

OHIO AUDITOR OF STATE

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TO: All Public Offices
Independent Public Accountants

FROM: Keith Faber
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SUBJECT: Governmental Accounting Standards Board Statement No. 101 –
Compensated Absences

Background Information

The Governmental Accounting Standards Board (GASB) Statement No. 101, *Compensated Absences*, is focused on more effectively meeting the informational needs of financial statement users through updating the recognition and measurement guidance for compensated absences under a unified model and by amending certain previously required disclosures.

The requirements of this Statement apply to all Ohio state and local governments that prepare GAAP (Generally Accepted Accounting Principles) Statements, including those with a GAAP reporting requirement per Ohio Admin. Code (OAC) §117-2-03(B). Some other governments may be subject to GAAP reporting requirements, such as through a debt covenant. GASB 101 is effective for financial statements for periods beginning after December 15, 2023. This means governments with a December 31 fiscal year end must apply the provisions to their December 31, 2024, GAAP financial statements; schools and other governments with a June 30 fiscal year end must apply GASB 101 to their June 30, 2025, GAAP financial statements.

Applicability to Non-GAAP entities is addressed later in this bulletin.

Classification – Standards of Governmental Accounting and Financial Reporting Changes

GASB 101 establishes classification criteria in paragraphs 2 through 7 for standards of governmental accounting and financial reporting for compensated absences along with the

associated salary-related payments that include certain defined contribution pensions and defined contribution other postemployment benefits.

Compensated absences are defined as leave for which employees may receive one or more of the following:

- a) Cash payments when taking leave for time off;
- b) Cash payments for unused leave upon termination of employment; or
- c) Any noncash settlements, including conversion to defined benefit postemployment benefits.

Payment or settlement of compensated absences may occur during or after termination of employment and generally do not have a set payment schedule. Examples of qualifying leave includes vacation, sick, parental, bereavement and sabbatical leave as well as paid time off and holidays. (GASB 101 ¶ 3) See GASB 101 paragraph 4 for additional discussion of sabbatical leave.

Termination of employment, in this context, is specific to the conclusion of active service employment whether through voluntary resignation/retirement, termination or any other reason. (GASB 101 ¶ 5)

Recognition and Measurement

The economic resources measurement focus recognizes liabilities for compensated absences for leave that either has not been used or leave that has been used but not yet paid or settled. There is no requirement to aggregate these leave types for financial statement display. (GASB 101 ¶ 8)

Leave That Has Not Been Used

Except as discussed on the next page, report a liability for leave that has not been used if all the following are true (GASB 101 ¶¶9-12):

- a) Leave is attributable to employee services rendered, meaning the employee has performed the services required to earn the leave.
- b) Leave accumulates, meaning it was earned in one reporting period and carried forward to the next reporting period to be used for time off, paid in cash or settled in a future period.
- c) Leave is *more likely than not*¹ to be used for time off or otherwise paid in cash or settled in a noncash means by assessing relevant factors such as:
 - a. Employment policies
 - b. Eligibility for use or future payment
 - c. Entity's history of use, payment or potential forfeiture
 - d. Taking into account any information that may not represent future trends or patterns.

¹ Any likelihood greater than 50 percent is considered *more likely than not*.

Any leave that is more likely than not to be settled through conversion to defined benefit postemployment benefits should not be recognized as a liability for compensated absences. (GASB 101 ¶13)

Consider any leave types that are dependent upon a sporadic event affecting a small proportion of employees in a reporting period, refraining from recognizing a liability for these instances until the leave commences (examples include: parental and military leaves along with jury duty). Additional leave types that should not be recognized as a liability until used include any leave that may be taken without specific limits and holiday leave taken on a specific date (excluding floating holidays that employees use at their discretion). (GASB 101 ¶¶14 and 15 and GASB 101 ¶B29)

An employee's pay rate at the date of the financial statements should be utilized as the measuring factor for the leave liability unless one of the following criteria are met:

- 1) Proportionately allocate an employee's adjusted pay rate from the rate in place at the financial statement date if some or all the leave is likely to be paid at the adjusted rate. This includes instances where rates are adjusted by policy (at termination, for example) but does not include anticipated rate increases for cost of living, negotiated agreement changes, or merit raises in the following year(s).
- 2) If leave is not attributable to a specific employee but rather grouped in a "leave pool" available to all employees on an as-needed basis, the government should use an estimated pay based on the eligible employee population.
- 3) Leave likely to be settled through a noncash means, other than conversion to defined benefit postemployment benefits, should measure the liability on the estimated amount of settlement.

