

MANAGING RETRENCHMENT FROM THE LEGAL PERSPECTIVE

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ABSTRACT

Retrenchment is termination by the employer of the service of an employee for any reason whatsoever, otherwise than as punishment inflicted by way of disciplinary action. This paper aims to focus on the prerogative of the management to retrench the employee in the case of redundancy. It also discusses the law governing retrenchment in Malaysia as in the Industrial Relations Act 1967, Employment Act 1955 and the Code of Conduct for Industrial Harmony 1975. It also evaluates the key steps in managing retrenchment together with the post retrenchment obligations of an employer. Finally, this paper examines the effects of non-compliance with the legal rights of the redundant employees.

Key words: retrenchment; managerial prerogative; procedures; non-compliance; dismissal.

Introduction

Retrenchment is termination by the employer of the service of an employee. It generally occurs where employees lose their job due to circumstances such as the closure of the business or a reduction in the number of employees. The reason could be the financial position of the firm, lack of work, reorganisation within the organisation or it may be closing down completely.

Retrenchment is not defined in Malaysian statutes. The term "retrenchment" has been explicitly explained by his Lordship Datuk Gopal Sri Ram, JCA in *William Jacks and Co. (M) Bhd. v. S. Balasingham*¹, as follows:

"Retrenchment means the discharge of surplus labour or staff by an employer for any reasons whatsoever otherwise than as a punishment inflicted by way of disciplinary action. Whether the retrenchment exercise in a particular case is bona fide or otherwise is a question of fact and degree depending on the peculiar circumstances of the case. It is well settled that the employer is entitled to organize his business in the manner he considers best. So long as the managerial power is exercised bona fide, the decision is immune from examination even by the Industrial Court. However, the Industrial Court is empowered and indeed duty-bound to investigate the facts and circumstances of the case to determine whether the exercise of power is in fact bona fide".

In *Credit Corporation (M) Bhd. v Choo Kam Sing & Anor*² [1996] 8 CLJ 86, the High Court adopted the definition in section 81(2) Employment Protection (Consolidation) Act 1978 which provides that an employee who is dismissed shall be taken to be dismissed by reason of redundancy if the dismissal is wholly or mainly attributable to:

- (a) the fact that his employer has ceased or intends to cease:
 - (i) to carry on the business for the purpose of which the employee was employed by him, or
 - (ii) to carry on that business in the place where the employee was so employed, or
- (b) the fact that the requirements of that business:
 - (i) for employees to carry out work of a particular kind, or
 - (ii) for employees to carry out work of a particular kind in the place where the employee was employed by the employer has ceased or diminished or are expected to cease or diminish.

The Employment Appeal Tribunal³ (UK) has formulated a three stage test to assist in determining whether a dismissal was a redundancy dismissal. The test has the following questions:

- (a) was the employee dismissed?
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¹ [1997] 3 CLJ 235

² [1996] 8 CLJ 86

³ The Employment Appeal Tribunal is a tribunal public body in England and Wales and Scotland, and its primary role is to hear appeals from Employment Tribunals in England, Scotland and Wales.

- (b) had the requirements of the business for employees to carry out work of a particular kind ceased or diminished or are expected to cease or diminish?
- (c) was the dismissal of the employee caused wholly or mainly by the state of affairs in (b) (above)?

If the answer to all three questions above is yes, then there is a redundancy dismissal.

2.0 Law Governing Managerial Prerogative and Right to Retrench

The relevant rules on retrenchment exercise are discussed with reference to Industrial Relations Act 1967, Employment Act 1955, The International Instruments and The Code of Conduct for Industrial Harmony 1975.

2.1 Industrial Relations Act 1967

Every employer has the right and privilege to organize his business in the manner he thinks fit for the purpose of economy or convenience. Section 13(3) Industrial Relations Act (IRA) 1967 recognizes the employer's right to terminate any workman by reason of redundancy or by reason of the reorganization of an employer's profession, business, trade or work. However, this right of the employer is limited by the law that he must act *bona fide* and not capriciously. Where it is shown that the exercise of these prerogatives is *mala fide* or amounts to unfair labour practice or indicates victimisation, the Industrial Court will not hesitate to strike down such exercise as bad (*Adam Abdullah v. Malaysian Oxygen Bhd.* [2012] 2 MELR 357).

