

# HOT TOPIC

February 2026

## THE BUDGET & HR: ESSENTIAL ADJUSTMENTS FOR 2026

### 1. INTRODUCTION

The UK business landscape will undergo a significant shift from April 2026. The combined impact of the Autumn Budget 2025 and the [Employment Rights Act 2025](#) (ERA 25) represent a fundamental recalibration of the relationship between employers and employees. Together, these fiscal and statutory reforms are designed to strengthen protections for lower-paid workers, but they will also require employers to make material changes to both their cost base and compliance frameworks.

Failure to prepare will not be a theoretical risk. From the start of the 2026/27 financial year, unprepared organisations face a heightened exposure to financial penalties, unplanned cost increases, and substantial administrative disruption.

For senior leaders, the priority is therefore clear: organisations that do not align their workforce costs and compliance arrangements ahead of April 2026 will experience avoidable financial strain. In this month's *Hot Topic*, we examine the key statutory reforms and fiscal measures in detail and set out practical considerations for how employers can respond.



## 2. THE FISCAL IMPACT OF THE 2025 BUDGET

The November 2025 Budget set a clear three-year direction of travel. The Government has committed to raising the wage floor while maintaining income tax thresholds, a deliberate approach commonly referred to as *fiscal drag*, which results in more individuals being drawn into higher tax bands over time.

In parallel, the Government confirmed the Low Pay Commission's recommendations for significant increases to statutory minimum pay rates for 2026/27. For many employers—particularly those in sectors such as retail and hospitality where pay often sits at or close to the statutory minimum—this will require a fundamental review of pay structures. Without intervention, organisations risk wage compression, where pay differentials between employees with differing levels of skill, experience, or responsibility are eroded.

The forthcoming increases in April 2026 are material:

- The National Living Wage (for workers aged 21 and over) will rise by 4.1%.
- The National Minimum Wage for 18–20-year-olds will increase by 8.5%, taking the statutory minimum to £10.85 per hour.
- The apprentice rate for those aged 16–17 will increase by 6% to £8.00 per hour.

For employers with younger workforces or significant apprenticeship populations, these changes will drive a sharper and more immediate increase in employment costs.

## 3. REMOVAL OF AGE-BASED BANDINGS AND WIDER IMPLICATIONS

It is also important to note the Government's longer-term commitment to removing age-based minimum wage bandings entirely, so that all adults are entitled to the same minimum wage. While the implementation date has yet to be confirmed, the policy direction is clear. In addition, the methodology for setting minimum pay rates has already been broadened to explicitly take account of cost-of-living considerations.

The combined effect of these reforms will be sustained upward pressure on wage costs, with a disproportionate impact on sectors traditionally associated with younger or lower-paid workers. Employers will need to revisit budgets and forecasts to account not only for rising minimum wage costs, but also for the interaction with other reforms, including changes to Statutory Sick Pay.

Beyond pure cost modelling, organisations will need to review existing pay structures to ensure they remain competitive, fair, and sustainable. In many cases, this will require adjustments to pay rates above the statutory minimum to preserve meaningful differentials and protect employee engagement.

## 4. OTHER FISCAL POLICY CHANGES

It is also important to recognise the cumulative impact of wider fiscal policy changes that have affected employers since April 2025. These measures have already increased the baseline cost of employment, before any additional obligations arising from the Employment Rights Act 2025 (ERA 25) are considered.



- The employer Secondary Class 1 National Insurance contribution rate increased to 15%, having remained at 13.8% for more than a decade.
- Employer Class 1A and Class 1B National Insurance rates, which apply to most taxable benefits and expenses, also rose to 15%.
- The Secondary National Insurance threshold—the point at which employers become liable to pay employer NICs on employees' earnings—was reduced from £9,100 to £5,000 per annum. This threshold is not scheduled to increase again until April 2028, when it will rise in line with the Consumer Prices Index.

Taken together, these fiscal changes materially reduce employers' financial headroom. They constrain the capacity to fund discretionary pay increases, invest in recruitment, or absorb further cost pressures. Crucially, these impacts are separate from, and in addition to, the increased costs and compliance requirements expected to arise from the reforms introduced under ERA 25.

## 5. OVERVIEW OF THE EMPLOYMENT RIGHTS ACT (ERA) 2025

The ERA 2025 Act aims to guarantee "fair pay for a fair day's work" while tackling systemic employment inequality. These reforms span approximately 30 areas of employment law. While some changes carry an obvious cost implication, even those that don't will incur indirect costs through increased management time, system updates, and training requirements.

### **Direct Cost Drivers: Key Reforms**

The following 10 reforms are expected to have the most significant direct financial impact on employers:

1. **Statutory Sick Pay (SSP) Expansion:** SSP will become a "day one" right from 6 April 2026. The Lower Earnings Limit will also be removed, making all employees eligible. Payment of SSP will also be calculated using the new method of either the statutory rate or 80% of normal weekly earnings (whichever is lower).
2. **School Support Staff:** Reinstatement of the national negotiating body.
3. **Adult Social Care:** Establishment of a negotiating body and "Fair Pay Agreements."
4. **Tipping Legislation:** Mandatory workforce consultation on tipping policies, with a formal review required every three years.
5. **Two-Tier Code on Procurement:** Public sector contractors must match the terms and conditions of the public sector workers they work alongside.
6. **Redundancy Penalties:** The maximum "Protective Award" for failing to consult on collective redundancies will double from April 2026 from 90 to **180 days' pay** per employee.
7. **Enforcement Fines:** The Fair Work Agency once fully established will be able to fine employers up to **200%** of unpaid sums (capped at £20,000 per employee) where there are failures in the payment of statutory payments such as SSP, holiday pay and NMW.
8. **Tribunal Reforms:** Includes longer claim windows, unfair dismissal protection starting after just 6 months, and the removal of the compensatory cap.
9. **Guaranteed Hours:** Contracts will in the future need to reflect actual hours worked over a reference period (likely 12 weeks).

