# Difference between Retrenchment, VSS, & MSS

Although the end result is the same for retrenchments, VSS and MSS (i.e. the employee is no longer employed), there are differences.

## Retrenchment

This is dismissal of employees who are regarded as surplus to requirements. The company / department itself is not being closed, but rather a select group of employees are retrenched. Not all employees are retrenched.
Companies in carrying out retrenchment are required to abide the legal provisions of the Employment Act 1955 (where relevant) and the general rule of LIFO (Last In First Out).

## VSS

Voluntary Separation Scheme. This arises when a company that is not officially retrenching but nonetheless wishes to get rid of employees.
In this scenario, the company will make an announcement that is addressed to the employees along the lines of 1) "*Profit hasn't been good*" 2) "*We have been making losses"* 3) "*The company is not dismissing anyone, but will welcome application from employees to be considered for VSS"*.
It is like a job advertisement that invites applicants. The difference here is that it is not a job advertisement, but rather, an invitation by the company for application by the employees, to be considered for VSS.

Usually the company will also talk about the terms and conditions of the VSS (compensation terms, qualifications, requirements etc).

Because of the nature of VSS, it is usually more difficult for employees who have left the company on VSS to challenge this in the Malaysian courts.

## MSS

Mutual Separation Scheme. This arises when both parties agree to terminate the employment relationship. The keyword is **"mutual",** i.e. both parties agree to a settlement that is a win-win scenario for them.

## Section 20 IRA 1967

As is the case with all dismissals of employees, the employer has the burden of proving just cause or excuse in dismissing the employee(s).

If it is a retrenchment and the purported reason is eg, losses for the preceding xx number of years, then the employer must be able to show the losses by way of the profit and loss account, etc.

A VSS is more difficult for the employee to argue unless it can be shown that the employee was coerced into it, or there existed the usual elements that may render the VSS void or voidable.

It is settled law that a company has the right to organise and reorganise its business in the manner it considers best for better business management and efficacy. In this respect, the company may reorganise or restructure by *inter alia* retrenching surplus labour. However, in doing so, the company must act bona fide and not capriciously or with motives of victimisation or unfair labour practices, as held in William Jacks & Co (M) Sdn Bhd v S.Balasingam.

To justify retrenchment, there must first be redundancy. In proving redundancy, there must be a surplus of labour or the requirements of

the job functions of the employee have ceased or diminished to the extent that the job no longer exists.

**Guidelines to the Procedure of Retrenchment**

**(A) Providing the Employee Notice**

The Employment Act 1955 ("EA") and the Employment (Termination and Lay Off Benefits) Regulations 1980 ("Regulations") govern the retrenchment exercise of employees who earn not more than RM2,000 monthly and manual workers irrespective of the amount of their monthly salaries. For employees who fall within the EA, the length of notice period depends on the employees' length of employment:-

| Duration of employment on the date on which notice is given | Length of notice |
|---|---|
| Less than 2 years | Not less than 4 weeks |
| 2 years or more but less than 5 years | Not less than 6 weeks |
| 5 years or more | Not less than 8 weeks |

For employees who do not fall within the EA, the length of notice period would be in accordance with their employment contract

**(B) Compliance with Code of Conduct for Industrial Harmony 1975 (the "Code")**

If it is found that there is redundancy, the Industrial Court ("Court") has encouraged for retrenchment exercise to be carried out, as far as possible, in accordance with the accepted standards of procedure and guidelines such as the Code. Clause 22(a) of the Code states that if retrenchment becomes necessary despite having taken appropriate measures, the employer should take among others, the following measures:-

(i)Give early warning to the employees concerned;

(ii)Introduce schemes for voluntary retrenchment and retirement benefits;

(iii) Retire employee who are beyond their normal retiring age;

(iv) Assist in co-operation with the Ministry of Human Resources, the employees to find work outside the undertaking;

(v)Spread termination of employment over a longer period;

(vi) Ensure that no such announcement is made before the employees and their representatives or trade union have been informed.

The Code also states that the selection for retrenchment should be based on the following:-

(i)need for the efficient operation of the company;

(ii)ability, experience, skill and occupational qualifications;

(iii) length of service (Last in, First Out "LIFO" principle) and status (non citizens, casual, temporary, permanent);

(iv)age;

(v)family situation; and

(vi) other criteria as may be formulated in the context of national policies.

**(C) Reporting the Retrenchment**

Employers are required to report the retrenchment, voluntary separation, temporary layoff or an employee's pay-cut, if applicable, to the nearest Labour Office before any said act termination action via the prescribed Termination Form.

Failure to submit the report within the stipulated timeline is an offence under the EA and the employer could be fined for not more than RM10,000 for each offence.

