

Important points for Gratuity and Leave encashment actuarial valuation arising from the New Labour Codes:

1. What is the definition of wages?

Reference – The Definition of wages at point (88) on Page 12 in The Code of Social Security, 2020

Extract from the code –

"wages" means all remuneration, whether by way of salaries, allowances or otherwise, expressed in terms of money or capable of being so expressed which would, if the terms of employment, express or implied, were fulfilled, be payable to a person employed in respect of his employment or of work done in such employment, and includes, —

(a) basic pay;

(b) dearness allowance; and

(c) retaining allowance, if any,

but does not include— (a) any bonus payable under any law for the time being in force, which does not form part of the remuneration payable under the terms of employment;

(b) the value of any house-accommodation, or of the supply of light, water, medical attendance or other amenity or of any service excluded from the computation of wages by a general or special order of the appropriate Government;

(c) any contribution paid by the employer to any pension or provident fund, and the interest which may have accrued thereon;

(d) any conveyance allowance or the value of any travelling concession;

(e) any sum paid to the employed person to defray special expenses entailed on him by the nature of his employment;

(f) house rent allowance;

(g) remuneration payable under any award or settlement between the parties or order of a court or Tribunal;

(h) any overtime allowance;

(i) any commission payable to the employee;

(j) any gratuity payable on the termination of employment;

(k) any retrenchment compensation or other retirement benefit payable to the employee or any ex gratia payment made to him on the termination of employment, under any law for the time being in force:

Provided that for calculating the wages under this clause, if payments made by the employer to the employee under sub-clauses (a) to (i) exceeds one-half, or such other per cent. as may be notified by the Central Government, of the all remuneration calculated under this clause, the amount which exceeds such one-half, or the per cent. so notified, shall be deemed as remuneration and shall be accordingly added in wages under this clause: Provided further that

for the purpose of equal wages to all genders and for the purpose of payment of wages, the emoluments specified in sub-clauses (d), (f), (g) and (h) shall be taken for computation of wage.

Interpretation –

The new Labour Codes have subsumed the Payment of Gratuity Act, 1972 and they require gratuity payment to all employees to be calculated based on last drawn wages which should be minimum 50% of total remuneration.

These codes establish a standardized framework where the core components of "wages" must primarily include Basic Pay, Dearness Allowance (DA), Retaining Allowance (If any), and Special Allowance. To arrive at the legally approved wage figure, employers must systematically exclude the specific components listed from point (a) to (k) from an employee's total remuneration to arrive at "wages".

A significant statement in this definition states that if these exclusions (a) to (i) collectively exceed 50% of the total remuneration, the excess amount must be added back to the "wages" for statutory calculations.

2. How special allowance treated in wage definition? Is it part of wages?

Reference –

The Definition of wages at point (88) in The Code of Social Security, 2020

Extract from the code –

Same as for Question 1

Interpretation –

In most modern corporate salary structures, "Special Allowance" constitutes a substantial portion of an employee's total pay. Since the term "Special Allowance" is not explicitly mentioned in the list of statutory exclusions (a) to (k), it logically follows that this component should be treated as a part of the core "wages" for the purpose of benefit calculations. However, if a company chooses to define this allowance in a way that aligns it with one of the specific exclusions permitted under the Act, they may legally remove it from the wage definition.

Some common components of Salary

	Component	Included in wage?	Excluded from wage?	Considered in total remuneration
	Basic pay	Yes	No	Yes
	Dearness Allowance	Yes	No	Yes
	Retaining Allowance	Yes	No	Yes
(a)	Any bonus payable under any law, which does not form part of remuneration payable under terms of employment (Statutory Bonus)	No	Yes	Yes
(b)	Value of any house-accommodation, or of the supply of light, water, medical attendance or other amenity	No	Yes	Yes
(c)	Any contribution paid by the employer to any pension or provident fund, and the interest which may have accrued thereon	No	Yes	Yes
(d)	Any conveyance allowance or the value of any travelling concession	No	Yes	Yes
(e)	Any sum paid to defray special expenses entailed by nature of employment	No	Yes	Yes
(f)	House Rent Allowance	No	Yes	Yes
(g)	Remuneration payable under award / settlement / order of court or Tribunal	No	Yes	Yes
(h)	Any overtime allowance	No	Yes	Yes
(i)	Any commission payable to the employee	No	Yes	Yes
(j)	Any gratuity payable on the termination of employment	No	Yes	No
(k)	Any retrenchment compensation or other retirement benefit payable to employee or any ex-gratia payment made on termination of employment, under any law for the time being in force.	No	Yes	No
Components NOT LISTED in the definition				
	Special Allowances (Include all allowances which are not part of above components from (a) to (i))	Yes	No	Yes
	Variable Bonus/ Performance Bonus	No	Yes	No
	Reimbursements for books and magazines, Food Coupons, Travel, Entertainment, Broadband, mobile phone	No	Yes	No
	ESOP	No	Yes	No
	Leave Travel Allowance (Reimbursements type)	No	Yes	Yes
	Leave Travel Allowances (Fixed % for all employees)	Yes	No	Yes

Common Scenarios of Salary Structure

Scenario 1: If your Wages before Implementation of New Labour codes is already 50% of Total Remuneration but you have other components like Special Allowances which is not mentioned in the excluded category, they will be treated as a part of wages and be added to your wages.

Salary Components	Per Month
Basic	40,000
DA	10,000
HRA	20,000
Conveyance Allowance	10,000
Special Allowances	20,000
Total Remuneration	1,00,000

Scenario 1	Pre Implementation	Post Implementation
Wages For gratuity	50,000	70,000
Component of Salary Included	Basic + DA	Basic + DA + Special Allowances
Ratio of Wages/Total Remuneration	$50,000/1,00,000 = 50\%$	$70,000/1,00,000 = 70\%$

Scenario 2: If Your Wages before Implementation of New Labour codes is not 50% of Total Remuneration then excess allowances over 50% will be added back to the wages.

Salary Components	Per Month
Basic	35,000
DA	10,000
HRA	35,000
Conveyance Allowance	20,000
Special Allowances	0
Total Remuneration	1,00,000

Scenario 2	Pre Implementation	Post Implementation
Wages for Gratuity	45,000	50,000*
Component of Salary Included	Basic + DA	Deemed Wages
Ratio of Wages/Total Remuneration	$45,000/1,00,000 = 45\%$	$50,000/1,00,000 = 50\%$

* As your wages should be minimum 50% of Total Remuneration and Excess Allowances over the 50% should be added back to the wages.