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December 18, 2006

Jay Holmquist, General Manager
Nebraska Rural Electric Association
P.O. Box 82048
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Re: Recent legal developments regarding employer paid leave plans

Dear Jay:

You have asked that I provide a summary of the recent Nebraska Supreme Court decision in *Roseland v. Strategic Staff Management,* 272 Neb. 4324, ____NW2d ____ (2006) ("*Roseland*"), and the ramifications that the decision may have on Public Power Districts and Electric Coops. I further discuss options which your members may consider in handling their own policies governing paid leave plans offered to their employees.

On October 20, 2006, the Nebraska Supreme Court unanimously decided the *Roseland* case by issuing a written opinion declaring that "accrued vacation time, which is part of an employment agreement, is due and payable as wages upon termination of employment." Prior to this decision, many employers had policies governing their vacation (and sick) leave plans which did not allow for payment of unused time under certain circumstances. Some employers included "use it or lose it" policies in their leave plans, while others allowed for a carryover from year-to-year but provided that unused time would not be paid as wages upon termination. In light of the *Roseland* decision, each employer must reevaluate its policies regarding paid time off to ensure they comply with the law and, at the same time, do not expose the employer to unwanted liability for payment of wages for unused time. This is particularly true with respect to generous paid leave plans where the employer may allow the accrual of hundreds of days.

In *Roseland*, four employees, one of whom was the former president of the company, sued their former employer after voluntarily resigning their employment for payment of their accrued but unused vacation time. The employer's policy handbook provided that employees would be allowed one week of vacation after one year of employment, two weeks after two years of employment, and three weeks after five years of employment. The employer denied the claim for wages by citing to its policy handbook, which provided that "accrued, but unused vacation will not be carried over from year to year. Upon resignation or termination, employees will not be paid for vacation time available."

The employees in *Roseland* first prevailed in the District Court of Douglas County, which determined that the Nebraska Wage Payment and Collection Act (the "Act")[1] required that employees receive wages for their accrued but unused vacation upon termination. However, the Nebraska Court of Appeals disagreed. The Court of Appeals essentially determined that employers and employees are free to agree upon terms mutually acceptable, and that the agreement between the parties in *Roseland* provided that wages would not be paid for unused vacation. The employees in *Roseland* then petitioned the Nebraska Supreme Court to review the Court of Appeals decision.

The Nebraska Supreme Court's decision hinged entirely upon the language used in the Act. Under the Act, all wages owed at termination must be paid at the next regular payday or within two weeks of termination, whichever is sooner. The Act provides, in part, that, "**Wages** means compensation for labor or services rendered by an employee, **including fringe benefits**, when previously agreed to and conditions stipulated have been met by the employee, whether the amount is determined on a time, task, fee, commission, or other basis.... " The Act further defines fringe benefits as including "**sick and vacation leave plans**, disability income protection plans, retirement, pension, or profit-sharing plans, health and accident benefit plans, and **any other employee benefit plans** or benefit programs regardless of whether the employee participates in such plans or programs...." The Supreme Court concluded that since the definition of wages included fringe benefits, and because the definition of fringe benefits included vacation leave, earned vacation constitutes wages.

The Supreme Court determined that any provision in a policy handbook or agreement between an employee and employer which provides that wages will not be paid for earned but unused vacation time is contrary to the Act and therefore void. Thus, the employees in *Roseland* were entitled to receive wages for unused vacation time at the time of their terminations.

Although the *Roseland* decision was limited to the specific facts presented to the court, i.e. earned but unused vacation at termination, the decision has broader implications. Because vacation and sick leave plans are addressed in the exact same manner in the Act, the decision appears to be equally applicable to sick leave and perhaps other leave plans commonly offered by other employers. Thus, public power districts and electric coops must review all such plans to ensure that they accurately reflect the law and the intentions behind offering such paid leave.

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[1] Which applies to political subdivisions as well as cooperatives and private employers. *Neb. Rev. Stat.* § 48-1220(2).

The crux of the *Roseland* decision was the *accrual* of the right to take paid time off. Under the Court's rationale, once the employee meets the conditions entitling him or her to such a benefit, i.e. the right to take paid time off, the benefit cannot be taken away or forfeited. It becomes a wage which must be paid either during employment or, at the latest, termination.

