



CRITICAL ANALYSIS OF THE PAYMENT OF BONUS ACT, 1965

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ABSTRACT

The employees of a company are given statutory right to share the profit of their employer through The Payment of Bonus Act, 1965. Bonus is generally referred to as a reward that is given to a worker and therefore, the main objective of the Act is rewarding the employees for their work and contribution in the organisation. The practice of payment of bonus was first spotted during the world wars when an organisation granted 10% of the wage as war bonus to its employees and since then payment of bonus has brought about wave of happiness among the family of the employees which has also resulted in increase in performance of the workers in the firm. The aim of this research paper is to analyse the provisions of the Act and the latest amendments made to the Act. The researchers will look into the history of the Act. The researchers will also look into the rights and duties of both the employees and the employer under the act. The researchers will discuss the eligibility for bonus under the Act and critically analyse the same. The researchers will also analyse the maximum and the minimum bonus that can be given to a worker and deadline for payment of said bonus. The research paper will also talk about the offences and penalties under the Act and also critically analyse the amendments of the Act. The researchers will discuss the merits and demerits of the said amendment and the ceiling limit on the amount considered for calculation of bonus under the Act.

INTRODUCTION-

Bonus in its generic sense is a cash payment made to the employees in addition to the wages. It is referred to as a reward that is given to a worker and therefore, the main objective of the act is rewarding the employees for their work and contribution in the organisation. Bonus was granted

for the first time to the employees in the textile industry of Pre-independent India in 1917, more commonly referred to as 'war bonus', due to an increase in wages being allowed owing to war conditions. Bonus is not an ex-gratia payment, wherein it has been held that payment of bonus is not based on any moral obligation and 'Full Bench Formula' ought to be necessary for payment of bonus.¹ The formula laid down by the Labour Appellate Tribunal was to calculate the gross profits of an enterprise to include²-

1. Return on paid up capital at the rate of 6%
2. Return on working capital between 2% - 4%
3. Depreciation worked on a national basis
4. Rehabilitation
5. Income Tax

Through this calculation, if there arose any surplus on the income generated, it ought to be distributed equitably among employees. However, labour unions were not satisfied with the Full Bench Formula as the rehabilitation charge mentioned could wipe out the available surplus and therefore, the Hon'ble Supreme Court laid down two conditions which had to be satisfied before a demand for bonus could be justified wherein, firstly, the wages fell short of the living standard and secondly, the industry makes huge profits part of which are due to the contribution made by the employees in increasing production.³

Therefore, broadly speaking, the scheme of the Act is fourth-dimensional⁴-

1. To impose statutory liability on employer to pay bonus to employees
2. To define payment of bonus as per the prescribed formula
3. Scheme of set-off and set-on to pay minimum and maximum bonus applicable
4. To provide machinery for enforcement of liability for payment of bonus.

The Payment of Bonus Act, 1965 is a significant piece of legislation in India that governs the payment of bonuses to employees. While the Act was introduced with the objective of promoting employee welfare and ensuring fair distribution of profits, it has been subject to both praise and

¹ Mill Owners Association v. Rastriya Mill Mazdoor Sangh, (1952) LAC 423.

² Id.

³ Muir Mill Ltd. Suti Mill Mazdoor Union, (1995) I LLJ 1.

⁴ Jalan Trading Co. Mill Mazdoor Sabha, AIR 1967 SC 691.

criticism. The Act applies to establishments employing a certain minimum number of employees and having a specified level of profit. Critics argue that the coverage threshold may exclude many small-scale enterprises, thereby limiting the benefits to a significant portion of the workforce. The Act mandates that a specific percentage of profits should be allocated as the bonus amount, which is determined based on a predetermined formula. Critics argue that this approach doesn't take into account the financial health or performance of individual companies, and can sometimes place an unnecessary burden on struggling enterprises.

The Act provides several definitions related to different aspects of bonus calculation, but some of these definitions are considered ambiguous. This ambiguity can lead to confusion and disputes between employers and employees, resulting in legal complications and delays in the payment of bonuses. The Act excludes certain categories of employees from receiving bonuses, such as those who have been dismissed for misconduct. Critics argue that this provision can be misused by employers to deny bonuses to deserving employees or create an environment of fear where employees may hesitate to raise legitimate concerns.

