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# **EMPLOYEE'S STATE INSURANCE** **CORPORATION: DOWNFALL IN ITS** **LEGAL MECHANISMS<sup>1</sup>**

Authored by - Nandha Kumar S A

## **INTRODUCTION**

The Employee State Insurance is one type of an integrated social safeguard system having multidimensional and customized to offer security and protection to the employees. The significance behind the amalgamation of legislations under the Social Security Code 2020 largely will facilitate the Implementation and remove the multiplicity of definitions and authorities without compromising the basic concepts of welfare and benefits to workers. Further the use of technology for effective enforcement of the provisions of the Code, intended with a view to ensure transparency, accountability and facilitating the ease of compliance. The Code it also widens the scope of the benefits to the fixed term employees which will be a big step towards equity.

Under the ESI Act, if a principal employer fails or neglects to pay contributions to employees and thereby disentitles them to certain benefits, or an appropriate scale of benefits, the ESI Corporation ("**ESIC**") may pay the aggrieved employees the benefits they are rightly entitled to and recover such amount from the employer. The Code expands the scope of this provision to include the employer's failure or neglect to insure (i) an employee at the time of his appointment, which deprives him of entitled benefits and (ii) employee on/after the date of accident resulting in personal injury, which disentitles him to receive dependent benefit or disablement benefit. In such cases, ESIC is empowered to provide the entitled benefits to the concerned employees and recover from the employer the capitalized value of such benefits, after adjusting any contribution/interest/damages that the employer is liable to pay for non-payment or delayed payment of requisite contributions.

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Under the Code, establishments that have a smaller number of employees than the prescribed threshold for coverage under the provisions of the Employees' Provident Fund ("EPF") and the Employees' State Insurance Fund ("ESI") have the option to avail of voluntary coverage under the same and subsequently opt out of such voluntary coverage, subject to fulfilment of certain conditions. By providing such flexibility, the Code seeks to facilitate provision of such benefits to employees of smaller establishments while providing a safety net for employers to opt out of such coverage. The Code comprehensively defines 'establishments' to mean, amongst others, places such as factories, motor transport undertakings, and newspaper establishments, where an industry, trade, business, manufacture, or occupation is carried on. All such establishments covered by the Code will need to obtain a registration. However, establishments that are already registered under any other Central labour law in force will not be required to obtain such registration as their existing registration will be deemed to be a registration for purposes of the Code.

Under the EPF Act and ESI Act, no limitation period is prescribed for recovery of past dues from employers. Further, no formal direction or guidance has been given by the respective authorities with regard to the period of assessment for past non-compliance. This creates undue hardships for employers against whom the EPF/ESI authorities initiate recovery proceedings for any retrospective period, as per their discretion. The Code provides a limitation period of five years for such proceedings and thereby safeguards the employer's pecuniary interest. As such, employers will be able to estimate the maximum liability for past non-compliance under the Code. All employees who earn less than ₹ 21,000/month are covered under the ESI scheme. ESI under Code on Social Security reduces this threshold by making Chapter IV applicable to every establishment where 10 or more persons are employed.

Presently, the ESI Act does not operate at a pan-India level and is being implemented district-wise through notification. However, ESI under the new Code has been made applicable to the entire country, subject to the specified threshold of 10 employees in an establishment. Further, a provision has been introduced in the First Schedule to enable the Central Government to notify applicability of ESIC Act on those classes of establishment, which engage in hazardous or life-threatening activities. In these classes of establishment, ESI will be applicable even if only one worker is employed. Provisions for voluntary inclusion under the ESI Scheme have also been introduced. An employer of a plantation may opt for ESI under the Code on Social Security by giving willingness to the ESI Corporation. Further, a non-obstante clause [Section

1(7)] enables voluntary membership under ESI even if the number of employees in an establishment is less than the specified threshold of 10. In case an employer and a majority of the employees of an establishment agree to be covered by ESI, then on an application made by the employer or otherwise, the Director General of ESIC may allow the applicability of ESI to such establishment.

These measures, of voluntary membership, reduced threshold of 10 employees and applicability to establishments carrying out hazardous activities, will help in widening the applicability of ESI under the Code on Social Security at a pan-India level across establishments. At present, 3.5 crore families are covered under the ESI Scheme. It is expected that the coverage will increase to 10 crore families under the new Code.

Digitization of procedures through a centralized web-based portal, the Shram Suvidha Portal, is expected to simplify compliance processes for employers. Digitization will also help in maintaining a database of information that is easily accessible for disbursement of benefits. The Code has a provision for centralized inspection through the web portal. While the Central Government has not notified any Rules in this regard, it may do so in the future. Additionally,

Under **Section 122(6)(c)** of the Social Security Code, the Inspector-cum-Facilitator has the power of search and seizure in respect of any offence that the Inspector believes to have been committed by the employer. Earlier, there was no such provision for search and seizure under the ESI Act, but now this search and seizure can be exercised to ensure compliance related to ESI under the Code.

