FRUSTRATING OR PERHAPS SUPPORTIVE OF ECONOMIC ACTIVITY? A LAW AND ECONOMICS TAKE ON LABOUR LAW IN INDIA

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I. INTRODUCTION

Of course, there is much that is written and discussed about Indian labour laws and in most of the mainstream writing there is a sense that these laws frustrate economic activity on many accounts. It is said there are too many laws making compliance difficult for the businessman, the restrictions that they impose lead to inefficiencies and that the law must change substantially (at least as they are in their present form) –the recent move to collapse labour laws into codes is conceivably the culmination of this chain of thinking. While there may or may not be sufficient virtue to the idea that to study labour law is to gauge how it impedes economic activity, this direction of study is perhaps not entirely in the spirit of the analysis favoured by the *law and economics* understanding of approaching the problem. Though there are varieties of law and economics approaches – my broad understanding goes back to the cradle of the discipline emphasising the key insight featured by Coase that law effects efficiency when transaction costs are present.[1] My intent here is to highlight a set of transaction costs – the ones that are characteristically emphasised by the *incomplete contracts* literature. Such transaction costs are endemically present in the labour market and I therefore argue that our attention needs to shift by analysing law in this light. Thus, rather than obsessively viewing law as an impediment, we need to appreciate the point that the many labour laws are perhaps present to correct some market failure i.e. counter the presence of transaction costs. If indeed this is accepted we might see (at least a sub set) of labour laws are supportive of efficient productive activity rather than being efficiency thwarting. This has many implications for

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[1] R. H. Coase, *The Problem of Social Cost, 3* JOURNAL OF LAW AND ECONOMICS, 1-44 (1960).

the ongoing labour reform which should be taken into cognisance above all else to genuinely encourage productive relations.

To make this point I begin by discussing the many thresholds specified by Indian labour law in terms of coverage -size of the unit, definition of workers etc., and the fact that much of labour reform is directed at constricting this coverage. The analytical basis of this seems to lie in the belief that labour markets are competitive and I briefly go over the literature which has furthered this view in the Indian context. If we correct this analytic and pay attention to how the contours of the firm have come to be defined within the incomplete contract framework, then it is also evident that this frame allows us to approach law and the labour market with greater insight than is the case otherwise. Thus, over the next two sections I briefly go over the central arguments associated with incomplete contract theory and how it is of relevance to understanding the labour market. In the final part of the essay I attempt to use the insights gathered to briefly remark on the law pertaining to contract labour and apprentices in India. This is followed by a concluding comment.

II. THE MANY THRESHOLDS OF INDIAN LABOUR LAW

India has a plethora of labour laws and one of the key characteristics of these laws is that they are oriented to covering specific categories of establishments and workers, producing a minutia of thresholds. For instance, safety and health requirements for workers become mandatory only if the *Factories Act 1948* is applicable to the unit- thus the factory unit needs to be using power and employing 10 or more workers, and if not using power, employing 20 or more workers on any day of the preceding 12 months for the requirements of the Act to be bestowed on workers. Similarly, the labour laws covering social security such as The *Employees' Provident Fund and Miscellaneous Provisions Act 1952* comes into force only if the unit is employing more than twenty workers. The size of the establishment is also a criterion for the prevalence of standard terms of employment and the requirement that due procedure be followed when disciplinary action is initiated against workers -these issues become legally binding only in establishments that employ fifty or more workers and thus come under the cover of *the Industrial Employment (Standing Orders) Act, 1946*.

More notoriously under the *Industrial Disputes Act 1947* only establishments employing more than hundred workers (recently in some states this threshold has changed) need to get permission from the government before lay-offs, retrenchment or closure is allowed to be put into effect. It is the case that not only must the establishment in which the worker is working be covered by the appropriate law but the worker herself must belong to a category that has access to the law – typically for a worker to have the legal standing to raise an industrial dispute she must be a 'workman' as defined by Section 2(s) of the Industrial Disputes Act[2].

