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Opinion No. 06-169

Employees' Entitlement to Unused Vacation Pay upon Termination of Employment Pursuant to Tenn. Code Ann. § 50-2-103(a)(3)

QUESTION

Whether Tenn. Code Ann. § 50-2-103(a)(3) requires that an employee's final wages include unused "vacation pay or other compensatory time" upon the employee's termination of employment?

OPINION

No. Unless the employer's policy or its labor agreement specifically requires compensation of unused "vacation pay or other compensatory time" to an employee upon his or her termination of employment, Tenn. Code Ann. § 50-2-103(a)(3) does not require that an employee's final wages include such compensation.

ANALYSIS

We have been asked to clarify a previous Attorney General Opinion in which we concluded that, under the Wage Regulation Act ("Act"), "an employee who has accrued vacation leave under his or her employee's employment policy . . . is entitled to receive payment for accumulated vacation leave upon termination of employment." Op. Tenn. Att'y Gen. No. 00-132 (Aug. 17, 2000) (quoting Tenn. Code Ann. § 50-2-103(a)(3)). Upon review, we conclude that the Opinion interpreting the cited provision of the Act is ambiguous and in need of clarification.

The Act applies to private employers that employ five or more employees. Tenn. Code Ann. § 50-2-103(b). In particular, section 50-2-103(a) governs the compensation of employees in private employment settings. The General Assembly amended section (a) of the statute in 1999, adding the provision at issue here, *see* 1999 Tenn. Pub. Acts ch. 32, § 1, which provides as follows:

> (a) All wages or compensation of employees in private employments shall be due and payable as follows:

> (1) All such wages or compensation earned and unpaid prior to the first day of any month shall be due and payable not later than the twentieth day of the month following the one in which such wages were earned;
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> (2) All wages or compensation earned and unpaid prior to the sixteenth day of any month shall be due and payable not later than the fifth day of the succeeding month; and
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> (3) For the purposes of this subsection (a), *the final wages of an employee who quits or is discharged shall include any vacation pay or other compensatory time that is owed to the employee by virtue of company policy or labor agreement. This subdivision (a)(3) does not mandate employers to provide vacations, either paid or unpaid, nor does it require that employers establish written vacation pay policies.*

Tenn. Code Ann. § 50-2-103(a) (2006) (emphasis added). The Department of Labor and Workforce Development ("Department") is empowered to enforce these provisions, the violation of which constitutes a class B misdemeanor. *Id.* at §§ 50-2-103(i)-(j). In addition, the Department may assess a civil penalty for willful violations of these provisions. *Id.* at § 50-2-103(i).

Your question states that Opinion No. 00-132 ostensibly disregards the effect of an employer's policy on the payment of unused vacation pay. You also note that many Tennessee employers' policies do not pay employees for unused vacation pay when the employee quits or is discharged. This is commonly referred to as a "use-it or lose-it" policy.

The Department, relying on our previous Opinion, has interpreted Tenn. Code Ann. § 50-2-103(a)(3) as requiring payment of unused accrued vacation pay to an employee when he or she quits or is discharged, even if the employer's policy disallows such payment.[1] The Department views vacation pay as "accrued" and, therefore, protected from an employer's policy that would forfeit such compensation. To support its interpretation, the Department principally relies on *Rose v. Tipton County Pub. Works Dept.*, 953 S.W.2d 690, 693 (Tenn. Ct. App. 1997); and *Vargo v. Lincoln Brass Works, Inc.*, 115 S.W.3d 487, 491 (Tenn. Ct. App. 2002), in which the Court of Appeals stated the well-known rule that, to construe provisions in employee handbooks as part of an employment contract, they must be phrased in binding terms to both employer and employee. In the Department's view, an employer's policy manual or handbook that forfeits or limits "accrued" vacation pay must be binding on employer and employee, and not subject to rescission by the employer. Under the Department's interpretation of Tenn. Code Ann. § 50-2-103(a)(3), absent a binding agreement regarding unused vacation pay that allows forfeiture or limitation of this type of compensation, an employee's final wages must include unused vacation pay.

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[1]The Department, however, agrees that an employer's "use-it or lose-it" vacation policy could be properly enforced.

