

FINANCIAL IMPLICATIONS OF

# NEW LABOUR CODES

Effective from: 21 November 2025

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**CA PANKAJ KUMAR TRIVEDI**

**TRIVEDI & BANG, CHARTERED ACCOUNTANTS**

**Hyderabad Branch of SIRC of ICAI**

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# Disclaimer

**Personal Opinions:** The views and opinions expressed in this presentation are my personal views as a practitioner. They should not be construed as opinions or official positions of ICAI, any regulatory body or any employer.

**Evolving Area of Law:** The New Labour Codes are a new and evolving area of law. Rules and clarifications are still being notified. I acknowledge that there may be equally valid alternative interpretations of certain provisions, and I respect those opinions.

**Not Legal Advice:** This presentation is for educational purposes only. It does not constitute legal advice. Specific situations should be evaluated with qualified legal counsel.

**For Finance & CA Professionals:** This session is designed from the lens of a Chartered Accountant dealing with payroll, financial reporting, and tax compliance.

# The Four Labour Codes — An Overview

*29 Central labour laws consolidated into 4 comprehensive codes | Effective: 21 November 2025*

1

## Code on Wages, 2019

*4 laws consolidated*

Minimum Wages Act • Payment of Wages Act  
Payment of Bonus Act • Equal Remuneration Act

2

## Industrial Relations Code, 2020

*3 laws consolidated*

Trade Unions Act  
Industrial Employment (Standing Orders) Act  
Industrial Disputes Act

3

## Code on Social Security, 2020

*9 laws consolidated*

EPF Act • ESI Act • Gratuity Act  
Maternity Benefit Act • EDLI & others

4

## OSH & Working Conditions Code, 2020

*13 laws consolidated*

Factories Act • Mines Act  
Contract Labour Act & 10 other laws

*State governments may supplement/modify central framework. State-specific Shops & Establishments Acts continue to apply.*

# Appointment Letters — Now Mandatory

## What the Law Requires

Every employer **must issue a letter of appointment in prescribed form** to every employee. Existing employees who had not received one must be issued within **3 months of Code commencement (i.e., by 20 February 2026)**.

## Who is Covered? — 'Establishment'

As per COW, Establishment is any place where trade, business, manufacture or occupation is carried on — including Government establishments..

For OSH, additionally, establishment is where 10 or more workers are employed.

## CA's Action Point

Audit whether all your clients have issued appointment letters in prescribed format to all employees — including contractual and fixed-term staff. This is a quick compliance win with material penalty exposure if missed.

## PENALTY (Section 111)

### First Offence

Fine up to ₹2,00,000

### Subsequent Offence

Fine up to ₹3,00,000

+

Additional ₹2,000/day for continuing contravention

# Payment of Wages — Timelines & Key Changes

## Section 17 | Code on Wages, 2019

**Daily Wage**

→ End of shift on the same day

**Weekly Wage**


→ Last working day of the week (before weekly holiday)

**Fortnightly Wage**

→ Before end of 2nd day after the fortnight ends

**Monthly Wage**

→ Before expiry of 7th day of the following month

 **Key Rule:** Monthly wages must be paid before the **7th of the following month**. Delayed payment triggers penalty under Section 54. Ensure payroll processes are front-loaded.

# Wages on Separation & Mode of Payment

Section 17(2) & Section 15 | Code on Wages, 2019

## Wages on Separation

Section 17(2) | Code on Wages, 2019

### Wages within 2 Working Days

Applies to all cases of separation:

Removed • Dismissed • Retrenched  
Resigned • Closure of establishment

**New Law**  
Uniform 2 days for ALL

## Mode of Payment of Wages

Section 15 — now explicitly permits:

 Coin or Currency Notes (Cash)

 Cheque (with employee consent)

 Direct Bank Transfer / NEFT

*Old law (Sec 6, Payment of Wages Act) did not permit direct bank transfers — now explicitly allowed under new Code.*

 **Mode of Payment of Bonus**

Section 39 | Code on Wages, 2019

Bonus must be paid by **crediting to the employee's bank account.**

# Penalties for Non-Compliance with Wage Timelines

Section 54 | Code on Wages, 2019

## First Time Offence

**Fine up to ₹20,000**

## Repeat Offence (within 5 years)

**Imprisonment up to 1 month OR Fine up to ₹40,000  
OR Both**

### KEY PROVISIONS & CA IMPLICATIONS

#### ✓ Compounding of Offences (New)

Employers may settle wage violations by compounding (paying a prescribed amount) without undergoing prosecution. Encourages voluntary compliance before legal proceedings begin.

