Holiday Pay - The Bear Necessities

You will undoubtedly have seen the press surrounding the holiday pay decision last week, under the lead case of *Bear Scotland Limited v Fulton*. There are numerous commentaries on the case, not all accurate or helpful and some are more alarmist than they need to be. Here is our view of the case:

What does the case decide?

The judgment concerned three joined cases, all involving employees who had worked regular overtime (which they were obliged to perform if requested by the employer). In accordance with the UK Working Time Regulations (WTR), their holiday pay excluded the overtime and was based only on their basic/ minimum hours on the basis that this reflected their 'normal pay'. The Employment Appeals Tribunal has decided this was wrong because, in these cases, the overtime was worked so regularly that it had to be included in the calculation of 'normal pay' for holiday pay purposes. The overtime pay was 'intrinsically linked' to the performance of work.

Is it a surprise?

While the decision is of significant practical importance, the core element of it (to include regular overtime in holiday pay) is fairly unsurprising based on previous European cases that had already made clear that regular payments intrinsically linked to work carried out (such as allowances for pilots for time spent flying and monthly commissions received by sales people) had to be included in holiday pay.

Is it all bad news for employers?

In fact, the outcome could have been significantly worse. First, it is important to remember that this only applies to overtime worked sufficiently regularly that it is part of normal pay. What is 'sufficiently regular'? We do not know but there must be a difference between the employee who works beyond their core hours every week as opposed to one who works the odd extra hour here and there over the course of a year. Secondly, overtime is only included in the first four of the statutory weeks' of holiday (which the EC working time directive requires), not the additional 1.6 weeks provided by the UK law. Thirdly and perhaps most significantly, the scope for back pay claims has been limited. It had previously been suggested that claims for previous underpaid holiday could go back several years (perhaps even to 1998 when the WTR were introduced). The decision however is that such claims will not succeed where there has been a three month gap between underpayments. A word of caution here however is that this part of the decision is likely to be challenged on appeal as the reasons given for this aspect do not look particularly convincing.

Are there unanswered questions?

Apart from the question of what constitutes 'regular' overtime, there are certain other points which are not resolved. First of those is whether the same treatment applies to voluntary overtime, i.e. overtime an employee may accept if offered but which they can decline if they wish. It seems likely that this will be treated in the same way but strictly speaking it is unanswered at the moment. Naturally it may be easier to show that voluntary overtime is not worked 'normally' so that may be an obstacle for employees. Second is how the overtime component in holiday pay is to be calculated. The European courts have said before that it is for the national courts to work out what reference period would be appropriate when calculating the average amount of overtime worked, but the EAT did not deal specifically with this point. Under the WTR, the usual reference period for

workers with variable remuneration is 12 weeks, though the courts may decide another period is appropriate. From an employer's perspective a 12 week reference period could result in a skewed result if an employee's overtime follows a pattern of peaks and troughs; holiday would become more valuable at certain times of year. The EAT allowed the employees' appeal by amending the wording of the WTR so it would seem to follow that the reference period of 12 weeks applies for now, unless there is further clarification from the courts.

It is also unclear whether individuals can sue for breach of contract for any shortfall in pay. There are arguments both ways on the point and this issue is likely to be key for any former employees wanting to claim back holiday pay, and for employees who cannot claim that their underpaid holiday pay amounts to a series of underpayments.

So what should we do?

The case will undoubtedly be appealed and so this is not the last word on these issues. For now, we would suggest that you initially consider the following two questions:

- Does any part of your workforce work regular or frequent overtime?
- What would the impact be of including such overtime in the statutory four week holiday pay?

Once you have a feel for the scale of the issue (if there is one), then you can decide whether to bite the bullet and start including overtime payments going forward or adopt a 'wait and see' approach. There are pros and cons to both. For example, you could begin including overtime now as this may help break the link to previous underpayments and so reduce the risk of large back-pay claims. However, this could itself trigger claims to back-pay. You might, therefore decide that you are better to wait for the outcome of the inevitable appeal for more certainty and to avoid alerting your workforce to the right to claim.

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