The question posed is one of statutory interpretation, requiring us to determine whether the Department's interpretation of § 50-2-103(a)(3), in light of our previous Opinion and of the Court of Appeals' decisions, is reasonable. In construing statutes, we must "ascertain and give effect to the legislative intent without unduly restricting or expanding a statute's coverage beyond its intended scope." *Wilson v. Johnson County*, 879 S.W.2d 807, 809 (Tenn. 1994). When the statute is unambiguous, legislative intent is determined from the statute's plain and ordinary meaning of the language used. *Freeman v. Marco Transp. Co.*, 27 S.W.3d 909, 911 (Tenn. 2000). The statutory language must be "read in the context of the entire statute, without any forced or subtle construction which would extend or limit its meaning." *National Gas Distribs. v. State*, 804 S.W.2d 66, 67 (Tenn. 1991).

We note that, in Tennessee, "interpretations of statutes by administrative agencies are customarily given respect and accorded deference by courts." *Riggs v. Burson*, 941 S.W.2d 44, 50-51 (Tenn. 1997) (citing *Chevron U.S.A. v. Natural Resources Defense Council*, 467 U.S. 837, 844 (1984)). Accordingly, courts will defer to the Department's interpretation without substituting "their own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency." *Chevron*, 467 U.S. at 844.

Applying the above principles of statutory interpretation, we conclude that, unless the employer's policy or the labor agreement requires compensation of unused "vacation pay or other compensatory time" to an employee upon his or her termination of employment,[2] Tenn. Code Ann. § 50-2-103(a)(3) does not require that an employee's final wages include such compensation. As a threshold matter, we conclude that Tenn. Code Ann. § 50-2-103(a)(3) is unambiguous and, therefore, we determine legislative intent from the plain meaning of the statute's language. *Freeman*, 27 S.W.3d at 911. The statute's plain text predicates payment to an employee of unused vacation pay on the existence of a company policy or a labor agreement that would provide for such compensation. Under the law, an employee's final wages upon termination must include vacation pay "that is owed by virtue of company policy or labor agreement." Tenn. Code Ann. § 50-2-103(a)(3). The prepositional phrase "by virtue of" means "because of." *Webster's New World College Dictionary* 1597 (4th ed. 2001). Thus, an employee's final wages shall include unused vacation pay only if an employer established a relevant policy and if that policy *obligates* the employer to pay for such compensation. Likewise, in cases when an employment contract exists, an employee must be compensated for unused vacation pay if the contract *requires* such compensation. The second sentence in § 50-2-103(a)(3) also supports our reading of the statute. This sentence clarifies that employers need not provide paid or unpaid vacations to its employees or that employers need not establish written vacation pay policies. Hence, it follows that, by not establishing a vacation pay policy with respect to termination, or by not including such a clause in an employment contract, an employer would not have to compensate its employees for this time.

In essence, the text of the employer's company policy or of its labor agreement, if any exists,

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[2]By "termination," we mean that an employee either was involuntarily terminated, or voluntarily terminated the employment relationship. We also assume that the employer's policy is in effect at the time of the employee's termination.

will dictate whether an employee's "final wages," under Tenn. Code Ann. § 50-2-103(a)(3), "shall include any vacation pay or other compensatory time." Section 50-2-103(a)(3) effectively gives the force of law to an employer's policy or to a labor agreement on the issue of whether unused vacation pay is owed to an employee at his or her termination.

We respectfully disagree with the Department's construction of § 50-2-103(a)(3). Under the Department's interpretation, if the employer established a "use-it or lose-it" vacation policy, or a policy that forfeits any unused vacation pay, the Department would nevertheless require that the employee's final wages include vacation pay because the employee already would have "accrued" it. This interpretation disregards the effect of the employer's unused vacation policy contrary to the plain meaning of § 50-2-103(a)(3). As we noted above, if the employer's vacation policy[3] specifically disallowed such compensation upon an employee's termination, the employee's "final wages" would not include vacation pay because this pay would not be owed "by virtue of company policy." Tenn. Code Ann. § 50-2-103(a)(3).

We note that the circumstances under which a court may determine that a vacation pay policy or a employment contract creates a binding obligation to deem unused vacation pay "owed" to the employee upon termination will vary upon the facts of the case. Cases such as *Rose* and *Vargo* would be relevant to determine whether the employer's policy or the employment contract constitutes a binding agreement so that the employee's "final wages . . . shall include any vacation pay or other compensatory time that is owed to the employee by virtue of company policy or labor agreement." Tenn. Code Ann. § 50-2-103(a)(3).

[3]We see no material analytical distinction between an employer's "use-it or lose-it" vacation policy and a policy that allows for "forfeiture" of unused vacation time at termination. In our view, these are both forfeiture policies and in neither case, as we show in the above examples, would the employee's final wages include vacation pay.

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