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TO: Local Government Finance Officials and Their Independent Auditors
FROM: Kendra Boyle, Director, Fiscal Management Section
SUBJECT: GASB Statement No. 101, *Compensated Absences*
DATE: May 2, 2025

In June 2022, the Governmental Accounting Standards Board (GASB) issued [Statement No. 101, *Compensated Absences*](#) (Statement 101). This Statement is effective for fiscal years beginning after December 15, 2023. For most local governments and public authorities in North Carolina, this Statement is now effective for the fiscal year beginning July 1, 2024. Statement 101 replaces GASB Statement No. 16, *Accounting for Compensated Absences* (Statement 16), which was issued in November 1992. Statement 101 aims to align recognition and measurement guidance under a unified model that considers forms of compensated absences that were not prevalent when Statement 16 was issued. Statement 101 does NOT have a budgetary or financial reporting impact on a local government's governmental funds. The entries required by the Statement are reported in the government-wide statements and in the proprietary and fiduciary fund statements (if applicable) as explained more fully below. The following guidance includes provisions reproduced directly from Statement 101.

This memorandum¹ is organized as follows:

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¹ This memorandum reflects the collaborative input of subject matter experts and technical advisors from the UNC School of Government and other organizations, whose contributions were integral to its preparation.

Scope and Exception

Scope

Statement 101 establishes standards of accounting and financial reporting for compensated absences and associated salary-related payments, including certain defined contribution pensions and defined contribution other postemployment benefits (OPEB).

Exception

The provisions of the Statement do not apply to benefits that are within the scope of GASB Statement No. 47, *Accounting for Termination Benefits*, as amended.

Definition and Additional Exceptions

Definition

Under the new guidance, a compensated absence is broadly defined as leave for which an employee may receive one or more:

- Cash payments when leave is used for time off.
- Other cash payments, such as a payment for unused leave upon termination of employment.
- Noncash settlements, such as a conversion to defined benefit postemployment benefits.

The GASB clarified in the Statement 101 basis for conclusions that the termination of employment refers to the end of an employee's active service for any reason.

The definition of compensated absences may include benefits, such as vacation pay, sick leave, paid time off (PTO), holidays, parental leave, bereavement leave, and certain types of sabbatical leave. However, as noted later in this memo, not all benefits that meet the definition of a compensated absence are reported as a compensated absence liability.

Compensated absences do not have a payment schedule and could occur during employment or upon termination of employment. As discussed later in this memo, the lack of a payment schedule and other factors adds to the complexity of the calculations associated with compensated absences liabilities, especially sick leave.

Additional Exceptions

While not excluded from the scope of Statement 101, the projected effects on an employer's defined benefit postemployment benefits liabilities resulting from a conversion of compensated absences should not be included in the calculation of the compensated absences liability. These liabilities currently are reported as part of the defined benefit pension and defined benefit OPEB liabilities.

While not specifically addressed in Statement 101, as discussed below, leave that is more likely than not² to be forfeited at termination from employment also is not included in the calculation of the compensated absences liability.

² As defined in the statement, "The term *more likely than not* means a likelihood of more than 50 percent."

Recognition, Cost/Benefit Exceptions, and Measurement

Economic Resources Measurement Focus Used in the Government-Wide Financial Statements and Proprietary and Fiduciary Fund Financial Statements

Liabilities for compensated absences are required to be recognized in financial statements prepared using the economic resources measurement focus for leave that has:

- Not been used.
- Been used, but not yet paid or settled.

Applicable salary-related payments that are directly and incrementally associated with the leave should be included in the measurement of compensated absences liabilities (see discussion below for exceptions). A payment is *directly associated* if the amount of the payment is a function of salary to be paid (that is, the amount of the payment depends on the amount of salary to be paid). A payment is *incrementally associated* if the unit of local government will make a payment in addition to the payment for the salary. Payments that are directly and incrementally associated with leave include the employer's portion of Social Security taxes, Medicare taxes, and defined contribution pension plan contributions (see specific recognition and measurement guidance below).

Unused and used compensated absences liabilities are not required to be aggregated for display in the financial statements (for example, liabilities associated with leave that has been used can be reported with wages/salaries payable).

Leave That Has Not Been Used

Recognition

A liability is required to be recognized for leave that has not been used if all the following are true:

- The leave is attributable to services already rendered (that is, services that are required to earn the leave have been performed).
- The leave accumulates (that is, the leave can be carried forward to future reporting periods which may be in the same calendar year).
- The leave is more likely than not to be used for time off or otherwise paid in cash or settled through noncash means.

