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Reforming Gratuity Rights in India: A Critical Study of the One-Year Rule for Fixed-Term Workers under the Code on Social Security 2020

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Gratuity has long been treated in India as a reward for loyalty and long service, payable only after an employee completes five years of continuous work with one employer. This rule, contained in the Payment of Gratuity Act 1972, left out a large and growing section of the workforce, namely fixed-term and contractual workers, who rarely stay with one employer for five years, even though they contribute the same effort as permanent staff. The Code on Social Security 2020 attempts to correct this gap. Section 53 of the Code retains the five-year rule for regular employees. Still, it creates a separate, much shorter path for fixed-term employees, who may become eligible for gratuity on a proportionate basis after completing just one year of service, or on the expiry of their contract, whichever the law is read to intend. This paper examines the historical background of gratuity law in India, the reasons behind the introduction of the one-year rule, and the manner in which Section 53 has been drafted. It argues that while the reform is a welcome and overdue step toward treating fixed-term workers fairly, its language is unclear on the precise trigger for eligibility, its implementation has been delayed because States have not framed matching rules, and its benefits may be limited by the continuing exclusion of small establishments and by the risk that employers structure contracts to fall just short of one year. The paper closes with concrete suggestions, including an anti-avoidance rule for repeated short-term contracts, a firm timeline for State rulemaking, and simpler guidance on calculating pro rata gratuity, so that the promise of the 2020 reform is not lost in practice.

Keywords: *gratuity, fixed-term employment, continuous service, labour codes.*

INTRODUCTION

Gratuity is a payment made by an employer to an employee in recognition of years of service to the organisation. It is neither a bonus nor part of regular wages. It is meant to be a lump-sum benefit paid at the end of service, usually at retirement, resignation, or death, so that a worker who has spent a large part of their working life with one employer does not leave empty-handed. The Supreme Court explained this purpose long ago, holding that the purpose of gratuity is to provide a measure of financial security to a worker after years of service, almost as an acknowledgement of the contribution made to the establishment's growth.[1]

For nearly five decades, gratuity in India was governed almost entirely by the Payment of Gratuity Act, 1972. Under this Act, an employee had to complete five years of continuous service with the same employer before becoming eligible for gratuity. This condition worked reasonably well when most jobs were permanent, but it left out an increasing number of workers who were hired for a fixed period, through contractors, or on short, renewable contracts.[2] Such workers rarely completed five years with one employer, not because they contributed less, but because their engagement was inherently temporary.

The Government of India, through the process of labour law reform that began around 2019, merged twenty-nine central labour laws into four Codes: The Code on Wages, 2019, the Industrial Relations Code, 2020, the Occupational Safety, Health and Working Conditions Code, 2020, and the Code on Social Security, 2020. The Code on Social Security, 2020, replaced nine earlier social security laws, including the Payment of Gratuity Act, 1972, the Employees' Provident Funds and Miscellaneous Provisions Act, 1952, the Employees' State Insurance Act, 1948, and the Maternity Benefit Act, 1961, bringing them under a single consolidated statute.[3] While Parliament passed the Code in September 2020, it was brought into force across the country only later, with the Central Government notifying 21 November 2025 as

[1] *Delhi Cloth and General Mills Co Ltd v Their Workmen & Ors Etc* (1970) AIR 919; *Indian Hume Pipe Co Ltd v Its Workmen & Anr* (1960) AIR 251

[2] 'Code on Social Security, 2020: Towards Universal and Inclusive Social Protection' (*Press Information Bureau,* 22 November 2025) <https://www.pib.gov.in/FactsheetDetails.aspx?Id=150473&reg=3&lang=2> accessed 19 June 2026

[3] Code on Social Security 2020

the date on which all four Labour Codes finally took effect. The delay itself became a subject of debate, since the Rules required for smooth implementation were still being finalised by several States even after the Central notification.[4]

One of the most discussed changes introduced by the Code is in Section 53, which addresses gratuity payments. While the section keeps the old five-year rule for most employees, it adds a special, much shorter path for a category of workers called "fixed-term employees". Under this new rule, a fixed-term employee, someone hired under a written contract for a defined period, becomes eligible for gratuity after completing one year of service and receives the amount on a proportionate basis, rather than waiting five years or losing the benefit altogether when the contract ends. This is a significant departure from the position under the 1972 Act, where fixed-term or contractual employees whose service ended before five years received no gratuity at all, regardless of how long or how productively they had worked.[5]