Over time of course there have been many changes to the law, largely by initiating changes in thresholds and the coverage of laws. Since labour lies in the concurrent list of the Indian Constitution, it is the case that many of the states periodically amend labour legislations. A recent spate of amendments by states has re-specified some of the thresholds as gestures of reform. For example, the state of Rajasthan changed the coverage of three prominent labour legislations:

i. The *Contract Labour (Regulation and Abolition) Act, 1970* which was applicable to establishments employing 20 or more workers, has now been made applicable to establishments employing 50 or more workers;
ii. The Factories Act 1948, which as we have noted above was legislated to cover establishments employing 10 or more workers (using power) and 20 or more workers (not using power), has now been amended to cover only establishments employing 20 or more workers (using power) and 40 or more (not using power);
iii. Chapter V B of the *Industrial Disputes Act 1947*, which required establishments employing more than 100 workers to seek permission from the government before they initiated lay-offs, retrenchments or closure, has been amended so that now only establishments employing 300 or more workers are required to seek permission. Similar *threshold* - oriented changes have been made in the states of Madhya Pradesh and of Gujarat as well. It is also the case that the shrinking coverage of labour laws is not confined to legislative changes but

[2] See JAIVIR SINGH, LABOUR, EMPLOYMENT AND ECONOMIC GROWTH IN INDIA (Cambridge University Press Delhi 2015).

also extends to the gradual changes initiated by the higher judiciary of the country as they refine the point as to which category of workers will be covered by the law.

The Supreme Court of India has played an important role in this matter – when called upon to define the rights of contract labour (labour that is hired through a labour contractor and referred as agency workers to in other parts of the world)in the case of *Steel Authority of India*[3], a Constitution Bench of the Indian Supreme Court ruled that there was no obligation on the employer to employ the contract labour that had been abolished by the government (a move that would be initiated because contract workers were doing the jobs meant for regular labour invoking the *Contract Labour (Regulation and Abolition) Act*).Further, as per this judgment the question as to whether contract labour is doing the work of regular worker is an independent issue, which the Bench said needs to be litigated as an industrial dispute separately. A subsequent case[4] said that the test to discern whether the contract labour agreement is "sham, nominal and is a mere camouflage", requires one to see who pays the salary -if the contract is for the supply of labour then the worker will work under the 'directions, supervision and control of the principal employer" but since the salary is paid by the contractor the "ultimate supervision and control lies with a contractor". The originality of the judgment is to label the contractor's control as *primary* and the principal employer's control as *secondary*. This test is undoubtedly calculated to make it tougher for workers hired as contract labour to establish an employment relationship with the principal employer. These judgments and others of their kind[5] have engendered a very large shift in the proportion of the workers employed as contract workers – in fact according to data obtained from the Annual Survey of Industry by 2015 thirty five percent of the labour force employed in the formal manufacturing sector consists of contract labour.[6]

III. LABOUR LAW AND THE EFFICIENCY-EQUITY TRADE-OFF

[3] Steel Authority of India v. National Union Water Front Workers, AIR 2001 SC 3527.
[4] International Airport Authority of India v. International Air Cargo Workers Union, (2009) 13 SCC 374.
[5] Secretary, State of Karnataka and Ors vs. Umadevi and Ors, AIR 2006 SC 1806, (2006) 4 SCC 1.
[6] For a discussion on the connections between the Supreme Court judgments and the growth of contract labour see DEB KUSUM DAS ET. AL, EMPLOYMENT POLICY IN EMERGING ECONOMIES: THE INDIAN CASE 42-63(Routledge: London 2018).

