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### Recent guidelines by Employees' Provident Fund Organisation on the definition of basic wages and conducting inquiry

#### In brief

The Employee Provident Fund Organization (EPFO) has recently issued a Circular providing guidelines<sup>1</sup> on the matters pertaining to the following:

- The definition of “basic wages” on which contributions to the Provident Fund (PF) is to be calculated
- Conducting inquiry under Section 7A of the Employees Provident Funds and Miscellaneous Provisions Act, 1952 (the Act)

The key features of the above guidelines are as follows:

#### Key guidelines

##### Clarification on the definition of basic wages

- Basic wages comprise all payments except the specified exclusions.
- Allowances that are ordinarily, necessarily and uniformly paid to the employees are to be treated as part of the basic wages.

<sup>1</sup> [http://www.epfindia.com/Circulars/Y2012-13/CirQJA\\_345.pdf](http://www.epfindia.com/Circulars/Y2012-13/CirQJA_345.pdf)

- The confusion in the definition of wages primarily arises from the expression "commission or any other similar allowance payable to the employee" in section 2(b) (ii) of the Act<sup>2</sup> as "commission" and "any other similar allowance" are read as two separate expressions and hence "any other allowance" is read as an omnibus exclusion, thereby encouraging the subterfuge of splitting of wages to exclude the PF liabilities.
- The expression "commission or any other similar allowance payable to the employee" is one continuous term meaning commission or any other "commission" like allowance by whatever nomenclature referred. Thus "basic wages" is subject to exclusions expressly referred to in the above definition and no other.

### **Guidelines for conducting inquiry**

- Compliance branch of each of the field offices shall be divided into two broad divisions:
  - (i) Administration division to investigate and report on the complaints, defaults, compliances, remittance status, etc.
  - (ii) Judicial division to exclusively conduct enquiries under the Act
- Detailed procedures have been prescribed in relation to initiation of inquiry and its disposal.

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<sup>2</sup> "Basic wages" means all emoluments which are earned by an employee while on duty or [on leave or on holidays with wages in either case] in accordance with the terms of employment and which are paid or payable in cash to him, but does not include -

- (i) The cash value of any food concession
- (ii) Any dearness allowance (that is to say, all cash payments by whatever name called paid to an employee on account of a rise in the cost of living), house-rent allowance, overtime allowance, bonus, commission or any other similar allowance payable to the employee in respect of his employment or of work done in such employment
- (iii) Any presents made by the employer

- Inquiries should be initiated only after actionable and verifiable information is provided to the compliance officer.
- Relevant records, including the history of the establishment, shall be made available online to compliance officers for their consideration.
- No inquiry or investigation shall ordinarily go beyond seven years except in cases where specific verifiable complaint or information is received.

### **Our comments**

The recent clarification provided by the EPFO has huge ramifications as any allowance (other than those specifically excluded) that is being given universally, necessarily and ordinarily to all employees across the board form part of basic salary. Hence, PF contributions becomes payable on such allowances. It will result in an additional cost for the employer and lower take-home salary for the employees, due to an increase in their contribution on such allowances.

It is relevant to mention that there are conflicting judgments by the High Courts of India on the interpretation of the term "basic wages" provided in the Act. Recently, the Madhya Pradesh (MP) High Court<sup>3</sup> ruled that allowances that are given universally, necessarily and ordinarily to all employees forms part of basic salary. The said judgment has been challenged in the Supreme Court and the matter is yet to be decided. The decision by the Supreme Court would perhaps provide a direction in the matter but till then, this circular is a wake-up call for the employers to review their position in relation to their compensation structure. The other guidelines in relation to inquiry and audit are to improve the enforcement and streamline the compliance process currently being followed by the authorities.

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<sup>3</sup> Montage Enterprises Pvt. Ltd. v. Employees Provident Fund and Another [W.P. No. 1857 of 2011] (Madhya Pradesh)

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