

Is Your Business Prepared to Deal with the Time Bomb of Vacation Pay Liability

As the US economy slowly begins to shake off the blow of the sub-prime mortgage crisis and the subsequent deep recession and associated high unemployment, employers now look forward to a warming economic trend and the possibility of adding or upgrading staff. Consequently, employees will necessarily become more mobile. While in 2009 and early 2010 most employees seem content to stay where they are, as the economy begins to rebound the siren call of greener grass will certainly make employees more willing to jump ship for the next big thing or even what is perceived to be merely a better deal. Employers will be faced with a host of employment law issues, some with significant fiscal consequences as a result of employees renewed mobility and desire to find a more fulfilling or at least more enriching work place. One of these potentially fiscally devastating issues is accrued, but unused vacation time which will be owed to employees as they resign or are terminated in favor of higher quality replacements.

As economic conditions change both employees and employers will decide if the time is right to find a better job, hire better talent or just generally try to improve the quality of the work place. This will result in numerous resignations and terminations so that employees can switch from one company to another. One consequence of this sudden surge in employee mobility will be the huge corporate liability for all these employees accrued but unused vacation. This liability accumulates daily throughout the Southern California business sector from the smallest mom and pop operations to Fortune 500 companies like the steady march of a river through a canyon.

As most California employees know, even better than their employers, an individual who does not use all of his or her accrued vacation pay cannot be made to forfeit the pay or the right to be paid for those days at a later date. A vacation policy which requires employees to "use or lose" their accrued vacation is not compliant with California law. Unfortunately, for most employers more employees are conversant with state law concerning vacation policies and their limitations than their employers, who have drafted and/or developed the policies under which these employees are granted vacation.

If you, as an employer, have a large work force with many senior employees who have accrued significant vacation time over their years of employment, having several of these employees leave your business at the same time can cause a staggering amount of damage to your cash flow and more importantly your bottom line. For these reasons, it is recommended that all California employers do a yearly audit of their potential vacation liability so that an appropriate plan of action can be created to limit the exposure. In addition, as an employer it's important to develop a solution for decreasing the liability over time so as not to have the company absorb a huge hit in anyone fiscal quarter or year. It does not take much imagination for employers to picture a scenario where several long term employees leave all at once creating a huge abyss in the company's cash flow.

Furthermore, even if many of these days were accrued when the employee was a rookie making close to minimum wage by the time that employee leaves those days are worth the same as the days accrued in the employee's 30th year of service. These funds must be paid, in almost all instances, within no more than 72 hours after the employee's separation. Fortunately for California employers there are tools to limit this liability and even actions which can be taken to reduce liability over time before each of these employees separates from your company.

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California Law is clear that an employee who is terminated without having taken all of the accrued vacation time must be paid for the vacation time as wages at his or her final rate of pay. In order to prevent such problems it is wise to have a vacation policy that includes a "cap" on a accruals. A cap provides an employee from earning additional vacation time after a specified amount of vacation has been accumulated. (Usually, though not legally required, two times the yearly vacation benefit). California Courts have held that unlike use it or lose it policies, which cause a forfeiture of vested vacation pay, caps on accrual are lawful since vacation pay in and of itself is a right only if the employer has agreed to provide paid vacation time.

That's right, there is no requirement that employees be offered paid vacation, though there are a multitude of excellent reasons for providing paid vacation benefits. Employers have the right to adopt policies that prevent accrual of vacation during certain waiting periods (i.e. a probationary or introductory period) or during certain leaves of absences assuming specific criteria are met. It should be noted however, that the Department of Labor Standards Enforcement ("DLSE") takes a fairly dim view of vacation accrual waiting periods that it considers a pretense. These policies, often called "cliff vesting" usually state an employee accrues no vacation during their introductory or probationary period but concurrently with completion of that period, has some amount of vacation immediately granted. In other words, employers should not simply try to circumvent vacation accrual for employees that might not survive their probationary period.

Vacations can be a wonderful source of morale for businesses allowing employees to recharge their batteries and rekindle their work energies by having some time away from the office, work site, or other place of employment. However, incorrectly drafted and/or enforced vacation policies can result in huge liabilities to long term employees based on unused vacation and/or multiple administrative claims or other annoyances including litigation if the polices are not well drafted and in compliance with California's ever changing web of employment laws governing vacation. The last thing a manager, business owner, or department head needs is to spend time dealing with issues arising from a poorly drafted and/or executed vacation policy which is intended to improve employee morale and performance. Most importantly during these difficult economic times can any business really face having to pay large sums of money to long term separating employees as a result of huge vacation banks?