Payroll Accruals and the 27th Pay Period Conundrum

What is a payroll accrual?

Payroll accruals are a method for adjusting the personnel expenditures so they fall in the proper accounting period. This allows a fiscal entity to follow one of the basic accounting guidelines called the matching principle, which says that expenditures (or expenses) are recorded in the same accounting period as the related appropriations (or revenues).

Payroll accruals are required by both General Accepted Accounting Principles (GAAP) and the NYS Office of the Comptroller's Accounting & Reporting Manual (ARM). Historically the Town has not been recording these entries, but in an effort to become fulling GAAP compliant we should begin doing so.

Payroll accruals would happen only during the transition between fiscal years, when there is a pay period that spans the year end transition, with some days of the pay period being in the old year and some in the new with the actual pay date falling in the new year.

What happens when you do a payroll accrual?

An accrual is an accounting adjustment. One calculates what the cost is for the days related to the year that just ended and then makes accounting entries to remove that expenditure from the new fiscal year and "move" it back to the corresponding fiscal year. The cash position does not change; it is an entry in the accounting system only.

The transition between the 2018 and 2019 year offers a good opportunity to initiate these accruals for several reasons. Firstly, if we followed our regular schedule, the pay period that runs from 12/16/2018 – 12/29/2018 would be paid in 2019. The normal pay date would be Tuesday 1/1/2019, however with the banks closed that day it would actually be paid on 1/2/2019. Because all the days being paid for are in December, that entire payroll would then need to be accrued into the 2018 fiscal year. Additionally, there are 2 days (12/30, 12/31) of the following pay period that would also need to be accrued.

Our proposal is to adjust the pay date schedule so that the 12/16/2018-12/29/2018 pay period has a pay date of 12/31/2018. Then the entire pay period would naturally fall into the correct fiscal year. Only the remaining 2 days of the next pay period would need to be accrued. This adjustment will help us smooth out the cycle going forward.

What about that pesky 27th pay period?

Unfortunately the need for a 27th pay period cannot be ignored, it will happen periodically and we just happen to be in that point of our cycle. A bi-weekly payroll schedule and 26 pay periods in a year actually only covers 364 days each year (14 days/pay period X 26 pay periods) not 365 days. That means that at least 1 day per year is missed. Adding onto that, are leap years which fall approximately every 4 years. These unaccounted for days add up to necessitate a 27th pay period approximately every 11 years. This need for a 27th pay period introduces a conundrum with not only morale and equity issues but the possibility of legal repercussions if one group of employees felt that they were unfairly being treated differently than another group.

Further complicating the issue for the Town is the added restrictions related to pay for Elected Officials. At the Town, there are essentially 4 different types of staff with regard to how they are paid:

Pay Type	Pay Frequency	# of People	Initials
Hourly	Bi-Weekly	10 + seasonal	SK, MM, LA, RB, BC, SM, CS, SS, MB, LD
Salary (Non-Elected)	Bi-Weekly	4	AC, NT, TM, JZ
Elected Official	Bi-Weekly	5	MD, TS, ET, CP, DR
Elected Official	Monthly	4	MB, RG, JH, NZ

According to Town Law, the amount paid to Elected Officials cannot be more or less than what was published in the notice of hearing on the preliminary budget without passing a local law subject to permissive or mandatory referendum. In other words, Elected Official's pay is tied to the amount in the notice of public hearing not the budget line items.

That leads us to the question of non-elected salaried staff vs hourly staff. During a 27th pay period, hourly staff will need to be paid however many hours they have worked during that time. Where the situation becomes murky is how to treat the staff that are paid on a salaried basis. If the salaried staff are not also paid their normal salary for that pay period then a full time **hourly** staff would get 80 hours, or 1 full pay period, of pay more than a **salaried** staff person

The 27th pay period serves to essential make up for all those "unaccounted for" days as described above. To outline the concern over fairness, let's take the example of an hourly and a salaried staff person that start out at the same pay rate:

Year 1 Pay – 26 pay periods

Year 1			
	Annual	Pay Period	Hourly
Salary	$ 50,000.00	$ 1,923.08	$ 24.04
Hourly	$ 50,000.00	$ 1,923.08	$ 24.04
Difference	$ -	$ -	$ -

Year 2 Pay with 3% Increase – 27 pay periods

Year 2			
	Annual	Pay Period	Hourly
Salary	$ 51,500.00	$ 1,907.41	$ 23.84
Hourly	$ 53,480.77	$ 1,980.77	$ 24.76
Difference	$ 1,980.77	$ 73.36	$ 0.92

Year 3 Pay with 3% Increase - 26 pay periods

Year 3			
	Annual	Pay Period	Hourly
Salary	$ 53,045.00	$ 2,040.19	$ 25.50
Hourly	$ 53,045.00	$ 2,040.19	$ 25.50
Difference	$ -	$ -	$ -

As these tables illustrate, two employees who start out in the same place can end up being treated differently when it comes to a 27th pay period and one of those people could end up being paid significantly less.

Many different solutions were considered and analyzed in order to come to what we believe is the best solution. In detail, the solution would be as follows:

-The pay period that runs from 12/16/2018-12/29/2018 would be processed on 12/27 or 12/28 and would have a pay date of 12/31/2018
-The hourly staff would be paid at their 2018 hourly pay rate for any hours recorded on their time sheet for that pay period.
- The non-elected official staff that are paid on a salaried basis would be paid their regular 2018 per pay period rate.
- The elected officials that are normally on a bi-weekly pay schedule will not be paid during that pay period as they will already have reached the pay amounts listed on the notice of public hearing.
- The pay period that runs from 12/30/2018-01/12/2019 would be paid on 1/15/2019 at 2019 pay rates.
- At fiscal year end the 2 days of the 1/15/2019 payroll that fell in 2018 (12/30 & 12/31) would be accrued into 2018

The solution proposed above would be optimal for several reasons. Firstly, the Town would then be in compliance with the State Comptroller's Office and GAAP with regards to payroll accruals. Putting the 27th pay period in the 2018 fiscal year would mean that employee pay would be aligned to the dates being paid for, not the date paid. Making this adjustment in 2018 would be less expensive than waiting until 2019. This solution would not run afoul of laws regarding Elected Official pay but would allow for equity between employees in non-elected positions.

With regards to the financial end of the equation, both the cash and budget implications should be considered. With regards to cash, based on current estimates, we expect around $8,300 to be needed to pay hourly staff for the 12/16/2018-12/29/2018 pay period, although that number could change based on weather and other factors. There is no option not to pay the hourly staff for hours worked during this time. Correspondingly, for salaried staff the estimated cash needed for that pay period would be $6,800.

The proposed budget modifications would be needed for the accruals to happen regardless of any changes to the payroll schedule. The 2019 budget was built on this solution, both in the 2018 end of year estimates and the 2019 budgeted amounts. The good news is that based on current projections, there is enough in contingency to cover the A & B fund modifications. Additionally at this time, given all the uncertainly regarding highway payroll, I do not anticipate needing budget modifications for the Highway PS lines. This means that overall there would be no change to the total budget.

In summary, this would be the most equitable, cost effective way for the Town to smooth out these cycles and put us in a better position going forward by moving us into better compliance while not exceeding our total budget.