In the case of *Chay Kian Sin v. Measat Broadcast Network System Sdn. Bhd.*,⁴ the Industrial Court held that the employer has the right to organize its business in the manner it considers best. Nevertheless, in doing so the employer must act *bona fide* and not capriciously or with motive of victimisation and unfair labour practice.

It was again reiterated in the case of *Tuan Syed Hashim bin Tuan Long v Esso Production Malaysia Inc.*⁵ that the right to reorganize the company is the prerogative of the management to achieve maximum efficiency and effectiveness. It is important that the employer acts fairly and conducts the retrenchment *bona fide* and untainted by any unfair labour practice.

In the case of *Harris Solid State (M) Sdn. Bhd. & Anor v. Bruno Gentil Pereira & Ors.*,⁶ the court succinctly stated as follows:

“An employer may re-organize his commercial undertaking for any legitimate reasons such as promoting better economic viability. But he must not do so for a collateral purpose, for example, to victimize his workmen for their legitimate participation in union activities. Whether the particular exercise of the managerial power was exercised bona fide or for a collateral reasons is a question of fact that necessarily falls to be decided upon the peculiar circumstances of each case”.

While in the case of *William Jack & Co. (M) Sdn. Bhd. v. S. Balasingam* [1997] 3 CLJ 235, the Court of Appeal ruled that:

“Whether the retrenchment exercise in a particular case is bona fide or otherwise, is a question of fact and of degree depending for its resolution upon the peculiar facts and circumstances of each case. It is well-settled that an employer is entitled to organise his business in the manner he considers best. So long as that managerial power is exercised bona fide, the decision is immune from examination even by the Industrial Court. However, the Industrial Court is empowered, and indeed duty-bound, to investigate the facts and circumstances of a particular case to determine whether that exercise of power was in fact bona fide”. [Emphasis added]

Predominantly, the Industrial Courts have held that the managerial prerogatives of the employer are qualified rights and there are important principles to be taken into consideration. It is for the management to decide on the strength of the staff which it considers necessary for efficiency in its undertaking. When the management decides that workmen are surplus and that there is a need for retrenchment, an arbitration tribunal will not intervene unless it is shown that the decision was capricious or without reason, or was *mala fide*, or was actuated by victimization or unfair labour practice.

2.2 Employment Act 1955

Section 12(3) Employment Act⁷ (EA) 1955 provides that an employee may be terminated from service by an employer when such termination of service of an employee is attributable wholly or mainly to the fact that –

⁴ [2012] 4 ILR 400

⁵ [1997] 1 LNS 99

⁶ [1996] 4 CLJ 747

⁷ The Employment Act 1955 provides minimum terms and conditions to employees earning less than RM2000.00 and to any person who, irrespective of the amount of wages has entered into a contract of service with an employer as prescribed in the First Schedule to EA 1955

- (a) the employer has ceased, or intends to cease to carry on the business for the purpose of which the employee was employed;
- (b) the employer has ceased or intends to cease to carry on the business in the place at which the employee was contracted to work;
- (c) the requirements of that business for the employee to carry out work of a particular kind have ceased or diminished or are expected to cease or diminish; and
- (d) the requirements of that business for the employee to carry out work of a particular kind in the place at which he was contracted to work have ceased or diminished or are expected to cease or diminish.

2.3 International Labour Organisation

The International Instruments which set out the key principles relating to the dismissal of employees, including redundancy situations are:

- (a) Termination of Employment Convention, 1982 (No: 158) (Convention 158); and
- (b) Termination of Employment Recommendation, 1982 (No: 166) (Recommendation 166).

The Convention No: 158 requires member states to specify the grounds upon which an employee can be terminated from employment. This Convention is supported by the Termination of Employment Recommendation, No: 166, which contains further specific guidance with regard to retrenchment situations. Like many member states, Malaysia has not ratified Convention No: 158. However, many of the principles under Articles 1-11 in the Convention No: 158 have been implemented into Malaysia redundancy law.

2.4 The Code of Conduct for Industrial Harmony 1975

The Code of Conduct for Industrial Harmony (the Code) was introduced in 1975 as guidelines to employers and employees on the practice of industrial relations for achieving greater industrial harmony. Clause 20-24 of the Code emphasises on the redundancy and retrenchment situations.

