wish to make labor laws more flexible to allow choice and opportunities for employees. This includes flexibility in work hours, night shifts for women, or freedom to fix minimum wages. But these initiatives would require changes in legislation and have thus been shot down from the Centre (Debroy,

2011). But moving such legislation to the State list could avoid this problem.

Third, evidence suggests that States which were able to enact seemingly more “pro-worker regulations” have lost out on industrial production in general (Ministry of Finance, 2005). Study by Hasan and Jandoc (2012) shows that in labor-intensive manufacturing, states with flexible labor regulations enjoy a higher concentration of large-scale firms and smaller share of employees in small-scale firms. State-level reforms also help “to mitigate the detrimental effects that strict federal labor laws have on industrial outcomes” with regard to formal sector manufacturing units (Dougherty et al, 2013).

However, moving labor laws from Concurrent to State list will require a legislative amendment backed by the use of significant political capital. While this is difficult, it could be possible in the near future given the new Prime Minister Narendra Modi’s BJP being the first party with a majority seats since 1984 and first non-coalition since 1989. His affinity for decentralization (as former chief minister of Gujarat) increases his potential to push for decentralizing labour laws but the BJP does not yet have a majority in the Rajya Sabha. While moving these items to the State list would be best, there is no reason for states to try and reform laws that are still within their power on the Concurrent list.

### **Easier Scenario**

Even with the reform-oriented approach of the new government and their

majority in the Lok Sabha, moving labor from Concurrent to State list is not an easy task. One way around this would be to use Parliament’s power to confer enabling power to states. In other words, the Lok Sabha could push for a politically easier reform by inserting additional wording to subjects in the Concurrent list stating two things: The particular piece of Central legislation shall apply to all states that *do not amend* that law; whereas amended legislation shall apply in states that took the initiative to amend it (Panagariya, 2014). In general, changes made by states are void if “repugnant” to existing Parliamentary legislation unless the state has the President’s consent (Bakshi, 2013).

However, considering that the new government does not yet enjoy a majority in the Rajya Sabha, Parliament’s attempt to enable State power may be difficult. In this case, another approach could be seeking Presidential assent. Panagariya (2014) suggests that the “new government could facilitate this process by adopting a policy of time-bound decisions on proposals for amendments submitted by states.” For instance, he explains that government permission needed to lay off workers under IDA 1947 is rarely granted making the law restrictive. Here, a time clause could be added wherein the government has to make a decision on the layoff application within a stipulated period of time, failing which permission would be assumed as automatically granted. This could not only make labor laws relatively more flexible but also result in efficient decision-making.

The new BJP-led government in Rajasthan has recently adopted this route. The state's Cabinet cleared amendments to three labor-related Acts and is seeking Presidential assent directly, as it may be "repugnant" to existing Parliamentary legislation. The state has proposed changes to IDA so that permission for retrenchment is only required for firms employing 300+ people, as opposed to 100+ people. The state Cabinet has also introduced a three-year time limit for raising disputes; trade unions can't be registered without 30 percent worker representation, instead of the current 15 percent. Restrictions from the Contract Labor Act will apply only to companies with more than 50 workers, as opposed to the current 20; Factories Act would be applicable only to companies with 20 workers with power and 40 without power, as opposed to 10 and 20 respectively (Iyer, 2014).

### **Easiest Scenario**

While much hope is pinned on the new government, even the easier potential changes outlined would still take a while. In that interim, this paper attempts to identify the most common problems for business and workers and how State governments could undertake smaller reforms to achieve marginal progress to pave the way for bigger reforms in future. With six decades of deadlock on labor reforms, it is time to find a feasible approach by accounting for perceived short-term interests of those favoring the status quo and those demanding immediate reform.

The hope is that marginal progress now will ease the transition to bigger future reforms.

### **State Freedom & Flexibility for Employers**

Difficulties in complying with restrictive labor laws and inadequate supply of skilled labor are two of the major constraints for business (CII-KPMG, 2014). Employers with more than 100 workers are covered by the IDA and cannot fire anyone without prior consultation, notification to the public administration and workers' representation, followed by approval from both before collective dismissal (Iyer & Vijay, 2013). Only India, Pakistan, and Sri Lanka have such stringent rules. In addition, TeamLease (2009) recognises how "educated unemployment and shortage of competently skilled labour co-exist." State governments can act on some of the "controllable areas" of these problems in the interim of unleashing bigger reforms (FICCI-Bain, 2012a). Best practices emerge in areas where states have a larger ability to introduce reforms. However in this case, where states have a lesser capacity to legislate, strong, piecemeal initiatives undertaken by states can also serve as useful examples for other states (FICCI-Bain, 2012a).

**Educated unemployment and shortage of competently skilled labour co-exist.**

There is already some evidence of State initiatives that have brought about positive results. Besley and Burgess

(2004) show that states that “amended the IDA in a pro-worker direction experienced lower output, employment, investment and productivity in formal manufacturing.” A more recent study by Hasan and Jandoc (2012) concludes that Indian states with more flexible labor regulations tend to have larger-sized firms in labor-intensive industries. Debroy (2011) also identified various States – Uttar Pradesh, Andhra Pradesh, Punjab, Gujarat, Karnataka, Orissa, and Rajasthan – that took initiatives to reduce the number of inspectors for business enterprises. Gujarat has also amended the IDA to allow retrenching workers but only at a higher compensation of 45 days’ pay.

That positive state initiatives result in labor market flexibility and productivity is clear from indices produced by organizations like TeamLease or the Cato Institute, who have undertaken studies to rank State initiatives to improve labor regulations for business. The TeamLease (2009) labor ecosystem index aggregates labor demand, supply and regulation, showing Andhra Pradesh and Karnataka beating Delhi and Gujarat for the top spots on overall labor ecosystem, but several others who are improving on other variables. Cato’s 2013 Economic Freedom of the States of India index also ranks states under the category of regulation of labor and business (Debroy et al, 2013). While Gujarat and Tamil Nadu have maintained top spots since 2005 until now, states like Karnataka, Himachal Pradesh, Uttarakhand have made tremendous progress over the years, whereas Jharkhand and Madhya Pradesh

have slipped down in the same period. While this is not a definite measure, it gives a rough blueprint to assess what went right and wrong in the respective states. But most importantly, it creates competition to drive change.

### Identifying Best Practices

The Planning Commission’s state level assessment for manufacturing environment in March 2014 is a serious step in institutionalizing state initiatives in this area. It acknowledges that the first step should begin with generating awareness and motivation amongst states by comparison with other states. The next step is to highlight best practices, followed by how states can “tune up” their regulations by getting a sense of best practices in successful states (Planning Commission, 2014).

In association with Deloitte, the Planning Commission recently ranked states by the time taken and the effectiveness of the process for registration of manufacturing units under the Factories Act and other labor laws. The most popular practices that emerged were in areas like simplifying information and creating awareness, online renewals, and rationalization of inspections (Planning Commission, 2014). Mr. ArunMaira, member of the Planning Commission, argues that easing regulations for manufacturing enterprises should be in the hands of the states since almost three quarters of the regulations are state regulations (Rao, 2014). Outlined below are some examples of such state initiatives that aim

to simplify labor regulations, both to ease doing business and bolster a skilled workforce.

### **Labor Management System**

The “Mahashramm” initiative launched in 2010 by the State government of Maharashtra is an important electronic portal that enables efficient and timely services to businesses and reduces inspections. The portal provides online registration, application for licenses, exemptions, and renewals, in addition to paying salaries by cheques. Businesses can track the status of their application putting an end to delays and corruption that may arise in such cases. Filing and reconciling returns are simplified: businesses can file the 14 mandated returns in one go through one comprehensive annual report. Monthly returns are verified against bank statements and alerts are generated for non-compliance. In this manner, days taken to apply for licenses were reduced from 10 to 0.5; license renewal from 7 to 0.5; and returns filing from 15 to 0.5 (DIPP, 2014). However, businesses have to ensure that their employees are all registered on this system and have individual bank accounts (FICCI-Bain, 2012b).

### **Compliance in Special Economic Zones**

Special economic zones (SEZ) are designated areas to attract cutting edge infrastructure and foreign investment with the least possible regulations to boost economic activity. Gujarat has pioneered labor compliance in this area by the SEZ

Act of 2004 by making clear clauses for appointment and termination of labor for SEZ units. Flexibility in complying with IDA’s section V-A, V-B, V-C and V-D are offered (MSME, 2014). The SEZ Act has institutionalized the concept of ‘fixed term’ – different from contract workers – to satisfy work needed to be done for short periods (Debroy, 2011). This feature has brought about a major reduction in manpower days lost due to labor strikes. Gujarat, therefore, accounts for only 0.6 percent of India’s manpower days lost (CII-KPMG, 2014). In fact, recent research by Goldman Sachs (2014) argues that 40 million manufacturing jobs could be added to the economy if states made their labor laws as flexible as Gujarat. The state’s reform initiative brought a growth of 60 percent in manufacturing employment between 2000 and 2012 whereas West Bengal saw only a 22 percent increase (Goldman Sachs, 2014).

**40 million manufacturing jobs could be added to the economy if states made their labor laws as flexible as Gujarat.**

### **Self-certification & Inspector Rationalization**

The introduction of Single Window Act in 2002 made Andhra Pradesh the first state to introduce the concept of self-certification. This enabled firms to avoid arbitrary inspectors by submitting their muster rolls and registers along with a self-certification form showing compliance with various labor laws. However, it is the

state's thriving IT industry that goaded this practice. This is yet to be scaled up to the manufacturing sector, whereby labor laws are more in number as it falls under the jurisdiction of the Centre's Factories Act. While this initiative is laudable, improvements can be made by making inspections complaint-based or random as opposed to mandatory inspection currently. Third party agencies could also be recognized to issue compliance certificates (FICCI-Bain, 2012c).

**Third party agencies could also be recognized to issue compliance certificates.**

#### **Industry -University MoUs**

Gujarat, like a few other states, has been steering the setup of industrial training institutes (ITIs) to implement vocational training courses. But the state's government differentiates itself from ITI initiatives by other states with its campaigns to increase the participation of industry to strike a match between skills training and academia. As noted by FICCI, industrial organizations like Tata, LG, Eicher have signed MoUs with the state government's employment and training department specifying skills they require and in exchange offering placements to successful students. This has led to university-business integration. For example, Saurashtra University and Essar Group work together in designing course curriculum relevant to industry; ITI Kuberanagar works with Toyota and Eicher to make skills relevant to their business (FICCI-Bain, 2012d).

#### **State Freedom to Redesign NREGA**

Though well-intentioned, the former government's National Rural Employment Guarantee Act (NREGA) that guarantees 100 days of work to the rural poor, has unintended consequences. For India to boost growth, jobs, and productivity, it has to make a rapid transition from agriculture to manufacturing coupled with skilling programs, and thereby urbanization. Labor is four times more productive in industry and six times more in services compared to agriculture (Goldman Sachs, 2014). Government policies should incentivise this transition, but NREGA does the opposite. While rural wages are going up, slowing urbanization and productivity are together stoking inflation in India (Goldman Sachs, 2014).

**NREGA could be reformed to limit the number of rural jobs to those who strongly prefer to remain close to their households (for example, women).**

NREGA could be reformed to limit the number of rural jobs to those who strongly prefer to remain close to their households (for example, women). The government could instead channel the remaining funds to sponsor or subsidize these workers for 100 days in private sector labour-intensive industries. This would also incentivize employers to invest in their skills in that subsidized time and hire them full-time by paying wages for the rest of the 265 days or more (Kumar & Busvine, 2014). However,

NREGA is a one-size-fits-all Centrally Sponsored Scheme (CSS), where state governments contribute a share of the finances and responsible for implementation but have no say in design (Raghunandan & Aiyar, 2013). With the current government poised in favor of decentralized decision-making over CSS, the Planning Commission, with Prime Minister Modi at the helm, could extend more freedom to state governments to redesign their NREGA schemes to align more with productive jobs and urbanization.

### Social Security Reform

In the first quarter of 2014, 3,057,472 man-days were lost due to strikes and lockouts (Labor Bureau, 2014). While the formal sector is characterized by a rigid labor market, the 93% of the Indian workforce in the informal sector work under extremely flexible conditions. However, social security coverage is miniscule or non-existent. Evidence from the most unionized state of India, West Bengal, suggests that three of their largest trade unions (CITU, INTUC, AITUC) focus their work around security for workers in the informal economy (Sen, 2009). Scaling up security for informal sector workers could therefore be one of the most crucial factors in reducing the fierce resistance from trade unions. Trade unions worry about any discourse of reform equating it with dilution of their rights. This section argues for a two-pronged approach: identify and address trade union problems to the extent that it makes bargaining unnecessary and unattractive.

**The EPFO is 10-20 times more expensive than any other public or private government securities mutual fund in the world.**

### Social Security Cost-Value Mismatch

The cost and administrative burdens of India's social security schemes disincentivize employers from administering them. At the same time, employees find it unattractive to contribute to them. Benefits and contributions leave low-wage employees with only 50% of their monthly salary (Sabharwal, 2012). The EPFO is 10-20 times more expensive than any other public or private government securities mutual fund in the world (Sabharwal, 2012). In addition, its pension scheme has an unfunded hole of rupees 50,000 crore (Sabharwal, 2014). Moreover, the perceived value for money is fairly less for low-wage workers — the EPF has often been criticized for poor customer service. The ESI, on the other hand, is also blighted with poor hospital facilities and lack of staff (Sabharwal, 2012). It is also the world's only health insurance plan with a claim ratio of less than 50 percent (Sabharwal, 2014). Thus, businesses are increasingly moving to the cost-to-company approach of monetizing all benefits to include in salaries, as opposed to providing benefits over and above the gross salary.

Cost-cutting also leads to collusion between businesses and labor inspectors; unregistered firms often don't return their ex-employees contributions (Rajeev,



2009). Maharashtra's "Mahashramm" initiative mandates all businesses – in formal and informal sectors – to pay all salaries/wages by cheque. Businesses, banks, labor and network correspondents have to be all linked and financial institutions are expected to provide the linkage by extending the option of "no frills" bank accounts. This also ensures the payment of EPF to workers (FICCI-Bain, 2012b).

### **Competition to Reform**

Competition is yet another way to reform social security and improve value for money. With the extension of the National Pension System (NPS) to all Indian citizens, including from the informal sector – and the Pension Fund Regulatory and Development Authority (PFRDA) as regulator of the pension sector – employers should allow and encourage employees to opt into the scheme of their choice. The NPS, unlike the EPF, runs on a defined contribution mechanism whereby a pensioner gets back the amount proportional to his contribution, rather than a fixed return. The NPS also enjoys a higher rate of return than the 8.25% under EPF. The NPS scheme is web-enabled and removes the human interface that could invite rent-seeking, thereby inviting choice and contestability, and incentivizing EPFO to reform alongside (Asher, 2011).

### **Setting up Organizations**

State governments should look into investing and encouraging formal sector organizations modeled after private companies, like TeamLease Services, Ma

Foi, Randstad, and Manpower, in the informal sector. Besides offering human resource services, such organizations dedicate their operations towards improving their people supply chain by identifying and matching contract laborers, or temporary staff, a sensitive subject amongst the trade unions. Contract labor is often exploited in India's formal sector as short-term "informal" laborers absent social security provisions. The presence of such organizations would ensure that contract laborers get a fair wage for their services in addition to social security, on the assumption that temporary jobs are still better than no jobs.

### **Developing the Informal Sector**

Though ideal, formalization is impractical until informal workers are equipped with required skills and training to enable employers to invest in them and administer expensive social security options. Needless to mention, compliance with restrictive labor laws and poor infrastructure add to the problem. Policymakers need to think of ways to reduce the formality-informality trade off.

Costs of formalization include entry costs and operating costs (Loayza, 1997). Entry costs of doing business in India involve 12 procedures that take 27 days, costing 47 percent of income per capita with paid-in minimum capital of 125 percent - as opposed to 5 procedures in 11 days, costing 3.6 percent of income per capita, with just 10% paid-in minimum capital in the OECD (World Bank, 2014). Operating costs – complex taxes, labor regulations, property rights, contract en-

forcement, access to infrastructure – are already high. Ranking 134<sup>th</sup> out of 189 countries on the World Bank’s Doing Business index, India falls behind even her BRICS counterparts.

**Ranking 134<sup>th</sup> out of 189 countries on the World Bank’s Doing Business index, India falls behind even her BRICS counterparts.**

Costs of remaining informal include penalties and corruption, limited access to public services, missed opportunities on expansion, limited access to finance and cooperation with formal enterprises (Ishengoma & Kappel, 2006). However, the situation in India can be summed up as follows: “the opportunity costs of informality seem to be much lower than the cost of operating formally...total formality may mean closing up the business unless the business environment within which firms operate is improved” (Ishengoma & Kappel, 2006).

Instead, until costs decline, attempts should be directed at creating an assurance of sustainable livelihoods in the informal sector. For instance, states like Gujarat have been proactive in creating more choice and opportunities for farmers by amending restrictions on the Agricultural Produce Marketing Committee Act to allow them to sell their produce to wholesalers, exporters, industries and large trading companies (Shah, 2013). This would ensure a smooth transition for informal sector workers when the time is right to formalize.

### **Flexibility & Security – “Flexi-curity”**

**Any use of the term flexibility or reform agitates trade unions.**

Any use of the term flexibility or reform agitates trade unions. India’s formal sector offers no flexibility to firms, but as a contrast, workers enjoy good security coverage. So currently India has an absolute welfarist model – something that a low middle income country cannot afford. Instead, a good formula to emulate is Denmark’s flexi-curity model: a tripartite model that combines flexibility for employers, security for workers, and an active labor market policy to encourage skilling programs and matching the unemployed.

In addition to the reforms highlighted above, flexi-curity could be kickstarted by segregating IDA’s meanings of lay-off, retrenchment and closure provisions. The three concepts reflect increasing degrees of severity, and unbundling them could make them more palatable to trade unions, making it easier to sell reforms (Debroy, 2012). It is speculated that if compensation for layoffs and retrenchment were increased from 30 days’ pay per year worked to 45 days, political resistance may diminish. In West Bengal, this compensation is higher for layoffs – 50% of basic wages plus other benefits for the first 90 days and 75% thereafter until disposal (Sen, 2009).

Severance pay policies in India are already “modest” by international com-

parisons (Asher & Mukhopadhyaya, 2005). That brings forth the scope to trade off higher severance pay for three important opportunities – greater operational flexibility for businesses, greater professionalism in policy design and implementation by labor ministries, and lower transaction costs for new companies (Asher & Mukhopadhyaya, 2005).

### **Like-minded Unionism**

Trade unions comprising similar industry units are more credible and easier to engage with. On the other hand, unions with members from mutually exclusive industries and varied interests lead to unchecked multiplicity whereby member demands arise out of herd mentality, and lack credibility. The Amendment Act 2001 to Trade Unions Act 1926 was channeled towards addressing superfluous multiplicity. As a result, 10,274 registrations were cancelled in 2001 in West Bengal, they probably did not meet the criteria of the Amendment in terms of industrial homogeneity (Sen, 2009). While there has not been much research on the direct implications of such outcomes, the main aim of such reforms is to ensure “orderly growth, reduce multiplicity and promote internal democracy in the industrial organization and the economy” (Business Portal of India, 2013). With state unions comprising 89 percent of the total pie and informal unions on the rise, there is more reason to make this item part of the State list.

### **Improving Work Conditions**

In addition to scaling up security in the informal sector, creating better work

conditions could also make bargaining through unions unnecessary making labor relations more efficient. Examples from successful approaches used by companies show minimized backlash from unions. This includes community development, work benefits, and timely breaks.

Community development measures include renovating railway stations, bathing ghats, or social welfare activities like eye test camps – sometimes in partnership with local bodies like the panchayats (Sen, 2009). Benefits that go over and above the pay package, like free transport, dining halls, or extra cash for buying household items have also worked in the past. The kind of composition of work times, breaks, and benefits could also incentivize amicability.

In this manner, unions in large firms with increased benefits are seeing a decline especially in the case of young and white-collar employees, who do not indicate a strong urge to unionize. Moreover, state unions comprise nearly 90 percent of the total pie and informal unions are growing. Such patterns summon the increasing need to shift reform narrative to the states and the informal sector (Sen, 2009).

### **Concluding Remarks**

Labor market reform is one of the most politically difficult tasks in a large democracy like India. India’s labor legislation is archaic, restrictive, and convoluted, thereby discouraging businesses to expand and create more jobs. If India

is to realize its full growth potential, it will need to reform its heavily regulated labor market by ushering in more flexibility and scaling up security for workers. Currently, 93 percent of workforce that is employed in the informal sector where productivity is low and wages are small, stands to benefit from such reforms. However, resistance from vested interests and lack of political capital in New Delhi has contributed to six decades of impasse on this issue.

This paper identifies the most ideal reform scenarios in order of political sensitivity. This ranges from re-writing the IDA and other restrictive laws; to moving labour legislation from the Concurrent to the State list; to seeking Presidential assent for State-initiated changes. However, the paper lays out detailed and easier policy reform options to pave the way for bigger reforms in future.

The best way forward is to engage all major stakeholders – businesses, employees, and bureaucrats – to bring about smaller reforms by plucking the low-hanging fruits. The paper identifies procedural reforms undertaken by different states that spur flexibility and clarity in labor laws to facilitate the ease of doing business. Examples from states like Gujarat and Andhra Pradesh show initiatives to simplify compliance processes and also connect skilling programs to the needs of industry. Similarly, the last section argues for ways to scale up social security coverage in the informal sector and making bargaining unnecessary. Inciting competition between social security schemes, organizations to match

workers, and improving work conditions can bring more security to workers and encourage good quality unionism.

Interim reforms outlined in this paper from successful practices are intended to help push labor market dynamics. Regulatory practices need to adapt to evolving structures – as otherwise welfare cannot be advanced. In the face of a slowing growth rate, attempts to tame the deficit and inflation, and a forthcoming demographic dividend, India's political elite must remember that boosting good quality jobs is a matter of top priority.

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By Invitation

## Labor Market Flexibility & Trajectories of Development: Lessons from Brazil, India & China

Anil Verma & Ana Virginia Moreira Gomes

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*In China, labor policy first diluted employment security rights to facilitate re-allocation of labor to the private sector. When new labor problems emerged, policy shifted to re-regulate the labor market. Brazil's success in achieving economic growth and social progress simultaneously is unparalleled: informality, income inequality and unemployment decreased. India needs macro-level flexibility in re-allocating labor from informal to formal work, from rural to urban areas, and from the unskilled to the skilled. Micro-level flexibility through termination of employment must be coupled with stronger social security programs for adequate severance pay and re-training for other employment and also stronger protection for workers in the informal sector.*

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### Introduction

The debate around labor reforms in India became prominent once again with the election of a majority BJP government in May 2014. This change in government came when despite much debate in the past, the previous Congress-led governments had failed to undertake any significant reform. Great expectations now await the new government for reforms in labor policy. It is in this context that we examine the labor and employment system in India with particular attention to the issue of labor flexibility.

**When one considers potential solutions there is an alarming lack of consensus on possible directions for reform.**

Recent research in India has richly documented the dysfunctions of the Indian industrial relations system to establish the case for substantive reforms in a number of areas (Shyam Sundar, 2012; 2011; Sharma 2006; Sodhi, 2011). However, when one considers potential solutions there is an alarming lack of con-



sensus on possible directions for reform. It is arguably one of the reasons why previous governments found themselves stymied into inaction. The analysis in this paper explores possible avenues for reform around which parties to the employment system could converge. It can be useful to look for relevant lessons from both inside and outside India in a search for better ideas. It is in this spirit, that we compare the labor and employment systems in India, China and Brazil. These insights can be useful in breaking the gridlock around labor reforms, which in turn, could contribute to sustained economic development.

Why compare India with China and Brazil? Despite significant differences, these three countries face many similar challenges. They are striving to reduce poverty, improve education and health, and to become full employment economies. All three are among the biggest countries in the world in terms of population, landmass and total GNP. Together with Russia they became known as BRIC, a moniker for investors looking to profit from high growth emerging economies.

China and Brazil also share many of India's challenges in making their labor and employment systems more skilled, productive and flexible. For example, in moving its 450+ million workforce from the public sector to the private sector, China faced a challenge unprecedented in history in scale and scope. Labor regulations needed to be changed dramatically. This transformation of the labor market is far from being perfect or complete but a substantive set of regulations was put in place to facilitate this large-scale re-allocation of labor. Brazil, al-

ready a middle-income country, faces the challenge of moving its labor and employment system to the next higher level from its current plateau. Most skilled labor is in short supply despite a large labor pool that is largely unskilled or semi-skilled. Labor regulation is designed to protect workers and jobs but its large informal economy leaves many workers unprotected. So, improving the skills of its workforce and reducing informality in the labor market are significant challenges.

In the next section we provide a brief comparative sketch of the main characteristics of the three countries. This is followed by an overview of the Indian case for labor reforms. Lastly, we review the lessons that policymakers in India can draw from the experiences of China and Brazil for developing a consensus around much needed labor reforms.

### **BIC: A Comparative Overview**

India and China are the only countries in the world with a population in excess of one billion each. Although Brazil is much smaller with a population approaching 200 million, it is the dominant economy in its neighborhood much in the way that India dominates South Asia and, China, the global economy. There are other similarities. Although China has been able to sustain its high growth rate over a much longer period, both India and Brazil are also considered to be emerging economies that boosted their historically anemic growth rates to new highs in the most recent decade. High rates of growth have generated more jobs, reduced poverty and raised the aspirations for a better life. Scores of enterprises from these three

countries have confidently expanded at home and overseas.

income countries (USD 11,208), India at the low end (USD1,499) with China near the middle of this range (USD6,807) (Table 1).

In terms of per capita GDP in 2013, Brazil was at the higher end of middle-

**Table 1 A Comparative Look at Brazil, India, China**

	Year	Brazil	India	China
Population (millions)	2013	200.4	1,252.0	1,357.0
GDP per capita (US\$)	2013	11,208	1,499	6,807
Av Annual GDP Growth Rate (%)	5-yr: 2009-13	3.6	7.0	10.1
	10-yr:2004-13	4.6	6.7	8.9
Average Annual Inflation Rate (%)	2006-13	5.2%	9.3%	3.7%
Human Dev Index (HDI)	2012	0.73	0.554	0.699
HDI Rank	2012	85	136	101
Adult Literacy Rate	2010	90.0%	62.8%	94.0%
Male Life Expectancy (yrs)	2010	70.7	64.4	72.1
Female Life Expectancy (yrs)	2010	77.4	67.6	75.6
Doctors per 1000 pop.	2010	1.8	0.6	1.4
Fertility Rate (Per Woman)	2010	1.8	2.5	1.6
Workforce in Agriculture (%)	2011	15	47	35
Labor Force Participation Rate - Total	2012	70.0	56.0	70.7
Labor Force Participation Rate - female	2012	50.1	29.0	64.0
Trade Union Density (%)	2010	17.8	2.4	NA
# of Strikes & Lockouts	2008	411	423	NA

Sources: www.wdi.worldbank.org

Trade Union Density and Strike data from www.ilo.org

There are a number of similarities and differences in factors relating to workforce development and the resulting flexibility of labor. First, India has the youngest workforce while Brazil has the oldest of the three countries. The population pyramid for Brazil has been shrinking now for many years already. In China, the pyramid has just begun to shrink while in India it is still expanding at the base. These trends suggest that

**India needs to generate new jobs at a much faster rate over a longer time period than do Brazil and China.**

India needs to generate new jobs at a much faster rate over a longer time period than do Brazil and China (Goswami, 2014).

India has the largest share of its population still living in rural areas and dependent on agriculture. This share is the lowest for Brazil, which has become a largely urbanized country in recent decades. But despite such urbanization Brazil's workforce is underutilized in the north and the north-east while southern Brazil experiences critical labor shortages. Brazil is also a large landmass with relatively poor infrastructure that makes it hard to relocate the workforce and jobs.

India is the smallest of the three countries in terms of area but poor infrastructure creates problems of mobility with attendant adverse consequences for flexible allocation of labor. China is also a large land mass and has experienced uneven development between the fast developing north and coastal areas on the one hand and the less developed regions of central and western China on the other. Large investments in coastal infrastructure have made China an export powerhouse but its challenges in managing migrant labor resulting from the uneven development remain substantial.

In terms of inequality, Brazil has the highest degree of income inequality of the three countries. Its Gini coefficient, a measure of inequality, was 54.7 in 2009 compared to 33.9 in India (measured in 2010) and 42.1 in China (also measured in 2010). But, whereas inequality increased in both China and India since the 1990s, Brazil is among the few countries that have managed to reduce inequality in recent decades. Its Gini coefficient declined from an exceptionally high level of 63.3 in 1989 to 54.7 in 2009. For India, the Gini increased relatively moderately from 30.8 in 1994 to 33.9 in 2010. In China, inequality rose more significantly from 32.4 in 1990 to 42.1 in 2009.<sup>1</sup>

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<sup>1</sup>To put these coefficients in perspective, it may be noted that among the developed countries, Norway (26), Sweden (25) and Germany (28) are relatively more equal while the U.S. (41) is at the high end with Australia (35 in 1994), Canada (33), France (33 in 1995) and the UK (36 in 1999) falling in the middle of the range. Unless otherwise noted Gini coefficients were measured in the year 2000. All Gini coefficients accessed from [wdi.worldbank.org](http://wdi.worldbank.org)

Both China and India have followed a trend that Piketty (2014) contends is a law of development itself: the rate at which wealth becomes concentrated in a few hands, i.e., rate of rising inequality, exceeds the rate of economic growth. So, even as countries grow economically, they inevitably contribute to rising inequality. This is a challenge for all societies but for developing nations it poses a specially difficult challenge: how to sustain growth that would raise living standards for all without increasing inequality or even better, while reducing inequality?

### Flexibility Debate

The labor flexibility debate is often framed within the narrow context of the workplace or the level of the firm. In India, a major demand of those advocating for greater labor flexibility is to ask the government to spell out an “exit” policy that would make it easier for employers to terminate employment for workers who are no longer needed because of changes in technology or in demand for its products or in its financial ability to sustain a workforce. By itself this is not an unreasonable demand. Schumpeter’s concept of “creative destruction” captures well the dynamics of economic growth in our era of globalization. No job or workplace or firm can remain unaltered for forever. The need to restructure, reorganize and refocus the enterprise is forever present in the global economy and it needs to be facilitated by domestic policy for sustained growth.

This approach to flexibility has been criticized by a number of scholars for

various reasons that are discussed in the next section. The purpose here is to put this debate in the larger context of development so that we can look beyond India's borders for lessons on how best to facilitate flexibility. The narrowly-framed flexibility debate loses its moorings if it is not embedded in the larger context of India's developmental needs. When one examines the larger context for human resources in India, a number of issues become apparent.

First, India has a much larger share of its population in rural areas. In 2013, 68% of India's population lived in rural areas while in China, this proportion was 47% and shrinking rapidly. In Brazil, less than 15% of the population is rural. The generally accepted wisdom is that it is extremely difficult to raise incomes, provide a decent level of education and health services, and create a full employment economy if a large share of the population lives in rural areas. It is for this reason that China has embarked on an ambitious program to urbanize its population (Yusuf & Saich, 2008; Davis, 2013; China Development Research Foundation, 2013). Urbanization does not necessarily mean that there has to be a shift of rural population to existing cities, which would be a huge challenge in itself given that Indian cities are already overcrowded. Rather, it implies that more areas need to be urbanized by developing smaller towns into cities. Any new labor policy initiatives need to carefully weigh the implications for future urbanization. Labor policies need to create the kind of flexibility that would smoothen the path to urbanization. An urbanization

strategy would involve massive investments in construction of urban infrastructures. From this perspective, it can be argued that India needs not only labor flexibility at the micro level but also help urbanize its population.

**India's skill development infrastructure lags behind its aspirations for ambitious and sustained economic growth.**

Second, India's skill development infrastructure lags behind its aspirations for ambitious and sustained economic growth. The skill development infrastructure includes the basic education system, the post-secondary and post-graduate university level institutions, on-the-job workplace training, and research institutions. Drèze and Sen (2010) emphasize several key ideas about basic education in India. First, basic education has been neglected by all elites including the government, employers and unions. They speculate that this neglect may be related to the potential of education to challenge power and privilege vested in the status quo. Second, basic education has been limited in its reach. Literacy levels, even according to government supplied and somewhat inflated statistics, remain low compared to China and Brazil. The adult literacy level in 2010 was 62.8% compared to 90% in Brazil and 94% in China (Table 1). Female literacy levels are reportedly even lower although reliable estimates are hard to find. Third, there are large variations in primary school attendance and achievement within the system across provinces, gender, family

income and the urban-rural divide. Fourth, although some gains have been made in literacy levels in the last two decades, the system remains far short of even the modest goal of achieving universal primary education up till the age of 14. Moreover, school attendance, the most common measure of education, says little about the level of learning taking place. Numerous surveys have found public schools largely understaffed and underfunded, often lacking the most basic facilities such as a separate toilet for girls, let alone qualified and dedicated teachers (Drèze & Sen, 2010).

India has some excellent post-secondary and post-graduate educational institutions. The Indian Institutes of Technology and the Indian Institutes of Management have acquired national and international prominence in post-secondary education in technology and management respectively. A few dozen other universities and research institutions have similar reputations for excellence. However, for many other hundreds of thousands of qualified students, world-class higher education remains out of reach. The RUSA<sup>2</sup> initiative launched in October 2013 by the Government of India is an ambitious effort to improve the share of high school graduates going on to post-secondary education from 19.4% in 2012-13 to 30% by 2020 (Deloitte, 2013). A similar initiative for vocational education was set up in 2009. The National Skill Development Mission set up a three-tier structure with

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<sup>2</sup>Rashtriya Uchchatar Shiksha Abhiyan (RUSA) in Hindi translates approximately to: National Higher Education Campaign.

the goal of bringing industry-relevant vocational education to 550 million people by 2022 (Sodhi, 2014). These campaigns seek to improve the quality of higher education through a series of administrative reforms, coordination with states, and improved targeted funding to institutions based on meeting performance targets. Although it is too early to tell if these campaigns are yielding the desired results, these initiatives provide a clear signal that policymakers are taking note and tackling the education deficits at the highest levels of policymaking.

### **Labor Flexibility Argument & Evidence**

The argument for labor flexibility is that workplace level labor flexibility allows for efficient allocation and re-allocation of labor to fit the demand pattern for products or services. This flexibility allows the enterprise to operate at optimal efficiency that, in turn, makes it competitive. The ensuing efficiency and competitiveness would then attract new investments and lead to growth in output and, ultimately, in jobs. Although intuitively appealing, this argument needs to be placed within the industrial relations context and validated by evidence.

Several studies have examined the empirical evidence for the hypothesized effects of labor flexibility on efficiency and welfare outcomes. An ILO study is worth mentioning because of its scope and comparative focus. Sharkh (2008) examined evidence from a number of countries that span the spectrum in terms of both labor flexibility and social security programs. The

underlying hypothesis comes from the notion that system performance is enhanced not simply by making labor flexible but by combining labor flexibility with a safety net, the so-called “flexicurity” principle (Keller & Seifert, 2002; Sarfati & Bonoli, 2002). The study concluded that the relationship between labor flexibility and system outcomes is more complex than suggested by proponents of labor flexibility. Moreover, a system could do well on some outcome measures such as employment but that outcome may be associated with other less desirable outcomes such as greater inequality. In other words, there is no magic bullet. Within those qualifiers, the study did find that countries that were high on labor flexibility but poor on the safety net were not the star performers. Equally, countries that were low on labor flexibility but high on the safety net also performed sub-optimally. However, an optimal middle ground on the flexibility-rigidity scale where a basic form of social insurance when combined with moderate dismissal protection, yielded better results across a range of outcomes. The message for policymakers is that simplistic notions of creating labor flexibility by removing protections for labor can be self-defeating particularly for developing countries. Rather, countries hoping to improve system outcomes ought to combine labor flexibility with enhancements in the safety net if they are to achieve goals of economic growth and of increasing worker welfare at the same time.

### **Flexibility Debate in India**

Certain facts and trends concerning labor flexibility in India have become clear in the evidence and the debate that

has occurred in recent years. First, India has one of the strongest legal regimes of employment protection. Second, the legal regime suffers from a proliferation of regulations that often overlap and are not easy to follow. Most writers on the subject acknowledge this complex web of laws and advocate the kind of simplification that would lead to better understanding of the regulations and thereby, better compliance (Sharma, 2006).

