



## **From Chaos to Clarity: India's New Compensation Law**

**Employment and Labor**



## CHEAT SHEET

- **The Code.** The Code of Wages (Code) in India amends and consolidates labor laws relating to wages and bonuses. It has been approved in parliament but has not yet been given an effective date.
- **Employee perspective.** The Code has been welcomed by employees and been perceived as a positive step in labor reform, in that it addresses gender-based disparity and the fair and timely payment of wages and settlements.
- **Compliance relief.** The Code offers compliance relief for employers, combining multiple registers into a single one and digitalizing inspection processes.
- **Offenses.** While the penalties are steep for non-compliance, employers have the opportunity to rectify certain offenses and will not be prosecuted if they do so in an identified period of time.

On Aug. 8, 2019, the Ministry of Law and Justice in India formally announced its Code of Wages (Code), which amended and consolidated labor laws relating to wages, bonus, and similar matters that are applicable to all workers in India. The Code repeals the 1936 Payment of Wages Act (PWA),

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the 1948 Minimum Wages Act (MWA), the 1965 Payment of Bonus Act (PBA), and the 1976 Equal Remuneration Act (ERA).

Within hours of the Code being notified, the employment teams of companies doing business in India got busy researching the potential implications. My manager requested I prepare a presentation for our legal team and other relevant internal stakeholders, such as the human resources and compensation and benefits teams, on the key features of this Code.

This article will discuss the history and coverage; salient features that affect employers and employees; and enforcement reforms, including the offenses and penalties.

## **History and coverage**

The Second National Commission on Labour (NCL), established on October 15, 1999, recommended that the existing labor laws should be classified into broader groups for easier compliance. Some of the draft codes have been discussed and deliberated upon for the past several years, but none of them were ultimately put into effect. As a part of the labor reforms initiatives undertaken by the Central Ministry of Labour and Employment, steps are actively being taken to amalgamate, simplify, and rationalize the 38 labor laws into four codes. The laws have been broadly categorized into four categories: (1) wages; (2) industrial relations; (3) social security and welfare; and (4) safety and working conditions. Among these 38 laws, at least 17 are over 50 years old, and a few of them even date back to the pre-independence era. This Code is the first of four proposed codes that has been successfully approved by the Parliament of India but its effective date has not yet been announced by the central government. Although the 2019 Code on Occupation Health, Safety, and Working Conditions was simultaneously introduced in the Indian Parliament, it has not yet passed.

## **Salient features**

### **Wage ceilings based on sector abolished**

The scope and applicability of the benefits that were available under PWA and MWA have been expanded considerably under the new Code.

While the PWA applies to employees who draw a salary below the statutory stipulated limit, the Code will apply to all employees irrespective of the wage ceiling. Currently, the MWA lists the occupations where employers are required to pay minimum wages to workers. The MWA applies to the organized sectors like IT, pharma, medicine, as well as certain workers in unorganized sectors, such as agricultural workers. The central and state governments may add more occupations to this list and mandate that minimum wages be paid for those occupations as well. At present, there are more than 1,700 occupations identified by the central and state governments. The Code proposes to do away with the concept of bringing specific occupations under the MWA and instead mandates that minimum wages be paid for all types of employment — irrespective of whether they are in the organized or the unorganized sector.

### **Wage redefined under the Code**

Previously, there were 12 definitions of wages in various labor laws, which often lead to litigation in addition to difficult implementation. The Code proposes a common definition of wages, which will enable employers to take a consistent and uniform approach and avoid multiple interpretations.

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The definition of wages includes basic pay; dearness allowance (a cost of living adjustment allowance paid to government and public sector employees and pensioners in India to mitigate inflation); and retaining allowance (an allowance paid by an employer to retain employee). The Code excludes the following components from the definition of wages:

- a. Bonus payments;
- b. Value of the house/accommodation, supply of light, water, medical attendance or other amenity or of any service excluded from the computation of wages by an order of the appropriate government;
- c. Employer contributions to any pension or provident fund;
- d. Conveyance allowances (a type of allowance offered to employees for travel to and from the workplace);
- e. Sums paid to the employee to defray special expenses on him by the nature of his employment;
- f. House rent allowance;
- g. Remuneration payable under award or settlement between the parties or order of court or tribunal;
- h. Overtime allowance;
- i. Commission payable to employee;
- j. Gratuity payments (a lump sum that an employer with more than 10 employees pays to the employees who have completed a minimum of five years of full-time service with the employer, which means a minimum of 240 days a year); and,
- k. Retrenchment compensation or other separation benefits payable to the employee or any ex-gratia payment made to the employee on the termination of his employment.

Notwithstanding the above, it is important to note that the Code introduces a special methodology for computation of wages and, in certain circumstances, various components of wages that are ordinarily understood to be excluded.

For example, for the purpose of equal wages to all genders, and for the purpose of payment of wages, the emoluments specified in clauses (d), (f), (g), and (h) (specified above), shall also be considered for computation of wages.

