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# Whitepaper on coverage of allowances for PF calculation

Based on a Supreme court decision dated 28<sup>th</sup> February'2019

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# 1. Context

- Inclusion of various allowances for calculation of contribution to provident fund (to be referred as “PF” in this whitepaper) has always been a matter of dispute between the establishments and PF authorities.
- This dispute has arisen mainly because of lack of complete clarity in the definition of “basic wages” and amount on which the contribution is to be calculated.
- Supreme Court has already dealt this issue in detail in the case of Bridge and Roof Co. (India) Ltd. Vs. Union of India [(1963) 3 SCR 978].
- However, this matter again reached to the level of Supreme Court in multiple appeals to decide whether certain special allowances like conveyance allowance, medical allowance, education allowance etc. will be considered for calculation of PF contribution.
- This whitepaper dissects the latest Supreme Court ruling (dated 28<sup>th</sup> February’2019) on this issue with impact analysis.



## 2. Current practice

- To understand this issue better, it's important to discuss two important provisions of the The Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (PF Act) :
  - Definition of basic wages as per Section 2(b) of the PF Act: The term 'basic wages' is defined to mean all emoluments which are earned by an employee in accordance with the terms of contract of employment and which are paid or payable in cash but does not include the following:
    - Cash value of any food concession;
    - Dearness allowance, house rent allowance, overtime allowance, bonus, commission or any other similar allowance payable in respect of employment;
    - Present made by the employer
  - However, as per Section 6 of the PF Act, the contribution will be calculated on following amounts:
    - Basic wages;
    - Dearness allowance;
    - Retaining allowance; and
    - Cash value of any food concession
- So, if you observe the provisions of both the Sections, dearness allowance and cash value of any food concession have been excluded from the definition of basic wages but included for the purpose of calculating the PF contribution.



- However, other allowances like house rent allowance, overtime allowance etc. stands excluded for the purpose of calculation of PF contribution.
- Over a period of time, certain new allowances came into practice which formed the total salary of the employee. Some of the example are Medical Allowance, Conveyance Allowance, Education Allowance, Special Allowance etc.
- In practice, most of the establishments (on which PF provisions are applicable) doesn't include these allowances while calculating the PF contribution.
- However PF authorities, during their inspection, always raise the demand for the short deduction of PF on these allowances.

### 3. Supreme court ruling



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- Supreme court placed reliance on many of it's earlier judgments on the similar issues. It has mainly relied on the principles of 'universality' and 'contingency' laid down in its earlier decisions in the case of Bridge and Roof Co. and Manipal Academy of Higher Education.
- The test whether a allowance should be included in "basic wages" for the calculation of PF contribution will depend on following principles:
  - Where the wage is universally, necessarily and ordinarily paid to all across the board such emoluments are basic wages.
  - Where the payment is available to be specially paid to those who avail of the opportunity is not basic wages.
- Supreme court placed it on record that establishments could not present any evidence which shows that the allowances in question were not paid to all employees or has any direct nexus with the extra output or efforts by the employee.

## ....contd. [3. Supreme court ruling]



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- Supreme court upheld and agreed with the decisions of PF Authority and Appellate Authority that the allowances in question were part of basic wages but camouflaged as allowances to avoid the deduction and deposit of PF contribution.
- It was also held that for an amount to go beyond the basic wages, it has to be shown that the employee concerned has become eligible to get the extra amount beyond the normal work which the employee was otherwise required to put in.



## 4. Impact

- It's impact will be in those cases where the basic wages of employees is less than Rs. 15,000 and their salary structure includes some of the allowances which are paid to all employees. Now, these allowances need to be included to calculate the PF contribution.
- For domestic employees having basic salary of more than Rs. 15,000, the deduction is restricted up to Rs. 15,000 as per proviso to Para 26A of Employee's Provident Fund Scheme. So, this ruling will not have any impact on these domestic employees.
- However, for international employees/workers proviso to Para 26A is not applicable. Accordingly, these commonly paid allowances will be included in the calculation of PF contribution in the case of such international employees/workers.



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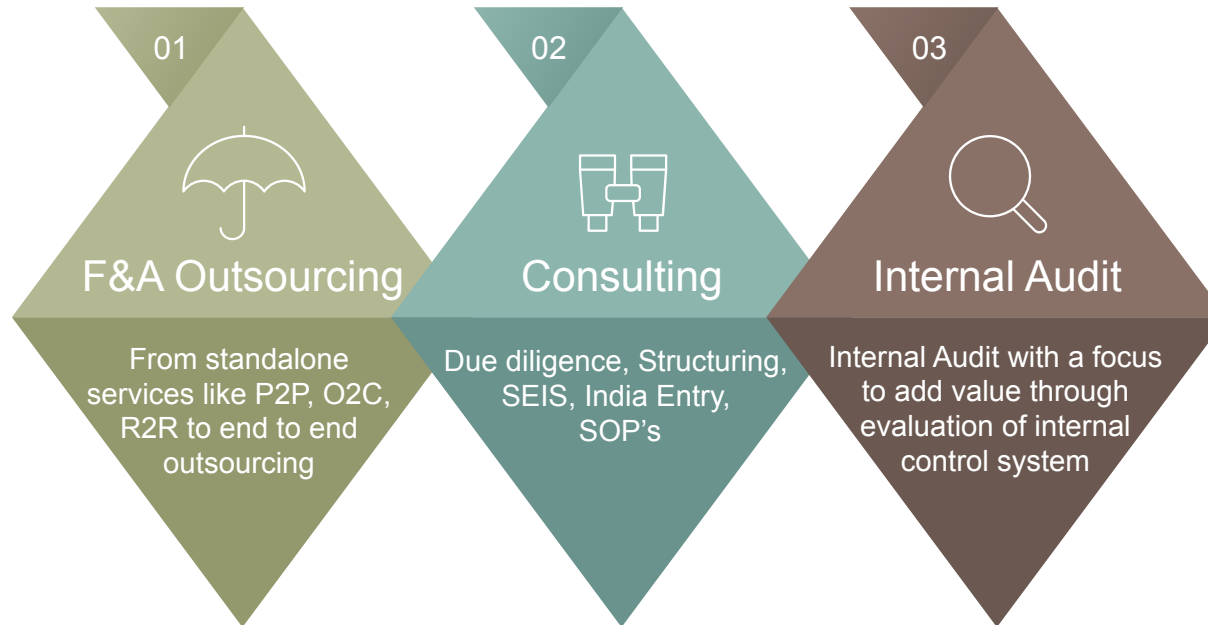
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