It is of course not the intent here to list the many intricacies of Indian labour law in detail but the point is that the labour law reform is centred around a discourse that apart from encouraging self-certification in lieu of having a regime of factory inspectors[7], seeks to constrict the number of workers and establishments that are covered by labour laws. A good deal of this orientation follows from the premise that Indian labour laws lower the demand for labour as well asthe perception that it is very cumbersome for a firm to meet the requirements imposed by various labour laws. This kind of thinking which lies at the core of the policy rhetoric, is quite firmly sourced in the academic work on the Indian labour market. The standard literature on the formal sector labour market in India has focused on the obstinate paradox that typifies the Indian economy – viz., that in spite of a comparatively high rate of growth of output, the expansion in employment is quite small. The overarching practice has been to suggest that this is due to the contraction in the demand for labour produced by restrictive labour laws. Starting with the earliest exposition on the matter which showed that the (in) famous Chapter VB of the Industrial Disputes Act dampens the demand for labour[8], successive work has continued to target the Act as the source of critical rigidity in the law. A recurrently cited paper by Besley and Burgess relates pro-labour/pro employer legislative changes made by Indian states to the Industrial Disputes Act to both levels of output and employment, concluding that pro-labour states perform poorly on both counts[9]. These results have been criticized in the grounds that the methodology is flawed but this point has been largely ignored[10]. In fact, subsequent work has continued to use the same

[7] In 2014 the Government of India launched a slew of reforms designed to reduce lengthy inspection and compliance procedures. Prominent among these moves is the *Shram Suvidha Portal* which, allows employers to submit a self-certified single compliance report for 16 Central labour laws. This reform is expected to simplify business operations by putting the onus of compliance on enterprises through self-certification.

[8] P.R. Fallon & R.E.B. Lucas, *Job Security Regulation and Dynamic Demand for Industrial Labor in India and Zimbabwe,* 40 (2) JOURNAL OF DEVELOPMENT ECONOMICS, 241- 275 (1993).

[9] T. Besleyand R. Burgess, *Can Regulation Hinder Economic Performance? Evidence from India*, 119 QUARTERLY JOURNAL OF ECONOMICS, 91-134 (2004).

[10] Aditya Bhattacharjea, *Labour market regulation and industrial performance in India: A critical review of the empirical evidence,* 49 (2) INDIAN JOURNAL OF LABOUR ECONOMICS, 211-232 (2006).
Aditya Bhattacharjea"*The Effects of Employment Protection Legislation on Indian Manufacturing,* 44 (22) ECONOMIC AND POLITICAL WEEKLY, 55-62 (2009).

measure[11], while others have expanded it to incorporate changes in other labour laws as well – all these studies underline the assessment that that the more pro-labour states have worse labour and output outcomes[12].

The idea behind these studies is that labour laws inhibit employers from hiring workers because employers have to carry 'stocks' of labour in the face of product market downturns, leading employers to constrain hiring and possibly also to increase capital – labour ratios. The efficiency cost is further compounded because the restriction on the ability of firms to make adjustments in response to exogenous changes harms all workers (as a group) since long run demand for labour diminishes. This kind of thinking is firmly based on the premise that the labour market is typically competitive, where wages reflect the capacities of workers and if the market is allowed to function without impediments it would result in the efficient allocation of resources, including labour. Admittedly these outcomes may be inequitable and in the absence of perfect insurance markets for labour impose the costs of unforeseen shocks on workers. The many laws and institutions pertaining to minimum wages, unions, termination compensation, unemployment insurance, centralized bargaining to name a few, come to be typically viewed as devices that compensate for these risks and inequities. If one works with the conviction that the labour market is competitive then such labour laws cannot but be a source of inefficiency, implying that we have to eternally confront an inescapable equity (fairness) - efficiency trade off that will always accompany legal intervention in the labour market. It is thus no surprise that reform of labour law has come to be associated with restricting coverage to a sequentially smaller fraction of the labour force – after all it follows that if the coverage and content of labour law were expanded, it is but pernicious - while it may increase the welfare of some workers, it would lead to an enormous efficiency loss.

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[11] P. Aghion, R. Burgess, S. J. Redding and F. Zilibotti, "*The Unequal effects of Liberalization: Evidence from dismantling the License Raj in India*, 98 (4) AMERICAN ECONOMIC REVIEW, 1397-1412 (2008).
Ahmad Ahsan and Carmen Pagés, *Are All Labor Regulations Equal? Evidence from Indian Manufacturing,* 3394 INSTITUE FOR THE STUDY OF LABOR (2008).

