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Holiday pay rules – What's changing in 2024 and what is the impact for employers?

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The Government has unveiled **draft legislation** to reform UK holiday pay rules by amending the Working Time Regulations 1998 (**WTR**) from 1 January 2024.

Here is an overview of what's changing (and what's not changing) and of considerations and next steps for employers.

Rights to paid holiday

What's not changing

- Workers will continue to be entitled to two distinct pots of annual holiday; the four weeks' entitlement derived from EU law (Regulation 13 holiday) and the 1.6 weeks' entitlement based on UK law (Regulation 13A holiday), paid at different minimum rates. The Government has dropped its plan to combine these into a single holiday entitlement with a single rate of pay.
- Regulation 13 and 13A holiday pay will still be calculated in accordance with the rules on "a week's pay" under the Employment Rights Act 1996.

Changes to restate EU law

- The amended WTR will clarify which elements of pay must be factored into Regulation 13 holiday pay, based on retained EU case law principles on "normal remuneration". As well as elements already falling within the current statutory definition of a "week's pay", these will include:

- payments, including commission, intrinsically linked to the performance of tasks that a worker is contractually obliged to carry out;
- payments for professional or personal status relating to length of service, seniority or professional qualifications; and
- payments, such as overtime payments, that have been regularly paid to a worker in the previous 52 weeks.

What's the impact for employers?

- Employers can continue to pay for Regulation 13 and Regulation 13A holiday at different minimum rates and will not be required to "level up" and pay for it all at the higher (Regulation 13) rate – although, in practice, many employers do. That said, calculating and applying different rates is administratively burdensome. The position has also been complicated by the Supreme Court's recent finding in *Chief Constable of the Police Service of Northern Ireland and another v Agnew and others* that all holiday should be viewed as part of a "single composite pot"; a carefully drafted policy could potentially get around this for those who want to pay at different rates.
- Employers should check that their Regulation 13 holiday pay factors in the additional components in the revised definition of "a week's pay". Many have already aligned their practices with retained ECJ case rulings, to include commission, allowances and regular overtime payments, so this should not be an issue. There are still grey areas, such as whether an annual bonus should be taken into account, which could give rise to disputes.
- Employers who have been underpaying holiday (for example, by paying Regulation 13 holiday at the rate of basic pay only) should review the changes with a view to adopting a compliant approach. This could also help to mitigate their risk exposure to historic claims.
- The changes appear to be only a holding position as the Government intends to "consider more fundamental reforms to the rate of holiday pay". However, whether such reforms will materialise if there is a change of government remains to be seen.

Holiday rules for workers with irregular hours and part-year workers

What's changing

- There will be new rules for calculating the holiday entitlement of "irregular hours workers" (those who have wholly or mostly variable paid hours in each pay period) and "part-year workers" (those who are contracted to work only part of a year and who are not required to work or be paid for at least a week of each year). These will apply **for holiday years starting on or after 1 April 2024** and such workers will be removed from the Regulation 13 and 13A provisions at that time.
- Their holiday entitlement ("Regulation 15B" holiday) will be calculated in hours and will accrue on the last day of each pay period at the rate of 12.07% of the actual hours worked in that pay period (12.07% is used as this represents the proportion of a worker's 5.6 weeks' statutory annual leave in relation to the remaining 46.4 working weeks in a year). However, where they have been on family-related leave or sick leave, employers can work out their holiday entitlement based on their average hours worked over a 52-week reference period.
- Employers can also choose to implement a system of rolled-up holiday pay for irregular hours and part-year workers (a practice that has been technically unlawful under EU case law for some years). This would involve paying a supplement of 12.07% of all pay for work done, at the same time as that work is paid for, instead of paying for holiday when it is taken. The 12.07% must be based on the worker's "total earnings in a pay period" and apply to all statutory holiday.

What's the impact for employers?

