



Governed by GASB? Learn the New Rules on Compensated Absences

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Agenda

- High-level – what and why
- Review existing guidance
- Definition and examples of compensated absences
- Calculation
- ACFR reporting and disclosure
- Implementation
 - Policy considerations
 - Tackling gaps in information
 - What are the challenges?

Guidelines for today's session

- Ask questions throughout
- Take notes (but the PowerPoint will be given to you!)
- Have fun!
 - *Wrong:* The meat and potatoes of vacation accounting
 - *Correct:* A Cheeseburger in Paradise



ChatGPT

Certainly! The number 101 has been used in various cultural contexts. Here are some examples:

1. Movies:

- "101 Dalmatians": A classic Disney animated film (1961) and its live-action adaptations.
- "101 Reykjavík": An Icelandic film released in 2000.
- "101 Rent Boys": A documentary film released in 2000.

2. Books:

- "Room 101" in George Orwell's novel "1984": Room 101 is the place in the novel where people's worst fears are realized, reflecting the idea of psychological manipulation and control.
- "101 Ways to Bug Your Parents" by Lee Wardlaw: A children's novel published in 1996.
- "101 Dalmatians" by Dodie Smith: The novel that inspired the Disney animated film.

6. Pop Culture:

- **101st Airborne Division:** A well-known unit of the United States Army, famous for its actions during World War II, particularly in the D-Day invasion of Normandy.

GASB 101, Compensated Absences

- **What's Changing?**
 - Provide guidance for all leave, not just vacation and sick time
 - Book liability for what is earned and likely to be paid, not what is paid on termination
 - Provide guidance on measuring the amount due within one year
 - Require only a net increase/decrease in the notes
- **Why?**
 - Government PTO policies have significantly changed since these standards were issued
- **When?**
 - Year Ends after December 15, 2024 (12/31/2024 & 9/30/2025)

What's NOT Changing?

- Does NOT supersede GASB 47, *Accounting for Termination Benefits*
- Termination Benefits (AKA Severance Pay) = pay/benefits paid triggered upon the termination of an employee (or announcement of intent) (AKA layoffs)
- Compensated absences = earned during employment

Existing Definition:

Statement 16 defined compensated absences in paragraph 1 as “absences for which employees will be paid, such as vacation, sick leave, and sabbatical leave.”

Why the change?

GASB identified several primary reasons to revise the guidance:

1. Lack of guidance for certain types of leave
2. Inconsistent application of standards
3. Changes to the conceptual framework have been made since GASB 16

1) Lack of guidance for certain types of leave

Statement 16 differentiated between different types of paid leave, specifically:

- Vacation leave
- Sick leave

Since that time, governments have increasingly adopted PTO, comp time, and other forms of leave

2) Inconsistent application of standards

Application was inconsistent in practice:

- Accrual of sick leave
- Disclosure of changes in long-term liabilities
- Amounts due within one year

3) Conceptual Framework changes

The provisions in GASB 16 have not been evaluated in light of the conceptual framework with regard to 1) what note disclosures should be required, and 2) whether and when compensated absences should be recognized as a liability.

3. A *compensated absence* is leave for which employees may receive one or more (a) cash payments when the leave is used for time off; (b) other cash payments, such as payment for unused leave upon termination of employment; or (c) noncash settlements, such as conversion to defined benefit postemployment benefits. The payment or settlement could occur during employment or upon termination of employment. Compensated absences generally do not have a set payment schedule. Examples of compensated absences include vacation (or annual) leave, sick leave, paid time off (PTO), holidays, parental leave, bereavement leave, and certain types of sabbatical leave.

GASB 101 outlines three criteria for what is reported as a compensated absence:

1. Does the absence accumulate? (i.e. carries to future periods)
2. Is the absence attributable to services performed?
3. Is it more likely than not (>50%) to either be paid or settled through other means?

1) Does the absence accumulate?

An absence that accumulates is one that can be carried forward from the reporting period in which it is earned to a future reporting period when it will be paid or settled.

For example, an employee who does not use all the vacation time earned in one year may have the ability to use it in the next year.

In contrast, paid holidays that are linked to a specific date often are required to be used when the holiday occurs.

2) Is the absence attributable to services performed?

An absence that is attributable to services rendered is one for which an employee has already performed the services required to earn the absence.

Likely to be based on services performed:

- PTO
- Sick leave
- Comp time
- Sabbatical leave

May or may not be based on services performed:

- Holidays
- Military leave
- Maternity leave
- Bereavement leave
- Jury duty

3) Is it more likely than not (>50%) to either be paid or settled through other means?