This paper closely examines the one-year rule. It asks three questions. First, why was the rule introduced, and what problem was it meant to solve? Second, how exactly does Section 53 work, and is its language clear enough to be applied without confusion? Third, does the rule, as drafted and as implemented, actually deliver the protection it promises, or does it create new gaps and opportunities for employers to avoid liability? The paper argues that the one-year rule is a necessary and fair correction to a long-standing anomaly in Indian labour law, but that its current drafting and the slow pace of State-level implementation mean that its benefits are, for now, only partly realised. The paper concludes with specific suggestions for making the rule clearer and more effective.

HISTORICAL AND LEGAL BACKGROUND OF GRATUITY IN INDIA

Before 1972, gratuity payments in India were governed by a mix of State laws, industry-specific settlements, and judicial awards, with no single national standard. The Supreme Court had, through a series of industrial disputes, tried to bring some consistency to the

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[4] Jay Mehta 'Gratuity promise delayed: New labour laws spark confusion, employees wait as states suspend regulations' (*Whalesbook,* 24 December 2025) <https://www.whalesbook.com/news/Telugu/economy/Gratuity-Promise-Delayed-New-Labour-Laws-Spark-Confusion-Employees-Wait-as-States-Hold-Back-Rules/694bcab3e10c98d0787b1ac3> accessed 19 June 2026

[5] Sheena Ogra and Anirudh Agarwal, 'The Code on Social Security 2020: Addressing the Key Changes and Their Impact' (*Ahlawat and Associates,* 30 January 2023) <https://www.ahlawatassociates.com/blog/code-on-social-security> accessed 19 June 2026

practice. Still, real uniformity came only when Parliament passed the Payment of Gratuity Act in 1972, which came into force on 16 September 1972.[6] The Act applied to every factory, mine, oilfield, plantation, port, and railway company, and to every shop or establishment employing ten or more persons on any day in the preceding twelve months.

Section 4(1) of the 1972 Act laid down the central rule: gratuity becomes payable to an employee on termination of employment after the employee has rendered continuous service for not less than five years. The only exceptions were termination by death or disablement, where the five-year requirement did not apply. The Act defined "continuous service" in Section 2A, treating a year of work as complete even if there were breaks due to sickness, accident, authorised leave, or absence without leave that had not been treated as a formal break in service under the employer's rules.[7] For an employee who had not worked every single day of the year, the Act still deemed the year to be "continuous" if the employee had actually worked at least 240 days in ordinary establishments, or 190 days in the case of mining work or establishments working fewer than six days a week.[8]

This five-year threshold and the manner of its calculation generated a fair amount of litigation. Employers sometimes argued that an employee who had not completed the full five years, even by a matter of days, was not entitled to any gratuity, leading to hardship in individual cases. Courts have generally read the continuous service requirement strictly but fairly, giving employees credit for authorised absences and for years in which they crossed the 240-day mark, while denying credit for years in which attendance fell below that mark. Commentators have long pointed out that the exact interaction between the "five years" language in Section 4(1) and the 240-day rule in Section 2A(2) has never been free of confusion, forcing authorities to interpret the two provisions together on a case-by-case basis.[9]

What the 1972 Act never addressed, because such arrangements were far less common at the time, was the position of an employee hired for a fixed term from the outset, someone whose

[6] Payment of Gratuity Act 1972
[7] Payment of Gratuity Act 1972, s 2A
[8] Payment of Gratuity Act 1972
[9] Chirag Mittal, 'The Jurisprudence Of Gratuity: Deconstructing The Minimum "Continuous Service" Requirement For Payment Of Gratuity' (2025) 7(3) IJLLR <https://www.ijllr.com/post/the-jurisprudence-of-gratuity-deconstructing-the-minimum-continuous-service-requirement-for-payme> accessed 19 June 2026

contract was designed to end well before five years had passed. Such a worker, however hard they worked and however many contracts they completed one after another, fell entirely outside the gratuity net unless a fresh contract was treated as continuous with the earlier one. As short-term and contractual hiring grew in the following decades, this omission became increasingly difficult to justify.

