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THE CONCEPT OF BONUS

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THE CONCEPT OF BONUS

English jurisprudence is replete with a myriad examples of judge-made law - the foundation and edifice of that legal system is built around the tenet of precedents. Judge-made law is a rarer phenomenon in India and the credit of payment of an annual bonus to labour rests with the juridical initiative of the Industrial Court, Bombay, in 1948.

Early history

An ex-gratia payment by the textile industry of Bombay and Ahmedabad during the First World War years, with the industry booming, can be seen as the beginnings in India of the proliferation of the pay packet beyond earnings dependant on the hourly - rate or daily wage. Hidayatullah, J. of the Supreme Court described this payment in the words : "The payment of bonus had its origin in the generosity of the textile employers during the First World War when they voluntarily gave away 10 per cent (later upto 35 per cent) additional wages as 'war bonus'." ¹

Post-war slack led to resistance of the continuation of payment of "war bonus" by the textile industry. It was contended before the Bonus Dispute Committee headed by Sir John Mac leod, Chief Justice of the Bombay High Court, that payment of bonus for five consecutive years had led the workmen to look upon these annual payments as a part of their wages. The Committee did not accept this argument and concluded that there was no enforceable claim against the mill-owners and an annual payment of bonus could not be upheld by a Court of Law.

In 1931, the Whitely Commission dismissed the introduction of profit-sharing schemes : "Suggestions have been made from time to time that the difficulty (labour securing a just share of the results

of industry) by the general adoption of profit sharing schemes, but, this movement has made practically no progress in India, and in the present stage of industrial development, such schemes are unlikely to prove useful or effective."²

During the Second World War, in the wake of war-time conditions, industry made large profits and either through the intervention of Government as in the case of the textile industry of Bombay or through compulsory references to adjudication of trade or industrial disputes under the machinery set up by the Defence of India Act, bonus came to be recognised as payable out of profits. Mr Justice Chagla observed: "But the distribution of increased profits among workers is better achieved by giving an annual bonus than by further increase in wages."³

The Industrial Court, Bombay: Awards

In awarding the equivalent of 4½ months' basic wages in the dispute for bonus for 1948 in the textile industry of Bombay, the Court observed:

"Labour as well as the working capital employed in the industry both contribute to the profit made and both are, therefore, entitled to claim a legitimate return, out of profit, and such a legitimate return so far as labour is concerned, must be based on the living wage standard. It is, however, to be remembered that a claim to bonus might be admissible even if the living wage standard were completely attained. It may, therefore, be stated that so long as the living wage standard has not been attained the bonus partakes primarily of the character of the satisfaction, often partial and temporary of the deficiency in the legitimate income of the average worker in the industry, and that once such income has been attained it would also partake of the character of profit sharing. Owing to this dual character of bonus it would be a mistake to regard a demand for bonus as a demand

for profit-sharing pure and simple."⁴

TABLE 1

CONCEPT OF BONUS : Stage I

Efforts of labour + the use of Working Capital leads to Profit

Bonus justified to - 1. get to living standard wage and
2. as profit sharing.

It was when considering the question of bonus for 1949 of the textile industry in Bombay that the Industrial Court introduced the dictum of no profit-no bonus : "It may well be expedient from the point of view of industrial peace and progress to determine, the quantum of bonus industry-wise in a giver locality; but in the absence of any legislative provision enjoining upon us the obligation to direct even those mills that have not made profits but have suffered losses instead to pay bonus alike with those that have made profits, we do not think we would be adjudicating equitably in relation to the former if we direct them to pay bonus."⁵

TABLE 2

CONCEPT OF BONUS : Stage II

Efforts of labour + the use of working capital leads to Profit
No profit, no bonus.

Bonus justified to 1. get to living standard wage
2. as profit-sharing

The Labour Appellate Tribunal : Formula

If the awards of the Industrial Court, Bombay, were the embryo of the concept of bonus, what has variously been described as the LAT or Full Bench formula is the first shoot in the developing law governing the payment of Bonus. The Labour Appellate Tribunal in enunciating its formula was sitting in appeal against the award of the Industrial Court, Bombay, in the dispute for bonus of the textile industry of Bombay for the year 1949.

The Tribunal proceeded on the premise that since both labour and capital contributed to the earnings of an industrial concern, it was but fair that labour should derive some benefit provided there was surplus after meeting prior or necessary charges. The quantum of bonus must depend upon the relative prosperity of the concern during the year under review and would be reflected in the amount of residuary surplus of profits.