**(D) Retrenchment Benefits**

For employees who fall within the EA, the Regulations provide that an employee would be entitled to termination or lay-off benefits if the employee was employed under a continuous contract of employment for at least 12 months before the termination. Pursuant to the Regulations, the quantum of termination benefits to be paid is prescribed.

For employees who do not fall within the EA, the obligation to pay retrenchment benefits and the quantum of retrenchment benefits, if any, would be in accordance with their employment contract, if applicable.

Employers are also required to submit the prescribed form to the Inland Revenue Board of Malaysia at least 30 days before the date of retrenchment.

**A Guise to Dismissing the Employee?**

Having such a prerogative power, there have been circumstances where employers have dismissed their employees under the guise of retrenchment. In these circumstances, the Court may find that the employees are being dismissed without just cause or excuse.

For example, it was held that the retrenchment was not bona fide (authentic) where the employee was made redundant but the job with the same duties and functions remain (vacant post) or where employees who were terminated were in fact all active union members (Union Busting).

If the Court finds that there is unfair labour practice under the guise of retrenchment due to abuse of prerogative power or there is no genuine retrenchment the Court, being a court of equity and good conscience may conclude that the termination or dismissal was without just cause or excuse. In this case, the Court may order reinstatement or compensation in-lieu of reinstatement and back wages of a maximum of 12 months of the employee's last drawn salary for a probationer or a maximum of 24 months for a confirmed employee.

It is important to comply with the requirements for retrenchment because the Court will not hesitate to protect the employees if it is found that the retrenchment was made mala fide (in bad faith or with intent to deceive) or that the requirements for retrenchment were not complied with.

Retrenchments are often (but not necessarily) the result of economic downturns and are commonly understood as being part of a company’s business strategy to deal with business losses.

However, this understanding may be incomplete as there are many legal considerations that go behind the scene in a retrenchment exercise; companies do not have absolute autonomy in the way they run their business and are not insulated from scrutiny by virtue of it being a “business decision”.

Here are the 7 things you should know about retrenchment from a legal perspective:

**What is retrenchment and what is redundancy? Is there a difference in meaning behind the terminology?**

Retrenchment is a form of dismissal that is justified on the basis that the roles of the employees concerned have become redundant. Proof of redundancy, that is, surplus of labour, is required for a retrenchment exercise to be valid. Redundancy can arise in many situations, examples include cessation of job functions, merger of work units and discontinuation of production line.

Put in another way, redundancy is a situation where the employee or position is no longer required. Retrenchment is the action taken to terminate the employment relationship in the event of redundancy.

**In what situation can a company retrench an employee?**

Companies are generally at liberty to organize their business enterprise in a manner that best achieves their objective of maximizing profit, so long as the exercise is bona fide. As employees’ livelihoods are affected by the exercise, courts have been willing to interfere where it can be shown that the decision to reorganize is capricious, without reason or actuated by unfair labour practice.

Companies that are suffering losses may decide on a business strategy to minimize the impact of poor economic
conditions, by for example terminating some employees and outsourcing those job functions to third parties in order to reduce costs. This reduced turnover and decision to outsource job functions are some of the justifications that have been accepted by courts as being bona fide and beyond the purview of courts’ intervention. That being said, the courts will still examine the entire factual circumstances surrounding the employee’s dismissal before coming to a conclusion as to whether the dismissal was fair.

The burden of proving that the retrenchment was bona fide lies on the employer, and it is not on the employee to show that the retrenchment was unfair. In 2012, in quoting a decision of the Court of Appeal, the Federal Court held that it is insufficient for an employer to merely show evidence of a reorganization or reduced sales. The employer had a duty to prove that the circumstances were such that the employees' functions were reduced to such an extent that they are considered redundant.

**What guidelines should employers follow when selecting employees to retrench?**

The Code of Conduct for Industrial Harmony ("Code") provides guidelines on the best practice for retrenchment exercises. While not legally binding, failure to comply may be a factor that courts take into consideration in determining whether the retrenchment exercise was carried out in a fair manner.

The Code contains suggested criteria for employers to consider when selecting employees to retrench. This includes:

- Ability
- Experience
- Skill and occupation qualifications
- Age
- Family situation
- Length of service
- Status (non-citizens, casual, temporary, permanent).

A common industrial practice is also to retrench employees based on the LIFO principle, ie "Last In, First Out", whereby the most junior employee (measured in terms of length of service) in a particular category is selected for retrenchment. It is not mandatory for employers to use the LIFO principle, although it is recognized as one of the more objective means of selection.

Employers can depart from the LIFO principle if they have an alternative, objective selection criteria. LIFO may also be inapplicable in situations where there is only one employee in the affected category or position.
In cases where there are foreign workers occupying posts similar to that of local employees, the Employment Act 1955 requires that the services of foreign workers be terminated first.