The Court of Appeals has recently handed down a decision against one of the local cooperatives wherein the *Roseland* case was relied upon. Like *Roseland*, the case hinged upon unused vacation time. The court found *Roseland* dictated that the cooperative's former employee was entitled to approximately 37 days of pay for unused vacation he had available at the time of his termination, notwithstanding language to the contrary in the policy manual. The court reasoned that where an employee handbook provided that 1 day of vacation would be given per month, a wage was earned once the employee completed working during the month. Thus, the court focused on when the right to take paid time off was "earned", and held that any conditions provided for in the cooperative's policy handbook which provided the employee would forfeit vacation time after it was earned were void.

This decision further demonstrates that the courts are likely to apply *Roseland* to sick leave and other types of paid time off. While it certainly is reasonable to stipulate, for example, that earned sick leave cannot be taken unless the employee is actually sick, it would be logically inconsistent for the courts to allow for the forfeiture of sick leave after it is earned or has accrued. Since *Roseland*, the Nebraska Department of Labor has indicated that wages for unused sick leave must be paid upon termination.

This development in Nebraska's wage law creates several issues for employers. First, employers who have failed to pay wages upon termination for unused paid leave are subject to claims by former employees. The statute of limitations for such claims is four years where there is no written document evidencing the employment relationship, and five years in the case of written employment contracts. Although it is arguable, a plausible argument can be made that the statute of limitations in the case of employees who acknowledge receipt of written policy handbooks is five years as the handbook and signed acknowledgment constitute written documentation of the employment relationship. Thus, exposure to such claims from former employees can be quite broad.

One of the questions commonly being asked is whether the *Roseland* decision has retroactive application. Although not addressed by the court, I believe the court's answer would be yes. The reason is that the court purported to be applying the Act's definition of wages, which includes fringe benefits (which is defined to include vacation and sick leave plans), and these definitions have been in effect for many years. In other words, from its perspective, the court did not change the law; rather, it was applying the law that has been in effect for years. Consequently, employers should assume that claims not otherwise barred by the statute of limitations will be analyzed by the courts in the same way as *Roseland*.

Another issue employers must deal with is current employees with large amounts of accrued sick leave, vacation leave, or generally, paid time off. This issue is intertwined with the issue of how to modify policies governing the accrual of time off in the future. Two

principles are important in considering how to go forward. One is that, as stated above, *once the right to take time off accrues or is earned, it cannot be taken away*. Thus, for an employee who has earned 180 days of sick leave, for example, the employer cannot unilaterally take it away. The other important principle is that *the focus is on the accrual of the right to take time off* as agreed upon by the employer and the employee. The law does not prohibit employers to limit the accrual of paid time off. As such, when considering revisions to policies, the focus should be on limiting the right to accrue paid time off. Importantly, conditions placed upon paid leave *once it has accrued* will be void to the extent that such conditions result in a loss or forfeiture of the time or pay.

As you are aware, an attempt is underway to persuade the Nebraska Legislature to revise the Act. Hopefully, the attempt will succeed and the ability of the employer and the employee to agree to the terms they so choose will be restored. However, in the interim, public power districts and electric coops should take steps to limit the risks presented by the recent developments. There are numerous options available, some of which are discussed below.

First, employers who wish to allow employees to earn paid time off and receive pay for any or all unused time should not have to change their policies. This is not true, however, if their policy provides that unused time is lost or forfeited under any circumstances.

Generally speaking, employers will want to be very careful in stipulating how and when time accrues. Many employers have, in the past, provided that a specific amount of time is earned each year, and that if not used it is lost. In light of *Roseland*, a better way to attain the same result is to change the policy by setting a cap on the amount of time that can be accrued. For instance, rather than providing that two weeks per year is given and that unused time is lost, employers can simply provide that two weeks per year is given and that employees cannot accrue more than two weeks of time. Similarly, using sick leave as an example, employers can provide that one day per month can be accrued, but no more than 10 days total can be accrued. Once the employee reaches the limit, no additional time will accrue and the employer's exposure to claims for large amounts of wages for unused time will be limited. In light of *Roseland*, the employer will still have exposure to demands for wages for unused time; however, the cap limits that exposure to a manageable amount.

As to employers who presently have employees with large amounts of time accrued pursuant to past and present policies, one option is to adopt a new plan which 1) caps the number of days which can accrue, 2) provides that employees will be given credit for previously-accrued time, and 3) further provides that they will not accrue additional time until they have used enough of their previously-accrued time to bring them below the cap. For example, the policy could set the cap on sick leave at 30 days. Employees who had previously accrued 180 days would not accrue any additional days until after they use at least 151 days of their time. At that time they would be below the threshold of 30, and could accrue another sick day according to the accrual schedule stated in the new policy. No accrued time is ever taken from the employee.

