Reconsidering Your Vacation Package in Nevada

Insights
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I. Introduction

Increasingly, the benefits package offered by employers is a top priority for job seekers around the country. This focus is clearly justified because a good benefits package can account for 30% or more of an employee's total compensation. As Nevada employers struggle to attract quality employees by creating comprehensive benefits packages, it is important to consider all of their possible consequences.

One of the most troublesome issues for employers is their obligation with respect to vacation benefits. Although a grant of two weeks paid vacation per year may seem simple enough to apply, a review of the following questions could cause a change in opinion: Will the employee be entitled to payment in lieu of vacation time during employment? Upon termination? Can an employee accumulate vacation time over a number of years? Will an employee be entitled to vacation time while on strike?

While an employer's obligation for vacation benefits is largely a matter of ordinary contract law, some issues peculiar to vacation policies are worthy of note. This article will address some of these more salient issues, and pitfalls, surrounding vacation benefits. In particular, the article discusses specific problems associated with the creation of a benefits policy in the context of an employer's obligation upon termination. Next, the authors consider the effect that modification of the policy and express conditions on the accrual of benefits will have on an employee's right to collect unused vacation benefits upon termination. Finally, the article discusses an employer's provision of vacation benefits in the context of three federal laws—the National Labor Relations Act, the Family Medical Leave Act, and the Employee Retirement Income Security Act. Based on this discussion, the authors provide a general checklist for employers to consider when creating a vacation policy of their own.

Readers should note that there is very little Nevada law on this subject and that this article is primarily based on the law of other states. The authors believe that vacation policies carefully formed with the following discussion in mind will likely survive a subsequent ruling by Nevada courts. As always, employers should consult with their attorney before fashioning these and other employment policies.

II. Payment Upon Termination

A majority of the states that have addressed the issue do recognize vacation pay to be "wages" due and owing upon the termination of employment, absent agreement to the contrary. Generally, this

means employees are entitled to a pro rata share of their vacation benefits upon termination. A New Jersey court, in *Textile Workers Union v. Paris Fabric Mills*, provided representative reasoning:

It is beyond dispute that an agreement to pay vacation pay to employees made to them before they performed their services, and based upon length of service and time worked, is not a gratuity but is a form of compensation for services, and when the services are rendered, the right to secure the promised compensation is vested as much as the right to receive wages or other forms of compensation.

On the other hand, a minority of the states to address the topic, including Connecticut and Missouri, do not recognize vacation pay as wages upon termination for purposes of their wage and hour statutes, unless the employment contract specifically provides otherwise.

Unfortunately, the Nevada wage and hour statute, NRS 608.020 *et seq*., which requires an employer to provide earned, but unpaid, wages and compensation upon termination, fails to define "wages and compensation" either to include or exclude vacation pay. Moreover, the Nevada Supreme Court has yet to decide the issue. Nevertheless, in the "Frequently Asked Questions" section of its internet web page, the Office of the Labor Commissioner has stated: "Nevada requires payment only for time worked and does not require payment for vacation time [upon termination]. Civil action may be warranted in this case."

Even though the Nevada Labor Commissioner may not enforce the wage and hour statute to require the payment of unused vacation time upon termination, the Nevada statute does not foreclose that possibility. In addition, the Commissioner specifically recognized the right of a terminated employee to pursue recovery under a breach of contract theory. In either case, the employer's policy, whether oral or written, becomes extremely important. With very little Nevada case law on the subject, a review of the law in other states will shed some light on the issues involved as well as on the likely direction of future interpretation of the Nevada statute.

A. Creating the Employment Policy

The law has always recognized an employer's right to set the terms and conditions of employment. Consequently, an employer may choose to deny vacation benefits altogether. On the other hand, by its words or deeds, an employer may establish, or modify, its vacation policy, through either intention or inadvertence.