#### 📄 Improvement Notices (New)

Inspectors may issue improvement notices giving employers an opportunity to rectify violations before prosecution. Key compliance tool under the new framework.

**CA Action Point:** Ensure payroll is disbursed by the 7th of each month. For client separations, set up a standing process for same-day/next-day full-and-final settlement. Repeat violations carry imprisonment risk — do not treat this as a minor compliance item.

# Permissible Deductions from Wages

*Section 18 | Code on Wages, 2019*

## **Fines**

For acts/omissions specified in disciplinary rules or contract

## **Absence from Duty**

Proportionate deduction for days actually absent

## **Accommodation & Amenities**

Rent, utilities, subsidised canteen provided by employer

## **Advances & Recovery**

Travel advance, bonus advance, or any contractual advance

## **Statutory Deductions**

*Income Tax (TDS), Employee PF, Employee ESI, Professional Tax*

## **Court Orders / Welfare Fund**

Deductions as per court orders; welfare fund contributions

## **50% CAP on Total Deductions**

Total deductions in any wage period CANNOT exceed 50% of the employee's wages for that period (Section 18).

## **Section 18(4) — Employee Protection**

If employer deducts but does not deposit (e.g., TDS, PF), the employee will NOT be held responsible. Supports claims under Section 205 of Income Tax Act.

# The Redefined Concept of 'Wages'

Section 2(y) | Code on Wages, 2019 — Applicable across all 4 Labour Codes

## ✓ WAGES Includes

- Basic Pay
- Dearness Allowance (DA)
- Retaining Allowance
- Remuneration in kind (up to 15% of total)

## ✗ EXCLUDED FROM WAGES

- Statutory bonus (not forming part of remuneration)
- HRA
- Conveyance/Travel Assistance
- Employer's PF/Pension contribution
- Overtime Allowance
- Commission • Gratuity on termination
- Retrenchment/retirement compensation

## THE CRITICAL 50% RULE

If the total of all excluded components (other than Gratuity and Retrenchment Compensation ) exceeds 50% of total remuneration, the EXCESS shall be deemed as WAGES

## Remuneration in Kind

Value of remuneration in kind up to 15% of total remuneration also forms part of wages.

For equal wages and Payment of Wages purposes — HRA, Conveyance, Special Allowance & Commission are also included in computation of wage.

# The 50% Rule — Illustration When Excess Gets Deemed as Wages

*Scenario: Excluded components exceed 50% threshold — the excess is treated as Wages*

Component	Annual (₹)	Status
Basic Pay	3,00,000	WAGES ✓
House Rent Allowance	2,40,000	Excluded
Conveyance Allowance	90,000	Excluded
Employer PF Contribution	36,000	Excluded
Special Allowance	34,000	WAGES ✓
<b>TOTAL CTC</b>	<b>7,00,000</b>	

**Impact:** Gratuity, leave encashment, will now be computed on higher wage base of ₹3,50,000 instead of ₹3,00,000. Employer liability increases proportionately.

## 50% RULE CHECK

Total Remuneration: ₹7,00,000  
50% Threshold: ₹3,50,000

### Excluded Components:

HRA: ₹2,40,000  
Conveyance: ₹ 90,000  
Employer PF: ₹ 36,000  
**Total Excluded: ₹3,66,000**

 **Excluded ₹3,66,000 > 50% Threshold ₹3,50,000**  
**Excess = ₹16,000 DEEMED as WAGES**

**Total WAGES =**

**₹3,50,000**

(Basic ₹3,00,000 + Spl All ₹ 34,000+Deemed Excess ₹16,000)

# The 50% Rule — Illustration to understand Impact

*How excluded components can be 'deemed' as wages*

Component	Annual Amount (₹)	Status
Basic Pay	4,00,000	WAGES ✓
Dearness Allowance	—	WAGES ✓
House Rent Allowance	1,60,000	Excluded
Conveyance Allowance	60,000	Excluded
Children Education Allow.	36,000	WAGES ✓ (not in exclusion list)
Children Hostel Allow.	60,000	WAGES ✓ (not in exclusion list)
Employer PF Contribution	48,000	Excluded
Special Allowance	2,36,000	WAGES ✓ (not in exclusion list)
<b>TOTAL CTC</b>	<b>10,00,000</b>	