Clause 20 of the Code provides that in circumstances where redundancy is likely an employer should take positive steps to minimize reductions of workforce by the adoption of appropriate measures such as:

- i. to stop recruitment of new employees except for critical areas;
- ii. to limit overtime work;
- iii. to limit work on weekly rest days and public holidays;
- iv. to reduce weekly working days or reduce the number of shifts;
- v. to reduce daily working hours;
- vi. to conduct retraining programmes⁷ for workers;
- vii. to identify alternative jobs and to transfer workers to other divisions/other jobs in the same company;
- viii. to implement temporary lay-off (temporary shut down by offering fair salary and to assist the employees affected in obtaining temporary employment elsewhere until normal operation resumes); and
- ix. to introduce pay-cut in a fair manner at all levels and to be implemented as a last resort after other cost cutting measures have been carried out.

Clause 21 of the Code explained that the ultimate responsibility for deciding on the size of the workforce must rest with the employer. However the above steps should be taken by the employer after consultation with his employees' representatives or their trade unions.

Clause 22 (a) of the Code further provides that if retrenchment becomes necessary, despite having taken appropriate measures, the employer should take the following measures:

- i. giving as early a warning, as practicable, to the workers concerned;
- ii. introducing schemes for voluntary retrenchment and retirement and for payment of redundancy and retirement benefits;
- iii. retiring workers who are beyond their normal retiring age;
- iv. assisting in co-operation with the Ministry of Human Resources, the workers to find work outside the undertaking;
- v. spreading termination of employment over a longer period;
- vi. ensuring that no such announcement is made before the workers and their representatives or trade union have been informed.

The above Code has been given recognition by section 30(5A) IRA 1967 (*Said Dharmalingam v. Malayan Breweries (M) Sdn. Bhd.*⁸. In *Trident Malaysia Sdn. Bhd. v. National Union of Commercial Workers*,⁹ the court said:

⁸ [1997] 1 CLJ 646)

⁹ [1987] 2 ILR 190

“In short the Court is of the view that the provisions relating to redundancy and retrenchment in the Code of Conduct for Industrial Harmony were not adhered to by the Company and even if the retrenchments were bona fide the operating of the redundancy situation by the Company would have been found to be unacceptable by this Court as being unfair and the dismissals to be unjust therefore.”

3.0 Burden of Proof

The burden of prove lies on the employer to prove the actual redundancy. In *Bayer (M) Sdn. Bhd. v. Ng Hong Pau*,¹⁰ the Court of Appeal opined that on redundancy, it cannot be gainsaid that the appellant must come to the court with concrete proof. The burden is on the appellant to prove actual redundancy on which the dismissal was grounded.

The standard of proof that needs to be met by the employer in a redundancy case is the civil standard on a balance of probabilities. This standard is said to be flexible so that the degree of probability required is proportionate to the nature and gravity of the issue. Further, section 30(5) IRA 1967 also emphasised that the Industrial Court should not be burdened with the technicalities regarding the rules of evidence and procedure that are applied in a court of law (*Telekom Malaysia Kawasan Utara v. Krishnan Kutty Sanguni Nair & Anor.*¹¹ This approach was reaffirmed in the case of *K A Sanduran Nehru Ratnam v. I-Berhad.*¹²

4.0 Key Steps in Managing Retrenchment

It is advisable for the employer to plan and manage proper steps to have a smooth retrenchment exercise. The employer is suggested to adopt the following steps.

4.1 Consultation with the Trade Union

As a matter of good employee relations and fairness, the employer should consult with the trade union about the proposed redundancies. Consultation with the trade union must be undertaken by the employer with a view to reaching agreement on issues such as ways of avoiding dismissals or reducing the number of employee to be dismissed. This duty applies even when the employees to be made redundant are volunteers and irrespective of the number of redundancies proposed. If there is no trade union, meeting should be held individually with the employees that could be affected by the retrenchment.

4.2 Notice to the Labour Office

The Employment Retrenchment Notification 2004 makes a responsibility on the employers to report to the nearest Labour Office of any planned redundancies. An employer who is proposing to dismiss his employees on the reason of surplus must notify the labour office *vide* the prescribed Form PK1/98 at least one month prior to the retrenchment of the employee. An employer who fails to notify the Labour Office of the proposed redundancy as accordance to section 63 of the EA 1955 commits an offence punishable under section 99A EA 1955 of a fine not exceeding ten thousand ringgit.