THE CHANGING NATURE OF EMPLOYMENT: FIXED-TERM WORK AND THE CASE FOR REFORM

Over the last two decades, Indian employers across manufacturing, services, and information technology have increasingly moved away from hiring only permanent staff. Instead, many positions are now filled through fixed-term contracts, contract labour supplied by staffing agencies, and, more recently, gig and platform-based engagements. This shift gives employers the flexibility to match staffing to demand and gives some workers access to jobs they might not otherwise get. Still, it also means that a large part of the workforce never accumulates the long, unbroken service that the 1972 Act rewarded.

The law had already begun to respond to this shift before the 2020 Codes. In 2018, the Central Government amended the Industrial Employment (Standing Orders) Act, 1946, to formally recognise "fixed-term employment" as a distinct category and to require that fixed-term employees receive the same hours of work, wages, and statutory benefits as permanent employees performing similar work. However, this 2018 amendment did not itself change the gratuity threshold, so a fixed-term worker could, in theory, be entitled to parity in pay and other benefits while still being denied gratuity simply because the five-year condition under the 1972 Act had not changed. This gap between the promise of parity and the reality of the gratuity rule was one of the specific problems the Code on Social Security, 2020, was designed to close.

The policy rationale for extending gratuity to fixed-term workers rests on a simple idea of fairness: a worker's entitlement to a share of the value created over years of work should not depend on the label attached to the employment contract. Two workers doing the same job, one permanent and one on a fixed-term contract, should not be treated so differently merely because one was hired under a contract designed to end early. Denying gratuity to fixed-term staff also created a perverse incentive for employers to prefer fixed-term hiring specifically to avoid gratuity liability, rather than for genuine business reasons. The 2020 reform was intended to remove this incentive.

THE CODE ON SOCIAL SECURITY, 2020: STRUCTURE AND SECTION 53

The Code on Social Security, 2020, is a consolidating statute. It brings together provisions on provident fund, employee state insurance, maternity benefit, gratuity, and, for the first time, a framework for social security for gig workers, platform workers, and unorganised sector workers. Chapter V of the Code, titled "Gratuity", deals specifically with this benefit, and Section 53 sets out the conditions under which gratuity becomes payable.[10] The Code defines a fixed-term employee as a person engaged based on a written contract of employment for a fixed period, and it requires that such an employee receive the same hours of work, wages, allowances, and other benefits as a permanent employee doing comparable work, on a basis proportionate to the period actually served.

Section 53(1) largely repeats the old five-year rule for the general workforce: gratuity is payable to an employee on termination of employment after the employee has rendered continuous service for not less than five years, whether that termination happens on superannuation, retirement, resignation, or death or disablement, in which case the five-year condition does not apply. Journalists continue to have a shorter three-year threshold, reflecting the position under the earlier Working Journalists Act.[11] What is new is the specific treatment of fixed-term employees. The Code adds that the requirement of five years of continuous service does not apply where the employee's exit is due to the expiry of a fixed-term contract. Industry commentary and the draft central rules explain that a fixed-term employee becomes entitled to gratuity, on a proportionate basis, once the employee has rendered at least one year of service under that contract. One illustration commonly used to explain the resulting calculation involves an employee on a twenty-one-month fixed-term contract: at the end of the contract, gratuity is worked out using the ordinary formula of fifteen days' wages for each completed year of service, and then further adjusted proportionately to reflect the exact period served, so that a worker who completes twenty-

[10] Code on Social Security 2020, s 53
[11] Code on Social Security 2020, s 53(1)

one months out of a notional two-year comparison period receives a corresponding fraction of the two-year entitlement rather than the full amount or nothing at all.[12]

This is a genuinely new right. Under the 1972 Act, a fixed-term worker who left after twenty-one months, however hard they had worked, would have received no gratuity whatsoever, because the flat five-year threshold offered no partial credit. Under the Code, the same worker now has a clear statutory claim, calculated proportionately, once at least a year has been completed. The introduction of pro-rata payment, rather than an all-or-nothing five-year cliff, is arguably as important a change as the reduction of the qualifying period itself.