A unit of local government is required to evaluate whether leave is more likely than not to be used for time off or otherwise paid in cash or settled through noncash means by assessing relevant factors, including the following:

- The government's employment policies related to compensated absences
- Whether leave that has been earned is, or will become, eligible for use or payment in the future
- Historical information about the use, payment, or forfeiture of compensated absences
- Information known to the unit of local government that would indicate that historical information may not be representative of future trends or patterns.

Again, leave that is more likely than not to be settled through conversion to defined benefit postemployment benefits or forfeited should not be recognized as a liability for compensated absences.

Cost/Benefit Exceptions

For compensated absences triggered by sporadic events affecting a relatively small proportion of employees in any reporting period, a unit of local government is required **not** to recognize a liability until the leave commences. This type of compensated absence includes parental leave, military leave, and jury duty leave. This exception does not apply to sick leave and unrestricted sabbatical leave.

In addition, for the following categories of compensated absences, a government should not recognize a liability until the leave is used:

- Leave that employees can take as needed without specific limits (sometimes referred to as *unlimited leave*)
- Holiday leave that is taken on a specific date not at the discretion of employees

Measurement

A liability for leave that has not been used is required to be measured using an employee's pay rate as of the date of the financial statements. Even if a salary increase related to the next fiscal year has been adopted, the pay rate as of the end of the current reporting period should be used.

Changes to the measurement of the liability in future periods due to a change in pay rate are required to be recognized as a change in estimate in the period of the change.

As noted in the basis for conclusions, the GASB decided not to provide guidance on the flow assumption in Statement 101. However, some context is needed in applying the flow assumption, and, based on the approaches illustrated in this memo, a flow assumption is not needed (see discussion of flow assumptions below).

Leave That Has Been Used

Recognition

A liability for leave that has been used is required to be reported when leave is used for time off but has not yet been paid in cash or settled through noncash means. As previously noted, this liability includes parental leave, military leave, jury-duty leave, unlimited leave, and holiday leave.

Measurement

A liability for leave that has been used, including any applicable salary-related payments (see specific guidance below), should be measured at the amount of the cash payment or noncash settlement to be made for the use of the leave.

Salary-Related Payments

Recognition

Salary-related payments are obligations that a unit of local government incurs related to providing leave in exchange for services rendered. (Note: The term *salary* in *salary-related payments* represents any pay provided to the employee, whether it is a fixed amount or an hourly wage.) Again, examples of salary-related payments

include the employer share of Social Security taxes, Medicare taxes, and defined contribution pension and defined contribution OPEB contributions.

Defined contribution plans are different from the Local Governmental Employees' Retirement System (LGERS), which is a defined benefit (DB) plan. Defined contribution plans depend on employee/employer contributions and investment performance, unlike defined benefit plans which promise a fixed payout. Examples of defined contribution plans are a 401(k) plan or a 457 plan.

For leave that has not been used, expense for salary-related payments related to defined contribution pensions or defined contribution OPEB is required to be recognized at the same time as the liability for that leave is recognized and is further required to be reported as pension expense or OPEB expense, as applicable. Those amounts are required to be reported as a compensated absences liability and not as a pension liability or an OPEB liability.

For leave that has been used, salary-related payments related to defined contribution pensions or defined contribution OPEB are required to be reported as a pension liability or an OPEB liability.

Exceptions to Recognition

As previously noted, salary-related payments associated with defined benefit pensions or defined benefit OPEB should not be included in the measurement of liabilities for compensated absences.

Measurement

A unit of local government is required to include in the measurement of its liabilities for compensated absences (for both leave that has been used and leave that has not been used) salary-related payments that are directly and incrementally associated with the leave, except as noted below. As previously noted, even if an increase in a salary-related rate for the next fiscal year has been adopted, the rate as of the end of the current reporting period should be used. Changes to the measurement of the portion of the liability that is for salary-related payments in future periods due to a change in rate are classified as a change in estimate and should be recognized in the period of the change.

Current Financial Resources Measurement Focus Used in the Governmental Fund Financial Statements

Recognition

A liability for compensated absences is required to be recognized on a basis consistent with governmental fund accounting principles. The amount of compensated absences recognized as expenditures in financial statements prepared using the current financial resources measurement focus is required to be the amount that normally would be liquidated with expendable available financial resources based on the guidance provided in GASB Interpretation 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*. This guidance does not represent a change from current practice.