[12] Sean M. Dougherty *Labour regulation and employment dynamics at the state level in India*, 1 (4) REVIEW OF MARKET INTEGRATION (2009).
Sean M. Dougherty, V.C.F. Robles and Kala Krishna, *Employment Protection Legislation and Plant-Level Productivity in India*, 17693 NATIONAL BUREAU OF ECONOMIC RESEARCH (2011).

However, the discussion changes somewhat if we disabuse ourselves of the competitive market fetish and follow MacLeod's lead to take cognisance of the fact that some form of *labour law* has been in place since antiquity and this probably indicates the point that labour market institutions are a response to some market failure - the institution in question (labour law inclusive) may actually be solving a resource allocation problem rather than creating a problem.[13] This is of course precisely the point of *law and economics* analysis underscored in its genesis by Coase – law has consequences for efficiency in a world where transaction costs are important.[14] How precisely the law matters of course varies across different contexts and in the labour market there are a variety of circumstances but I would like to pursue a chain of thinking that has originated from the work pioneered by Coase on the boundaries of the firm[15].

IV. INCOMPLETE CONTRACTS

Coase in his classic 1937 paper, sought to provide an explanation for the existence of the firm – he suggested that the hierarchical commands replace the market in certain instances when the 'costs of the price mechanism' make the organization of economic activity in the market costly and this makes for the firm. The limits of such firms are reached when the marginal benefit of working inside the firm equals the marginal cost of administrative errors. Although Coase explained the 'costs of the price mechanism' (the term that metamorphosed into transaction costs) as negotiation costs, later work by Williamson[16] and Klein *et al*[17] went on to link transaction costs with opportunism associated with relationship-specific investment that leads to hold up problems. This work established that vertical integration can prevent such opportunism, but, because it stresses only the benefits of integration, the limits to the firm remain undefined. The limits of the firm

[13] O. ASHENFELTER & D. CARD, 4B HANDBOOK OF LABOR ECONOMICS 1591-1696 (North Holland 2011).
[14] R. H. Coase, *The Problem of Social Cost, 3* JOURNAL OF LAW AND ECONOMICS, 1-44 (1960).
[15] R. H. Coase, *The Nature of the Firm,* 4 (16) ECONOMICA, NEW SERIES, 386-405 (1937).
[16] OLIVER WILLIAMSON, MARKETS AND HIERARCHIES: ANALYIS AND ANTITRUST IMPLICATIONS (New York: Free Press 1975).
OLIVER WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM (New York: Free Press 1985).

[17] Benjamin Klien, R. Crawford and A. Alchian, *Vertical Integration, Appropriable Rents and the Competitive Contracting process* 21 JOURNAL OF LAW AND ECONOMICS, 297-326 (1978).

came to be more fully specified in the classic paper by Grossman and Hart[18]. In this work they suggest a model of two stage economic activity – an ex-ante stage where agents make relationship specific investments and an ex post stage when production decisions are taken. Though ex-post contracts are presumed to be efficient, ex-ante contracts are characterised as being typically incomplete because of the presence of transactions costs associated with hold ups. In this scenario, ownership defined as residual rights (property rights that remain with a party in relation to non-human assets after contractual activity is over)becomes an important determinant of the ex-post surplus, which in turn affects incentives to make ex-ante investments. Accordingly, a merger does not generate unequivocal benefits since the owner-manager (who is taken over) loses incentives to invest in the ex-ante relationship specific investment. Hence if the criterion for the efficient size of the firm is the most favourable level of ex-ante investment, then highly complementary assets should be owned in common but as the firm grows and the relation of one asset to the other diminishes then separation is better.

To phrase the point differently though integration checks hold ups, such gains do not always adequately compensate incentive losses. The Grossman- Hart model looked at costs and benefits of integration from the perspective of incentives for top management but later work by Hart and Moore extends the model to look at the impact of changes in ownership on incentives of not only owner managers but also non-owners of assets (employees)[19].The representative situation examined in this work involves an asset when employers have ownership rights but workers do not and involves analysing how the incentives of employees change as integration occurs or, to phrase it differently, when asset ownership becomes more or less concentrated. In this model agents take action at time period 0– say make an asset specific investment in developing a skill, which will pay off at time period 1 as the fruits of increased productivity. However, such a pay-off will ensue to the agent only if she has access to the specific asset in question. Since writing complete contracts at

[18] S. Grossmanand O. Hart, *The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration,* 94 JOURNAL OF POLITICAL ECONOMY, 691 (1986).