To estimate whether an absence is *more likely than not* to be paid or settled, consider several relevant factors:

- Employment policies (esp. if some leave differs by class of employee)
- Whether benefits for services rendered are not payable now but may become eligible for payment in the future
- Historical precedent/experience, unless aware of information indicating that historical data is not representative

Exceptions

GASB 101 specifies certain types of leave that should be recognized when the leave **commences** or is **used**, rather than when the leave is **earned**.

- **Recognize on commencement:** Leave that is dependent upon the occurrence of a sporadic event that affects a relatively small proportion of employees in any reporting period (parental leave, military leave, and jury duty)
- **Recognize when used:** unlimited PTO, holiday leave that must be used on a specific date

Pooled leave

If the leave is not attributable to a specific employee as of the date of the financial statements (for example, if leave has been donated to a shared employee leave pool), a government should measure the liability using an estimated pay rate that is representative of the eligible employee population.

Noncash settlement

For leave that is more likely than not to be settled through noncash means, measure the liability based on the amount for which it is more likely than not to be settled.

- Exception: DB OPEB – **do not** recognize compensated absences for leave to be converted to DB OPEB

Practical Consideration

It's reasonable that most or all regular leave types will be eventually used or paid on termination. But what about huge leave balances beyond what pays out at termination?

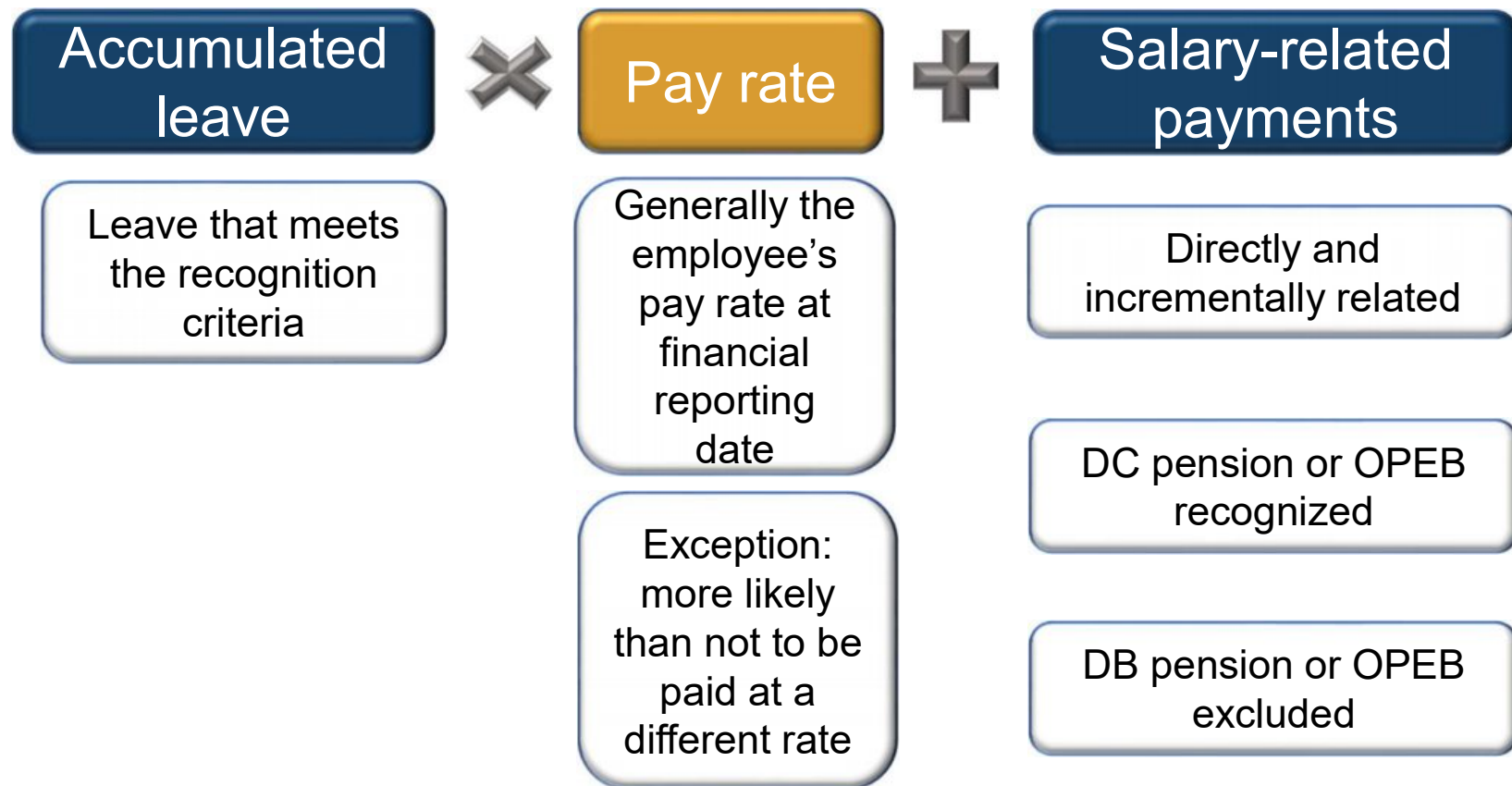
Example:

Joe is a longtime employee who earns 120 hours of vacation per year. As of 9/30/2025, Joe has a vacation balance of 684 hours. Company policy allows for payment of 80 hours upon termination. Joe does not get out much and never takes all his vacation; for the last 5 years, he has used vacation of 64, 36, 100, 44, and 50 hours.

How much should be recognized as compensated absences?

Auditor's Perspective – Management's Estimate

- **Keep in mind – Auditor's perspective for estimates > acceptable error for other areas**
- **Consider example: Expected \$1.0m, actual 1.1m**
 - Cash = sad auditor :(
 - Estimated comp abs = PFW :D
- **Auditor's responsibility less about precise \$ of the balance**
 - More emphasis on the reasonableness of:
 - The methodology
 - The inputs used for estimating
- **Large emphasis on evidence of bias**



Directly and Incrementally Associated

- **Direct** = the amount of the payment depends on the salary paid
 - The more you make, the bigger it will be
- **Incremental** = the gov't will make a payment in addition to a payment for the salary
- Example: Contributing to a DC Pension plan
 - If they take the leave, you contribute (AKA this is incremental)
 - If they retire, you don't contribute (AKA NOT incremental)
- Example: FICA/Medicare

If we may muddy the water...

- DC Pension – should you split out amount estimated to be taken at retirement vs. amount estimated to be taken upon use?
 - If they retire, you don't contribute to pension
 - If they take leave, you do contribute

The provisions of this Statement need
not be applied to immaterial items.

Rate of pay

- Use rate that the accumulated leave is expected to be settled with (the pay rate as of FYE in most cases)
- Changes due to change in pay rate should be recognized in the period of the change
 - Translation – don't worry about raises that took effect right after year-end
- Consider policy situations where a different rate of pay is used. Examples might be:
 - Sick leave paid at 50% of pay rate
 - Leave paid at 50% of pay rate upon termination (e.g., estimate how much would be paid during employment and how much will be paid on termination)

Salary-related payments

- Defined as “additional obligations that a government incurs related to paying an employee for services rendered”
- Include salary-related payments that are directly or incrementally associated with payments or settlements to be made for compensated absences
 - Directly associated: amount of the payment is a function of the salary to be paid (i.e. FICA)
 - Incrementally associated: payment made in addition to the payment for the compensated absence

Salary-related payments – Defined Contribution (DC) Pensions and OPEB

- Salary-related payments related to DC pension or OPEB that are directly and incrementally associated with payments to be made for compensated absences should be:
 - Recognized as pension/OPEB expense when the compensated absence is recognized
 - Included as part of compensated absences, NOT reported as a pension or OPEB liability
 - Only recognize a pension/OPEB liability when the leave is used
- Future changes to this calculation due to changes in contribution rate should be recognized in the period of the change

Salary-related payments – Defined Benefit (DB) Pension and OPEB

- Salary-related payments related to DB pension or OPEB are not included
- Rationale is that the future contributions are already reflected in the existing pension and OPEB liabilities

Amount due within one year

- GASB 101 does not provide guidance on estimation of the amount due within 1 year
- If employment policies specify a FIFO or LIFO approach to taking leave, it would be reasonable to mirror that approach
- Practical approach: if you've been using a flat %, can you support **why?**

Reporting in financial statements

- No significant changes to current guidance
- Not recognized in governmental funds except for amounts due as of the F/S date (i.e. an employee terminated at YE but paid after YE)
- For DC pension/OPEB: include accrued amounts in pension/OPEB expense

Notes to the financial statements

- Removes requirement to disclose liquidating funds
- Adds option to present a net change, rather than increases and decreases
 - Must state that the amount is a net change

