The Employment Appeal Tribunal (EAT) decision in the combined cases of Bear Scotland Ltd v Fulton & Others, Hertel (UK) Ltd v Woods & others and Amec Group Ltd v Law & others came out on 4 November.

The decision, which confirms what constitutes 'normal remuneration' for holiday pay purposes, and specifically looked at the issue of overtime and holiday pay, quickly became one of the leading news items of the day, and #holidaypay even started trending on Twitter.

But with the news settling down, and lawyers and HR teams across the UK now considering the implications from an employment perspective, what about those for pensions and benefits more widely?

If the definition of 'normal remuneration' for holiday pay purposes has been clarified, are there knock-on consequences for how pay is treated in respect of a worker's pension, and what will this mean for UK businesses?

Analysis

What is the issue with holiday pay and overtime?

The EAT in the combined cases of Bear Scotland Ltd v Fulton & Others, Hertel (UK) Ltd v Woods & others and Amec Group Ltd v Law & others was asked to determine what constitutes 'normal remuneration' for holiday pay purposes, and specifically whether or not it is to include guaranteed and non-guaranteed overtime worked in the period prior to leave being taken.
We considered the employment law consequences of the holiday pay judgment in our alert issued on 4 November 2014. The EAT has confirmed that:

- Holiday pay must correspond to normal remuneration, which is what is normally received by a worker including "non-guaranteed" overtime, but only for the first four weeks of statutory leave (sometimes referred to as "regulation 13" leave).
- There may be limited scope for workers to recover underpayment of holiday pay by way of an unlawful deduction from wages claim, as underpayments will only form part of a series of deductions where less than three months has elapsed between the "deductions".
- A series of deductions of wages claims are likely (but not guaranteed) to be broken by periods of three months or more elapsing between the first four weeks of statutory leave taken from one year to the next.

What is the impact on UK businesses?

The Business Secretary Vince Cable has announced that a taskforce has been established to urgently assess the possible impact of the judgement. Some commentators have speculated that the impact of the judgment on UK businesses of having to include overtime pay in holiday leave could mean a 3-5% increase in their overall wage bill.

Leave to appeal has been granted so this is not necessarily the end of the story, but it is an issue affected employers must address.

But what about the implications for other benefits, such as pensions and PHI, which might refer to the 'normal remuneration' of a worker for the starting point of how contributions or benefits are calculated?

'Normal remuneration' and workplace pension reform

If the recent EAT decision is likely to impact a business in terms of increasing its wage bill, it may well have consequences for workplace pension reform in terms of:

- the assessment and categorisation of workers into eligible jobholders, non-eligible jobholders and entitled workers;
- the contributions paid to and by such workers; and/or
- if relevant, the qualifying scheme that has been used to discharge the employer's duties.
Automatic enrolment is a complicated area - for a refresher on some of the terms used in this note see our comprehensive guide on workplace pension reform.

Assessment

The Pensions Act 2008 introduced a duty on employers to automatically enrol all UK workers who are aged between 22 and their state pension age and who earn above the "qualifying earnings" threshold into an 'automatic enrolment scheme'. Employers and employees have to pay at least a minimum level of contributions into the scheme.

The key definition that underpins the assessment of workers and calculation of contributions in most cases is "Qualifying Earnings". This is a reference to a band of earnings made up of salary, wages, commission, overtimes, and statutory sick pay, statutory maternity, paternity and adoption pay. In our view, this definition is wide enough to catch holiday pay.

The reference period for establishing what is normal pay for holiday pay purposes has not yet been established, but it is likely an average should be taken over a reference period prior to taking the leave.

If (as some commentators have suggested) the reference period is established as a 12-week period, this could have an impact for employers, especially those who have peak periods in which workers typically work overtime.

Payment of a higher level of holiday pay could tip some workers over the 'qualifying earnings' threshold in the month in which they are assessed. This would lead to an increase in the number of eligible jobholders an employer needs to automatically enrol into a pension scheme. More importantly, even if the actual impact on enrolment is not significant, it may require a change to worker assessment and payroll processes.

This point is best illustrated by an example. A 25-year old worker is contracted to work for ten hours a week and is paid the national minimum wage. He would not, therefore, qualify as an eligible jobholder whenever he worked his basic hours. That same worker does, however, work a lot of overtime for a three-month period over the peak Christmas trading period (covering November through to January). He then decides to take holiday in February when work levels return to normal and he goes back to working his contractual number of hours for the rest of the year.

