

HOLIDAY PAY AND OVERTIME - IMPLICATIONS OF FREIGHTLINER DECISION FOR PENSION SCHEMES

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In *Neal v Freightliner Limited*, the Employment Tribunal (ET) looked at the payment of overtime during a worker's statutory holiday leave. Previously, only guaranteed contractual overtime has been included in holiday pay calculations. However, the ET decided that non-guaranteed overtime (whether compulsory or voluntary) should also be included.

Calculating holiday pay

Under the Working Time Directive (WTD), a worker is entitled to four weeks of paid annual leave. The Working Time Regulations 1998 (WTR) implement the WTD in the UK. The *British Airways plc v Williams* case established that a worker must be no worse off financially during annual leave than if he/she had continued working. So, under EU law, workers are entitled to receive their 'normal remuneration' when taking statutory holiday leave.

The traditional view is that guaranteed contractual overtime (obligatory on the part of the employer and the worker) counts towards 'normal remuneration'. Non-guaranteed overtime does not count for workers with normal contractual hours. Statutory holiday pay has therefore traditionally been calculated by reference to contractual hours only.

The Employment Tribunal decision in *Neal v Freightliner Limited* found that statutory holiday pay must include non-guaranteed overtime, whether compulsory or voluntary. Furthermore, an individual can potentially claim for several years of underpayments. In the case in question, the individual was able to claim for underpayments going back to 2007 when his employment began.

Background

Mr Neal began employment in 2007. He was contracted to work a basic 35-hour week made up of seven-hour shifts, but was required to work overtime when necessary. He was expected to work one out of three Saturdays and could volunteer to do more Saturday work if he wished. In reality, his shifts and working hours were never as short as seven hours. Instead, he was consistently scheduled to work shifts of 8.5 or nine hours in accordance with the rosters, and occasionally shifts of up to 12 hours to cover for absent colleagues.

The employer calculated Mr Neal's statutory holiday pay with reference to his 35-hour basic salary only, with overtime disregarded. Mr Neal issued a written grievance followed by a claim in the Birmingham Employment Tribunal on the premise that he had received several underpayments of holiday pay. Mr Neal argued that his holiday pay (in respect of the four weeks' holiday required by the WTD) had to be calculated by reference to his pay for all hours worked, including non-guaranteed overtime.

Decision of the Employment Tribunal

The Employment Tribunal found that holiday pay should be based on Mr Neal's 'normal remuneration'. Since this normal remuneration included a certain amount of overtime, this should have been taken into account when calculating his holiday pay.

The tribunal accepted that the overtime worked by Mr Neal could be classed as 'voluntary' overtime. However, crucially, the fact that he may have 'volunteered' to work outside his contracted hours did not mean that the performance of tasks during overtime were not still 'intrinsically linked' to the performance of his contract of employment. It was irrelevant whether the overtime was voluntary or not.

Claims for holiday pay arrears can go back several years, to the introduction of the WTR in 1998 or commencement of employment, whichever is the later. In Mr Neal's case, he claimed all underpayments of his four weeks' annual leave since the date his employment commenced in 2007.

Implications for employers

The effect of the Neal decision is that overtime, whether guaranteed contractually or not, must be taken into account in calculating a worker's pay in respect of the four weeks' holiday leave required by the WTD.

This could lead to a considerable rise in holiday pay bills for many employers. Workers

may make claims for holiday pay arrears going back several years. As such, while individual underpayments may be relatively small, they may accumulate to a significant liability. Some employers may not have complete records of overtime so it could be difficult for them to work out what workers should have been paid.

Implications for pension schemes

As Neal is an Employment Tribunal decision only, it does not have to be followed by other employment tribunals. The employer is currently seeking permission to appeal and the outcome of any such appeal is eagerly awaited.

Subject to the further developments noted above, the Neal decision could have implications for pension schemes and sponsoring employers.

If non-contractual overtime has been excluded from the calculation of a member's holiday pay, this could have knock on pension consequences. For example, if a pension scheme's rules provide that **all** of a member's pay is pensionable and the calculation of their holiday pay did not take account of non-contractual overtime, their pensionable pay may be lower than it should have been. Even a definition of pensionable pay which is a basic pay only could lead to member challenge, depending on how basic pay has been interpreted in practice.

Employers will need to consider how they have been calculating holiday pay and pensionable pay in practice. They will then need to examine whether this practice accords with the Neal decision and the definition of pensionable pay under their scheme rules. If members have had their pensionable pay calculated incorrectly, there is a risk of challenge.

In a defined contribution scheme, members could potentially bring claims for backdated employer contributions. It is arguable that the member should also pay backdated contributions (as both they and their employer will have underpaid contributions to the scheme). In a defined benefit scheme, member challenges might arise in relation to the incorrect calculation of their pension benefits.

Another potential area for challenge relates to the calculation of a member's death in service lump sum.

What should employers do next?

Again, as Neal is an Employment Tribunal decision only, it does not have to be followed by other employment tribunals. The employer is currently seeking permission to appeal and the outcome of any such appeal is eagerly awaited.

It could be complex and expensive for employers to recalculate members' pay and pension entitlements on the basis of the Neal decision. While some employers are taking pre-emptive action to close down any legacy claims, others are adopting a "wait and see" approach.

While the full effects of Neal will only be revealed in time, some actions employers may wish to consider are:

- Accurately record the hours that each employee works.
- Consider reviewing the definition of pensionable pay in your pension scheme rules to ascertain whether you could be impacted by the Neal decision.
- If you receive a claim for back payments of pay/pension contributions or in relation to the incorrect calculation of pension benefits seek legal advice.
- If you are compromising claims for underpayments of holiday pay, consider any pensions implications.

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