## 50% RULE CHECK

**Total Remuneration** ₹10,00,000

### Excluded Components:

HRA: ₹ 1,60,000

Conveyance: ₹ 60,000

Employer PF: ₹ 48,000

**Total Excluded:** ₹ 2,68,000

**50% Threshold:** ₹5,00,000

**Excluded < 50% ✓**

*No Deeming needed in this case.*

**Total WAGES:** ₹7,32,000

*(Basic + CEA + Hostel + Special)*

# Quantified Impact (One Employee)— Worked Example

CTC of ₹10,00,000 | 6 Years of Service | 25 Days Leave

Component	Before 21-Nov-2025	After 21-Nov-2025	Increase	Impact (% of CTC)
Wage Basis	Basic: ₹4,00,000 p.a.	Wages: ₹7,32,000 p.a.	+₹3,32,000	—
Monthly Wages	₹33,333	₹61,000	+₹27,667	—
Gratuity Liability	₹1,15,383	₹2,11,154	+₹95,771	9.57%
Leave Encashment Liab.	₹27,778	₹50,833	+₹23,055	2.31%
<b>TOTAL LIABILITY</b>	<b>₹1,43,161</b>	<b>₹2,61,987</b>	<b>+₹1,18,826</b>	<b>11.88%</b>

**Key Insight: For every ₹100 of CTC, in this example, the employer's additional annual liability for gratuity + leave encashment alone is approximately ₹11.88.**

# Pay Restructuring to Manage Impact — Section 124 Warning

COSS Section 124 | Code on Social Security, 2020

## ⚠ Section 124 — COSS: Anti-Reduction Clause & Section 40 of IR

No employer shall, by reason only of his liability under this code, directly or indirectly reduce wages or the total quantum of benefits to which an employee is entitled under the terms of employment.

Section 40 of IR code states that no Changes can be made in conditions of Service without giving 21 days notice to Employees

Pay Component	Current Structure	Restructured	Change
Basic Pay	₹4,00,000	₹5,00,000	↑
HRA	₹1,60,000	₹2,50,000	↑
Children Edu. Allow.	₹36,000	₹36,000	—
Children Hostel Allow.	₹60,000	—	↓ Removed
Conveyance Allow.	₹60,000	₹1,20,000	↑
Employer PF	₹48,000	₹60,000	↑
Special Allowance	₹2,36,000	₹34,000	↓↓ Reduced
<b>Total CTC</b>	<b>₹10,00,000</b>	<b>₹10,00,000</b>	<b>Same ✓</b>
<b>Wage Base (Gratuity)</b>	<b>₹7,32,000</b>	<b>₹5,70,000</b>	<b>↓ Reduced</b>
<b>Gratuity Liability</b>	<b>₹2,11,154</b>	<b>₹1,64,424</b>	<b>↓ ₹46,730 saved</b>
<b>Leave Encashment</b>	<b>₹50,833</b>	<b>₹39,583</b>	<b>↓ ₹11,250 saved</b>

# Financial Impact Areas

*Where the New Wage Definition Changes the Numbers*

## Gratuity

Before:  $15/26 \times \text{Monthly Basic} \times \text{Years}$

After:  $15/26 \times \text{Monthly Wages} \times \text{Years}$   
Compulsory Insurance Policy U/s 57 of COSS

**HIGH** — Wage base nearly doubles in many structures

## Leave Encashment

Before: % of Basic Pay

After: Based on Wages  
There is now no provision of Lapse of Earned Leave/Privilege Rules. Employer need to Pay

**HIGH** — Increases payout

## Bonus

Before: Based on Basic Pay

After: Based on Wages

**MEDIUM** — Increases payout

## Provident Fund (EPF)

Before: 12% of Basic + DA

After: Governed by EPF Act (narrow definition of basic wages = Basic + DA only)

**CURRENTLY LOW** — EPF Act definition remains unchanged for now

**⚠️ Priority Alert:** Gratuity and Leave Encashment carry HIGH impact — commission fresh actuarial valuations immediately and recognise incremental liability as past service cost per Ind AS 19 / AS 15.

# Allowances — Key Interpretation Challenges

## *Areas of Uncertainty Under the New Definition of Wages*

### Leave Travel Allowance (LTA)

Exclusion list mentions 'travelling concession'. If LTA is paid monthly as part of CTC → likely WAGES. If paid once a year on production of bills → may qualify as exclusion. Naming it 'LTA' alone doesn't make it excluded.

### Special Allowance

Not in the exclusion list. Typically treated as WAGES. One of the most debated items. Some argue it falls under 'special expenses' — but only if paid against actual reimbursement of costs, not as a flat amount.