Bhirdikar, Paul and Murthy (2011) analyzed industry data to examine the link between labor market flexibility and employment over 1999-2006. They found that formal employment shrank even as contract and informal employment grew significantly. It suggests that employers have increasingly resorted to contract labor and to informal work to cut labor costs. Employers have effectively bypassed the formal legal protections that make re-allocation of labor rather inflexible. Within the organized manufacturing sector they found a trend towards hiring contract labor and a rise in flexible work arrangements. In services, economic growth boosted employment but the bulk of it was in informal employment. Importantly, they found that states with stronger worker protection laws, accounted for more workers hired on contracts. Another study examining the effect of external shocks (in this case, average rainfall) on employment found that states with more pro-employer legal regimes did show relatively higher employment effects compared to states with more pro-labor regulations (Adhvaryu, Chari & Sharma, 2013). These findings suggest that the strong worker protec-

tion laws do not necessarily correlate with more (and secure) employment.

**Strong worker protection laws do not necessarily correlate with more (and secure) employment.**

The evidence from such studies suggests that flexible regimes do result in greater employment but even these jobs are often contract jobs or in the informal sector. Labor protection laws appear to have been largely by-passed by employers to create *de facto* labor flexibility given that there have been almost no changes in legal regulation (Sharma, 2006, Shyam Sundar, 2012; Maiti, 2013). The labor market has been rendered flexible despite restrictive labor laws due to the large informal sector and casualization of employment in the formal sector.

### **Economic Growth & Labor Regulation in China**

China is currently closing the gap between the world's largest economy, the U.S., and itself at a fast rate. It is expected to be the world's largest economy sometime in 2014 if GDP is measured in purchasing power parity (PPP) terms and by 2025 in exchange rate terms, if current trends in GDP growth rates continue for another decade. China's scale and the enormous transformation of its economy within a generation, provide a unique opportunity to learn about the inter-related dynamics of economic and social development. When China began to liberalize its economy in 1977-78, it faced two huge

challenges in terms of its labor force. First, it needed to shift some 450+ million people from the state sector to the private sector. Second, a huge migration was to occur from rural areas to the urban centers. Labor and employment policies were continually adjusted over the last thirty-plus years to facilitate these transitions. Although some of these policy initiatives did achieve desired results, many gaps persist in both policy and outcomes that need to be addressed through further reforms. To facilitate the transition to the private sector, policymakers in China had to first undo the employment and wage laws of the previous era when the "iron rice bowl" defined a system of lifelong employment security and state-fixed wages. So, a *de facto* deregulation of employment security and wage fixing was instituted. Before 1978, all workers in China were assigned to jobs by the state after completion of education. Wages were also fixed by the state. Employers could not fire workers, which resulted in lifetime employment for all. This employment system reduced mobility and incentives, and led to inefficiencies due to overstaffing, low morale, and low productivity (Meng, 2000).

**A de facto deregulation of employment security and wage fixing was instituted.**

Reforms first took root in the rural farm sector where effective deregulation of prices led to rapid mechanization, rising yields and increasing incomes. It was not until the mid-1990s that the government began restructuring state-run

enterprises. The largest state-owned enterprises would remain with the state while smaller ones were cut loose from state finances to compete in the marketplace on their own or go bankrupt. To accomplish this transition, labor policy was revised in 1986 to allow employers to hire on a contractual basis. Wages were also deregulated in the emergent private sector. Lastly, workers were encouraged and supported, financially and with requisite training, to become self-employed in their own small business. Within a few years of such deregulation, millions of state sector workers were laid off with some compensation, who then began to swell the ranks of the private sector (Meng, 2012; 2004; Appleton, Knight, Song & Xia, 2002; Giles, Park & Cai, 2006). Known as the *xiagang*, they numbered over 40 million by 2002 (Betcherman, 2005).

China's system of *hukou*, i.e., a permit that defines residency as rural or urban, played an important role in the transformation. It allowed the government to control allocation of labor first within the urban system and later from rural to urban areas. Brazil and India have no equivalent system which effectively makes the allocation of labor more market-driven but it also fuels the growth of the informal labor market with all its attendant problems of worker protection. Although China continues to ease its restrictions on rural-urban migration, a majority of the population still holds rural *hukou*. Meng (2012) puts it at 72% of the population based on the 1% Population Survey of 2005 and other NBS data.

Even as state enterprises were shedding employment more than 100 million rural workers moved into cities by 2002. What rural migrants could get were sometimes referred to as 3D jobs: dirty, dangerous, and demeaning. Rural workers were generally less educated but more likely to be employed because of their willingness to accept jobs that urban workers would refuse. Their numbers have continued to rise with the rapidly growing economy. By 2012, there were more than 260 million migrant workers, with an average monthly salary of 2,290 yuan (\$374.09), according to a report by the National Bureau of Statistics of China (Song, 2013).

These two large-scale mobilizations, i.e., state sector to private sector and rural to urban, encapsulate both the triumphs and the trials of China's strategy to restructure its labor market. The deregulation of wages and employment facilitated the movement but at a considerable human cost. Policy responses to the problems created by these mobilizations can be divided into two parts: an earlier stage of providing immediate relief to dislocated workers and a later stage of re-regulation to address long-term problems of a freer labor market. Each of these is discussed in turn.

When a worker lost her (or his) job with a state-owned enterprise, she also lost with it the social protection and services that came with these jobs. In 1998, the government under pressure to provide some relief, introduced a new labor adjustment policy requiring state-owned enterprises to provide a living allowance



and maintain social services for laid-off workers for up to three years while the worker searched for reemployment. If after three years, a worker was not re-employed, he would finally separate from the enterprise and seek unemployment benefits from the state. A centralized unemployment program was established in the early 2000s. However, its coverage and operation fell short of expectations at least in its early years. There were numerous cases of labor protests erupting because workers had not received payments and/or benefits as promised or provided for in formal regulations. In many cases, local or state governments have had to assume the financial burden of these regulations. Where layoffs were particularly large and could not be met by the local or state governments, the central government stepped in to ensure that workers were paid (Betcherman, 2004).

Even as the private sector grew it gave rise to new labor problems from non-payment of wages and violations of work hours requirements to unsafe working conditions. The policy response was to introduce new legislation to regulate in emerging areas while reinforcing already regulated areas. In particular, two laws exemplify this phase of re-regulation. In 2004, a special regulation on minimum wage was issued which was a revision of the “Enterprise Minimum Wage Regulation” of 1993 (Cooke & Rubery, 2002). It did not set a national minimum wage but rather created rules under which state governments could set minimum wages for cities or municipal-level aggregations after consulting unions and

employers at the local level. Further, the Labor Contract Law came into force beginning January 1, 2008. This legislation laid down the fundamental framework for the employment relationship. It spells out the terms that must be included in every employment contract from initial appointment to rules for termination of employment and severance pay. For many workers who had enjoyed absolute employment security in the pre-reform era this law was a final notice that the old system was now permanently replaced by a new regime that allows employers to lay off workers and terminate employment under certain conditions. For many others who had experienced the turmoil of the transition era after reforms with confusion over their rights as an employee, this was a welcome wind blowing in greater order and clarity over rules of the employment game. The Labor Contract Law was followed up with the Labor Disputes Mediation and Arbitration Law (LDMAL) which specifies how disputes are to be resolved including arbitration. It is an integral part of ensuring that workers’ rights under the Labor Contract Law are protected when disputes arise.

**Two challenges stand out that are now shaping labor regulations in China: first, a significant growth in the informal economy, and second, the rising level of labor unrest.**

By 2012, the private sector in China accounted for over 60% of the national output (Yiyuan, 2013). China now shares some of the same problems that other

developing countries with a market economy face. In particular, two challenges stand out that are now shaping labor regulations in China: first, a significant growth in the informal economy, and second, the rising level of labor unrest.

### **Informalization**

Informal markets were relatively controlled in their size under the older socialist when almost everyone lived and worked within a defined work unit, the so-called *danwei*. But when the deregulation of the 1980s and the 1990s took hold, millions of workers had to find their own employment. Inevitably, this mobilization has given rise to increasing numbers of workers being employed (or self-employed) in the informal economy (Cooke, 2011). By 2009, according to some estimates, nearly 30% of the urban labor force, and 65% of the 150 million rural migrant workers in urban areas were employed informally (Cai & Chan, 2009).

From a labor and employment perspective, the informal labor market is an unregulated zone where workers end up involuntarily or voluntarily. Demand for such labor is so great especially in the urban service sector that for many workers there is no choice but to become informal. Informality occurs due to a number of factors. Some are casual or contract workers needed for temporary work such as repair and construction in formal establishments. Others are employed by small and medium size establishments that are themselves unregistered and hence maintain no payroll nor pay any

taxes. Another category of informal workers may be employed by informal organizations that supply labor on a casual basis to other organizations. Xu (2007) notes that in Shanghai alone more than 400,000 workers were employed in such arrangements including nearly half of that number in local public services such as street cleaning and garbage collection, etc.

As may be expected, most informal workers take these jobs because they have few other options given their level of education and, frequently, the lack of an urban *hukou*. This leads to widespread exploitation and violation of existing laws and protections. By all accounts, the problems of labor exploitation are well recognized by the government in Beijing but the Central Government needs the support of provincial and local governments to enforce labor laws designed to protect workers.

### **Labor Unrest**

The All China Federation of Trade Unions (ACFTU) is the only recognized trade union in China. Although it is not completely independent of the government and the Communist Party, most writers suggest that the ACFTU has come under increasing pressure to speak up for workers who have become powerless against the tide of privatization. Much of this pressure comes from labor protests that have been breaking out spontaneously in recent years. In fact, employers have been signing collective agreements that are permissible under the Labor Contract Law. According to

ACFTU data cited in Liu (2011), there were 1.4 million establishments that had signed 2.438 million collective agreements covering 184.6 million workers. Although reliable data on the number of disputes or work stoppages are not available, some idea of the extent of unrest can be gleaned from the official (and likely understated) numbers. According to the China Statistics Yearbook, there were 589244 labor disputes “accepted” by the official labor dispute arbitration committees (LDACs) in 2011 of which 6592 were classified as collective disputes covering 174,785 employees (as cited in Liu, 2014). Though these numbers look small compared to the size of China’s labor force it should be noted that official reporting greatly underestimates the actual number because most disputes would be either unreported or not “accepted” if they did not follow certain criteria.

The policy response so far has involved the Labor Contract Law and associated laws and regulations. But, policy remains unclear in many areas of collective disputes, which leads to a large variety of responses depending on the choices made by state and local authorities. The possibility remains that the government could introduce new legislation in the future that would address collective disputes and their resolution more specifically and directly.

### **Brazil’s Policy Challenges**

Brazil’s economy enjoyed resurgence under the democratic rule after many decades of slow growth and military rule.

After conquering hyperinflation in the 1990s, economic reforms under Presidents Cardoso and Lula led to higher growth in the 2000s. The economy began to embrace globalization, albeit gradually and cautiously. The gradual opening up of the economy brought increasing pressures on the labor market to adopt reforms. It has led to significant changes in the Brazilian employment relationship justified, rightly or otherwise, by the perceived need to be competitive in a global market. One prominent challenge is to invest in the education and skills of its workforce. The other challenge is increasing labor flexibility even as the size of the informal economy is reduced.

### **Education & Skill Development**

Despite being a middle-income country, Brazil’s investments in developing a skilled workforce have lagged behind the pace of capital investment in the country. The inadequacy of its investment in basic education is well demonstrated by the performance of its pupils on standardized international tests. In the OECD Pisa (Programme for International Student Assessment) study, Brazilian students ranked 52<sup>nd</sup>-54<sup>th</sup> out of 65 countries in reading and 57<sup>th</sup>-60<sup>th</sup> out of 65 in science and mathematics (OECD, 2012). While Brazilian students performed below the OECD average, their scores in mathematics have improved since 2003 from 356 to 391 score points, making Brazil the country with the largest performance gains since 2003. Significant improvements are also found in reading and science. Between 2003 and 2012,

Brazil also expanded enrolment in primary and secondary schools, with enrollment rates for 15 year olds rising from 65% in 2003 to 78% in 2012.

An earlier study had found that Brazilian teachers are often poorly educated and teach on subjects they know little about, while no federal program exists to better train and monitor their performance (JBIC, 2005). The government of President Rousseff initiated a series of measures to strengthen the skills of Brazilians including better funding of schools for teachers, equipment and infrastructure. Another ambitious initiative is the Science without Borders program, which is sending 100,000 students on scholarships to study science and technology at leading foreign universities. In return, Brazil is hosting students from other countries on an exchange basis. Brazilian students spend up to a year abroad studying with well-known professors abroad. The hope is that they will return to Brazil with new knowledge and inspired passion for further learning. Eventually, they are expected to meet the continuing demand for skilled labor needed for sustained development.

### **Informality, Flexibility & Policy Responses**

After the crisis in the 1990s, the country's economy has been on a recovery path: unemployment reached a low of 7.1 % in the first trimester of 2014 (IBGE, 2014:5) and in almost all the regions, job growth occurred through formal employment. Informality – workers who lack registration or are working in

an irregular way or are self-employed, with no formal links to the social security system or the FGTS<sup>3</sup> — has been in a continuous decline since the 2000s. Between 2000 and 2012, formal work increased from 44.6% to 56.9% of the workforce (IBGE, 2013:142). Informality declined further from 38% in 2010 to 33% in 2013 (IPEA, 2014:14). Berg (2010:12) cites the following reasons for the decrease of informality: more inclusive macroeconomic policies that promote the demand for formal workers; demographic shifts in the Brazilian population; educational policies; micro-level policies that promote the formalization of small enterprises including ones that employ only one worker.

The broad concept of informal economy – based on the production unit – includes different forms of informality: e.g., tax evasion, small enterprises, street trade, illegal work, temporary work, domestic work, precarious work, etc. (Cacciamali, 2000:153). According to Cacciamali (2000:164), there are two major elements present in informal labor markets: the subordinated labor and self-employed work. Their relationships share common traits: high job mobility; low and highly variable earnings; absence of social protection and labor regulation;

<sup>3</sup> Fundo de Garantia por Tempo de Serviço is Severance Indemnity Fund, a mandatory fund created by the Law #5.107, in 1966. Only employers contribute to it and the current rate of contribution is 8% of the wage, which is paid by the employer into a state-managed fund. It can be used by the individual in case of being dismissed without cause, to cover expenses during illnesses, or to build or buy one's first primary residence.

flexible and unpredictable hours and duties; and generally lower qualification. Pochmann (1999) argued that the legal ease of hiring and firing combined with an abundant supply of low-skill workers and the lack of workers' organizations in the workplace gave employers excessive power in the employment relationship. The combination of these factors places Brazil among the countries with the highest firing rates – 64% in 2012 (DIEESE, 2014: 12). Prior to 1966, workers acquired lifelong employment security under Brazilian law after ten years of continuous employment. A new regime was introduced in 1966 with the creation of the FGTS, a fund that would pay compensation to workers who lost their jobs. This regime gradually replaced the old system of lifelong employment security. The old system was fully replaced by the 1988 Federal Constitution, which permits firing workers but requires indemnification from the FGTS. Brazil has not ratified ILO Convention 158 on termination of employment and still lacks rules on the procedure for and limits on termination of employment.

Besides the traditional types of informal work – in small production units, domestic work, and illegal work – there are newer types of informal work that have become more prominent in recent years. These jobs result from the adoption of more flexible work relations. Globalization and the search for labor flexibility constitute the framework within which new types of informal work has grown. Formal employees were turned into consultants, cooperative members, outsourced workers or partners. These

new relations can be found not only in the more disadvantaged segments of the labor market, but also among the more qualified and traditional segments, e.g., health, education, management, and law. No longer does informal work limit itself to any specific sector, demographic group or region.

This picture indicates that informality is not a transitory problem. Even though informality has been decreasing in Brazil, it is unlikely to disappear any time soon. It is important to identify an appropriate labor policy response to promote formalization and thereby provide protection to the most vulnerable workers. For example, laws can help increase the cost of informality and, at the same time, the benefits of formalization. Previous research has found that the main reason for choice of informality is to avoid taxes and the cost of social security (Neri, 2002:4). For example, healthcare access is universal in Brazil. However, access to private healthcare is much higher among formal workers with a labor registration card (42.9%) than among other groups such as the self-employed (15.3%), employees with no labor registration card (16.3%), agricultural workers (18.4%), domestic workers (15.9%) and unpaid workers (24.3%) (Neri, 2002: 4). Informal workers do not have any income guarantee protection in case of accident, sickness or unemployment. However, they are covered by the public pensions system, even though they do not make any contributions. The value of their pension is based on the minimum wage – R\$724,00, approximately US\$316 per month. Many informal sector employ-

ers and workers are reluctant to contribute to the social security fund because they will receive the public pension regardless of whether they contribute or not. Guaranteeing a low pension without the obligation of any contribution to the social security system has a negative effect on formalization. The problem here is that this guarantee makes the cost of formalization higher without increasing its gains. Thus, we disagree with Chen (2007:11) that one policy goal should be to “decrease the cost of working informally”. Since formality is an important way to guarantee social protection, the real policy challenge is to increase the benefits of formalization and to increase the costs of informality (e.g., with inspections, fines, etc.) “without necessarily increasing or reducing informality’s benefits” (Carmargo & Reis, 2005 :277).

### **Brazil: Trends in Labor Flexibility**

During the economic crisis in the 1990s, the Brazilian government began to modernize by embracing some degree of labor deregulation and flexibilization. One important argument in this discourse was that the rigidity of the labor market was one of the reasons of informality. An inflexible formal labor market drove both employers and workers to subscribe to the informal labor market. Some minor alterations were made in the Brazilian labor code – the CLT<sup>4</sup>— had the objective of creating jobs and to ease access of informal workers to formality.

<sup>4</sup> The CLT (Consolidação das Leis do Trabalho) was promulgated by the Federal Decree-law # 5.542 on 1 May 1943, joining all the legal texts covering individual and collective labor relations.

The main changes in the law were the approval of a temporary contract,<sup>5</sup> suspension of the labor contract,<sup>6</sup> and compensation of hours.<sup>7</sup> These were piecemeal reforms that ended up not having a significant impact on the labor market. No comprehensive labor reform has been undertaken in recent years. Looking at the Brazilian case, the most important examples of *de facto* flexibility are labor outsourcing and employment cooperatives. These practices did not come from legal reforms, but from fraudulent practices and by escaping trade unions.

Labor outsourcing (*terceirização*)<sup>8</sup> is allowed by the Superior Labor Court - SLC, rulling #331, in the case of intermediary services, when there is no direct subordination and the work is performed by the individual specified in the labor contract. The SLC requirements have not been enough to effectively regulate this practice, which disguises the *de facto* employment relationship by making a non-employment contractual arrangement with a third party to avoid the costs of a bilateral employment relationship. According to Pochmann (2007:12-14), who examined the period between 1985 and 2005 in the state of São Paulo, the number of workers in these triangu-

<sup>5</sup> Law 9.601 of 1998.

<sup>6</sup> *Consolidação das Leis do Trabalho (CLT)*, Decree-law nr. 5452, art. 476 (promulgated 1 May 1943).

<sup>7</sup> Law 10.101 (enacted 19 December 2000).

<sup>8</sup> “Triangular employment relationships occur when employees of an enterprise (the “provider”) perform work for a third party (the “user enterprise”) to whom their employer provides labor or services.” ILO, 2003 at 39.

lar relationships increased from 60,400 to 423,900; indeed, 12.1% of the formal jobs created during this period consisted of these relationships. As well, the number of enterprises that provide triangular services went up from 257 in 1985 to 6,308 twenty years later. In 2005, almost a third of these enterprises had no employees, only “partners” in the enterprise (another term used to disguise the employment relationship). There has been some ongoing discussion in National Congress to regulate labor outsourcing. The main points of this debate is whether to allow labor outsourcing both in intermediary and final activities of the enterprise and on who bears the liability for violation of labor rights. There is still no consensus on these issues and labor outsourcing remains largely unregulated and widespread in the labor market.

The employment cooperatives also act as “providers” of workers (*cooperativas de mão-de-obra*). In the case of the disguised cooperatives (the ones that act only to provide labor for employers), the workers are deemed to be full members of a cooperative, and not eligible for the benefits that come with employee status. Employment cooperatives were regulated by the law #12.690 from 2012, establishing new conditions for their functioning and rights for their member. The law aims to decrease the incidence of fraudulent employment cooperatives.

Both practices (labor outsourcing and employment cooperatives) are not illegal *per se*. They become illegal only if fraudulent practices disguise the actual employment relationship in the eyes of

the law by resorting to outsourcing or the use of worker cooperatives. Therefore, there is a gray area in which even big enterprises can comfortably hire workers through those relations behind a thin veil of legality. Only if the case goes to a labor court, the employment relationship can be identified and recognized by law, but this remedy is not so efficient. Usually, workers will go to the court only after dismissal, since there is no protection against dismissal before deciding to sue the enterprise. Also, there are time limits on when legal questions can be taken to court. Complaints can not be taken to court after an absolute limit of 5 years after the event, or during the employment relationship, or after 2 years of the end of the relationship.

### **Informality and flexibility**

There has been a strong movement in recent years advocating more flexibility in the labor market, arguing that labor rights make the employment relationship expensive and rigid, and thus not accessible to informal workers. The cost of an employment relationship then has been the object of a sharp debate. Calculations of “rollup” costs over and above base pay for payroll taxes, mandatory benefits and the like vary from 19.4% to 101% (Gomes, 2001:109-10). There are different ways of making the assessment, and no clear consensus over any of them. Because many labor rights have direct implications for money paid to workers, directly or indirectly, rights are seen as an added cost factor, which seems to be a good reason to many for abolishing them.

In this context, labor regulation has been associated more with the problems in the labor market than as a solution to the challenges brought by globalization. For example, although there was a decline in the informality rate in the last decade, Ramos (2006:34) calls attention to the fact that sometimes informality is seen as a solution to the lack of opportunities in the labor market. However, as the author emphasizes, informality is generally a survival strategy when the labor market is not able to produce enough jobs with acceptable standards. It is in the informal market that we find the most excluded segments of the Brazilian population: 51.3% of poor Brazilians are in families whose principal earners are informal workers (Neri, 2000:5).

**The experience of the 1990s and 2000s did not support the claim that labour regulations caused growing informality”.**

Recent trends in informality have been analyzed by a number of studies. Berg (2010) reviewed all evidence available at the time to conclude that, “the experience of the 1990s and 2000s did not support the claim that labour regulations caused growing informality”. Among other evidence, she cites the strong growth in formal jobs in the 2000s, a period during which the minimum wage nearly doubled in real terms. In a growing economy, labor regulation *per se* is not necessarily an impediment. In fact, some labor policies, such as the minimum wage, can stimulate growth and job creation by increasing the income of the poorest segments.

Instead of just deregulating or creating more flexible labor relations, Brazil has developed social policies that create social and economic opportunities to the more excluded segments of the population and, in some cases, introduced more regulation aiming to formalize some sectors of the labor force characterized by high informality, as was the case of the employment cooperatives law and the more recent domestic workers constitutional amendment (Constitutional Amendment 72 of 2013). Brazil’s experience suggests that governments, rather than focusing on deregulating the labor market, should tackle issues of labor flexibility and informality by encouraging firms “to register their businesses and their workers, either through simplifying registration, lowering taxes or providing incentives to develop high-road competitiveness strategies” (Berg, 2010).

### Policy Priorities for India

Recent policy developments in both China and Brazil provide useful insights to policymakers in India in terms of crafting future labor policy. China has made great strides in recent decades. When China began its economic liberalization circa 1980, its per capita income was lower than India’s. By 2013, China’s per capita GDP was more than four times that of India’s (Table 1). Brazil’s per capita GDP is more than seven times that of India’s. Both China and Brazil also have higher attainments on some indices of social and human development. The 2012 Human Development Index for India was 0.554, well below both Brazil’s HDI of 0.73 and China’s of 0.699 (Table



1). The challenge for India is not only to once again kick-start economic growth but to make significant social gains at the same time.

When we consider India's needs in this light it puts the labor flexibility debate in a somewhat different light. As suggested earlier, there is no doubt that some reform of the complex web of labor laws would bring greater clarity for both employers and workers. On the other hand, simply making it easier for employers to hire and fire would be an over-simplification of a policy challenge. Moreover, there is no guarantee that any social gains would result from a single and simple change in the law. Even the potential economic benefits could be negated by a regressive "race to the bottom" when Indian firms would be tempted to compete on the basis of cost cutting rather than through innovation and value addition.

Lessons from China have to be drawn with the caveat that the government in Beijing can afford to be a lot more authoritarian than its counterpart in New Delhi. But these differences may not be as significant for economic policymaking as it may appear at first glance. First, a majority government in New Delhi wields more power in carrying its agenda through the parliament. Second, Beijing's authority may be supreme in political life but in many aspects of workplace governance including labor flexibility, the central government's role can be more limited as it navigates policy implementation by enlisting the help of state and local authorities.

China's experience with the great transition shows us that labor regulation needs to be designed in accordance with development goals and needs of the nation. In the early phase of its economic liberalization, labor policy tilted in favor of employers by diluting employment security rights of millions of workers. The "iron rice bowl" guarantee of lifelong employment was removed to facilitate a shift of employment from the state sector to the private sector. However, when the shift accelerated and other labor problems began to crop up such as informality and increasing level of labor disputes, both individual and collective, the policymakers moved gradually to re-regulate the labor market. The re-regulation has at its core the pluralist objectives of protecting the rights of both employees and employers. One lesson to take away from China's experience is that regulation needs to be adjusted to development needs over time. When greater labor mobility is desired across sectors then labor policy needs to facilitate transfers. However, China's experience has also shown that policies facilitating mobility can not address deficits in aggregate demand for labor. To make the economy grow other types of reforms may be warranted and they should not be confused with an undue emphasis on de-regulating labor policy.

**When greater labor mobility is desired across sectors then labor policy needs to facilitate transfers.**

We also learn from the China experience that both over-regulation and

under-regulation have costs associated with them. The same policy can appear to be a case of over-regulation in one time period and inadequate regulation in another time period. This notion of “appropriate” regulation may be criticized by some who would argue that worker rights should be based on principles rather than on the state of the economy. Certainly, raising the bar on rights is often considered as righting the historical wrongs. In this formulation, any deregulation is regressive, amounting to nothing more than “turning the clock backwards”. This may be true of certain core labor standards which are well-articulated by the ILO in its *Decent Work* agenda (ILO 2001). But labor regulation is much more than core labor standards. Moreover, the early theorists and practitioners in the then emerging field of labor market regulation and employment relationships, such as the Webbs in the U.K., John R. Commons in the U.S. and Mackenzie King in Canada, held that labor regulation should be closely related to industry and workplace conditions for both efficiency and stability considerations (Kaufman 2004). This view has a parallel in monetary economics, which can be helpful as an analogy. Money supply in any economy is regulated by the central bank to reflect growth in the production of goods and services. If money supply keeps in step with economic growth, growth can be expected to be sustainable and prices can be expected to be stable. If money supply grows faster than the rate of economic growth it would lead to rising prices (i.e., inflation). On the other hand, if money supply grows more slowly than the economy, the limited supply of money would compromise economic

growth and ultimately, the surplus would fund more and better jobs. So, just as monetary supply tries to keep step with economic growth, so should regulation evolve as labor market needs and goals change over time. It should be pointed out that the analogy is not perfect specially when we consider adjustment cycles. In case of money supply, adjustment frequency can be very short, sometimes as short as monthly or even at normal times, quarterly. Labor regulation does not need to be adjusted so frequently. It may be several years before sufficient changes take place to warrant changes in regulation or on occasion it may occur over a shorter duration.

Brazil’s experience in reducing informality and income inequality is even more pertinent to India’s case. Although democracy arrived in Brazil more recently, it is proving to be as resilient as India’s. With a Presidential system it provides more stability and continuity in policymaking than does India’s parliamentary system of governance. Brazil has embarked on an ambitious program of providing universal healthcare and education. As a middle income country, it faces greater pressures from globalization to cut costs and improve flexibility. The policy response has been to pursue social programs as aggressively as pro-market reforms aimed at improving macro-economic efficiency. Brazil is among the very few countries where economic growth has occurred at the same time as social progress as measured by decreasing informality, decreasing income inequality and decreasing unemployment.

## Conclusions

As of mid-2014, India was facing great opportunities as well as significant challenges for reforms which if done right, could propel the country and its citizens towards greater prosperity (Tellis, 2014). Our analysis of Brazil and China suggests two overarching paradigms that could inform policy reforms in India. First, the labor flexibility debate needs to be recast in light of development priorities of the nation. India needs re-allocation of labor from the informal sector to the formal sector on a large-scale. Ubiquitous informality holds back economic growth as well as gains for labor in terms of legal protections, income, working conditions and skill development. India needs flexibility incenting informal workers and employers to move to formal status. India also needs a re-allocation of labor from rural to urban areas. Rural residence prevents people from having access to better education, health and employment prospects. Lack of opportunities for improving skills and accessing employment perpetuates poverty. Similarly, the educated but unemployed youth need policies that would facilitate easier transition from school to work.

These are all examples of re-allocation of labor in which India needs the kind of flexibility that would allow these transitions to occur smoothly. It is labor flexibility at a macro-level without which micro-level flexibility by itself would not lead to the achievement of key goals of development.

Second, India needs to build consensus around a grander vision of reducing

poverty through education and urbanization and by investing in people's skills and in physical infrastructure. The human development and infrastructure gap between India and other major emerging economies such as Brazil and China are considerable but bridgeable. India lacks not the physical, human capital or financial resources but the political will and administrative capacity to deliver results. Only a shared grand vision can loosen the status quo sufficiently for change to seep into the ossified layers of government and other institutions of governance.

**Workers should have access to compensation based on length of service and the opportunity to re-train for other employment.**

The above does not, in any way, negate the need for reforms for greater labor flexibility at the workplace level. At the very least, some administrative simplification of the web of labor laws will certainly help. But, if re-allocation of labor across firms and industries is to be made easier by allowing employers to terminate employment more freely then this policy must be matched with simultaneous policy responses in at least two areas. First, workers should have access to compensation based on length of service and the opportunity to re-train for other employment. Such worker assistance programs have been used in other countries with considerable success. Second, worker protection by law and through enforcement must be strengthened in the informal sector. Some aspects

of informality have to do with lack of literacy and local capacity to accommodate formality. But, a large share of informality lies in weak enforcement of existing regulations and fraudulent practices. These “leaks” can be plugged if government has the political will to do so.

Discussions of labor flexibility at the workplace level should not occur without a consideration of adequate labor protections, not only at the workplace level but also in the labor market at large. If such reforms are not coupled, we may see economic growth but without any significant social progress (Sodhi, 2011). If India is to join its peers on the world stage as a large but also a dynamic and strong economy, it can not afford to take a narrow view of labor flexibility. The flexibility debate is a great opportunity to leapfrog out of the small pond to begin building a world-class labor force that is as flexible as it is skilled and secure.

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**By Invitation**

## **Quo Vadis, Industrial Relations Disputes Resolution...?**

**Jerome Joseph**

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*Differences and disputes are intrinsic to employer-employee relationships thus necessitating fair disputes resolution mechanisms and processes. The increased demand for labor law reforms and the general trend underlying the target provisions for change point towards an assertion of the managerial prerogative of employers on grounds of competitive survival and growth through labor market flexibility. However, disputes resolution reforms need to bear in mind that in the pursuit of shareholder centric dividends, the democratic dividend of workplace democracy should not be sacrificed. The reforms related to fair and speedy disputes resolution deliverability therefore should be geared towards creating workplace “ombuds-committees” and strengthening conciliation services while leaving the democratic rights of labor untouched.*

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### **Quo Vadis, Industrial Relations Disputes Resolution...?**

The clamor for labor law reforms is back to centre stage with the change of guard at the Centre in India and the first move has been initiated by a state government run by the same party now in charge of labor policy changes at the Centre. The targets again are three labor legislations which have been the focal points in the labor market flexibility debate – The Industrial Disputes Act (1947), Contract Labor (Regulation & Abolition) Act, 1970 and the Factories Act (1948)(indianexpress, rajasthan-shows-way-in-labour-reforms). Many of these moves are in response to demands from industry associations. For instance, according to FICCI, “The multiplicity of labor laws has created confusion and complexity.” (economictimes. indiatimes, 2014dl-sachdev). With the clear objective of asserting the managerial prerogative of employers, according to FICCI the Industrial Disputes Act should be amended to facilitate ‘hire and fire’ to meet market demands and to give employers the power to change service conditions without the statutory 21day notice that needs to be given to employees before any such



change is implemented. Trade unions have their own stand on the reforms debate as reflected in statements by their leaders. According to the General Secretary of the Centre of Indian Trade Unions, “The labor force is the real contributor to the value-added society so they should be treated as human beings and not as a commodity. Proper enforcement and protection of laws should be there for the labor force. Labor standards are often ignored by employers and exploitation of workers takes place. These violations should be taken seriously by the government and the violators should be punished.” (economicstimes.indiatimes, 2014dl-sachdev).

**Labor standards are often ignored by employers and exploitation of workers takes place.**

The stage is thus set with the players ranged on various sides of the reforms debates and demands with the inevitable differences and disputes which will be played out in the various theatres of representative forums on offer in a democratic setting made possible by the mosaic of the Indian Constitution. While there are many themes which will be the focus of the reforms drama and the diverse enactments of *dramatis personae*, this paper will focus on one area which will always remain significant in employer-employee relations whatever the denouement on other reform themes which are likely to be enacted in the near future. The area in question is that of disputes and disputes resolution in employer-employee relations and the question to

be addressed here is related to the nature of reforms in this important sphere of stakeholder engagement.

### **Ecosystem of Industrial Relations Disputes**

A consideration of the changes needed in disputes resolution will have to take into account the ecosystem of industrial relations disputes in today’s context. The history of industrial relations shows that as long as there is an employer and an employee, and there are terms and employment contracts, there will be differences and disputes, conflicts over rights and conflicts over interests, standoffs between what the employee is expected to deliver and what the employee gets in return from the employer. Even if all the laws are amended in line with organizational-managerial and investor demands, the fundamental contradictions between employer and employee will remain on the workplace justice fronts. Disputes in industrial relations cannot be wished away through legal reforms in the thrust towards greater “labor market flexibility”. The removal of prevailing fences and boundaries which may result from such changes will necessitate higher order disputes resolution agencies, strategies, methods, processes and competencies in order to create a fair workplace informed by human dignity and speedy disposal of industrial relations disputes.

Table 1 gives a glimpse of the causes of disputes in industrial relations during the period 1961-2011. Disputes over wages and allowances, bonus, personnel,

retrenchment, leave and working hours, indiscipline and violence and a whole host of causes under the category “others” which include layoffs, workload issues, union rivalries, have held constant over the past fifty years. Some evidence is available as to what happens when organized labor shrinks and the agencies

of the state withdraw in playing their mediatory and statutory role in the data given in Table 1. As trade union numbers dwindle and “de facto” reforms through a tactical withdrawal of state labor department services, workplace indiscipline and violence seems to have escalated as is evident from the 1961-2011 data.

**Table 1 Industrial Disputes by Causes: 1961-2011**

	1961	1971	1981	1991	2001	2011
Wages and Allowances	30.44	34.30	28.70	28.90	24.63	24.90
Bonus	06.85	14.10	07.80	04.65	06.53	03.80
Personnel	29.30	23.00	21.40	17.90	10.98	09.20
Retrenchment	00.00	00.00	00.00	02.59	01.34	00.50
Leave and Working Hours	02.97	01.40	02.20	01.20	00.20	00.30
Indiscipline and Violence	00.00	03.60	10.20	22.26	23.20	30.80
Others (Lay-off, Union Rivalry, Work Load, Gherao, Not Known)	30.44	23.60	29.70	22.50	33.20	30.50
Total	100.00	100.00	100.00	100.00	100.00	100.00

Source: Indian Labour Year Book: 1961-2011

Besides the 50 year decadal data on workplace indiscipline and violence, there have been three major incidents of serious workplace violence leading to the tragic loss of life in the recent past between 2008 and 2012– a Greater Noida firm (timesofindia.indiatimes 2008 india-unit-graziano-trasmissioni-commercial-production), a Coimbatore firm (dnaindia 2009 12-arrested-for-murder-of-pricol-v-p-near-coimbatore) and a Manesar firm (timesofindia.indiatimes2012manesar-plant-awanish-kumar-dzire) which were linked to on-going disputes and thus have a bearing on the discourse on reforms related to disputes resolution. A careful analysis of anecdotal information available in the public domain related to the three tragic events referred to above suggests ample evidence of a serious deficit

in the area of industrial relations disputes resolution.

**At the root of the three incidents clearly is the progressive increase in “de facto labor market flexibility”.**

At the root of the three incidents clearly is the progressive increase in “de facto labor market flexibility” expressed in the form of the ratio of contract workers to permanent workers. The insecurity and inequality which enters into the shop floor dynamics as a result of the contradictions inherent in workforce structures becomes a major factor accounting for the simmering discontent. The Coimbatore firm workers, for in-

stance, were agitating for over two years against the hiring of contract workers prior to the workplace incident (reuters 2009-pricol-killing-labour-at-the-receiving-end). According to the top management, at the Manesar plant, the ratio of regular to contract was 50-50 before the incident as compared to 30-35 percent contract workers in the parent country (businessstoday.intoday 2012-violence-at-maruti-manesar-criminal-act).