Previously, his employer may have used a three-month postponement notice to postpone the requirement to automatically enrol the worker during the November to January period.
When the worker was reassessed in February at the end of the three-month period, their earnings would have dropped to the lower level making it unlikely that they would be assessed as being eligible for automatic enrolment.

However if, in this instance, the worker is paid for their holiday (which is likely to reflect the higher overtime payments from work done in the previous three months) in February, they may earn above the monthly earnings trigger for automatic enrolment, and need to be enrolled as an eligible jobholder.

**Contributions**

If a worker’s take home pay in a month they have statutory holiday pay increases, it follows that the pension contributions paid to and in respect of them may be higher. This will depend on what forms 'pensionable pay' for the scheme being used, and whether employers are basing deductions on 'Qualifying Earnings', or just basic pay.

**Qualifying Schemes**

Employers who have set up a 'qualifying scheme' to comply with their automatic enrolment duties will also need to assess those schemes, to understand whether or not the impact of increased holiday pay (and any shift in balance between 'basic pay' and overall remuneration) is likely to alter the basis on which they have self-certified.

**Wider issues involving pension schemes**

We considered potential pension implications of any decision on overtime during a worker's statutory holiday leave in a previous alert.

The implications for UK pension schemes are likely to be dependent on:

- the outcome of Vince Cable’s taskforce review; and
- the definitions around 'salary', 'pensionable salary', 'earnings' etc used in the documentation for a particular pension scheme.

For occupational and personal pension schemes, the increase in holiday pay for workers may lead to a corresponding rise in the pension costs for the employer, if contributions are based on anything other than basic pay (and include overtime, for example).
The same could be said for defined benefit and career average schemes, although it is likely to be more complicated to establish the overall effect on the financial impact on the employer costs, and the overall impact on the pension for the employee. Again, the starting point will be analysing what pensionable earnings or salary those benefits are based on.

Other Benefits

There will potentially be consequences for other remuneration-based benefits, including life cover and income protection.

Why should employers look at this?

In terms of types of claims an employee could bring in respect of their pension benefits, the damage for employers could be a hidden but additional cost. Employees may be able to bring successful claims to the Pension Ombudsman when they come to take their benefits by establishing those benefits do not accord with what they should have been paid under the scheme documentation.

Businesses who don't actively engage with this, and start looking at the potential implications of the decision now, are likely to find themselves on the back-foot in the event of an employee challenge. The EAT decision is likely to be the subject of a further appeal. Leave to appeal has been given on all issues involved in this case, so there is no guarantee that the position taken on limitation will remain as it is.

Prioritising the issues now in terms of future payments is likely to lead to a much smoother transition in terms of integrating and planning and budgeting for the impact of the decision. Dealing with the past now could also create certainty for the business and avoid the gamble of a Court of Appeal decision overturning the current position.

On the flip side, if employers proactively deal with this issue, they could potentially end up paying employees a higher contribution than they otherwise need to - the potential to claw back any such overpayments is likely to be limited and complicated.

What decision businesses make will depend on their appetite for risk, position with the workforce, and the overall costs implications of acting now, or waiting to see where the conclusions ultimately fall once all appeals have been exhausted by the parties in this case. However, failing to conduct that cost-benefit analysis at all is not recommended.
What should employers be doing now?

So that employers are prepared to act quickly on the implications of this decision to minimise disruption to their business planning, budget accordingly and mitigate the risk of employee challenge, we recommend that employers:

- assess their pension scheme documentation to ascertain what (if any) impact the decision on 'normal remuneration' for statutory holiday pay will have on the definitions and benefits payable under that documentation;
- analyse workforce patterns in relation to workplace pension reform and automatic enrolment to assess whether there is likely to be a knock-on consequence of costs in that area;
- consider existing payroll and administrative systems and processes and determine whether any changes will need to be made to ensure that the employer continues to comply with its employer duties under the Pensions Act 2008;
- ensure that it is paying at least the minimum level of contributions in any automatic enrolment schemes or qualifying pension schemes;
- consider the pensions aspects of any settlements on holiday pay issues agreed with workers; and
- seek legal advice in the event an employee raises a query or challenge in relation to backdated contributions.

What about Trustees?

Trustees should be checking with the employer as to the 'remedial' action required.