The Code further prescribes that if the sum-total of the excluded components (apart from gratuity and retrenchment compensation) exceeds 50 percent (or such other percent as notified by the central government) of the total remuneration, then that portion of the amount exceeding 50 percent (or such other percent as notified by the central government) shall also be calculated as wages under the Code. This is a unique provision and is seemingly aimed at compensation structures where wages are less than 50 percent of the total remuneration of the employee. This provision could result in situations where the wage of an employee must be recalculated. For example, if the aggregate of commission/ sales incentive, house rent allowance, and overtime exceeds 50 percent of the monthly salary for that particular month, there could be a possibility of re-computation of wages.

In these situations where the wage could fluctuate, computation of bonus under the Code or payment of wages for overtime work, would also fluctuate and be impacted. Additionally, this could potentially have a knock-on impact if the proposed labor code on social security relies on the given definition of wages under this Code; in which case any pay-outs/contributions (like gratuity, provident fund, retrenchment compensation) that are linked to wages would also fluctuate.

These changes have increased the work of the compensation and benefits team and have a significant impact on the employers who now are very careful in devising the salary structure of the employees due to these fluctuating and variable parts.

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## **Floor wages introduced for consistency**

The Code introduces a new concept of “floor wages,” which aims to bring consistency across geographies and different state governments and employers across India. The introduction of floor wages has been welcomed by the employees. These rates will be fixed by the central government, accounting for the minimum living standards of a worker. While the floor wage will be fixed by the central government, the minimum wages may differ from state to state. However, in no case, the minimum wage fixed by any state government shall be less than the floor wage. It can, however, be higher than the floor wage. The minimum rates of wages fixed by the state government cannot be less than floor wages as determined by the central government. However, if the existing minimum wages fixed by the appropriate government is higher than the floor wage, they cannot reduce the minimum wages. It is also necessary to note that the Code prescribes that the minimum rate of wages is to be reviewed and revised by the appropriate government in intervals not exceeding five years.

## **Employers must comply with time limit for payment of wages**

The Code has brought several changes in terms of time limit for payment of wages, which means that now employers must expeditiously process full and final (F and F) settlements for their exiting employees.

Under the present PWA, the employer can pay wages to their employees within 10 days after expiration of the wage-period if the employer has more than 1,000 employees. This will change once the Code comes into effect.

The Code proposes to make it mandatory for the employer to pay within seven days from expiration of the wage period, irrespective of the size of the company. The Code also mandates payment of wages within a period of two working days, from the date of the employee’s removal, dismissal, retrenchment, or resignation from employment. While the current PWA has a similar provision for payment of wages within two days from the date of termination of his employment, payment of wages on account of voluntary resignation by employees has been brought within the same time limits.

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## **Employers empowered to choose the “mode” of payment of wages**

The Code now requires the employers to choose the mode of payment of wages in either coins; currency notes; by check; by crediting to the bank account; or through electronic means. Employers can fix the wage period as either: daily, weekly, fortnightly, or monthly. The Code empowers the employer to deduct an employee’s wages on certain grounds including fines; absence from duty; accommodation given by the employer; or recovery of advances given to the employee, among others. These deductions should however not exceed 50 percent of the employee’s total wage.

## **Another item added to the list of disqualifications for bonus entitlement**

To ensure fair working conditions, the Code has added to the already existing list of disqualifications

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(as set forth in the payment of bonus act), for receiving a bonus. It provides that dismissal from service due to conviction for sexual harassment would also be considered grounds for not receiving a bonus.

Further, the Code goes a step ahead and prohibits gender discrimination in matters related to wages and recruitment of employees for the same work or work of similar nature.

## **Amalgamation of existing “overtime rates” and abolition of gender discrimination**

The Code has amalgamated the applicable overtime rate across board and prescribes that such rate will not be less than twice the normal rate of wages.

The Code inter-alia includes provision prohibiting the discrimination on grounds of gender (1) with respect to wages by employers, with respect to same work or work of a similar nature done by employees and (2) with respect to recruitment of employees for same work or work of a similar nature. This is a huge welcome by female employees across India as statistics so far show that female employees earn roughly 45 percent less than male employees in the same occupation.

Further, the Code goes a step ahead and prohibits gender discrimination in matters related to wages and recruitment of employees for the same work or work of similar nature. Work of similar nature is defined as work for which the skill, effort, experience, and responsibility required are the same.

## **Compliance relief for employers**

The Code consolidates the requirement of multiple registers under PWA, MWA, and PBA and provides for a single register containing details regarding persons employed, muster roll, wages, etc. This will lead to easing out periodical compliances (administrative filing requirements) for employers under current laws and is a great welcome by the employers. The form of the register is yet to be prescribed.

