

## Non - HR Briefing Note

# Holiday pay – are you getting it right?

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Developments in recent years relating to the calculation of holiday pay have left many business owners confused about how to calculate holiday pay and the consequences of getting it wrong.

With the recent launch of a Government campaign designed to boost awareness of holiday rights, it is increasingly important for employers to approach holiday pay in the correct way.

### **Do you need to take action?**

In this briefing note, we explain the basic principles relating to the calculation of holiday pay and future developments that you ought to be aware of in relation to the calculation of holiday pay.

It is clear that both the Courts and the Government are keen to ensure that workers receive the holiday pay to which they are entitled. As this area develops, it is important for employers to ensure that they are calculating holiday pay correctly. Employers should consider whether they are calculating holiday pay on the correct basis and, if not, what changes should be made and how any such changes should be implemented

### **What are the issues relating to the calculation of holiday pay?**

In the UK workers are entitled to a minimum of 5.6 weeks paid holiday per year (inclusive of bank and public holidays).

Holiday pay in the UK is calculated by reference to the complicated provisions of the Employment Rights Act 1996 concerning a "week's pay". In essence, these provisions provide that in some cases, holiday pay is paid by reference to a worker's basic salary only.

However, recent case law relating to holiday entitlement has established that workers are entitled to receive "normal remuneration" during periods of holiday on the basis that there should be no financial disincentives for workers to take their holiday entitlement.

This means that in some cases, holiday pay calculations should include basic salary and other regular payments and that holiday pay ought to be based on average earnings over an appropriate reference period. In practice, this means that if you calculate holiday pay for your workers by reference to basic salary only, you may need to reconsider your approach.

### **What is normal remuneration?**

Payments made to workers in addition to their basic salary will form part of normal remuneration where the payment is made regularly over a sufficient period for the payment to be regarded as a normal part of the worker's pay arrangements.

One recent example considered by the employment tribunal concerned overtime payments to ambulance drivers. In this case, payments for voluntary overtime which was worked one in every five weeks was considered to form part of the worker's normal remuneration. This meant that holiday pay calculations should take the overtime payments into account.

The following types of payment are likely to be regarded as part of a worker's normal remuneration where they are paid on a regular basis over a sufficient period:

- Commission payments
- Bonus payment and other incentive payments
- Productivity or performance bonuses
- Overtime pay (whether compulsory or voluntary, guaranteed or non-guaranteed)
- Payments that relate to the personal and professional status of workers such as those based on seniority, length of service or professional qualifications
- Shift allowances and premiums
- Standby payments and payments for emergency call out duties
- Travel and allowances that are treated as taxable remuneration
- Any other regular payments

Benefits in kind, expenses and one off bonuses or occasional payments should not be taken into account for the purposes of calculating holiday pay.

### **What is an appropriate reference period?**

Usually employers are safe to assume that holiday pay should be calculated by reference to average earnings over the 12 working weeks prior to the period of holiday. However, recent case law suggests that the reference period must be appropriate to the circumstances. If a worker's earnings fluctuate during the year, the worker may be able to argue that a 12 week period is not appropriate as they may end up being paid less for their holiday during some months than others.

As casual worker or part-year worker who would be subject to such fluctuating earnings must be treated no less favourably than a full time employee and the reference period and method of calculating holiday pay used **must** reflect this principle.

In reality, however, a 12 week reference period may mean casual workers and part-year workers are treated **more** favourably than other employees if they have worked and been paid more than usual in the previous 12 weeks. In this instance, a casual/part-year worker will receive an inflated amount in comparison to their average yearly earnings.

To address this issue, the Government has announced changes in this area. From 6 April 2020, the reference period for determine a week's pay will increase from 12 weeks to 52 weeks.

This means that if you are currently calculating holiday pay using a 12 week reference period, consideration should be given to making changes to this calculation in due course.

## Consequences of calculating holiday pay incorrectly

Workers can bring claims in the employment tribunal for any shortfall in holiday pay. The value of such claims is the difference between the actual holiday pay paid to the worker and the amount that should have been paid to the worker.

Since 2015, workers can usually only claim shortfalls in holiday pay relating to the period of 2 years immediately prior to the claim. However, the 2 year limit on holiday pay claims may not apply where the worker has been prevented by the employer from taking their holiday entitlement. The employment tribunal recently decided that a worker who had been effectively prevented from taking his holiday entitlement over a period of 13 years was entitled to be paid for all accrued but untaken holiday entitlement relating to his whole period of employment. The reasoning behind this decision was that an employer that does not allow a worker to exercise their right to paid holiday must bear the consequences.

Once an employer begins paying holiday at the correct rate and continues to do so, it is usually the case that the worker will only have a period of 3 months to lodge their claims.

## Future Developments

The Government published "The Good Work Plan" on 17 December 2018. It has been described by the Government as the biggest reform in employment law in the last 20 years and includes various proposals in relation to holiday rights. In particular:

- The Government has launched a campaign to boost awareness of holiday rights. In due course this will include new guidance produced in conjunction with ACAS with real life examples to support the interpretation of holiday pay rules.
- As mentioned above, from April 2020 the reference period for calculating holiday pay will increase from 12 weeks to 52 weeks. This ensures that workers who do not have regular working patterns are not disadvantaged by having to take their holiday at a quiet time of the year when their weekly pay might be lower.
- The Government will introduce state enforcement of holiday pay rights for vulnerable workers. Further details will be available in due course.

Taylor Walton's employment law team is happy to assist with any queries relating to holidays.

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