Contractualization has led to wage disparities between permanent and contract employees contravening the “equal pay for equal work” principle leading to serious disaffection and disputes with managements. The Coimbatore firm workers were agitating for over two years against the non-payment of pay and other benefits prior to the incident (reuters/2009/pricol-killing-labor-at-the-receiving-end). The management had also been deducting up to Rs.1,000 a month from each worker citing the loss incurred by the company as the reason (hindu/2009/09/26/). The Greater Noida firm dismissed 250 contract employees in June after they had staged a sit-in demanding a salary raise and the status of permanent employees consequent to the Greater Noida firm reneging on an agreement to provide a 3000 Rupees per month pay increase, by attaching conditions to the pay hike (timesofindia. indiatimes. 2008-india-unit-graziano-trasmissioni-commercial-production). A fact-finding team of a union that visited the spot after the September 22 incident found that out of the 1200 workers employed in the factory, only 500 were regular workers, and the rest were on contract. The

Greater Noida firm at the time paid its regular workers Rs.3200 a month for working 12 hours a day; contract workers were paid Rs.2200 per month, and denied various rights (sanhati/998/12)

Disaffection and discontent and worker reactions with wages and working conditions have been countered with terminations and suspensions which are used freely especially at the slightest sign of mobilization and collectivization for enhancing wages or for demanding regularization. For forming a union the Coimbatore firm terminated about 1,500 workers who had not been made permanent for the last 20 years (cpiml/liberation, 2009). The company terminated 42 employees for indiscipline on grounds of preventing capacity utilization of the factory and stopping other workers from carrying out their duties (dnaindia 2009 report12-arrested-for-murder-of-pricol-v-p-near- coimbatore).

The Greater Noida firm had been compelled by worker protests to agree to reinstate all but 15 of the 200 contract employees whom it had dismissed after they had staged a sit-in demanding a salary raise and the status of permanent employees (timesofindia. indiatimes. 2008). The Manesar plant’s reaction to the July 18 violence was strong, “There is no scope to retain any of the workers involved in the assault and violence at Manesar. We want to create a strong deterrent with a clear message to miscreants that the guilty have no chance as we restart production” (economic-times.indiatimes,2012). Again as reported, the Manesar Plant, while lifting the

month-long lockout from August 21 served termination notices on 500 regular workers (indianexpress, 2012 manesar-violence-maruti-suzuki-to-lift-lockout-sacks-500-workers)

**Another tactic used is to threaten closure although this has not been implemented in any of the three cases.**

Another tactic used is to threaten closure although this has not been implemented in any of the three cases. The Coimbatore firm, for instance, said these strikes have hit profitability and they could shift base (reuters/2009/pricol-killing-labor-at-the-receiving-end). When the Greater Noida firm top management came to India after the incident and a local company director said as quoted, "One of the key issues they will discuss is whether the Greater Noida plant should continue to function or be closed down. (timesofindia.indiatimes, 2008\_greater-noida-lalit-kishore-chaudhary-marcello-lamberto)

As many as six workers who formed a union in Coimbatore were transferred to Uttaranchal (cpiml/liberation/2009) and the workers protested against it a couple of years before the incident (cpiml/liberation/2009). A senior official was quoted as saying that the HR manager was targeted because he was "weaning away" employees from a union that was leading the protests (hindu, 2009/09/23). Though the workers were ready for talks, the management said they should not be part of a particular trade union (cpiml/liberation/2009).

"There is no compromise on violence," was the Manesartop management assertion when asked whether he was ready to engage the Union, in any kind of peace talks to start operations (Ttimesofindia.indiatimes,2012-07-21, manesar-plant-maruti-suzuki-workers-union-shinzo-nakanishi). And when asked what would happen to the new union that had got recognition from the Haryana Government as well as the Manesar management's support after the previous one was disbanded last year, the response was unequivocal—"It will be derecognized, for sure" (timesofindia.indiatimes/2012-07-22, manesar-plant-awanish-kumar-dzire)

To try and offset the influence of the union on the worker, a good conduct bond was required to be signed by the workers at the Manesar plant to declare they would "not resort to go slow, intermittent stoppage of work, stay-in-strike, work-to-rule, sabotage or otherwise indulge in any activity, which would hamper normal production in the manufacturing unit" and was intended as a preventive mechanism (indianexpress,2011/11/29maruti-good-conduct-bond—unfair). In addition, as an alternative to worker affinity to unions, top management said that the company had taken steps to improve relations with the workers by engaging a consultant to conduct an impartial assessment and also conducted communication programs. "Perhaps it was not enough" (timesofindia.indiatimes, 2012-07-21manesar-plant-maruti-suzuki-workers-union-shinzo-nakanishi) to show any permanent result and remove any chances of a trust deficit. From what

transpired on July 18<sup>th</sup>, such initiatives did not appear to have weaned away workers from their unions or improved relationships with supervisors and managers. “The management and the workers need to improve relationships,” MSI Chairman said (english.samaylive/maruti-violence-manesar-new-delhi-gurgaon-business-news.html)

**The underlying inducers which have emerged are also the main themes of the reforms agenda related to industrial relations.**

The analysis and interpretation of the three tragic workplace incidents and the emergent insight into the ecosystem of industrial relations disputes suggests that the underlying inducers which have emerged are also the main themes of the reforms agenda related to industrial relations. In a sense the analysis is also indicative of the kind of issues which industrial relations will confront if the *de facto* reforms of lived industrial relations experiences as described above become a *de jure* reality through changes in labor laws.

However in the backdrop of a long and well established context of a democratic society and polity, industrial relations has evolved into a complex phenomenon in which employers and their organizations, employees and their collective associations as well as the state and its agencies connect in order to evolve procedural as well as substantive policies and instruments to regulate the point of contact employer-employee relationship, to manage contra-

dictions which arise in their transactions and to work towards consensus among contending stakeholders. Conflict and congruence, contradictions and consensus, cooperation and confrontation characterize the interactions of various stakeholders brought together by the contract of employment within the framework of legality and constitutionality. Respect for constitutionally and legally conferred rights like the right to associate, right to be recognized, right to represent workers in collective bargaining processes, right to withdraw labor when all else fails could be the foundations for strengthening fair and speedy disposal of disputes even as the Indian democracy considers reforms in the arena of disputes resolution.

The changes in labor laws initiated by the state of Rajasthan are but a harbinger of things to come in the thrust towards labor market flexibility. Disputes are likely to increase as a consequence even as labor feels the heat. Disputes resolution needs to be strengthened for the sake of the vulnerable employee and for the survival of organizations which provide livelihoods for the employed. What are the changes which can create a fair industrial relations disputes resolution system is the question before us.

#### **Disputes Resolution Practices: Current Scenario**

The Industrial Disputes Act 1947 prescribes a multi stage structure for resolution of disputes:

Level I: Works Committees to address and deal with issues on an ongoing basis in a proactive and participative manner.

Level II: When a collective of workers feels aggrieved and negotiations with management fails, can resort to a strike by giving a strike notice as per the provisions of the Act or conversely management can declare a lockout when it apprehends threat to the firm's assets or personnel. The provisions related to strikes or lockouts as a means of disputes resolution are as follows:

- A notice of strike or lockout is to be issued and from the date of issue of the notice, the notice is valid for 6 weeks.
- The strike can commence only after 14 days of the date of issue of the strike notice
- A strike or lockout during the pendency of conciliation or arbitration or adjudication proceedings would be declared illegal with the attendant consequences in respect of employees like the initiation of disciplinary proceedings under the Industrial Employment Standing Orders Act (1946) which may lead to dismissal and the imposition of the "no work, no pay" principle for a period equivalent to the duration of the illegal strike.

Level III: On receipt of the notice of strike or lockout, the appropriate government – state or Centre depending on jurisdiction – initiates conciliation proceed-

ings by appointing a Conciliation Officer to negotiate with the parties and try and help the parties to find a solution as per the provisions of the Act towards a settlement. Conciliation is mandatory in "public utilities" and recommended in non-public utilities although generally conciliation is initiated even in such cases. Any organization is deemed to be a public utility if it is notified as a public utility by appropriate government.

Level IV: If conciliation fails, there are three possibilities – the appropriate government can refrain from further action, or make a reference of the dispute either to arbitration proceedings or to the Labor Courts for adjudication proceedings. If the appropriate government refrains from further action, the ball is back in management-employee court for either negotiating an agreement amicably or engaged in a contest of wills through a prolonged strike or lockout till either party blinks.

Level V: If reference is made for arbitration as per the provisions of the Act subject to the consent of both parties, the dispute goes through arbitration proceedings towards an award.

Level VI: If reference is made to the Labor Court, the disputes go through adjudication proceedings with provision for appeals by either of the aggrieved parties through a single judge and then a Bench of the High Court on to the Supreme Court for a decade or more of litigated resolution of the dispute with all the attendant delays, costs and consequences. Labor courts have original jurisdiction only in termination cases.

The praxis of industrial relations disputes resolution system seems to be oriented to containment of the disputants as well as the dispute rather than inclined towards a purposeful deliverability of sustainable solutions within the framework of legality, constitutionality and mutuality within a specified, reasonable time frame. There is also the tendency to use the elements of the resolution processes to stall and to obstruct rather than to move towards a legally, constitutionally and substantively sustainable conclusion. Once disputes get into the statutory processes, they meander around interminably with negative work life and livelihood consequences for the more vulnerable among the employee categories with mounting frustration and anger among the marginalized leading to untoward and avoidable incidents.

If disputes are inevitable in industrial relations irrespective of whether the current laws are amended or not, and if deliverability of sustainable solutions informed by skill and speed is the goal, the current arrangements are woefully lacking. If disputes resolution is to be given an identity and character, and the focus is on legally, constitutionally and substantively sustainable deliverability, bringing about changes in the disputes resolution machinery becomes a categorical imperative.

### **Fair & Speedy Disputes Resolution**

The first change proposed is to replace the Works Committee with an Organizational Ombudperson or Ombuds

Committee which is representative, impartial, independent to deal with employee grievances and disputes internally, amicably and honorably. The composition could consist of a management representative, a trade union or an elected worker representative and a neutral third party acceptable to both parties as Convenor. The Ombuds Committee should be effective enough to find solutions through an iterative and interactive process with the main parties to the dispute within specified time frames.

**The Ombuds Committee should be effective enough to find solutions through an iterative and interactive process.**

The second change can be by making a strategic shift from government run disputes resolution machinery to a professionally run disputes resolution machinery within the framework of “minimum government, maximum governance”. This will call for deregulation of the disputes resolution processes especially with reference to the conciliation machinery. This will mean conciliation services to deal with industrial relations disputes will be offered both by government and professional service organizations, will have the same powers as they have now and will be fee based. Accreditation and registration systems can be developed to have a choice of recognized conciliation and mediation services on offer for disputants. Disputants can approach whichever agency they see as capable of independent, impartial solu-

tions deliverability in the shortest possible time at reasonable cost and within a framework of purposeful mutuality. This will also open up employment possibilities for disputes resolution professionals skilled and experienced in this field and professionalize disputes resolution.

The third change relates to the power of reference of appropriate government to labor courts and industrial tribunals if conciliation or mediation fails. More often than not the power of reference has been used to curb strikes and lockouts rather than to resolve disputes. It is for the disputants to decide if they wish to seek justice from the courts or not and to weigh the costs and benefits of litigation over a conciliated or mediated resolution of the dispute or through strikes and lockouts. Labor courts should also be primarily oriented to get labor and management to resolve disputes through conciliation processes. The feasibility for labor courts to be given original jurisdiction (currently available only in termination cases) should be explored so that any aggrieved party – individual employee, a group of employees, a trade union, an individual employer, a group of employers or an association of employers can approach the labor court with provision for appeals to the High Court and Supreme Court as may be necessary or permissible as the contending disputants move towards a resolution of their dispute. This will give protection to aggrieved individual employees to seek justice in the context of non-unionized or even unionized settings. The possibility of litigation or direct action as a choice available to individual or collective dis-

putants might act as a check and also serve as a leverage to seek resolution through conciliation and mediation from the reinforced services available with both government as well as non-government professional conciliation agencies.

The current practice of using conciliation as well as the power of reference to curb strikes and lockouts and not so much to find conciliated solutions through professional, independent and impartial services needs a rethink. This conclusion is based on the current provisions of law related to strikes and lockouts in the Industrial Disputes Act 1947 wherein the restrictions on strikes and lockouts described earlier only have to do with making a determination on whether the strike or lockout is legal or illegal with the penalties associated with engaging in an illegal strike or lockout activity. The provisions of law only spell out the penalties which can be imposed when a strike is declared illegal but by themselves they do not prevent a strike or a lockout from taking place. The calling of a strike in the pursuit of dispute resolution by a union or collective of workers is a function of collectively mobilized power and perceived ability to sustain the withdrawal of labor long enough to get managements to the negotiating table and to negotiate a resolution. The current practice of using conciliation and the power of reference as restrictions on strikes is only adding to the low credibility of concilia-

**By themselves they do not prevent a strike or a lockout from taking place.**



tion as a disputes resolution mechanism, which in industrial relations circles is considered just a “waiting room” before the dispute is referred to adjudication. While the provisions related to giving a strike notice before going on a strike and the specification of a strike date may be retained, the provisions prohibiting strikes during the pendency of conciliation should be repealed in order to give conciliation a fighting chance as a disputes resolution mechanism. The prospect of prolonged litigation or direct action should impel management and labor towards reinforced and professional conciliation and mediation services. The reforms related to disputes resolution therefore should be geared towards strengthening the ombuds committee and the conciliation alternative as the key instruments of fair and speedy solutions deliverability through relevant amendments to the Industrial Disputes Act 1947.

### **Conciliation Services & Conciliator Competencies**

The challenge of recasting the disputes resolution identity with Ombuds committees and Conciliation can be met only through the enhancement of capabilities and competencies rather than by succumbing to the clamor for the expansion of the statutory powers and authority of the conciliator. Based on our interactions with Central Conciliators, our informed and considered view is that the following competencies are necessary to fulfill their roles with credibility and professionalism:

1. *Interpretative Understanding of Labor Laws Towards Disputes*

*Resolution:* This skill calls for not only understanding labor laws which fall within their jurisdiction but also to be able to interpret the laws in specific disputes contexts while trying to get the disputing parties to move towards sustainable agreements and settlements. The higher order competency is the ability to interpret law in the context of disputes which may arise in the industrial relations context to ensure legality and constitutionality while seeking resolution of the substantive issues.

2. *Multiple Stakeholder Orientation:*

Invariably, the practice of industrial relations is characterized by multiple stakeholders engaging each other on a roller coaster cooperation-conflict continuum. Different stakeholders dealing with the issues on the table bring different perceptions and interpretations which may often make the situation appear intractable to the uninitiated. For the seasoned conciliator, the challenge is to see the issues on the table through the eyes of the interacting stakeholders and to try and steer their expectations into a zone of workable agreements by helping them to recognize areas of congruence and divergence through a process of iterative engagement.

3. *Solutions Generation Capability:*

Disputes in the industrial relations arena are often characterized by rigid bargaining positions and partisan posturing. Ruthless power play featuring a fruitless exercise of blaming and point scoring vitiates relationships and stakeholder com-

munications. In this context the ability to help disputants to see beyond the game playing and getting them to move towards a reasonably sustainable agreement is best served by the ability to generate creative solution propositions. The more the solution propositions generated the greater the possibility of getting the disputants to the dotted line. This is possible only if the conciliator can see beyond the partisan perceptions and conflicting expectations and visualize solution propositions which can lead to sustainable outcomes informed by legality and constitutionality.

4. *Self-Confident Serenity*: Disputes in the industrial relations space are informed by atmospherics and theatrics. The conciliator needs to guard against misinformation and misrepresentation by one or more of the disputing parties. Verbal abuse and physical threats, allegations and accusations are all inextricable components of industrial relations disputes. The ability to be able to maintain one's composure whatever the provocation and the capacity for verbal dexterity in the midst of verbal violence can go a long way in gaining respect and staying in control of the situation whatever the ultimate outcome.
5. *Professional Relationship Building Skills*: Conciliators in today's environments face greater danger of collusive or opportunistic relationship orientations in their engagements with disputing parties. A collusive approach to relationships involves swinging towards one or other of the disputing parties for personal gain or to avoid personal loss with little sensitivity to conflict of interest considerations. An opportunistic relationship orientation operates on the basis of expediency and instant gratification. A professional relationship orientation is always conscious of one's role as a conciliator wherein one is part of the disputes resolution process and yet not part of the dispute. The challenge is to maintain that equilibrium day in and day out in the midst of playing out one's role – a state of mind which can best be described as one of detached engagement.
6. *Integrity based Credibility*: The greatest danger in today's opportunistic environment is to surrender integrity based credibility to the lure of illicit gain and instant gratification. In a context of corruption and bribery, abuse of power and misuse of statutory authority, adopting a policy of unflinching and unyielding integrity is a rare standard of professional behavior. Conciliation without credibility is like a body without a soul and is essential for long term effectiveness as conciliators
7. *Resilience*: Given the nature of the conciliation process and considering that the process is based on disputant voluntarism and the disputant commitment to speedy resolution, setbacks and failures are intrinsic to the process. To be a great conciliator calls for great resilience in the

wake of hostile posturing, rigid positional bargaining and raw power play especially by the more powerful disputants. The ability to stay the course with persistence and patience are vital qualities for the conciliator.

8. *Transactional Impartiality*: Very often, stakeholders engaged in industrial relations disputes perceive conciliators to be biased in their dealings— epithets like pro labor or pro employer are often heard in industrial relations circles. Few conciliators earn the respect of stakeholders on both sides of the fence on grounds of transactional and relational impartiality, independence, fair play and purposefulness. The ability to be respectful to all and partial to none while being intensely engaged with the stakeholders in order to try and move them towards a sustainable settlement is a daunting task but critical to the long term effectiveness and efficiency of conciliators

Besides these competencies, conciliators also need to expend efforts in “perspective building” in order to understand better the changing context of conciliation processes and the attendant need for conciliation professionals to become more aware of the dynamics underlying industrial relations today. Some of the elements in the perspective building framework are as follows:

- Developing a critical understanding of the contemporary economic and business environments in order to better appreciate the challenges and opportunities confronting conciliation

professionals. A deeper understanding of the thinking behind modern commercial businesses with their unwavering focus on profit maximization and the impact such a focus has on workers, consumers and the ecological environment can help in situating the conciliator role dynamics, pressures and challenges.

- Gaining a better understanding of the impact of the neo liberal ideologies and free market orientations on the industrial relations institutions like legislative bodies, labor ministries and functionaries, workers and trade unions, legal provisions and compliance pressures, collective bargaining and settlement processes, disputes resolution and adjudication processes.
- Within the above context, while acknowledging the legal acumen of the conciliators born of long years of experience in their multifaceted roles as regulators and enforcers, there is also need to look at the conciliator role and to recognize that there is a need to focus on one single skill which could make or mar the compliance and conciliatory role of the commissioners – the skill of negotiating - to move the interacting employers, employees and unions individually and collectively towards better processes, better relationships and better outcomes.
- Need to realize that business “utilitarianism” driven by shareholder centric profit maximization has to be countered with the normative infusion

of legal and constitutional standards within the conciliator jurisdiction considering that even compliance with law is seen purely in cost benefit terms by business in a market driven economy

- Need to uphold legal and constitutional rights of individual and organized labor even as the conciliator steers the disputants towards a sustainable outcome.

The perspective building approach should move away from an overly legalistic approach towards a skill based approach. Legal acumen is necessary in understanding and applying law in a creative manner to industrial relations situations, but what is needed in today's dynamic and volatile environment in which market dynamics dominates discourse, is the ability to influence interacting industrial relations solutions through astute and enhanced conciliator capability. Speedy disposal will only come through skilled handling of multiple stakeholders and their conflicting and congruent interests. Solutions generation creativity comes through human and social sensitivity.

As long as there are employers and employees and a contract of employment, there will be disputes and the direction of reforms as well as the industrial relations experiences of the recent past suggest higher workplace volatility and hence the need for systems for speedy and skillful resolution of disputes in a fair and just manner. Utilitarian Reforms oriented to unitarist restoration of managerial prerogative are contra indicated with the democratic ethos of the constitution-

ally constructed industrial relations disputes resolution system in India. Managerial prerogative can manage resources but the democratic dividend unleashes resourcefulness through connectedness and relatedness. It is the clash of the anti-thesis with the thesis which produces a higher order synthesis – this is the law of higher order change.

Strikes and lockouts, conciliation, arbitration and adjudication are options available to resolve disputes. Credible Ombuds Committees and competent conciliation can still hold its own provided Ombuds Committee professionals and conciliation services have the right competencies and the right perspectives to deploy the competencies for facilitated disputes resolution processes, while it is incumbent on disputants to work towards strengthening the ecosystem for conciliated settlements as opposed to resolving disputes through other available methods.

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**By Invitation**

## **Reforming the Industrial Dispute & Trade Union Acts**

**Tushar Poddar**

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*This paper looks at how labor laws in India may have slowed down employment growth. It estimates how much growth is being foregone due to the lack of labor mobility from agriculture to industry. It then focuses on Industrial Disputes Act and Trade Unions Act. The paper discusses specific provisions which may have negatively impacted employment growth, including the provisions for employment termination in India, requiring the permission of the government and consultations with trade unions. It examines how they need to be reformed, by looking at lessons from within India and other countries. Finally, it examines the case of Korea as a success story in generating labor-intensive manufacturing growth.*

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### **Introduction**

India's employment growth in recent years has been anemic. The economy added only about 2 million jobs each year in FY05-FY12, compared to 12 million a year in the five years before that. Moreover, increasing numbers of workers are leaving the workforce – the labor force participation rate fell by 3 percentage points over the same period. As a labor-abundant country, India should be generating jobs in labor-intensive manufacturing. However, the manufacturing sector saw a net decline of 5 million jobs in FY05-FY10 at a time when industrial growth was very strong at over 9% during this period. The industries that are losing jobs are in the most labor-intensive sectors – textiles, electronics, and apparel. Firms are substituting capital for labor.

This paper begins by looking at structural problems in India's labor market, and how they have hindered employment. We estimate how much growth is being foregone due to the lack of movement of surplus labor from agriculture to industry. We then focus on labor laws – two in particular that we believe could reap large dividends if they are reformed. We look at labor laws in other countries in order

to distill lessons from how those labor laws have been revised. We conclude by looking at employment growth examples from some of the more successful manufacturing countries in Asia, Korea in particular.

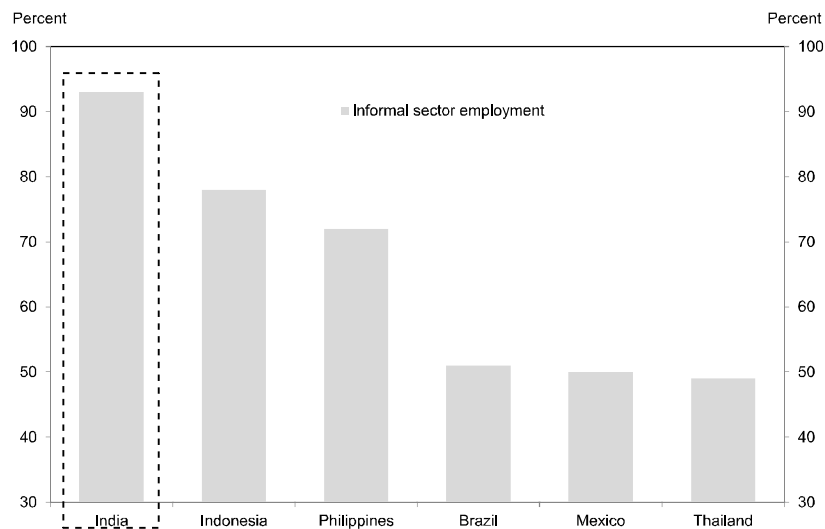
### The Labor Problem

In theory, India can realize significant labor market gains from its favorable demographics due to: 1) increases in labor input from the young; 2) economies of scale in operation – as a firm grows, it can initially have increasing returns to scale – whereby adding more labor and other inputs leads to a more than proportional increase in output; and 3) urbanization – moving labor from low-productivity agriculture to high-productivity industry and services.

**Employment growth has been anemic, and this is reducing the gains from labor input from the young.**

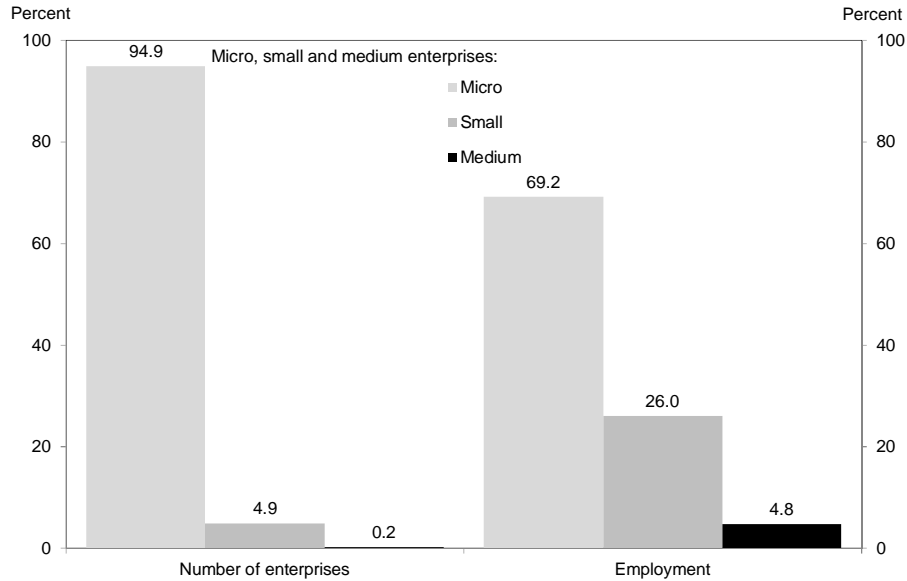
In practice, the gains have been much smaller than they could have been. Employment growth has been anemic, as discussed above, and this is reducing the gains from labor input from the young. India's employment profile is remarkable for its small scale and informality. To escape stringent laws, entrepreneurs keep the scale of their operations small. Most workers are in small enterprises, with their share in enterprises employing less than six people at 65.6%. Self-employed workers constitute half the workforce.

**Exhibit 1 Informal employment is highest in India**



Source: Planning Commission (2013): *Twelfth Five Year Plan (2012-2017)*, Volume III, 22. Employment and Skill Development

**Exhibit 2 Scale of employment is very small**



Source: Fourth All India Census of Micro, Small and Medium Enterprises, 2006-07: Registered Sector; Planning Commission, 12th Five Year Plan Draft

According to research by the World Bank, the value added per worker in the informal sector is less than half of the value added per worker in the formal sector. Further, employers have no incentive to invest in skills of contractual workers or in providing insurance.

**Complex labor laws incentivize firms to remain small and stay in the informal sector.**

Complex labor laws incentivize firms to remain small and stay in the informal sector. This allows them to remain under the radar of labor officials and escape stringent provisions. The large number of laws leads to inspection visits by different officials under different laws, which increases transaction costs and opens up

opportunities for rent-seeking. There is also no standardization of documentation required or time periods for which records have to be kept. The inflexibility of labor laws has prevented large-scale employment growth in manufacturing. Moving workers from the informal to the formal sector can unleash productivity growth. In addition, formal workers in the formal sector pay taxes, so revenue collections can rise.

Labor mobility has also been hampered, as labor laws have reduced the demand for manufacturing labor. We use a simple framework to estimate the impact of labor mobility on growth rates. We broke down GDP growth into three components: 1) the contribution from sectoral increases in labor productivity, suitably weighted by the sector's share



of GDP; 2) the contribution from growth in the labor force in the sector, in the absence of labor mobility, again weighted by the sector's share of GDP; and 3) the impact on GDP growth from inter-sectoral labor mobility, in the presence of differences in sectoral labor productivity levels.

These are summarized in the equation (1) below:

$$g = S^A \pi^A + S^I \pi^I + (1 - S^A - S^I) \pi^S \\ + S^A n^A + S^I n^I + (1 - S^A - S^I) n^S \\ + (l^A \times \frac{\Pi^I - \Pi^A}{\Pi} \times m^{AI}) + (l^A \times \frac{\Pi^S - \Pi^A}{\Pi} \times m^{AS}) + (l^I \times \frac{\Pi^S - \Pi^I}{\Pi} \times m^{IS})$$

where:

superscript A stands for agriculture, I stands for industry, S stands for services.

g: GDP growth

s: share of a sector in GDP

n: natural rate of growth of labor force in the sector

l: share of a sector in total employment

$\Pi$ : level of labor productivity

$\pi$ : growth rate of labor productivity

m: the net movement of labor between sectors (e.g.,  $m^{AS}$  stands for labor movement from agricultural to industry).

The contribution of inter-sectoral labor mobility on overall GDP growth is represented by:

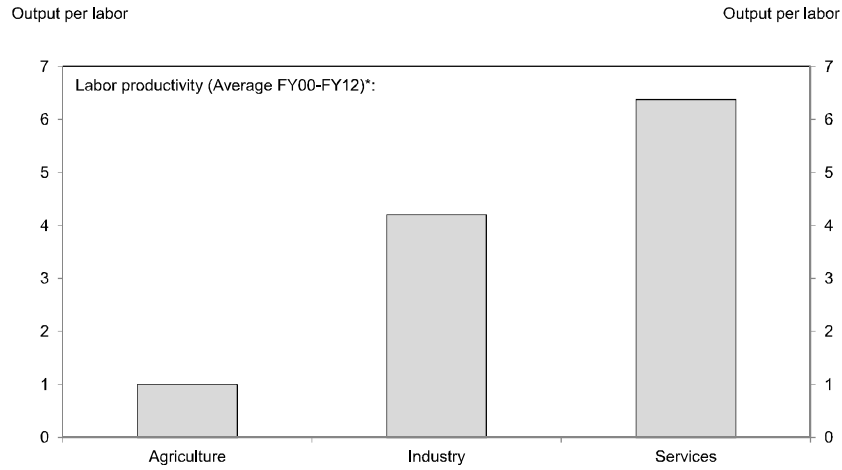
$$(l^A \times \frac{\Pi^I - \Pi^A}{\Pi} \times m^{AI}) + (l^A \times \frac{\Pi^S - \Pi^A}{\Pi} \times m^{AS}) + (l^I \times \frac{\Pi^S - \Pi^I}{\Pi} \times m^{IS}) \quad (2)$$

We find that labor is four times more productive in industry and six times more productive in services compared to agriculture (Exhibit 3). We measured the impact on GDP of urbanization by looking at productivity differences between agriculture and the manufacturing and services sector. We find that in recent years the increase in GDP due to the shift from rural to urban areas has not increased significantly. The increase in GDP from the migration of workers from agriculture to other sectors was 0.87 percentage points of GDP, according to our estimates, in FY05-FY12. This was not significantly higher than the contribution of migration in FY00-FY05 of 0.73 percentage points of GDP. Moreover, the contribution of moving from agriculture to industry has actually fallen over this period. Compare this with China, where we estimate urbanization is contributing 2-3 percentage points to GDP growth.

### The Straitjacket of Labor Laws

India has some 44 labor laws, which are enacted by the Central Government and enforced by both the Central as well as state governments. In addition, there are also labor laws enacted and enforced by the various state governments. Some laws date from the colonial era. The Trade Unions Act is from 1926, the Workmen's Compensation Act is from 1923, and the Factories Act is from 1948. We focus on two acts in particular, that

**Exhibit 3 Labor is much more productive in industry & services compared to agriculture**



\*Industry and services productivity is expressed as a proportion of productivity in agriculture.

Source: “India: Adding 110 million jobs”, *Goldman Sachs Asia Economics Analyst (2014)*, Issue No: 14/13

have some of the most restrictive provisions and where we believe labor reforms can have the largest impact on manufacturing employment and growth.

**The Industrial Disputes Act (1947)**

The law deals with the firing of workers, strikes, and the closure of firms. We believe this law has done more to hold back the growth of India’s manufacturing sector than any other policy. It keeps most of the labor force in the informal sector, primarily in temporary jobs, preventing employers from investing in their training.

We believe the most consequential part of the Industrial Disputes Act is Chapter Vb, which deals with special provisions relating to lay-off, retrenchment and closure in certain establishments. This chapter is applicable to all firms that

have more than 100 workers. “Lay-offs” denote being out of work temporarily, though still remaining on the employer’s payroll, while “retrenchment” implies permanent loss of job.

Sections 25M and 25N deal with procedures to be followed for lay-offs and retrenchment, respectively. Under both sections, the prior permission of the government is required on an application made in this regard. For retrenchment, the workman has to be given three months’ notice in writing indicating the reasons for the retrenchment. Importantly, the government consults with the workman before giving permission: “The appropriate government, after making such enquiry as it thinks fit and after giving a reasonable opportunity of being heard to the employer, the workmen concerned and the person interested in such retrenchment, may, having regard to the

genuineness and adequacy of the reasons stated by the employer, the interests of the workmen and all other relevant factors, ...grant or refuse to grant such permission...”

Section 25O deals with the procedure for closing down an undertaking. The employer has to apply for permission at least 90 days before the date of closure. Workmen are entitled to receive compensation equivalent to 15 days’ average pay for every year of service.

Section 25Q of the Industrial Disputes Act lays out the penalty for lay-off and retrenchment without previous permission: “Any employer, who contravenes the provisions of section 25M section 25N shall be punishable with imprisonment for a term which may extend to one month, or with fine which may extend to one thousand rupees, or with both.”

Section 25R, which deals with penalty for closure, argues that any employer that closes down an undertaking without complying with the procedure of getting permission from the government shall be punishable with imprisonment for a term that may extend to six months or with a fine that may extend to five thousand rupees, or with both.

In addition, there is Section 25G on procedure for retrenchment: “the employer shall ordinarily retrench the workman who was the last person to be employed in this category.” The principle followed is last come, first go. There is no consideration of merit.

**A factory job is not a voluntary contract between an individual and an employer, but a tri-partite arrangement with the government.**

A factory job is not a voluntary contract between an individual and an employer, but a tri-partite arrangement with the government.

These provisions, which have seen some more pro-worker amendments by the states, essentially mean that the government is involved with every lay-off and retrenchment of workers. A factory job is not a voluntary contract between an individual and an employer, but a tri-partite arrangement with the government. Moreover, whenever a worker needs to be fired, the government would consult with the workers and their representatives, thereby bringing in the approval of the trade unions in the case. As a result, Indian employers looking to lay-off or retrench workers are presumed to be acting improperly until they can prove otherwise. India stands virtually alone among countries in having such stringent norms for employment termination. This sort of government permission is not required in any developed country and almost none of the emerging markets requires the permission of the government and consultations with trade unions. Even countries with restrictive labor regulations (for example, Bangladesh, Philippines, and Malaysia), do not require consultation and approval from trade unions.

There are few, if any, countries that require government permission to fire

workers. In China, to dismiss a worker does not require prior authorization from the government though the labor administration must be informed. In Malaysia, the courts do not interfere with the employers' decision to retrench workers provided the decision is bona fide and not taken to victimize the employee.

### **Comparing Gujarat & West Bengal**

An interesting case study is a comparison between Gujarat and West Bengal on state amendments to the Industrial Disputes Act. The Gujarat government amended the Industrial Disputes Act in 2004 to allow for greater flexibility in the labor market for Special Economic Zones (SEZ). It allowed firms within the SEZ to lay off workers, without seeking the permission of the government, by simply giving one month's notice to the worker. To allow for firm exit, the law was amended such that the employer can close an undertaking by giving two months' notice to the government. Contrast this with the normal legal requirement of getting permission from the government, with the latter giving an opportunity for the employees to be heard on the issue. The Gujarat Act 12 changed the definition of "industrial dispute" to exclude the termination of service of an employee in an SEZ, thereby significantly reducing the scope for litigation.

The West Bengal Government, in contrast, made several pro-worker changes. The IDA was amended to be applicable to more firms – those employing above 50 workers. It changed the laws to make it virtually impossible to

shut down a loss-making factory. The employer with the application for closure must contain the particulars of the quantum, mode, manner and time of payment of compensation to the workmen. The owner is also required to furnish a guarantee to discharge liability for payment of compensation to the workmen. Most factory owners thus prefer to keep their loss-making units barely viable, but strip their assets. Not only this, the West Bengal amendment says that where an application for closing down an undertaking is made, the appropriate government may issue such directions as may be necessary for maintaining normalcy and continuity of work during the notice period. This allows the government to keep a loss-making enterprise afloat even after the employers are unable to do so. This prevents the churn of capital and labor, which is at the heart of modern enterprise.