4.3 Determining Selection criteria

Redundancy selection essentially involves two matters, firstly the choice of criteria upon which the selection process will be based and secondly, the application of the chosen criteria to the employees in question. It is essential that during a redundancy process that the employer ensures that fair and transparent criteria for selection for redundancy are identified and applied consistently. This will help employers when explaining to employees the reason for their selection.

According to Clause 22(b) of the Code, such criteria, which should have been worked out in advance with the employees' representatives or trade union may include:

- (i) the need for the efficient operation of the establishment or undertaking;
- (ii) ability, experience, skill and occupational qualifications of individual workers;
- (iii) consideration for length of service and status;
- (iv) age;
- (v) family situation; and
- (vi) such other criteria as may be formulated in the context of national policies.

4.4 Statutory Notice for Termination

Employers who are retrenching employees must give notice and offer retrenchment benefits to eligible employees. Employers are also bound by the EA 1955 in respect to termination notice for redundant employees. All employers are required to comply with section

¹⁰ [1999] 4 MLJ 361

¹¹ [2002] 3 CLJ 314

¹² [2007] 1 CLJ 347

12(2) EA 1955 which require sufficient notice to be given to the employees before retrenchment exercise being carried out. If the contract of employment does not specify the period of notice, the notice shall be as follows:

- (i) four weeks' notice for those employed for less than two years;
- (ii) six weeks' notice for those employed from two to five years; and
- (iii) eight weeks' notice for those employed for five years or more.

Employees who are terminated without adequate notice of termination, can claim indemnity which must be paid latest by the last day the contract of service is terminated. However, the statutory requirements for the above minimum notice period does not apply to other category of employees who is not within the ambit of the EA 1955.

4.5 The rule 'Last in First out' (LIFO)

LIFO (Last In First Out) is the golden rule of procedural retrenchment law. The LIFO [last in first out] or "last come first go" principle requires the most junior employee to be retrenched before the more senior ones in the same category. The principle is intended to afford a healthy safeguard against discrimination of workmen in the matter of retrenchment. In the case of *Workmen of Sudder Workshop of Jorehaut Tea Co Ltd v. The Management of Jorehaut Tea Co. Ltd.*,¹³ the Supreme Court said: "The rule is that the employer shall retrench the workman who came last, first, popularly known as 'last come first go'.

The onus of justifying a departure from the LIFO principle is on the employer. The employer must have sound and valid reasons for departure from the LIFO principle.¹⁴ While in *Carrier International Sdn. Bhd. v. Rahim Kassim & Ors*¹⁵ it was postulated that:

"... though the Code has no legal force (Penang Seberang Prai Textiles & Government Industry Employees Union v. Dragon & Phoenix [1989] 1 MLJ 48) it is a relevant factor for the purpose of considering the overall reasonableness of the employer's action in dismissal cases. In this regard the learned chairman is correct when he took into consideration the fact that there was no consultation held with the 1st respondent before his dismissal as one of the grounds that the dismissal was without just cause or excuse..."

4.6 Foreign Employee

Section 60N EA 1955 provides that the employer shall not terminate the services of a local employee unless he has first terminated the services of all foreign employees employed by him in a capacity similar to that of a local employee. Despite the Foreign Worker First Out (FWFO) policy, the employers are advised to fulfill their contractual obligations by ensuring adequate compensation are paid to the foreign employees for early termination of employment agreement, that is for the remaining duration of their employment agreement.

4.7 Lay off

Lay off is an alternative to retrenchment. If the employer is moving towards a retrenchment, he is required to practice lay off first and if he is unable to continue lay off then retrenchment become necessary. The employer should explain to the employees the reason for the lay off or short-time working and apply the same standard of selection criteria as for redundancy. The criteria should be reasonable and applied in a fair manner.

Regulation 5(1) Employment (Termination and Lay-off Benefits) Regulations 1980 explains that it is deemed to be laid off if the employer does not provide work for at least a total of twelve normal working days within any period of consecutive weeks; and the employee is not entitled to any remuneration in which he is not provided with work. While, Regulation 5(2) emphasized that in case of lay off, the continuity of a contract of employment of an employee shall not be treated as broken and as a result of which no lay off benefits payment has to be paid.