Implementation, however, has not been smooth. The four Labour Codes, including the Code on Social Security, were notified as being in force from 21 November 2025, but the detailed rules needed to operationalise many of its provisions, including forms for claiming gratuity and procedural requirements for employers, are framed separately by the Central Government and by each State Government under their respective rule-making powers. As of the end of 2025, several States had not yet notified their own rules, and this created genuine confusion in the market: some employers treated the one-year gratuity right for fixed-term staff as not yet legally binding until State rules were notified, while labour law commentators argued that the substantive right itself came into force with the Code, and that States could only prescribe procedural detail, not withhold the entitlement.[13] This gap between what the law says on paper and what is actually being paid to workers on the ground is one of the central practical problems examined in the next section.

CRITICAL ANALYSIS OF THE ONE-YEAR RULE

Positive Aspects of the Reform: Correcting a Long-Standing Unfairness: The most important achievement of Section 53 is that it finally aligns the gratuity law with the reality of modern employment. Fixed-term workers who put in genuine, productive years of service no longer walk away with nothing simply because their contract was structured to end before five years. This brings gratuity law closer to the constitutional direction set out in Articles 39,

[12] 'Social Security Code, 2020: Impact on Gratuity Liability' (*InsurTech Actuary*) <https://itactuary.com/learn/social-security-code-2020-impact-on-gratuity-liability/> accessed 19 June 2026

[13] Riya Kapoor, 'Gratuity Twist: New Labour Codes Spark Confusion – Is 1 Year Now Enough?' (*Whalesbook*, 13 December 2025) <https://www.whalesbook.com/news/English/economy/Gratuity-Twist-New-Labour-Codes-Spark-Confusion-Is-1-Year-Now-Enough/693d3de462283e60493713d0> accessed 19 June 2026

41, and 42 of the Constitution, which call upon the State to secure just and humane conditions of work and to provide for a worker's basic economic security.

Reduced Incentive to Misuse Fixed-Term Hiring: When fixed-term and permanent workers are entitled to gratuity on materially similar terms, adjusted only for the length of service actually rendered, an employer has less reason to prefer fixed-term contracts purely as a device to avoid gratuity liability. This supports the broader purpose of the 2018 Standing Orders amendment, which sought parity between fixed-term and permanent staff but had left this particular gap unaddressed until now.

Recognition of a Shift already Underway: By formally defining fixed-term employment and building a gratuity pathway around it, the Code acknowledges a hiring pattern that has existed in practice for years without adequate legal recognition. In doing so, it moves Indian labour law a step closer to international practice, since instruments such as the International Labour Organisation's standards on non-discrimination for workers with atypical contracts, and comparable rules in other jurisdictions such as the European Union's Fixed-Term Work Directive, are built on the same underlying principle that a worker's entitlements should not be reduced merely because of the type of contract used to hire them.

CONCERNS AND GAPS IN THE PRESENT FRAMEWORK

Lack of Clarity on the Precise Trigger for Eligibility: Reading Section 53 alongside secondary commentary and the draft rules reveals a real ambiguity: is a fixed-term employee entitled to gratuity purely upon completing one year of service, in the same way a permanent employee becomes entitled after five years, or is the entitlement tied specifically to the expiry or termination of the fixed-term contract, with one year being simply the minimum period that the employee must have served? Different commentators have read the provision differently, and news reports from around the time the Codes came into force show that even industry experts were divided on whether gratuity is now payable to all employees after one year, or only to fixed-term employees on a pro rata basis when their contracts end. This is not a small drafting issue. If eligibility depends on contract expiry, an employee whose one-year fixed-term contract is not renewed has a clear claim, but an employee on a three-year fixed-term contract who is only one year into that contract does not yet have an accrued right and must wait for the contract to end or be terminated. If, instead, the right accrues solely upon completing one year of continuous service, regardless of when the contract ends, the practical effect is considerably broader. The absence of a single, unambiguous reading invites litigation of exactly the kind that surrounded the 240-day rule under the old Act for decades.[14]

Delay and Inconsistency in State-Level Implementation: Labour is a subject on the Concurrent List, and both the Central Government and State Governments have rule-making power under the Code. The Central Government notified the Code as in force from 21 November 2025, but many States had still not issued their own implementing rules months later. This created a situation where the legal right technically existed, but employers, uncertain about compliance obligations and fearing inconsistent enforcement, continued applying the old five-year rule in practice. For a worker whose fixed-term contract ends during this transition period, the gap between an entitlement that exists on paper and a benefit that is actually paid is not an abstract problem; it is the difference between receiving gratuity and receiving nothing.