Display

Compensated absences are not required to be separately displayed in the financial statements; however, depending on the magnitude of the liability, separate display may be warranted. The GASB clarified in the basis for conclusions that the liability for leave that has been used, but has not yet been paid or settled, can be reported as another liability (for example, salaries payable).

Disclosures

For the purpose of the long-term liabilities disclosure, a unit of local government is required to present either (a) the separate increases and decreases or (b) a net increase or a net decrease in its liability for compensated absences included in that disclosure. A unit that presents a net increase or a net decrease should indicate that it is a net amount (for example, in a footnote to the changes in long-term liabilities disclosure).

The disclosure requirement in GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, paragraph 119, related to which fund or funds typically have been used to liquidate the long-term liabilities in prior years is now not required to be applied to liabilities for compensated absences.

Certain Considerations and Determinations

Preparing for the implementation of Statement 101 on compensated absences requires many different issues to be considered and decisions to be made. First, it is crucial to understand the new unified model for recognizing and measuring liabilities for compensated absences as presented above (primarily based on a verbatim presentation of the Statement 101 provisions). Units of local government should also ensure that staff completely understand their compensated absences policies and gain an understanding of what data is to be documented and by whom.

Next steps - The following list covers a few items to consider or decide on when implementing Statement 101 (this list is not all-inclusive):

Review and Evaluate Leave Policies

Government officials should review their leave policies to identify which benefits meet the definition of a compensated absence and to ensure that the policies are current, correct, and documented. If the unit has documented policies, ensure they match what the unit is awarding in practice. If policy changes are needed, they must be adopted and documented before fiscal year end 2025.

Ensure That Leave Records Are Accurate

A unit of local government needs to maintain accurate records of obligations for vacation leave, sick leave, and any other compensated absence benefits, as defined by the GASB, that a unit provides to its employees. The balances in a unit's recordkeeping system should be regularly reconciled to ensure that those balances are accurate. This is especially important for the balances at the end of each fiscal year, including at the beginning of the implementation of Statement 101 (July 1, 2024, for most units in North Carolina). The actual hours of the various types of compensated absence leave — including subcategories of sick leave, which will depend on the measurement approach selected, as noted below — and the pay rates in effect at the end of the fiscal year before implementation need to be identified. It is these amounts that will be used to calculate ending net position, the change in accounting principle from the implementation of Statement 101, and net position and fund net position, as restated, for the implementation of Statement 101.

Sick Leave

For most units of local government, the most significant change as a result of the implementation of Statement 101 will come from the change in the accounting for sick leave. The impact for almost every unit will occur in financial statements where the economic resources measurement focus is applied (government-wide statements, proprietary fund statements, and fiduciary fund statements). Not all sick leave will become a

compensated absences liability even in these financial statements. Determining the sick leave liability generally will be a more complex calculation than the calculation of the vacation leave liability and likely will be affected by each unit's past experience. However, officials need to be sure to include all types of leave to which this standard applies in their calculations.

Salary-Related Payments

As previously noted, the term *salary-related payments* refers to payments that are directly and incrementally related to compensated absences liabilities. Again, properly identifying the related payments at the end of the reporting period is necessary to fairly present the compensated absences liability.

Materiality

The concept of materiality underlies all GASB standards. The assessment of whether compensated absences is material or whether a specific compensated absence will have a material effect on the liability as a whole should be based on the specific facts and circumstances of each unit of local government. In addition to quantitative assessments, qualitative factors (those that may influence a decision-maker's assessment) need to be considered.

Actuaries

Statement 101 does not require that an actuary be used in the analysis of a unit of local government's historical experience and the calculation of the compensated absences liability. If an actuary is used, the actuary needs to be cognizant of the "more likely than not" approach used in determining the compensated absences liability, which may not be consistent (within acceptable parameters) with how most actuarially determined liabilities are calculated.

Independent Auditor

If possible, it is important for government officials to discuss the implementation of Statement 101 with their external auditor as the unit of local government moves through the implementation process. A decision needs to be made regarding the extent to which the unit's staff can discuss with the auditor the best approach to proposed policies and procedures while still preserving the independence of the auditor.

