INSIGHT
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INSIGHT – SC DECIDES ON WHETHER PF CONTRIBUTIONS ARE TO BE MADE ON ALLOWANCES

On February 28, 2019, the Supreme Court of India ("**SC**") in the case of *Regional Provident Fund Commissioner (II) West Bengal* v. *Vivekananda Vidyamandir and Others*, and other connected matters[1] ("**Judgement**"), held that employers are required to make contributions ("**PF Contributions**") under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 ("**EPF Act**") on certain allowances that comprise an employee's salary.

At the outset, it is clarified that this Judgement does not amend the existing position of law. However, this Judgement has been much awaited primarily because in light of the pendency of this case, many employers were not making contributions on certain components of salary and stay orders had also been passed by various courts dealing with the question of whether specific allowances should be considered as part of Basic Wages (*as defined below*) under the EPF Act. In light of this, set out below is a brief analysis of this Judgement.

1. What is the background to the Judgement?

A number of appeals were pending before the SC on a common question of law, i.e., whether certain special allowances paid by an employer to its employees would fall within the meaning of the expression 'basic wages' under Section 2(b)(ii) ("**Basic Wages**") read with Section 6 of the EPF Act, for the purpose of computation of PF Contributions. The SC decided to hear all of these matters together and dispose them of by way of a single order. Vivekananda Vidyamandir and four other parties (Surya Roshni Limited, U-Flex Limited, Montage Enterprise Private Limited and Saint Gobain Glass Limited), were the appellants in the abovementioned matters ("**Appellants**"). The Appellants paid different types of allowances to their employees which were in the nature of travel allowance, conveyance allowance, canteen allowance, house rent allowance, management allowance, night shift incentives, medical allowance,

[1] SC Civil Appeal No. 6221/2011.

city compensatory allowance etc. (collectively "**Special Allowances**"), on which they were not making PF Contributions. The Judgement decides on whether the PF Contributions should be made on each such Special Allowances.

2. What did the Supreme Court decide?

The SC in this Judgement, relying on the principles laid down by it in the landmark decision of *Bridge and Roof Co. (India) Limited* v. *Union of India*[2] ("**Bridge Roof Case**"), which has been subsequently cited by the SC in decisions such as the *Manipal Academy of Higher Education v. Provident Fund Commissioner*[3], held that the following principles should be used to determine whether the Special Allowances should be considered as part of Basic Wages:

(i) Emoluments paid by an employer to the employee which is universally, necessarily and ordinarily paid to all employees across the board will form part of Basic Wages;

(ii) Payments which are specially paid to those who avail of the opportunity is not Basic Wages. For instance, overtime allowance is not Basic Wages because *inter alia*, it depends on the extra effort put by the concerned employee; and

(iii) Any payment by way of special incentive or work is not Basic Wages.

The SC noted that the Appellants did not provide relevant materials to establish that the Special Allowances paid to their respective employees were either variable or were linked to any incentive to promote greater output by an employee nor was there any evidence in place suggesting that the Special Allowances were not paid across the board to all employees in a particular category or were being paid especially to those who avail of the opportunity.

The SC accordingly held that the factual conclusions and concurrent findings arrived at by the respective PF authorities and appellant authorities, that the Special Allowances were part of Basic Wages and were camouflaged as allowances to avoid PF Contributions on these components, merited no interference.

3. Has the Judgement changed the current position of law in relation to determination of Basic Wages?

The Judgement has not changed the current position of law. The SC has only ruled on whether the Special Allowances disputed in the present matter should be considered as part of Basic Wages in light of the specific facts and circumstances of each of the appeals filed before it. The Judgement has relied on the principles laid down in the landmark Bridge Roof Case (decided by a 6-judge bench in 1962) to arrive at its decision, thereby simply reiterating the existing position of law.

4. If there is no change to the current position of law, why is the Judgement significant?

While the Bridge Roof Case had set out the position of law on this subject, in light of the pendency of the present matter before the SC, stay orders had been passed by various courts dealing with the question of whether specific allowances should be considered as part of Basic Wages. In addition, a number of employers had also been refraining from making contributions on certain components of salary citing the pendency of the present matter before the SC. To this extent, the Judgement has been much awaited.

Now that the SC has passed the Judgement, the protection offered by the abovementioned stay orders will no longer exist and employers will be required to make PF Contributions on all components of salary that come within the definition of Basic Wages, as per the principles laid down in the Bridge Roof Case (and upheld by the Judgement). While the Judgement will have no impact on decided cases, employers are also likely to receive adverse rulings from the Industrial Tribunal and relevant courts on pending and future matters, on this issue.

It is specifically clarified that the Judgement will have no impact on domestic workers for whom PF Contributions are being made on at least INR 15,000 per month (which is the wage threshold for applicability of the EPF Act).

However, since PF authorities are likely to scrutinize employers more closely in light of the Judgement,

[2] *Bridge and Roof Co. (India) Limited* v. *Union of India* (1963) 3 SCR 978.
[3] *Manipal Academy of Higher Education* v. *Provident Fund Commissioner* (2008) 5 SCC 428.

employers would be well advised to carry out an assessment of internal practices and policies to ensure that PF Contributions are being made on the appropriate components of salary for international workers (for whom there is no wage threshold) and domestic workers (for whom contributions are being made on an amount less than INR 15,000) by examining, based on the already existing principles set out in the Bridge Roof Case (and reiterated by the Judgement), if an excluded allowance is universally, necessarily and ordinarily being paid to employees across the board[4].

4 Please note that the Special Allowances on which some of the Appellants have been required to make PF Contributions includes house rent allowance, a component that is specifically excluded from the definition of Basic Wages. PF authorities have historically not required employers to make PF Contributions on house rent allowance regardless of the manner in which it is paid. However, in light of the Judgement, it is a possibility that the PF authorities will, going forward, look into the nature of the house rent allowance being paid, to assess if it is universally, necessarily and ordinarily paid to employees across the board and whether it is only being paid to those who avail of the opportunity, in order to determine if PF Contributions should be made on house rent allowance.

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