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Contents

Article

Engaging Contract Labour: The prerequisites and the pitfalls 2

Notifications & Circulars 6

Ratio Decidendi 7

July
2015



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Engaging Contract Labour: The prerequisites and the pitfalls

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Introduction

Companies engage contract labour to keep the head count low and for the scalability and flexibility it provides in management of workforce. Though employment of contract labour in India has attracted debates, it has become a significant and growing form of employment, engaged in different occupations including skilled, semi skilled and unskilled jobs across sectors. While engaging contract labours, companies need to exercise caution and need to understand the laws that govern their relationship with the contract labours. In this article we would discuss the fundamentals of engaging contract labour and the pitfalls that can be avoided to have a congenial environment in the company.

Contract Labour: Definition & engagement

“Contract labour” can be distinguished from “direct labour” in terms of employment relationship with the principal establishment and the method of wage payment. A workman is deemed to be a contract labour when he/she is hired in connection with the work or “contract for service” of an establishment by or through a contractor. They are indirect employees; persons who are hired, supervised and remunerated by a contractor who, in turn is compensated by the establishment. In either form, contract labour is neither borne on pay roll or muster roll or wages paid directly to the labour. (*Report of the National Commission on Labour, 1969*)

The Contract Labour (Regulation & Abolition) Act, 1970 (Act) permits companies and establishments in the manufacturing and services sectors to engage contract labour through contractors. Such an engagement can be only for work that do not form part of the core operations, which is guided by the memorandum of association of the company. Prior to the enactment of the Act, in the case of *Standard Vacuum Refinery Company v. Their Workmen (1960)*, the Supreme Court of India had observed that contract labour should not be employed where: (i) The work is perennial and must go on from day to day; (ii) The work is incidental to and necessary for the work of the factory; (iii) The work is sufficient to employ considerable number of whole time workmen; and (iv) The work is being done in most concerns through regular workmen.

The Act allows the government to prohibit employers from employing contract labour in its core process after examining whether (i) the work performed by contract labour is permanent in nature; (ii) the process or operation is incidental or necessary for the employer; (iii) such process or work is ordinarily performed by regular employees of other similar employers; and (iv) sufficient number of whole-time employees can be deployed to perform the work. Therefore, contract labours are generally engaged for support services like housekeeping, gardening, security, catering, maintenance, transport, etc.

Salient Features of the Act

Intent & coverage: The Act provides for regulation of the employment of contract labour and its abolition under certain circumstances. It covers every establishment in which 20 or more workmen are employed on any day of the preceding 12 months as contract labour and every contractor who employs or who employed on any day of the preceding 12 months, 20 or more contract employee. It does not apply to establishments where the work is of intermittent and casual nature unless work performed is more than 120 days and 60 days in a year respectively. (Section 1)

Advisory Boards: The Act provides for setting up of Central and State Advisory Contract Labour Boards by the central and state governments to advise the respective governments on matters arising out of the administration of the Act. (Section 3 & 4)

Registration & licenses: The establishments covered under the Act are required to be registered as principal employers with the appropriate authorities. Every contractor is required to obtain a licence and not to undertake or execute any work through contract labour, except under and in accordance with the licence issued in that behalf by the licensing officer. The licence granted is subject to conditions relating to hours of work, fixation of wages and other essential amenities in respect of contract as prescribed in the rules. (Section 7 & 12)

Facilities to contract labours: The Act has laid down certain amenities to be provided by the contractor to the contract

labour for establishment of canteens and rest rooms, arrangements for sufficient supply of wholesome drinking water, latrines and urinals, washing facilities and first aid facilities have been made obligatory. In case of failure on the part of the contractor to provide these facilities, the principal employer is liable to provide the same. (Section 16, 17, 18, 19 and 20)

Payment of wages: The contractor is required to pay wages and a duty is cast on him to ensure disbursement of wages in the presence of the authorised representative of the principal employer. In case of failure on the part of the contractor to pay wages either in part or in full, the principal employer is liable to pay the same. The contract labour that performs same or similar kind of work as regular workmen will be entitled to the same wages and service conditions as regular workmen as per the Rules. (Section 21)

Offences: For contravention of the provisions of the Act or any rules made there under, the punishment is imprisonment for a maximum term up to 3 months and a fine up to a maximum of Rs. 1000. In case of a company, the company as well as every person in-charge of and responsible to the company for the conduct of its business at the time of the commission of the offence shall be deemed guilty. (Section 23, 24 & 25)

Registers & displays: Principal employer and contractor have the responsibility to maintain registers and records of contract labours, work performed by them, wages,

and other particulars as specified in the Rules. Notices are also to be exhibited within the premises regarding hours of work, nature of duty and other information as prescribed under the Rules. (Section 29)

Abolition of contract labour: After consultation with the Central Board or State Board, government can prohibit, by notification in the official gazette, employment of contract labour in any establishment in any process, operation or other work. The guidelines for deciding upon the abolition of contract labour in any process, operation or other work in any establishment are – (i) Conditions of work and benefits provided to the contract labour; (ii) Whether the work is of a perennial nature; (iii) Whether the work is incidental or necessary for the work of an establishment; (iv) Whether the work is sufficient to employ a considerable number of whole-time workmen; (v) Whether the work is being done ordinarily through regular workman in that establishment or a similar establishment.