Gathering Data

The data that is gathered will depend on the specific compensated absences benefits that a unit of local government offers and the measurement approach employed by the unit. The GASB did not establish a required measurement approach and the LGC does not endorse a specific measurement approach; therefore, the following approaches presented (comprehensive and **practical expedient**³) for data gathering are for illustrative purposes only. Of these two approaches illustrated, LGC staff believe that most units in North Carolina will find the **practical expedient** approach the best fit. Please note that the unit should select an approach based on its own facts and circumstances, applying professional judgment. Selecting an approach will require extensive discussions between the unit and its auditor to ensure they are in agreement. The comprehensive and **practical expedient** approaches are just two of many approaches that may be considered and agreed upon between units and their auditors.

³ All references to practical expedients are **bolded** to assist the reader.

Data Needed for the Comprehensive Approach

The comprehensive approach is focused on calculating the sick leave liability. The data needed to apply this approach begins with sick leave hours that are classified into one of three categories: ⁴

- More likely than not to be forfeited when an employee departs service
- More likely than not to be converted to service credit for the determination of defined benefit pensions or OPEB benefits
- More likely than not to be used during employment or paid upon termination (hereinafter, referred to as “used” in this section)

The key to the execution of the comprehensive approach is having accurate balances of the number of hours of total sick leave outstanding at the end of each reporting period, the number of hours of sick leave “earned” during the reporting period, and the number of hours of sick leave deducted during the period. Without accurate records of actual forfeited leave, the actual leave that was converted to service credit during the reporting period, and the actual hours of sick leave used during the reporting period, the application of this approach may result in a compensated absences liability that is not fairly stated. In addition, at a minimum, information regarding the associated expense function needs to be captured so that the expense associated with sick leave can be properly reflected in the appropriate change statements (for example, the Statement of Activities), as is currently reported for vacation leave.

Historical information from personnel records about the forfeiture, conversion (service credit), or use (leave taken) of sick leave normally should be evaluated in the assessment of the compensated absences liability when this approach is employed. It should be noted that Statement 101 did not specify a particular number of years to use in evaluating historical information. Under this approach, the number of past years to review is a matter of professional judgement. Units of local government that have begun the implementation process are commonly analyzing four to five years of experience; however, the number of years used should be determined by local officials based on the specific facts and circumstances of that unit.

These percentages based on historical data for the three categories will be used as a surrogate for the actual use of sick leave over an employee’s service period.

Forfeitures

Based on the analysis of prior periods, a percentage of sick leave balances associated with forfeitures can be determined (average of all the periods analyzed). However, government officials also should be aware that patterns and trends may change based on changes in laws and policies or a change in the working environment. In those cases, historical information may no longer be representative of a unit of local government’s experience as it relates to current balances.

Conversion to Service Credits

In determining estimated service credits, units of local government have at least two alternatives to consider. The first employs the same percentage that the pension or OPEB plans actuary uses to determine how much of outstanding leave should be incorporated into the pension or OPEB liability. While the actuary uses a probability-weighted approach versus a more likely than not approach and the percentage is based on all participating entities in the plan, there may be circumstances from a materiality standpoint where this **practical expedient**

⁴ Amounts transferred in from and out to other government units should be allocated into or removed from one or more of these three categories.

can be employed for the service credit portion of the calculation. The advantage of this approach is that it can be easily determined. The disadvantage is that the actuarial percentage is based on all participants in the plan and may not accurately reflect the result of the specific unit. The sum of the three categories should equal 100 percent; therefore, if the percentage is not government specific, adjustments may need to be made.

The second alternative is based on the unit of local government's own experience using actual service credits earned and applied upon termination. Again, in this alternative, the number of past years to review is a matter of professional judgement. Those considerations include individual cases that could result in misleading data that need to be addressed.

Based on the analysis of prior periods, a percentage of compensated balances associated with service credits can be determined (average of all the periods analyzed). However, as with forfeitures, government officials also should be aware that patterns and trends may change based on changes in laws and policies. Again, in those cases, historical information may no longer be representative of a unit of local government's experience as it relates to current balances.

Used During Employment

Once the averages have been determined for forfeitures and conversion to service credits, theoretically, the remaining deductions during the reporting period (see discussion of transfers below) are used for sick leave. However, because of the need to collect information at a more detailed level for other purposes (for example, the allocation of the sick leave liability to an activity or fund, the determination of sick leave expense by function, or the use of dollar-value LIFO), the analytical approach used to determine forfeitures and service credits should be employed.

