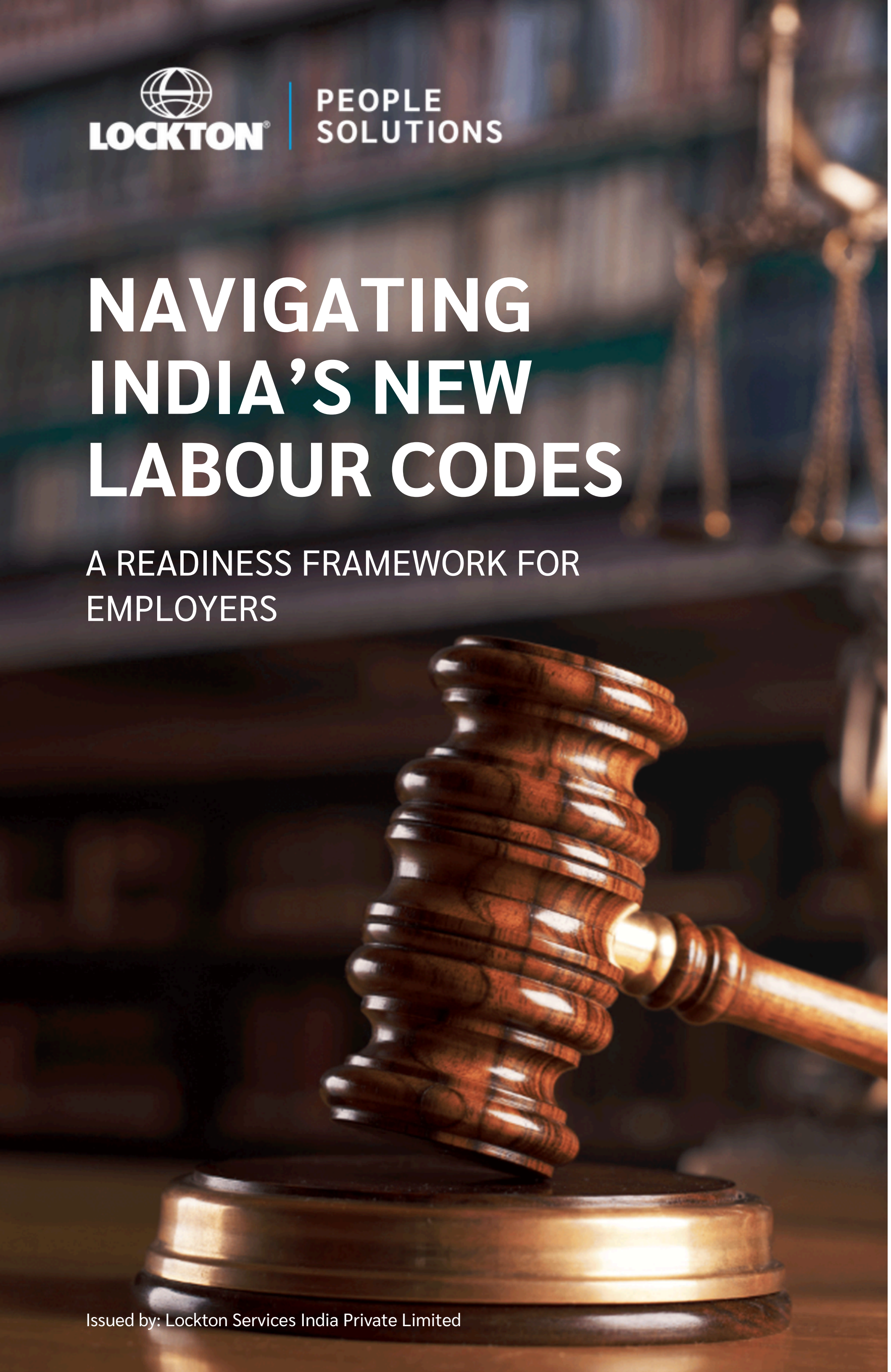

LOCKTON | PEOPLE SOLUTIONS

NAVIGATING INDIA'S NEW LABOUR CODES

A READINESS FRAMEWORK FOR EMPLOYERS

Issued by: Lockton Services India Private Limited

On 21 November 2025, the Government of India brought into effect the four labour codes:

- The Code on Wages, 2019
- The Code on Social Security, 2020
- The Occupational Safety, Health & Working Conditions (OSHWC) Code, 2020
- The Industrial Relations (IR) Code, 2020

These codes consolidate 29 existing labour legislations into a simplified, modern framework aligned with the needs of India's evolving workforce and economy.