**Notification to the authorities**

Employers are required to submit an employment notification retrenchment form (PK Form) to any Labour Office, failure of which carries a punishment of a fine of RM10,000.00. Employers are required to disclose information such as the reasons for the retrenchment, number of workforce, number of workers involved in voluntary separation scheme, etc.

The PK Form is filed in parts and in stages, the first taking place 30 days before the actual retrenchment, and the rest to be filed within 14 days and 30 days after the date of retrenchment. The PK Form is a notification requirement, and is not a request for approval. As such, employers do not need approval from the labour office before they can conduct retrenchment exercises.

**Does the law require employers to pay any retrenchment benefits?**

The relevant provisions are found in regulations 3, 4 and 6 of the Employment (Termination and Lay-off Benefits) Regulations 1990. These provisions are only applicable to employees coming within the purview of the Employment Act 1955, eg: employees whose salary do not exceed RM2,000 a month or who are engaged in manual labour.

Under the Regulations, only employees who have been employed under a continuous contract of employment of not less than 12 months before the date of termination are entitled to the termination benefits, which are as follows:

| **Length of Service** | **Termination Benefits** |
|---|---|
| Less than 2 years | 10 days' wages for every year of service |
| 2 years or more, but less than 5 years | 15 days' wages for every year of service |
| 5 years or more | 20 days' wages for every year of service |

During acquisitions, employees may be “transferred” to the acquiring company for reorganization reasons. From a legal perspective, this involves terminating the existing employment contract with the target company and having a new job offer extended from the acquirer. In such situations, employees are not entitled to termination benefits if:

- the acquirer offers to continue to employ the employee under terms and conditions of employment not less favourable than their existing contract with the target company; and
- the employee unreasonably refuses the offer

For employees not covered under the Employment Act 1955, their termination benefits would depend on the terms of their contract.

**Can employees challenge a retrenchment?**

In the absence of a valid justification for the retrenchment exercise, the termination may amount to dismissal without just cause and excuse entitling employees to remedies such as backwages, reinstatement and/or compensation in lieu of reinstatement.

An employee who believes they have been unfairly retrenched must lodge a complaint with the Director General of Industrial Relations within 60 days from the date of the dismissal. If parties are unable to settle their dispute during the conciliation meeting ordered by the Department of Industrial Relations, the Minister of Human Resources may refer the matter to the Industrial Court for adjudication.

**Best practices for retrenchment**

For a start, employers should, where possible, comply with the Code (mentioned earlier) and any other guidelines that may be issued by the Ministry of Human Resources in order to strengthen their case that the retrenchment exercise was objective and bona fide.

Some of the best practices (as extracted from the Code) include:

Firstly, consider whether there are other alternatives for cost-cutting, as opposed to retrenchment, eg:

- Limitation of recruitment (head count freeze)
- Restriction of overtime work
- Reduction in shifts worked
- Reduction in number of hours worked
- Retraining and/or transferring to other departments or subsidiaries within the organisation
- Giving as early warning, as practicable, to the workers concerned
- Introducing schemes for voluntary retrenchment and retirement (eg: VSS)
- Retiring workers who are beyond the retirement age first
- Provide payment of redundancy and/or retirement benefits
- Having a (well documented) objective selection criteria
- Spreading termination of employees over a longer period

Consider other alternatives to retrenchment such re-training and/or transferring the employee to other departments / subsidiaries within the organisation, temporary reduction of working hours; etc

Adopting best practices is not just to pre-empt the likelihood of the exercise being successfully challenged in court but to also ensure that employers adopt policies that are in accordance with fair and equitable labour practice.

## PART XIIA -TERMINATION, LAY-OFF, AND RETIREMENT BENEFITS

### 60J. Termination, lay-off and retirement benefits

(1) The Minister may, by regulations made under this Act, provide for the entitlement of employees to, and for the payment by employers of --

- (a) termination benefits;
- (b) lay-off benefits;
- (c) retirement benefits.

(2) Without prejudice to the generality of subsection (1), regulations made by virtue of subsection (1) may provide --

- (a) for the definition of the expression "termination benefits", "lay-off benefits", or "retirement benefits", as the case may be, and for the circumstances in which the same shall be payable;
- (b) for the application thereof to employees who were in employment under a contract of service immediately before the commencement of such regulations and who continue in such employment after the commencement thereof;
- (c) for the application thereof to all employees generally or to any particular class, category or description of employees;
- (d) for the exclusion from the application thereof of any particular employee or employees, or any class, category or description of employees;
- (e) for the payment of different rates or amounts of termination benefits, lay-off benefits, or retirement benefits, as the case may be, to different classes, categories or descriptions of employees.

## 60N. Termination of employment by reason of redundancy

Where an employer is required to reduce his workforce by reason of redundancy necessitating the retrenchment of any number of employees, 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 the local employee.