If detailed information by employee related to forfeitures or service credit conversions does not exist, is not considered reliable, or time is not available to conduct the analysis of these categories, the **practical expedient** approach (as presented below) can be employed. The unit of local government will not have the additional assurance that all data has been captured and classified into the proper category; however, there may be cases where this is the only practical path to the implementation of Statement 101.

Transfers and Other Additions

When an employee moves from one North Carolina unit of local government, their sick leave balances may transfer with them. In addition, if an employee returns to service within a two-year period, some units reinstate leave balances. As previously noted in footnote 4, transfers in and out or other additions should be allocated to or deducted from the appropriate categories. In the case of a transfer out, amounts are deducted from the categories which the sick leave has been allocated to; whereas, in the case of transfers in or other additions, the employee data is analyzed and allocated to the appropriate category. As a **practical expedient**, unless the amounts are significant and there is evidence to the contrary, the same percentages calculated for the three categories can be applied to transfers and other additions.

Salary-Related Payments

For salary-related payments, the data gathering should be focused on the rates that are in effect at the end of the reporting period.

Leave Earned

Capturing the amount of sick leave added to each employee's benefit balance during the period is critical in determining the overall amount of sick leave hours outstanding as of the end of the reporting period. However,

it is important to note that, unlike vacation benefits, the amount of sick leave added to each balance does not translate to earnings because not all additions will be used. This distinction is critical in applying the flow assumption, if applicable, as noted below.

Flow Assumption

The use of a flow assumption under the comprehensive approach is not needed to calculate the sick leave liability; the current liability, if a classified statement of net position is presented; or the amount due within one year for disclosure purposes.

Practical Expedient Approach

Because the goal of gathering data is to determine the percentage of the total sick leave outstanding, as previously noted, the unit of local government could limit its analysis to only this category. The benefit of this method could substantially reduce the amount of time needed for the analysis because the effort is focused on one category. The downside is that there would be one less control available to assess whether the result is reasonable. Remember that even when using a **practical expedient**, compensated absence expenses will need to be reported by function in the government-wide statements and also within the fund financial statements using the economic resources measurement focus and the accrual basis of accounting. The calculation of the total compensated absence liability at year end is only part of the process.

This approach eliminates the need to analyze data related to forfeitures and service credit conversion; however, the remaining data needs to be collected.

Calculating the Compensated Absences Liability — Focusing on Sick Leave

The following provides an overview of calculations associated with the compensated absences requirements and related disclosures in a unit of local government's financial statements resulting from the implementation of Statement 101. Keep in mind that the numbers and hours in the following example in this memo do not come from an actual unit of government and are not intended to represent actual amounts that a unit will experience. They are intended to show relationships and how amounts flow into the financial statements. This overview will be reflected in the Illustrative Financial Statements for Carolina County for the fiscal year ending June 30, 2025. The illustrative financial statements assume that all Statement 101 compensated absences calculations have been completed and that the resulting journal entries were recorded in the county's general ledger.

Theoretically, compensated absences liabilities recognized in the financial statements are calculated using accumulated leave that is more likely than not to be used or paid upon termination (normally based on number of hours) multiplied by the employee's pay rate and the salary-related payments rate at the date of the financial statements. As noted in the previous section, this calculation is more complex than this straight-forward formula.

Step 1 — Determine a level on which to base the calculation

Any compensated absences calculation should begin with determining the base level on which the applicable steps are applied. In other words, at what base level should the liability and related expense be calculated. There are several potential base levels, including by:

- Employee
- Employees with similar job functions
- Employees in the same program

- Employees in the same functional category
- Employees by activity (governmental and business-type)
- All employees

The level selected will be influenced by a number of factors, including sophistication and accuracy of human resource records. However, the use of one of the more detailed levels (for example, by employee) will likely reduce the possibility of over or understatement of the compensated absences liability, especially in the case of sick leave. While consistency is an important qualitative characteristic of financial reporting, as a **practical expedient**, a unit of local government could use one level for vacation pay where all benefits are used or paid upon termination (for example, all employees) and another for sick leave where only a portion of the total sick leave is used (for example, by employee or employees with similar job functions). To potentially reduce the cost of implementation, additional **practical expedient** considerations will be introduced in the remaining steps.

Step 2 — Establish a look-back period⁵

The calculation of the sick leave portion of total compensated absence liability will be the focus of Steps 2-6.

When a portion of sick leave at the end of the reporting period does not meet the definition of “more likely than not” to be used or paid upon termination (“used”), the portion of sick leave which **is** more likely than not to be used needs to be determined. For example, some hours may be more likely to be forfeited or converted to service credits for pensions or OPEB.