The Code has added grandparents under the definition of '**dependent**' [**Section 24(c)(viii)**] if the grandparent is wholly or in part dependent on the earnings of the employee at the time of their death and if no parent of the employee is alive. The ESI Act did not provide for this. This is a welcome addition towards recognizing and providing for the welfare of senior citizens. It is to be noted that the rates of contribution and quantum of benefits are the same for ESI under the Code on Social Security as in the ESI Act at present.

The Key changes in regard with Social Security Code 2020 and the Prior legislation is,

- The SS Code allows for **voluntary registration/ inclusion** under the Employee State Insurance if the employer and majority of the employees agree.

- By providing such flexibility, the Code seeks to facilitate provision of such benefits to employees of smaller establishments while providing a safety net for employers to opt out of such coverage.
- Further, the Government has the power to extend the Employee State Insurance Scheme to any hazardous occupation irrespective of the number of employees employed.
- The SS Code also provides for coverage of Gig Workers and Unorganized Sectors under the Employee State Insurance Scheme.
- The employer shall pay in respect of every employee, whether employed by him directly or through a contractor, both the employer's contribution and the employee's contribution.
- Neither the employer nor the contractor shall be entitled to deduct the employer's contribution from any wages payable to an employee or otherwise to recover it from him.
- Under the EPF Act and ESI Act, no limitation period is prescribed for recovery of past dues from employers. Further, no formal direction or guidance has been given by the respective authorities with regard to the period of assessment for past non-compliance.
- This creates undue hardships for employers against whom the EPF/ESI authorities initiate recovery proceedings for any retrospective period, as per their discretion.
- The Code provides a limitation period of five years for such proceedings and thereby safeguards the employer's pecuniary interest. As such, employers will be able to estimate the maximum liability for past non-compliance under the Code and this limitation is tailored in a way that justifies employer's pecuniary interest.
- Under the ESI Act, if a principal employer fails or neglects to pay contributions to employees and thereby disentitles them to certain benefits, or an appropriate scale of benefits, the ESI Corporation ("**ESIC**") may pay the aggrieved employees the benefits they are rightly entitled to and recover such amount from the employer.
- The Code expands the scope of this provision to include the employer's failure or neglect to insure an employee at the time of his appointment, which deprives him of entitled benefits and employee on/after the date of accident resulting in personal injury, which disentitles him to receive dependent benefit or disablement benefit.
- In such cases, ESIC is empowered to provide the entitled benefits to the concerned employees and recover from the employer the capitalized value of such benefits, after

adjusting any contribution/interest/damages that the employer is liable to pay for non-payment or delayed payment of requisite contributions.

- Currently, **the employee's contribution rate is 0.75% of their wages, and the employer's contribution rate is 3.25% of the wages paid/payable for the employees**, W.E.F. 1-7-2019. (Previously it was 1.75 for Employee and 4.25 for Employer) The employees who receive a daily average wage of up to **Rs. 137 (176 in prior legislation)** are exempt from paying their share of contribution. However, ER has to do his contribution.
- Illustration, Let us say Mr.Y is an employee working in an Establishment, fulfilling the threshold limit and fit the wage ceiling. So, Employer's Contribution will be  $3.25 \times 21,000$  which is 157.5 and the Employee's contribution for ESI Scheme is  $0.75 \times 21,000$  which is 682.5. So, on that note a total amount of 840 will be made.
- The onus of deducting the contribution and depositing the same is on the employer. The employer must deposit the amount within 15 days of the end of the calendar month in which the deduction is made. The same can be deposited online or to authorized designated branches.

## PROVISIONAL INTERPRETATIONS

- **Section 43** of the Code seeks to make the owner or occupier of factories or other establishment or the owner of the tenement or lodgings liable for payment of the amount of the extra expenditure incurred by the corporation as sickness benefit, where the corporation considers that the incidence of sickness among the insured persons is **excessive due to the default or neglect** of the owner or the occupier of the factory or other establishment or the owner of the tenements or lodgings. When the corporation considers that the incidence of sickness among insured persons is excessive by reason of, Insanitary working conditions in a factory or other establishment, any tenements or lodgings occupied by insured person and such conditions is attributable to neglect of owner under any enactment for the time being in force,
- Then the corporation may send a claim for the payment of amount of the extra expenditure incurred as sickness benefit - if not settled by agreement –then the corporation may refer the matter to the appropriate government.
- If prima facie is there for inquiry, appoint a competent person to hold an inquiry, if proved that's the default is on the owner or occupier of that establishment – then the

amount of extra expenditure incurred as sickness benefit shall be paid to the corporation. That determination may be enforced as if it were a decree for payment of money passed in a suit by a civil court