The first charge on gross profits should be the amount of money that would be necessary for rehabilitation, replacement and modernisation of machinery. The Tribunal was of the view that depreciation allowed under the Income-Tax Act was insufficient for this purpose as it only constituted a percentage of the written down value and would be insufficient for these purposes and needed to be augmented by an extra provision each year under "reserves".

The next charge on gross profits enjoined a fair return on capital, normally 6%, and on reserves employed as working capital, at a lower rate.

Distribution of surplus after these charges needed to bear in mind the three interests of the need of the employees, the claims of the

shareholders and the requirements of the industry itself. The Tribunal observed :

" The subject is not readily responsive to any rigid principle or precise formula, and so far we have not been able to discover a general formula. This does not, however, mean that the answer to this issue is in any way fortuitous Our approach to this problem is motivated by the requirement that we should ensure and achieve industrial peace which is essential for the development and expansion of industry. This can be achieved by having a contented labour force on the one hand, and on the other, an investing public who would be attracted to the industry by a steady and progressive return on capital which the industry may be able to offer. It goes without saying that if the residuary surplus is appreciably larger in any particular year it should be possible for the company to give a more liberal bonus to the employees."⁶

Whenever, there was "available surplus" after meeting the prior charges, bonus was paid and expressed as a percentage of the annual basic wage earning of workers.

Table 3

CONCEPT OF BONUS : Stage III			
Use of capital	} yielding profit	Prior charge 1	- Reserve for rehabilitation, replacement, modernisation
+		Prior charge 2	- Return on paid-up capital & reserves used as working capital.
Effort of labour		Bonus	- From available surplus, if any, bonus to labour to attain living standard wage and thereafter as profit sharing.

The Supreme Court on bonus

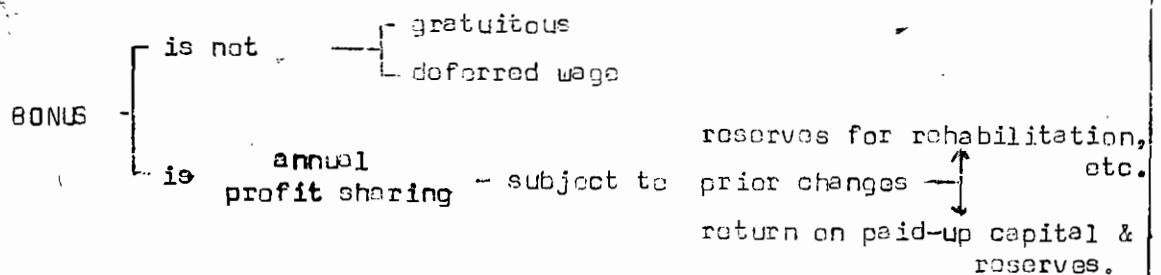
The Supreme Court had several occasions to consider the LAT formula. The highest Court of the land made it clear that bonus was not a gratuitous payment, that it was not a deferred wage but stipulated that where wages fall short of the living wage and industry was making a profit, a claim for bonus could be legitimately made by the workmen. The formula as enunciated by the LAT was generally accepted and the Supreme Court refused to revise the formula. Gajendragadkar, J. observed:

" If the legislature feels that the claim for social and economic justice made by labour should be redefined on a clearer basis, it can step in and legislate in that behalf."⁷

The LAT formula had no legislative recognition, nor was it based on "any strict theory of legal rights or obligations, it was intended to make an equitable division of distributable profits after making reasonable allocations for prior charges." "In essence, it was only a workable solution. It satisfied neither the employer nor the workmen. Disputes continued though the formula was generally adhered to": Hidayatallah, J. of the Supreme Court of India.¹

Table 4

CONCEPT OF BONUS : Stage IV



The Meher Commission and The Payment of Bonus Act, 1965

Continuous litigation, general dissatisfaction of both employers and labour, industrial strife and the refusal of the Supreme Court to examine afresh and alter the LAT formula, made the situation ripe for legislative intervention.

At the conclusion of the deliberations of the second and third meetings of the 18th session of the Standing Labour Committee, a Commission was set up under the Chairmanship of Shri M R Meher by the Government of India with very wide terms of reference.