[19] Oliver Hart and John Moore, *Property Rights and the Nature of the Firm,* 98 (6) THE JOURNAL OF POLITICAL ECONOMY, 1119-1158 (1990). A more general non-specialist account can be found in Oliver Hart, *An Economist's Perspective on the Theory of the Firm*: *Contractual Freedom in Corporate Law,* 89 (7) COLUMBIA LAW REVIEW, 1757-1774 (1989).

time period 0 to cover such situations is not possible (returns at time period 1 being un-contractible at time period 0) the agent's marketability/bargaining position at time period 1 will depend on her access to assets and is hence sensitive to allocation of asset ownership. Consequently, the act of investment by an agent at time period 1 is connected to whether he owns the asset and if he does not own it, then who owns it. The broad propositions to emerge from the model are that:

i. for efficient investment, ownership of assets should lie with agents who are indispensable to the economic activity in question even though they do not necessarily make the ex-ante investment decisions and;
ii. for efficient investment assets that are complementary should be owned together.

V. INCOMPLETE CONTRACTS AND THE LABOUR MARKET

By now the insights of the incomplete contracts model have been extended to many branches of economics (the Nobel prize for economics was handed out to Oliver Hart in 2016) and the incomplete contract model has much to offer to help us think of the labour market as well. There is of course a very large literature[20]on incomplete contracts and labour markets but for my current expositional purposes, it is perhaps best to turn back to the early work to appreciate the role of the incomplete contract paradigm in labour markets. To quickly recapitulate, the seminal paper by Klein *et al*[21] is concerned with hold up problems. They tell us that *ex- ante* contracts involving relationship specific investment cannot cover risks that show up *ex-post*, on account of the physical unfeasibility of writing up such complex contracts. They point out that the more specific an investment is to a relationship, greater is the possibility of at least one of the parties usurping

[20] For example see James M. Malcomson, *Contracts, Hold-Up, and Labor Markets, 35 (4) JOURNAL OF ECONOMIC LITERATURE*, 1916-1957 (1997). Also among many other works see W. B MacLeod and V. Nakavanchara, *Can Wrongful Discharge Law Enhance Employment?* 117 ECONOMIC JOURNAL, F218–F278 (2007).

[21] Benjamin Klien, R. Crawford and A. Alchian, *Vertical Integration, Appropriable Rents and the Competitive Contracting process* 21 JOURNAL OF LAW AND ECONOMICS, 297- 326, (1978).

'quasi-rent' from the gains of the relationship ex-post. The anticipation of this can prevent value generating ex-ante decisions to invest. They suggest that vertical integration can somewhat assuage this problem, leading to more efficient levels of investment.

In the labour market context Kline *et al* call attention to the point that vertical integration ends up being approximated by long-term contracts or even by extra-legal implicit contracts. The import of such institutions is apparent when we reflect on an example-let us take the notional case of a worker hired to maintain an asset and if he does not do a good job, he can be fired but were it the case that he is the only person who has learned the skill of maintaining the asset and has the special ability to do so, he can then hold up the owner of the asset and earn a quasi-rent. To resolve the difficulty, it is not conceivable to vertically integrate as in other markets – employers cannot 'own' the worker on account of anti-slavery laws. So, some form of vertical integration such as having a long-term relation – a franchise agreement or even an agency agreement perhaps, which is more vertically integrated with an employer than the case of a worker who can be fired at will,is better at preventing a large hold-up.