In creating a vacation policy, then, employers should take special care to ensure that all employees are informed of its provisions and, thus, bound by them. An Indiana case, *Die & Mold v. Western*, highlights this problem in the context of an oral vacation policy. There, the court rejected the employer's defense to a claim for unused vacation benefits. Although management personnel testified to the policy's unwritten requirement that the employee be employed on his anniversary date to become eligible for benefits, the court found no evidence that any of the employees were aware of that condition. Thus, the court denied the restriction and granted the employee his unused

aware of that condition." Thus, the court denied the restriction and granted the employee his unused vacation benefits. On the other hand, courts have readily denied vacation benefits to employees when they fail to meet conditions that were effectively communicated to them, by written policy or otherwise.

Employers also should take special care to ensure that all supervisory personnel are on the same page with respect to the interpretation and enforcement of their vacation policies. Inconsistent enforcement may alter the intended meaning of an employer's policy. In a recent Louisiana case, *Potvin v. Wright's Sound Gallery*, the court found the terminated employee was entitled to his unused vacation pay despite an unwritten company rule prohibiting remuneration for unused vacation time. The court relied principally on the fact that one of the company's co-owners, who was presumed to have full knowledge of company policies, had issued a check for the claimed amount shortly after the employee's resignation. Although the employer subsequently retracted the payment by stopping payment on the check, the damage had already been done. In effect, the employer had admitted that the vacation benefits were due and owning.

Therefore, as with any other contractual provision of employment, an employer should set, and enforce, the terms of its vacation policy with care. Whether oral or written, the employer should ensure that all employees are informed of the parameters of the promise and that its management personnel are taught to consistently apply those rules.

B. Modifying the Employment Policy

Courts usually consider an employee handbook to be a unilateral contract offered by the employer and accepted by the employee upon commencing and continuing to work. Generally, then, in order to modify the benefits provision, an employer must ensure that there is some sort of bargained for exchange between employer and employee. However, courts differ on the parameters of that exchange and on the effect of the resulting modification in determining the employer's liability for unused benefits at termination.

In a 1983 case, *Southwest Gas Corp. v. Ahmad*, the Nevada Supreme Court held that the employee's knowledge of the subsequent changes or additions, coupled with continued employment, is sufficient to hold employees bound by the new provisions. Still, many courts have recently held that employees are always bound by modifications to existing policies. The United States District Court for the District of Maryland stated: "[P]rovisions added to an employee manual after an employee is hired apply to that employee because it is understood that the employee consents to the policy modification by continuing to work." Moreover, according to some courts, this reasoning may apply whether the original agreement expressly reserves the right to modify the terms of the employment agreement or not and regardless of whether the employee is actually aware of the changes. Nevertheless, as a general rule, an employer should always be sure to notify employees *prior* to instituting any changes in its employment policy.

Once it is determined that the employee is entitled to some sort of vacation pay, employers are left to decide which one of its policies will set the terms – the policy in effect at the time of accrual, the

decide which one of its policies will set the terms—the policy in effect at the time of accrual, the policy in effect at the time of termination, or some combination thereof.

A number of courts have held that whether the terminated employee is entitled to accrued vacation pay upon termination is determined by the policy of the employer in effect at the time the work is performed and not the employer's policy that is in effect at the time of termination. In accordance with this theory, some courts, including courts in North Carolina and Oregon, have determined that even when the employer successfully changes the policy, the terminated employee is entitled to payment of all vacation earned according to the policy in effect prior to that change.

On the other hand, at least one court, the United States District Court for the District of Maryland, recently held that because employees could not demand cash payment for unused vacation time *during* employment, "whether or not [the employee] is entitled to her accrued vacation pay must turn on the personnel policy in effect at the time of her termination."

Unfortunately, it is not clear where the Nevada courts might lean in this regard. It would appear, however, that the better view holds that the policy in effect at the time of accrual controls. This view is consistent with the concept of vacation pay as wages because wages are earned as work is performed. Moreover, according to the unilateral contract theory discussed above, an employee chooses to take employment, in part, based on the policy in effect at the time of hire and the commencement of work.

C. Can the Policy Provide for Forfeiture of Vacation Benefits?

Many employers attempt to limit their liability for unused vacation benefits upon termination. These attempts meet with differing reactions depending on the state involved and the words employed. While employers may generally impose reasonable restrictions on the *accrual* of vacation benefits, as discussed below, they should avoid imposing conditions on the *payment* of accrued benefits.

