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India Inc figures out new salary structures to meet labour codes

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Corporate India is taking a fresh look at compensation structures following a change in the definition of "wages" under the new labour codes that come into effect on April 1.

Faced with potentially higher compensation pay-outs and implementation challenges, several companies are evaluating different permutations and combinations of salary structures to mitigate the impact on their financials and on their employees. This exercise also includes streamlining the organisation structure, mapping out roles that may be delivered from home, and those that may follow a hybrid model of delivery, say human resources (HR) experts.

Simultaneously, businesses have, through industry associations, reached out to the government for more clarity on whether components such as company-provided car, bonuses, stocks options etcetera would fall under the new definition of "wages".

The new definition under the Code of Wages, 2019, includes three components: Basic pay, dearness allowance and retention payment. Experts say what has triggered an analysis of the cost-to-company (CTC) structure is the 50 per cent cap on exclusions, and remuneration in kind as an inclusion. The new wage code mandates that basic pay will at most be 50 per cent of an employee's CTC. Accordingly, allowances such as leave travel, house rent, conveyance and overtime would be part of the remaining.

"If the payment made under exclusions exceeds 50 per cent, the excess amount will be deemed as remuneration and will accordingly be added to wages," says Avik Biswas, partner at law firm, IndusLaw.

Once the labour codes are implemented, companies will need to revisit and restructure their employee compensation packages in such a way that basic pay, dearness allowance and retaining allowance constitute at least 50 per cent of the total wages, while other components (allowances, etc) are capped at 50 per cent of the total wages, Biswas points out.

Based on how wages are determined and calculated, there will be long-term cost and tax implications for both the employers and the employees, says experts.

Most companies are looking at a scenario of basic salary being put at 50 per cent of the total pay so as to be compliant with the code, says Anandorup Ghose, partner, Deloitte India. However, this is likely to lead to multiple knock-on effects. These include an increase in basic salary-linked benefits liability and quantum of pay-outs for companies, covering both statutory and non-statutory benefits, such as leaves encashment, superannuation etc.

The potential scenarios include some employees getting lesser cash-in-hand, higher gratuity payouts by companies, higher tax liability on senior management employees at the time of availing of gratuity, among others, say experts.

Initial estimates point towards a 3 per cent to 6 per cent increase in the overall employee compensation cost for companies. However, the individual impact on different salary components would vary, says Navneet Rattan, director, performance & rewards at Aon Consulting.

For instance, the increased outgo for gratuity pay-outs — linked to basic salary — could range between 30-40 per cent and 80-90 per cent for some companies, depending on the demographic profile of senior employees and how long they have been with the organisation.

"Our advice to clients has been to prepare for best- and worst-case scenarios, both from the perspective of cost and impact on employee and employer," says Rattan.

Nishant Madhukar, HR head at Ferns N Petals, agrees that the new rules are likely to increase the employer's liability towards retirement benefits, such as leave encashment, gratuity payouts as the basic salary increases. "More contribution towards provident fund would impact the take-home salary, which, if the employer intends to match, will add to the cost to the company," he says.

Madhukar shares the dilemma that many employers face. “If the employer wants to maintain the same CTC, the take-home will get reduced. And if the take-home is to be maintained, the CTC will increase,” he says.

With the tax exemption bucket staying as is, there would be attendant impact on tax liability.

Employers are in a dilemma on whether they should restructure their CTC components or maintain status quo until there is further clarity on these concepts, says Vikram Shroff, partner, Nishith Desai Associates. In the absence of a clear position at the moment, a wait-and-watch approach might seem practical, he adds.

Another issue that many employers are grappling with concerns gig and platform workers under the new labour codes. The Code on Social Security recognises non-traditional forms of work engagement, including gig and platform workers. The code contemplates framing of social security schemes by the central and state governments with financial contribution from industry.

Experts point out that the code envisages that employer contributions would range from 1-2 per cent of the annual turnover and would not exceed 5 per cent of the actual sums paid or payable to gig and platform workers.

However, there is lack of clarity on the definition of “turnover”. Industry players say they need more clarity on whether “turnover” refers to the entire entity’s revenue, or only the revenue earned from the platform in question.

“Unless the government comes back with clarity, companies would be reluctant to restructure the remunerations of gig workers,” says Biswas.

HR experts point out that most companies are already looking to make work-from-home (WFH) a permanent feature of their work model. Several organisations are in the process of evaluating roles that could be delivered from home, and those that need to follow a hybrid model.

Over time, performance evaluation criteria are also likely to undergo a change with more focus on availability and accountability, say experts. Also, businesses are opening up to investment in new performance measurement tools and technology.

What most HR experts, however, agree on is that the new definition of wages is likely to make the remuneration packages simpler and standardised over time.

“The long-term impact of the code may be that the organisations might start to look at simplified salary structures, with lesser number of components in the pay,” says Rattan. The re-balance could, however, see some tax-friendly components disappear from the structure.