The Klein *et al* paper also talks of human capital investments undertaken by workers – such investments have elements that are captured very well by the incomplete contracts rubric. The classic work of Becker brought out the distinction between general and specific capital with general capital defined as being useful across employers and specific capital being associated with increasing the productivity of the worker in her current job[22]. While general human capital is another matter, specific human capital involves a series of ex ante investment decisions by both employers and workers, which are subject to an ex-post risk of quasi-rent appropriation. Consider the appropriation of quasi rent by employees when employers invest in specific human capital. In such instances employees can quit after gaining valuable training provided by employers – a reaction by employers can push up wages to retain workers, but that is no guarantee that workers will remain and complex wage schedules are atypical with wages often tending to be rigid. This train of thinking has generated a large literature emphasising the wide variety of institutions that

[22] GARY BECKER, HUMAN CAPITAL (The University of Chicago Press 1964).

govern quantitative adjustments in labour markets.[23] There are concerns of the appropriation of quasi-rent at the other end of the relationship as well – consider the case where workers have invested in specific human capital on the job and before taking the job and employers opportunistically fire workers nearing retirement depriving them from enjoying the returns of investing in the job. While the role of trade unions is conventionally relegated to forming a cartel to engineer wage setting, they are probably particularly important as institutions that play an important role in monitoring and enforcing long term contracts to help preserve returns to employees with investments in specific human capital.

VI. INCOMPLETE CONTRACTS IN THE LABOUR MARKET AND INDIAN LABOUR LAW

Though it will be only a tip of the iceberg, I would like to bring up a couple of contexts within which our general discussion finds some place in specific instances. One of these is in relation to the large-scale deployment of contract labour mentioned earlier, and the other in relation to *The Apprentice Act 1961* and the *Skilling India* Policy of the Indian government.

A) CONTRACT LABOUR

There is an obvious echo of the concerns raised by the incomplete contract framework that is reflected in the contents of a qualitative study on contract labour that I have been involved with[24]. Over this study it was found that contract workers in a number of industries and locations all over India, seldom, if ever, belong to unions and unions are not interested in having contract workers as members. This generally observed pattern can be explained by the law laid down by the Supreme Court in relation to contract labour which was referred to earlier – as was noted after the Steel

[23] For example, see Hashimoto, Masanori, and Ben T. Yu, *Specific capital, employment contracts, and wage rigidity,* 11 (2) THE BELL JOURNAL OF ECONOMICS, 536-549 (1980). and also see Hashimoto, Masanori, *Bonus payments, on-the-job training, and lifetime employment in Japan*, 87 (5) THE JOURNAL OF POLITICAL ECONOMY, 1086-1104 (1979).

[24] PANKAJ KUMAR ET. AL, ISSUES IN LAW AND PUBLIC POLICY ON CONTRACT LABOUR IN INDIA: COMPARATIVE INSIGHTS FROM CHINA (Springer Singapore 2018).

Authority[25] judgement of the Indian Supreme Court Indian employers can hire contract labour through the offices of a contractor and are under no obligation to absorb them into permanent jobs. This effectively means that contract workers do not have many rights that the court will uphold – indeed subsequent to the Steel Authority judgment, it is the case that the rights of all temporary workers were definitively curtailed by the Supreme Court in the Uma Devi case[26].

With no rights for contract workers, it is not surprising that contract workers do not interact with unions and vice versa. For employers while this has meant paying out lower wages and flexibility to fire workers, it has also meant that many of them complain that the workers they hire are not sufficiently skilled and do not stay long enough to be skilled. Perhaps the most interesting part of the qualitative study that illustrates this is from Rudrapur. Rudrapur is a town located in the foothills of the Himalayas near Nainital where a number of industries have set up manufacturing units following fiscal incentives given out by the government, ostensibly to develop the region and provide employment to the people residing in the hinterland of the town. Over the interviews conducted, most of the manufacturing firms in the region expressed precisely this dilemma – while contract workers can be flexibly fired and used as substitutes for regular workers, they do not stick around and generally do not adequately invest in doing the job. In this setting there was an interesting anomaly, which makes a point of import. A heavy transport manufacturer located in the Rudrapur region was able to raise the productivity of workers by signing an agreement with a trade union, which enabled contract workers (this was one of those very rare cases when unions and contract workers interacted with each other) to be treated at par with regular labour. Among other benefits that accrued to contract labour was the fact that they were assured of tenure till the age of 58 years. Presumably this was the source of the phenomena that contract workers actually took care to invest in the job and raise productivity. While the agreement that allowed contract workers to get benefits that were similar to those of regular workers was the joint product of both the management as well as the trade unions playing a crucial role, the agreement was also under strain because the local government machinery considered it illegal. Under the *Contract Labour (Regulation*

[25] Steel Authority of India v. National Union Water Front Workers, AIR 2001 SC 3527.