A handful of states, including California, Illinois, and, most recently, Louisiana, have enacted legislation which specifically prohibits employment contracts or policies that provide for forfeiture of earned vacation pay upon termination. Rather, employers must pay accrued vacation pay upon termination where such benefits are offered in the employment contract or policy and the employee is terminated without having taken time off for vested vacation benefits.

The remaining states continue to recognize an employer's right to maintain full control over the parameters of the vacation benefits it offers, including denying them altogether, in its policy or contract of employment. Nevertheless, many states limit forfeiture where the payment of *accrued* vacation pay is conditioned upon so-called "conditions subsequent," as opposed to conditions precedent to accrual itself. The Montana Supreme Court recently declared that "vacation pay is earned by virtue of an employee's labor and once it has accrued … an employer may not then impose conditions subsequent which would, if unmet, effectively divest an employee of that accrued vacation."

The court emphasized that the employment contract at issue "provides one week paid vacation pay per year after the completion of the first year of employment (first anniversary date)" and states that "[a]t the end of the first year an employee has one week of paid vacation accrued." The contract included similar language regarding the two weeks earned after the second year of employment. The court emphasized: "Thus in no uncertain terms, [the company] states that it 'will provide two weeks paid vacation' to employees who reach their second anniversary date." The court concluded that employers can have reasonable restrictions on accrual, but once accrued, they can not impose conditions subsequent. Therefore, the court nullified the following conditions subsequent to the collection of unpaid vacation benefits upon termination: (1) that employees take vacation in consecutive days in the next calendar year, (2) that employees request vacation 30 days in advance, and (3) that employees work their regularly scheduled shifts both before and after vacation.

Nevertheless, properly worded vacation policies may impose valid and enforceable restrictions on the accrual of vacation benefits. Thus, even in California, where no "use it or lose it" provisions are permitted, the labor department recognizes provisions for establishing a ceiling on the amount of vacation or vacation pay that can accrue without being taken. California also allows provisions that no vacation is earned during the first year of employment, or any other reasonable period of employment, and that, when vacation is earned, it accrues at an accelerating rate during the year.

Courts have upheld other limits on the ability of an employee to collect otherwise accrued vacation benefits as well. For instance, an employer may require that an employee be employed on his or her anniversary date in order to be eligible for vacation benefits for the previous year. Moreover, a requirement that an employee give two weeks written notice of intent to terminate has been upheld as a valid condition precedent to the accrual of vacation benefits. Courts have also upheld the nonpayment of accrued vacation time when there was an express condition that if the employee quit, he was not entitled to unused accrued vacation time, or where the employer's personnel policies clearly stated that employees terminated for cause were not due cash representing accrued but unused vacation pay, or where there was a clear provision in the employee handbook providing that terminated employees were not eligible for any paid vacation.

Of course, these otherwise valid "conditions precedent" will be valid only where they are reasonable and not a subterfuge to deny an employee a vacation or vacation benefits. In fact, some courts have recognized actions for wrongful termination where an employee was allegedly terminated in order to avoid liability for said benefits.

In any case, as discussed above, it is important that the employee is made aware of any conditions imposed upon the right to receive vacation benefits. It is only when the employee is informed of such conditions before accrual that enforcement can be assured.

III. Vacation Pay And Vacation Benefits During A Strike

A related source of confusion for employers with vacation policies is their application during a strike. In this context, an employer's established vacation policy, and its record of enforcement,

becomes extremely important.

It is well settled that, under the National Labor Relations Act ("NLRA"), an employer may not deny accrued benefits during a strike absent proof of a legitimate and substantial business justification. Such justification may be that the employer relied on a nondiscriminatory contract interpretation that is reasonable and arguably correct. However, with respect to the denial of vacation benefits in particular, the National Labor Relations Board, in *Noel Foods*, categorically rejected the argument that "one cannot be a paid vacationer and an economic striker at the same time."

Nonetheless, when the striking employees request vacation pay in lieu of time off, the Board will readily deny their claim where the contract or handbook does not provide for vacation pay apart from taking time off. The claim will also fail where the contract provides that employees can receive pay in lieu of vacation time only in specified circumstances, such as termination and lay off. In such cases, the employee is not denied his or her rights, but rather seeks a benefit not provided for in the contract. It is important, however, that there be no evidence that the employer had ever departed from the terms of the contract and granted vacation pay in lieu of leave in the past.