The results are quite clear-cut. While Gujarat saw a 60% growth in manufacturing employment in 2000-2012, West Bengal saw only a 22% increase.

**There is a strong case for adopting an entirely new law to govern industrial relations.**

Given the issues detailed above, and considering that the Industrial Disputes Act dates back to 1947, we believe there is a strong case for adopting an entirely new law to govern industrial relations. Due to several state amendments over the decades, the law has become unwieldy, apart from the strict measures

mentioned above, which we believe are clearly in need of revision. However, a new law may take several years in order to get a consensus among the states. In the meantime, the Gujarat amendment shows one way forward. The most stringent conditions, especially regarding retrenchment, may be excluded for the SEZs. This would allow these zones to be havens of employment and allow market forces to work in the labor market. With the government no longer involved in every employment decision, employers would be encouraged to increase formal employment and expand manufacturing, thereby taking advantage of economies of scale and investing more in the training of their workers.

### **The Trade Unions Act (1926)**

We believe there are at least three key aspects of this act that merit retooling. First, the act allows for a multiplicity of trade unions. The Trade Unions Act stipulates that any seven or more workers can form a trade union and apply for registration. Further amendments allow the formation of at least ten unions in an establishment with a size of 70 workers. This means multiple trade unions in an establishment, which can reduce harmony, increase conflict, and promote competition between them.

Second, members enjoy immunity from criminal and civil liability when furthering the interests of the trade union. This immunity allows them to call strikes, which can hinder the smooth functioning of industrial units. This includes breaching terms of the employment contract.

Third, the law provides the scope for outsiders to the tune of 50% of the office bearers. This is undesirable as it opens the door to outsiders who can capture the unions and may not have the interest of firm employees as their priority.

It is instructive to see how other countries have reduced the role of trade unions. Bangladesh reformed its labor laws in 2006 and now requires a minimum membership of 30% of workers to form a trade union. In Sri Lanka, at least 40% of workers on whose behalf the trade union seeks to bargain with the employer should be members of such a trade union. In Pakistan, 20% of workmen should be members of a union to be entitled for registration. However, for collective bargaining, the union with at least one-third of workers employed in an establishment will be eligible for collective bargaining.

**The union with at least one-third of workers employed in an establishment will be eligible for collective bargaining.**

In the US, to curtail the power of unions, the Taft-Hartley Act was passed in 1947. It declared closed shops as illegal. A closed shop is where the employer agrees to hire only union members and an employee who resigns from the union must be dismissed. The act forbade strikes in order to assign particular work to the employees. For a strike or lay-off, an 80-day notice had to be given by either side. Further, the president could

obtain an 80-day injunction to stop the continuation of a strike. This has been used often by US presidents to forestall industrial strikes. The act strengthened the employees' rights relative to the established union in several ways, including that an employee's membership of an established union is not required for him to work. The landmark act helped correct the balance in industrial relations and led to reduced industrial action and strikes as the US economy entered its historic post-war economic expansion.

In the UK, Margaret Thatcher's Government passed six pieces of legislation in 1980-1993 to reduce union bargaining power. Initially, the permissible grounds to refuse to join a union were extended. The definition of a trade dispute was narrowed to cover only disputes between workers and their employer, and the applicability of unions' immunity for civil and criminal liability was reduced. Inter-union disputes and all others lost immunity. Unions became financially liable to employers by unlawful industrial action. Industrial action outside the authorized terms could lead to the union being sued for damages and result in injunctions being granted against the union. Contracts specifying that only union labor was to be employed were outlawed. All unions were required to ballot members before engaging in industrial action. Absent such a ballot, the union automatically lost immunity and could be sued for breach of contract. Individual union members had the right to take their union to court when industrial action had not been the sub-

ject of a lawful ballot. Further, union members could not be disciplined for failing to participate in a strike. These pieces of legislation changed the nature of industrial relations in the UK, and they were followed by a period of strong economic growth and job creation.

**These pieces of legislation changed the nature of industrial relations in the UK, and they were followed by a period of strong economic growth and job creation.**

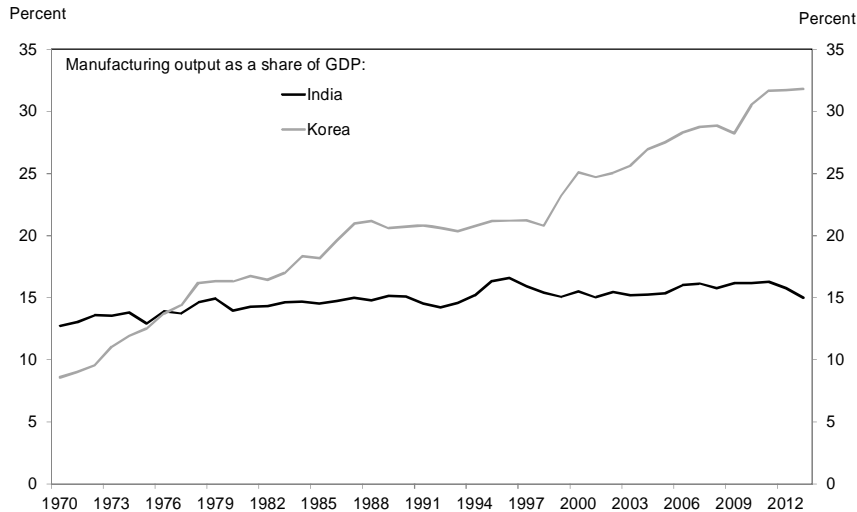
Given how outdated the Trade Unions Act has become, there is a clear need to overhaul to act to make it more applicable to the modern era. Legislation in the US and particularly the UK provide examples of how this can be done with sufficient political will. A modern act could promote better relations between employers and unions, encourage greater formal sector employment and economies of scale, and lead to less conflict.

### **Lessons from Korea**

India has one of the lowest shares of manufacturing in GDP in Asia, at about 15%. An interesting comparison is with Korea, which has one of the highest shares of manufacturing in output at over 30%. India and Korea's share of manufacturing in output was similar until the early 1970s at about 14% of GDP. However, the trajectory since then has diverged dramatically. While Korea's share of manufacturing in GDP has acceler-

ated, India's share has stagnated at about 15%. Korea's per-capita income was 2.5 times that of India's in the early 1950s. Today it stands at eight times.

**Exhibit 4 India and Korea manufacturing as a share of GDP has diverged since the 1970s**



Source: "How India can become the next Korea", *Goldman Sachs Asia Economics Analyst (2014)*, Issue No: 14/15

Korea's labor laws during 1970s-1990s were liberal, allowing considerable flexibility in employment decisions. Until the mid-1970s, Korea's labor markets were in a state of permanent excess labor supply on rapid urbanization and demographic tailwinds. About 3% of the population was aged over 65 years in 1970 compared to 11% in 2010, with the working age population growing at around 3% per annum in the 1970s. Against this backdrop, labor regulations focused on job creation and training, and the formation and activities of labor unions were restricted until the late 1980s, especially for foreign-invested companies. The minimum wage was introduced only in 1988, and Korea did not join the ILO until 1991.

Korea's manufacturing growth began with labor-intensive industries. In 1970, the main export items were textiles, plywood and wigs, representing 40%, 11% and 11% respectively. Given that these are labor-intensive sectors, exports drove job creation. The main items changed to garments, steel plate, and footwear in 1980. Garments remained the top export item in 1990, with a 12% share but followed by semiconductors, footwear and TVs. By 2000, however, the top export items were transformed to capital-intensive items; the top five items were semiconductors, computers, automobiles, petroleum products, and ships. Industrial sectors, of which most are manufacturing, have stopped adding to their share of total employment since the peak of 28.5% in 1988.

The experience of other success stories in manufacturing in the region is similar. In China, in its high-growth phase starting from 1998, computers, electronics, electrical machinery, and textiles added the most jobs in manufacturing. Similarly, Taiwan saw similar increases in computers, electronics, electric parts, and leather products from the 1970s. Thus, in the initial growth phase, the labor-intensive sectors see the most rapid growth. As growth gets more broad-based, more technology-based sectors become the key drivers of job creation. This provides valuable lessons for the sectoral composition of growth in India.

There is little doubt from the Asian examples that the initial phase of growth has to come from intensively using the factor that is the most abundant: labor. India's growth strategy has to rely on labor-intensive manufacturing, and to do that requires urgent attention on laws governing labor. India's labor laws are currently not geared to encourage large-scale labor-intensive manufacturing, and we believe the Industrial Disputes Act and the Trade Unions Act should be changed to make them more supportive of job creation. Such a retooling of India's labor laws would also be in line with the new government's stated priority of ensuring sufficient jobs for India's youth.

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**By Invitation**

## **Labour Law Reform in India**

**J.S. Sodhi**

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*There has been an all pervasive recognition that the country needs to reform its labor law regime. It has become counterproductive to the twin objectives of job creation and industrial peace and hurts the very people it meant to benefit. Successive governments failed to match their rhetoric with concrete action. The present government's intent of reform followed by selective swift action is a welcome departure from the past. Malaise of the labor laws is deep rooted and covers the broad spectrum of 44 Central and a large number of State laws. The paper, however, takes up the critical changes needed to make these laws less cumbersome and less rigid while keeping intact the legitimate rights of the workers.*

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### **Introduction**

Universally the power structure in the society has been and is weighed towards the haves and therefore, the weaker sections of the society need protection. India has been no exception. That was the primary motivation for organization of workers and formulation of labor laws by the governments across the world. In India, except for four decades 1950-90, the balance of power has remained with the employers. Since the 1990s, however, the state has been soft in implementing labor laws in its letter and spirit. It realizes that the labor law regime is out of sync with the realities of the economic environment and it has not been able to restore cordial industrial relations and peace.

Industrial relations had worsened during the last decade which witnessed managements' aggressiveness towards the workers and trade unions. They have been resisting formation of unions at the enterprise level and coercing the unions, wherever they exist, to terminate their political affiliations and insist on not to have outside leadership. Employment of contract labor has increased manifold much of which is in violation of the Contract Labor (Regulation & Abolition) Act,

1970. Such workers are paid much less wages compared to a permanent worker doing the same job and have no security of job (Sodhi-ILO, 2010).

**Government of India has also been an active player in the employment of contract labor in contravention of the Contract Labor Act.**

Strangely enough, Government of India has also been an active player in the employment of contract labor in contravention of the Contract Labor Act. In fact it is the largest employer of contract labor. The violation of other labor laws is happening under its very nose. Labor law enforcement in Export Promotion Zones is negligible. The position is similar in the IT sector. State governments like Kerala have passed orders restricting the functioning of trade unions. Haryana State Government had passed a similar order preventing its employees from going on strike.

### **The Legal Framework**

**There are 44 Central and a large number of State laws in the country.**

The country has plethora of labor laws. Since labor in India is on the concurrent list, the Central and the state governments are competent to enact legislation. There are 44 Central and a Large number of State laws in the country. The Central laws are categorized in to three viz: those enacted and enforced by the

Central Government (12 in number); those enacted by the Central and enforced both by the Central as well as the State governments (16 in number); and, those enacted and enforced by the various State governments which apply to respective states (16 in number). The most critical laws were enacted before or just after Independence (the Trade Union Act, 1926, Industrial Disputes Act, 1947, Workmen Compensation Act 1923, Payment of Wages Act 1936 and the Industrial Employment-Standing Orders-Act, 1948). Amongst others, majority were enacted 30 years back. Chronologically, sixteen of the forty four Central laws were enacted before or immediately after Independence, nine in the late 1950s and the 1960s, ten in the 1970s, six in 1980s, two each in the nineties and one in the last decade. (Annex 1)

### **Changing Labor Laws**

Obviously, the laws are too old. While the age of the law per se may not be an indicator of its relevance or otherwise, it is important to mention that liberalization and globalization, which began in the 1990s, had totally changed the economic paradigm in the country. The context in which these laws were enacted has, therefore, undergone a metamorphosis.

With these laws in the background, doing business in India is a cumbersome vocation particularly for an upright entrepreneur. The multifarious labor laws, with varying connotations and definitions, force the employer into submission to the labor inspectorate, multiple trade unions

and rigidities in which it cannot retrench any employee once employed (subject to the completion of 240 days of continuous work). The laws bind him to not even close the enterprise. Government permission is required to effect these changes.

**The object of formulating labor laws was laudable but the changing economic environment has made them outdated.**

The object of formulating labor laws was laudable but the changing economic environment has made them outdated. The malady is well recognized at the highest levels. The former Prime Minister Dr Manmohan Singh had repeatedly stated that labor laws needed to be changed. He had said (ILC 40<sup>th</sup> Session) “the process of doing business with India has to become less intimidating, less cumbersome and less bureaucratic to attract more investment. Many of the legacies of the past have not much relevance today. Indeed, some of them have become counterproductive today and may well be hurting the very people they are meant to benefit”. He further stated that the country needed new laws which provided safety standards catered to the basic needs of workers, took care of their welfare and were flexible enough to create rather than destroy jobs.

The plea for changes in the labor laws had gathered momentum with the present government’s commitment to create a conducive environment for investors and liberate the entrepreneurs from the tyranny of myriad labor laws. Equally im-

portant is the fact that India needs to create 80 million jobs during the next 10 years while at present it has created only two million jobs every year during 2005-12. Almost five million persons lost jobs in the labor intensive manufacturing like the textiles and apparels and electronics during 2005-10. According to Goldman Sachs, it is because firms are substituting capital for labor largely because of fear of coming into the ambit of a large number of labor laws.

Despite the felt need, the noise and commitment have almost never been followed through with any concrete action. The logic given for no major changes in the laws is that any change in Central legislation has to be approved by both houses of the Parliament and the States (labor is on the concurrent list) can bring in appropriate regulations given in the broad structure of labor laws (Panagariaya, 2014). The President of India has the constitutional authority to amend the laws as sent by the State governments under section 254 (2) of the Constitution. However, despite this, only states like Gujrat, Maharashtra, Andhra Pradesh and Rajasthan (proposed amendments), amongst others have addressed the issue to some extent.

Amendments have also been made during the last four years to the Central laws. The Employees Compensation Act (earlier known as Workmen’s Compensation Act) had been changed with respect to the wage ceiling limit, which was increased from Rs. 4000 to Rs 8000 per month for purpose of calculating compensation along with other minor changes;

Employee State Insurance Act, 1948 was amended to improve the quality of service under the scheme; the Plantation Labor Act, 1951 was amended to provide safety and occupational health care to plantation workers and the Industrial Disputes Act, 1947 was amended in 2010 to: amplify the term 'appropriate government' defined under section 2(a) of the Act; enhance the wage ceiling from Rs. 1600/- to Rs. 10000/- per month to cover workmen working in supervising capacity; provide direct access to workman to the labor court or tribunal in case of disputes arising out of Section 2 (a) of the Act; establish grievance redressal machinery; and, empower labor courts or Tribunals to execute Awards. Some of the proposed amendments are with various committees of the Parliament and at various stages of discussions.

#### **Amendments by State Governments**

Some of the state government's have been active in making amendments. For example, the Gujarat government had made changes allowing the SEZ's to lay off redundant workers without seeking the permission of the government. It mandated the SEZ's to give a formal notice, severance pay and a compensation of 45 days for a year of work rather than the 15 days given to other workers. It also allowed "Fixed Term Employment" under the Industrial Standing Order Act 1946 and Gujarat Rules 1955 which defines conditions of employment, Self consolidation-cum-consolidated Annual Return scheme; keeping a maximum of two inspection registers and, following the Supreme Court verdict, no pay for no work was also introduced.

The State of Rajasthan has recently proposed changes in the Industrial Disputes Act, 1947 to the effect that government permission will now not be required for retrenchment in companies employing up to 300 (up from 100 under the Central Act) workers. Other amendments relate to the change in the Factories Act regarding the applicability of the Contract Labor Act, 1970 to establishments by raising the limit of number of workers to 20 and 40 with or without power up from the present 10 and 20 workers. These amendments though have to be ratified by the President of India.

Andhra Pradesh government had made amendments in the Contract Labor Act, 1970 which were hailed as a model for other states to follow. It had introduced a clause restraining the employment of contract labor in core activities of any establishment if the same was prohibited by notification. However, wide ranging exemptions were made such as the normal functioning of the establishments such that the activity is ordinarily done through contractors; or the activities are such that they do not require full time workers for the major portion of the working hours in a day or for longer periods as the case may be; and any sudden increase of volume of work in the core activity which needs to be accomplished in a specified time. The amendments amply clarified the core activity meaning as any activity for which establishment is set up which includes any activity essential or necessary to the core activity with certain exceptions.

West Bengal government has turned the clock back in 2014 by making it virtually impossible to shut down a loss making factory. The law in the state applies to all establishments employing up to 60 workers.

It is argued that the States of Gujarat, Andhra Pradesh, Maharashtra and now Rajasthan have made meaningful amendments to labor laws of the country. Gujarat has been able to create more manufacturing jobs than other states, such as West Bengal & Kerala with restrictive labor laws. However, these forward looking changes have been done by a handful of states and are partial in nature. Moreover, the amendments relating to the Central laws have not addressed most of the core issues plaguing the labor laws.

Let us, for example, take up some core issues being discussed and debated in the context of labor law reform. These are: too many laws and their consolidation; anomalies and divergent definitions of the worker, establishment, wages etc.; employment of contract labor in activities longer than presently allowed; applicability of labor laws to companies with varying size & employment; labor administration and enforcement of labor laws or the inspector raj, dispute settlement; and rigidities of labor laws. The demand to remove rigidities has drawn the maximum attention and debate. Let us take it up first along with other issues related Acts.

### **ID Act 1947**

*Flexibility vs. Rigidity:* Flexibility debate in India has been mired in the

controversy of too much protection to the workers: lay off and retrenchment of the workers; and, the closure of the enterprise. The clauses state that an employer cannot layoff or retrench any worker or close down operations of the establishment without prior permission from the appropriate government. There is though a caveat that permission is deemed to have been granted by the appropriate government after 60 days if no communication is received by then.

This clause, according to employers and economists, has been a major bottleneck of employment generation in the organized sector. While total employment has increased during the last ten years, formal sector employment has been decreasing i.e., employment generation in smaller establishments (where no permission is required for lay off, retrenchment and closure) has been increasing faster than in other (those with 100 workers and above) establishments.

**While total employment has increased during the last ten years, formal sector employment has been decreasing.**

In view of these rigidities, the employers have been resorting to technology up gradation with the intention of keeping their workforce below 100. UNIDO's (2012) report in this context states that the clause relating to applicability of the ID Act has kept the Indian enterprises small. According to them, the

average number of workers in Indian firms in the organized sector is 75 (UNIDO, 2012), compared to 178 in Indonesia and 191 in China. The Government of India's Economic Survey (2012-13) stated that it could be due to the outdated labor laws.

It is also argued that India is among the very few countries where prior permission is required for lay off, retrenchment and closure. A comparison with other countries (Table 1) shows that such permission is required in India, Pakistan and Sri Lanka only. Such permission is not required in Bangladesh, China, Indonesia, Philippines, Malaysia, Thailand and Vietnam. In all countries of Europe, North America, and those in Africa, such a permission is not required. In China, Indonesia and Vietnam and most of the countries in Europe and Africa, only prior consultations are required with the trade unions. In UK, every employer must give a reasonable notice after one month of work for severance of employment and after two years of service, employers must provide a sufficiently fair reason of dismissal and redundancy payments.

The Government of India had set up many committees, including the Second National Commission on Labor (NCL, 2002) to look into the broad framework of labor laws including the ID Act and suggest changes. The NCL which had broad based consultations had suggested a fine balance between organizations' need and workers interest. It had suggested that prior permission may not be necessary in respect of layoff and re-

trenchment in an establishment of any size. It, however, suggested an enhancement of the notice period from one to two months and enhancement of retrenchment compensation from the present 30 to 45 days. For closure of the enterprise too the compensation (which is 30 to 60 day's salary depending upon whether it is a sick and ongoing industry with a view to become viable, nonprofit organization etc.) may be enhanced.

**Prior permission may not be necessary in respect of layoff and retrenchment in an establishment of any size.**

The issue and the prognosis appear simple and should be implemented. However, there is a huge question mark on the role and intentions of the employers while dealing with the issue. Many argue that the employer's attitude is just to get rid of the workers because of multifarious reasons not necessarily connected with the vagaries of business. Some of these are: permanent workers are drawing much higher salaries by virtue of the number of years of service and replacing them would reduce their wage costs substantially. Most of them are unionized and they do not submit to the whims of the employer; the process of legal suspension is very cumbersome even for the genuine delinquents. Senior age worker's skills and productivity are always a matter of concern. In any case the employer is happy to have a workforce whom they can hire and fire. Large scale employment of contract labor, much in contravention of the law, is a

**Table 1 Labor Laws Provisions Related to Consultations and Notifications Prior to Collective Dismissal: Comparison in Select Countries**

Country	Prior Consul- tations with trade unions re- quired	Notification to the public admin- is tration required	Notification to the workers' repre- -tative required	Approval by public admini- stration or judicial bodies required	Consent of workers' repre- -atives required	Employers obligations to consider alt ernatives to dismissal required
<b>ASIA</b>						
Bangladesh	No	Yes	Yes	No	No	No
China	Yes	Yes	Yes	No	No	Yes
India	Yes	Yes	Yes	Yes	Yes*	Yes
Indonesia	Yes	No	Yes	No	No	Yes
Pakistan	-	-	Yes	Yes	-	-
Philippines	No	Yes	No	No	No	No
Malaysia	No	Yes	No	No	No	No
Sri Lanka	No	Yes	No	Yes	No	No
Thailand	No	Yes	No	No	No	No
Vietnam	Yes	Yes	Yes	No	Yes	Yes
<b>EUROPE</b>						
France	Yes	Yes	Yes	No	No	Yes
Germany	Yes	Yes	Yes	No	No	Yes
Russia	Yes	Yes	Yes	No	No	Yes
UK	Yes	Yes	Yes	No	No	Yes
<b>NORTH AMERICA</b>						
USA	No	Yes	Yes	No	No	No
<b>FRICA</b>						
South Africa	Yes	No	Yes	No	No	Yes
Tanzania	Yes	No	Yes	No	No	Yes
Uganda	No	Yes	Yes	No	No	No

Source: International Labour Organisation (1947) cited in Exim Bank (2013)

\* Section 25N of ID Act states that the appropriate government or the specified authority may grant or refuse permission after giving a reasonable opportunity of being heard to the employer, the workmen, and the persons interested in such retrenchment, which implies that without the consent of the workers' union it would be difficult to get the permission granted.

point in this direction. It is, therefore, rightly feared that giving them the right to hire and fire would result in large scale unemployment in the organized sector with an adverse effect on working conditions of those (contract or casual workers) who will be hired.

Despite this, there is acceptance that no government permission may be re-

quired for lay-off, retrenchment and closure of the enterprise and required changes may be made in Chapter VA and VB of the ID Act. But given the attitude of a large section of the employers, it may be appropriate to make it justifiable (based on economic/business ups and downs which they should give in writing to the unions and have discussions with them). The retrenchment compensation

though must be high (at least 60 days of each year of completed service or number of years of service left whichever is less) including a notice period of two months may be statutorily fixed. This is to enable employers to achieve flexibility but in case of absolute necessity only. The issue of closure may also be dealt in a similar manner. It is well known that there are sick companies in India but not sick employers. In fact, many of them remain very rich and enjoy a lavish life style.

*Notice of Change:* Section 9A (item 11 of fourth schedule of ID Act) requires employer to give 21 days notice of change in workers conditions (with respect to change in technology, workload, manning, shift work etc). It has been forcefully argued that in today's context, it is a serious drawback on the functioning of day to day activities of the factory as many changes are to be implemented at a short notice. The employers have been demanding that this section should be completely deleted from the ID Act.

It is fair that no notice may be required and the amendment may be made after discussions with the unions on the legitimacy of the change.

*Dispute Settlement:* The ID Act sets a procedure for settling labor disputes through collective bargaining-- Section 18 (1), negotiation, conciliation-Section 18 (3) and mediation, voluntary arbitration (Section 10A), compulsory adjudication in labor court (Section 7) and industrial Tribunal (section 7A) and National Tribunals (Section 7B). Labor courts are

constituted by the appropriate government for the adjudication of industrial disputes relating to any other matter specified in the Second Schedule. Industrial tribunals likewise are constituted for the same purpose under the Second or the Third Schedule.

The ID Act's main objective was to contain dispute, promote cordial industrial relations and keep litigation to the minimum. However, experience has proved to the contrary. The major reasons have been: lack of trust between the employers and the unions/workers; lack of success of conciliation; legal provisions (section 2a and section 36 of the ID Act) permitting a worker or a union to raise a dispute any time after its occurrence; lack of faith in the arbitration process; the dilatory legal process which is favored by the employers; absence of a proper and statutory bi-partite forum (Works Committees have been defunct for a long time) to settle differences without the third party intervention; and above all employers' disinclination to settle the dispute as a majority of them are regarding the dismissal of the employees.

The solution lies in introducing multiple amendments of having competent conciliation officers (Sodhi & Guha, 2006), fixing a limit of one year for raising a dispute (Section 2A and Section 36), barring the unions below 15% of the representation and most importantly, bringing in amendment to statutorily promote bi-partite forums to settle disputes rather than depending upon a third party for the same. The country can take cue from the German Co-determination Model which



**The solution lies in introducing multiple amendments of having competent conciliation officers.**

has statutory bi-partite forums where most of the issues have to be resolved (Sodhi et.al, 1995).

Most of the disputes in the labor tribunals and courts relate to suspension and dismissal of the worker. There is a fair and a comprehensive mechanism of suspension and dismissal given in the ID Act. It is suggested that if the worker is dismissed after proper and fair enquiry on charges of violence, sabotage, assault, as well as insubordination of any kind, the matter may be deemed to have been sorted out at this stage itself and it should not be allowed to be escalated upwards as allowing the worker to raise this dispute at higher levels is tantamount to questioning of the process of suspension of the employee.

An amendment may be made here to broad base the representation of suspension and dismissal process by including one person of eminence in the existing process-an ombudsman type to allay the apprehensions of the unions and workers about the fairness of the process. The recommendation of the committee should be binding on both the parties on a broad based list of acts of misconduct which may be developed by the government. Similar process may be followed in other cases of differences including the grievance redressal machinery between the management and the workers/unions. No dispute under this list may be allowed to go

to the labor tribunals or court. In a few others (10-20% of the cases), if the dispute remains unresolved at the bi-partite level, it may be referred to conciliation and upon its failure to arbitration or adjudication with a directive that the legal process would be completed on a maximum of three hearings. This change may be brought about statutorily. This will, on the one hand, reduce the role of third party intervention and on the other, de-burden the courts leading to a speedy completion of the pending cases.

*Applicability of the Act:* The ID Act is applicable to every enterprise irrespective of the number of workers. However, Chapter VB of the Act is applicable to enterprises which are not seasonal or work is not performed intermittently employing more than 100 workers on an average per working day in the preceding 12 months. The applicability was reduced from 300 to 100 workers during the Emergency (1976). There has been intense debate on the restoration of the manpower threshold limit as according to some studies (Fallon & Lucas, 1993) the 1976 amendment of the ID Act 1947 reduced the demand for labor by 17.5%. The employers have also been arguing that this threshold limit should be restored. This change may be favorably considered.

### **Contract Labor (Regulation & Abolition) Act, 1970**

The Act allows employment of contract labor in a large number of activities which are considered peripheral in nature. It stipulates that such employment

should be provided through contractors who are expected to adhere to the legal obligations of employment of contract labor. The Act applies to every establishment in which 20 or more workmen are employed or were employed on any day of the preceding 12 months. It does not apply to establishments where the work is of intermittent nature. The Act applies to establishments of the government and local authorities as well.

The 'appropriate government' under section 10 (1) of the Act is authorized after consultation with the Central or State Boards to prohibit employment of contract labor in any establishment in any process operation or other work. Such restrictions are often decided on the basis of: whether the work is of perennial nature; whether the work is incidental or necessary for the work of an establishment; whether the work is sufficient to employ a considerable number of whole time workmen; and, whether the work is being done ordinarily through regular workmen in that establishment or a similar establishment.

The main purpose of the Act was to facilitate the employment of workmen in activities which are not perennial and do not form the core activity of the organization. However, the practice has been otherwise both by the government and other organizations. The reason given is the inflexibility of the existing labor laws. Also, employers' claim that in today's changing economic-environment, the distinction between the core and non-core does not exist. This belief by the employers has led to large scale employment of

contract labor, mostly in contravention of provisions of the Contract Labor Act.

Admittedly, the rigidities of labor laws and employers inability to regulate their workforce in high and lows of the demand is an important issue and organizations must have the flexibility to adjust work force to remain competitive. There are two sets of the policy changes which may be considered here. One, the recommendation that flexibility can be introduced by deleting Ch. VB and Section 9A of the ID Act as highlighted in the earlier part of the paper. If this amendment is made, contract labor should only be permitted as per the law in non-core activities and the appropriate government should strictly enforce their right to abolish them in activities which are core to the organization. Aberrations may invite serious penalties which need to be enhanced sufficiently.

**Contract labor should only be permitted as per the law in non-core activities.**

Two, in the absence of the suggested changes in the ID Act, the law should be renamed as Contract Labor Regulation Act and the word 'prohibition' may be removed. However, contract labor employment may be allowed in specified activities, the list of which may be decided through consultations. This should be done if the industry would employ them responsibly by paying wages suitably calibrated with the skill levels of the employees rather the minimum wages. Wages should be fixed in relation to the equivalence of the job in which per-

manent workers of a particular organization are engaged, the level of skills required for the job and years of experience of those being employed as a contract labor (Sodhi, 2013). Tripartite consensus on engagement of contract labor and payments as well as the working conditions must be created before Section 10 of the Act is deleted. An integral part of the amendment is the responsibility of the contractor and the aberrations inviting severe penalty on them.

Another possible approach in engagement of contract labor is the concept of 'Fixed Term Employment' under which employment is for a predetermined period and wages and allowances as well as statutory benefits would be similar to regular workers with such workers not having any right to regularization after completion of the term.

### **The Trade Union Act, 1926**

The Act and its many clauses have led to more confusion and problems than sorting them out. It gives the right to any seven persons to register a union but is silent on its recognition in the enterprise. The Act allows one-third of its leaders as outsiders. All this has led to multiplicity of unions, problems in recognition of unions and outside leadership (Section 16) which led to politically motivated leaders' interference in the affairs of the establishment.

The multiplicity of trade unions is abhorred by the employers and creates problems with respect to their recognition as a bargaining agent. Even countries like Bangladesh and Srilanka have enacted far reaching amendments to suit

the present competitive environment. For example, Bangladesh reformed its labor law and minimum membership of workers required for forming a trade union is 30, in Pakistan 20 % for its registration and union with one third of the workers for collective bargaining (2012 amendment). In Sri Lanka, only the union with 40% of the membership in the company can engage in collective bargaining (EXIM Bank, 2013).

It is suggested that only one outsider may be allowed as an outside leader and that there should be a limit of companies in which an outsider can become a leader of internal unions. Second National Commission on Labor (NCL) had made a number of meaningful suggestions to bring amendments in the Trade Union Act. These were: union must have the representation of 20% of the workers for its recognition as a bargaining unit; and that section 16 of the Trade Union Act may be deleted. These are important suggestions and the Act may accordingly be amended.

### **Labor Administration**

Labor administration comprises Labor Commissioners, Labor Officers and Labor Inspectors. Section 4(1) (9b) (v) of Chapter 6 defines their roles and duties. The most difficult and annoying part of labor administration for the employers is the inspection notoriously given the label of Inspector Raj. The labor officers and inspectors are expected to verify multifarious sets of regulations under the labor and industrial relations legal framework. The officials have the power to seek information/records as well as en-

ter any establishment, factory or office and make copies of any documents maintained by the management. They can impose fine for any labor law violations.

**Since the employers find it extremely cumbersome to maintain such registers, the violations are high.**

The system has been unable to meet the laudable objective of monitoring the implementation of labor laws largely because of the multifarious registers and regulations. The scope extends to regulating the height of urinals to workers wash rooms to how often the workplace must be lime washed. The employer is expected to maintain 6 different registers of attendance logs, 10 different accounts of overtime wages, five types of annual returns besides adhering to a host of other stipulations and maintenance of registers. Since the employers find it extremely cumbersome to maintain such registers, the violations are high. The employer prefers to give bribes rather than maintain all the registers and they find a willing partner amongst majority of labor inspectors. This system has remained ineffective because quite often labor officers do not have reliable information about the location and dispersal of establishments within their jurisdiction. The ratio of labor inspectors to the number of enterprises is also adverse. It is physically impossible to cover the area and the number of companies under the jurisdiction of one inspector. Even facilities like transport and other logistics to carry out inspections are insufficient.

For a policy recommendation, the two issues which need to be looked at are: the number of laws and their procedures have to be simplified along with a drastic reduction in the items under inspection; and total freedom from inspection which the employers want would be total disregard of the primary obligation of the state to formulate and regulate the implementation of the laws. There is, therefore, the need to maintain a balance first by statutorily reducing the provisions and list of inspections while keeping intact the objective as administering the compliance or otherwise of the legal obligations. The matter has been under consideration and a number of suggestions which have already come up as follows.

The Prime Minister's Council on Trade & Industry on 4<sup>th</sup> December 2004 was set up under the Chairmanship of Anwarul Hoda, Member (Industry), Planning Commission and it recommended in December 2005, the following steps:

“A system of third party inspection should be established to give to enterprises an option to get their regulatory compliance certified by reliable agencies like the ISO 14001 certification by the Quality Council of India, Occupational Health and Safety Standard (OHSAS 18001) by the British Standard Institute UK, Social Accountability Standard (SA 8000) by Social Accountability International, USA and corresponding standard developed by Bureau of Indian Standards (BIS). Once such certification has been obtained, the unit should be exempted from routine inspection. Special inspection would be authorized only on receipt of credible complaints”.

The employers demand is for self certification and some of the state governments have already introduced this system. However, given the rent seeking behavior of the labor inspectorate, the employers will get away with whatever they do. The Government of India's program of filling e-returns is welcome. But this not being implemented swiftly and may take a long time. Therefore, till the time this process is completed, a mechanism of joint inspections with joint annual calendar of inspections should be developed. However, it is imperative that the list of inspection is significantly pruned.

**It is imperative that the list of inspection is significantly pruned.**

### Other Issues

*Too many laws:* There are too many laws and there is an urgent need to consolidate them. As Second National Commission on Labor (NCL) suggested, these must be grouped together under five categories: labor relations; wages & working conditions; social security, and a separate bill for agricultural workers and others in the unorganized sector. Also, there are different laws applicable to establishments according to micro, small and medium, size of workforce and across sectors. This should be done away with.

*Different definition of the worker in laws:* There is also the problem of no uniform definition of a worker in the

Acts. Some like the Minimum Wages Act, Payment of Gratuity Act, Employee Provident Fund Act and others do not define a 'worker' and instead define an 'employee' with different definitions. The ID Act Section 2(g) defines workman "as any person (including an apprentice) employed in any industry to do any manual, unskilled, skilled, technical, operational, clerical or supervisory work for hire or reward.....". This in itself has given rise to ambiguity as courts have upheld that even a Pilot is a workman since their work is of technical nature. Even supervisors are a part of the definition of a worker according to the ID Act.

One definition of a workmen irrespective of the act and the size of establishment is the immediate need. The supervisors should be out of the ambit of the definition of the worker except in the smaller establishments (10 and 20 workers), in which the salary is of below Rs. 10000/-.

A summary at all the suggested amendments in labour laws is given in Table 2.