Compliances under the Act

The Act requires both the principal employer and the contractor to implement their respective statutory obligations. In a factory, the owner or occupier or manager is considered a principal employer; but in an establishment or a company, the person who is in control and supervision of establishment or company will be the principal employer. Principal employer is the one who employs contract labour through a contractor. Contractor undertakes to perform a job for the principal employer through contract labour other than mere supply of

goods or articles of manufacture or supplies contract labour for any work of the principal employer & includes a sub-contractor.

The Act mandates that the principal employer should be registered and the contractor have a valid license prior to engaging contract labours. In *Workmen of Best & Crompton Industries Ltd. v. Best & Crompton Industries Ltd.*, the Madras High Court has held that the principal employer must engage contract labour through a contractor who has a valid license, because an invalid license of a contractor would imply direct employment of contract labour by the principal employer. Further, such a license of the contractor is job specific, non-transferable for any other job and indicative of the maximum number of contract labours to be engaged.

The Act puts onus on the contractor for providing all statutory benefits to contract labour with the rider that in case the contractor fails to do so, the obligation would fall on the principal employer. This position was clarified by the Supreme Court in *People's Union for Democratic Rights v. Union of India*, wherein it was held that if the contractor fails to fulfil its duties under the Act then the principal employer shall be under an obligation to provide all amenities and benefits prescribed under the law to contract labour deployed at its establishment. Therefore, it becomes necessary for the principal employer to witness disbursement of wages to the contract labour by the contractor, collect all the necessary documents that establishes that the statutory benefits are being made available to the

contract labours by the contractor. Though registers like muster roll, wage register, etc., are largely to be maintained by the contractor, principal employer is also required to keep copies of such records and also additionally display the details regarding the nature of duties of work, work hours, etc.

Precautions while engaging contract labour

Prior to engaging a contractor labour, it is crucial for the principal employer to register it with the authorities. Secondly, it should verify the licenses of the contractors. Thereafter, the principal employers must execute contract with the contractors with the terms of engagement. No contract labour should be made to work on the core areas of the company. The contractor should not be an employee of the principal employer. Principal employer should not exercise direct control (*including matters of payments, discipline and removal/termination*) and supervision (*principal employer has a right to assess the abilities and skills of the workers employed by the contractor to ensure the quality of service provided under the contract, without actually managing or directing such contract labour*) over the contract labours and that should be done by the contractors.

In *Haldia Refinery Canteen Employees Union & Others v. Indian Oil Corporation Limited*, the Supreme Court laid down certain guidelines for engaging contract labour: (i) Principal employer must not interfere with the contractor for engaging contract labour and contractor must have free hand; (ii) Wages should be disbursed by the contractor,

principal employer must only witness; (iii) Contractor is liable to pay all statutory benefits such as provident fund contributions, leave salary, medical benefits, and observe statutory working hours for its employees and maintain records thereof; (iv) Contractor is responsible for proper maintenance of registers, records and accounts for compliance with statutory provisions/obligations; (v) Principal employer should avoid managing the contract labour; (vi) Contractor is liable to defend/indemnify the principal employer from any liability or penalty which may be imposed by authorities for any violation by the contractor of such laws, regulations and also against all claims, suits or proceedings.

Conclusion

Essentially, the principal employer needs to be diligent and exercise precautions while engaging contract labours. In case the compliances specifically in relation to the mandatorily benefits payments are not done by the contractors, the onus of making payments falls on principal employer. Contract labours are engaged to make the processes simpler with the intention to manage the workforce in an easier way. However, lack of due diligence can land companies into troubles. Though engaging contract labours should always be done by way of executing a contract with the contractor, exercising due diligence would be of great significance as contractual safeguards may not offer sufficient protection to principal employers.

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Notifications & Circulars

Dishonor of cheques – Jurisdiction for filing of cases clarified: The President of India has promulgated the Negotiable Instruments (Amendment) Ordinance, 2015 (No. 6 of 2015), dated 15th June, 2015. The Ordinance provides for filing of cases only by a Court within whose local jurisdiction the bank branch of the payee, where the payee delivers the cheque for payment is situated. Further, where a complaint has been filed against the drawer of a cheque in the court having jurisdiction under the new scheme of jurisdiction, all subsequent complaints arising out of Section 138 against the same drawer shall be filed before the same court, irrespective of whether, those cheques were presented for payment within the territorial jurisdiction of that court.