5.0 Redundancy Benefits

Employees who has been employed by an employer more than 12 months and are in the contract of employment are entitled to receive the redundancy benefits as provided in Employment (Termination and Lay-off Benefits) Regulations 1980, EA 1955 as follows:

- a. ten days' wages for each year of service if he has been employed by the employer less than two years.
- b. fifteen days' wages for each year of service if he has been employed by the employer more than two years but less than five years.
- c. twenty days' wages for each year of service if he has been employed by the employer five years or more.

Regulation 11 further requires the redundancy payment be paid by the employer to the employee not later than seven days after the contract of service of an employee is terminated.

¹³ AIR 1980, S.C 1454

¹⁴ *Ganda Palm Services Sdn. Bhd. Teluk Intan v Ng Wah Chiew & 2 Other Award* 40/1986

¹⁵ [2006] 2 ILR 879

6.0 Voluntary Separation Scheme (VSS)

Today VSS has become popular as a means of reducing the number of employee. A VSS is a scheme where employees are allowed to leave or resign from their service by receiving severance package or compensation from the company. A VSS is done as part of the effort to curb with financial difficulties and reduce expenditure in the long run.

In the case of *AK. Bindal & Anor v. Union of India & Anor*,¹⁶ the Supreme Court of India had succinctly laid down the governing principles for VSS thus:

“...The Voluntary Retirement Scheme (VRS) which is sometimes called Voluntary Separation Scheme (VSS) is introduced by companies and industrial establishments in order to reduce the surplus staff and to bring in financial efficiency.

The whole idea of implementing VRS is to save costs and improve our productivity. The main purpose of paying this amount is to bring about a complete cessation of the jural relationship between the employer and the employee. After the amount is paid and the employee ceases to be under the employment of the company or the undertaking, he leaves with all his rights and there is no question of him again agitating for any kind of his past rights, with his erstwhile employer including making any claim with regard to enhancement of pay scale for an earlier period.

If the employee is still permitted to raise a grievance regarding enhancement of pay scale from a retrospective date, even after he had opted for Voluntary Retirement Scheme and had accepted the amount paid to him, the whole purpose of introducing the scheme would be totally frustrated”.

The author, Ashgar Ali Ali Mohamed in his article "*Voluntary Retrenchment: Voluntary or Manual Separation Scheme*"¹⁷, outlined the effect of a Voluntary Separation Scheme as follows:

“When an employee makes an application for VSS, he is considered as offering his early retirement to the company, subject to the company's acceptance of it. When the company accepts the application for VSS, the contract of employment is said to be terminated by mutual consent and it is not considered a dismissal”.

In *Abdul Aziz Ismail & Ors v. Royal Selangor Clubs*,¹⁸ the Industrial Court held that the employees had voluntarily applied to participate in the VSS initiated by the club and when the latter had accepted their VSS applications, it had resulted in a cessation of their employments.

7.0 Compliance with Collective Agreement

Collective agreement is an agreement in writing concluded between an employer or a trade union of employers on the one hand and a trade union of workmen on the other relating to the terms and conditions of employment and work of workmen or concerning relations between such parties. It is provided for in section 17 of the IRA 1967 that a collective agreement which has been taken cognizance of by the Court shall be deemed to be an award and shall be binding on the parties to the agreement including all workmen who are employed or subsequently employed in the undertaking or part of the undertaking to which the agreement relates. Section 17 IRA 1967 further states that the collective agreement shall be an implied term of the contract between the workmen and employers bound by the agreement that the rates of wages to be paid and the conditions of employment to be observed under the contract shall be in accordance to the agreement. As such, if a retrenchment exercise was to carried out without compliance with the procedures set in the collective agreement it can amount to dismissal.

In *Dunlop Industries Employees Union v. Dunlop Malaysian Industries Bhd.*¹⁹ the Supreme Court struck down an entire retrenchment exercise as the company failed to give notice of retrenchment prior to retrenchment. The court held that the retrenchment was carried out contrary to the collective agreement.

8.0 Post Retrenchment Obligations by the Employer

Where there is a necessity to recruit employees for the category of employees who were retrenched, company is to give preference to employees who were retrenched if they wish to be reemployed. In the event such employees are reemployed, they are to be treated as new employees as they were paid retrenchment or termination benefits.