Bonus received a niche in the statute books of the country following the Report of the Meher Commission, initially as an Ordinance promulgated by the President of India on May 29, 1965, later replaced by The Payment of Bonus Act, 1965.

The legislature had made several changes to the existing law on bonus :

a) Bonus would, henceforth, be payable to any employee earning less than Rs 1,600 per month, but, in calculating bonus payable in any year for those in receipt of salary or wages in excess of Rs 750 per month, it shall be calculated as if his monthly earnings were Rs 750 per month. For the purposes of determining bonus both basic wages and dearness allowance would be taken into reckoning.

b) A minimum bonus of 4% of eligible wages and a maximum of 20% were introduced. The principle of set-on and set-off for those years, where bonus was in excess of maximum or allocable surplus was insufficient to pay minimum bonus during a cycle of four years was introduced.

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c) A complicated formula starting with gross profits and providing for return on paid-up capital at 8%, reserves at 6% lead to the determination of available surplus of which 60% was distributable to labour as allocable surplus. The bonus payable was expressed as the percentage such allocable surplus bears to total eligible wages (this constitutes to total wage bill of all employees earning below Rs 750 + wage bill of all those earning over that figure pegged at Rs 750 per month).

Table 5

CONCEPT OF BONUS : Stage V		
Bonus payable	<ul style="list-style-type: none"> — minimum 4% whether there is profit, allocable surplus or not — of basic + d.a. not exceeding Rs 750 .m. — maximum 20% 	<ul style="list-style-type: none"> per annum but set-off and set-on available
Employer and employees can vary the formula and come to their own arrangements.		

d) Employers and employees were given the freedom to bargain and use any other formula in terms of provisions of Section 34 (3) of the Act.

An appraisal of the Concept of bonus upto 1965

From the five tables on the concept of bonus it is evident that a lot of confusion prevailed as to what was the precise nature of bonus.

Having defined bonus as an adjunct to obtain a living standard wage which when that standard was attained would take the nature of profit sharing, both the Industrial Court and the Labour Appellate Tribunal cloaked this payment with the dual characteristics of wage and profit-sharing, but, in excluding loss-making units from the purview slanted the concept in favour of profit sharing.

The Supreme Court, on the other hand, left no doubt as to what it was not - it was not an ex gratia payment and it was not deferred wage. It was annual profit-sharing.

The Payment of Bonus Act, 1965, in fixing a minimum bonus, whether there was profit or allocable surplus, removed the underlying concept of profit-sharing and extended it beyond an annual review on the performance of each year by introducing the principle of set-off and set-on. Bonus had become a continuous process. In allowing the dynamics of collective bargaining to evolve formulae different from the Act, the legislature had introduced a totally new dimension - there was no sacrosanct arithmetic any longer to determine the payment of bonus.

The accent of judicial redress was substituted with collective bargaining which often degenerated into violent and coercive bargaining with the law and order machinery and the administrative nexus for the resolution of industrial disputes playing a larger role in the resolution of conflicts which were to abound. An era of the annual tamasha of bonus had been ushered in.

Legislative changes since 1965

In September, 1972, the President of India promulgated an Ordinance raising minimum bonus to 8 1/3%. The Ordinance also provided that despite what the yield of bonus either under the Act was a result of any arrangement between the employer and the employee worked out to, bonus in excess of what was paid the previous year would be paid into the Provident Fund of the employee concerned.

Another Ordinance in 1975 was part of a package adopted by the Government of India to bring run-away inflation under control. No bonus was payable any longer in the absence of allocable surplus. Section 34 (3) which allowed bargaining between the parties to evolve any formula other than the one under the Act, was removed. Payment beyond what was worked out under the Schedule to the Act received penal treatment under the provisions of the Income Tax Act - such payments could not be deducted as expenditure.

At the end of the decade after the Payment of Bonus Act had become a part of the law of the land, the concept of Bonus had taken a full circle, turned volte face and gone back to the initial definition of the concept of profit-sharing, shedding any **link** with wages and the eternal and unrewarding **chase** of catching up with the living wage.

Table 6

THE CONCEPT OF BONUS : Stage VI

BONUS is profit sharing dependent on allocable surplus each year - the principle of set-on and set-off over a cycle of years providing a link between the past and the future.

Having done away with Section 34 (3), an amending Act brought in a link with production and productivity in lieu of bonus based on profits payable under the Act. Under a mutual agreement both employer and employee could substitute a production/productivity agreement provided payments do not exceed 20% of the salary/wage earned during the year.

