Earned (Accrued) Vacation and Payout Practices



ARE EMPLOYERS REQUIRED TO PROVIDE PAID VACATION TO EMPLOYEES?

Many employers believe that they are required to provide paid vacation; however federal law does not require employers to offer such a benefit. Because of the significant benefits both employers and employees realize as a result of time away from work, however, it is customary for employers to provide it. Many employers find that paid vacation bolsters both recruitment and retention. Although the law does not require paid vacation, once an employer makes it available, it must carefully draft its policy to avoid ambiguity and comply with state law. Complaints regarding vacation time often arise as breach of contract claims, which can be costly and time-consuming to defend.

ARE EMPLOYERS REQUIRED TO PAY AND EMPLOYEE FOR UNUSED EARNED VACATION?

The legal question most often associated with the payment of vacation pay is what happens to an employee's unused earned vacation credits upon the termination of employment. Nearly all states classify vacation as "wages," which, if owed to an employee, must be paid at the time of termination or within a certain specified period of time (usually a matter of a few days or even hours) following an employee's resignation or discharge. Nearly all states, however, are in agreement that all conditions to earning paid vacation must be met in order for vacation to be deemed "wages" that are due an employee upon the termination of employment.

Conversely, nearly all states strictly prohibit employer policies or practices under which employees are required to forfeit their earned vacation upon the termination of their employment for whatever reason. A policy under which earned vacation is forfeited due to an employee's failure to provide advance notice of resignation or if the employee is fired for certain work rule violations likewise generally is unenforceable and can subject an employer to civil liability and even criminal penalties. Any employer should consult its legal counsel before attempting to enforce any kind of "wage forfeiture" policy.

The conditions precedent to earning vacation usually involves a certain period of employment or continuous service by the employee. However, even when the

employer's policy requires an employee to work a certain period of time (say, a year) before becoming eligible to take paid vacation, the law of some states provides that vacation vests on a pro-rata basis and cannot be forfeited if an employee does not reach the anniversary date when she otherwise would become eligible to take paid vacation. Under such a rule, an employee who quit or was fired after working nine months would be entitled to be paid, upon termination, for two-thirds of the vacation she would have been eligible for had the employment continued for a full year.

Other states require an employee both to have accrued the vacation and to be eligible to take vacation at the time of termination in order to receive vacation pay. Under this rule, if an employer's policy requires an employee to work a full year before becoming eligible for two weeks of vacation in year two of the employee's employment, the employee would not be entitled to any vacation pay if he quit or was discharged before the first anniversary date of his employment. Most states are in agreement, however, that when an employer's policy provides for paid vacation, and an employee is terminated without having used vested vacation time, all vested vacation time must be paid to the employee as wages upon the termination of her employment.

A related issue arises when an employer has an accrual-based vacation policy under which employees accrue a certain number of vacation days per month up to a maximum number of vacation days per year. Under this kind of policy, employers invariably advance vacation to their employees (i.e., they permit their employees to use more paid vacation days than they have accrued at the time of their vacation). For example, the policy of ABC Company allows its employees to accrue one and a half vacation days per month up to a maximum of 15 vacation days per year. An employee asks to schedule a ski vacation in February. The problem is, under ABC Company's policy, the employee has accrued only one and a half days of vacation. "No problem," says ABC, "under our policy, we'll advance you the vacation you want, and you can work it off when you return." The employee takes a two-week vacation and quits a month later. Can ABC Company require the employee to pay back the unearned vacation it advanced its employee?

In most states, the answer is an unequivocal yes. Many states expressly allow employers to set off the amount of unearned vacation previously paid to an employee against the wages or salary earned by the employee through her termination date. Some states, however, prohibit employers from withholding or offsetting any amounts from wages due to a separated employee even when it's clear the employee owes the employer. So, in our example, it would behoove ABC Company to consult its lawyer to determine whether the applicable state law permits a setoff. This is especially so because most states impose strict penalties when an employer fails to pay an employee all "wages" or other compensation due upon the termination of employment.

It is critical that employers keep accurate records of the amount of vacation both earned and taken by their employees. Because nearly all states consider unused earned vacation pay to be wages due an employee upon the termination of employment, an employer's failure to include vacation pay in an employee's final paycheck could result in strict legal liability as well as unexpected legal bills.

Nearly all states require the employer to pay the employee's attorney fees and litigation expenses if a lawsuit is required to collect unpaid wages, including

unpaid vacation.