Compliance with the Act requires employers to maintain detailed records, file annual returns, and undergo audits, which can be time-consuming and burdensome, especially for small-scale enterprises. This administrative burden adds to the overall cost of doing business. The Act does not provide flexibility to employers in determining the bonus payout structure or linking it to individual or team performance. Critics argue that a more flexible approach could incentivize employees and encourage higher productivity and performance. While the Act mandates a percentage of profits to be allocated as bonuses, it does not provide a framework for profit-sharing beyond that. Critics argue that profit-sharing schemes can motivate employees to align their interests with the company's success and foster a sense of ownership. The Act has not undergone significant revisions since its introduction in 1965, despite substantial changes in the economic landscape and labor market dynamics. Critics argue that the act needs to be periodically reviewed and updated to address emerging challenges and align with modern business practices.

While the Payment of Bonus Act, 1965 aims to protect the interests of employees and ensure fair distribution of profits, it has faced criticism on various fronts. The Act's limited coverage, rigid bonus calculation formula, administrative burden, lack of flexibility, and failure to address contemporary issues have been areas of concern. To make the act more effective, it is crucial to

consider these criticisms and undertake necessary reforms that strike a balance between employee welfare and the practical realities of the business environment.

FEATURES OF PAYMENT OF BONUS ACT

The Payment of Bonus Act, 1965 provides for various statutory obligations on calculation of bonus, computation of gross profits and available surplus, concept of set-off and set-on, payment of minimum and maximum bonus, time-limit for payment of bonus etc.

Sec. 4 of the Act provides for computation of gross profits wherein the calculation be done as provided under the First Schedule of the Act in case of a banking company and under Second Schedule for any other case.⁵ It has been held that the scheme framed by a company for the payment of bonus to reduce liability of income tax wherein the amount paid by the company ought to be added back for the purpose of computing the gross profit irrespective of the varying names provided to a payment of bonus scheme.⁶

Sec. 5 of the Act provides for the computation of available surplus wherein such surplus shall be the gross profit for an accounting year upon deduction of sums referred to under Sec. 6 of the Act.⁷ A claim for depreciation on account of double shift can be allowed even if it was not claimed not claimed under the Income Tax Act, wherein the amount of income tax payable for the bonus year is to be calculated after deducting statutory depreciation and not notional normal depreciation.⁸ Furthermore, rehabilitation is a substantial reserve item which goes to reduce the available surplus and thus as a result, affects the right of the employees to receive the bonus, and therefore, the employer ought to provide all relevant material to justify such claim.⁹

Sec. 8 provides for eligibility of bonus wherein every employee shall be entitled to be paid bonus in accordance to the Act by his employer in an accounting year, however, the employee should have worked for not less than thirty working days in that year.¹⁰ The scope of the meaning of the term 'worked' has been analysed by the Hon'ble High Court of Gujarat wherein it was held that as long as the employee is 'ready and willing to work', the employee is entitled to bonus and an

⁵ Sec. 4, Payment of Bonus Act, 1965, No. 21.

⁶ All India Voltas & Volkart Employees Federation v. Voltas Ltd., (1985) II ILJ 409 (SC).

⁷ Sec. 5, Payment of Bonus Act, 1965, No. 21.

⁸ B.E. Supply Co. v. The Workmen, AIR 1972 SC 330.

⁹ Binny Ltd. v. Workmen, AIR 1973 SC 353.

¹⁰ Sec. 8, Payment of Bonus Act, 1965, No. 21.

overt act of the employer to not provide explicit work to that employee is not a valid reason to not pay bonus.¹¹

Sec. 9 of the Act provides for disqualification for bonus, wherein an employee would be disqualified from receiving bonus if he is dismissed from service for fraud, violent behavior within the workplace, theft, misappropriation or sabotage of any workplace property.¹² It is important to note that the disqualification of payment of bonus to the employee by the employer is based on an accounting year, and the employer cannot deny payment of bonus to the employee based on his past conduct in previous accounting years.¹³

While Sec. 10 provides for payment of minimum bonus¹⁴, Sec. 11 of the Act provides for payment of maximum bonus.¹⁵ It has been held that the minimum bonus amount should be 8.33% of the salary or wages, and an amount of 20% the salary or wages be the cap limit for maximum bonus earned. The provision received an amendment in 2015 which shall be analysed later in the paper. The Constitutional validity of Sec. 10 was analysed and whether it was ultra vires to Art. 19(1)(g) and Art. 301, wherein the Hon'ble Supreme Court upheld the statutory provision as minimum bonus payment came under the reasonable restriction of public interest under Art. 19(6) and Art. 302. Furthermore, the statute upheld the Directive Principles of State Policy through Art. 39 and Art. 43.¹⁶

Sec. 27 of the Act provides for appointment of inspectors by the appropriate Government through notification in the *Official Gazette*. An inspector may require an employer to furnish such information as he may consider necessary and enter any establishment to examine records relating to the employment of persons or the payment of salary or wage or bonus in the establishment.¹⁷

PENAL PROVISIONS-

¹¹ ONGC Sabarmati v. Sham Kumar Sahegal, (1995) I LLJ 863 (Guj).

