Managing your annual leave costs

Commentary by Tony McKone, Director McKone Consultancy Ltd. 4 September 2013

It is often said by business that "people are our biggest asset" – this is very true. What is not said as often though is that this asset comes with costs that need to be managed. One of these costs is the employees' annual leave entitlement. If left unchecked, that leave cost can quickly become an expensive liability for the organisation.

Under the Holidays Act 2003 and its various amendments, employers must provide employees a minimum of four weeks' annual leave. This is a minimum requirement and the Act does not prevent an employer agreeing to provide more than four weeks leave. An employer cannot contract out of the statutory minimum four weeks leave.

In general an employee becomes entitled to their annual leave after 12 months employment and that leave entitlement then remains in force until the employee has taken all their entitlement as a paid holiday. Annual leave is not forfeited if left untaken.

This means that if you do not manage an employee's leave that entitlement will continue to grow and will remain on your books as a liability to be paid when the employee eventually takes that leave or when their employment terminates.

In the first year of employment, whilst an employee technically does not have any entitlement to annual leave, the leave balance commences to accrue at a rate of 1.67 days per month, until finally on the employee's anniversary date, when they become entitled to the annual leave, they have 20 days owing them.

Of course, the accrual does not stop building just because the anniversary date has arisen. The 20 days accrual becomes an entitlement on the anniversary date and a new accrual commences over the next 12 month period.

If an employee is not taking their annual leave, 20 days can become 40 and continue to grow.

There is an expectation that an employee takes at least one two-week break from work after 12 months of employment, and every year thereafter. This break is for rest and recreation – a time to effectively recharge the batteries.

If your employees are not taking their holidays, then they are likely to become less productive. The cost to your organisation then compounds – it is not just the building leave liability; it is also the cost of that lost productivity.

The best way to ensure your employees are taking appropriate holidays is to request them to provide you a leave plan setting out their intentions for when they will take a holiday. If an employee does not provide a leave plan and you and the employee cannot agree on when that leave will be taken then you are entitled to direct them to take leave. To do so you must however provide at least 14 days' notice of the requirement to take leave.

If you do need to go down this path, seek advice first.

There are certain things you need to do and some that you cannot do when considering requiring an employee to take leave. For example, before you can require an employee to take their leave you must have consulted with them about the timing of the leave and taken reasonable steps to try and reach an agreement on when the leave should be taken first. You can only require an employee to use their entitlement (that is the leave to which they are currently entitled). This means that you cannot require an employee to use any leave accruing for their next anniversary date.

If you need assistance with the management of your employees leave please contact us.