It may be noted that the issue regarding territorial jurisdiction in cases of dishonour of cheques under Section 138 of the Negotiable Instruments Act, 1881 has been a contested one though the Supreme Court in its decision of *Dashrath Rupsingh Rathod v. State of Maharashtra* (AIR 2014 SC 3519) did try to clarify the same. Presently, the Bill relating to the amendment had been passed by the Lok Sabha but is pending in the Rajya Sabha.

Companies law - Circulation and filing of financial statement, clarified: Ministry of Corporate Affairs has clarified that a company holding a general meeting after giving a shorter notice (less than 21 days) as provided under Section 101 of the Companies Act, 2013 can also circulate financial statements (to be

laid/considered in the same general meeting) at such shorter notice. General Circular No. 11/2015, dated 21-7-2015 issued in this regard also clarifies that in case of a foreign subsidiary, which is not required to get its accounts audited as per legal requirements prevalent in the country of its incorporation, and which does not get such accounts audited, the holding/parent Indian may place/file such unaudited accounts to comply with requirements of Section 136(1) and 137(1) as applicable.

FEMA Regulation relating to issue of security amended: The Reserve Bank of India has issued Notification No. FEMA 344/2015-RB to amend Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000. The new amendments insert two new definitions of ‘employee stock option’ and ‘sweat equity shares’ and replace the existing regulation relating to issue of shares under employee stock option scheme to person resident outside India. Under the amendment, an Indian Company may issue employee stock option or sweat equity shares to its employees/directors or employees/directors of its holding company or joint venture or wholly owned overseas subsidiary/subsidiaries who are resident outside India under certain conditions. RBI may require (but not compulsorily as earlier) a report as it deems necessary.

Food Safety and Standards – Draft regulations proposed: Food Safety and Standards Authority of India has proposed

certain draft regulations in Food Safety and Standards (Contaminants, Toxins and Residues) Regulations, 2011, Food Safety and Standards (Food Product standards and Food Additives) Regulations, 2011, and Food Safety and Standards (Packaging and labeling) Regulations, 2011. While in respect of contaminants toxins and residues, draft regulations seek to insert certain articles of food and the specified limits of metal contaminants in the food (calculated in parts per million by weight), in case of Food Product standards and Food Additives, there is a proposal to substitute current regulation relating to salted fish/dried salted fish and stipulate new requirements. Further, in packaging and labeling regulations, labeling requirements of edible vegetable oils/edible vegetable fat in pre-packaged foods is sought to be substituted.

Aviation - External Commercial Borrowing terms to continue: Reserve Bank of India has by A.P. (DIR Series) Circular No.109 informed Authorized Dealer Category-I Banks that ECB which can be raised by airline companies for working capital as a permissible end-use, under the approval route, subject to the conditions stipulated in earlier A.P. (DIR Series) Circular No. 113 dated April 24, 2012, shall continue till 31st of March, 2016.

Aviation - Applicability of CAR relating to training schools/establishments extended: The Directorate General of Civil Aviation has by Public Notice dated 1-7-2015 extended the Civil Aviation Requirement relating to Training Schools and Establishments (Section 2 Series E Part VIII), up to 31-7-2018. The batch inducted in July 2015 will be the last batch under the current requirements.

Ratio Decidendi

Companies Law - Consideration for a valid arrangement scheme: The petitioner companies sought sanction from the Bombay High Court for a composite scheme of arrangement and amalgamation, which involved a demerger in the first part and an amalgamation in the second. The concerned Regional Director of the Ministry of Corporate Affairs opposed the scheme, contending that while it was not opposed to public interest, it was not compliant with Section 394(1) of the Companies Act, 1956 (which was applicable in this case) due to the fact that the consideration provided to the shareholders of the transferor company in the demerger part

of the scheme was not from the end of the transferee company on whom the demerged undertaking would vest (on a going concern basis), but was from the end of the parent of the transferee company, which the residual part of the transferor company would merge with in the second part of the composite scheme. The High Court however observed that clauses (i) to (vi) in Section 394(1) were merely enabling provisions and not compulsory in any sense. The court concluded that there was no compulsory requirement that the consideration be provided in the form of the transferee's companies shares specifically, or any shares at all, for that matter. [*In Re: Thomas*

Cook Insurance Services (India) Limited, Company Scheme Petition No. 99 of 2015 & No. 100 of 2015, decided on 2-7-2015, Bombay High Court]