[Table 7]

THE CONCEPT OF BONUS : Stage VII

BONUS

is profit sharing dependant on allocable surplus each year subject to a maximum of 20% of salary/wages

Can partake the nature of production/productivity payments subject to a maximum of 20% of salary/wages.

The views of the Profit Sharing Committee consisting of representatives of employers, employees and Government set up in May 1948 had this to say :

" For one thing, profits made by industry depend on many factors besides labour, and to that extent, do not bear any measurable relation to what labour does or does not do. An undertaking in which labour has performed its full part might fail to make any profits because of other reasons while large profits might be made in spite of irregularities or slackness of labour. Conditions of production vary from industry to industry and from undertaking to undertaking within each industry. The productivity of labour is dependant among other things, on the nature

of equipment and the efficiency of organisation and supervision. Then, again, the measurement of total production in terms of a common unit is a very difficult task. Even the final products of an industry or undertaking are not always uniform and easily measurable. To prescribe a norm of annual production is even more difficult. Further the basic conditions in any one year may be quite different from the conditions on which the norm has been determined. The production equipment might have increased or diminished or improved or deteriorated in the meantime. The size and composition of the labour force might similarly have changed. There may be involuntary interruptions for which no one is responsible. To compare actual production in any given year with the norm would, therefore, be extremely unscientific and unsatisfactory. To compare total production in any industry with the normal total production of that industry would be even more unsatisfactory basis, as the number of working units in the industry might itself vary from year to year."⁸

The voice echoing back from nearly three decades ago, truly summarises the problems of vagaries of linking productivity or production in lieu of bonus and is as true today as it was when propounded in 1948. Any attempt to resolve the divergent needs of increased norms of productivity, so dear to the heart of the employer; more earnings without any tangible increase in efforts, so cherished by the individual worker and groups of workers; and the national aspirations to eradicate unemployment in a determined span of time are so **irreconcilable** that any pot-pourri evolved in bi- or tri-partite negotiations must lead to a totally unsatisfactory compromise of dubious distinction.

The changes in 1977

8 1/3 per cent of eligible wages is to be paid to employees whether there is any allocable surplus or not or where allocable surplus is below the requirement to disburse this amount. Where the allocable

surplus exceeds this amount, collective bargaining can be resorted to determine the formula for disbursement which in any event shall not exceed 20%. Has the mismatched alliance of production/productivity been torn asunder? To follow independent paths or are still united as an escape for a different formula to pay bonus between 8 1/3 and 20 per cent.

Table 8

THE CONCEPT OF BONUS : Stage VIII

Bonus

8 1/3% distributable as minimum irrespective of allocable surplus being absent or below that level

maximum 20%. Between 8 1/3 and 20%.

By collective bargaining

By production/productivity agreements.

CONCLUSION :

In a short span of thirty years or less the concept of bonus has undergone several changes. The initial confusion of whether it was payable in the absence of profit or partook in the nature of any link with wages was cleared by the Supreme Court. The introduction of the concept of minimum bonus when there was no allocable surplus put a stamp of legislative sanction to the claims of labour that bonus was deferred wage. Legislation

extended an annual review to a balance-sheet covering a span of years by introducing set-on and set-off. The shift from judicial resolution of disputes to the collective bargaining table ensued. A full circle of change was completed when the 1975 Ordinance took the payment of bonus back to the concept of profit sharing by providing that no allocable surplus - no bonus. Simultaneously, a link with production/productivity was also attempted. And in 1977 one can read the beginnings of a policy that concedes 8 1/3% as deferred wage; payments between 8 1/3 and 20%, allocable surplus being adequate and over what is needed to pay 8 1/3, as at the mercy of collective bargaining. This leaves the fate of the issue in the hands of employer and labour. What price is industry willing to pay for peace? How much is labour prepared to sacrifice by way of loss of wages?

The thorny path of bonus is not yet out of the vicissitudes that have dogged it since the judges of the land bestowed the right to a lump-sum payment each year to the employees of industry. Clarity in the definition of the concept of bonus is of paramount importance and as a nation we cannot afford so many changes in the life time of a worker and in a single generation as we have witnessed in thirty years or less. The annual bone of contention between employer and employee must rest for some years on an inflexible definition of the concept as provided by the legislature.

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