### Statutory Bonus

Excluded only if it is payable under law AND does not form part of remuneration under the contract. If your offer letter specifies a 'guaranteed bonus of ₹X', it is likely WAGES — not excluded.

### Reimbursement vs Allowance

If paid as a flat monthly amount (regardless of actual expense) → WAGES. If paid against actual bills/proof of expenditure → qualifies as 'sum to defray special expenses' → Excluded.

**Key Principle: Naming a component as 'Allowance' does not automatically make it excluded. The substance of the payment determines its classification — not the label.**

# Other Key Financial Impact Areas

## *Social Security Code & IR Code Changes*

### **Fixed-Term Employee Gratuity**

Now eligible for gratuity after just 1 year of service (vs. 5 years for permanent employees). Pro-rata basis. Significant liability for companies using fixed-term contracts to avoid gratuity.

### **Gig & Platform Workers**

Aggregators must contribute 1–2% of annual turnover (capped at 5% of amounts paid to gig workers) to a Social Security Fund. Implications for Swiggy, Zomato, Ola-type businesses and their vendors.

### **Mandatory Health Checkups**

Free annual health checkups for employees, especially those above 40 years. Operational cost addition — to be budgeted annually.

### **Creche Facility**

Establishments with more than 50 workers need to provide Creche facility. One off Capex + recurring running expenses. Tie up permissible

### **Restructuring Costs**

Legal opinion, Consultancy, additional internal effort to be extended on a one time basis. Increase in Internal audit scope – annual impact

### **Amendments in Finance Act**

Need to Consider certain amendments made in 2026 such as HRA, Benefits in terms of Car Reimbursements, PF contribution in Excess of 12% of Basic to make changes which will help employees save tax as well as Provide Justification for Changes.

# Accounting Implications — ICAI's Position

*Past Service Cost Recognition | Ind AS 19 / AS 15*

## ICAI FAQs (December 2025):

Any incremental gratuity and leave encashment liability arising from the Labour Codes should be recognised IMMEDIATELY as an expense — treated as Past Service Cost — and NOT deferred or spread as a purely prospective adjustment.

### Gratuity Provision

Actuarial valuation reports (for Ind AS/GAAP) must now be updated using the new wage base. The incremental liability is a one-time P&L hit (past service cost) — cannot be capitalised or deferred.

### Tax Treatment

Gratuity contributions to approved funds remain tax deductible. Additional actuarial provisions not funded may not be deductible until actually paid. Revisit tax planning.

### Leave Encashment

Similarly, leave encashment liability computed on wages (not Basic) must be restated. Incremental amount treated as past service cost under AS 15 / Ind AS 19.

### Disclosure

Companies should disclose the impact of the new Labour Codes in their financial statements. Material changes to significant estimates should be flagged in notes to accounts.

# CA's Action Checklist for Clients

*Immediate Priorities — Post 21 November 2025*

1

## Payroll Timeline Compliance

Ensure monthly wages are paid by 7th of following month. Review separation pay process (2 working days).

2

## Pay Restructuring (if needed)

Plan prospectively within bounds of Section 124. Ensure CTC and take-home are not reduced. Obtain employee consent.

3

## Monitor State Rules

Track state-specific notifications. Some states (MP, UP) have granted exemptions, others have not yet notified. Watch for changes.

4

## Fixed-Term Contract Review

All fixed-term employees now earn pro-rata gratuity after 1 year. Revise budgets and HR policies.

## CONCLUSION

# Key Takeaways

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- This is an evolving area — rules are still being notified. Multiple interpretations exist for allowances like Special Allowance, LTA, and Children Education Allowance.
- The financial impact is real and immediate — gratuity, leave encashment, and bonus liabilities must be revisited for every client which has a significant workforce.
- Scrutinies from the Labour Department are expected to increase significantly. Wrong classification of pay components has a material financial impact.
- Pay restructuring is a legitimate planning tool — but must be done within the bounds of Section 124 and cannot be just used to reduce employee benefits.
- Immediate action required: appointment letters, wage structure analysis, actuarial revaluation, and financial statement updates.

The story is unfolding as we speak.....

# THANK YOU!

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**CA PANKAJ KUMAR TRIVEDI**  
TRIVEDI & BANG, CHARTERED ACCOUNTANTS

9246509697, [pankaj.trivedi@trivbang.com](mailto:pankaj.trivedi@trivbang.com)