Clause 23 of the Code also emphasised that employees, who are retrenched, should be given priority of engagement or re-engagement, as far as is possible, by the employer when he engages workers.

In *Kesatuan Pekerja-pekerja Perusahaan Logam v. KL George Kent (M) Bhd.*²⁰, there was a provision in a collective agreement between the employer and employees that they agreed to observe the provisions of the Code. One of the provisions in the Code provides that the retrenched employees should be given priority for re-engagement. However, the Industrial Court in its decision

¹⁶ [2003] 3 LRI 837

¹⁷ [2015] 1 ILR iii

¹⁸ [2015] 2 ILR 546

¹⁹ [1978] 1 MLJ 232

²⁰ [1991] 1 MLJ 230

did not consider this provision. On appeal the High Court reversed the Industrial Court's decision and held that the employer was bound to follow the provision of the Code, which provided that the retrenched employees should be given priority of engagement or re-engagement rather than bringing in new employees.

9.0 Remedy for Unfair Dismissal

The Industrial Relations Act 1967 applies to all workers including migrant workers and they have right to pursue their rights if infringed in the Industrial Court. Section 2 EA 1955 defines a workman as "any person... employed by an employer under a contract of employment to work for hire or reward and for the purposes of any proceedings in relation to a trade dispute...". The First Schedule Item 1 of EA 1955 further describes the category of workers as "any persons irrespective of his occupation who has entered into a contract of service with an employer..." and, in Item 2 it describes the other category of workers covered by the Act.

Employers who do not comply with the law and regulations on redundancy may face actions for unfair dismissal. In order for a dismissal to be fair, the employer has to show that redundancy was the reason for the dismissal, and that redundancy was handled in a fair manner. Employees may bring action against their employer for unjustified dismissal under section 20 IRA 1967. In a successful case of unfair dismissal, the Industrial Court may award back wages not exceeding 24 months from the date of dismissal, compensation *in lieu* of reinstatement and other monetary compensation as the court think just (2nd Schedule IRA 1967).

In *Wee Chee Khoon v. Citibank Berhad*,²¹ the Court finds that the claimant had not become redundant and the Bank's decision to terminate him was without just cause or excuse. The Court allowed the claimant's application and award compensation *in lieu* of reinstatement as an order of reinstatement is not an appropriate remedy. Meanwhile, in *Adam Abdullah v. Malaysian Oxygen Bhd.*,²² the court orders that the back wages should be reduced taking into account the retrenchment benefits was paid to the claimant at the time of his dismissal.

10.0 Conclusion

Redundancies are an unfortunate reality for almost all employers. Before taking any action, the employer needs to ensure that the reason for the proposed dismissals is genuinely redundancy. If an employer falsely labels a dismissal as a redundancy, this is likely to render the dismissal unfair. If the retrenchment exercise is tainted with *malafide* or amounted to unfair labour practice then the employer must face the consequences of a legal action. The Industrial Court has the power to award a reasonable amount depending on the facts and merits of each case based on the grounds of equity and good conscience. If in cases of reinstatement of employee which is not possible, the court will order the employer to pay back wages and other monetary compensation.

Employer may take steps that go beyond retrenchment benefit payments and compliance with basic legal requirements to demonstrate corporate social responsibility in relation to retrenchment. Employers can assist retrenched employees to find alternative employment at another workplace when no suitable alternative job is available with the same employer.

Aside from the altruistic nuances of corporate social responsible, the employees should be exposed to some form induction to the legal aspect of their employment from HR consultants and lawyer or otherwise. it would be would be a bitter pill to swallow by the employer but the reality of good industrial practices would warrant such a swift and bold actions to be taken by the trade union and others championing the employees' rights to be obstinately steadfast in demanding that the legal awareness amongst the employees to be part and parcel of the package deal. it would seems plausible to include that package in the collective agreements as a suggestions worthy of considerations. that shall be a cost mandatorily borne by the employer as part of their corporate commitments simpliciter to honour the collective agreements between them and the employees.

It is further suggested that ILO Convention No 158 and No 166 should be ratified by the government. The Code also should be transposed into legislation to avoid unclear area especially on the legal effect of the Code.

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²¹ [2011] 2 LNS 495

²² [2012] 2 ILR 416