CDLE’s Official Guidance on Use-It-Or-Lose-It Vacation Policies: Still Prohibited

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The use of so-called “use-it-or-lose-it” vacation pay policies is receiving significant attention in Colorado, both from the Colorado Department of Labor and Employment (CDLE) and from employers trying to make sense of the CDLE’s recent announcements. A typical use-it-or-lose-it policy includes a clause with a date by which employees must use their earned and accrued vacation hours to avoid forfeiting or losing those hours. There has been a lot of confusion regarding the legality of these policies under the Colorado Wage Claim Act (CWCA). However, despite recent CDLE guidance, Colorado law has not changed: vacation pay is a wage that cannot be subject to forfeiture. Like all forms of wages, vacation pay cannot be taken from employees once earned. Under the CWCA, requiring employees to forfeit earned vacation hours because the hours are unused is analogous to requiring them to forfeit their paychecks because the funds sit unused in the employees’ personal checking accounts.

Although use-it-or-lose-it policies violate Colorado law, employers have other—less risky—options to achieve a similar result. Below we discuss the state of Colorado law—both statutory and case law—on this issue as well as the CDLE’s recent guidance on use-it-or-lose-it vacation policies. We also provide several reasons why Colorado employers may want to impose a cap on employees’ vacation accrual provisions, thereby restricting their ability to continue earning vacation hours once they accrue the number of hours selected as the cap.

**Colorado Law on Use-It-Or-Lose-It Vacation Pay Policies**

Under the CWCA, the terms “wages” and “compensation” are used interchangeably and include “vacation pay earned in accordance with the terms of any agreement.” Consequently, if an employer provides employees with paid vacation, it must pay the employee at the end of the employment relationship for all of his or her unused accrued vacation. Indeed, under Colorado case law, employees who have an enforceable right to receive payment for accrued leave under an employment agreement or policy have a vested interest in that compensation when it is earned. For example, the Colorado Supreme Court held that “accrued leave is, in effect, a debt due to the employee as part of the compensation the employee has earned for work already performed.” In re Marriage of Cardona & Castro, 316 P.3d 626, 634 (Colo. 2014).

Once an employee earns “compensation,” he or she is entitled to it. Accordingly, a use-it-or-lose-it policy requiring employees to forfeit a portion of their accrued vacation time, which is deemed “earned compensation,” violates the CWCA.

**Colorado Courts and “PTO” Policies**
Unlike vacation pay, an employee's accrued sick time is not considered "wages" or "compensation" under the CWCA. The same goes for "personal" time when personal time is granted to employees separate and apart from vacation time. Therefore, unlike vacation pay, a use-it-or-lose-it policy for sick or personal time is likely permissible under Colorado law.

However, when an employer lumps paid vacation, sick, and personal time into one bank and refers to the bank as paid time off (or PTO), the entire bank can potentially be used as vacation pay and could fall within the CWCA’s definition of "wages." Unless the policy expressly states PTO is not to be paid out for vacation leave or otherwise distinguishes between vacation, sick, and personal leave, a court will be unable to differentiate between PTO that can be used for vacation and PTO that is limited to sick or personal leave. Indeed, in a different context, the Colorado Supreme Court recognized that the "value of leave . . . may be . . . difficult to ascertain" in instances where "different types of leave [are] combined in one comprehensive paid time off (PTO) plan." In re Marriage of Cardona & Castro, 316 P.3d 626, 635 (Colo. 2014).

Even though Colorado courts have not squarely addressed this issue, employers should ensure that they do not inadvertently violate the CWCA. Accordingly, the analysis for use-it-or-lose-it vacation policies also applies to most use-it-or-lose-it PTO policies that are simply a different way to characterize vacation. While it would be beneficial to employers and a welcomed ruling, we find it hard to believe that a Colorado court will uphold a use-it-or-lose-it PTO policy where the PTO is earned and accrued by the employee and can be used for vacation simply because the employer calls it PTO instead of vacation. We are not aware of any Colorado court endorsing this approach and believe there is significant risk in use-it-or-lose-it PTO policies that include an earned and accrued vacation component.