As part of such a policy, the employer could require employees to use their accrued time so as to decrease the amount of unused time held by its employees. The employer is free to dictate when the employee can or will take paid time off, and it may make particular sense to do this to bring certain employees down to the new cap. Another option for employers is to "buy" accrued time from employees in order to bring all employees within the new cap.

While perhaps not a viable option for many employers competing in the employment market, some may wish to cut off their exposure to claims for wages for unused time altogether by eliminating certain paid leave plans. Again, employers are free to prohibit the accrual of any additional time from this point forward; they cannot, however, cause previously-accrued time off to be forfeited by eliminating a current leave plan.

The issue regarding sick leave seems to present the biggest concern for employers because many have afforded their employees very generous amounts of sick leave for dealing with catastrophic health or personal issues. As presently structured, many current plans leave employers exposed to large wage claims when an employee separates from employment. If the attempt to persuade the Legislature to change the Act is unsuccessful, employers who nevertheless want to offer generous sick leave to employees should consider new approaches. While there is no guarantee that exposure to wage claims will be eliminated, there are ways in which such plans might be structured in order to present a strong argument that wages are not owed.

For example, one alternative would be to create an annual sick leave bank whereby the employer puts in 300 days (the amount would obviously depend on the number of employees) and then allows employees to acquire credits which could then be used to take time off if all other conditions are met. The plan could provide that under no circumstances will the employer pay out more than the allotted days put in the plan. This type of plan may or may not lead to a result different from that in *Roseland* if presented to the court. However, the argument against payment of wages would be much stronger. If the employer is going to offer generous leave anyway, there is not much lost by using such approach. Obviously, there are numerous ways in which such plans could be structured, and it is advisable to consult with an attorney to seek help in devising the specific language to use in setting forth the plan.

One last consideration for revising paid leave plans is the rate of pay. Generally, the rate of pay to employees is left to whatever the employer and the employee agree to. For example, an employee and an employer are free to agree that one rate of pay is applicable when performing certain tasks, but that another rate is applicable when performing other tasks. The only limitations are those set forth by state and federal minimum wage and overtime laws. In light of this, it may be advisable for employers provide a different, lower rate of pay in their long term leave plans. Just as some disability insurance policies provide for payment of less than full regular wages, a sick leave policy could provide that time will be paid at something less than the employee's regular rate (but not less than the federal minimum wage). Such a sick leave rate should be the same and not be dependent on whether wages are being paid for actual leave taken or for unused time at termination. This approach would allow some benefit to employees with health issues, while also providing less exposure for payment of unused time at termination. It may also discourage abuse of the benefit.

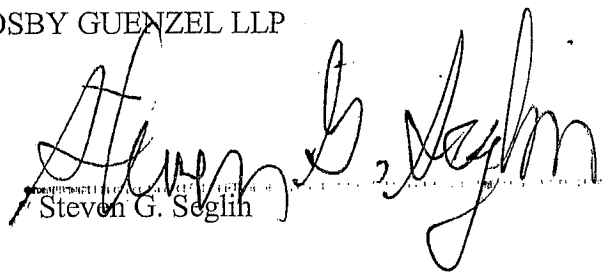
The above options will not be suited for all employers, as each presents different circumstances. As to employers seeking to revise their policies, it is advisable to seek the aid of an attorney familiar with this area of the law to ensure that the new policy does not present unintended risks. This is particularly true in light of some of the unanswered questions which remain following the *Roseland* case. Careful drafting may be the difference between a successful wage claim and one that is rejected by the courts.

Lastly, your members should be advised that the incidence of claims for wages will likely increase in light of *Roseland.* The Act provides that a successful employee is entitled to attorneys fees. Also, employers may be exposed to additional, significant statutory penalties equal to twice the wage award where the court finds the employer willfully refused to pay wages on a clearly valid claim. Consequently, employers should consult with their attorneys before determining whether to pay or reject a claim for wages.

I would be happy to further discuss any of these issues with you or your members. I will be following additional developments in this area and will advise you of the same as I receive them.

Sincerely,

CROSBY GUENZEL LLP

By 
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