Board / Audit Committee One-Pager

ESIC under Code on Social Security – Risk, Direction & Readiness

Why this matters now

Employees' State Insurance Corporation has, through its 30 December 2025 notification, confirmed that the Code on Social Security, 2020 (CoSS) is operational for ESIC purposes from 21 November 2025, replacing the ESI Act, 1948 as the governing statute.

This marks a shift in legal interpretation, even though operational mechanics are still evolving.

What has changed

Area	Earlier Position	Current Direction
Governing law	ESI Act, 1948	Code on Social Security, 2020
Wage interpretation	Practice & periodicity driven	Statutory definition + 50% cap
Allowance structuring	Broad flexibility	Structurally constrained
ESIC coverage	Relatively static	Directionally expanding
Enforcement style	Act-centric	Code-centric

Key risk exposure

- Allowance-heavy salary structures are more vulnerable
- Employees earlier kept outside ESIC may become coverable
- Legacy interpretations under the ESI Act may not hold in future inspections

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What the notification does not do

- No retrospective liability creation
- No immediate wage restructuring mandate
- No revised wage ceiling notification yet

Recommended Board posture

✓ Maintain current compliance
✓ Document wage rationale
✓ Prepare payroll systems for Code-based computation
✓ Avoid aggressive structuring in new compensation designs

Bottom line: This is a transition phase, not a disruption phase. Preparedness now prevents enforcement risk later.

Worked Numerical Illustration

Old ESIC vs Code-Based ESIC (Practical Example)

Example 1 – Allowance-heavy structure

Salary Structure (Monthly)

Component	Amount (₹)
Basic	12,000
HRA	10,000
Conveyance	4,000
Special Allowance	14,000
Gross Salary	40,000

Old ESIC (Act-based practice)

- Included: Basic + HRA + Special Allowance
- Excluded: Conveyance
- ESIC wages ≈ ₹36,000
- Employee kept outside coverage due to structuring / practice

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Code on Social Security reading

- Total remuneration: ₹40,000
- Excluded items aggregated (HRA + Conveyance + part of Special Allowance): ₹28,000
- 50% of total remuneration = ₹20,000

➞Excess exclusion = ₹8,000
➞Deemed wages increase by ₹8,000

Revised ESIC wage base ≈ ₹28,000

Impact:
Employee earlier outside ESIC may now fall within coverable wage logic, depending on ceiling notification.

Example 2 – Balanced structure

Component	Amount (₹)
Basic + DA	22,000
HRA	8,000
Conveyance	2,000
Incentive (quarterly)	8,000
Gross	40,000

- Exclusions within 50% cap
- No deemed addition
- Minimal change in ESIC exposure

Key takeaway from examples

❌ESIC wages are not automatically 50% of gross
✅The ability to suppress ESIC wages through exclusions is reduced

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Client-Ready Advisory

ESIC & Code on Social Security – What Employers Need to Know Now

The Employees' State Insurance Corporation (ESIC) has issued a notification dated 30 December 2025, confirming that the Code on Social Security, 2020 is now the governing legislation for ESIC, effective 21 November 2025.

While earlier ESIC advisories over the past year had created mixed signals — some of which were later clarified or diluted — this notification represents a post-implementation position and therefore carries greater legal significance.

How ESIC wages were earlier understood

Under the ESI Act, wage determination evolved through practice:

- Regular monthly payments were included
- Non-monthly or deferred payments were often excluded
- Periodicity and linkage to the wage cycle were decisive

This allowed allowance-heavy structures to remain administratively viable.

What changes under the Code

The Code introduces:

- A statutory definition of wages
- Aggregation of exclusions
- A 50% cap on excluded components

This fundamentally reduces the scope for exclusion-driven structuring.

Will ESIC coverage increase

Not automatically. However:

- Some employees earlier outside coverage may become coverable
- Exposure depends on actual wage composition
- Artificial allowance splitting is now structurally discouraged

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When should employers act

Immediate actions

- Review wage structures internally
- Document current ESIC computation logic
- Prepare payroll systems for Code-based calculations

What can wait

- Full restructuring of legacy salaries
- Retrospective recomputation

When restructuring becomes necessary

Once ESIC issues:

- revised wage ceilings, or
- contribution computation rules under CoSS, or
- inspection orders applying Code wages directly

Karma's counsel view

This is a regulatory transition, not a compliance shock.
Employers who treat this phase as a preparation window will be best placed when ESIC enforcement fully aligns with the Code framework.