Continuing Exclusion of Small Establishments: Gratuity under the Code, as under the 1972 Act, applies only to establishments employing ten or more persons. Many fixed-term and contractual workers are engaged precisely in smaller establishments and by smaller contractors, where the threshold is not met. As long as this threshold remains unchanged, a significant share of the very workforce the one-year rule was designed to protect continues to fall outside its coverage altogether, regardless of how the eligibility trigger under Section 53 is finally interpreted.

Risk of Contract Structuring to Avoid Liability: A predictable employer response to any bright-line threshold is to design contracts that fall just short of it. Just as the five-year rule under the 1972 Act sometimes led to employees being eased out shortly before the fifth year, a poorly monitored one-year rule for fixed-term staff creates a similar risk at a shorter time scale: contracts fixed at eleven months, or repeated short-term renewals with brief gaps in between, could be used to prevent any single spell of service from ever reaching the one-year mark. Without a specific anti-avoidance provision treating repeated, back-to-back fixed-term

[14] 'Gratuity Calculator: Fixed-Term Employees Eligibility & Pro-Rata Rules' (*Bhatt & Joshi Associates,* 15 May 2026) <https://bhattandjoshiassociates.com/the-gratuity-conundrum-for-fixed-term-employees/> accessed 19 June 2026

contracts with the same employer as continuous service, the protective purpose of Section 53 can be defeated through careful contract drafting.

Complexity in Computing the Proportionate Amount: The ordinary gratuity formula, fifteen days' wages for each completed year of service, was designed for employees who complete whole years of service, typically well beyond five years. Applying this formula on a pro-rata basis to fixed-term employees who may serve for periods such as fourteen months, twenty-one months, or two and a half years requires further clarification, particularly regarding how partial years beyond six months are treated, and how the definition of "wages" under the Code, which now includes a rule requiring at least fifty per cent of total remuneration to be treated as wages for this purpose, interacts with the gratuity calculation. Without clear worked examples in the rules themselves, employers and workers are left to rely on illustrative calculations published by private commentators rather than authoritative guidance.

Silence on Transitional Cases: The Code does not clearly address how service rendered under a fixed-term contract that began before 21 November 2025 but continues or ends after that date should be treated for the one-year count. Nor is it clear how the one-year rule for fixed-term staff interacts with the shorter three-year rule already available to journalists, or with the special 75 per cent attendance rule that applies to seasonal establishments. These are not hypothetical difficulties; they are the kind of first-generation disputes that typically arise whenever a new statutory threshold replaces an older one.

Weak Practical Enforcement for a Vulnerable Group: Fixed-term and contractual workers, almost by definition, have less bargaining power and job security than permanent staff and are less likely to pursue a legal claim against a former employer for a relatively modest gratuity, particularly once the contract has ended. The working relationship is over unless the Code's inspection and penalty machinery is used proactively to check employer compliance with the one-year rule, rather than relying on individual workers to file claims; the right created by Section 53 risks becoming, for many fixed-term workers. This right exists on paper more than in practice.

A BRIEF COMPARATIVE NOTE

India is not alone in trying to close the gap between the protections available to permanent and non-permanent staff. The European Union's Fixed-Term Work Directive of 1999 is built around a clear principle of non-discrimination: a fixed-term worker should not be treated less favourably than a comparable permanent worker purely because of the fixed-term nature of the contract, unless the difference in treatment is justified on objective grounds. That Directive also requires member States to introduce at least one of several measures to prevent abuse arising from the use of successive fixed-term contracts, such as setting a maximum total duration for such contracts or a maximum number of renewals. The International Labour Organisation's standards on termination of employment likewise encourage member States to ensure that workers on contracts of limited duration are not deprived of protections available to other workers without an objective justification.