Arbitration - Ouster of the Civil Court's jurisdiction: The Karnataka High Court has upheld the Order passed by the lower court, holding that an application for a temporary injunction under arbitration law (made under Section 9 of the Arbitration & Conciliation Act, 1996 read with Order XXXIX, Rules 1 & 2 of the Civil Procedure Code, 1908) cannot be maintained before a Civil Court when the matter falls within Section 241 of the Companies Act, 2013, notwithstanding a consensual arbitration clause in the agreement between the parties. Section 241 of the Companies Act, 2013 provides for a recourse before the National Company Law Tribunal/Appellate National Company Law Tribunal (formed under Section 408/410 respectively) for prevention of oppression and mismanagement, while Section 430 of the Act provides that no Civil Court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which these tribunals are empowered to determine under the Act. This scheme of the Act led the Karnataka High Court to its conclusion that the Civil Court's jurisdiction is ousted in such cases. [*Wilfred D' Souza & Ors. v. Lotus Shopping Centres Pvt. Ltd.*, M.F.A. No. 2573 of 2015, decided on 18-6-2015, Karnataka High Court]

Competition law – Factors for dominance: The Competition Commission of India (CCI) has set aside the application of

the informant alleging contravention of the provisions of Section 4 of the Competition Act, by an airline in India. The informant here was of the view that the airline, being dominant in the market, has devised a standard form of terms and conditions for the public and any person desirous of travelling by it is required to accept those conditions in totality, irrespective of how onerous and one-sided the terms and conditions may be. The Commission however found no *prima facie* case of contravention of the provisions of Section 4. It was held that there was absence of dominance of the airline in the market of air transport services for passengers in India.

For determination of dominance or the absence of it, the Commission first noted that the airline in question was a leading player in terms of domestic passengers availing the airline services. However, it took into consideration other aspects as well, and compared value of total assets of the competing companies also. The airline was found to be not dominant by the Commission as it observed that size of the asset value of the airline in question was lesser than that of other airlines. It was noted that presence of other players in a significant way in the relevant market indicates that the consumers had option to avail service from other players, and they could easily compare fare, timing and availability of seats across various airline companies, incurring negligible cost. [*Udit Gupta v. Interglobe Aviation Limited - Case No. 28 of 2015, decided on 25-6-2015]*

SEBI has jurisdiction in respect of GDRs

Supreme Court of India has upheld the jurisdiction of SEBI to exercise its powers under the provisions of the Securities and Exchange Board of India Act, 1992 and SCR Act, 1956 read along with the Regulations, to proceed against the Lead Manager for the so called fraudulent transaction in respect of issuance of Global Depository Receipts (GDRs). The court in this regard rejected the contention that as from cradle to grave GDRs are dealt with outside the country in the global market, SEBI lacks jurisdiction in proceeding against the managers. Noting that existence of GDRs is always dependent upon the extent of underlying ordinary shares lying with the domestic custodian bank, the court also observed that GDRs would fall within the definition of 'securities' as defined under Section 2(h) of the SCR Act. It was held that even if GDR as such is not specifically referred to under the definition of 'securities' under said provision, by virtue of sub-clause (iii) of the said section, any rights or interests in securities would also fall within the definition of securities.

Further, observing that power invested with SEBI for passing such orders, restraining person from accessing the securities market and prohibiting any person associated with securities market to buy, sell or deal in securities, can even be exercised against "any person", the court stated that the Board is fully empowered to pass appropriate orders to protect the interest of investors in securities and

securities market. The court in this regard also took note of the nature of allegations and was of the view that SEBI has got every jurisdiction to proceed against the Lead Manager as well as the issuing company. It was also held that there is no statutory prohibition either under FEMA or the RBI Act preventing SEBI from taking action in exercise of its powers under Section 11, 11B and 12A of the SEBI Act, 1992, and that specific provisions of SEBI Act, 1992 provided for necessary powers with the SEBI casting a duty on it to protect the interests of the Indian investors. [*Securities and Exchange Board of India v. Pan Asia Advisors Ltd.* - Civil Appeal No.10560 of 2013, decided on 6-7-2015, Supreme Court]

Negotiable Instruments Act - Liability of a company and persons in charge of and responsible to the company:

The Supreme Court of India has ruled that under Section 138 of the Negotiable Instruments Act, 1881, it is the drawer of the cheque alone that attracts liability. It was held that therefore if the cheque is drawn by a director of the company in his individual capacity and not on behalf of the company or in his capacity as the director, the company and its other directors/persons in charge of and responsible to it for its business cannot be punished. The court in this regard observed that even if the cheque is drawn in order to pay the company's dues or discharge the company's liability, the company and such other persons cannot be made liable if the individual draws it with his personal account maintained by his banker. The Apex court hence rejected that the accused party's contention that he must

be acquitted since the company and its other directors were not made a party to the complaint. Impugned orders passed by the High Court and the Metropolitan Magistrate who had accepted

this contention were both set aside. [*Mainuddin Abdul Sattar Shaikh v. Vijay D. Salvi*, Criminal Appeal No. 1472 of 2009, decided on 6-7-2015, Supreme Court of India]

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