As discussed in the Gathering Data section, a **practical expedient** to estimating the number of hours in this category can be based, in many cases, on a historical look-back period. As previously noted, many units of local government use a four-to-five-year look-back period to determine this amount (normally based on a percentage). In this illustration, a five-year look-back period is used.

Step 3 — Determine the percentage associated with the sick leave expected to be used category

There are two methods that can be used to determine the percentage associated with the sick leave expected to be used category. The first method provides a comprehensive means to make this determination. The second method is a **practical expedient** intended to reduce the burden associated with this determination.

Comprehensive Method

Using the method outlined in the Gathering Data section, for each year of the look-back period, the number of hours deducted related to sick leave during the reporting period for each of the applicable categories⁶ should be identified:

- Forfeited when an employee departs service
- Converted to service credit for the determination of defined benefit pensions or OPEB benefits
- Used during employment

⁵ For compensated absences that vest (for example, vacation pay), this step normally is not necessary. All leave balances of this type are expected to be used, unless transfers out (for example, from vacation leave to sick leave) are determined to be significant. If such a transfer is made, then the unit needs to determine if that transfer will be used as sick leave.

⁶ Including a portion of transfers to or from other units of government and reinstatements that result from a rehire.

If detailed records are available, individual employee amounts can be used to determine these amounts. As a **practical expedient**, the base level used to determine these amounts can be different than the base level used to make the overall calculation. For example, the employee population for each year could be used even when the base level on which the calculation is made is by individual employee. Even in this case, if a group of employees or even individual employees in a smaller government unit with different pay rates use their sick leave in a manner that is not consistent with the percentages determined using a **practical expedient**, the results may be misleading.

To illustrate this step, using the comprehensive method with a **practical expedient**, the following is a table of deductions over a five-year period:

	Year 1		Year 2		Year 3		Year 4		Year 5		Total	
	Hours Deducted	%										
Forfeited	13,580	14.29%	15,460	17.10%	15,380	16.04%	12,780	12.84%	13,340	14.04%	70,540	14.82%
Converted	63,380	66.67%	57,970	64.10%	61,530	64.15%	65,750	66.06%	61,670	64.91%	310,300	65.20%
Used	18,100	19.04%	17,000	18.80%	19,000	19.81%	21,000	21.10%	20,000	21.05%	95,100	19.98%
Total	95,060	100.00%	90,430	100.00%	95,910	100.00%	99,530	100.00%	95,010	100.00%	475,940	100.00%

Practical Expedient Method

Because the goal of this step is to determine the percentage of the total leave outstanding that is expected to be used, as a **practical expedient**, the unit of local government could limit its analysis to only this category. As previously noted, the benefit of this method could substantially reduce the amount of time needed for the analysis because the effort is focused on one category. The downside is that there would be one less control available to assess whether the result is reasonable.

Under this method, the additional **practical expedients** introduced in the comprehensive method also could be employed.

To illustrate this step, using the **practical expedient** method, the following is a table of deductions over a five-year period:

	Year 1		Year 2		Year 3		Year 4		Year 5		Total	
	Hours Deducted	%										
Used	18,100	19.04%	17,000	18.80%	19,000	19.81%	21,000	21.10%	20,000	21.05%	95,100	19.98%

Step 4 — Determine the number of hours of sick leave outstanding associated with sick leave expected to be used

Based on the **practical expedient** method illustration, the next step in the calculation of the sick leave liability is to determine the total number of hours associated with the sick leave used. Again, if detailed records are available, individual employee records can be used to determine this number.

As a **practical expedient**, the total number of hours can be determined by multiplying the percentage of hours used for sick leave by the total number of sick leave hours outstanding. In this case, if the HR system reports 150,000 hours of sick leave benefits are outstanding at the end of the reporting period, the number of hours allocated to sick leave expected to be used is 29,970 hours (19.98% associated with the sick leave expected to be used).

If each of the unit of local government's 1,000 employees receive 12 days (96 hours per employee) of sick leave benefit days a year, it is estimated that 19 hours per employee of sick leave is "earned" per year (again, 19.98% estimated to be used of the 96 hours received). That is, 19,181 hours for the entire employee population are earned per reporting period.

