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No. 50

HR Broadcast – Holiday Pay

We have produced a number of HR Broadcasts over the last eighteen months on the subject of Holiday Pay, and here is the latest instalment from the Employment Appeal Tribunal (EAT) which follows the much awaited but also much anticipated judgement in *Lock v British Gas Trading Ltd* [2016]. This confirmed the Working Time Directive (WTD), requiring commission to be taken into account when calculating holiday pay. However, there are still questions to be answered. Not the least of these is how to calculate reference periods, i.e. the period that should be used to calculate the average. We await the answer to that one!

Let's wind back a little:-

The WTD requires all member states of the EU to ensure that workers have the right to at least four weeks' paid annual leave, but does not specify how to calculate this holiday pay. The regulations used a calculation that was already well established in UK legislation, namely the one in the Employment Rights Act 1996 (ERA). However, time has shown that not only is that calculation not well suited to calculating holiday pay but it is not adequate to meet the directive's purposes. If a worker will not receive their usual remuneration on holiday, they may be deterred from exercising their right to annual leave in contravention of the directive's aims.

The key to calculating a week's pay under the Employment Rights Act is to work out which sub-category the employee falls into. For example, do they have normal working hours and, if so, does pay vary according to the day, or time of day, their work or the amount of work done?

Lock v British Gas Trading was an important case: allow me to recap. Mr Lock had normal hours of work and therefore fell within s221 of the ERA. As a sales consultant for British Gas, he was paid basic salary plus commission. The commission was based on the number and type of contracts he persuaded customers to enter into. He was paid on output (Sales) as opposed to input (hours worked). On average, commission made up about 60% of his pay. When he took annual leave, he did not generate any commission and, when calculating his holiday pay, his employer took only his basic pay into account. Mr Lock brought an employment tribunal claim for unlawful deduction of wages. The issue of whether commission should be included in holiday pay has proved to be a long-running one, with Mr Lock first presenting his claim to the employment tribunal back in April 2012. The tribunal then referred Mr Lock's case to the European Court of Justice (ECJ), which ruled in May 2014 that the directive does require workers to receive commission as part of their holiday pay.

Bear Scotland v Fulton By the time *Lock* was remitted back to the employment tribunal, the tribunal had the benefit of the EAT's decision in *Bear Scotland Ltd v Fulton* [2014]. In that case, the EAT held that payments for overtime which a worker is required to work but which an employer is not required to offer (non-guaranteed overtime) is 'normal remuneration' for the purposes of Article 7 of the directive. The EAT concluded that 'normal pay is that which is normally received'. On the facts of *Bear Scotland,* where the pattern of work was settled, it saw no difficulty in identifying the overtime payments as 'normal' pay and accepted that:

…where there is no such 'normal' remuneration an average taken over a reference period is appropriate.

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The EAT held that the claimants should have been paid during their holidays for the overtime they would otherwise have done, in accordance with Article 7. .

The EAT and Lock

The tribunal in *Lock* followed *Bear Scotland* and agreed that the regulations should be interpreted to conform to the directive. British Gas appealed against this decision on three grounds:

- *Bear Scotland* concerned non-guaranteed overtime, which is specifically dealt with in the ERA, whereas there is no similar statutory provision applying to results-based commission cases;
- *Bear Scotland* was wrongly decided because the EAT was bound by the Court of Appeal decision in *Bamsey v Albon Engineering and Manufacturing plc* [2004] that only guaranteed overtime should be included in holiday pay (this case was decided before subsequent ECJ case law on the meaning of Article 7); and
- The EAT is not bound by its own decisions and *Bear Scotland* should not be followed because the decision was 'manifestly' wrong.

In the EAT, it was considered whether *Bear Scotland* was distinguishable from *Lock* as there is no express provision in the ERA on commission. It was not.

In the situation where an employee works guaranteed and non-guaranteed overtime then the position is clear in that these overtime payments must be included with the calculation of holiday pay for the first 20 days of holiday using a reference period of 12 weeks.

Guaranteed overtime is where the employer is obliged by the contract to offer and pay for agreed overtime. Following a judgment in 2004, guaranteed overtime must be included within the calculation of holiday pay.

Non-guaranteed overtime is where there is no obligation by the employer to offer overtime but if they do then the worker is obliged by the contract to work overtime.

Voluntary overtime is where the employer asks the worker to work overtime and the worker is free to turn down the request as there is no contractual obligation on either side to offer or refuse overtime.

The situation as regards voluntary overtime remains unclear as it has not been directly considered by any recent judgments, so there is currently no definitive case law to suggest that voluntary overtime needs to be taken into account when calculating holiday pay or what reference period to use.

Conclusion

The conclusion is that holiday pay must include commission and that any doubts about *Bear Scotland* can be put aside will not come as a surprise to many. However, it should be noted that British Gas has been granted leave to appeal to the Court of Appeal, so we may have to revisit these issues yet again.

In the meantime, ambiguity remains over the correct reference period for calculating holiday pay. When the ECJ heard *Lock,* it ruled that holiday pay must correspond to the worker's 'normal remuneration' and that this was a matter for the

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national courts to work out by taking an average over a reference period that it 'considered to be representative'. We still await the reference period guidance for commission but for guaranteed and non- guaranteed overtime it is 12 weeks. We will continue to wait for that most crucial element of this case for some time to come – therefore the saga continues.

However, what is our advice right now? This is very difficult and we have to suggest that you make your own decision; either average all overtime now or possibly completely ignore the point and wait until the law has decided. As regards voluntary overtime again this is a decision for you. You may, out of goodwill and good HR, wish to make a payment but right now there is no legal obligation to do so. The only problem is that if a future case does settle that even voluntary overtime is to be treated as normal pay then there might be a back pay claim which in theory could go back six years.