### Concluding Remarks

Business must not be tied up to too many rules and regulations and then expected to deliver. Labor law reform though not the only contributor, will pave the way for robust growth and investment. It has been an important agenda of a number of governments, national committees and the Second National

Table 2 Suggested Labor Law Changes at a Glance

Labor Law	Current Legislation	Proposed Amendment/Change
<b>1.ID Act, 1947</b>		
• Lay off, Retrenchment & Closure (Chapter VB, VA)	<ul style="list-style-type: none"> <li>• Government permission required</li> <li>• Retrenchment compensation of 15 days for each year completed.</li> <li>• One month's prior notice indicating reason for retrenchment</li> <li>• Compensation for closure depends upon whether the industry is sick, non-profit etc.</li> </ul>	<ol style="list-style-type: none"> <li>No government permission may be required for lay off, retrenchment and closure</li> <li>Retrenchment compensation to be increased to 45 days per year of completed or number of years of service left whichever is less</li> <li>Notice period of 2 months for retrenchment</li> <li>Closure requirements may be made stringent with higher compensation compared to the present one.</li> </ol>
• Notice of Change (Section 9A)	<ul style="list-style-type: none"> <li>• 21 days notice to be given to the government.</li> </ul>	<ol style="list-style-type: none"> <li>No government notice may be required</li> <li>Carry out the changes after discussion of the legitimacy of change with the unions/workers. Submit the legitimacy report to the government.</li> </ol>
<b>2.Dispute Settlement</b>		
• Provision for raising a dispute (Section 2 A & Section 26)	<ul style="list-style-type: none"> <li>• Permits a worker/union to resort to a dispute any time</li> </ul>	<ol style="list-style-type: none"> <li>Put a six month limit for raising a dispute</li> </ol>
• Collective bargaining Section 18(1), (3), and Labour Courts (Section 7A & B), Voluntary arbitration (Section 10A) and Compulsory adjudication (Section 7)	<ul style="list-style-type: none"> <li>• Bi-partite forums, except Works Committees, are not statutory in Nature</li> </ul>	<ol style="list-style-type: none"> <li>Bar unions with less than 15% from raising the dispute</li> <li>Provide legal sanctity to the bi-partite forums like the co-determination model of Germany.</li> <li>Involve a third party like the ombudsman in the enquiry process of suspension and dismissal.</li> <li>The recommendation should be binding (on a broad based mutually developed list). On both the parties.</li> <li>The remaining 10-20% of the cases, where disagreement persists, should be referred for conciliation and upon its failure to voluntary arbitration or adjudication.</li> </ol>

<p><b>3.Contract Labor (Regulation and Prohibition Act, 1970</b></p>	<ul style="list-style-type: none"> <li>• Meant for regulation and prohibition of contract labour employment</li> <li>• Applicability of the Act to establishments with 10 &amp; 20 worker, with and without power</li> <li>• Section 10 of the Act allows prohibition of contract labour in any process, operation or other work in any establishment</li> <li>• Contract labor is entitle to the payment of Minimum Wages as announced by the government from time to tome</li> </ul>	<ol style="list-style-type: none"> <li>a. Keep the applicability limit of worker from 10 to 20.</li> <li>b. Mutually develop a broader list of core activities</li> <li>c. In case chapter VA &amp; VB are amended, Section 10 for the Contract Labour Act may not be amended.</li> <li>d. Introduce an amendment in CL Act that the employer may pay contract labour above the minimum wages calibrated with the skill levels of such workers having a bearing with the wages of permanent workers in each establishment.</li> <li>e. Introduce 'Fixed Term Employment' for a pre-terminated period with wages equivalent to the regular workers with no right to regularization.</li> </ol>
<p><b>4. Trade Union Act, 1926</b></p>	<ul style="list-style-type: none"> <li>• Section 16 allows one third of its leaders to be outsiders</li> </ul>	<ol style="list-style-type: none"> <li>a. Only one outsider member may be allowed as an outside leader.</li> <li>b. Put a limit in the number establishments an outsider can be leader of internal unions.</li> <li>c. Unions must have the representation of 20% of the workers for its recognition as a bargaining agent</li> </ol>
<p><b>5.Labor Inspection</b></p>	<ul style="list-style-type: none"> <li>• To seek compliances of labor law stipulations</li> </ul>	<ol style="list-style-type: none"> <li>a. Reduce the items/registers required by employers for labor inspection.</li> <li>b. Allow submission of online compliances. Till this takes place, allow self certification with strict penalties</li> </ol>

<p><b>6. Others</b></p> <ul style="list-style-type: none"> <li>• Too many Laws</li> <li>• Different definitions of 'Worker' in Acts</li> <li>• Supervisors are categorized along with worker</li> <li>• Penalties for labor law violations</li> </ul>	<p>• Consolidation of labor laws</p>
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All laws may be consolidated under five categories.

1. Labor relations
  2. Wages and other components of compensation
  3. Working conditions
  4. Social security
  5. Agricultural and other workers with unorganized sectors
- One definition of worker irrespective of the Act.
  - Only supervisors with a salary of Rs. 10,000/- may be covered under the Acts.
  - The current penalties are an insufficient deterrent to violate labour laws. These must be enhanced substantially.

Commission on Labor. All of them have categorically stated the need to change labor laws. What has stalled these reforms is the lack of consensus among the three actors i.e., the government, employers and the unions. The unions and the employers just would not give up an inch of their respective turfs. Yet a consensus at the tripartite forums is the essence of the labor law framework of India. The Central Government had also not been steadfast despite understanding the felt need and public postures. The stalemate has, therefore, continued. The governments have also been anxious of the so called 'political backlash'. It is difficult to comprehend that successive governments have not been so much concerned about giving legal protection at par with the organized sector workers to 94% of the unorganized sector workers but is worried about the political backlash of making amendments for six percent of them. It will be pertinent to highlight here that the coverage of ID Act, 1947, the rigidity clauses of which have been the bone of contention, has a coverage of about 1.4% of the workforce or 3% of the hired workforce. The other apprehension is of large scale retrenchments and closure which is not without valid reason. This though can be addressed by substantially increasing the compensation to be paid in such cases so that the employer resorts to them only in case of absolute necessity. The experience of some of the state governments like Andhra Pradesh for the contract labor, Gujarat for making a number of desired



changes in the labor laws and now the proposed ones in Rajasthan should help the authorities in allaying some of these apprehensions to create an investor and business friendly, environment. As long as the amendments in labor laws do not trample the rights of workers, these should be carried forward. Finally, the Central Government must take the lead in bringing the desired amendments rather than passing the buck on to the State governments. Leaving it to the latter will only escalate disparities within the country with its economic and social consequences.

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## Annex I Labor Laws Enacted by the Central Government

Sl No.	Name of the Act
<b>a. Labor laws enacted &amp; enforced by Central Government</b>	
1.	The Employees' State Insurance Act, 1948
2.	The Employees' Provident Fund and Miscellaneous Provisions Act, 1952
3.	The Dock Workers (Safety, Health and Welfare) Act, 1986
4.	The Mines Act, 1952
5.	The Iron Ore Mines, Manganese Ore Mines and Chrome Ore Mines Labor Welfare(Cess) Act, 1976
6.	The Iron Ore Mines, Manganese Ore Mines and Chrome Ore Mines Labor Welfare Fund Act, 1976
7.	The Mica Mines Labor Welfare Fund Act, 1946
8.	The Beedi Workers Welfare Cess Act, 1976
9.	The Limestone and Dolomite Mines Labor Welfare Fund Act, 1972
10.	The Cine Wokers Welfare (Cess) act, 1981

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- 11 The Beedi Workers Welfare Fund Act, 1976  
12 The Cine Workers Welfare Fund Act, 1981
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**b. Labour Laws enacted by Central and enforced by both the Central as well as the State Governments**

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- 13 The Child Labour (Prohibition and Regulation) Act, 1986  
14. The Building and Other Construction Workers' (Regulation of Employment and Conditions of Service) Act, 1996  
15. The Contract Labor (Regulation and Abolition) Act, 1970  
16. The Equal Remuneration Act, 1976  
17. The Industrial Disputes Act, 1947  
18. The Industrial Employment (Standing Orders) Act, 1946  
19. The Inter-State Migrant Workmen (Regulation of Employment and Conditions of Service) Act, 1979  
20. The Labor Laws (Exemption from Furnishing Returns and Maintaining Registers by Certain Establishments) Act, 1988  
21. The Maternity Benefit Act, 1961  
22. The Minimum Wages Act, 1948  
23. The Payment of Bonus Act, 1965  
24. The Payment of Gratuity Act, 1972  
25. The Payment of Wages Act, 1936  
26. The Cine Workers and Cinema Theatre Workers (Regulation of Employment) Act, 1981  
27. The Building and Other Construction Workers Cess Act, 1996  
28. The Apprentices Act, 1961
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**c. Labour Laws enacted by Central Government and Enforced by the State Governments**

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29. The Employers' Liability Act, 1938  
30. The Factories Act, 1948  
31. The Motor Transport Workers Act, 1961  
32. The Personal Injuries (Compensation Insurance) Act, 1963  
33. The Personal Injuries (Emergency Provisions) Act, 1962  
34. The Plantation Labor Act, 1951  
35. The Sales Promotion Employees (Conditions of Service) Act, 1976  
36. The Trade Unions Act, 1926  
37. The Weekly Holidays Act, 1942  
38. The Working Journalists and Other Newspapers Employees (Conditions of Service) and Miscellaneous Provisions Act, 1955  
39. The Workmen's Compensation Act, 1923  
40. The Employment Exchange (Compulsory Notification of Vacancies) Act, 1959  
41. The Children (Pledging of Labour) Act, 1938  
42. The Bonded Labour System (Abolition) Act, 1976  
43. The Beedi and Cigar Workers (Conditions of Employment) Act, 1966  
44. The Unorganized Workers' Social Security Act, 2008
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**By Invitation**

## **Indian Industrial Relations Law: Case for Reform**

**Debi S. Saini**

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*Indian labor laws were conceived in the pre-independence period or shortly afterwards based on an import-substitution and statist model of economic development. They were premised on adversarial IR assumptions, social justice and industrial peace. The paradigm is shifting towards global competition, productivity, efficiency and mutual cooperation. IR is giving way to employee relations. This paper examines the way the Industrial Disputes Act 1947, the Trade Unions Act 1926, and the Industrial Employment (Standing Orders) Act 1946 have been working and to what effect. It discusses a broad framework of changes that need to be effected in them so as to be aligned with the contemporary global and Indian economic realities.*

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### **Introduction**

An economic growth model that a country adopts has to have a clear notion of the basic postulates of industrial relations (IR) as a facilitator. After attaining Independence, India adopted the statist, import-substitution model of economic development. Economic planning, licensing, foreign exchange rationing and regulation, and capital market regulation policies were followed strictly so as to be aligned with the national priorities. Economic growth was juxtaposed with “social justice” as an essential societal value. Trade unions were allowed to flourish and expand as instruments of promoting countervailing power of the working class subject to the above values. Simultaneously was preached the concept of responsible unionism; as adversarial collective bargaining was seen as the “law of the jungle.” Especially during the 1960s and 1970s trade unions grew in strength. But this model ceased to be effective and resulted in what came to be labeled as “the Hindu rate of growth.” Eventually, the model led into a deep crisis during the late eighties. Critics reminded the planners the virtues of Thatcherism and Reaganomics, and suggested the adoption of the globalization model as a savior. The new

economic policy (NEP) adopted in July 1991 was symptomatic of a shift from the pursuit of values like social justice, status, and welfare state to efficiency, productivity, freedom of contract, market focus, competition and flexibility of work. The then finance minister, Dr. Manmohan Singh who later became Prime Minister during 2004-2014, promised labor law reform to facilitate the new paradigm. For addressing the systemic malaise of the earlier model, market was viewed as an instrument of delivering justice through the 'trickle down'.

**Employers saw trade unions to be hindering operational flexibility without which they found it very difficult to compete in the chaotic economic environment.**

The above policies of globalization eventually got reflected in a new kind of workplace order. Employers saw trade unions to be hindering operational flexibility without which (flexibility) they found it very difficult to compete in the chaotic economic environment. State became far less sympathetic to the cause of social justice and the resultant union crisis; this was still more so in the developing countries. The institution of trade unionism and collective bargaining came under heavy pressure so as to take a comprehensive care of all employees at work (Kochan et al., 1986). Cost became a concern due to the rising intensity of competition. Collective bargaining zones were getting squeezed; and employers found it

difficult to be liberal in granting wage increases.

India has about 47 major pieces of central labor legislation and more than 100 pieces of state labor legislation that were intended to carry out the Constitutional vision of building a welfare state as envisaged in the Directive Principles of the State Policy. These directives have been described as the "soul" of Indian Constitution (Dhavan, 1989). Indian labor laws can be grouped into five major categories i.e. laws relating to: working conditions, wages and monetary benefits, industrial relations, social security and miscellaneous labor laws (Saini, 2011 for a detailed discussion). Some of these laws were already in existence at the time of Independence; more were added later.

The supporters of globalization have argued that many pieces of Indian labor legislation have lost their relevance due to changes in the global and Indian economic environment and the onset of the intense competition. Research exists to testify that perceived rigidities in Indian labor law have been negatively impacting the development of the Indian economy (Mitchell, Mahy & Gahan, 2012: 41). International institutions like the World Bank, IMF, and foreign investors have been waiting since long about fulfillment of the government's promise to make changes in labor law, and still more so in the IR law. The top most concern of industry is the belief that too much of job security promotes inefficiency and low productivity. It also reduces labor mobility that is a necessary condition for effi-

cient working of firms in a competitive environment. The example of China is being cited to support this; as it has undertaken industrial re-structuring as per the needs of the investors and globalization. At the same time, there is plenty of literature to testify that the system is implemented such that there are severe problems in justice reaching the workers (Saini, 1997; Mitchell, Mahy&Gahan, 2012: 22).

In the above context, this paper examines the structure and working of Indian IR law and suggests areas of state action through reform. Towards this end, it discusses the framework of changes that need to be effected in them so as to be in sync with the contemporary global and Indian economic realities. It also analyses the new employee relations strategies that employers are following to stay ahead in the era of intense competition. On the basis of the analysis of the structure and working of the three main pieces of IR legislation in India, it has argued for a case of reform in many aspects of these three Acts. The paper also identifies areas of action for the trade unions, employers and the state.

### **The Indian IR Law: Structure & Working**

Many alternative models of social and economic justice have been adopted in different parts of the world in the field of industrial relations (IR). These models range from powerful corporatism of Continental Europe to complete voluntarism of the type where labor law has been seen as only a footnote to col-

lective bargaining (also named as the Classical Oxford School of IR in pre-Thatcher UK) to substantial legalism and state involvement in USA to almost no labor law in some parts of the developing world (Saini, 2003). Indian model is somewhere in between, upholding the freedom to unionize and promoting industrial peace through negotiation as well as state control of the industrial action. Globalization has, however, made its indelible impact on these models. And, there is a trend towards a greater degree of cooperation in IR.

**The Industrial Disputes Act 1947 (IDA) is the most important piece of IR legislation in the country.**

India's IR law is enshrined in three pieces of legislation: the Industrial Disputes Act 1947 (IDA), the Trade Unions Act 1926 (TUA), and the Industrial Employment (Standing Orders) Act 1946 (IESOA). The Industrial Disputes Act 1947 (IDA) is the most important piece of IR legislation in the country. It has its roots in the Rule 81-A of Defence of India Rules that was promulgated by the British Indian Government in 1942 to control industrial unrest in the country, as the British were focusing themselves on fighting the Second World War and could not afford to have a rising curve of industrial disputes. This rule envisaged a system of compulsory adjudication of industrial disputes by government-appointed tribunals in case the disputant parties failed to resolve it bilaterally. Even after the War was over, it was found that Rule 81-A was successful in

controlling the industrial unrest. Shortly before Independence in April, 1947, this rule was converted into a full-fledged Act in the form of IDA. The Act envisages a conciliation-adjudication-arbitration model of industrial disputes resolution. It empowers the “appropriate government”, in its discretion, to refer an industrial dispute for adjudication either on failure of conciliation or even without any resort to conciliation. Among others, the Act provides for a dispute prevention mechanism in the form of works committee, conciliation officers, board of conciliation, and court of inquiry. After the failure of the dispute to get resolved through the preventive mechanism, it can be referred by the appropriate government, in its discretion, for adjudication to a labor court or industrial tribunal, depending upon the nature and type of the dispute.

Initially, only disputes espoused by a trade union or substantial number of persons were treated as industrial disputes, but later on, a provision for processing individual termination (including dismissal, discharge or retrenchment) disputes was inducted in the IDA, thus treating some individual disputes as industrial disputes. The 2010 amendment to the IDA is the latest. Among others, it has provided that for individual termination disputes the parties can directly approach the labor court, and no reference is required for the same.<sup>1</sup> There is a provision for entering into conciliated settlement under section 12 (3), which has wider applica-

<sup>1</sup> Discretionary reference by the appropriate government is still a necessity for adjudication of collective interest disputes.

tion on all present and future workers of the organization till the settlement is in operation. In addition, under section 18 (1), parties can enter into a voluntary settlement (without the intervention of the CO); but this settlement is enforceable only against the signatories. In 1971, section 11-A was inducted in the IDA at the behest of trade union leadership, which claimed rampant victimization of the workmen by the employers. This had the effect of making labor court virtually a court of appeal in termination cases. In these cases, the labor court could alter the punishment even if the workman is found guilty of misconduct. This provision is seen by the industry as contributing to inflexibility, and as an obstruction in maintaining discipline. It is argued that under this section courts have many times exonerated delinquent workers or given much less punishment to them even when they were found guilty of having committed a misconduct.

**Courts have many times exonerated delinquent workers or given much less punishment to them even when they were found guilty of having committed a misconduct.**

The strike provisions of the IDA are provided in sections 22 to 25. Workers employed in a public utility service cannot go on strike without giving a notice of at least 14 days, and before the day specified in the notice. But there is no such provision that obliges workers to give strike notice in non-public utilities. They may even go on a lightning strike instantaneously, and yet the strike would

not be considered as illegal for not serving any notice. Also, there is no provision in the Indian law for conducting a strike ballot amongst workers. Thus, even a minority of workers can give a call for strike. Section 36 of the Act bans the presence of lawyers in conciliation proceedings. It also restricts lawyers' appearance before the adjudicatory bodies. But a lawyer can be allowed to appear before these bodies if the other party gives his consent to this effect. Section 9-A provides for a notice of 21 days to be given by the employer before making any change in service conditions of the workmen.<sup>2</sup> This provision is also being contested by the industry as it restricts its flexibility, and finds it difficult to adjust to the needs of the changing business environment. For, workers raise an industrial dispute once such notice is given, which further restricts the employer's flexibility.

The TUA confers on workers the freedom to register a trade union subject to the requirements of the Act. There is a provision for creation of a political fund for being used for different political purposes. This is another provision which has attracted bitter criticism. The Act also provides to unions and workers immunity against civil and criminal liability for participating in certain types of industrial action. Maximum problems faced by workers under the TUA relate to registration of a trade union. There are widespread malpractices indulged in at the

office of the registrar of trade unions, and often workers are denied trade union registration on frivolous grounds. Many a time, political pressures or court intervention is sought for compelling the registrar to register the trade union.

**The standing orders when certified are deemed to have become a part of the contract of employment.**

The main objective of the IESOA is to ensure standardization of the terms of employment and their certification by a government officer, who is known as the certifying officer. He is charged with the duty of certifying that the contents of the standing orders are just and fair. There is also provision for payment of subsistence allowance during the suspension period while the domestic inquiry is being conducted against the worker. The standing orders also contain among others, the procedure for taking disciplinary action against the workers. The standing orders when certified by the certifying officer are deemed to have become a part of the contract of employment.

Looking at the way the IR law is working, it can be said that the industrial disputes resolution systems and processes suffer from the problems of delay, formalism and inaccessibility (Baxi, 1993; Saini, 1997). The system has not been able to check the commission of unfair labor practices (ULPs)<sup>3</sup> both by the employers and the employees (Saini,

<sup>2</sup> The matters in respect of which change in service conditions cannot be done have been provided in Schedule IV of the IDA.

<sup>3</sup> See the Fifth Schedule of the Industrial Disputes Act 1947.

1995). The law has also not been able to protect the interest of the trade union leaders who come in the forefront to fight for their associates. A study of the actual working of the adjudication system found that especially in the context of medium and small organizations, labor tribunals, in effect, do the work of providing “legitimacy to the union-smashing exercises of the employers” (Saini, 1997).

There is a serious problem of the non-enforcement of labor laws from the workers’ point of view. This is largely a result of the acts of collusion between employers, bureaucracy, labor law consultants, and even union leaders, especially in the private sector (Saini, 1995a). At the same time, comparatively progressive employers are supporters of most of these provisions, but are asking for changes in some of these provisions so as to adapt to the needs of the changed times. Especially the MNCs and conscientious employers want an IR framework with simpler laws. They want to keep themselves away from maneuverings that are known to be taking place at the behest of the labor department or ‘brief-case union leaders’.

There are some good indicators for the employers. More dismissal decisions rendered by the higher judiciary are going in favor of the employer in the name of efficiency and productivity. Also, over the years, the number of strikes is declining, and so is the number of mandays lost.

A new IR strategy is discernible from the IR policies of more progres-

sive organizations and many MNCs. They are pursuing union-substitution strategies through provision of better employee welfare, care, empowerment, employee involvement, and communication. This is called neo-unitarism—also called the IBM model of employee relations. Companies like the Tata Steel are very successfully practicing a paternalistic IR model (Saini & Budhwar, 2013). Even some manufacturing companies like Jindal Aluminium Ltd. in Bangalore are practicing IBM type of non-union policies (Patil, 1998). At the same time there are many stories of success in resisting these HR strategies which are perceived by the union to be diluting the efficacy of union strength. (Ramaswamy, 2000; 219). There are also revelations that unions are becoming more cooperative with the employers than before in the private as well as public sectors (Ramaswamy, 1994; VenkataRatnam, 2003).

**Unions are becoming more cooperative with the employers than before in the private as well as public sectors.**

Overall, we are witnessing an era of a greater degree of cooperation even as it might be partly due to the covert pressure on the trade union leaders. But it has also to do with the workers realizing that employers can no more shell out money to meet all types of demands. Cooperation seems to be becoming the need of the employers as well as the employees.



## Policy Suggestions and Recommendations

On the basis of the structure and working of these industrial relations and other laws, the following amendments to the Indian IR legislation are suggested:

1. *Renaming the IDA as the Employee Relations Act:* The term industrial relations came into vogue in the late nineteenth century, more and more gained popularity during and after the Second World War. After the War was over more and more employers entered into collective agreements with their employees. Trade unions also showed rise in their membership. The focus of IR was on the relationships between an employer and the employees and resolving industrial disputes collectively through the involvement of union. But since the 1980s and beyond, a sea change is discernible in the IR field. Large sections of the workforce are temporary, part-time, ad hoc, agency and contract workers, who may not be members of any union. They expect to be talked to individually for their motivation and commitment. There is more emphasis on forging cooperation through employee engagement interventions almost all over. Both researchers and employers are now using the term employee relations (ER) which emphasizes more on the individual than the unionized worker force. Though many use the two terms IR and ER interchangeably, the focus in the former is more on the unionized and in the latter more on the individual employee. ER involves building relationship and organizational culture through human resource interventions for employee commitment (Saini & Budhwar, 2013). Hence a case for re-naming the IDA as the Employees Relations Act.
2. *Integration & Simplification:* India has 47 central labor statutes, and some 150 pieces of state labor legislation. There is a demand for integration and simplification of these laws so that at least trade union leaders and common managers can understand their spirit and contents. Ironically, no attempt has been made in this regard. Sometime back the National Labor Law Association prepared, what they referred to as the draft Indian Labor Code, 1994 (NLLA, 1994). This was an attempt to imbibe fundamental principles of Indian labor jurisprudence in an integrated manner. This code was also an attempt to integrate and simplify definitions of certain terms as defined in different pieces of labor legislation. Presently, we have some 13 different definitions of wages, and as many definitions of worker and other terms. This causes tremendous confusion in the mind of the worker and all others dealing with these pieces of legislation.
3. *Industrial Relations Commissions (IRCs):* As is clear from the earlier sections, IDA has its roots in a temporary war-time ordinance. In most developed countries, labor disputes are resolved through collective bar-

gaining, and not through adjudication. India had intense debate during 1970s and 1980s about constitution of autonomous multi-member industrial relations commissions (IRCs) at the central and state levels in place of the present industrial tribunals that are presided over by one person only. This debate started after the recommendations of the first National Commission on Labor (Government of India, 1969). Later on, the NLLA's Draft Labor Code of 1994 also made similar recommendations of setting up autonomous commissions.<sup>4</sup> Even the second National Commission on Labor 2002 (Government of India, 2002) endorsed the recommendation to provide for IRCs at the central and state levels. They were to deal with interests as well as rights in labor matters. The functions expected to be performed by these IRCs included: certification of bargaining agents and bargaining councils; deciding the level at which collective bargaining shall be held; mediation of disputes if desired by disputant parties; and adjudication of disputes

not settled by any of the above methods. Despite nearly three decades of debate, recommendations to constitute the IRCs were never put into operation. Presently, it seems to have gone into oblivion; the concerned parties have even forgotten about them. It is suggested that with a view to arrive at more acceptable solutions to IR problems there is an urgent need to put the recommendation for constituting these IRCs into operation. These IRCs would have one judicial and two non-judicial members who should be experts in matters related to labor issues and social sciences. The labor courts could continue to decide individual termination matters, as activated directly by the workman concerned directly.

4. *Re-orienting the Conciliators & Adjudicators*: IR adjudication is a unique branch of law. Many distinguished jurists and sociologists of law have opined that every person handling labor matters should have the knowledge of law and social sciences. Otto Kahn-Freund, a celebrated labor expert insisted that a lawyer could not understand law, let alone be an educated lawyer unless/he learnt the law in conjunction with other social science disciplines. Another jurist, Justice Brandeis, has gone to the extent of commenting that "a lawyer who has not studied economics and sociology is very apt to become a public enemy" (Wedderburn, 1983:30). This is true of labor law where scholars and judges often need to cross disciplin-

<sup>4</sup> On the basis of the recommendations of the National Commission on Labor (Government of India, 1969) and some other committees, NLLA also recommended constitution of such multi-member mediation-cum-adjudicatory bodies at the state and the central levels. The NLLA National Labor Code draft used the term National Labor Relations Commission (NLRCs) in place of IRCs. It also provided that NLRCs shall have powers exercisable by the Supreme Court of India under clause 2 of Article 32 of the Constitution. It also envisages the taking away of the jurisdiction of the high courts over the labor relations commissions.

ary boundaries to articulate labor justice issues. Report of the First Labor law Review Committee of the Government of Gujarat had envisaged a continuous training for a period of six months for the new recruits to labor judiciary and also a refresher course for labor court judges and labor officers at the end of every three years (Desai, 1994; Government of Gujarat, 1974). It is suggested that the Central Government establishes a special national institute exclusively to train labor judges, labor administrators and members of the proposed IRCs. It will help developing in them the acumen for the inquisitorial method of dispute processing.

5. *Sending the Conciliation File to Adjudicator*: It is a fact that the conciliation file of the industrial dispute contains some useful data that can be helpful in understanding the nuances of the case by the presiding officer of tribunal/labor court concerned. But it is never sent to them. It may be recalled that the whole purpose of the IDA was promoting inquisitorial and not adversarial investigation of the industrial dispute. The file can help understand better the issues on hand, the attitude and behavior of the parties concerned on the issues, the nature of the demands including their genuineness, the pressures on them, and the contents of the failure report by the conciliation officer including the confidential part. This will also make the COs more responsible in writing the failure report. It is therefore suggested that

the entire conciliation file including the failure report of the CO should be forwarded to the labor court/industrial tribunal along with the reference order. Further, this will help dilute legalism in processing the industrial disputes.

6. *Lawyers in Conciliation & Adjudication Processes*: Section 36 of the IDA prohibits the presence of lawyers in the conciliation process, and restricts their presence in adjudication proceedings. Lawyers have been described as “traditional elites” (Abel, 1973) and “repeat players” (Munger, 1991: 604), and having endless ingenuity. Often, they tire out the other side as also the judges by indulging in endless arguments. The idea underlying section 36 of the IDA was to ensure that an industrial dispute does not become a complete lawyers’ domain and subjected to legal wrangling; but must be discussed between the parties as one involving economic relations through political solutions. But the situation today is such that in labor courts and tribunals lawyers have completely taken over the industrial disputes resolution processes. This leads to a greater degree of legalization or what has been known as juridification<sup>5</sup> There should be complete ban on lawyers

<sup>5</sup> The term “juridification” does not exist in English. It has been borrowed from German. It refers to the extent to which the behavior of personnel and other managers in dealing with collective and individual employment issues is determined by reference to legal norms and procedures rather than to voluntarily agreed norms (Saini 1995).

to appear before these bodies, except only at the argument stage if necessary where articulation of legal point might be in question. This will save the ER from becoming over-legalized.

7. *The Fate of Sections 11-A*<sup>6</sup> Section 11-A envisages that even in cases of disciplinary action taken by an employer after a properly conducted domestic inquiry, if a labor court/tribunal finds that the employer's order of dismissal or discharge is not justified, it may set aside such an order and direct re-instatement of the workman on such terms and conditions as it thinks fit or give some other relief to the workman including lesser punishment in lieu of discharge.
8. *Strike/Lockout Notice & Strike Ballots*: In the neo-liberal world, work stoppages are becoming less relevant. As mentioned before, under the IDA there is no provision for strike/lockout notice in non-public utility service operations. There is a need to make such a provision, unless strike is called under a grave and emergent situation (e.g. a lockout declared in a emergent situation of violence, etc.). Also, there is a need

for provision for strike ballot before going on strike, in which not less than 50 per cent of the workers should vote in favor of the strike before a legal strike can be called.

9. *Chapter V-B of IDA*: Perhaps the most controversial issues in Indian labor legislation is Chapter V-B of the IDA, which applies to factories, plantations and mines that employ 100 or more workers. This chapter contains, among others, sections 25-M, 25-N, and 25-O. These sections provide for the prior permission of the appropriate government before any workman in such industries can be laid-off or retrenched or the undertaking is closed down respectively. It has been the experience of industries that most state governments have denied totally or unduly delayed such permission, which is often done on extraneous considerations. Interestingly, India is the only country in the world (besides Zimbabwe, which followed Indian law on this issue), which provides for such a provision. This chapter was inducted in the IDA in 1976 and the number of workers provided for the purpose of its application then was 300 or more. This number was later on reduced to 100 or more in 1982. In a highly competitive world, some organizations are bound to fail or perform low despite their best efforts. So it is important to ask, what the justification of this chapter today is. How can we ask a non-viable organization to continue to exist in its original form without making any change in the employment structure

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and thus suffer perennial losses? No law is immutable and has to change in the changed context. Such provisions are bound to adversely impact foreign direct investment (FDI) in the country as well.

**How can we ask a non-viable organization to continue to exist in its original form without making any change in the employment structure and thus suffer perennial losses?**

The new NDA government has the massive mandate of people; and they have from it high expectation of the economic turnaround, which is unthinkable without effecting realistic labor law reforms. Keeping this in view, this number for applicability of chapter V-B may be reduced to 1000 or more workmen in the first attempt. After some two years or so it can be scrapped altogether so that workers can remain prepared for the same.

Simultaneously, retrenchment provisions can be made more attractive. Presently, under section 25-F and 25-FFF 15 days' wage for every completed year of service is provided as retrenchment/closure compensation, which is too meager. In actuality, companies that have effected retrenchment/closure as a result of a settlement, through voluntary retirement scheme (VRS), have provided far more attractive packages. It is suggested that apart from raising the employment limit for applicability of

chapter V-B to 1000 or more workers, retrenchment compensation should be such as to be perceived as an equally attractive option for the worker. Omkar Goswami Committee Report had suggested 45 days wages for every completed year of service as the retrenchment/closure compensation (Government of India, 1993). This may also motivate the employer to re-deploy and re-train the surplus employees rather than retrench them; at the same time, it will minimize the trade unions' resistance to retrenchment and promote greater flexibility.

**Retrenchment compensation should be such as to be perceived as an equally attractive option for the worker.**

*10. Trade Union Multiplicity & Politics:* Especially after the globalization, one can witness steep diminution in the trade union power in general. It is almost impossible to organize a trade union in new organizations without the support and patronage of outsider union federations. For example, in the case of Honda Motorcycles and Scooters India Ltd. (HMSI) workers' victory was unthinkable without the help and support of Gurudas Dasgupta (Secretary of AITUC & *Rajya Sabha* MP) and the Congress President Sonia Gandhi (Saini, 2006). However, if a trade union does not want outsiders in its executive body that should remain a choice with it. It is good that through

the 2001 amendment to the Trade Unions Act, 1926, we have limited the presence of outsiders in the union executive from  $\frac{1}{2}$  to  $\frac{1}{3}$ <sup>rd</sup> of the executive members of the trade union, subject to a maximum of five. This can be further reduced to  $\frac{1}{4}$ <sup>th</sup> subject to a maximum of three or four. As the economy progresses and workers become still more mature to decide whether they want a union or not by themselves, this number can be reduced gradually.

The 2001 amendment to the Trade Union Act 1926 has also provided a minimum number of persons who must be members of the proposed trade union at the time of registration. This is 10 per cent of the total workforce or 100 whichever is lower. We should remove the number 100, and insist that any trade union that wishes to register must have at least  $\frac{1}{10}$ <sup>th</sup> of the workforce as applicants, subject to a minimum of seven whichever is higher. We must keep in mind that in the developed world, there is mostly one trade union federation at the national level. In the UK, we have just one trade union federation, the Trade Union Congress (TUC). The USA had only two, the American federation of Labor (AFL) and Confederation of Industrial Organization (CIO). The workers noticed that two was a crowd and proved antithetical to their interest. So they merged, after which it is known as AFL-CIO. Also, a number of trade unions in India do not submit annual returns as per the law. It

should be provided that any union that does not do so for three years or more should automatically stand de-registered. This will lead to more responsible unionism.

11. *Punishment & Fines for Labor Law Violation*: If we look at the punishments provided and fines imposable for violation of different pieces of labor legislation, it is clear that they are shockingly low in most cases. We still have Rs 10 or 50 or 100 as fines for such violations. Even imprisonment provided is just about one to six months in most cases, which almost never takes place, and the delinquent is mostly left by imposing meager fine. Similar is the situation for non-payment of minimum wages or undue deduction from wages, or delay in payment of wages. Under the IESOA, there is no imprisonment for violating the law. It is just fine. The fines are so inadequate that the employers take these provisions casually. Similar is the situation under the IDA. Section 29 envisages imprisonment for six months and or a fine or both and for continuing breach with a further fine of rupees two hundred for every day during which the breach continues. Minimum imprisonment for the employer and the workmen, contravening any provision, should not be less than two years and must be increased depending upon the severity of the particular violation. Even the Unfair Labor Practices (ULPs) are committed by the parties with impunity. There is a strong case for making these sentences and fines realistic.

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## Concluding Remarks

**It is not quite correct to think that the Indian labor law is highly in favor of the worker.**

From the foregoing discussion it is discernible that there is a clear case of reform and re-definition of the rights and responsibilities of the two sides on the lines suggested. At the same time, it is not quite correct to think that the Indian labor law is highly in favor of the worker. That is more a myth than reality in most cases (Saini, 2003; 1997). However, some parts of the framework are not in tune with the contemporary global and Indian realities. Chapter V-B of the IDA is the real villain of the peace. Most MNCs want simple, workable labor law framework. But they would have to work within the ethos of the agreed framework and the constitutional values, and not adopt strategies of exploitation of labor through low-wage strategies. In actuality, chapter V-B proves to be the only social protection to the Indian worker as there is no system of unemployment insurance for them like in the developed world. Therefore, the retrenchment/closure compensation has to be realistic. The present tokenism of just 15 days wage for every completed year of service should be changed through legislative action.

Further, for being more effective, trade unions will eventually have to form coalition federations like in national governance such as UPA and NDA so that fragmentation of the worker power can

be minimized. While industrial conflict has assumed a different color and dimension today, it has not withered away nor will it in the near future. The unions have a fierce challenge ahead in order to survive and be meaningful for a realistic role. They also have to devise and explore worker-oriented meanings of concepts such as “flexibility, security and opportunity” more through cooperative and dialogue than through adversarial means (Hyman, 1999). For a greater incidence of social legitimacy trade unions have also to conduct themselves democratically and give up oligarchic functioning. The Gen Y worker has very different expectations from the employer as well as the union. The worker would stay with the union only if s/he sees any tangible gains by being in the union.

The state cannot be oblivious to the needs of the worker, as has been the case in the recent past. The worker is prepared for being violent if he is made to feel desperate. That is the message from some of the incidents of industrial violence from recent cases such as HMSI, Graziano, Maruti-Suzuki, Northbrooke Jute Mills, and many similar instances. The state ought not to feel complacent at the declining strikes and man days lost data. This is not a symbol of effectiveness of the role played in IR by the state agencies, but is largely due to declining labor power. The state’s policy of indifference or being with the employer in the interest of more FDI or regional industrial development is not sustainable. It must prepare its conciliation and adjudication mechanisms for performing more professional roles as per expectations.

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By Invitation

## Legal Reforms for the Self-Employed: Three Urban Cases

**Martha Alter Chen, Roopa Madhav & Kamala Sankaran**

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*Four out of five urban workers in modern India are engaged in the informal economy, and half of these are self-employed. This article examines what legal reforms are needed for home-based producers, street vendors and waste pickers who together represent one-fifth of the urban workforce. The article describes the conditions of employment and work processes of these groups, and introduces key organizations of these workers. It then examines the legal demands of these organizations, grouped under: municipal, sector-specific, employment or commercial, and macro-economic. Finally the article draws out lessons for legal reforms for the self-employed including the need for legal identity and incorporation into economic planning.*

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### Introduction

The need to balance job creation with basic protection for workers — to make economic growth inclusive — is a major challenge for the early 21<sup>st</sup> century. In India, as in most countries, labor laws rest on the assumption of a clear employer-employee relationship, and commercial laws rest on the assumption of incorporated enterprises with documented accounts. But eighty per cent of the urban workforce in India is informal, and half of urban informal workers are self-employed (Chen & Raveendran, 2011, updated 2014). The mismatch between the existing legal frameworks around employment and the existing employment structure creates a major challenge for policy makers and calls for significant legal reform.