- Employers should review contractual arrangements with atypical workers to identify who falls within scope of these rules.
- The new 12.07% accrual rate effectively reverses the impact of the Supreme Court's (2022) ruling in *Harpur Trust v Brazel*, which led to some part-year workers getting more holiday than part-time workers who work the same number of hours. It does this by ensuring that workers' entitlements are proportionate to the hours that they work. This is a simpler system for employers to administer and one that many used prior to the ruling.
- While rolled-up holiday pay could be a useful solution to ease complex holiday pay calculations, a cost impact analysis should be undertaken to assess whether it would be more costly (given the required 12.07% supplement on all pay) than statutory holiday pay. Contracts should be checked to assess whether worker consent is needed to change to rolled-up holiday pay. Employers would also have to allow workers a reasonable opportunity to take their statutory 5.6 weeks' holiday, even if rolled-up holiday pay is used.

Holiday carry-over

Changes to restate EU law

- The rules create new statutory rights, based on retained EU case law principles, for workers to carry their untaken statutory holiday forward to the next holiday year in certain situations. The following can be carried forward:
    - up to 5.6 weeks' holiday when a worker can't take this due to being on statutory maternity or adoption leave, paternity leave, shared parental leave, parental leave or parental bereavement leave;
    - up to four weeks' holiday (ie the Regulation 13 entitlement) if the worker can't take this because of sick leave (defined as their "absence from work due to sickness or injury"), provided any carried-over holiday is taken within 18 months of the end of the holiday year in which the worker originally became entitled to it; and
    - up to four weeks' holiday if the employer either: (i) hasn't recognised the worker's right to this holiday (for example, due to misclassifying them as self-employed); or (ii) hasn't given them a reasonable opportunity, or encouraged them, to take it; or (iii) hasn't warned the worker that any holiday not taken by the end of the holiday year, and which cannot be carried over, will be lost.

  Irregular hours workers and part-year workers will be allowed to carry over their Regulation 15B holiday in the same situations and to use it within the same time limits.

Other changes

- Workers' rights to carry over up to four weeks' holiday, which they have been unable to take due to the effects of Coronavirus, will be abolished from 1 January 2024. However, they will have until 31 March 2024 to use up any such holiday that they have accrued before 1 January 2024.

What's the impact for employers?

- These changes reflect EU case law principles on holiday carry-over and are likely to be practices that many employers adopt anyway. The new 18-month carry-over cut-off in sickness cases will at least provide certainty for employers, although it is longer than some case rulings had suggested.
- Contracts, policies and communications should make clear that workers are encouraged to take their holiday and that they will lose any untaken entitlement at the end of the holiday year (subject to any permitted carry-over). This will mitigate the risk of workers asserting their new statutory rights to carry all unused entitlement forward to the next year. Practices and provisions on the accrual and carry-over of holiday in cases of sick leave, maternity and other statutory family-related leave should also be reviewed to ensure compliance with the new rules.

Working time record-keeping

What's changing

- The new rules will remove the additional record-keeping requirements imposed by the 2019 case (*Federación de Servicios de Comisiones Obreras (CCOO) v Deutsche Bank SAE*) in which the ECJ ruled that employers must keep records of workers' daily working hours to show that they are affording workers their rest period and rest break entitlements.

What's the impact for employers?

- This change will alleviate the record-keeping burden for employers, as well as the uncertainty as to what the 2019 ruling has required and how it could be implemented. Employers still won't have an explicit obligation to keep records of daily working hours, but they must keep adequate records to demonstrate compliance with the WTR and be mindful of broader legal duties to look after workers' health and safety. Failure to keep adequate records is a criminal offence enforced by the Health and Safety Executive (**HSE**). HSE is also responsible for enforcing working time limits so there is risk exposure if records are inadequate. That said, there has been little or no HSE enforcement action in this area, indicating that the risks of being pursued, certainly for minor record-keeping breaches, remain relatively low.

For further information or assistance on these changes and their impact for your organisation, please speak to your usual contact in the Allen & Overy LLP UK Employment Team.