Step 5 — Apply salary and salary-related rates to the number of hours of sick leave outstanding associated with the sick leave expected to be used to determine the sick leave liability

Once the estimated number of hours associated with sick leave that is more likely than not to be used has been determined, a salary rate and a salary-related rate should be applied to those hours. Again, the following results are for illustrative purposes only and do not take materiality into consideration.

If the calculation of the number of hours has been based on an individual employee level, then the individual employee's salary rate should be applied to the hours related to each employee using a spreadsheet or, in some cases, the human resource system. For example, if an employee is expected to have "earned" 250 hours based on their service to date, those hours are multiplied by the employee's salary rate of \$52 per hour. The result (\$13,000) would then be multiplied by any salary-related payment (in this case, the employer's portion of Social Security taxes (6.2%), Medicare taxes (1.45%), and a defined contribution pension plan contribution (5%)). The result is a \$14,645 sick leave liability for that employee.

As a **practical expedient**, the unit of local government could use the total hours outstanding per Step 4 (29,970 hours) multiplied by the average salary for all employees (for example, \$35 per hour). The result (\$1,048,950) would then be multiplied by any salary-related payment (in this case, the employer's portion of Social Security taxes (6.2%), Medicare taxes (1.45%), and a defined contribution pension plan contribution (5%)). The result is a \$1,181,642 sick leave liability.

Step 6 — Consider whether to apply flow assumption to the number of hours of sick leave outstanding associated with the sick leave expected to be used to determine the current portion of the liability and the amount due within one year disclosure

No Flow Assumption

As a **practical expedient**, the current portion of the sick leave liability and the amount of sick leave due in one year disclosure can be determined without the use of a flow assumption. The amounts for the display and disclosure (which should be equal in total) could be determined by using the average number of sick leave hours used per reporting period over the look-back period multiplied by the average pay rate/hour and the salary-related payments. Because the current liability and amount due in one year are intended to be based on the liability reported at the end of the reporting period, adjustments (for example, approved salary increases for the next year) would not be necessary.

If a Flow Assumption Is Used

In situations where the entire amount of a compensated absence balance will be used (for example, vacation leave), establishing a policy regarding the application of a flow assumption can be used to calculate the absences due within one year in the changes in long-term liabilities disclosure and the current portion of compensated absences balance. Ever since paragraph 119 of Statement 34 was implemented, there has been a need to consider employing a flow assumption in this situation. Also, as previously noted, if another approach is used to calculate the sick leave liability, there may be a need for the use of a flow assumption.

If the use of a flow assumption is employed, LGC staff recommend the same flow assumption be applied from reporting period to reporting period.

FIFO (First In First Out)

The use of FIFO is normally less complex than Last In First Out (LIFO). This is primarily because it does not require the assessment of use to determine if a layer of hours earned in a prior period has been consumed. When applying the FIFO flow assumption, the hours earned in prior periods are always consumed first until that balance is zero.

Base level used in applying the flow assumption

Applying the FIFO flow assumption at an employee level normally will provide the most representationally faithful result. However, employees can be grouped.

Applying the effect of the flow assumption

If the percentage of sick leave used is based on historical data, the application of a flow assumption likely will differ from that historical assumption. In applying the FIFO flow assumption to individual employees, some will use:

- None, a portion, or all the beginning sick leave hours “earned” balance (as noted several times, these hours will be a percentage of the total number of hours in the employee’s account).
- All the beginning sick leave hours “earned” balance and some or all of the hours “earned” during the current year.

For those employees with no beginning sick leave “earned” balance, all of the sick leave used will be associated with the hours “earned” during the current period.

LIFO⁷

Base level used in applying the flow assumption

Applying the LIFO flow assumption at an employee level will provide the most representationally faithful result. Caution should be exercised in any aggregation used when applying the LIFO flow assumption.

Applying the effect of the flow assumption

Once more, if the percentage of sick leave used is based on historical data, the application of a flow assumption likely will differ from that assumption. In applying the LIFO flow assumption to individual employees, some will use:

- None, a portion, or all the hours “earned” during the current year (again, the hours “earned” will be a percentage of the total number of hours credited to the employee’s account during the current reporting period). Therefore, the beginning LIFO layer will not be used.
- All the hours “earned” during the current year and a portion of the beginning sick leave hours “earned” balance.

⁷ If dollar-value LIFO is used as the flow assumption, aggregation beyond this level could result in a misstatement of the sick leave liability.

- All the hours “earned” during the current year and all of the beginning sick leave hours “earned” balance.

The disclosure of flow assumption is addressed in Step 7.

