

Payroll – Holiday pay

One of the intentions of the Holidays Act 2003 is to make it easier to calculate employees' holiday pay. Holiday pay is not just an employee's pay while on annual leave – it can mean several different things. It is therefore important to understand what it is and how to correctly calculate holiday pay under the Holidays Act 2003.

What is holiday pay?

Holiday pay is a term used by the Holidays Act 2003 to mean different things:

- ✦ An employee's pay while they are on annual leave;
- ✦ 6% added to final pay if employment is terminated (or there's a customary closedown) within 12 months of an employee starting work for an employer; or
- ✦ An employee's pay while they are away from work on a public holiday or alternative holiday.

The minimum rate for holiday pay on termination or closedown within a year of employment will increase to 8% from 1 April 2007. This is because the minimum annual leave entitlement will be increasing to 4 weeks.

Holiday pay for an employee who is on annual leave must be the greater of their:

- ✦ Ordinary weekly pay; and
- ✦ Average weekly earnings.

Ordinary weekly pay

'Ordinary weekly pay' is what the employee receives for an ordinary working week.

Ordinary weekly pay:

- ✦ Includes productivity and incentive payments, such as commission, regular overtime, and cash value of board or lodgings provided as part of the employee's 'package'; but

- ✦ Doesn't include discretionary and one-off payments.

If it's not possible to determine an employee's ordinary weekly pay, the pay must be calculated by using the following formula:

$$\frac{a - b}{c}$$

where:

'a' is the employee's gross earnings for:

- ✦ The 4 calendar weeks before the end of the pay period immediately before the calculation is made; or
- ✦ If the employee's normal pay period is longer than 4 weeks, that pay period immediately before the calculation is made.

'b' is the total amount of productivity or incentive-based payments, plus payments for overtime that are not a regular part of the employee's pay, plus any one-off or exceptional payments.

'c' is 4.

For example, a salesperson's gross earnings for 4 weeks was \$3,800. This included \$1,200 for commission made on sales and \$200 for extra hours worked while attending an exhibition.

Their ordinary weekly pay for the period is therefore:

$$\frac{3800 - 1400}{4} = \$600$$

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where:

'a' is their gross earnings, ie \$3,800.

'b' is commission plus non-regular overtime, ie \$1,200 + \$200.

'c' is 4 calendar weeks.

Average weekly earnings

'Average weekly earnings' are the employee's gross earnings for the previous 12 months, divided by 52.

Gross earnings include paid leave, certain allowances, overtime, productivity, and incentive payments, such as commission, first-week compensation for a work-related injury, and the cash value of board or lodgings provided as part of the employee's 'package'.

It does not include payments not covered by the employment agreement, such as discretionary payments, weekly compensation from ACC, and reimbursement payments or allowances for work-related expenses, such as business trips, meal and tool allowances, etc.

When does it have to be paid?

Employees are entitled to be paid holiday pay before starting a period of annual leave, unless:

- ✦ You and the employee agree that they are to be paid on the day they would normally be paid if they weren't on leave; or
- ✦ The employee's employment has ended.

For employees that are paid weekly, this usually poses no problems. However, the same rule applies to employees who have their wages direct credited each month. All employees are entitled to be paid before taking their annual leave.

Where there is a closedown over Christmas, wages are paid on the usual day for such payment and holiday pay is usually paid at the end of the last day at work before the closedown.

Holiday pay on termination

If the employee's employment ends within 12 months of them starting work for you, i.e. before the employee qualifies for annual leave, you must add 6% of their gross earnings to their final pay, minus:

- ✦ Any payment for holidays taken in advance, and any holiday pay which has been paid with ordinary pay.

For example, an employee took one week's annual leave in advance in their first year of employment.

Their ordinary weekly pay was \$500. At the start of a closedown, or if their employment ends, the following would apply if they've worked there for less than 12 months:

- ✦ Gross earnings for the period (36 weeks): \$18,000.
- ✦ Value of 6% of gross earnings: \$1,080.
- ✦ Minus holiday pay already paid: \$500.
- ✦ Balance owing to the worker (gross): \$580.

'Pay as you go' holiday pay

Employers can include holiday pay in ordinary pay ('pay as you go'), but only in certain situations where:

- ✦ There is a genuine, fixed-term employment agreement for less than 12 months; or
- ✦ It's impractical to provide 3 weeks' annual leave because the work is too irregular or intermittent.

For holiday pay to be paid in ordinary pay it must be:

- ✦ Agreed to in the employment agreement;
- ✦ An identifiable component of the pay (e.g. noted on the pay slip); and
- ✦ At least 6% of gross earnings.

'Pay as you go' holiday pay can only be used if it's genuinely not possible to predict the pattern

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of employment, such as employees 'on call' to cover for sick employees.

If 'pay as you go' holiday pay is used incorrectly, and employment lasts longer than 12 months, the employee becomes entitled to 3 weeks' paid annual leave, even though they received holiday pay during their first year – in other words, they get paid twice for annual leave 'earned' in their first year.

Public holidays

Employees are entitled to their 'relevant daily pay' for a public holiday, or for an alternative holiday they 'earned' by working on a public holiday. Further information on relevant daily pay is provided in a separate fact sheet – contact us.

Note that the law can and does change quickly. The latest on holidays legislation can be found on www.ers.govt.nz.

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