Employee requests to take vacation time, as opposed to vacation pay, prove more difficult. If it is deemed a request to take vacation time, the employer's denial of the request will likely be considered lawful where the employee fails to meet some condition precedent in the contract, such as working at least 8 hours on the last scheduled workday before the vacation begins.

Without an express contractual limitation, the employer may prove it relied on some other reasonable and arguably correct interpretation of the contract. For instance, it may help that the employer maintains contractual provisions which leave it to the discretion of the employer to arrange the time of vacation to least interfere with the company's operations. In addition, a long-standing practice of canceling, or refusing to schedule, vacations during strikes may establish an enforceable term or condition of employment. Finally, the Board has recognized that "a common understanding of 'vacation' is respite from work" so that an employer's interpretation of the contract as precluding vacation leave during a strike may be reasonable and arguably correct and, standing alone, suffice to exonerate the employer.

In any event, forcing employees to reschedule, or forego, vacation time during a strike does not really divest them of accrued benefits, but rather merely postpones the enjoyment thereof. Thus, it is unlikely employers will be found in violation of the NLRA, absent some other proof of unlawful motivation.

IV. Family Medical Leave Act

Although a full discussion of the Family Medical Leave Act ("FMLA") is beyond the scope of this article, it bears some discussion in this context. The FMLA provides up to twelve weeks of unpaid leave for the serious health condition of the employee, his/her spouse, child or parent; or the birth of a child or placement of a child for adoption or foster care. According to the regulations interpreting the FMLA, an eligible employee may choose to substitute any accrued paid leave, including paid vacation or personal leave, for FMLA leave. According to FMLA regulations, "[n]o limitations may be

placed by the employer on substitution of paid vacation or personal leave for these purposes. On the other hand, if the employee does not so choose, the employer may require the employee to substitute accrued paid leave for FMLA leave. If neither the employee nor the employer elects the substitution, the employee shall remain entitled to all of the paid leave accrued or earned under the employer's plan.

While it may be clear that employers' FMLA policies should include provisions to this effect, it is also advisable that employers include a complementary provision in their paid vacation leave policy. This is especially the case where the employer will require that paid vacation leave be substituted for unpaid FMLA leave.

V. Employment Retirement Income Security Act

The Employment Retirement Income Security Act ("ERISA") covers employee welfare benefit plans, including a plan, fund, or program for medical, sickness, hospital, accident, disability, death, or vacation benefits. Any such plan, fund, or program therefore must generally comply with ERISA's reporting and disclosure requirements and be subject to its broad preemption rules. Nevertheless, the United States Supreme Court has held that the reference to vacation payments in ERISA should be understood to include only those rare instances where "either the employee's right to a benefit is contingent upon some future occurrence or the employee bears a risk different from his ordinary employment risk." In other words, an employer should be concerned about possible ERISA application only in the unlikely situation where vacation benefits do not come from the employer's general assets, but rather the employer has set aside separate funding.

VI. Vacation policy checklist

- Consider creating a written vacation policy and asking employees to sign an acknowledgement that they have received and reviewed the policy.
- Ensure that all supervisory personnel are aware of its provisions to ensure consistent enforcement. Consider placing application and enforcement of the vacation policy in the hands of one person or department.
- Ensure that all employees are aware of the vacation policy upon hire and immediately upon modification of its terms.
- Consider expressly reserving the right to modify the terms of the policy.
- Consider limiting vacation benefits to taking time off, including establishing a reasonable condition precedent to taking time off, such as requiring that each employee work at least eight hours on the day before vacation.
- Consider expressly reserving the right to reschedule or limit vacations, consistent with business necessity.
- Consider whether benefits will be allowed to accumulate.
- Consider whether unused vacation time will be paid upon termination and whether there will be any limits on that right.

any limits on that right.

- When limiting vacation rights, ensure that conditions expressly apply to the accrual, not merely the payment, of vacation benefits.

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