Further, the “inspector” under the previous regime has been replaced with an “inspector-cum-facilitator,” who has additional duties of guiding and advising employers and employees on effective implementation. Inspections are now possible through a web-based inspection scheme and electronic summoning of information, which may ease compliance burdens for employers, and be in sync with current trends towards digitalization.

## **Enforcement reforms: Offenses and penalties**

The Code contemplates three kinds of contraventions: (1) payment of an amount that is less than the amount due to the employee under the Code; (2) non-maintenance or improper maintenance of records under the Code; and (3) any other contravention of the Code.<sup>4</sup>

Where an employee has been paid an amount that is lesser than the amount due to the employee under the Code, the employer is punishable with a fine of INR 50,000 for the first violation. If the employer is again convicted for a similar offense within five years from the date of commission of the first offense, then after the subsequent offense the employer shall be punishable with imprisonment for a term of three months or a fine of up to INR 1,00,000 or both.

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Once, the Code comes into effect, it will be interesting to see how the above penalties are imposed on the employers through audit findings and annual inspections done by the labor department of the concerned state government. It will also be interesting to see if the penalty amounts will be reimbursed to the employees who had been underpaid or if the government keep the penalty amounts. Including imprisonment of employer seeks to increase the burden on the board of directors of the employers to ensure that the compliances set forth in the Code are strictly followed.

The employers are required to maintain proper records and preserve them for a minimum period of three years. For not maintaining proper records, the employer is punishable with a fine of up to INR 10,000.

For any other contravention, the employer is punishable with a fine of INR 20,000 for the first offense. If the employer is again convicted for a similar offense within five years from the date of commission of the first offense, then on such second or subsequent offense the employer shall be punishable with imprisonment for a term that may extend to one month or with a fine of up to INR 40,000 or both.

The Code allows the employer to be given an opportunity to cure his or her first-time contravention of certain provisions of the Code (e.g., offenses other than payment of amounts lesser than amounts due under the Code). In such cases, the Code prescribes that the inspector–cum–facilitator shall give an opportunity to the employer to comply with the Code within the identified time period and, if complied with, no prosecution shall be initiated. No such opportunity to cure a breach of the Code shall be granted if a violation of similar nature is repeated within five years from the date of first violation and prosecution shall be initiated right away.

The Code also provides for an ability to compound offenses under the Code, at any time before or after initiation of the prosecution. Offenses under the Code can be compounded for a sum of 50 percent of the maximum fine prescribed. However, once compounded, another compounding will not be permitted within a period of five years of the commission of a similar offense that was earlier compounded.

Hence, penalties for non-compliances have now been substantially enhanced by the Code, which may foster a compliance culture by acting as a deterrent. Additionally, providing for compounding of offenses may lead to greater enforcement. Finally, the Code clearly prescribes the burden of proof in case of claims of non-payment or deficient payment of wages or bonus to be on the employer.

## **Employee-friendly provisions**

The Code has introduced some interesting provisions that are employee friendly. Where a claim has been filed on account of non-payment of remuneration or bonus or less payment of wages or bonus or on account of making deductions not authorized by this Code from the wages of an employee, the burden of proof falls on the employer to show that wages had been paid. Further, any contract or agreement whereby an employee relinquishes the right to any amount or the right to bonus due to him under the Code shall be null and void in so far as it purports to remove or reduce the liability of any person to pay such amount under the Code. Lastly, the provisions of the Code shall supersede over any inconsistent provision in any other law, act, award or agreement, or contract or service entered by and between employer and employee. This indicates that the obligations set forth by the Code cannot be negotiated away by the employer.

Gone are the days when employers could take it easy on nonpayment of overtime wages as shops and establishments laws hardly provided a deterrent with a paltry fine.

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## A step toward labor reform

The Code has been welcomed by employees across India by addressing issues of gender-based disparity, ensuring fair and timely payment of wages and settlement post termination/resignation. The Code is seen as a definite positive step toward labor reform and was long awaited. However, it awaits the test of time for its true merit.

On one hand, the Code emphasizes compliance as it increases the cost of non-compliance. Gone are the days when employers could take it easy on nonpayment of overtime wages as shops and establishments laws hardly provided a deterrent with a paltry fine. At the same time, diligent employers who are willing to comply with the Code get an opportunity to compound the offense. Prior to the Code, only some states had introduced provisions for compounding offenses. The Code makes this opportunity to compound uniformly available and is a step forward in the direction of ease-of-business. In some cases, the Code also provides an opportunity to rectify breach and in which case employers need not worry about prosecution. Further, the Code's provisions appear to be exhaustive, and only the test of time will tell whether the changes introduced by the Code will achieve its objectives and solve the concerns that it purports to address.

## References

Clause 6 of the Code.

Annual Report, PLFS 2017-18 (2019), Periodic Labour Force Survey (PLFS), National Statistical Office, Ministry of Statistics and Programme Implementation, Government of India.

Clause 3 and 14 of the Code.

Chapter 8 of the Code.

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