**10. Shift Cancellation Pay and Notice Rights:** In the future, workers must be paid if a shift is cancelled, moved, or shortened by the employer and that reasonable notice of shifts, with mandatory compensation for late changes.

#### **The introduction of the regulator 'The Fair Work Agency' (FWA)**

The launch of the **Fair Work Agency (FWA)** represents a massive shift in UK employment enforcement. By merging bodies like the NMW unit and the Gangmasters Authority, this regulator will hold unprecedented powers to:

- **Enforce Payments:** Issue notices for underpayment of SSP, holiday pay, and minimum wage.
- **Levy Heavy Fines:** Apply civil penalties of up to 200% of the arrears.
- **Audit Historic Breaches:** The FWA can inspect sites, interview staff, and scrutinise records dating back **six years**.

**Note:** While most employers remain compliant, these measures are specifically designed to eradicate unlawful practices that can still be found to be undertaken by unscrupulous businesses that deny workers their statutory rights.

## **6. OPERATIONAL AND STRATEGIC CONSIDERATIONS**

Implementing these changes will bring additional operational demands. Payroll systems and processes will need updating, increase administrative complexity and compliance risk if not managed carefully. While higher minimum pay rates may support attraction and retention in tight labour markets—potentially reducing recruitment costs over time—they also increase the overall cost of employment.

Some businesses may seek to offset these pressures through price increases, which could affect competitiveness, particularly in price-sensitive markets. However, the reforms also create a more level playing field, as all employers will be subject to the same minimum wage requirements regardless of worker age. This removes the incentive to favour younger workers purely on cost grounds and supports fairer workforce practices across sectors.

Taken together, these changes demand early, strategic planning. Employers that act now, by reassessing pay structures, updating financial forecasts, and strengthening compliance frameworks, will be far better positioned to absorb the impact and maintain organisational resilience into the next financial year.

## **7. IMPLICATIONS FOR SME'S**

The Employment Rights Act 2025, combined with the 2024/2025 Autumn Budgets, represents the most seismic shift in UK employment law in a generation. For Small and Medium-sized Enterprises (SMEs), the era of "informal flexibility" is ending, replaced by a mandate for structured compliance and procedural rigour.

#### **Financial liabilities and payroll**

- **SSP reform:** This is a direct overhead increase. SMEs with part-time or low-wage staff will see sick pay liabilities jump. To mitigate a potential rise in intermittent absences, employers must tighten absence management and mandate return-to-work interviews.
- **Sector-wide pay agreements:** In social care and education, "Fair Pay Agreements" will be legally binding. This removes the ability for small providers to compete on price by offering lower wages than larger local competitors.



- **Public sector tendering:** The "Two-Tier Code" means SMEs bidding for government contracts can no longer rely on lower labour costs; they must match public sector wages and pensions.

### Compliance: The Fair Work Agency (FWA)

The FWA changes the focus from "reactive" to "proactive" enforcement.

- Unlike Tribunals, which require an employee to sue, the FWA will be able to proactively audit the workplace and bring a claim on behalf of a worker – even if they were not intending to. Placing a greater burden on accurate and full employment records.

### The end of low-risk dismissals

Coming into force in January 2027, tribunal reforms will transform risk management regarding unfair dismissals:

- **Removal of the compensatory cap:** currently, employers can price the risk of a settlement. Yet, under this reform to remove the cap, it introduces greater financial risk. Dismissing a high earner unfairly for example, could result in awards exceeding £250,000 (covering years of lost salary and bonuses). A single lost claim of this magnitude could bankrupt an SME.
- **No-win-no-fee surge:** With unlimited potential awards, ordinary unfair dismissal cases become attractive to solicitors that operate on a no-win-no-fee basis and therefore likely increase the volume of litigation.
- **The 6-month qualifying service:** From January 2027, protection from unfair dismissal becomes available from 6 months service, rather than the current 2 years. SMEs must adopt a "keep or fire" mindset by month four to allow for notice periods before full legal protections apply in the situation.
- **The risk of memory fade:** The window to claim at tribunal will double to 6 months, effective from October 2026. SMEs will need to maintain meticulous records for longer to defend against claims where witnesses may have moved on or memories have blurred.

### Operational & scheduling constraints

- **Guaranteed minimum hours:** when this reform comes in (not before 2027), it is expected to end the ability to keep staff on "standby" indefinitely and to operate a flexible workforce.
- **Shift cancellation & notice:** SMEs, particularly in retail and hospitality, will be required to have more rigorous procedures and processes when workforce planning to avoid paying for unworked hours.
- **Tipping policy:** From October 2026, failing to have a written, consulted-upon tipping policy becomes a legal vulnerability. Because consultation is mandatory, the policy itself will be open to negotiation, potentially driving up costs.

## 8. REGISTER FOR OUR FREE VIRTUAL EMPLOYMENT LAW SEMINAR

Each year, Business HR Solutions host its annual employment law seminar, and the one in 2026 will perhaps be one of the most significant ones we have held.

Please do join us for our seminar in which we will focus on the Employment Rights Bill, and other changes expected in 2026, which will also include interesting and significant case rulings.

[Register Here](#)



## NEED EXPERT HR ADVICE? GET 30 MINUTES FREE!

The festive season can bring a range of HR and legal risks, from misconduct and discrimination to health and safety concerns. Book your FREE 30-minute HR advice session to discuss how to protect your business this December and ensure your workplace celebrations stay compliant, inclusive and low-risk.

**[Contact us today to schedule your free consultation](#)**