[26] Secretary, State of Karnataka and Ors vs. Umadevi and Ors AIR, 2006 SC 1806, (2006) 4 SCC1.

and Abolition) Act, 1970 the government labour department needs to initiate moves to abolish contract labour if the job such labour has been hired for is perennial. It is precisely this sort of riddle that labour law reform in India needs to address. By confusing the removal of coverage of various facets of labour law as law reform, the system is encouraging a de facto *employment at will* type regime which may work well if one worker is substituted easily for another – as is the case with unskilled work. However, to the degree that one worker *cannot* be substituted one for another, where investment in the job and in the location where the job has been gained are important and specific human capital as skill is important, it becomes vital for labour law to offer variegated terms to workers – some categories of workers need to be assured of tenure if they are to invest in the job. This is best done by having some basic rights for all labour in place and then proceeding to allow employers to design contracts that suit them best with worker interests being represented by unions. The mere creation of thresholds in statues and judgments invariably leads to perverse effects rather than support for economic activity.

B) THE APPRENTICE ACT 1961 AND THE 'SKILLING INDIA' POLICY

Though the 'flexibility' of the formal labour market has been an omnipresent presence in relation to the discourse around labour law in India – till recently, there has been little talk about connecting labour and labour law with skills. However, a law was put in place about fifty years ago namely the Apprentice Act 1961, which was set up to make it mandatory for certain employers to engage apprentices in designated trades. Broadly speaking, the Act regulates and controls the programme of training of apprentices. Apart from providing the structure of training to apprentices, the law also specifies that a contract of apprenticeship be required to engage a person as an apprentice. Further the obligations of employers are listed, which included provision of training, proper training personnel and the carrying out of obligations under the contract of apprenticeship. The obligations of the apprentice include a conscientious attempt to train oneself, to attend classes regularly and carry out the lawful orders of the employer as well as carry out obligations listed in the contract of apprenticeship. The Act also governs payment of stipend to apprentices at a rate not less than a specified minimum and cannot be paid on a piece rate basis.

There is a restriction on working hours and overtime is discouraged and apprentices are supposed to be able to enjoy the holidays listed in the establishment of apprenticeship. The law does not give the apprentices any rights to a future job and the case law also supports the position that apprentices do not have any rights to a job[27].

There have been minor amendments[28] to the Act over the years but recently a consciousness has emerged that Indian workers are not adequately skilled. Thus, more substantial changes to the Act were initiated in 2014 upon the recommendations of an Inter-Ministerial Group (IMG).[29] The changes were aimed at ostensibly (rhetorically) making apprenticeship more responsive to youth and industry and also aimed at providing greater incentives to employers by making the terms of the enterprise more favourable so that employers are encouraged to train and hire apprentices. The red tape associated with the functioning of the law has been cut down and the new law allows the incorporation of new trades for the purpose of apprenticeship.

The point that needs to be noted over the changes in the law is that apart from some enhancement in the stipend and an 'opportunity to get skilled' the Act does not really provide or rather provide weak returns to workers who may apprentice themselves. Section 22 of the Apprentice Act says "It shall not be obligatory on the part of the employer to offer any employment to any apprentice who has completed the period of his apprenticeship training in his establishment, nor shall it be obligatory on the part of the apprentice to accept an employment under the employer." In this context the Apprentice (Amendment Act) 2014 adds the clause "Every employer shall formulate its own policy for recruiting any apprentice training at his establishment" This is somewhat hopeful from the viewpoint of workers who may be able to invest in the jobs if the employment policy offers some form of tenure. However, it may be noted that one needs a particular kind of

