Employer's Guide to Calculating Annual Leave and Holiday Pay…

When employing staff, it is important to understand the holiday entitlements they must be provided.

What the employee must be paid changes depending on the nature of their employment.

If you fail to correctly provide holiday and leave entitlements, you run the risk of having to pay the employee their entire legal entitlement and facing severe penalties for the breaches.

Penalties aside, many businesses can face severe cash flow problems if required to make substantial unexpected payment of arrears.

In a recent case, an employer was ordered to pay over $37,000 to an employee. The employee was employed permanently, but only paid 8% of her income as holiday pay, and provided no annual leave. The annual leave entitlement was calculated from the beginning of her employment and ordered to be paid out for 10 years.

Permanent Employees (full and part time)

- Permanent employees are entitled to a minimum of 4 weeks annual leave after working for the employer for 12 months. This is in addition to public holidays that are observed.
- If the anniversary of the start date is reset due to a closedown period, the 12 month period then runs again from the beginning of the close down.
- After working for 12 months, the employee may request to be paid out for a week of their leave per year. It is important to remember that this cannot be part of the employee's contract. It must remain the employee's choice if and when to request to be paid out. An employer is not obliged to agree to make a pay-out.

If the employment comes to an end, all outstanding annual leave must be paid out in the final pay.

- If 12 months have passed, the accrued leave must be paid at the rate of the greater of the employee's ordinary weekly pay or average weekly earnings over the past 12 months.
- If 12 months have passed, but the employee has already used up the first year's leave, then any outstanding proportion of annual leave the employee has become entitled to should be paid out at 8% of their pay over that period since the new leave started to accumulate.
- If a permanent employee leaves before 12 months of continuous employment, they are still entitled to holiday pay. This is calculated at 8% of their total earnings over the period of employment.

When paying annual leave at the time taken:

- If the employee has worked less than 12 months, but is approved leave, this should be deducted from any accrued annual leave.
- When calculating how much to pay, it must be at the rate of the greater of the employee's ordinary weekly pay or average weekly earnings over the past 12 months.
- This means as an employee is promoted, or given pay increases, the value of their accrued and due annual leave increases.

Fixed Term Employees

Fixed term employee entitlements differ depending the amount of time they have been working, and the circumstances under which this was agreed.

If a fixed-term employee works continuously for 12 months, they may become entitled to annual leave.

- If the original fixed term contract stated that the employee was to be employed for less than 12 months, but has continued working and being paid beyond this time, without a new and genuine fixed term agreement in place, they are deemed to be permanent employees.
    - The employee becomes entitled to all rights afforded to a permanent employee, including 4 weeks annual leave. However:
    - Leave payments that have already been paid to the employee over the previous 12 months may be deducted from what becomes owed.
- If the fixed-term employee is employed under two or more agreements that results in them working for over 12 months:
    - The employer and employee may agree to continue paying holiday pay on an "as you earn" basis. This must be recorded in their employment agreement.
- If the fixed-term agreement ends on the completion of a project or an event, and lasts over 12 months:
    - Annual leave of 4 weeks becomes due at the anniversary of 12 months employment. It is best if this is a possibility to not pay 8% as you go, but to pay annual leave at the end of the contract, or allow leave to be taken and paid at the time of taking the leave.

If the term of continuous employment does not exceed 12 months:

- The employer and employee may agree in the employment agreement that holiday pay be paid on an "as you earn" basis. The law requires that this is at least 8% of the employee's gross income and is paid at the same time as wages. It must be identified as holiday pay in the wage slip and separately calculated.
- Alternatively, the holiday pay becomes accrued and is paid out as part of the employee's final pay.

Note that the holiday pay component of the employee's income must be recorded separately in wage records, and be identifiable as holiday pay.

Casual Employees

Casual employees are those that work highly varied hours every week, sometimes none at all.

If an employee's work is in a regular pattern and the hours do not change, they should be a part-time permanent employee with the corresponding entitlements, not casual.

Since casual employees may be working few to no hours some weeks, this makes providing 4 weeks annual leave problematic.

- The employer and employee may agree in the employment agreement that the employee be paid 8% of their income as holiday pay instead of accruing annual leave.
- This must be recorded as a separate component of the employee's pay on their payslip, and be identified as holiday pay.
- Alternatively, holiday pay is to be accumulated, and paid out to the employee at 8% of their earnings during employment when they leave.
- If holiday pay is not paid as part of wages, it should be accumulated, and the employee may request to be paid out for up to a week's worth per year.

Aside from having to repay any employees their correct holiday entitlements, employers face expensive penalties for breaching the Holidays Act if they get it wrong.

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