Determining leave more likely than not to be used

From SYSTEM		From SYSTEM	Calculated	Calculated	Calculated
		Accumulated (unused) sick days as of date of termination	Days earned over service years	Sick days used over service years	Weighted Average sick days used over service years
Years of service	A	C	D (A*12 days)	E (D-C)	(A*E)
Former employee #1	8	42	96	54	432
Former employee #2	9	45	108	63	567
Former employee #3	12	40	144	104	1,248
Former employee #4	17	70	204	134	2,278
Former employee #5	22	100	264	164	3,608
Former employee #6	28	179	336	157	4,396
Former employee #7	32	160	384	224	7,168
Totals	128				19,697
Average	18 A				154 F
Average years of service for employees with over 18 years of service	27 AA				185 G

Days earned annually

12 HR1 - From HR records

Determining amount of salary-related payments

	<u>For leave that is used as time off</u>
Social Security (6.2%)	6.20%
Medicare (1.45%)	1.45%
457b DC plan (5%)	<u>5.00%</u>
Total % of salary related payments	12.65% F1

Calculating the current year liability

	From SYSTEM	From SYSTEM	Calculated	From SYSTEM	Calculated	Calculated	Calculated	Calculated	Calculated	Calculated	Calculated
							Identify the expectation, days more likely than not to be used based on former employee sample	Days more likely to be taken in future based on average days used by former employees	Days more likely than not to be used, capped by days accrued as of FYE	If Days more likely than not to be used are ZERO, estimate on individual basis	Estimated Liability of days more likely than not to be used by employees as sick time off
Active employees	Years of service to date	Daily pay rate	Days earned to date	Accrued unused sick leave days at FYE	Days used over service years to date	Average days used annually	R*	N*	O*	P*	Q ((P+O)*I)
	H	I	J (H*HR1)	K	L (J-K)	M (K / H)					
Active employee 1	5	\$ 223	60	38	22	4.00	154	132	38	-	8,474.00
Active employee 2	6	\$ 238	72	40	32	5.00	154	122	40	-	9,520.00
Active employee 3	7	\$ 461	84	30	54	8.00	154	100	30	-	13,830.00
Active employee 4	7	\$ 346	84	28	56	8.00	154	98	28	-	9,688.00
Active employee 5	8	\$ 384	96	50	46	6.00	154	108	50	-	19,200.00
Active employee 6	10	\$ 238	120	48	72	7.00	154	82	48	-	11,424.00
Active employee 7	12	\$ 269	144	36	108	9.00	154	46	36	-	9,684.00
Active employee 8	12	\$ 169	144	52	92	8.00	154	62	52	-	8,788.00
Active employee 9	15	\$ 338	180	42	138	9.00	154	16	16	-	5,408.00
Active employee 10	16	\$ 319	192	110	82	5.00	154	72	72	-	22,968.00
Active employee 11	16	\$ 288	192	100	92	6.00	154	62	62	-	17,856.00
Active employee 12	18	\$ 423	216	145	71	4.00	185	114	114	-	48,222.00
Active employee 13	20	\$ 461	240	120	120	6.00	185	65	65	-	29,965.00
Active employee 14	24	\$ 365	288	160	128	5.00	185	57	57	-	20,805.00
Active employee 15	29	\$ 403	348	154	194	7.00	185	-	-	7	2,821.00
Active employee 16	34	\$ 576	408	200	208	6.00	185	-	-	6	3,456.00
											\$ 242,109.00
											22.67% F1
											Salary-related payments \$ 54,886.00
											Total Compensated absences liability \$ 296,995.00

Interested in learning more?

- This template is available from GFOA at www.gfoa.org
- Search "Compensated Absences Tool – FIFO and LIFO", and it can be accessed with a GFOA member login
- We're happy to chat if you have questions, so feel free to reach out! (our contact info is on the last slide of this presentation)

Getting a Head Start

- **Review leave policies**
 - Are policies overly complex?
 - Ensure that leave policies aren't becoming de-facto retirement or severance pay
 - Large unused balances may be evidence that the leave is difficult to use
- **Policy amendments can still be made before implementation – if you start early**

Getting a Head Start

- **Get with HR on what info is available**
 - Several estimates or assumptions will need to be informed (hopefully) with some data
 - Leave earned and taken by employee over time
 - How much are “other” forms of leave actually used? (sick)
- **Start developing estimates of unavailable data**
 - Most important data is balances by employee as of CYE and PYE (and more if you can)
 - Leave earned – make an estimate using your policies
 - Leave taken – can back into this if you have balances and amount earned
 - Pay rate – historical data not particularly useful
- **Can start by redoing last year’s calculation**