(GASB 101 ¶¶ 16-19)

Leave That Has Been Used

Report a liability when leave is used for time off but has not yet been paid in cash or settled through any noncash means as previously discussed. The measurement should be based upon the applicable payment amount, plus any salary-related payments, at the time of payment or settlement. (GASB 101 ¶ 21)

Salary-Related Payments

Salary²-related payments are obligations related to leave in exchange for services rendered encompassing items such as the employer shares of Social Security and Medicare taxes. A government should include in the measurement of its liabilities for compensated absences (used and not used) salary-related payments associated with the leave. These payments can be directly associated as a function of salary or incrementally associated if the government is making a payment in addition to the payment of salary. (GASB 101 ¶¶ 22-24)

² When determining if payments are salary-related, "salary" indicates pay provided to the employee, whether it is a fixed amount or an hourly wage.

Salary-related payments related to defined benefit pensions or defined benefit OPEB should not be included in the measurement of liabilities for compensated absences. (GASB 101 ¶ 26)

Developing Estimations

The GASB Board (the Board) considered adapting either the termination payment method or the vesting method for sick leave, ultimately choosing not to do so believing that requiring a specific method to determine the estimate may be too rigid. Specific to the vesting method's inclusion in GASB 16, there was a valid concern that the historical information required for the termination payment method might not be readily available to all governments to make a good faith accurate estimation. The Board believes that governments now generally have access to historical data that can facilitate such an estimate. (GASB 101 ¶ B13)

The information necessary to estimate the liability for compensated absences is expected to be available from payroll records or human resources and that all governments would have the ability to determine a reasonable estimate for the liability for compensated absences. (GASB 101 ¶ B21)

The Board also considered measuring the compensated absence liability at either present or current value. Present value is typically employed for long-term liabilities when there is a schedule of payments due over time. Compensated absences generally do not have a set payment schedule and are required to estimate amounts and timing for future years. Therefore, the Board concluded that the liability for compensated absences should be measured at current value rather than present value. Moreover, the Board believes that the measurement of liabilities for compensated absences at current value is comparable to discounting expected future cash flows at the inflation rate, therefore achieving much of what present value intends to achieve. (GASB 101 ¶ B37)

Amount Due within One Year

As previously noted, compensated absences generally do not have a set payment schedule requiring an estimated amount specific to due within one year. While taking under consideration the difficulties in assessing short-term liquidity specific to this liability, the Board concluded that the liability should report two components, due within and due in more than one year. There is no belief in calculating a due within one year liability is any more difficult than in determining other required estimates. (GASB 101 ¶ B41)

Flows Assumption

A key component in determining the estimate of the amount due within one year is identifying the flow assumption, whether it is a first in, first out (FIFO) or a last in, first out (LIFO) assumption. Whether implicit or explicit, the flow assumption is used to determine whether the amount a government expects to pay in the next reporting period will be assigned first to the liability at the date of the financial statements (FIFO) or to the leave earned in the next reporting period (LIFO).

The flow assumption can be determined based upon policies, negotiated agreements, and current practices in place. (GASB 101 ¶¶ B43-B45)

Financial Statements Prepared Using the Current Financial Resources Measurement Focus

All liabilities for compensated absences are accounted for and reported on a basis consistent with governmental fund accounting principles. The financial statements, specific to compensated absences expenditures, should utilize the current financial resources measurement focus. This should be the amount that normally would be liquidated with expendable available financial resources, consistent with guidance provided in GASB Interpretation 6, as amended. (GASB 101 ¶ 29)

Notes to Financial Statements

GASB 101 amends the long-term liabilities disclosure required by GASB Statement No. 34, and indicates local governments should present either separate increases and decreases or an aggregate net increase or net decrease in the liability for compensated absences. If presenting the net increase/decrease, the government should indicate that it is utilizing the net amount. (GASB 101 ¶ 30)

Applicability to Non-GAAP Entities

Governments not statutorily required to prepare GAAP statements that prepare regulatory statements and governments that prepare Other Comprehensive Basis of Accounting (OCBOA) statements will not need to make any changes to their financial statements. Any disclosures in the summary of significant accounting policies related to accumulated leave should be updated to describe the accounting treatment for accumulated leave, including balances that can be used for time off as well as balances for which employees are entitled to cash payments, as applicable.

Transition

Governments should restate beginning net position, applying GASB Statement No. 100 – *Accounting Changes and Error Corrections*. GASB 101 transition guidance identifies changes to conform with GASB 101 as a change in accounting principle. (GASB 101 ¶33)

Additional Resources Available on the Auditor of State’s Website

The Auditor of State’s Office has a Frequently Asked Questions (FAQ) document available related to GASB 101’s implementation available on our website at:

<http://www.ohioauditor.gov/references/gasbfaqs.html>.

The FAQs will be updated as additional information becomes available.

Questions

If you have any questions regarding the information presented in this Bulletin, please contact Local Government Services at the Auditor of State's Office at (800) 345-2519.

A handwritten signature in black ink that reads "Keith Faber". The signature is written in a cursive style with a large, stylized "K" and "F".

Keith Faber
Ohio Auditor of State