**Labor laws rest on the assumption of a clear employer-employee relationship.**

At the beginning of the 21<sup>st</sup> century, employment grew at a faster rate per year in urban India than in rural India (Chandrasekhar & Ghosh, 2007). As of

2004-05, over half (54%) of the urban working age (15+) population was in the labor force, either actively working or actively seeking work: 79 percent of men and 24 per cent of women (ibid). But since 2004-05, there has been a marked slowdown in employment growth in both rural and urban India. By 2011-12, just under half (49%) of the urban working age population was in the labor force: 76 per cent of men and 21 per cent of women (Chen & Raveendran, 2011, updated 2014). This slowdown in employment growth was accompanied by a decline in self-employment, which had been growing. By 2011-12, the shares of self-employment and wage employment in total urban employment had reverted to their 1999-00 levels: at 42 and 58 per cent, respectively (ibid).

However, the urban informal workforce was almost evenly divided between self-employment (51%) and wage employment (49%) in 2011-12. There are three main categories of the self-employed: employers (who hire others), own account workers (who run single person or family enterprises without hired workers), and unpaid contributing family workers. In 2011-12, 38 per cent of the urban informal workforce (39% of men and 31% of women) were own account workers; 11 per cent (8% of men and 20% of women) were unpaid contributing family workers; and only 3 per cent of men and 0.5 per cent of women were employers (ibid).

This article examines what laws and regulations impinge on — and what legal reforms are needed for — three groups of informal self-employed in urban India:

home-based workers, street vendors and waste pickers. In 2011-12, these three groups combined represented one-fifth of the total urban workforce in India: home-based workers (15%), street vendors (4%) and waste pickers (1%). Home-based work was particularly significant for women: representing almost a third (32%) of the female urban workforce. The article describes the conditions of employment and work processes of these three groups, and introduces key organizations of these workers in India. It then examines the legal demands of these organizations of workers. Finally it draws out some lessons for legal reforms for the self-employed in India and elsewhere. This article draws on findings and recommendations from three multi-country initiatives led by the global network WIEGO (Women in Informal Employment: Globalizing and Organizing): an on-going program to improve official national statistics on informal employment around the world; a 2012 study of urban informal workers in 10 cities/9 countries (including waste pickers in Pune and home-based workers plus street vendors in Ahmedabad); and a multi-year project on law and informality in four countries (Ghana, India, Peru and Thailand). Many of the sector-specific findings, as well as recommendations of the 10-city study and the 4-country project, are common across the different cities and countries. In other words, what is detailed below about legal reforms for home-based workers, street vendors and waste pickers is not unique to India.

### **Home-Based Workers**

Home-based workers produce goods or services for the market from their own

homes or adjacent grounds and premises: stitching garments and weaving textiles; making craft products; processing and preparing food items; assembling or packaging electronics, automobile parts, and pharmaceutical products; selling goods or providing services (laundry, hair-cutting, beautician services); or doing clerical or professional work, among other activities. Although they remain largely invisible, home-based workers are engaged in many branches of industry and represent a significant share (14%) of the urban workforce in India, particularly among women workers (32%).

**Inadequate housing is a commonly cited problem by home-based workers.**

For home-based workers, whose home is also their workplace, housing is an essential productive asset. Inadequate housing is a commonly cited problem by home-based workers. A small house hampers productivity: as the home-based worker cannot take bulk work orders because she cannot store raw materials and her work is interrupted by competing needs for the same space of other household members and activities. Poor quality housing allows goods and raw materials to be damaged. Monsoon rains force home-based workers to suspend or reduce production, as equipment, raw materials or finished goods get damaged when roofs leak or houses flood; products (e.g. incense sticks) cannot dry due to leaks and humidity; and orders are reduced due to decreased demand and/or difficulties associated with transport during the rains (Chen, 2014).

When the home is also the workplace, basic infrastructure services are essential for the productivity of work, especially electricity and water. The accessibility and cost of public transport is also a key factor for home-based workers who commute to markets on a regular, if not daily, basis to buy raw materials and other supplies, to negotiate orders, and to sell finished goods. A recent study of home-based workers in Ahmedabad (India), Bangkok (Thailand) and Lahore (Pakistan) found that transport accounted for 30 per cent of business expenses; and of those who had to pay for transport, one quarter operated at a loss (ibid). The distance between the home-based worker's home and the market, contractor, or customers she deals with is critical, affecting the cost of transport. When home-based workers are relocated to peripheral areas they often have poor access to public transport and their transport costs rise sharply.

There are two basic categories of home-based workers: independent self-employed workers who take entrepreneurial risks; and sub-contracted workers who depend on a firm or its contractors for work orders, supply of raw materials and sale of finished goods. This second category of home-based workers, the sub-contracted workers, is officially referred to as "homeworkers". Since they are not directly supervised by an employer, provide their own workspace and equipment, and cover many of the non-wage costs of production including power and transport, homeworkers are often classified as self-employed. However, because they are

dependent on a firm or its contractor for work orders, raw materials, and sale of finished goods, they are sometimes classified as wage workers. In reality, sub-contracted home-based workers – or homeworkers – occupy an intermediate status in employment between fully independent self-employed and fully dependent employees (Raveendran et al, 2013: 2). Also, many self-employed home-based workers are not fully independent: as they have limited access to capital, knowledge of markets, bargaining power, and control in commercial transactions.

Because they work at home, both groups of home-based workers tend to remain isolated from other workers in their sector (apart from those in their neighborhood) and to have limited knowledge of markets and market prices. These factors limit their ability to bargain for more favorable prices and piece rates or to negotiate with government for basic infrastructure and transport services.

While home-based workers are present in most branches of economic activity, they are concentrated in manufacturing, trade and repair services: in India in 2011-12, 73 per cent of women home-based workers were in manufacturing, 14 per cent in trade, 4 per cent offered education services, and 3 per cent provided lodging or ran small eateries (Raveendran et al, 2013). Among women home-based in the manufacturing sector, 29 per cent produced hand-rolled cigarettes (*bidis*), 26 per cent stitched or embellished garments, 22 per cent wove textiles, 6 per cent produced food or beverages; 7 per cent produced wood or cork

products (mainly incense sticks), and 5 per cent made furniture (ibid). Compared to women home-based workers, a lower percent of men home-based workers were in manufacturing (41%) and a higher percent were in trade (35%) and other services, including repairs (6%) (ibid).

**Home-based workers and their activities are affected by government policies and practices, notably land allocation, housing policies, basic infrastructure services, and public transport.**

Home-based workers and their activities are affected by government policies and practices, notably land allocation, housing policies, basic infrastructure services, and public transport. This is because their homes are their workplaces; and they have to commute to markets and transport supplies/goods to and from their homes. Legal reforms should support policy interventions that upgrade settlements with large concentrations of home-based workers to ensure they have adequate shelter, water, sanitation and electricity. If and when home-based workers and their families have to be relocated, efforts should be made to ensure the relocation sites have, from the outset, adequate shelter, basic infrastructure, transport services, and access to markets.

Home-based workers also need legal rights and protections against unequal and, often, exploitative value chain practices and relationships. Home-based workers have limited scope for negotia-

tion or leverage: due in large part to their isolation in their homes but also to exclusionary urban policies or practices and to unequal or exploitative value chain dynamics. To demand and secure their rights, home-based workers need increased bargaining power, which comes with being organized and being invited to have a seat at the policymaking, rule-setting or negotiating table. Thus, for home-based workers, belonging to their own organizations and having supportive intermediaries are critically important.

There are many organizations of women home-based workers in India and a South Asia regional network of home-based workers (Home Net South Asia) headquartered in India (see [www.homenetsouthasia.net](http://www.homenetsouthasia.net)). The Self-Employed Women's Association (SEWA), a trade union of some 2 million informal women workers, has organized home-based workers in 11 states of India. It is the lead organization in the regional network. SEWA has led the way in advocating for social protection and pension coverage to home-based workers; negotiating welfare boards for different categories of home-based workers; and negotiating higher piece rates for sub-contracted home-based workers who manufacture incense sticks, *bidis*, and garments.

### **Street Vendors**

Street vendors offer a range of goods and services from streets and other open public spaces. They represent 4 per cent of the urban workforce across India (Chen & Raveendran, 2011, update 2014). In large cities such as Mumbai

and Delhi there are 250 thousand or more street vendors (Bhowmik, 2014). Some street vendors come from castes or communities for whom street vending is a hereditary occupation. Others are migrants or laid-off workers for whom street vending affords low-end but steady employment. Also, many home-based producers of garments, textiles, crafts or cooked food sell their goods in street markets. Street vendors offer working people, and even middle class consumers, a convenient place to buy goods at low prices; serve as key links in the wider urban distribution system; and enrich the cultural life of cities.

In India and elsewhere, there are three basic categories of street vendors: those who buy goods, typically from wholesalers, and sell them at a margin (e.g. those who sell fresh fruit and vegetables); those who make, manufacture, or transform goods and sell them directly to consumers (e.g. cooked food vendors); and those who provide or perform services from a street or other open public space (e.g. barbers) (Roever, 2014). Those who buy-and-sell "are challenged to find good prices from suppliers; keep other costs, such as transport and storage, to a minimum; and sell at volume to generate profit" (Roever, 2014: 10). Those who transform goods "must find a place to make their goods, usually at home or in the street, but sometimes at a workshop or other unused space; then they must find a place to sell them to consumers. They must also find a place to store unsold goods, or to store the equipment used to make the goods (such as portable stoves or juice machines for

cooked food or prepared drink vendors). The work of these vendors entails value addition and is sometimes more dependent on workplace infrastructure, such as electricity and running water, than buy-sell traders” (ibid: 10). Service providers tend to “have fewer challenges when it comes to transporting goods, although they may need machinery or tools to be stored at or transported safely to their vending post. However, they are often reliant, like manufacturers, on electricity and/or need either specialized training or substantial access to capital to purchase the necessary machinery, tools or inputs” (ibid: 11).

Within these basic categories, street vendors can be further differentiated by a) whether they sell perishable or durable goods; b) whether they work on their own, with family workers, or with hired workers; c) whether they are independent, tied through credit-purchases to a wholesaler, or sell on commission for formal retailers; and d) whether they sell in central business districts or more peripheral areas, around wholesale markets, near transport nodes, religious institutions or educational institutions, or near residential areas.

More so than home-based workers, street vendors are directly affected by the regulations and policies of city governments and the practices of city officials. Across most cities of India, and other countries, government policies or practices undermine the ability of street vendors to pursue their livelihoods. Abuse of authority by the police and local officials is the most common com-

**Across most cities of India and other countries, government policies or practices undermine the ability of street vendors to pursue their livelihoods.**

plaint: this “includes police harassment, demands for bribes, arbitrary confiscations of merchandise, and physical abuse. These practices tend to take place in urban policy environments that do not define a role for street trade or offer a viable space to accommodate it. In that context, street traders also rank the lack of a fixed and secure workplace and evictions from (or demolitions of) existing workplaces among the most significant negative drivers” (ibid: 25). A study of street vendors and public space in Ahmedabad found that local leaders collect “protection” money each day, week or month from street vendors in their market areas which they hand over to the police after taking their cuts: the amount paid differs by whether the street vendor sells from the pavement or from a push cart (Brown et al, 2012).

Where cities attempt to regulate street vending, the licensing and permitting practices and their associated taxes, fees, tolls and levies have a significant impact on vendors. Most vendors “pay all manner of tolls, levies, and fees – as well as bribes – to use public space” (Roever, 2014: 26). But most street vendors lack urban infrastructure services at their vending sites, including running water and toilets, electricity, and waste removal. “Prepared food vendors must cook at home or ferry water to their

stalls, street tailors and hairdressers stop working when the power goes out, and market vendors spend time and money organizing ad-hoc waste removal systems where city services fail” (Roever, 2014: 26). The fact that most cities do not consult with street vendors around such practices only compounds the problem.

**The license regime for street vending is opaque and repressive.**

When they operate without a license, street vendors in India are considered illegal under most municipal acts: leaving them subject to treatment as criminals under the Indian Penal Code and to rent-seeking in the granting of licenses. But the license regime for street vending is opaque and repressive. Many cities have inappropriate license ceilings: for instance, in Mumbai, where there are an estimated 250,000 street vendors, the municipal corporation arbitrarily fixed a ceiling of only 14,000 licenses; and even these were not issued for many years (Bhowmik, 2000). In Kolkata, street vending without a license is a non-bailable offense (*ibid.*)

Estimates suggest that street vendors occupy only two percent of urban land but are legally barred from doing so. A 2000 study of street vending in seven cities of India found that only two cities, Bhubaneswar and Imphal, made provisions for street vendors in their city plans (*ibid.*). The other five cities, Ahmedabad, Bangalore, Delhi, Kolkata, Mumbai and Patna, earmarked spaces in their plans

for hospitals, parks, offices, residential colonies, and bus and rail terminals but excluded the vendors who naturally congregate around these areas, providing essential goods and services at low costs. Increasingly, cities around India, and elsewhere, are allocating public space for large-scale modern retail – malls and shopping arcades – while continuing to neglect small-scale traditional retail.

Because they congregate in public spaces street vendors come to know their common harsh treatment by local authorities. Because they often are banned or evicted from their vending sites street vendors know the value of collective action. As a result, more so than other groups, street vendors have organized themselves into trade unions and associations. The National Alliance of Street Vendors of India (NASVI) based in Delhi, is a federation of 715 street vendor organizations, trade unions and support organizations (NGOs). SEWA has large numbers of street vendors among its members across in many cities across 11 states of India. SEWA and NASVI led the long campaign for a national law of street vending, passed in March 2014, and continue to advocate for the law to be implemented.

**Waste Pickers**

Roughly one per cent of the urban workforce in India is engaged in waste collection and recycling (Chen & Raveendran, 2011, updated 2014). Waste pickers are those who do the primary collecting and sorting of waste, reclaiming reusable and recyclable materials.



Waste pickers may collect household waste door-to-door or from the curbside; commercial and industrial waste from dumpsters; or litter from streets and urban waterways. Some work on municipal dumps.

Treated as nuisances by authorities and with disdain by the public, waste pickers are usually ignored within public policy processes and frequently suffer low social status and self-esteem. They are particularly susceptible to violence by the police. They may face exploitation and intimidation by middlemen, which can affect their earnings. Most crucially, they are negatively impacted by the privatization of municipal solid waste management services which increases competition for waste and makes the recycling activities of waste pickers illegal.

Handling waste poses many health risks to workers. These are even greater for informal workers due to their unprotected exposure to contaminants and hazardous materials on a day-to-day basis. Risks include contact with fecal matter, paper saturated by toxic materials, bottles and containers with chemical or health residues, contaminated needles, and heavy metals from batteries (Cointreau, 2006). A lack of worker protection and poor access to health care aggravate these risks. Waste pickers face great risks of injury, especially those who work at open dumps and may be run over by trucks or become the victims of surface subsidence, slides and fires. They are also exposed to great quantities of toxic fumes. Waste pickers also endure ergo-

nomie hazards such as heavy lifting, static posture and repetition, and may have high incidences of low back and lower extremity pain (ibid.).

There are many organizations and a national alliance of waste pickers in India. Many of these organizations are legally incorporated and/or function as a trade union or cooperative, collectively bargaining for access to waste and waste collection contracts. If they secure a contract, these organizations then legally incorporate a cooperative and/or function as a cooperative, collectively providing a service. What is distinct about the organizations of waste pickers is that they have to both collectively bargain for access to waste and waste collection contracts and, if they receive a contract, collectively provide a service. The organizations have to perform, that is, the functions of both a trade union and a cooperative.

SEWA has been organizing waste pickers since the late 1970s, beginning in Ahmedabad city but now covering cities across several states: Bihar, Gujarat, Delhi, and more. SEWA has created nearly 90 waste pickers cooperatives to help its members negotiate collective work contracts and access to credit, training, and markets. The Kagad Kach Patra Kashtakari Panchayat (KKPKP) Union in Pune has also created a waste picker cooperative which has secured a contract for collecting and sorting waste from the Pune Municipality. Hasiru Dala, an organization of waste pickers in Bangalore, has teamed up with the IT sector to create

a cloud-based technology whereby households and firms that generate waste can procure waste management services directly from waste pickers and their organizations. Safai Sena is an association of waste pickers in Delhi supported by Chintan, an environmental research and action group. The Alliance of Indian Waste Pickers (AIW), a national network of 35 organizations in 22 cities, facilitates peer support, learning and advocacy among waste picker organizations and support NGOs.

**Waste pickers collect, recover and recycle a sizeable share of the waste generated by cities and, thus, contribute to both cleaning the cities and reducing carbon emissions.**

Individually and collectively, these organizations have made the case – and generated credible evidence – that waste pickers collect, recover and recycle a sizeable share of the waste generated by cities and, thus, contribute to both cleaning the cities and reducing carbon emissions.<sup>1</sup> But municipal governments across India continue to issue solid waste management contracts to private companies who compete with the waste pickers for waste and do not reclaim recyclables, thus contributing to carbon emissions.

<sup>1</sup> A 2009 report by Chintan estimates that informal recycling in Delhi reduced carbon dioxide (CO<sub>2</sub>) emissions by 962,133 tons last year — roughly equivalent to taking 175,000 vehicles off the road (Chintan, 2009).

## **Legal Demands**

The common legal rights that all three sectors demand and have pursued include the right to identity and dignity as workers, the right to work, the right to organize and to have their organizations represented in relevant policy-making and rule-setting processes, and the right to social protection coverage. There are ongoing legal struggles - with some victories - to extend the right of identify as workers to include own account workers and unpaid contributing family workers and to expand the right to work to include the right to livelihood. Organizations of informal workers are gaining increased official recognition and, to a lesser extent, increased representation in official policy-making and rule-setting processes.

In India, as elsewhere, there is greater reception to the demand for social protection than to the other legal demands of informal workers (Sankaran & Madhav, 2013). In India, several states have been willing to set up welfare funds and to invite companies to contribute to industry-specific welfare funds; to expand existing funds and schemes; to set up new health and pension schemes for informal workers. The national health insurance program, Rashtriya Swasthya Bima Yojna, is being extended to cover informal workers, including construction workers, domestic workers and street vendors. But the rules and procedures of this program are not very favorable for these workers or easy to navigate.

Indeed, “a complex range of sector-specific regulatory laws impact workers

in the informal economy, especially own-account workers and the self-employed more generally” (ibid: 5). For example, the right to access public resources - whether waste, urban space, or urban services (basic infrastructure and transport) - is fundamental to all sectors: key legal battles pit the privatization of these public resources against the demands for the right to livelihoods of informal workers (ibid).

The laws and regulations that impinge on urban informal workers, especially the self-employed, can be broadly categorized as follows:<sup>2</sup>

- *municipal regulations* that specify who can do what, where; determine access to - and use of - public resources; and balance conflicting needs and uses
- *sector-specific regulations* that govern specific sectors (e.g. manufacturing, trade, waste)
- *employment and commercial regulations* that govern economic transactions and relationships
- *macro-economic regulations* and policies that govern taxation, expenditure and investment.

What follows is the specific legal demands of the three groups of urban informal self-employed under each of these categories:

<sup>2</sup> This typology is an expanded version of a typology of regulations developed by Kamala Sankaran and Roopa Madhav who directed the 4-country project on Law and Informality of the WIEGO network and its local partners in each country (Sankaran & Madhav, 2013).

## Municipal Regulations

**Overly strict separation of land uses (such as single-use zones) can negatively impact the livelihoods of urban informal workers.**

*Zoning, land allocation, and relocation policies:* Overly strict separation of land uses (such as single-use zones) can negatively impact the livelihoods of urban informal workers. It is important to promote a balanced mix of uses that fruitfully interact with each other. In regard to home-based production and street trade, “it is important to distinguish not only land uses but also the scale of the uses – because, for example, a small tailor workshop may enrich a residential neighborhood while a sewing factory may cause undue nuisance” (Nohn, 2011:4). Distinguishing both land uses and the scale of uses would allow policy makers to better address the needs of home-based workers and street vendors. In the case of home-based work and street vending, “it may be advisable to let neighbors decide whether or not such activities are desirable in the neighborhood” (ibid). Most critically, evictions and relocations of homes and other workplaces, especially to the periphery of cities at a distance from markets, contractors and customers, pose a direct threat to the livelihoods of the urban self-employed.

*Access to - and use of - public resources and services:* most self-employed informal workers in urban areas rely on access to public resources for their livelihoods: for example,

- public land and housing for home-based workers
- public space for street vendors
- waste for waste pickers
- public space/warehouses for sorting and storage for street vendors and waste pickers
- basic infrastructure services at their homes for home-based workers and at their natural markets for street vendors
- public transport for all three groups

The policies and regulations that determine access to public resources and services are often biased against the working poor in the urban informal economy, who are not considered to be productive and are not, therefore, included in most urban plans or local economic development plans. Most critically, privatization of public resources and services often poses a direct threat to the livelihoods of the urban self-employed.

**Privatization of public resources and services often poses a direct threat to the livelihoods of the urban self-employed.**

On the other hand, policies, legislation and regulations that seek to protect the sustainable use of public resources and the environment may contribute to protecting livelihoods of the urban informal self-employed. For instance, policy or regulatory choices to protect the environment through composting and recovery of recyclables can protect the

livelihoods of a large number of waste pickers. Similarly, policy or regulatory choices to protect public green spaces might also support the livelihoods of street vendors by allowing them to vend around these spaces as part of the cultural landscape. Also, policy or regulatory choices to protect the environment might support home-based production, which leaves less of a carbon footprint than production in workshops and factories.

*Balance of conflicting needs and users:* Some legal and regulatory frameworks seek to balance competing interests of different groups - citizens, informal workers, other economic actors. Here are two key examples that affect street vendors:

- use of public space, such as sidewalks - street vendors
- public health regulations - street food vendors

Citizens have the right to use sidewalks and to be assured that street food is safe. In such cases when competing interests are legitimate, the legal demands of street vendors need to be carefully chosen and negotiated.

### **Sector-Specific Regulations**

Informal workers and their activities are affected by laws, regulations and policies that govern specific sectors of the economy: some of these fall under the jurisdiction of municipal governments, others under state or provincial

governments, and still others under the national government. Regulations that govern specific manufacturing industries should in principle cover home-based workers in those sectors: for example, home-based workers who produce hand-rolled cigarettes (*bidis*) should be entitled to certain protections and benefits mandated in two laws from the 1960s governing the *bidi* industry. Also, welfare funds set up for workers in specific manufacturing industries should cover home-based producers in those industries. But in both cases, home-based producers need to be organized and have supportive intermediaries to leverage these protections and benefits.

Street vendors are impacted by the regulations governing the location, management and fee structure of wholesale markets. Marketing costs at the wholesale markets include market fees, commission fees, loading and unloading charges. How much is incurred by sellers to or buyers from these markets is determined by local multi-stakeholder committees that manage wholesale markets and often differ for sellers/buyers of different goods such as fruits versus vegetables. And, as noted earlier, waste pickers are directly impacted by whether or not municipal governments decide to privatize solid waste management or retain public responsibility for social waste management.

### **Employment & Commercial Regulations**

In the 10-city study of the urban informal economy, in addition to hostile

government policies and practices, unfair practices by suppliers, buyers and competitors were identified as key negative drivers in the urban informal economy (Chen, 2014; Roeber, 2014). There are few regulatory frameworks that address value chain dynamics and relationships and those that exist typically address the concerns of sub-contracted, not self-employed, informal workers. Yet the informal self-employed are also often dependent on other actors in the value chain and this dependence renders them vulnerable to exploitation. Home-based workers often rely on specific suppliers or buyers as they lack market knowledge; street vendors often rely on specific wholesalers who sell them goods on credit; and waste pickers often sell to specific waste traders as they too lack market knowledge: in all such cases, the informal self-employed are not able to negotiate reasonable prices for what they buy or sell or protect themselves when the goods they buy or supplies they are given turn out to be of poor quality.

### **Macro-Economic Regulations**

In addition to hostile government policies or practices and unfair value chain dynamics, fluctuating demand and rising prices are key macro factors that impact negatively on the urban informal economy (Chen, 2014; Roeber, 2014). Therefore, ensuring steady markets and reasonable prices for their inputs and products is of critical importance to the informal self-employed. Whether or not prices should be set by governments or markets is hotly debated. Other accepted domains of macro-economic regulations and policies

**Fluctuating demand and rising prices are key macro factors that impact negatively on the urban informal economy.**

- taxation, expenditure and investment - are not particularly sensitive to the specific needs of the informal self-employed (Sankaran & Madhav, 2013). The whole issue of taxation and the informal economy needs to be better understood and addressed: most informal workers pay taxes and operating fees of various kinds but feel they get little in return from the government (Chen, 2014; Roever, 2014). The informal self-employed who pay value added tax (VAT) on supplies cannot easily claim tax rebates to which they might be entitled if their enterprises were legally incorporated (Valodia, 2014). Further, one important means to increase and stabilize demand for the goods and services of the informal self-employed is government procurement, notably: contracts to supply goods and services to public institutions such as schools or hospitals; and also contracts to provide waste management services.

### **Legal Reform in Action**

What does it take to bring about legal reforms in support of informal workers? Consider the case of legal reforms for street vendors. In the late 1990s, SEWA and the National Alliance of Street Vendors of India (NASVI) conducted studies on street vending in seven major cities of India (Bhowmik, 2000). The findings of this study were presented at a large meeting of street vendors in Delhi in 2001, or-

ganized by SEWA and NASVI in collaboration with the Ministry of Urban Development. At this meeting, the government promised to set up a taskforce to draft a national policy on street vending. This policy was approved by the cabinet of India in 2004. The same year, the government set up a National Commission on Enterprises in the Unorganized Sector (NCEUS), which was mandated, among other tasks, to review the national policy on street vendors. A new policy was approved in 2009.

While SEWA and NASVI had advocated for the national policy, they felt that a national policy was not enough: that street vendors also needed legal rights. They argued that street vending was not just an issue of urban policy but rather an issue of the legal right to livelihood (Bhowmik, 2014). They began organizing meetings and demonstrations of street vendors in all their constituencies across India to demand a uniform law to protect the livelihoods of street vendors by regulating street vending in an appropriate and transparent way.

The Street Vendors (Protection of Livelihoods and Regulation of Vending) Act was passed by the Lok Sabha (Lower House of the Parliament of India) in September 2013 and by the Rajya Sabha (Upper House) in February 2014, and received the assent of the President of India in March 2014. The Act aims to provide livelihood rights and social protection to street vendors and to regulate and improve the prevailing license system. "The Act states that no existing street vendor can be displaced until the local authorities conduct

a census of street vendors in the concerned urban centre. All existing vendors have to be provided with permits for conducting their business and a Town Vending Committee (TVC) will supervise the activities of the vendors. This committee, which will be the main policy making body on street vending, comprises municipal authorities, policy, the health department and other stakeholders. Representatives of street vendors will constitute 40% of its membership and women will comprise 33% of the street vendors' representatives" (Bhowmik, 2014:1).

The Act came into force on May 1, 2014. NASVI, SEWA and street vendors around the country welcomed this Act as a major victory as it mandates that street vendors should be protected, not just regulated, and specifies clear procedures for regulation and registration, including the local vending committees with street vendor representatives.

### **Legal Reforms for the Self Employed**

Legal reforms in support of the informal workforce in general, and the self-employed in particular, will require transforming the debates and mindsets about the informal economy. So long as the informal economy is viewed as illegal or even criminal and informal workers are blamed for being illegal or criminal, they will continue to remain under the punitive, rather than the protective, arm of the law. And yet most of the working poor in India are engaged in the informal economy where they are trying to earn an honest living in a hostile regulatory environment.

What is required is focused and sustained attention to determine which policies, laws and regulations impinge - directly or indirectly, negatively or positively - on workers in each sector of the informal economy. This will require on-going efforts to ensure that informal workers in all sectors are visible in labor force and other economic statistics, that in-depth case studies of specific groups of informal workers are prepared, and that organizations of informal workers have a voice in relevant policy-making and rule-setting processes. It will also require that informal workers and their activities are recognized and valued as the broad base of the workforce and economy in India and are incorporated into economic planning at all levels of government.

Legal reforms for the informal workforce in general, and the self-employed in particular, will also require transforming existing legal and regulatory frameworks. Here are some common issues or themes for future legal reforms that have emerged from the legal struggles summarized in this article:

### **Legal Recognition**

Underpinning the many legal demands raised by different groups of informal workers is a primary demand for legal recognition and status (Sankaran & Madhav, 2013). This demand for legal recognition has several inter-related dimensions. First, informal workers want to be recognized as being legal, not illegal. Through their legal struggles, they try to highlight that the existing regulatory frameworks force them to operate illegally: if their residential area

is zoned for single-use (home-based workers), if not enough licenses are issued (street vendors), or if waste is privatized (waste pickers), these informal workers and their activities are considered illegal. Second, informal workers want to be recognized as economic agents who contribute to the economy, to the city, to society and want to be integrated into local economic development and city plans. Third, they want legal recognition of their organizations and the related right of representation. Fourth, most informal workers, with the exception of employers who hire others, want to be recognized as workers<sup>3</sup> and, more specifically, to have their organizations recognized by the Workers Group in the tripartite system of the International Labor Organization.

**Informal workers want to be recognized as economic agents who contribute to the city, to society and want to be integrated into local economic development and city plans.**

### **Access Rights**

The livelihoods of informal workers, especially the self-employed, depend on

<sup>3</sup> The right of own account workers to be recognized as workers, belonging to the Working Group of the International Labor Organization, was endorsed in Clause 4 of the ILO Resolution on Decent Work & the Informal Economy, 2002 which reads: "Workers in the informal economy include both wage workers and own-account workers. Most own-account workers are as insecure and vulnerable as wage workers and move from one situation to the other. Because they lack protection, rights and representation, these workers often remain trapped in poverty" (ILO, 2002).

access to resources, especially to public resources and services. As noted throughout this paper access to key public resources are essential to the livelihoods of the three groups: for home-based workers, housing in central locations; for street vendors, vending sites in good locations, ideally in existing natural markets around transport nodes, institutions, and residential areas; for waste pickers, access to waste and also to solid waste management contracts; for home-based workers and street vendors, basic infrastructure services at their workplace; for street vendors and waste pickers, space to sort and store goods. And for all three groups, accessible and affordable public transport is essential. Evictions from established places of work as well as privatization of public resources and services are major threats to their livelihoods. For urban informal workers, most of these access rights are governed by municipal regulations: a mix of the regulations governing the resources themselves, including balancing competing users and interests, as well as regulations governing who can do what, and where.

### **Municipal Regulations**

Urban informal workers demand more inclusive municipal laws, policies and plans that take into account their contribution to the city economy and integrate their needs. In addition to integration into city plans and local economic development, each group of urban informal worker needs municipal governments to guarantee certain specific rights: home-based workers need housing rights



and mixed-use zoning of the areas where they live and work; street vendors need licenses (or permits) and secure vending sites, ideally in the natural markets where they have always vended; and waste pickers need access to waste and the right to bid for solid waste management contracts. Underlying all of these sector-specific demands is a common struggle against the tendency of municipal governments to privilege formal commercial enterprises over informal commercial enterprises and the leisure and consumption of the rich over the work and production of the poor. What is needed is a fundamental transformation of the vision of cities to embrace economic diversity - the informal and traditional alongside the formal and modern - and a fundamental transformation of the political economy of cities to reduce the disadvantage of the working poor in the urban informal economy.

### **Employment & Commercial Rights**

A key, but challenging, area of legal demands by informal workers is for rights pertaining to their working conditions as well as their economic relationships and transactions. Many informal workers do not operate within the bounds of traditional labor jurisprudence, which is premised on establishing an “employer-employee relationship”, notably the self-employed but also sub-contracted workers and even some informal wage workers (such as domestic workers).

But the informal self-employed also do not operate within the bounds of traditional commercial jurisprudence which

is premised on formal establishments of a certain size. Therefore, in their legal struggles, many organizations of informal workers turn to the state to be the arbiter and regulator of working conditions and relationships. But governments and the organizations of informal workers have struggled to formulate an effective response to this demand (Sankaran & Madhav, 2013). More can, and should, be done to modify and extend employment and commercial regulations to match and cover the various types of informal workers.

Finally, legal reforms for the informal workforce in general, and the self-employed in particular, will require fundamental rethinking regarding regulations and the informal economy. To begin with, there is a common assumption that the informal economy - and those who work in it - are outside the reach of the state or its laws. But, as the evidence presented in the article has illustrated, the informal workforce and their activities are not outside the reach of the state or its laws. Rather, often they are inside the punitive arm of the law but outside the protective arm of the law.

**The informal workforce and their activities are not outside the reach of the state or its laws.**

Secondly, labor and employment laws have limited salience for the informal self-employed. In urban India in 2011-12, only 3 per cent of men informal workers and half a per cent of women informal workers hired others. The vast ma-

jority of the informal self-employed are own account workers or unpaid contributing family workers (Chen & Raveendran, 2011, updated 2014).

Thirdly, a wide range of policies, laws and regulations have salience for the informal self-employed: from municipal to sector-specific to commercial regulations to macro-economic. What is required to reduce the legal risks and barriers faced by the working poor in the informal economy - and thereby to increase their earnings and productivity - is to assess and monitor the impact of all laws, regulations and policies on their livelihoods and lives. At present, most laws, regulations and policies relating to the functioning of cities and the economy ignore the productive roles and contributions of the working poor, relegating them to the domain of social policies. What the working poor in the informal economy want and need is legal recognition and legal protection as economic actors as well as integration into economic planning at all levels.

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**By Contribution**

## **Turnover Intentions among Indian Software Professionals**

**Gloryson R B Chalil & L Prasad**

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*The paper explores the influence of Maslach's three burnout dimensions (Depersonalization, Personal Accomplishment and Emotional Exhaustion) on various Job Attitudes in combination with Work Environmental factors, represented by Organizational Politics and Distributive Justice. Job Satisfaction is conceptualized as Intrinsic and Extrinsic components to identify the relative importance in the development of Turnover Intention. Results indicate the relative importance of Intrinsic Satisfaction; there was no empirical support for hypotheses involving Extrinsic Satisfaction. Results also indicate that process model of burnout is not applicable among software professionals. Organizational Politics became a central variable through multiple significant relationships with other study variables. The paper discusses the theoretical and managerial implications of these results and identifies various themes for future research.*

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### **Introduction**

During the past 20 years, Information Systems function has experienced a rapid growth in almost every organization resulting in the development of more complex and specialized jobs for software professionals (Hurang, 2001). Employment relationship has also undergone a dramatic shift wherein employees prefer to move across various organizations during the course of their working life without any commitment. For most of the software firms, retention of the organizational knowledge is closely linked with the ability to retain the employees. Approximately two thirds of the IT managers who participated in Longenecker & Scazzero (2003) study reported serious consideration about leaving the current organization. Turnover of Information System professionals has shown relationship with failed system projects and inadequate deployment of organization's resources (Igbaria & Guinmaraes, 1999). As one of the largest avoid-

able expenses, preventing employee turnover becomes an area of prime concern for most of the software firms.

Organizational issues cause more turnover than technological issues among managers in software firms (Longenecker & Scazzero, 2003). It means majority of the factors driving software professionals' retention are controllable for most organizations. This study is an attempt in that direction and makes three important contributions to the related literature. An inverse relationship between Turnover Intention and Job Satisfaction has been established in the literature. As the first contribution, this paper treats Job Satisfaction as two components, Intrinsic and Extrinsic Satisfaction to identify the relative importance of both in the development of Turnover Intention. Second, we consider the influence of three Burnout dimensions on various Job Attitudes in combination with Work Environmental factors, represented by Organizational Politics and Distributive Justice. Third, Distributive Justice has got comparatively less attention within justice literature in comparison with other facets of justice. This study contributes more towards the literature on this understudied facet of Justice.

### **Burnout among Software Professionals**

Burnout among software professionals has been examined only to a limited extent in literature. Salanova, Peiro & Schaufeli (2002) in their review on the relationship between the use of information technology and Burnout have identi-

fied just three empirical studies with complementary results. Software professionals are reported to suffer from either similar or higher stress than many of their colleagues (Hurang, 2001). Analysis of typical software professionals has provided evidence of work overload, role ambiguity, and role conflict.