¹² Sec. 9, Payment of Bonus Act, 1965, No. 21.

¹³ Himalaya Drug Co. Makali v. II Additional Labour Court, Bangalore, (1986) II LLJ 45 (Kar).

¹⁴ Sec. 10, Payment of Bonus Act, 1965, No. 21.

¹⁵ Sec. 11, Payment of Bonus Act, 1965, No. 21.

¹⁶ KM Mani v. PJ Antony, AIR 1979 SC 233.

¹⁷ Sec. 27, Payment of Bonus Act, 1965, No. 21.

Sec. 28 of the Act provides that if any person contravenes any provisions of the Act or any rule made thereunder or if any person fails to comply with a direction given to them, be punishable with imprisonment for a term which may extend up to six months or be liable to fine which may extend to Rs. 1000, or both.¹⁸

Sec. 29 of the Act provides for offences by companies, wherein if the offending person is a company, then every individual person who is responsible to the conduct of business of the company at the time of offence shall be deemed to be guilty and be held liable to be proceeded against and punished accordingly.¹⁹ It was held in the case of *V.B Sivalingam Chettiar, Managing Director Abirami Cotton Mills Ltd., Sullurpet v. State Represented by the Labour Officer, Nellore*, that for failure to maintain and produce registers on demand of the inspector, the Managing Director alone was tried for the offence. However, the Hon'ble Court held that the Managing Director, despite being the one responsible to the company, the company is also a juristic person and both the Managing Director as well as the company ought to share the responsibility and blame for the offence.²⁰

Sec. 30 provides for cognizance of offences under the Act wherein no court shall take cognizance of any offence punishable under this Act, save on complaint made by or under the authority of the appropriate Government and no court inferior to that of a presidency magistrate or a magistrate of the first class shall try any offence punishable under this Act.²¹

IMPACT OF AMENDMENT & CALCULATION OF BONUS

On 31 December 2015, the President gave his assent to certain amendments to the Payment of Bonus Act, 1965.²² The amendments have increased the wage threshold for determining applicability of the Act from Rs. 10,000 to Rs. 21,000 per month. Additionally, the wage ceiling for calculation of bonus has been increased from Rs. 3500 to Rs. 7000 per month.²³ Previously the maximum bonus payable was 20% of Rs. 3500 per month, wherein the minimum bonus payment

¹⁸ Sec. 28, Payment of Bonus Act, 1965, No. 21.

¹⁹ Sec. 29, Payment of Bonus Act, 1965, No. 21.

²⁰ (1986) II LLJ 104 (AP).

²¹ Sec. 30, Payment of Bonus Act, 1965, No. 21.

²² Payment of Bonus (Amendment) Act, 2015, No. 6 of 2016.

²³ Id.

was also capped at 8.33% of Rs. 3500 per month or Rs. 100, whichever is higher.²⁴ The calculation ceiling of Rs. 3500 has now been doubled to Rs. 7000 per month or the minimum wage for the scheduled employment, as fixed by the appropriate Government whichever is higher.²⁵ “The Amendment has sought to make more employees eligible for bonus by raising the ceiling limit of the monthly wages. The Amendment also increases the amount of bonus that would be received by the eligible employee as against the Principal Act which provided that the bonus payable to an employee will be in proportion to his or her salary or wage. However, if an employee’s salary is more than Rs. 3500 per month, for the purposes of calculation of bonus, the salary will be assumed to be Rs. 3500 per month. After the Amendment, this limit has been enhanced to Rs. 7000 per month or the minimum wage for the scheduled employment whichever is higher.”²⁶

Furthermore, the amendment provides for a retrospective effect from April 1st, 2014. However, there may arise certain complications due to this retrospective effect as companies could have already determined allocable surplus for the accounting year and therefore, the allocable surplus would have to be reassessed all over again from scratch.²⁷

Sec. 12 of the Act provides for calculation of bonus, wherein in the case of *Indian Cable Co. v. Workmen*²⁸, it was observed that even though officers drew salary between Rs. 750 and Rs. 1600 per month, are employees under Sec. 2(13) of the Act, and are eligible for bonus, the maximum cap limit is to be taken as Rs. 750 for calculation of bonus. When he is paid over and above his bonus an ex-gratia amount to make up for the loss occasioned by expenditure debited directly to Reserve. Such amount can therefore, be added back to the gross profits of the employer for purposes of working out available surplus.