- **Section 44** of the Code seeks to make provisions for scheme for other beneficiaries and other members of their family for providing medical facility in any hospital established by the corporation in any area which is [underutilized](#), on payment of [user charges](#), and the [terms](#) and conditions for the operation of the scheme shall be in accordance with the rules that's been made by the Central Government. The term "Other Beneficiaries" means persons other than employees insured under Section 28. Central government may by notification frame, amend, vary or rescind scheme for other beneficiaries
- **Section 45** of the Act seeks to provide for schemes for unorganized workers, [gig](#) workers and [platform](#) workers. The Central Government may, in consultation with the corporation and by notification, frame scheme for unorganized workers, gig workers and platform workers and the members of their families for providing benefits admissible under Chapter IV by the Corporation. The Contribution, user charges, scale of benefits, qualifying and eligibility conditions and other Terms and Conditions should be specified in the scheme.
- **Section 46** provide for exemption of factories or other establishments belonging to Government or any local authority. The appropriate Government may, after consultation with the corporation, by notification and subject to certain conditions as may be specified in the notification, exempt any factory or other establishment belonging to local authority, from the operation of Chapter IV, if the employees in any such factory or other establishment are otherwise **in receipt of benefits substantially similar or superior to the benefits provided under Chapter IV**
- **Section 47**, provides for contributions, etc., due to corporation to have priority over other debts. Any amount due under Chapter IV relating to ESI shall be the first charge on the assets of the Establishment to which it relates and shall be paid in priority in accordance with the provisions of the IBC, 2016. **Rani K. Lulla vs. Employees' State Insurance Corporation, Chennai. 2011 LLR 289** (Mad. HC), The Madras High court in this regard held that, for recovery of ESI dues, the personal property of a former Director of a Company cannot be attached.
- **Section 48** of the Code seeks to provide for Constitution of Employee's Insurance Court by State Government notification. Employee's Insurance Court shall consist of such

Number of Judges as the State Government may think fit. Any person who is or has been a Judicial Officer, Legal Practitioner of five years standing- shall be qualified to be a Judge of Employee's Insurance Court. State Government may appoint the same court for 2 or more local areas or two or more courts for the same local area. Government may regulate the distribution of business between them, when more than 1 EIC has been appointed for the same local area.

➤ **Section 49** of the Code seeks to specify the matters which shall be decided by Employee's Insurance Court. It further seeks to oust the Jurisdiction of Civil courts to decide or deal with any question or dispute so specified or to adjudicate on any liability which by or under the Act relating to this Chapter IV

- a) Whether any person is an employee within the meaning of the Code – and liable to pay Employee's Contribution
- b) The rates of wages or average daily wages of an Employee, the rate of Contribution made by an Employer, The person who is or was the employer in respect of any employee, the right of any person to any benefit under this chapter and as to the amount and duration,
- c) Relating to this chapter – disputes between Employer and Corporation, Employer and a Contractor, Person and a Corporation – also between Employer, Employee and a Contractor in respect of any Contribution or benefit or other dues payable or recoverable under this Code.
- d) Claim for the recovery of contributions from the ER under this code relating to this Chapter.
- e) Claim under [Section 41 \(8\)](#) – Recovery of the value or amount of the benefits received by a person when he is not lawfully entitled.
- f) Claim against an Employer u/s. 42 (Corporation rights when an employer fails to register)
- g) Order of the appellate authority under section 126 in respect of Chapter IV
- h) No matter which is in dispute between an Employer and Corporation, contribution or any other dues shall be raised by the Employer in the EIC unless he has deposited with that court 50% of the amount due from him as claimed by the Corporation. (Proviso clause states that, EIC for reasons to be recorded in writing- waive or reduce the amount to be deposited)

- **Section 50** of the Code seeks to provide that the Employee's Insurance Court shall have all the powers of a Civil Court for the purposes specified in sub-clause (1). Like summoning and attendance of witness, discovery and production of documents and material objects, oath and recording evidence- orders enforceable as of a civil court's decree.
- **Section 51** of the Code seeks to provide that the manner of commencement of proceedings before that court, the fees and procedure thereof shall be such as may be provided by rules by the State Government. Limitation for initiating the proceedings by the aggrieved person in EI Court **shall be 3 years** from the date on which the cause of action arises.
- **Section 52** of the SS Code 2020, provides for appeals to the HC from orders of Employee's Insurance Courts if it involves a Substantial Question of Law. Appeal shall be filed within a period of 60 days. Provisions 5 to 12 of the Limitation Act, 1963 applies to appeals under this section.
- **Section 133** deals with the Offences and Penalty for failure to pay contributions, etc. The Minimum sentence is 1 year up to a maximum of 3 years, and an enhanced fine of 1 lakh rupees (Section 85 of the ESIA -1948, previously- 10,000 Rs.).
- Section 133 of the Act seeks to provide penalty for failure to pay contributions, etc., that is in consonance with the gravity of the offences.
- Subsequent offence in this regard, **Section 134** provides with enhanced punishment of minimum 2 years and a fine of 3 lakh rupees.

