

Employee Benefit ■ Plan Review

Is Unlimited PTO Key to an Employee Retention Strategy?

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A relatively new trend may be key in a company's employee retention strategy: offering unlimited paid time off (PTO) to its workforce. Some employers may be nervous about not placing any cap at all on the amount of time workers can take off work, but a new flexible approach to workforce management may be just the ticket to separate an organization from competitors. What are the pros and cons to this strategy – and what legal issues do employers need to consider before unveiling an unlimited PTO policy of their own?

WHY A COMPANY MIGHT NEED A NEW APPROACH

The COVID-19 pandemic has left an indelible impact on the American workforce. After tackling the once daunting ordeal of instituting a primarily remote labor force, many employers realized that the modern approach boosted employee productivity – devoid of management's gaze. Yet, as the dust settled and companies began to relax, believing the worst was behind them, the pandemic, true to form, brought on another set of employment hurdles – employee resignations.

Ian Cook, writer of Harvard Business Review's article titled "Who Is Driving the Great Resignation,"¹ explains that the "tidal wave" of employee resignations has left

significant difficulties for employers to attract and retain top talent. According to a survey conducted by Pew Research Center, nearly 45% of Americans who quit their jobs cite "a lack of flexibility" and subpar benefits and health insurance as the primary catalyst driving their resignations. Now, more than ever, employers are left with the task of revamping their compensation and benefits policies to incentivize their top performers to stay.

WHAT IS UNLIMITED PTO?

If the pandemic has taught us anything, it is that employees are now pushing the limits to what they deem an archaic employment structure. The solution to retaining employees may be similar in effect to remote work – providing employees flexibility and autonomy through unlimited PTO.

Traditionally, an employee's time off has been separated into vacation and sick days, designated when the time is taken off work. In these scenarios, an employee may only take the number of vacation days allotted to that individual. Unlike paid sick leave, unused vacation at termination is paid out to the employee.

Unlimited PTO policies go one step further: they place no cap on the amount of time an employee can take off work. Again, the name itself may be daunting to some employers, but

an unlimited PTO policy benefits employees and employers alike. Under an unlimited PTO policy, employees receive their sought-after flexibility, and employers are alleviated by the burden of tracking employees' time off.

But as beneficial as unlimited PTO appears, employers must equally assess the benefits and potential liabilities the policy may pose before rolling one out.

POTENTIAL BENEFITS TO UNLIMITED PTO POLICIES

On its face, unlimited PTO is a win for both employees and employers. An unlimited PTO policy is a valuable recruiting tool as it promotes autonomy over the employee's own work/life balance. With more flexibility comes a greater responsibility for time management. Flexible policies around vacation can foster trust, avoid burnout, and focus on meeting objectives in a results-oriented environment rather than worrying about counting accrued vacation hours.

Along with the benefits of a potentially happier and healthier workforce, unlimited PTO also has employer benefits. Unlimited PTO is seen as a cost-saving technique. If an employee does not accrue vacation, then there is no need to pay out unused vacation days at the end of the employment relationship. However, in order for PTO not to accrue the unlimited PTO policy must truly be unlimited.

POTENTIAL PITFALLS TO UNLIMITED PTO POLICIES

So, is unlimited PTO too good to be true? Since unlimited PTO is a newer policy, case law and literature are scarce surrounding this topic. But there are some key issues to consider.

First and foremost, it is critical for employers to consult with a labor and employment attorney to ensure that an unlimited PTO policy is implemented correctly.

The next consideration: is the company operating in California?

California-Specific Concerns

Employers with California employees should be cautious to ensure that they have a truly unlimited PTO policy to prevent setting off California Labor Code Section 227.3. Although an employer is not mandated to provide vacation pay, the Section does provide that certain restrictions are placed on employers if they have an established policy to provide paid vacation.

California allows vacation accrual, caps on the maximum amount, and bans "use it or lose it" policies. Under California law,² earned vacation time is considered wages, and vacation time is earned, or vests, as labor is performed. Because vacation pay is regarded as the same as all other forms of compensation at termination, accrued vacation pay must be paid to the employee upon termination.

Recently, the holding in *McPherson v. EF Intercultural, Inc.*, provided more insight into how Section 227.3 fairs with unlimited PTO. The California appellate court held that it's possible for vacation time to vest despite an employer's efforts to establish an Unlimited PTO policy. The impact of the case is significant because California employers must pay unused vacation time when someone's employment ends, and a failure to pay can lead to severe costs and penalties. However, the court made it very clear that it is possible for a company to set up an unlimited paid vacation policy to avoid that consequence, as long as it properly communicates the policy and the vacation time is truly "unlimited."

Concerns for All Employers

But the concerns are not limited to employers with California operations. Additional problems related to unlimited PTO policies that apply across the board include, but are not limited to: inconsistent enforcement, employees taking less time off, and the creation of animosity among employees who

are paying attention to which of their colleagues are taking time off and those who are not. For example, unequal administration and approval of PTO may lead to potential discrimination claims.

Employers must also remain cautious when combining sick and vacation days into one unlimited PTO policy. An increasing number of states and municipalities require employers to provide a certain amount of paid sick leave. This regulatory framework presents several issues. For instance, what if an employee is denied leave that was meant to be requested as a sick day under the law? Such a scenario may expose an employer to potential risks for retaliation claims.

Other considerations include:

- Does management in the workplace require "face time" around the office – or at least favor those who show up more often than others?
- How are teams affected or treated differently?
- Is there a policy to determine whether the employee is using excessive leave or abusing the system?
- Will the company compensate an employee for unused time?
- Will other paid sick leave be considered separately?
- How will the company avoid subjective approval or discriminatory application of the policy?
- Are the company's wage statements compliant with the current sick leave policy and any state or local laws?

CONCLUSION

As vacation and time away from work are known to boost concentration, creativity, and morale, unlimited PTO may be the unsung hero to retaining employees. While there is uncertainty surrounding the new trend, it is clear that it may greatly benefit the employees and the employer's culture – but a carelessly

crafted policy will also expose employers to substantial risks.

Therefore, it is essential to effectuate a clear written policy that considers the interplay of state and local leave laws and mitigates risk to the

company while providing a benefit to its workers. 🌀

NOTES

1. <https://hbr.org/2021/09/who-is-driving-the-great-resignation>.
2. https://www.dir.ca.gov/dlse/faq_vacation.htm.

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