The CDLE’s Use-It-or-Lose-It Guidance

In 2014, the Colorado legislature implemented the Wage Protection Act of 2014, which amended the CWCA giving the CDLE enhanced ability to enforce the requirements of the CWCA. The amendments include:

1. establishing a procedure for the CDLE to adjudicate complaints for unpaid wages or compensation of $7,500 or less per employee;
2. increasing fines that can be imposed on employers; and
3. providing attorneys’ fees for employees paid less than the applicable minimum wage.

Along with an enhanced ability to enforce the CWCA requirements, the CDLE informally announced that use-it-or-lose-it vacation policies are impermissible under the CWCA and that it plans to target employers that use such policies. This informal announcement prompted much confusion as employers across the state questioned whether their use-it-or-lose-it policies violated Colorado law.

Based on the response to its informal announcement, the CDLE released official guidance in October 2015 presumably to clarify its interpretation of the law. In the frequently asked questions on the CDLE’s website, the agency indicates that use-it-or-lose-it provisions in vacation agreements "are permissible under the Colorado Wage Protection Act, provided that any such policy is included in the terms of an agreement between the employer and employee." However, employers should be cautious in broadly interpreting this statement to allow use-it-or-lose-it provisions...
that take away earned vacation time. Colorado courts likely will not uphold a use-it-or-lose-it policy simply because it is embodied in “an agreement” between an employer and its employees. To do so would essentially permit employers to declassify vacation as wages simply by decreeing it in its policies. Indeed, the next sentence of the CDLE’s official guidance states that a use-it-or-lose-it policy “may not operate to deprive an employee of earned vacation time and/or the wages associated with that time.”

According to the CDLE, the permissibility of a “use-it-or-lose-it” policy depends on whether and when the vacation time is considered “earned.” The CDLE also states that it will consider several factors in determining the answer to this question, including the employer’s historical practices, industry norms, and the subjective understandings of the employer and employee. This list of factors does not provide employers with clear guidelines in deciding whether their provisions will be deemed permissible by the CDLE.

Colorado employers should remain cautious when deciding whether to implement or retain a use-it-or-lose-it vacation policy. The CDLE’s guidance on the issue does not bind Colorado courts. The courts are not likely to interpret the CWCA as allowing use-it-or-lose-it vacation policies as they apply to earned and accrued vacation because the statute expressly states that vacation pay earned falls within the statute’s definition of wages. In fact, as described above, the Colorado Supreme Court recently relied on the CWCA in the context of a domestic court case to hold that vacation pay accrued is a “debt due to the employee.”

**Alternatives to Use-it-or-Lose-it Vacation Pay Policies**

To comply with Colorado law, employers should avoid use-it-or-lose-it vacation policies and consider implementing a cap on accrual instead. Under a cap policy, once an employee earns a certain number of vacation hours, he or she no longer accrues further vacation time until the employee takes some of his or her previously accrued vacation. After an employee uses vacation hours, vacation pay will again accrue at the usual rate. Employers are not required to retroactively grant employees the amount they would have earned during the time their accrued vacation exceeded the cap. Caps on accrual also have the effect of incentivizing employees to use their vacation hours because failure to do so essentially leaves money on the table.

While Colorado law is silent on the issue, other states that prohibit use-it-or-lose-it policies have published guidance on what constitutes a reasonable cap. For example, in California some suggest that employers set caps at anywhere from 1.5 to 2 times the annual accrual rate. Using this guidance, the cap could be in the range of 60 to 80 hours for an employer that allows employees to earn 40 hours of vacation per year.

Under a cap system, employees do not accrue vacation pay and later forfeit a portion of the total amount, which is akin to taking away compensation. Rather, employees are limited in the amount of vacation hours they are permitted to earn (or accrue) and are never required to forfeit wages.

**Conclusion**

Regardless of recent guidance by the CDLE, employers should continue to avoid use-it-or-lose-it vacation policies because such policies likely violate the CWCA. The use of catch-all PTO policies that include a use-it-or-lose-it provision is also dangerous
because employees may be forced to forfeit unused but accrued vacation time, which is considered earned wages under Colorado law. To accomplish the benefits of a use-it-or-lose-it policy, companies should consider a cap to limit vacation pay accrual.