## CASE LAWS

- ❖ **The Madras High Court in Regional Director, ESI Corporation v. Sundaram Clayton Ltd. and Management of Oriental Hotels Ltd., Chennai v. Employees' State Insurance Corporation**, Chennai held that an amount paid for employees to commute to and from work, paid under the heads of conveyance or travel allowance, is excluded from the definition under wages.
- ❖ This was affirmed by the Kerala High Court in Regional Director, **ESI Corporation, Thrissur v. Royal Plastics Industries, Aluva**
- ❖ Karnataka High Court in **Regional Director, Employees State Insurance Corporation v. M/s IT Solutions (India) Private Limited** held that the value of Conveyance Allowance cannot be excluded from the definition of 'wages'. The reasoning of the Karnataka High Court that Conveyance Allowance cannot be excluded from the definition of 'wages' was because Conveyance Allowance is paid every month to every employee like House Rent Allowance, in terms of the contract of employment, so as to meet to and for conveyance expenses, whereas travelling allowance is paid to the concerned employee when he or she is sent out of the station on duty to meet travelling expenses.

- ❖ This Controversy was finally put to rest by the Supreme Court in **ESI Vs. M/S. Texmo Industries (2021)** by affirming the Madras High Court's judgment and holding that conveyance allowance is not a part of wages as defined in **section 2(22) of the ESI Act 1948. Section 2 (88) (d) in the SS Code 2020** excludes conveyance allowance from the purview of wages. So, these kind of Interpretation on the provisions largely creates lack of predictability and uncertainty and it perplexes the intention of the Legislation per se. The uniform definition of wages under the Codes will, hopefully, put an end to the need for judicial intervention and interpretation. The definition is not without its own share of confusion but at least it is uniform and any judicial precedent will apply equally across all Codes.
- ❖ When employees of two units working in the same premises having functional integrality with common electricity connection, both the units will be treated one for the coverage under ESI Act. **Regional Director, Employees' State Insurance Corporation Ltd., Chennai vs. M/s. Ambika Offset. 2011 LLR 726 (Mad. HC)**
- ❖ Waiver of deposit of 50% of the amount as challenged in a petition under section 75 of the ESI Act rightly denied since no extraordinary circumstances have been made out from the petitioner. **M/s. Aakavi Spinning Mills Pvt. Ltd., Melasubrayapuram vs. Employees' State Insurance Corporation, Pondicherry. 2011 Lab. IC 3098 (Mad. HC)**
- ❖ An employee insured under the ESI Act can't claim 'compensation' under the Employee Compensation Act – **Abad Fisheries v. Commissioner for Employee Compensation, (1985) 50 FLR 512.**
- ❖ Insurance court can't travel beyond the parameters in extending the ESI Act – **ESIC, Orissa Region v. Gujarat Co-operative Milk Marketing Federation Ltd., 2009 LLR 615 (Ori HC).**
- ❖ An insured employee can't claim "disablement benefit" from the Employee's Insurance Court without first approaching the E.S.I.C. **Radhey Shyam v. ESIC (1989) 58 FLR 133 (MP).**
- ❖ Exempting persons or class of persons from coverage under ESI Act shouldn't be in a technical manner hence an employer, seeking exemption under ESI Act, has to prove that medical facilities and other benefits as extended to employees are better than those under the ESI Act – **Lark Laboratories (India) Ltd. v. Govt. of NCT, Delhi, 2006 LLR 1093: 2007 (1) LLJ 72 (Del HC)**

## DIRECTIONS & RECOMMENDATIONS

1. In its provisions the code falls short of safeguarding the interests of unorganized sector workers and articulates a framework of social security that is dependent on the goodwill of the corporates.

2. The reality is that the labour enforcement machinery has been ineffective because of poor enforcement, inadequate penalties, and corruption of the inspectors. How the changes in legislation will address these concerns is a true concern laid before us.
3. In a larger context there is no substantial change in the provisions of SS Code and the prior legislations except with that of the wage ceiling, threshold limit and few of key changes mentioned earlier.