The comparison is useful because it shows that the core idea behind Section 53, extending gratuity to fixed-term staff, is consistent with international practice and is, in principle, the right direction for Indian law to move in. What Indian law currently lacks, and what the comparative examples highlight, is the second element that usually accompanies such reforms: a specific anti-avoidance mechanism aimed at repeated or artificially short fixed-term contracts. Without such a mechanism, the substantive right created by Section 53 remains only as strong as an employer's willingness to comply with it in good faith.

SUGGESTIONS FOR REFORM

A Single, Unambiguous Eligibility Rule: The Central Rules under the Code should state, in plain and specific terms, whether a fixed-term employee's right to gratuity accrues on completing one year of continuous service, irrespective of whether the contract has ended, or only on the expiry or earlier termination of the contract, provided at least one year has been served. A single clear rule, applied uniformly, would remove the present confusion and reduce the scope for inconsistent employer practice and future litigation.

A Firm Timeline for State Rule-Making: Since the substantive entitlement under a Central Code cannot fairly be left dependent on the pace at which individual States frame their own procedural rules, the Central Government should consider prescribing a maximum period within which States must notify their own procedural rules after a Code comes into force, together with a default rule that Central procedures apply in any State that has not notified its own rules within that period. This would prevent the kind of prolonged uncertainty seen through late 2025 and into 2026.

An Anti-Avoidance Provision for Successive Short Contracts: The Rules should specifically provide that where an employee is engaged by the same employer under two or more fixed-term contracts with only a brief gap between them, the periods of service should be added together for the one-year threshold, rather than treated as separate spells of employment. This would directly address the risk of employers using repeated eleven-month contracts to defeat the purpose of Section 53, in the same way the European Union's Fixed-Term Work Directive addresses the risk of abuse through successive contracts.

Gradual Extension of Coverage to Smaller Establishments: Given that many fixed-term workers are employed in establishments with fewer than ten workers, the Government should examine a phased reduction of the coverage threshold, at least for the specific purpose of fixed-term gratuity, so that the benefit is not concentrated only among workers in larger organisations.

Published Worked Examples for Pro-Rata Computation: The Rules, or accompanying official guidance, should include clear worked examples showing exactly how the fifteen-days-per-year formula is to be applied on a pro-rata basis for common contract lengths, such as one year, eighteen months, and two years, so that both employers and workers can calculate the correct amount without depending on private commentary of uncertain accuracy.

Stronger Proactive Enforcement and Awareness: The labour inspection machinery under the Code should be directed to verify compliance with fixed-term gratuity requirements during routine inspections, rather than relying solely on individual worker complaints. Alongside this, the Government should run targeted awareness campaigns for fixed-term and contractual workers, many of whom may not yet know this new right exists, so that the benefit created by Section 53 is actually claimed rather than quietly lost.

CONCLUSION

The one-year gratuity rule for fixed-term employees under Section 53 of the Code on Social Security, 2020, addresses a genuine and long-standing gap in Indian labour law. For decades, the five-year rule under the Payment of Gratuity Act, 1972, quietly excluded a growing section of the workforce from a basic retirement benefit, not because they worked less, but because their contracts were structured to end early. By extending proportionate gratuity to fixed-term workers after just one year of service, the Code brings the law closer to the reality of how people are employed today and to the constitutional promise of just and humane conditions of work.

At the same time, this paper has shown that the reform, as currently worded and implemented, is not yet complete. The precise trigger for eligibility remains open to more than one reading; several States have been slow to notify the rules needed to make the right enforceable in practice, small establishments remain outside the gratuity net altogether, and nothing in the present framework specifically prevents employers from structuring contracts to fall just short of the one-year mark. None of these problems is difficult to fix. Clearer rules, a firm timeline for States, a simple anti-avoidance provision for successive contracts, and better enforcement and awareness would go a long way toward making sure that the one-year rule delivers, in practice, the protection it promises on paper. Until these steps are taken, the reform will remain a right that exists, but one that many of the workers it is meant to protect may never actually receive.