

## Client Alert

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## Exception to Implementation of Cost-Cutting Measures by Employers: Retrenchment

Following the Restriction of Movement Order ("**the Order**") which was first announced by the Malaysian Prime Minister on 16 March 2020, the Prime Minister subsequently extended the period of the Order on 25 March 2020 as a continued effort to curb the outbreak of the coronavirus ("**COVID-19**"). This has resulted in a prolonged state of partial lockdown in Malaysia from two (2) to four (4) weeks, which in effect would last from 18 March 2020 to 14 April 2020 ("**Period**"). There is also the likelihood that the Period may be further extended.

The Order which necessitates the closure of all businesses except essential services and imposes travel restrictions nationwide, has caused severe financial stress on businesses especially those in industries such as tourism, travel, aviation, retail and construction.

Moving forward in an unprecedented crisis like this, businesses are advised not to unilaterally implement employee related cost-cutting measures to sustain their operations. Are there any exceptions?

This alert examines those exceptions and sets out some best practices on retrenchment exercises.

### Cost-Cutting Measures

The natural options which an employer might consider in reducing his/her cost of operation include (i) reducing the employee's salary; (ii) asking employees to take unpaid leaves and/or (iii) utilising annual leave ("**Cost Cutting Measures**") especially for employees who are unable to discharge any form of work during the Period.

However, the Ministry of Human Resources ("**Ministry**") has made it clear through its FAQs dated **19 March 2020**, **23 March 2020** and **31 March 2020** that these Cost Cutting Measures are not allowed. Therefore, employers are obliged to pay the full salaries to its employees during the Period.

Employers who flout this obligation may open themselves to risk of statutory fines, or even the possibility of employees claiming constructive dismissal. The exception is that these Cost Cutting Measures are done with the mutual agreement of the employees or that they are implemented as a means to avoid Retrenchment. Assuming that mutual agreement is not possible, could a Retrenchment exercise be a viable option? Are employers permitted to lay-off employees as of right?

### Retrenchment

Retrenchment is a reduction of employees due to a surplus of workforce for reasons including economic recession. It is generally an employer's prerogative right to carry out such an exercise. However, such an exercise is subject to compliance with Malaysian industrial practice standards. Otherwise, an employer



may be exposed to potential claims of unlawful termination, which if found to be the case, may carry financial exposure of a maximum of 24 months + 1 month for each year of service for the affected employees last drawn salary.

### **How to minimise the legal risks when implementing retrenchment?**

When carrying out retrenchment, there are two key factors which have to be satisfied in order to minimise the risk of unfair dismissal claims:

#### **(a) Substantive business grounds**

- (i) The reason for retrenchment must be bona fide. If a business is financially impacted by the COVID-19 pandemic, this will likely be a genuine ground.
- (ii) To this end, the employer must ensure there are documents to support the claim of financial losses caused by the pandemic. The paper trail from the time a decision is made, internal discussions and minutes, employee evaluations and all correspondence ought to be retained as evidence.

#### **(b) Fair manner of implementation**

- (i) The employer must ensure that prior steps have been taken to avoid the retrenchment. The steps suggested by the Ministry include reducing working hours, limiting hiring of new employees, restricting overtime, limiting work on weekly rest days and public holidays, reducing the employees' salaries and laying off. Such practices must be consistent throughout the organisations and no single employee or group of employees should be singled out.
- (ii) If the redundancies are inevitable, the employers must terminate foreign employees first.
- (iii) For terminations involving local employees, the principle of last in first out must be followed unless the employer has strong justification not to do so.
- (iv) The general compliance with the Code of Conduct for Industrial Harmony.

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### **Conclusion**

The Industrial Court of Malaysia is fairly protective of employees. In cases where a retrenchment exercise is not carried out properly, it could potentially amount to claims of unlawful dismissal. In such a circumstance, an order for reinstatement may be made or a financial exposure of a maximum of 24 months of back wages + 1 month of salary for each completed year of service could be ordered.

Given the significant financial exposure, it is best for organisations to seek for legal advice prior to the implementation of a retrenchment exercise.