Step 7 — Develop note disclosures

Summary of significant accounting policies disclosure — Identify policies

Disclosure of the following policies is not required in GASB 101; however, consideration should be given to presenting these policies (including context) in the summary of significant accounting policies:

- Compensated absences benefits offered, including vesting rights, conversion provisions, and forfeiture provisions
- Methodology used to determine the compensated absences liability, including the flow assumption (if applicable)

Changes in long-term liabilities disclosure

Opening balance

The opening balance is the amount of compensated absences liability balance at the beginning of the reporting period based on the methodology used to develop this estimate.

Changes in long-term liabilities

These include the changes in salary rates and salary-related payment rates. As previously noted, this amount can be presented gross with additions and deductions or net (the net amount presented as an addition or deduction). The sick leave gross additions are \$756,259 (19,181 hours earned X \$35/hour + .1265 in salary related benefits), and the gross deductions are \$788,550 (20,000 hours used X \$35/hour + .1265 in salary related benefits). The net deduction is \$32,291.

Again, as previously noted, if the netting approach is used, the fact that the amount is netted needs to be disclosed.

Ending balance

The ending balance is the amount of compensated absences liability balance at the end of the reporting period based on the methodology used to develop this estimate. While this amount is independently calculated, based on the amounts presented in this schedule, the beginning balance plus or minus the changes should equal the ending balance. The balance for the illustrative disclosure is \$1,181,642 (based on the calculations in Step 5).

Determine the amount of sick leave liability expected to be due in one year

As previously noted, there is no payment schedule for compensated absences, so the amount expected to be paid in one year needs to be estimated. Approaches that can be used to estimate this amount are discussed in Step 6. The estimate based on the **practical expedient** method is \$749,911. (Note: The amount is calculated as 19,020 hours X \$35/hour + .1265 salary-related payments).

Amounts in the disclosure can be rounded to communicate that these are estimates and not based on payment schedules.

Disclosures

Summary of Significant Accounting Policies

The sick leave policies of Carolina County, as well as its hospital and Tourism Development Authority (TDA), provide for the unlimited accumulation of sick leave. Any unused sick leave accumulated at the time of retirement may be used in the determination of the length of service for retirement benefit purposes. Any unused sick leave accumulated for employees that leave the county before retirement is forfeited.

The county, the hospital, and the TDA use a five-year look-back period to estimate the amount of sick leave that has been earned and will be used as sick leave over the employee's service period. The liability for sick leave is based on this estimate.

Changes in Long-term Liabilities

Gross Amounts

Example Note Disclosure - Changes in Long-Term Liabilities - Gross Amounts						
	Beginning Balances	Additions	Deductions	Ending Balances	Amounts Due Within One Year	
Other liabilities:						
Compensated Absences:						
Vacation leave	\$ 5,445,017	\$ 3,360,012	\$ 2,280,013	\$ 6,525,015	\$ 2,920,000	
Sick leave	1,213,933	756,259	788,550	\$ 1,181,642	749,911	
Total compensated absences	\$ 6,658,950	\$ 4,116,270	\$ 3,068,563	\$ 7,706,657	\$ 3,669,911	

Note: The example is for illustrative purposes only. In the financial report disclosure only the total for the compensated absences needs to be presented

Net Amounts

Example Note Disclosure - Changes in Long-Term Liabilities - Net Amounts					
		Beginning Balances	Net Additions/Deduction	Ending Balances	Amounts Due Within One Year
Other liabilities:					
Compensated Absences:					
	Vacation leave	\$5,445,017	\$ 1,079,998	\$6,525,015	\$ 2,920,000
	Sick leave	1,213,933	(32,291)	1,181,642	749,911
	Total compensated absences	\$6,658,950	\$ 1,047,707	\$7,706,657	\$ 3,669,911

Note: The example is for illustrative purposes only. In the financial report disclosure only the total for the compensated absences needs to be presented

Conclusion

In conclusion, units of local government will need to review and consider the effect of leave policies; analyze leave balances; and use professional judgement, including relevant literature which may include information outside traditional accounting literature, in selecting the methodology to employ in determining the compensated absences liability. If implementation efforts have not started, the LGC staff urges units of local government to immediately begin evaluating the information associated with compensated absence leave that is currently available. If implementation has started, the suggestions and **practical expedients** outlined in this memo can assist units of local government in achieving a successful implementation.

If you have further questions on this memorandum, please contact:

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