[27] For example see Management of T.I. Diamond Chain Ltd. v. P.O. Labour Court, 2003 I CLR 57 (Mad.H.C.), Petroleum Employees Union v. Indian Oil Corporation Ltd., 2001 I CLR 785 (Bom.-D.B.).
[28] Since its initial legislation, the Apprentice Act has been amended in 1973, 1986, 1997 2007 and most recently in 2014.
[29] The Inter Ministerial Group (IMG) was constituted comprising representatives from Ministry of Railways, Ministry of Micro Small Medium Enterprises, Ministry of Power, Ministry of Defence, Planning Commission, National Skill Development Agency (NSDA), Working Group on The Directorate General of Employment and Training WG (DGE&T) for discussion on the suggestions received from PM's National Council on Skill Development (PMs NCSD), Central Apprenticeship Council (CAC) , National Commission on Labour (NCL), Indian Labour Conference (ILC) and CII.

wider legal regime that would support employer - employee contracts to be signed, particularly a robust union movement. As we noted above neither the statue nor the case law holds up any apprentice rights to a job.

After the passing of this legislation, in 2015 there has been a declaration of a National Policy on Skill Development and Entrepreneurship[30] under which an entire ministry called Ministry for Skill Development and Entrepreneurship has been set up to encourage the skilling of the workforce. While the document emphasizes various programs for increasing skills, there is very little mention on ensuring that workers are able to gain some sure returns to the investment that they would have put in to gain the skills. As long as the workers are not convinced about the ex-post benefits or return to be accrued out of such programme, it is obviously very low likelihood that they would want to invest in skills. Moreover, in a country like India, which is largely characterised by institutional deficits, workers will be less keen to invest in their skills which could affect skill building as a prime objective of these measures.

VII. CONCLUSION

India clearly needs law reform that will enhance ex-ante investment by workers – this is the only way the much-desired skilled work force will come into being. Empirical work has by now made it quite clear that a country's labour market institutions ((read law) affect workers skills and in turn determine the value and profile of the goods exported – in this the frame envisioned by the incomplete contract model is vital to understanding the economic processes.[31] Thus, we need less of reform that is merely 'pro-employer' – To make the case in point, one such 'pro-employer' change to the Factories Act in Rajasthan has the law saying that complaints against the employer upon violation of the Act would not receive cognizance by a court without prior written

[30]NATIONAL POLICY ON SKILL DEVELOPMENT AND ENTREPRENEURSHIP 2015, http://www.skilldevelopment.gov.in/assets/images/Skill%20India/policy%20booklet-%20Final.pdf (last visited Aug. 11, 2018).

[31] Heiwai Tang, *Labor market institutions, firm-specific skills, and trade patterns,* 87 JOURNAL OF INTERNATIONAL ECONOMICS 337–351 (2012).

permission from the state government. By merely making life more cumbersome for the employee rather than the employer, the law is not enhancing efficiency, rather as I have tried to argue, efficiency is contextual and when there is value to be generated from an ex-ante relationship specific investment, the correct law is one that governs the relationship over a long period and this is important for gaining value.

In fact, in relation to this I want to draw from an opinion piece written by Ram Singh where he exhorts the Indian judiciary to appreciate the economic consequences of the judgments it makes - but he warns that this should mean that it takes to treating public purpose narrowly as is often the wont – "treating economic growth and the revenue of the state as public purposes is walking on a slippery slope".[32] Instead it is more important than ever before for the courts and the legislature to work with analytical rigour that is cognisant of the complex interactions that form economic life. In many instances the wisdom and interpretation of the courts is particularly vital - as MacLeod and Nakavachara tell us that while legislation best governs the average case, but it is often the cases that come to be determined in courts on account of egregious behavior of employers are the crucial marginal cases[33]. These are the ones that need to be correct, otherwise we end up with a preventative fall in productive relations.

[32] Ram Singh, *Acres of Contention (Comment),* THE HINDU (June 19, 2018).
[33] W. B MacLeod and V. Nakavanchara, *Can Wrongful Discharge Law Enhance Employment?* 117 ECONOMIC JOURNAL, F218–F278 (2007).