Gratuity

A lump-sum reward for long service, (15 ÷ 26) × last salary × years.

Up to ₹20 lakh tax-free | Tax-free up to ₹20 lakh

What is Gratuity?

Gratuity is a lump sum your employer pays you as a thank-you for long service, now governed by the Code on Social Security, 2020, which replaced the Payment of Gratuity Act from 21 November 2025. Permanent employees become eligible after five years of continuous service (fixed-term employees after one year), and the amount is (15 ÷ 26) × your last monthly wages × years of service. It's tax-free up to ₹20 lakh in the private sector, a meaningful, often-overlooked part of your retirement kitty.

In brief

Suits	Employees with 5 years' continuous service; fixed-term employees after 1 year (labour codes, Nov 2025).
You get	15 days' last wages for each year of service; allowances above 50% of pay now count towards wages.
Your money	Paid by the employer on leaving, retirement, death or disability.
Tax	Tax-free up to ₹20 lakh for private-sector employees; government employees have a higher limit.
Watch for	Keep your nomination with the employer up to date.

Key facts

Formula	(15 ÷ 26) × last monthly wages × years of service
Eligibility	5 years of continuous service (waived on death/disability)
Tax-free cap	₹20 lakh (private sector); fully exempt for government staff
Paid by	Employer, within 30 days of it becoming due
Covered by	Code on Social Security, 2020 (since 21 Nov 2025)

What's new

Nov 2025 The four labour codes took effect on 21 November 2025. Gratuity now falls under the Code on Social Security; fixed-term employees qualify after one year, and if allowances exceed 50% of pay the excess counts towards the wages used for gratuity.

Questions and answers

THE BASICS

What is gratuity?

Gratuity is a statutory lump-sum benefit paid by an employer to an employee for rendering long, continuous service, on resignation, retirement, or exit after at least five years. It's a reward for loyalty, not a deduction from your salary, and is over and above your provident fund.

How is gratuity calculated?

For establishments covered by the Code on Social Security (earlier the Payment of Gratuity Act), the formula is: (15 ÷ 26) × last monthly wages (basic + DA, plus any allowances above 50% of pay) × completed years of service. The "15/26" represents 15 days' wages for each year, based on a 26-day working month. Our calculator applies this and the ₹20 lakh cap.

What counts as "salary" in the formula?

Under the labour codes, gratuity uses "wages": basic pay plus DA (and retaining allowance). If allowances such as HRA make up more than 50% of total pay, the excess is added back to wages, which can raise gratuity. It is the last drawn figure, which is why gratuity grows with tenure.

ELIGIBILITY

When do I become eligible for gratuity?

After completing five years of continuous service with the same employer. The five-year condition is waived if service ends due to the employee's death or disablement, in those cases gratuity is payable regardless of tenure.

How are partial years counted?

A year is counted as completed if you've worked it fully. For the final part-year, many establishments (and court rulings) treat service of 6 months or more as a full year and less than 6 months as ignored, so 7 years 8 months counts as 8 years. Our calculator uses whole years; adjust if your employer rounds.

TAX

Is gratuity taxable?

For private-sector employees covered by the Act, gratuity is tax-free up to ₹20 lakh (a lifetime limit across employers); anything above is taxable at slab. For government employees, gratuity is fully exempt with no ceiling. The exemption is the least of: the actual gratuity, the formula amount, or ₹20 lakh.

PAYMENT & RIGHTS

When must the employer pay it?

Within 30 days of gratuity becoming payable (i.e. from your last working day). If the employer delays beyond 30 days, they must pay simple interest on the amount for the delay period. Gratuity cannot be withheld except in specific cases of proven misconduct.

Can an employer refuse or forfeit gratuity?

Gratuity can be wholly or partly forfeited only if your services were terminated for specified misconduct, such as causing damage/loss to the employer's property (to that extent), or for riotous/violent conduct or an offence involving moral turpitude during employment. It cannot be denied merely because you resigned.

GOOD TO KNOW

Do fixed-term and contract employees get gratuity?

Fixed-term employees are entitled to gratuity on a pro-rata basis under recent labour reforms, even without completing five years. Genuine contract workers are typically covered by their contractor's obligations. The rules are evolving under the new Labour Codes.

Is gratuity the same as EPF or pension?

No, they're separate. EPF is a monthly contributory fund (you + employer), the EPS/NPS pays a pension, and gratuity is a one-time, employer-funded lump sum for long service. A retiring employee may receive all three.

Sources: EY alert on the labour codes.

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