HISTORY

India's labour laws span nearly 75 years, with several acts enacted during pre-Independence or early post-Independence years in an era where no internet or telecom infrastructure was available, no organized HR systems were in place and there was little to no automation in processes. Moreover, workforce models and business structures have fundamentally transformed with technology enablement, contractor, freelancer, gig-based workers and hybrid and flexible employment arrangements in place.

The new labour codes have been introduced to align India's labour ecosystem with current realities, simplify compliance, support worker protection and improve ease of doing business for economic growth.

What should employers expect?
While the central rules have been made effective, we should expect more clarity from the government in the coming weeks on the compliance processes, forms, register formats, and safety requirements. Companies are expected to follow current regulations till clarity on procedural aspects are provided.

Most states have also issued the draft rules, barring a few. The coming weeks may involve multiple notifications clarifying implementation processes.

While we wait for more clarity, some aspects of the labour codes become effective immediately from 21 November 2025. The definition of employee and worker has been clearly called out, along with recognizing additional workforce models like fixed term employees (FTEs), gig workers, contract labour – and employers can start evaluating their current workforce as per the new codes. A uniform definition of "Wages" has also been clearly called out which will have an impact on calculations related to Gratuity payout, PF, ESI, Leave Encashment, Statutory Bonus and Overtime.

KEY CHANGES & IMPACT AREAS

New 'Wage' definition and its implications to employers:
The labour codes standardized the definition of wages across all the four codes, bringing in consistency and clarity to benefit calculations across a wide range of benefits. While this brings uniformity leading to lower administrative complexity and lesser ambiguity on interpretation of salary for benefit payouts, this change will likely have an impact on benefit related costs for employers.
As per the Code of Wages, 2019 the new definition of 'wage' is broader in nature and states that if specified exclusions exceed 50% of the total remuneration, the excess must be added back to wages. Which means that wage must be at least 50% of the total remuneration.

Scenario 1 (Exclusions less than 50% of CTC)

Basic Pay: INR 40,000
Excluded Allowances from the definition of wage: INR 40,000
Retaining Allowance: INR 20,000
Total CTC: INR 100,000 In this case, Wage is calculated as INR 40,000 + INR 20,000 = INR 60,000 (Basic + Retaining Allowance)

Scenario 2 (Exclusions greater than 50% of CTC)

Basic Pay: INR 30,000
Excluded Allowances from the definition of wage: INR 60,000
Retaining Allowance: INR 10,000
Total CTC: INR 100,000 In this case, exclusions can be a maximum of 50% of total CTC (50% x 100,000 = INR 50,000), therefore INR 10,000 will be added back to Wages. Hence, wage is calculated as INR 30,000 + INR 10,000 + INR 10,000 = INR 50,000 (Basic + Retaining Allowance + Portion of exclusions added back to wages).

Few aspects to keep in mind:

- The Code on Wages, 2019 calls out the various components that can be considered as exclusions from the wage definition, and it is not necessary that the exclusions will be at least 50% of total remuneration. This can lead to wages being higher than 50% of total remuneration.
- The perception of increasing basic pay to 50% may not solve for the new definition of wages, and a carefully crafted restructuring of salary components needs to carried out by employers to minimize financial impact of benefit payouts.

Employers should look at this as an opportunity to restructure their salary components to be simplified, compliant and optimized to minimize financial impact. While employers might still want to retain certain allowances from a tax benefit point of view, various additional allowances that now will form a part of wage can be consolidated to provide a simplified salary structure to employees.

Impact to benefit schemes:
The new definition of wage will apply to calculate various benefit schemes like Gratuity, Employees' State Insurance, Overtime, and Statutory Bonus. These codes aim to enhance social security coverages across various workforce models like permanent employees, fixed term employees, contract labour and gig workers.

GRATUITY

Gratuity will now be calculated on the new definition of wage, which will be at least 50% of the total remuneration (can be higher depending on how the salary components are structured). Prior to the new codes, Gratuity was payable on the last drawn basic salary + dearness allowance which was typically lower than 50% of the total remuneration for most organizations. As a result, employees will receive a higher gratuity benefit as per the new codes and employers will most likely need to recognize a higher provision for this benefit in their books of accounts.