CONCLUSION-

²⁴ Sec. 10, Payment of Bonus Act, 1965, No. 21.

²⁵ *Supra* Note at 22.

²⁶ Rebecca Furtado, A Critical Analysis of the Payment of Bonus Act, 1965, Ipleaders, 30th November, 2016, <https://blog.iplayers.in/critical-analysis-payment-bonus-act-1965/>.

²⁷ Trilegal, Analysis of the Payment of Bonus (Amendment) Act, 2015, January 13th, 2016, [https://www.trilegal.com/index.php/publications/analysis/the-payment-of-bonus-amendment-act-2015#:~:text=The%20minimum%20bonus%20payment%20was,%60%20\(which%20is%20higher\)](https://www.trilegal.com/index.php/publications/analysis/the-payment-of-bonus-amendment-act-2015#:~:text=The%20minimum%20bonus%20payment%20was,%60%20(which%20is%20higher).).

²⁸ AIR 1972 SC 2195.

The amendment made to the Payment of Bonus Act, 1965 in 2015 has its own advantages and disadvantages. While the total amount of payment of minimum bonus under Sec. 10 has indeed risen and there has been a double of the amount, the retrospective application of the Act may raise a few eyebrows considering its drawbacks with respect to allocable surplus. However, the Payment of Bonus Act, 1965 ultimately strives to achieve one of the Constitution's basic structures, in Socialism, by striving to improve the lives of the employees of industries. This is in accordance with the Directive Principles of State Policy under Part IV, under Art. 39 and Art. 43 of the Constitution as a guiding light to achieve one of the goals of the preamble by endeavouring towards social justice.

To improve the implementation of the Payment of Bonus Act, 1965 and address some of the concerns raised, the following suggestions ought to be considered.

1. **Review Coverage Thresholds:** Evaluate and adjust the minimum employee count and profit criteria for coverage to ensure that a larger proportion of workers, including those in small-scale enterprises, are eligible for bonuses.
2. **Transparent Bonus Calculation:** Provide clear guidelines and methodologies for calculating bonuses that take into account the financial health and performance of individual companies. This could involve considering factors like profitability, productivity, and company-specific circumstances.
3. **Simplify Definitions:** Clarify and streamline the definitions used in the act to reduce ambiguity and minimize potential disputes between employers and employees. This will help in ensuring a smoother and more efficient implementation of the bonus calculation and payment process.
4. **Expanded Eligibility:** Revisit the exclusions for certain categories of employees and ensure that deserving employees are not unfairly denied bonuses. The criteria for exclusion, such as dismissal for misconduct, should be clearly defined and applied judiciously to prevent misuse.
5. **Easing Administrative Burden:** Simplify and streamline administrative requirements, such as record keeping, filing of returns, and audits, to reduce the burden on employers, particularly small-scale enterprises. Introduce digital platforms and simplified procedures to make compliance more manageable.

6. Flexibility in Bonus Structure: Allow employers some flexibility in designing bonus structures, such as linking bonuses to individual or team performance. This would encourage higher productivity, motivation, and a sense of ownership among employees.
7. Encourage Profit Sharing: Consider introducing provisions that go beyond a fixed percentage of profits and promote profit-sharing schemes. Such schemes can foster a sense of partnership and incentivize employees to actively contribute to the company's success.
8. Periodic Review: Establish a mechanism to periodically review and update the act to ensure its relevance and alignment with changing economic conditions and labor market dynamics. Regular assessments can help identify gaps and incorporate necessary reforms to enhance its effectiveness.
9. Public Awareness and Education: Conduct awareness campaigns to educate both employers and employees about their rights and obligations under the act. Promote voluntary compliance and create platforms for addressing queries and concerns related to the act's implementation.
10. Stakeholder Consultations: Involve relevant stakeholders, such as employers' associations, trade unions, and labor experts, in the review and amendment process. This would ensure that diverse perspectives are considered, and the revised act reflects a balanced approach.

By implementing these suggestions, it is possible to improve the implementation of the Payment of Bonus Act, 1965, making it more equitable, flexible, and in line with contemporary labor practices, while also addressing the concerns of employers and employees. The paper has critically analysed the historical importance of the payment of bonus in industries, on its evolution of calculation of the same, the features of the Payment of Bonus Act, 1965 on its computation of gross profits and surplus, eligibility of bonus, disqualification of payment of bonus, minimum payment of bonus, maximum payment of bonus, calculation of payment of bonus, the role of inspectors under the Act, the offences and penalty provisions, and finally the amendment made in 2015.