The three-dimensional conceptualization used by Maslach and her colleagues and its various modifications (Maslach, Schaufeli & Leiter, 2001) is still the most popular inventory to measure Burnout. Emotional Exhaustion is characterized by the lack of energy and a feeling that one's emotional resources are used up. It will usually coexist with feelings of frustration and tension. Depersonalization is characterized by the tendency of employees to treat people as objects. They start to display a detached and emotional callousness, and become more cynical towards coworkers and clients. Diminished Personal Accomplishment refers to the tendency to evaluate oneself negatively. Empirical evidence suggests that Burnout is a process that gradually develops over time resulting in various process models (Lieter & Maslach, 1988).

We also propose relationship among the three dimensions, leading to the development of Burnout among software professionals. Depersonalization is considered a dysfunctional coping and those software professionals who are not able to balance the work stressors will exhibit a tendency to distance themselves from job. Decreasing involvement with work may result in reduced accomplishments

and inability to achieve success, as in past, may lead to increasing Emotional Exhaustion. A process model with Depersonalization as the starting point and Emotional Exhaustion as the final stage will help us consider Emotional Exhaustion as the connecting link between Burnout and various Job Attitudes such as Job Satisfaction, Organizational Commitment and Turnover Intention as in existing literature (Brown & Benson, 2003; Moore, 2000). Hence

H1a: Burnout development among software professionals follows a sequence wherein Depersonalization leads to reduced Personal Accomplishment and reduced Personal Accomplishment leads to Emotional Exhaustion.

### Job Attitudes

Various review papers and meta-analysis have identified Job Satisfaction and Organizational Commitment as intervening variables in turnover process (Hom & Griffith, 1995; Tett & Mayer, 1993). Job satisfaction is generally recognized as a multifaceted construct with intrinsic and extrinsic job elements and research on software professionals emphasized the need to treat them separately (Hars & Ou, 2002).

Highly motivated individuals, who are strongly committed to their work, are more prone to suffer from Burnout. Working in a stressful environment will result in development of Burnout among software professionals with high intrinsic work motivation. Managers may fol-

low a tendency to assign critical projects to highly regarded employees, and these high performers find themselves trapped in an exhaustive situation which will ultimately result in a higher propensity to leave the job (Moore, 2000). Employees who get trapped in an exhaustive situation may not be able to derive satisfaction in those motivators which had been intrinsically rewarding before. Hence,

**Employees who get trapped in an exhaustive situation may not be able to derive satisfaction in those motivators which had been intrinsically rewarding before.**

H2a) Greater the Emotional Exhaustion among software professionals, lower their intrinsic Job Satisfaction.

While conducting research on professionals involved in open-source projects, Hars & Ou (2002) identified certain extrinsic rewards important to software professionals. Mainstream literature on Burnout and Job Satisfaction has treated both Extrinsic and Intrinsic Satisfaction as a combined variable with a negative relationship. Another objective is to compare the relative strength of the relationship of Emotional Exhaustion with both Extrinsic and Intrinsic Satisfaction. Employees suffering from Burnout may not be able to appreciate extrinsic factors such as pay, quality of supervision and administration of fringe benefits. Hence,

H2b) Greater the Emotional Exhaustion among software professionals lower their extrinsic Job Satisfaction.

Studies that have analyzed the relationship with Job Satisfaction, Organizational Commitment and Turnover have come up with conflicting results. While some researchers predict a direct negative relationship between Job Satisfaction and Turnover (Tett & Meyer, 1993) majority of studies conducted across a wide range of employees suggest a mediator role played by Organizational Commitment (Griffeth, Hom & Gaertner, 2000; Price & Mueller, 1986). Degree of Job satisfaction is associated with specific and tangible facets of job and requires relatively lesser time to develop than Organizational Commitment. Commitment with an organization develops over a period of time and more stable in nature. Satisfaction/dissatisfaction with extrinsic and intrinsic aspects of the job influences the development of organizational commitment over a period of time. Hence,

H3a) Greater the Intrinsic Job Satisfaction, greater the Organizational Commitment.

H3b) Greater the Extrinsic Job Satisfaction, greater the Organizational Commitment.

**Organizational Commitment is a strong predictor of Turnover.**

Organizational Commitment is a strong predictor of Turnover (Griffeth et al, 2000; Tett & Meyer, 1993). Mayer & Allen (1991) have come up with three-component conceptualization of Organizational Commitment involving affective, continuance and normative commitment

components. Affective Commitment refers to (a) strong belief and acceptance of the goals and values of the organization (b) readiness of employees to exert considerable effort on behalf of the organization and (c) represents a strong desire to remain as a member of the organization. Committed employees may have a desire to remain within the company because they identify the success and future of the organization with themselves and therefore exhibit a reduced Turnover Intention. Hence,

H4) Greater the Organizational Commitment lower the Turnover Intention.

### **Work Environment**

Previous research has shown the influence of Work Environment factors on Job Satisfaction and Turnover Intention (Griffeth et al, 2000). This study focuses on Work Environment factors such as Organizational Politics and Distributive Justice to study its interaction with Burn-out dimensions in the development of Job Attitudes.

Understanding Organizational Justice as a Work Environment is important for organizations because of its relationship with Job Attitudes such as Job Satisfaction and Organizational Commitment and subsequently to their propensity to search for another job (DeConinck & Stilwell, 2004). It has four distinct justice dimensions such as distributive, procedural, interpersonal and informational justice. Several studies have showed Distributive Justice as a better predictor of Job Satisfaction than procedural in line with Dis-

tributive Dominance Model suggested by Levanthal (1980). Distributive Justice has its roots in Equity Theory. Employees determine whether an outcome was fair by calculating the ratio of one's contributions such as experience and efforts to outcome such as pay and promotion and then comparing this ratio with that of others. Any perceived inequity in this comparison process may result in dissatisfaction. Some of the previous studies (DeConinck & Stilwell, 2004) have studied the relationship of Distributive Justice with extrinsic factors such as pay but not on intrinsic factors. In line with Equity Theory we hypothesize a positive relation with both extrinsic and intrinsic factors. Hence,

H5a) Greater the Distributive Justice greater the Intrinsic Satisfaction.

H5b) Greater the Distributive Justice greater the Extrinsic Satisfaction.

Despite the sound theoretical grounding, very few studies have tested the linkage between Burnout and Justice (Brown & Benson, 2003). Most of the employees consider themselves as good performers and expect equitable and fair returns for the same. Lack of Distributive Justice may prohibit the fulfillment of this expectation, and the employee who believes in the inability of the system to reward him fairly may feel emotionally depleted. Repeated occurrence of such incidents resulting in emotional depletion will finally lead to Emotional Exhaustion. Hence,

H5c) Greater the Distributive Justice lower the Emotional Exhaustion

Organizational Politics refers to the set of behaviors designed to maximize the self-interest, either in short term or long term and has a dysfunctional connotation in this study. Work Environment with a dominant political atmosphere could result in development of negative attitude among employees such as diminished Job Satisfaction (Witt, Andrews & Kacmar, 2000), Organizational Commitment (Cropanzano, Howes, Grandey & Toth, 1997) and greater Turnover Intentions (Cropanzano et al., 1997). In this context individual's perception about the politics attains more significance rather than the objective reality that exists in an organization. While individual employees perceive themselves as a victim of Organizational Politics, they get dissatisfied with both the extrinsic and the intrinsic rewards allotted to them, and exhibit a drop in Organizational Commitment. Other set of employees, who consider politics as undesirable may choose to withdraw from the organization as a means to avoid political activities. Hence,

H6a) Greater the Perceived Organizational Politics lower the Intrinsic Satisfaction, Extrinsic Satisfaction and Organizational Commitment, and greater the Turnover Intentions.

A Work Environment characterized by high-perceived Organizational Politics will not ensure fairness among every employee of the firm. Unfairness in distributing outcome can occur in two ways (Brown & Benson, 2003) in a politically dysfunctional Work Environment (a) al-

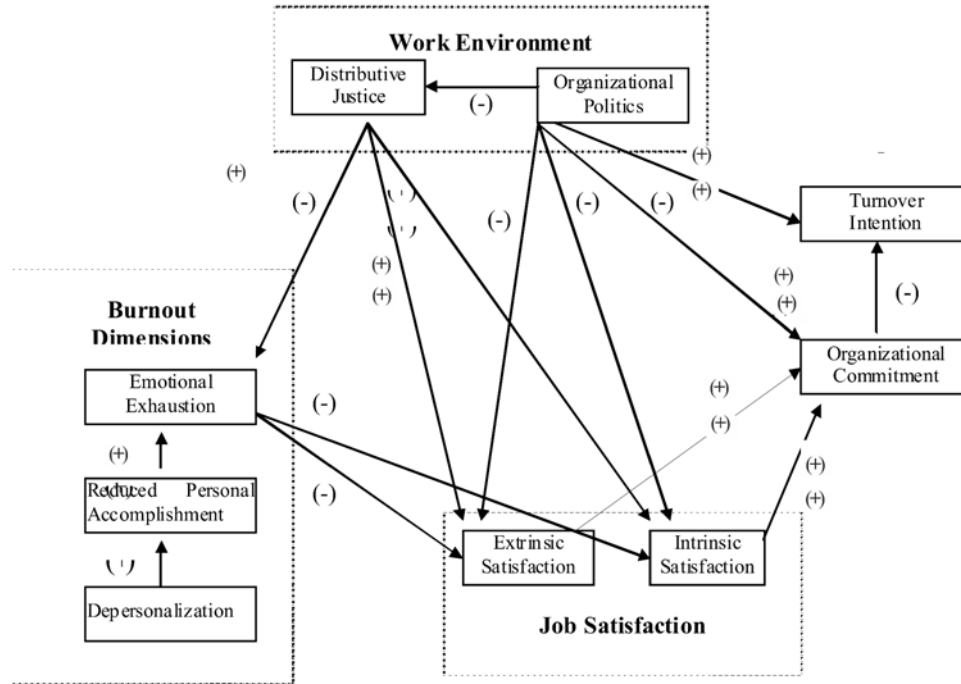


location of high rewards to favorites (b) setting up of unrealistic targets for the employees who are not considered as favorites of power centers. Hence,

H6b) Greater the Perceived Organizational Politics lower the Distributive Justice.

All hypothesized relations with directions are given in Fig. 1

Fig. 1 Hypothesized Model & Variables Included in the Study



**Methodology**

The participants were software professionals working in a medium sized firm in Bangalore, India. In order to ensure the familiarity with organizational fairness and established practices we limited our sample to those employees who have a minimum experience of two years in the current firm. Through HR department of the organization, we contacted the employees and 100 of them volunteered to participate in the study and filled the questionnaire. The mean age was

29.8 years with a standard deviation of 4 within the range between 23 and 46 years. Eighty percent of the respondents were males representing the typical gender ratio existing in most of the IT firms. 63 percent of the participants were married while 30 percent of the entire sample has one or more kids. Average work experience of the participants was 6.7 years with a standard deviation of 3.8 years. To ensure the confidentiality, researcher visited the organization and collected the filled questionnaires directly from respondents.

## Measures

To measure Burnout, twenty-two-item Maslach Burnout Inventory (Maslach & Jackson, 1981) was used generating separate scores for the three sub dimensions, viz., Emotional Exhaustion, Depersonalization and Reduced Personal Accomplishment. Emotional Exhaustion was measured with nine items ( $\alpha = 0.82$ ) like 'I feel emotionally drained during my work'; Depersonalization measured with five items ( $\alpha = 0.64$ ) like 'I feel I treat people in an impersonal manner'; and, Reduced Personal Accomplishment measured by eight reverse coded items ( $\alpha = 0.75$ ) like item 'I have accomplished many worthwhile things in this job'.

Spector (1997) developed a 36 job item measure for Job Satisfaction with nine sub dimensions such as pay, promotion, supervision, fringe benefits, contingent rewards, operating conditions, co-workers, nature of work and communication. Two sub dimensions that failed to report acceptable reliability were removed from further analysis. Seven of the remaining sub dimensions were classified into Extrinsic and Intrinsic Satisfaction. Thus Extrinsic Satisfaction is measured by adding all items under the sub dimensions of Pay, Supervision, Fringe Benefits and Communication (except one item), while Intrinsic Satisfaction had Promotion, Contingent Reward and Nature of Work as sub dimensions. Reliability scores for both were 0.87 and 0.79 respectively.

Ferris & Kacmer's (1992) five-item measure for Organizational Politics was

used, with a scale reliability of 0.78. A sample item was 'There are cliques and in-groups which hinder effectiveness here'. Distributive Justice was measured by a six-item scale developed by Price & Muller (1986) with a scale reliability of  $\alpha = 0.88$ . Items reflect the way in which management considers the effort, results produced, roles and responsibilities in deciding rewards. Allen and Mayer (1990) devised a measure for Affective Commitment with six items. One sample item is 'this organization has a great deal of personal meaning to me'. This study reported a reliability of  $\alpha = 0.73$ , for this measure. A six point Likert scale was used to measure Burnout dimensions, Job Satisfaction measures, Organizational Politics, Distributive Justice and Affective Commitment.

Turnover Intention measured using a single reverse coded item reads as 'length of time you planned to stay in the company'. Options given were ranged from less than one year to more than five years as five possible answers. Other studies have either supported or used a similar kind of measure for similar constructs (Wanous, Reichers & Hudy, 1997).

## Analysis

Path Analysis using Structural Equation Modeling (SEM) was employed to test the model presented in Fig. 1, since it provides a simultaneous test for various study hypotheses. Model parameters were estimated through the maximum likelihood method using LISREL 8.5. Several commonly

used fit indices were used to assess the overall model fit (Jöreskog & Sörbom, 1993): the Chi-square statistic; the Adjusted Goodness-of-Fit Index (AGFI); the Normed Fit Index (NFI), and the Comparative Fit Index (CFI) and the Root Mean Square Error of Approximation (RMSEA). Insignificant Chi-square value is desirable for SEM, since it suggests sufficient closeness between the model developed from samples covariance matrix and the true population covariance matrix. Significance of the specific relationships was estimated by t-values.

**Results**

Descriptive statistics and correlations are presented in Table 1. Chronbach's a reliabilities are in parenthesis along the diagonal.

Initial analysis of the hypothesized model has produced fit indices below the acceptable levels. Hypothesized model indicated a significant ( $p < 0.001$ ) Chi-square value of 51.72 with 21 degrees of freedom. Since all other fit indices (AGFI = 0.78, NFI = 0.74, CFI = 0.80) are below the suggested limit of 0.90, we examined the Modification Indices for theoretically feasible improvement. Two additional paths were added to the model in two steps based on suggested Modification Indices. We added a path from Depersonalization to Emotional Exhaustion (MI = 29.79) first and then another one from Reduced Personal Accomplishment to Affective Commitment. Final model indicated a non-significant ( $p > 0.001$ ) Chi-square value of 11.92 with 18

**Table 1 Means, Standard Deviations and Intercorrelations of Study Variables**

Variables	Mean	SD	1	2	3	4	5	6	7	8
Organizational politics	3.66	1.05	(0.78)							
Distributive Justice	3.62	1.22	-0.51**	(0.88)						
Emotional Exhaustion	2.31	0.76	0.16	-0.16	(0.82)					
Depersonalization	2.01	0.79	0.07	-0.09	0.57**	(0.64)				
Reduced Personal Accomplishment	2.72	0.87	-0.15	0.10	-0.18	-0.12	(0.75)			
Extrinsic Satisfaction	3.51	0.9	-0.62**	0.72**	-0.21*	-0.06	0.13	(0.87)		
Intrinsic Satisfaction	3.93	0.81	-0.57**	0.61**	-0.32**	-0.23*	0.07	0.75**	(0.79)	
Affective Commitment	4.42	0.99	-0.47**	0.43**	-0.18	-0.16	-0.17	0.45**	0.60**	(0.73)
Turnover Intention	2.13	1.06	0.14	-0.25*	0.09	-0.01	0.11	-0.22*	-0.27**	-0.38**

\* Correlation is significant at the 0.05 level (2-tailed) \*\* Correlation is significant at the 0.01 level (2-tailed) Reliabilities (alpha) are on the diagonal

degrees of freedom with acceptable fit indices (AGFI = 0.93, NFI = 0.94, CFI = 1.00). Improvements in fit indices as a

result of incorporating paths based on two Modification Indices are presented in Table 2.

**Table 2 Fit Indices for Various Nested Models**

Nested Models	Chi square	Df	p value	RMSEA	AGFI	NFI	CFI	Largest MI
I	49.53	20	< 0.001	0.12	0.77	0.75	0.80	29.79
I A	20.19	19	>0.1	0.03	0.90	0.90	0.98	8.58
I B	11.92	18	>0.1	0.00	0.93	0.95	1.00	3.09

Among Burnout dimensions the path estimate from Depersonalization to Reduced Personal Accomplishment (t value = -1.15) and Reduced Personal Accomplishment to Emotional Exhaustion (t value = -1.26) turned out to be insignificant, while the path estimate from Depersonalization to Emotional Exhaustion, as suggested by Modification Index remained significant (Standardized path coefficient = 0.53, t value = 6.60). Thus results do not support Hypothesis 1 suggesting a process model on Burnout development.

Hypothesis 2 received partial support wherein the path coefficient from Emotional Exhaustion to Extrinsic Satisfaction has not got empirical support (t value = 0.80), while the path coefficient to Intrinsic Satisfaction got strong support (standardized path coefficient = -0.22, t value = -2.86). In a similar manner the path towards Organizational Commitment from Intrinsic Satisfaction (standardized path coefficient = 0.60, t value = 5.25) got empirical support, while the path from Extrinsic Satisfaction became insignificant (t value = 0.45). Thus results produce partial support for Hypothesis 4. Organizational Commitment ex-

hibited a very strong significant path (standardized path coefficient = -0.43, t value = -3.76) in expected direction supporting Hypothesis 5.

The two hypotheses dealing with the relationship between Work Environment factors and two forms of Job Satisfaction got partial support. The path from Distributive Justice to Intrinsic Satisfaction (standardized path coefficient = 0.27, t value = 4.94) got very strong empirical support while the path to Extrinsic Satisfaction became insignificant (t value = 0.32). There was a very strongly significant path from Organizational Politics to Intrinsic Satisfaction (standardized path coefficient = -0.26, t value = -4.05), and an insignificant path (t value = -1.18) between Organizational Politics and Extrinsic Satisfaction. Results also exhibited moderately strong path to Organizational Commitment (standardized path coefficient = -0.21, t value = -2.42), insignificant path to turnover (t value = -0.49) and finally very strong path to Distributive Justice (standardized path coefficient = -0.59, t value = -5.16) supporting hypothesis 6(b). Final model with significant path coefficients is given in Fig. 2.

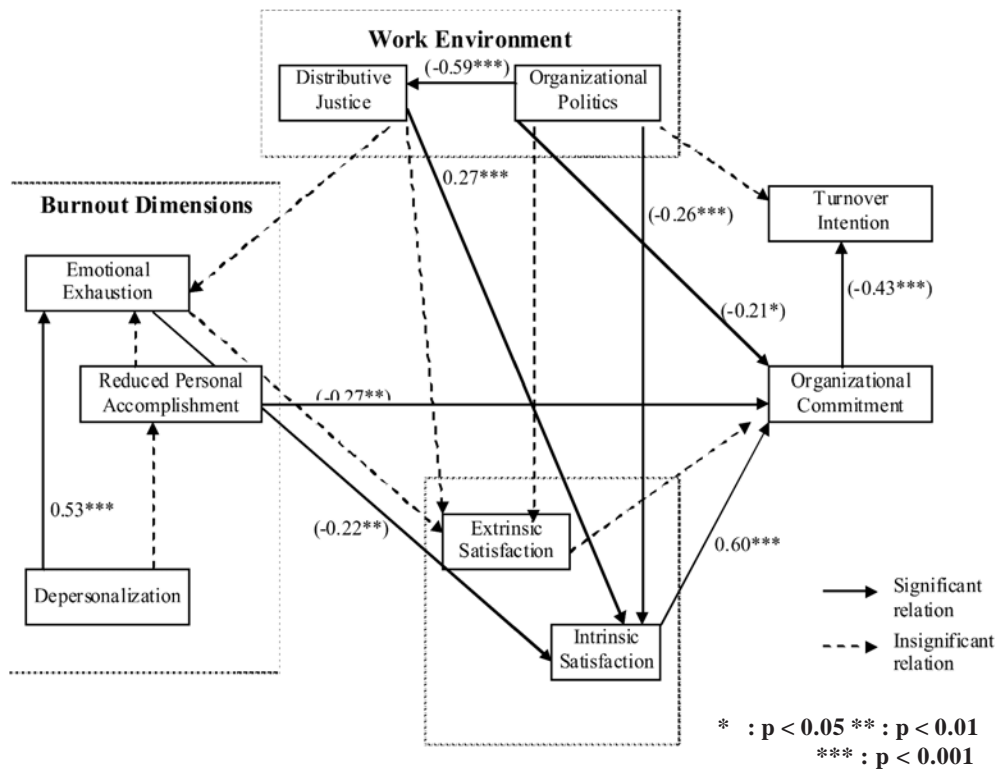
**Discussion**

The effects of Job Attitudes on turnover under various contexts have been well documented. But the combined effects of Work Environment and Burnout dimensions are yet to be explored. Examination of various facets of Job Satisfaction is useful, in understanding the reasons behind employee dissatisfaction and in subsequent preparation of an action plan for resolving the dissatisfaction (DeConinck et al., 2004). Categorization of satisfaction measures into Intrinsic and Extrinsic factors and identification of the

relative importance in a turnover model, serves as the initial attempt in this direction.

Any study on the combined effect on two distinctive sets of psychological constructs starts with identification of its connecting link. Our path analysis results clearly point to Intrinsic Satisfaction as the connecting link between work environment and Burnout dimensions in the development of various Job Attitudes. This constitutes the major theoretical contribution of this study and has great significance to practitioners.

**Fig. 2 Final Model and Standardized Solution from Path Analysis**



Most of the software jobs are highly demanding in terms of: (1) high workload requiring the employees to put in additional hours of extra work, (2) role ambiguity due to the inherent need to work in close relation with people outside their respective fields, (3) lack of sufficient and timely information and (4) nearly impossible deadlines.

According to conservation of resource theory, Burnout occurs as a result of losing certain valuable resources required to meet demands. Lack of resource will lead to Burnout and result in certain behavioral and attitudinal outcomes like coping responses, Turnover Intentions, and attitudinal changes like erosion of Organizational Commitment, Job Involvement and Job Satisfaction. Since certain demands that could trigger strain in the form of Physical and Emotional Exhaustion are inherent and inseparable to this profession, one solution is to increase the availability of resources within the job context. Empirical findings of this study emphasize on the need to provide more Intrinsic Satisfaction in terms of higher autonomy, regular feedback about performance, and identifiable piece of work requiring variety of skills. These initiatives will keep their Intrinsic Satisfaction high and help them derive better satisfaction from their job. It will result in positive cascading effect on other related Job Attitudes like increased Organizational Commitment and lower Turnover Intentions.

Previous research has also failed to get empirical support for the link between Intrinsic Satisfaction and Emotional Ex-

haustion. Houkes et al., (2003) has longitudinally studied the relation among Intrinsic Motivation, Emotional Exhaustion and Turnover Intention in two samples consisting of bank employees and teachers. While proving empirical evidence for Intrinsic Motivation and Turnover Intention, they failed to establish a link between Intrinsic Motivators and Emotional Exhaustion.

**Work Environment factors have a direct impact on Intrinsic Satisfaction while the same is lacking with Extrinsic Satisfaction.**

Work Environment factors have a direct impact on Intrinsic Satisfaction while the same is lacking with Extrinsic Satisfaction. Huang & Van de (2003) in their study across 46 nations conclude that certain basic necessities are a must to ensure Intrinsic Satisfaction. In our study, similar results were not obtained due to two possible reasons. Software professionals are getting a relatively higher pay and better working conditions than their counterparts in other professions and hence Extrinsic Satisfaction in terms of pay cease to motivate them further. They have already shifted to next level of needs (Maslow, 1954) and the current needs are better represented by factors included in Intrinsic Satisfaction. Another possible reason can be explained in terms of the job market condition wherein software professionals are always in demand. Hence, those software professionals who are extrinsically dissatisfied with the organization start searching for alternative employment and move out of the organi-

zation within a short span of time. Organization may try to retain crucial employees by revising their extrinsic rewards to the possible extent. As a result, at any point of time, the number of extrinsically dissatisfied employees in an organization is negligible.

**At any point of time, the number of extrinsically dissatisfied employees in an organization is negligible.**

Our study has not found any support for the relation between Extrinsic and Intrinsic Satisfaction. Highest Modification Index between these two variables is 1.75, which is not significantly strong enough to add a path between them. This indicates partial support for two-factor theory (Herzberg, 1959). Further studies are required to confirm the same in the context of software professionals.

Organizational Politics (OP) seems to be the central variable in this model influencing Distributive Justice, Intrinsic Satisfaction, and Organizational Commitment. Consistent with existing literature, our study found an inverse relation between OP and Job Attitude. Given the fact that politics is inevitable in every organization, management should take proactive steps to minimize the selfish motive arising out of it, by increasing available supportive mechanisms within the organizational context.

Lack of a link between Work Environment factors and Burnout dimensions was a surprise finding, which requires

further exploration in future studies. In line with the relationship between Work Environment factors, Burnout dimensions exhibit a link with Intrinsic Satisfaction (but not Extrinsic Satisfaction) through Emotional Exhaustion.

Our path analysis results failed to support hypothesized process model of Burnout development. While Emotional Exhaustion remains as the core component of Burnout, Reduced Personal Accomplishment seems to develop independently with a negative impact on Organizational Commitment. This result is consistent with previous research (Lee & Ashforth, 1996), which describes differential impact of Burnout dimensions on Job Attitudes. While Emotional Exhaustion exhibited an indirect relationship with Organizational Commitment through Intrinsic Satisfaction, Reduced Personal Accomplishment has shown a direct relation. Realization of a parallel (or simultaneous?) development of these dimensions, will help the managers develop a range of concurrent preventive and supportive measures to tackle the development of Burnout.

While our analysis has revealed interesting findings, many of them are indicative due to some limitations associated with this work. The study was based on the perceptual data collected from a single organization. In such a scenario, actual turnover data would have helped in building a better model, rather than Turnover Intention. In a job market dominated scenario, many of the turnover incidents are guided by impulsive decisions rather than rational decisions. Finally,

cross sectional nature of this study, may result in inherent weaknesses associated with most of the contemporary research of this type.

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**By Contribution**

## **Powerful Leadership & Excellence in Public Enterprises**

**V N Srivastava**

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*Leadership emerges from the core values of the organisation. It has been regarded as an important and powerful driver of excellence when adequately backed by globalization issues and flexibility in leaders' style dynamisms. This paper touches upon the cornerstones of the concepts and constructs surrounding powerful leadership and therefore, cuts across through and between various intervening concepts such as leadership, culture and also change. It provides a spectrum of leadership phenomena to explain the possible kind of leadership that is needed for the public sector enterprises to excel. It supports the theoretical underpinnings with a host of data through a study of a cross-section of senior managers in the organizations.*

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### **Introduction**

Within the literature on leadership, generally, there is a clear recognition of the link between leadership and culture in the process of change (Schein, 1992; Afsanesh, 1993; both cited in Parry & Proctor-Thomson, 2003; Kotter, 1998). Only through leadership can one develop and nurture a culture that is adaptive to change (Kotter, 1998:166). According to Schein (1992, cited in Parry & Proctor-Thomson, 2003), transformational leadership behavior such as directing attention to critical incidents, reacting to crisis, role modeling, formal statements and telling stories, legends and myths influence culture. Kilmann (1985) believes that leadership is critical because, as organisational culture develops and change, they also need to be managed and controlled. According to Bass (1998), survival of the organisation depends upon the shaping of the culture initiated by effective leaders, particularly during change efforts. Kotter & Heskett (1992:84) state that the single most visible factor which distinguishes major cultural changes that succeed from those that fail is 'competent leadership at the top'. They inspire and help create adaptive culture.

Romig (2001) reports that today's organisational leaders required a new kind of person having great managerial leadership talents and who did not depend on top-down organisational superiority and subordination. Reference is to powerful leadership in dealing with normal human responses such as fears, insecurity, self-doubt, confusion, etc firmly and sensitively, give support where it is needed and stand firm in the face of strong resistance. They help to create enhanced capacity in their people and who, in turn, become the steward of all the organisation's stakeholders (McLagan & Nel, 1996). According to them, the new style of leadership requires changes throughout the organisation and culture by looking deep within and transforming themselves, creating direct relationships with employees, helping managers and front line to change, acting as focused visionary and increasing organisational strengths.

### **Excellence in Leadership**

In achieving organisational development and excellence, the role of a successful entrepreneurial and/ or intrapreneurial leader is important and the leader has to be a powerful one who can communicate and inspire by appropriate means, the level of competence necessary to influence a group of individuals to become willing participants in the fulfillment of innovational goals (Darling & Beebe, 2007). They create new ideas, new products and services, new policies, new procedures and effective communication networks. According to Nurmi & Darling (1997) these leaders believe in "attention through vision", "meaning

through communication", "trust through positioning" and "confidence through respect". Through the vision they take their organisations beyond the horizon and the established map.

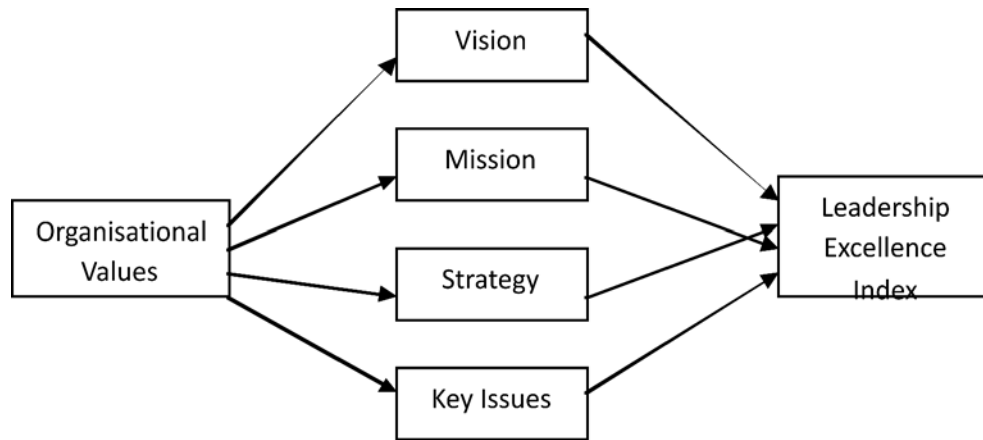
**Leadership is prime and leadership excellence emerges from the core values of the organisation.**

In Kanji's Business Excellence Model (Kanji & Moura, 2001), leadership plays a prime role for the creation of excellence in organisations. According to them, leadership is prime and leadership excellence emerges from the core values of the organisation. Bennis & Nanu (1985, cited in Northhouse, 1997) state that "management controls, arranges, does things right; leadership unleashes energy, sets the vision, does the right thing". This view is shared by Kotter (1990) when he states that the overriding function of the management is to provide order and consistency in organisations, whereas the primary function of leadership is to produce change and movement (Kanji & Moura, 2001). Georgiades & Macdonell's (1998) model also puts leadership at the center of effective functioning of an organisation with three main leadership tasks: establishment of the vision, the alignment of the culture, and specification of management practices. According to Nadler & Tushman (1990), leaders need to provide a focal point for the energies, hopes and aspirations of people and serve as role models whose behaviors, actions and personal energies demonstrate the desired behavior for concrete outcomes.

Kanji's model of leadership (Fig. 1) incorporates critical success factors for leadership identified as vision, mission, strategy and key issues which are essential for achieving excellence in leadership. To emerge as a powerful leader, therefore, the major challenge is man-

aging effectively the relationships among the globalization issues, the organisation's vision, mission and strategy, and leader's style dynamisms. The meaning of each of the model's constructs and relationships among them is explored in Fig. 1.

**Fig. 1 Kanji's Leadership Structural Equation Model**



Source: Adapted from Kanji & Moura (2001:710).

**Global Leadership**

The emergence of global leadership is the offshoot of what we call the management challenges of globalization issues, which need to develop executives to manage and lead from a global perspective (Mendenhall et al., 2003). Leadership began to be regarded as more complex and challenging to drive organisations towards excellence. Scholars came up with identical findings that developing global leadership and business competence in leaders was a high priority (Gregersen et al., 1998; Suutari, 2002; Mendenhall et al., 2003). Osland et al. (2006) identified challenges emanating from global contexts such as geographic

reach in terms of business operations, cultural reach in terms of people and intellectual reach in terms of development of global mindsets. Lane et al. (2004) argued that, as a term, globalization attempts to describe a complexity of four different kinds—multiplicity, interdependence, ambiguity and cross-cultural differences. The field of global leadership development has started developing and scholars are undertaking continuous research and surveys to contribute to this field in the nascent stage of development.

Some scholars have conceded that most competencies associated with leadership from the domestic and traditional leadership literature are necessary to lead

globally. The global context places high demands on the deployment of these competencies that for all intents and purposes render the phenomenon very differently (Mendenhall, 2008) and the study of global leadership therefore becomes necessary. Osland & Bird (2006) distinguish between global and domestic leadership in terms of issues related to connectedness, boundary spanning, complexity, ethical challenges, dealing with tensions and paradoxes, pattern recognition, and building learning environments, teams and community, and leading large-scale change efforts across diverse cultures. Living and working constantly in a global context, and experiencing the ongoing intensity of the dimensions of complexity (Lane et al., 2004) can trigger a transformational experience within managers (Osland, 1995). These powerful transformational or crucible experiences (Osland, 1995, Bennis & Thomas, 2002) have been found to produce new mental models in the individual—new worldviews, mindsets, perceptual acumen, and perspectives that simply do not exist within the people who have not gone through such a series of experiences in a global context.

### **Powerful Leadership**

Combining the strong aspects of what can be had from the traditional leadership literature and those that are essential from the global leadership literature has produced something that can be called as powerful leadership to make domestic organisations not only successful, but also achieve high organic growth amidst the severe challenges thrown or likely to be thrown by global organisations in the domestic place. It

is in this context that a review of global leadership literature will help develop an appropriate framework of ‘powerful leadership’ to have a distinct competitive advantage over global organisations. Domestic organisations, too, have to function together with global corporations as operating in isolation in the context of massive globalization phenomenon today is impossible. Tichy et al. (1992, cited in Mendenhall, 2008) wrote about “true globalists”, as they called them, who have (i) a global mindset; (ii) a set of global leadership skills and behaviors; (iii) energy, skills, and talent for global networking; (iv) the ability to build effective teams; and (v) global change agents skills. These leaders develop people and organisations simultaneously. Kets de Vries & Mead (1992) developed a list of leadership qualities that included envisioning, strong operational codes, environmental sense making, ability to instill values, inspiring, empowering, building and maintaining organisational networks, interpersonal skills, pattern recognition and cognitive complexity, and hardness. Rhinesmith’s (2003) articulation of global mindset has two components— intellectual intelligence and emotional intelligence. Both lead to business acumen and personal management. Articulating the vision, mission and strategy of an organisation is an important attribute of a leader (Kets de vries et al., 2004). Goldsmith et al. (2003) identified 15 dimensions of global leadership and noted that 10 of their dimensions are also found in domestic leadership and continue to be important. They are demonstration of integrity, encouraging constructive dialogues, creating shared vision, developing people, empowering people, customer satisfaction, maintaining competitive

advantage, leading change, achieving personal mastery and anticipating opportunities. Powerful leadership will also require possession of shared leadership, building partnerships and traits of thinking globally.

Goldsmith et al. (2003) list the following important leadership competencies to drive future organisations towards excellence: genuinely listening to others, creating and communicating a clear organisational vision, becoming a role model for living the very same organisational values, uniting an organisation into an effective team, clearly identifying priorities and focusing on a vital few, building partnerships across the company, and constantly treating people with respect and dignity. Leadership competencies to lead in the 21<sup>st</sup> century in domestic organisations can be drawn from McCall & Hollenbeck's (2002) model of global executives. The model is developed based on interviews with global executives (who are also global leaders) and focuses on the interaction and partnership between the individual and the organisation. Most of the competencies are appropriate for leading public and private sector enterprises and a great deal of attention is paid to this model as these can be powerful drivers of organisations towards excellence.

### **A Powerful Leader**

The important competencies required to make a powerful leader, among others, can be: leading and managing others—selection; development, motivation and team building; dealing with problematic relationships—headquarters, bosses, unions, government, media, politics; and

**Leadership will be required to be nurtured at all levels across the organisation.**

developing good leadership qualities within self and others. According to Chopard (2002, cited in Winter, 2003), to successfully manage high performing organisations who, worldwide, are operating in an environment of increasing volatility, high performance leadership is the only way. Leadership will be required to be nurtured at all levels across the organisation. Between 1984 and the present day, three things have changed: scale from national to global, speed from steady to fast, and standards from local to world class. Nelson Mandela influenced the world from his prison cell, and we are talking of a leadership which is powerful and can influence an organisation in the most turbulent state (Winter, 2003). Powerful leadership is bound to make a difference as they inspire creativity in the groups they lead. Efforts such as creative problem solving and strategy are essential to the work of leaders in the knowledge economy (Leonard & Swap, 1999).