Old Provisions	New Provisions under labour codes
Total monthly CTC: INR 100,000	Total monthly CTC: INR 100,000
Last drawn monthly basic salary (40% of CTC): INR 40,000	Last drawn monthly wage (at least 50% of CTC): INR 50,000
Years of Service: 10 years	Years of Service: 10 years
Gratuity Payable: 15 days of the last drawn monthly salary, for the number of years of service.	Gratuity Payable: 15 days of the last drawn monthly salary, for the number of years of service.
Gratuity Payable: INR 230,769 (15/26 x 40,000 x 10)	Gratuity Payable: INR 288,462 (15/26 x 50,000 x 10)

Retrospective Impact:
While these changes are effective from 21 November 2025, the gratuity formula applied is retrospective, i.e. if an employee has been working for 10 years and decides to leave the organization after 21 November 2025, the Gratuity will be payable on the new definition of wage for the entire 10-year duration that the employee has worked for the company.

Moreover, Gratuity benefit for Fixed Term Employees (FTEs) has been enhanced to be payable on a pro-rata basis for the time they serve the company. The minimum period of service to be eligible for Gratuity has changed to 1 year of service for FTEs. Prior to the new codes, FTEs were eligible to receive Gratuity after 5 years of continuous service. This change will have a significant impact to employers that employ FTEs.

Considering the various changes to Gratuity – organizations need to assess the impact to their gratuity benefit scheme and be ready to meet higher gratuity provisions to stay complaint. Those organizations that have funded their gratuity, will need to adjust their funding levels based on the new gratuity liability. The impact on gratuity will vary depending on the company's gratuity policy, for example, for organizations that have an uncapped gratuity scheme will have a higher impact as compared to those employers that have a capped gratuity scheme (i.e. capped to INR 20L). This also gives an opportunity to employers to re-evaluate their gratuity benefit policy to balance the additional benefit provided to employees and the additional cost obligation employers must bear.

PROVIDENT FUND (PF)

The notification issued by the Ministry of Labour and Employment on 21 November 2025 has specifically excluded repealing Employee's Provident Funds and Miscellaneous Provisions Acts (PF Act) and hence the existing PF provisions will continue to be in force until specifically notified by the Ministry of Labour and Employment. However, it is important to note that while the existing PF provisions continue - PF will be paid on the new definition of wage. This means that those employees who have a monthly basic salary lower than INR 15,000 (cap specified as per the PF Act) will benefit from a higher monthly PF contribution which will be on the new definition of wage and not the old definition of basic salary + DA. While this might not be a significant impact, employers will have to ensure these changes are implemented and policies are updated to stay compliant.

EMPLOYEES STATE INSURANCE ACT (ESI)

The coverage of ESI has been expanded to cover all establishments with 10 or more employees, including organized, unorganized, gig and platform workers. A mandatory coverage for all employees in establishments engaged in hazardous occupations. ESI that was previously calculated on gross salary will now be calculated on the new definition of wage, however the cap of INR 21,000 per month remains.

While the coverage of ESI has expanded, the contribution per employee has reduced as wage would be lower than gross salary for an employee. This means that the same ESI benefit will be provided to employees at a lower cost.

This also means that a larger base of employees will be eligible to receive ESI benefits as the wage cap is now INR 21,000 instead of the gross pay cap (i.e. employees with a CTC of up to INR 42,000 will be eligible for this benefit if wage is structured at 50% of CTC). Employers will need to assess the impact of this change and ensure compliance towards this benefit.

MANDATORY ANNUAL HEALTH CHECK-UPS

Employers are now required to provide free annual health check-ups to workers aged 40 and above, promoting preventive healthcare and timely diagnosis.

Additional key impact areas from code on wages, 2019:

1. National Floor Wage: A national minimum floor wage has been set by the central government to ensure all workers receive a wage at or above a basic standard of living. All states need to comply with this national floor wage and provide a minimum wage equal to or above the national floor wage. This aims to reduce wage differences across geographies and foster nationwide equity.

2. Working Hours & Overtime: Capped to 48 hours a week. The code provides flexibility to implement a four-day work week (12 hours per day), five-day work week (9.5 hours per day) or a six-day work week (8 hours per day) as long as the cap of 48 hours is not exceeded. Overtime must be paid at double the rate of wages to any work done beyond the normal working hours as defined by the company.

3. Statutory Bonus: Will now be paid on the new definition of wages. Prior to the codes, the statutory bonus was paid on total remuneration. This implies that a larger group of employees may now qualify for statutory bonus, as eligibility will be determined using the revised wage ceiling of INR 21,000 rather than total remuneration. In effect, employees with a CTC of up to INR 42,000 could fall within the scope of this benefit if wages are structured at 50% of CTC. Employers will need to assess the impact of this change and ensure compliance.

4 Timely Wage Payment: Wages must be paid on time as defined by the Code. For monthly payment of wages, the payment must be made within 7 days of the following month. For daily payment of wages, the payment must be made at the end of the daily shift. On termination or resignation, the full and final settlement must be completed within two working days. Employers will have to re-look at their processes for payouts to ensure compliance with these timelines. In addition, the government has also called out against discrimination based on gender – with equitable pay to be provided to men and women performing the same or similar work, consent from women working in night shifts and hazardous industries, stringent anti-harassment laws and complaint mechanisms to be adopted by organizations and return to work flexibility for new mothers.

Various categories of workforce defined:

The Codes now clearly define various workforce categories such as permanent employees, fixed-term employees, gig workers, and contract labour. They also distinguish between a 'worker' and an 'employee,' with expanded benefits for workers. Under the new framework, workers will now be entitled to overtime, leave encashment, statutory minimum wages, periodic health check-ups, and enhanced financial security linked to their wages.

The Labour Codes also clarify the role of contract labour and the nature of work they are permitted to undertake. Contract labour is restricted from performing the 'core activities' of an organisation, except under specific circumstances that have been expressly defined.

Fixed term employment is now recognized as an employment model with an aim to equate wages and social security benefits as provided to a permanent worker.

The government has also aimed to define the unorganized sector of gig workers, platform workers and other individuals in the unorganized sector by providing them with certain welfare and social security programs. This population will now be eligible to receive health protection, disability support, maternity benefits, and old-age pension programs via a social security fund. Aggregators are required to maintain a social security fund for gig workers and contribute 1-2% of their annual turnover capped at 5%.

This provides employers an opportunity to relook at their group policies to encompass a larger employee base. It's also important for employers to define their workforce categories as different benefit policies may be applicable across these workforce categories.

Preparing for Transition: How Lockton can help:
These reforms mark a major shift in the regulatory landscape and are expected to affect a large proportion of the workforce, as well as various HR processes and policies.

It is therefore critical for organizations to evaluate the implications comprehensively and prepare for a seamless transition to maintain compliance and operational efficiency.

Lockton's approach to ensure a seamless transition is as follows:

1. Workforce Classification Review: Employers should start by mapping their current workforce structures across permanent, FTEs, contract staff, gig workers. This will involve redesigning job descriptions as per definitions across these workforce models to ensure compliance clarity.
2. Revamp Employment Contracts: Relook at employment contracts to add clarity around fixed-term roles and their benefit eligibility. Employers will now be required to issue appointment letters to all workers to enhance transparency and provide greater job security.
3. Evaluate Compensation Structure: Review salary components to adhere to the new definition of wages. You may need to rebalance some salary components to ensure exclusions are close to 50% of total remuneration to minimise cost impact.
4. Impact to Benefits & Take-home Salary: Model impact of wages on PF, ESI, Gratuity, Statutory Bonus and other benefits to assess eligibility and payout quantum and then review the impact on take-home salary of employees.
5. Benefit Cost Obligations to Employer: Conduct actuarial valuations for defined benefit schemes to assess cost impact. Once cost impact is determined, you will need to evaluate funding strategy to meet the additional cost obligations. Parallelly, assess financial implications for additional benefit provisions like ESI, statutory bonus, annual medical Health check-ups and others.
6. Compliance Infrastructure Readiness: Assess and upgrade HRMS and payroll systems to align with the new Codes. Update statutory registers and strengthen record-keeping practices as mandated. Review current safety, welfare, and workplace standards to ensure full alignment with the revised requirements.
7. Policy Revamp: A complete policy redrafting will be required across benefits, policies and processes (Gratuity, PF, Overtime, Safety, Attendance, Working hours, Grievance redressal, etc.)
8. Change Management: The new codes will impact most employees in the organization, and a clearly crafted communication strategy needs to be in place. Employees, managers, leaders, HR teams (across payroll, benefits, operations, HR systems), compliance, legal and external vendors all need to be made aware of the changes and how this impacts each function. Managers and supervisors need to be equipped to answer employee queries.
9. Multi-State Compliance Planning: If you are across multiple states, you will need to track ongoing state notifications and build state-specific checklists to ensure compliance across multiple states.

Lockton India is fully equipped to guide employers through every stage of this transition.

If you are seeking a trusted partner to help you navigate these changes seamlessly, please reach out to us at:

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