Organisational leaders are continuously resorting to one or the other transformation efforts with a strong determination to transform and turnaround towards making it a great organisation. However, as Kotter (1995) reports, most transformation efforts fail, particularly because a critical mistake in any of the phases has a devastating impact, slowing momentum of pace of change and sometimes negative hard-won gains.

Also, many change leaders—internal or external—may have relatively lesser experience in renewing organisations and even very capable people often make at least one big error (Kotter, 1995). Eight steps listed by Kotter (1995) relate to establishing a sense of urgency, forming a powerful guiding coalition, creating a vision, communicating the vision, empowering others to act on the vision, planning for and creating short-term wins, consolidating improvements and producing still more changes and institutionalizing new approaches. Starting a transformation program, cascading it down below, and seeing it achieving transformational goals through the aggressive cooperation of many individuals are important. A paralyzed senior management has too many managers and not enough leaders. Enough real leaders are required in an organisation (Kotter, 1995), particularly ‘powerful leaders’ for driving and leading change towards its transformation and excellence. If a change target is the entire company, the CEO is the key; if it is needed in a division, the division general manager is the key. At all these key positions, great leaders, powerful leaders or change champions are needed. Kotter’s analysis towards creating a powerful guiding leadership coalition to have a minimum mass for something worthwhile to be happening is helpful in understanding the successful transformation efforts.

**If a change target is the entire company, the CEO is the key.**

According to Locander & Leuchauer (2006), the phrase, “simultaneous loose-tight properties” used by Peters & Waterman (1982) captures the essence of the leadership paradox of structure. Organisational units require to be so structured that work can be effectively coordinated, performed and assessed without robbing employees of their dignity, stifling their creativity, and inhibiting their ability (Locander & Leuchauer, 2006). Kotter & Heskett (1992: 146) identify successful leaders as those who repeatedly communicate their vision, allow people to challenge these messages and stimulate middle managers to take up the cause and provide leadership themselves. These are characteristics of transformational leadership and are described by Bass & Avolio (1993) to be made of five key compositions: idealized attributes, idealized influence behavior, inspirational motivation, intellectual stimulation, and individual consideration. Idealized influence and idealized attributes describe leaders who act as role models, can be trusted, are respected and demonstrate high ethical standards. Inspirational motivation involves arousing team spirit, motivation and enthusiasm. It also describes the process of creating vision for the future. Intellectual stimulation describes leadership that supports and encourages innovation and creativity. In addition, intellectual stimulation encourages the followers to question old assumptions. As the fourth transformational leadership style, individualized consideration occurs when leaders pay attention to the developmental needs of the followers, and develop personalized interactions and relationships (Bass & Avolio,

1997). Osterman (1994) found that concern for employees' well being was a primary factor contributing to innovation within an organisation. Podsakoff et al. (1990) defined similar constructs of transformational leadership, including identifying and articulating a vision, providing an appropriate model, and fostering acceptance of goals. Bass (1998) and Podsakoff et al. (1990) conceptualized transformational leadership as promoting flexibility, adaptability and innovation in their followers and their organisations. Gill et al. (1998) believe that the 'new post-bureaucratic organisation' will require transformational leadership for enhancing flexibility, horizontal networks, high-trust relationships, adaptability to change and uncertainty, innovation and empowerment of employees. Such a phenomenon will lead to the necessary reinvention of organisational cultures which, in turn, will lead to organisational success. According to Valle (1999), because of the changing nature of public service, the public sector requires new leadership that will promote flexibility and adaptability in organisations and in individuals. Public sector leadership must provide clear and pronounced vision, effective communication, and inspired motivation towards organisational goals. Leaders who inspire and help create adaptive organisational cultures possess the qualities of transformational leader-

**Public sector leadership must provide clear and pronounced vision, effective communication, and inspired motivation towards organisational goals.**

ship as described by Bass (1998). This may more appropriately be referred to as performance culture. Nutt & Backoff (1993) highlight factors such as using ideals (visions) that are co-created in the place of objectives or goals, moving to be proactive rather than threat driven, adopting innovative ideas, emphasizing participation of key stakeholders, reducing hierarchical distinctions, and empowering followers.

A powerful leadership must, however, use power and trust dimensions judiciously while leading. Kotter & Schlesinger (1979) defines power as "a measure of a person's potential to get others to do what he or she wants them to do, as well as to avoid being forced to do what he or she does not want to do". Machiavelli (1950) suggested fear and love as the main base of power. Hersey & Blanchard (1982) proposed seven bases of power—coercive, legitimate, expert, reward, referent, information, and connection. Pareek (1997, 2003) have given six bases of power in the coercive power group—organisational position (legitimate power), punishment (coercive power), charisma (charismatic power), personal relationship (emotional power), closeness to the source of power (reflected power), and withholding information or resources (manipulative power). He has also proposed six persuasive power bases—reward (reinforcing power), expert power, competence power, behavior power (being a role model), extension power (empathy, caring and helping others), and logical power (based on information and the rationale of the information).



## Followership

According to Kellerman (2007), in an era of flatter, networked organisations and cross-cutting teams of knowledge workers, it is not always obvious who exactly is following (or, for that matter, who exactly is leading) and how they are going about it. Reporting relationships are shifting and new talent-management tools are constantly emerging. A confluence of changes—cultural and technological—has influenced what subordinates want and how they behave. Leaders need to understand bosses better and to understand the dynamics between them and their followers.

At times they also act by withholding support from bad leaders, throwing their weight behind good ones, and sometimes claiming commanding voices for those lower down in the social or organisational hierarchy (Kellerman, 2007). CEOs share power and influence with a range of players, including boards, regulators, and shareholder activists. Expertise can—and often does—trump position as an indicator of who really is leading and who is really following (Drucker, 1967, cited in Kellerman, 2007). Kellerman also points out that relationship between superiors and their subordinates is not one-sided and nor are all followers one and the same. Followers too act in their own self-interests as leaders do. While followers may lack authority, at least in comparison with their superiors, they do not lack power and influence. According to Waterman (1994), to be a true leader, one needs to give up control in a

**Shared leadership is expected to gain prominence as the operating model of the future.**

narrow sense to have control in a much broader sense.

## Public Sector Leadership

Leaders, according to Goldsmith et al. (2003), can not embody all of the needed critical capabilities. However, in the present times of globalization issues, where the very changed nature of business organisation (merged, behavior, outsourced and virtual) is beginning to dictate organisations, shared leadership is expected to gain prominence as the operating model of the future. In future, there will be fewer “all knowing” CEOs; instead, leadership will be widely shared in executive teams. New demands for collective responsibility and accountability will emerge, as will competencies for sharing leadership. Not one person only, but more than one person will lead organisations collectively (Osland, 2008, cited in Mendenhall, 2008:51-52). Leaders style dynamism is about high performance leadership, developing leadership at all levels, shared leadership, and developing a second in command.

According to him, “high performance leaders” must harness two energies that are the “performance drivers”—mental and relationship energy, and two energies that are “performance enablers”—physical and emotional energy. Performance leaders can not build and capitalize on the knowledge, creativity and relationships

unless their physical energy (endurance) and their emotional energy (resilience) permit. Many leaders invest vast time and effort in increasing their knowledge and relationships and then fail to use these resources because of physical and emotional fatigue. Though some reviews had concluded that the situational leadership model has some logical and internal inconsistencies and lacks empirical support, it has been found to be adequately representing reality. Blank et al.'s (1990) framework also provides supportive evidences and is based on the assumption that subordinates' maturity moderates the leadership task relationship behaviors with indicators of leader effectiveness.

### **Research Based Analytics**

A qualitative research methodology was carried out using individual interviews and focus group discussions to assess the important issues that typically are associated with the achievement and nurturance of excellence. About 20 individual interviews of about 20 senior managers in public enterprises and 4 focus group discussions (6 - 7 in each group) were carried out.

Three important factors identified that was felt to be important related to:

1. Top Management Leadership
2. Leadership Effectiveness
3. Super-Speciality Centered Leadership

Within each of these factors of powerful leadership, it was found that there

are some sub factors which gives some kind of identity to leadership and they are discussed under each identified factor.

### **Top Management Leadership**

The top leadership in public enterprises needs to be full of dynamism and is evidenced by the fact that it is highly talked about also at every place in the organisation even when he has left the organization. His examples are often cited and have often left a deep mark on everybody's mind. The important sub factors of this phenomenon of leadership that came out were:

- i) *Vision Document Development:* Development of a vision document appears a theoretical exercise; however, it is important in traversing some distance in a planned way, though, mere development of a document does not guarantee or ensures achieving excellence. Referring to such an initiative by one of the public sector CMDs of public sector Hydropower Company, a group of employees mentioned:

“The present CMD has got a vision document developed: ‘Hydro Power 50000 MW initiative’. In this, projects worth 50000MW are identified and vision document prepared for development across the country. Policy makers have been persuaded and there is a constant push for hat by the top leadership. Vision document of public enterprises is a very valuable document related to public enterprises vision and mission fulfill-

ment. The present CMD's strengths are talked about as regards dynamism is concerned".

**Vision document of public enterprises is a very valuable document related to public enterprises vision and mission fulfillment.**

The powerfulness is being continuously talked about by people below. "What the great ones do, the less prattle off" (Shakespeare in Julius Ceaser). This is an important indicator of powerfulness of leadership.

ii) *Turnaround Leadership*: "In one of the public sector enterprises, a leader who had a stay of more than 7 years in the organisation is regarded as a turnaround leader because of whom the organisation is what it is today. The state of public enterprises when he took over as a CMD was not very good and was a 3500 MW company. However with his strategies, drives and plans it had had a continuous growth of projects, JVs etc and the projects finalized by him have started giving results now".

iii) *Global Leadership Initiatives*: "Public enterprises have started making a concerted drive towards achieving a place in the international community by beginning to providing consultancy services to developing countries in their areas of core competence such as hydropower engineering by an enterprise in hydro-power generation".

"It is a good thing. Achieving a world-wide status is one of the missions of public enterprises".

iv) *Leadership Ownership*: "In some public enterprises, leadership has been changing frequently and has been for durations ranging between 1-7 years, which in one case reportedly had the longest duration of 7 years. The next longest duration was 5 years. It is observed and also reported that there has been a maximum growth of the said public enterprises during this period."

Continuity of leadership is an important issue for higher organic growth. Enterprise may spirally go up or even go down.

### Leadership Effectiveness

i) *Assertive Leadership*: "A widespread feeling persists of the Ministry not giving free hand to some public enterprises and making frequent interferences in functioning. More than half of the time of the top leadership would be getting away in managing these interferences. At times, many CMDs act assertively, giving high empowerment to people and are supportive to innovative ideas and initiatives. As assertive leaders, they aptly manage what is called the 'interferences' coming from the bureaucratic and governmental regimes / processes, and not put them forth as limitations and constraints for achievements. A high clarity of directions with every decision has high

impacts in terms of motivation towards achieving excellence”.

- ii) *Developing Managers as Leaders:* “There is no specific initiative for developing leaders for taking up positions at various plants, projects, regions, etc. It is purely based on seniorities, competencies, exhibition of talents in positions held and also the personal choice of CMD. This is an important factor as evidenced by many respondents saying, ‘it is CMD’s team’. Through this process very dynamic heads of projects have been identified. In some places, projects have been completed in a record period of time and is among one of the talked about projects is an example. Heads of projects are generally given freedom to choose their team and members are not forced upon him for deliveries in the project. They are generally from among those who have earlier worked in the past with him and according to those project heads, they are capable of giving results, have gone through the project hardships”.
- iii) *Powerful Followers:* “Powerful followers, defacto the ‘leaders of tomorrow’ have made to the top levels including the ‘board’ level. They have reached those levels by greater trust, support, and empowerment and shared leadership processes. They have reached these positions by way of strength of their hard work. They have the capacity to take the organisation forward. There are also some at the chief level, plant level, who have huge capacity but do not get freedom need to be made good followers by giving good support to them. The followers wanting to take challenging tasks, if are supported in true spirits, will become very good followers who will be the future leaders.
- iv) *Developing Leadership Skills:* “Leadership development initiatives are mostly by way of exposing employees to leadership concepts and challenges for change and growth. There is also high emphasis of developing leadership among officers at Manager and above upto Executive Director through processes such as competency mapping, assessment and development centers”.
- v) *Coaching Subordinates:* “Whenever a subordinate is in a fix to decide between one he is being asked to do and what he is actually wanting to do is basically confronted with value laden issues, superiors have been found in some instances to giving their subordinate a patient hearing and facilitating him to take the most appropriate decision. The effort observed has been to building strength in the subordinate and develop or adapt more flexibility in leadership than remaining in a state of rigidity which is important for getting results”.
- vi) *Project Leadership Challenges:* In some public enterprises particularly the hydropower enterprises, the leadership has been admired for their capacity to achieve amidst odds, as

cited by some respondents: “Each project has a typical problem with respect to geographical and geological conditions, and tunneling operations for dam construction requires different strategies. Various issues also require to be handled particularly relating to environment, water, apart from technical drives required. A powerful leadership for completing projects before time is required”.

vii) *Developing Subordinate*: “There have been many instances where subordinates have been developed by superiors. They have been informally guided and coached to obtain higher qualifications and that has helped in raising knowledge levels of people in the organisation”.

### **Super-Speciality Centered Leadership**

“Based on three different nature of work involved in setting up hydro power plants, such as investigation, design and construction, the technical employees have developed specialized skills (super speciality) in their respective areas of working. Organisation has been particular about this and has provided several opportunities to those who have developed these kinds of specialities by providing international consultancy”.

i) *Leadership Development by Understudy*: “There has been a process of placing junior or new appointees at officer and supervisory levels to those having engineering degree and diploma but do not have experience. By working with those who have

been working on various projects for a long time these employees have been developing but of late since there has been reduced intakes at entry levels and so this process of developing as an understudy has also reduced. This has however been a very effective way of developing high level of technical competence among novice engineers and diploma holders”.

ii) *Work Pressure Management*: “The top leader has to manage high pressure from various quarters, central government, state government, local political leaders, union, and many others including difficult working conditions. In one project of a public sector, the tunnel boring machine got stuck in the mountain. The same is there and the decision is to be taken by the government and also to some extent political as local people are involved”. The environmental clearances are a part of public sector management and needs to be handled as per the environmental policies.

### **Conclusions**

Leadership needs to be given due importance to in public enterprises. Public enterprises need to focus on developing effective leadership skills for transforming organisations, and leading and managing change. A good leadership can transform an organization and help achieve excellence. There are several skills in those leaders and it is suggested that organizations undertake planned Leadership Skills Development programs at various levels.

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**By Contribution**

## **Strategy & Structural Dimensions – A Comparative Study of Four Industries**

**Bindu Gupta & Ajay Singh**

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*This study examines the linkage between organization's strategy and structural dimensions. There are significant differences among the organizations in terms of structural dimensions and the strategy used. Prospector strategy is used more in the IT industry, analyzer strategy in the banking industry and reactor strategy in power industry. Vertical linkages and formalization are more used in the power sector, horizontal linkages in automobile sector, centralization in banking sector. When the organization uses reactor as dominant strategy, vertical linkages and formalization were perceived more. Horizontal linkages are more prevalent in the organization using prospector strategy and organizations using the analyzer strategy were found to be high on centralization.*

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### **Introduction**

Organization Structure is a dynamic element which can change over time as a consequence of new organizational and environmental conditions. It reflects the way in which information and knowledge are distributed within an organization and it substantially influences the distribution and coordination of the company's resources, the communication processes and the social interaction between organizational members (Chen & Huang, 2007). It can be frequently customized so that staff could have access to and acquire new and varied knowledge that would help them to overcome a range of problems, fluctuations and diverse situations (Lloria, 2007). Studies (e.g., Dodgson, 1993; Fiol & Lyles, 1985) also have suggested that structures have an influence on the organization's learning ability. Researchers further suggest that organizational personnel are meaningless unless some type of structure is used to assign people to tasks and connect the activities of different people or functions (Denison, 2000; Drucker, 1974).

**Organizational structure may obstruct or support the capacity of the organization to adapt, innovate or improve its ability to add value for its customers.**

Organizational structure may obstruct or support the capacity of the organization to adapt, innovate or improve its ability to add value for its customers and to its performance. One of the purposes of the study was to understand the organizational strategy and structure in Indian organizations belonging to different industry segments. It also examines the relationship between strategy and structure. Although, there have been rich theoretical and empirical descriptions about structure and strategy (e.g., Schaffer & Litschert, 1990; Tse, 1991), this study intends to examine it further in the Indian context. The rationale behind are that the Indian culture is different from the western culture. Research suggests that when national and organizational cultures come into conflict, the national culture is likely to dominate (Hofstede, 1980; Pang et al., 1998).

Peters and Waterman (1982) and others reported that organizations in the United States (US) are influenced by national cultural values: there have been focus on open and honest communication and teamwork and staff are being empowered to make decisions (Mwaura et al., 1998). Hofstede (1980) found that in cultures with high power distance relationships, employees have limited expectations for participation in decision making. Given such cul-

tural considerations, the findings pertaining to the relationships between strategic orientation, organization structure and performance may not apply in the Indian cultural context, as Indian culture has been rated high on power distance and also differ on other value dimensions from US culture.

### Organizational Structure

Child (1972) defined organizational structure as “the formal allocation of work roles and the administrative mechanisms to control and integrate work activities including those which cross formal organizational boundaries”. Daft (1998) stated that organization structure determines the formal reporting communications and represents the levels which exist in administrative hierarchy and also specifies the extent of the managers’ control. The people’s formal communications, job status in an organization, the extent of accessing information, job descriptions, resource allocation, rules and regulations, compliance and implementing the rules, co-ordination between the activities, depend on designing organizational structure (Ergenli et. al., 2007). To understand the organizational structure, number of structural dimensions has been identified in various studies. Among the many structural dimensions, formalization, integration, centralization and complexity are commonly used in describing structural characteristics.

Centralization is the degree to which employees are empowered to make decisions. When decisions are kept at the top, an organization is centralized,

whereas in decentralized organizations, decisions are delegated to lower organizational levels (Daft, 1998). Formalization can be defined as the extent to which an organization uses rules and procedures to prescribe behavior such as the details on how, where, and by whom tasks are to be performed (Fredrickson, 1986). In the organization with higher level of formality, there are many bureaucratic and rigid rules and set procedures, and little individual freedom of action (Ahmed, 1998).

Complexity describes many, usually interrelated, parts of an organization (Fredrickson, 1986). Structural integration refers to the coordination of activities among the different specializations within the firm (Miller, 1987). The more the complexity increase, higher is the need for structural integration in the organization which can be in the form of vertical or horizontal linkages. Vertical linkages are used to coordinate corporate activities between the top and the bottom of the organization. Top management controls planning, problem solving, decision-making and directing (Hyden, 1994; Hankinson, 1999). Horizontal linkages help to integrate the different functions, units and expertise in the organization.

These structural dimensions influence firms' ability to perform efficiently or effectively. Studies indicates that members in highly centralized organizations had less motivation to learn, and were less efficient and slower in making decisions (Duhaime & Schwenk, 1985; Slevin & Covin, 1995). An organization with higher degree of formalization and cen-

**An organization with higher degree of formalization and centralization may make it easy to avoid chaos, inconsistency, and duplicated efforts.**

tralization may make it easy to avoid chaos, inconsistency, and duplicated efforts, especially within a large, complex organization (Adler, 1999). Chen et al., (2009) reported that formalization and centralization of organizational structure would affect staff's absorption capacity, and further affect organizational innovation performance.

An innovative organization needs open channels of communication, decentralization and informal decision making, and flexibility in processes and procedures. Loosely coupled decision linkages and loosely identified job descriptions are conducive to greater entrepreneurial and innovative activity (Mintzberg, 1979). Azadegan, (2008) opined that an organization with lower centralization has better capabilities for organizational innovation. Chen and Chang (2012) reported that the higher the degree of organizational centralization, the lower the absorptive capacity of the organization, and then the lower the degree of organizational innovation.

### **Organizational Strategy**

Organizational strategy can be defined as a plan for interacting with the competitive environments to achieve organizational goals (Daft, 1998). Through its strategy, an organization selects and

interprets its environment, and adapts its strategy to the requirements of the environment (Porter, 1985). Miles and Snow (1978) classified strategy types as defender, analyzer, prospector, and reactor. Defenders are internally oriented organizations. They stress efficiency, and are tightly organized firms focused on maintaining a niche with a limited range of products or services (Miles & Snow, 1978). They try to protect their markets through lower prices, high-quality, well-targeted products, and superior delivery while not often being at the forefront of industry developments. The prospectors have an external focus and assumes more business risk and attempt to be “first to market” with new products and services. These firms emphasize more in maintaining the image of an innovator in product terms than securing high profitability (McDaniel & Kolari, 1987). The structure of these firms is characterized by a low degree of formalization and routine, decentralization and lateral as well as vertical communication, emphasizing aspects such as innovation and flexibility.

Analyzers blend the characteristics of both the prospector and defender orientations (Miles & Snow, 1978). They are rarely first-in with new services or into new markets, but are often second-in with better offerings. The analyzer partitions its technology so that it can serve its stable domains with efficient technologies and its dynamic domains with flexible and effective technologies. They include flexibility as well as stability, adopting structures that can accommodate both stable and changing domains.

**Reactor organizations do not present any consistent pattern of response behavior to environmental conditions.**

Reactor organizations do not present any consistent pattern of response behavior to environmental conditions and their actions are mostly reaction to outside forces, such as the economy, competitors, or market pressures.

### Strategy & Structure

Why some organizations outperform others? The answer is grounded on the contingency perspective. It advocates that organizational structure follows from a firm’s strategic choices in response to its environment and successful firm performance to some degree results from a proper fit between environment, strategy and structure (e.g., Chandler, 1962; Child, 1972). It provides a motivation for an organization in misfit to move into fit to gain the higher performance that fit produces (Burns & Stalker, 1961).

Porter (1980) claims that organizations require a high degree in all of the structural dimensions in order to implement generic strategies. Miller (1988) reported that integration and formalization are relevant for performance for specific strategic types. Zeffane (1989) reported that certain structural dimensions must be present with given strategies in order for the firm to achieve high performance level. All these indicate that a ‘fit’ or, alternatively, an interaction between strategy and structure is relevant

to performance, hence managers must design the organization correctly if it is to be effective for a particular strategy (Fiedler, 1984; Fegghi Farahmand, 2005).

### Objectives of the Study

- a) To examine the structural dimension of the Indian organizations belonging to different industry segments
- b) To examine the strategy used by the Indian organizations belonging to different industry segments.
- c) To examine the relationship between strategy and structure in the Indian context.

### Hypotheses

- H1: There are significant differences in the structural dimensions used by organizations from different industry segments.
- H2: There are significant differences in the strategy used by organizations from different industry segments.
- H3: Organizations following defender strategy are high on formalization, centralization and vertical linkages.
- H4: Organizations following prospector strategy are high on both vertical and horizontal linkages.
- H5: Organizations with analyzer strategy are high on centralization and horizontal linkages.
- H6: Organizations following reactor strategy are high on centralization and formalization.

### Methodology

Data were collected by means of questionnaires that were sent through electronic mail. Overall 1000 questionnaires were mailed, and 431 usable questionnaires were received, with response rate 43.1 percent of respondents. The respondents came from 16 organizations from four industries namely, Banking (34.2%), Information Technology (22.3%), Power (18.3%), and Automobile (20.3%). Those selected for the study are high performance organizations within their industry segment and represent a right mix of public, and private sectors.

The average age of participants was 34.08 years, average experience in current organization being 4.96 years. Only those employees were requested to respond to questionnaire who have minimum three years of experience with the present organization. With respect to the level of qualifications, 65 percent were graduates; and 35 per cent were post-graduates. Male respondents accounted for 70 percent and 30 percent were the females.

*Banking:* Banking in India has a long and detailed history of more than 200 years. It includes nationalized banks, private banks and specialized banking institutions. Nationalized banks are the biggest lenders in the country because of the size of the banks and the penetration of the network. According to a World Bank report, there are around 3.5 ATMs and less than seven bank branches per 100,000 people and there will be improvement in near future as the Government

aims to have maximum financial inclusion in the country. (<http://www.ibef.org/industry/banking-india.aspx>).

*Information Technology:* This is among the rapidly growing industries in India and has created a brand equity for itself in the global markets. According to the report by Confederation of Indian Industry (CII), India's IT-business process outsourcing (BPO) industry revenue is expected to cross US\$ 225 billion mark by 2020. The report by Internet and Mobile Association of India (IAMAI) and IMRB International suggests that India is expected to become world's second-largest online community after China with 213 million internet users by December 2013 and 243 million by June 2014. All these reports suggest the potential of growth in this industry.

*Power:* India is the 5th largest power producer and one of the most diversified sectors in the world. The Planning Commission's 12<sup>th</sup> Plan projects that total domestic energy production would reach 669.6 million tons of oil equivalent (MTOE) by 2016–17 and 844 MTOE by 2021–22 (<http://www.ibef.org/industry/infrastructure/power-sector-india.aspx>).

*Automobile:* India is predicted to be among the world's top five auto-producers by 2015, with the increasing growth in demand with rising income, expanding middle class and young population base along with a large pool of skilled manpower and growing technology (<http://www.ibef.org/industry/india-automobiles.aspx>). Experts opine that in developed economies, automobile manu-

facturers buy more components and services from suppliers than they are used to and are increasingly relying on them to reduce costs, improve quality, and develop new processes and products faster than their rivals' can.

## Measures

*Business Strategy:* A multi-item scale developed by Parnell (1997), based on the work of Conant et al. (1990) was used for operationalizing the Miles and Snow strategic typology. There were a total of 12 questions with each consisting of four statements, one for each possible strategy. Each respondent was required to indicate which statement is true for his/her organization. The twelve responses for each participant in each organization was used to classify the business into one of the four strategy categories, depending on which strategy received more than or equal to 50 percent responses.

*Structure:* Structural configuration was measured by fourteen items designed to determine the dimensions, including vertical linkages (3 items), horizontal linkages (2 items), centralization (5 items), and formalization (4 items). These structural dimensions were measured using a scale ranging from [1] strongly disagree to [5] strongly agree. Reliabilities are as follows: .65 for vertical linkages, .60 for horizontal linkages, .65 for centralization and .77 for formalization.

## Results

*Business Strategy:* Table I shows the mean scores for all the strategies for each

industry. The results of ANOVA with repeated measure on strategy indicated the significant difference in the use of these four strategies ( $F(3, 428) = 110.60$ ,  $p, 0.00$ ). The result of ANOVA also indicated the significant differences in different industries for the use of prospector, analyzer, defender, and reactor strategies ( $F(3, 427) = 13.98$ ,  $p <, 0.00$ ;  $F(3, 427) = 106.83$ ,  $p <, 0.00$ ;  $F(3, 427) = 8.90$ ,  $p <, 0.00$ ; and  $F(3, 427) = 113.10$ ,  $p <, 0.00$ ), respectively. Thus the results support the stated hypotheses (H1) that there are significant differences in the use of strategy by the organizations from different industries. The mean scores indi-

**There are significant differences in the use of strategy by the organizations from different industries.**

cate that prospector strategy is used more in IT sector and less in power industry. Analyzer strategy is used most in banking sector. Reactor was reported to be used more in power sector (Table I). Defender was reported the least used categories across all strategies. Therefore, further in the analysis, no organization was categorized as belonging to defender strategy.

**Table 1 Mean Scores for Business Strategies**

Industry		P	A	D	R
Automobile	Mean	2.80	3.09	2.13	3.91
	N	92	92	92	92
	Std. Deviation	1.55	1.33	1.40	1.38
Banking	Mean	3.12	4.69	1.53	2.63
	N	155	155	155	155
	Std. Deviation	1.55	1.60	1.53	1.22
Information technology	Mean	4.05	3.19	1.80	2.95
	N	101	101	101	101
	Std. Deviation	1.93	2.28	1.27	1.99
Power	Mean	2.77	.72	2.41	6.09
	N	83	83	83	83
	Std. Deviation	1.03	.85	.91	1.08

Note: P- Prospector Strategy; A- Analyzer Strategy; D – Defender Strategy; R-Reactor Strategy

*Structural Dimensions:* Table 2 shows the mean scores for all structural dimensions for each industry. The results of ANOVA with repeated measure on structural dimensions indicated the significant difference in the use of these structural dimensions ( $F(3, 427) = 41.27$ ,  $p, 0.00$ ). The result of ANOVA indicated the significant differences among industries for the use of vertical linkages, horizontal linkages, centralization, and formalization

( $F(3, 427) = 77.54$ ,  $p <, 0.00$ ;  $F(3, 427) = 48.68$ ,  $p <, 0.00$ ;  $F(3, 427) = 40.49$ ,  $p <, 0.00$ ; and  $F(3, 427) = 103.26$ ,  $p, 0.00$ ), respectively and support the stated hypotheses (H2). The mean scores indicate that vertical linkages are more used in power sector than in IT sector. Horizontal linkages were reported in automobile sector centralization was reported more in banking sector and formalization is highly prevalent in power sector (Table 2).

**Table 2 Mean Scores for Organizational Structural Dimensions**

Industry		Vertical linkages	Horizontal linkages	Centralization	Formalization
Automobile	Mean	3.73	4.00	3.89	4.07
	N	92	92	92	92
	Std. Deviation	.62	.66	.38	.41
Banking	Mean	3.75	3.71	4.11	3.49
	N	155	155	155	155
	Std. Deviation	.68	1.01	.55	.65
Information Technology	Mean	3.12	2.93	3.37	3.40
	N	101	101	101	101
	Std. Deviation	1.15	.98	1.17	1.13
Power	Mean	4.81	2.78	3.23	5.00
	N	83	83	83	83
	Std. Deviation	.24	.28	.27	.00

**Strategy Structure**

Table 3 shows the mean scores of organizational structural dimensions for different strategies used by different organizations. Results of ANOVA indicated significant differences in the use of structural dimensions namely vertical linkages, horizontal linkages, centralization, and formalization with respect to the dominant strategy used by organizations ( $F(2, 428) = 60.84, p < 0.00.$ ;

$F(2, 428) = 23.19, p < 0.00$ ;  $F(2, 428) = 19.54, p < 0.00.$ ; and  $F(2, 428) = 82.70, p < 0.00$ ), respectively. Vertical linkages and formalization are perceived more when organization was reported to use reactor as dominant strategy. Horizontal linkages are more prevalent in the organization which followed prospector strategy. Organizations using the analyzer strategy were found to be high on centralization than organizations using other strategies.

**Table 3 Means Scores for Organizational Structural Dimensions for Different Strategies**

Strategy		Vertical linkages	Horizontal linkages	centralization	Formalization
Analyzer	Mean	3.34	3.29	3.96	3.34
	N	167	167	167	167
	Std. Deviation	.96	1.17	1.02	.98
Prospector	Mean	3.76	3.87	3.73	3.24
	N	127	127	127	127
	Std. Deviation	.81	.76	.56	.53
Reactor	Mean	4.38	3.13	3.42	4.50
	N	137	137	137	137
	Std. Deviation	.64	.66	.42	.68

**Discussion & Conclusion**

As the earlier researches suggest managers must design the organization

correctly if it is to be effective for a particular strategy (Fiedler, 1984; Feghhi Farahmand, 2005), the present research focused on identifying the strategy and



structural dimensions adopted in the Indian organizations and their alignment with the strategy of the organizations. The contribution of the study lies in examining the differences in the strategy and structure of organizations belonging to different industry sectors. The business environment varies for different industries and influenced by number of factors such as stakes of government, number of competitors, entry of global players, maturity of the industry, government regulations for the new entrant, requirement of capital, scope of innovation, dependence on the suppliers etc. which are likely to influence the internal characteristics of the organizations. The findings of the study support the hypotheses proposed for investigation and suggest that there are significant differences among organizations belonging to different industry segments in terms of structural dimensions and strategy. Also the use of structural dimensions varies depending on the strategy adopted by the organizations. These findings support those of Gupta, (2011) in the Indian context examining the differences in the use of strategy by organizations from different industry segments.

**The use of structural dimensions varies depending on the strategy adopted by the organizations.**

Organizations from the IT sector were reported to use the prospector strategy, and banking organizations the analyzer strategy. Organizations from automobile and power sectors have been found to use reactor strategy. Different explanations can be given for the same.

Miles and Snow (1978) proposed that organizations develop relatively enduring patterns of strategic behavior to co-align the organization with the environment. Prospectors perceive a dynamic, uncertain environment and maintain flexibility to combat environmental change and seek to identify and exploit new products and market opportunities. Indian IT industry started to cater to the needs of global clients, now going through a shift and there are a lot of opportunities for growth in this sector as opined by experts. These facts may justify respondent's perception of the organizations using the prospector strategy. Regarding the power sector, the electricity generation capacity in India is the fifth largest in the world, still there are number of issues such as a substantial percentage of population still in blackouts, frequency of power cuts, industrial customer facing problem, and regulations by state government etc. may be the reasons why power sector has been reported using reactor strategy.

Given the dependence on suppliers for auto parts, developing horizontal linkages becomes the major need of organizations from automobile sector. In the power sector any single mistake can be very expensive, that is why control and coordination is achieved through vertical linkages and formalization. Organizations belonging to banking sector were perceived high in centralization, the reason may be that the different branches of the bank spread over different geographies are controlled by the policy framework of corporate office and banking sector is governed by regulations by Reserve Bank of India. For IT sector,

most of the responses came from the employees working on client's projects, and that may be the reason why employees perceived that there is high degree of centralization and formalization.

As regards the relationship between strategy and structure, the direction is viewed differently by different authors. Some studies view structure as following strategy while others say strategy follows structure (Fredrick, 1986). While, the direction of causality between strategy and structure is beyond the scope of this study, our results indicate that these two are interrelated and need to be aligned to ensure organizational success and support the findings of earlier studies.

**The more proactive and aggressive a firm's strategic posture is, the more flexible its organizational structure would have to be.**

Organizations with the prospector strategy need to have a structure which can respond to particular control, coordination and learning problems created by a high degree of organizational innovativeness. Organizations with prospector strategy use more horizontal and vertical linkages and less centralization and formalization compared to organizations using other strategies. These findings are in alignment with Day (1986) who views that the more proactive and aggressive a firm's strategic posture is, the more flexible its organizational structure would have to be, to allow it to take advantage of new technologies, new

markets, and other changes in the value-added system. The overuse of vertical linkages and formalization may be the reasons the organizations reported using reactor strategy are not able to sense the changing environmental forces and have reacted when are faced with crisis. Nahm et al., (2003) also indicated that a formalized structure may result in employees losing their courage of innovation, independence and learning opportunity. Organizations using analyzer strategy were reported to use more centralization, the reason being that management wants to make sure that there is free flow of ideas as well as effective implementation of the same.

### Implications of the Study

This study suggests that the organizations that operate in different competitive environments and rely on different types of strategies should have different structural dimensions which help them to meet the unique demands of the competitive environment. The results obtained by the study have implications for Indian organizations:

- (1) Organizations in the Information Technology sector need to use more prospector strategy as there is lot of untapped market in this sector and scope for growth and innovation.
- (2) Organizations in the banking industry need to have blend of defender and prospector strategies, which can help the organizations to do its traditional roles of monetary transactions as well as to come with the new products

and services to meet the needs of customers.

- (3) Organizations with prospector strategy should support it with more vertical and horizontal linkages, which help to bring successful innovation.
- (4) Organizations which are high on vertical linkages and formalization are not able to identify and use the right strategy to position themselves.

### Conclusions

This study endorses the contention that structural dimensions need to be aligned with strategic intent. As the organization's strategy evolves, managers need to create or modify systems and structures to effectively implement the type of strategy selected. The findings of the study can be used as guidelines to select the right strategy and structural dimensions for the organizations to suit their environment.

The present study has also some limitations that need to be addressed in future research. The study could have assessed the performance of the organizations in terms of both financial and non-financial indicators which can be strong indicators of how the congruence between strategy and structural dimensions influence organization's effectiveness. Yet, some inferences can be made as the organizations surveyed were among the top in the country. Further the study did not examine the differences among organizations belonging to same industry segment as Indian organizations vary in terms of ownership, i.e. public, private

and multinational organizations. Future study can examine the differences in organizational strategy and structural dimensions with respect to size, ownership etc. The findings of the study suggest that structural dimensions and relationships between strategy and structure do not vary in different cultural contexts, however, conclusive statement can be made only with a cross cultural study. The authors opine that trend can be the same in different cultural contexts but the extent of implementation may vary depending on cultural values of a nation.

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