

The Payroll Accrual

Creating the accrual and reversing journal entries

Supplement to *Bookkeeping for Nonprofits*, by Murray Dropkin and James Halpin
ISBN 0-7879-7540-0, paperback, published by Jossey-Bass, An imprint of Wiley.
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What is a payroll accrual?

At the end of each accounting period (typically at the end of each month), we need to make adjusting entries to match revenues and expenses. A common entry to make is a payroll accrual, to record any wages earned by the employees but not yet included on a paycheck. With the payroll accrual entry, we charge (debit) wage expense and credit a current liability typically called "accrued payroll".

As with any accrual journal entry, we are shifting a monetary transaction from the period it is posted in to the period where it belongs.

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BOOKKEEPING FOR NONPROFITS

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As with any accounting monetary transaction, the period when

Matching is the concept of recording expenses incurred in generating revenue in the same period that we record the revenue. We try to match revenue with expenses.

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For example:

Our hospital is open 7 days per week, 24 hours per day. The payroll ends on a Saturday, and paychecks are dated the following Wednesday. As we work on our books for the month of October, we see that the last pay period ended on October 29th; those paychecks were dated November 2nd.

Sun	Mon	Tue	Wed	Thu	Fri	Sat
Oct 23	24	25	26	27	28	29
30	31	Nov 1	Checks 2	3	4	5

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7 day pay period in October is paid on a November paycheck

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Our pay period runs from October 23rd to October 29th. We have to accrue the payroll expense for the entire week, since those wages are paid on November 2nd. We also have to accrue the payroll expense for October 30 and October 31; these wages won't be paid until November 9th. Our total accrual will be for 9 days: 10/23 through 10/31.

Sun	Mon	Tue	Wed	Thu	Fri	Sat
Oct 23	24	25	26	27	28	Accrue 29
30	Accrue 31	Nov 1	Checks 2	3	4	5

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These last 2 days of October are not paid until November 9th.

Sun	Mon	Tue	Wed	Thu	Fri	Sat
Oct 23	24	25	26	27	28	Accrue 29
30	Accrue 31	Nov 1	Checks 2	3	4	5

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How much do we accrue?

We can easily obtain the actual expense for the week ended 10/29 by examining the payroll journal for that week. How we accrue the remaining 2 days depends on what information is available to us. If the payroll system is able to give us the exact amounts for those 2 days, we'll use the exact amounts. More typically, we need to estimate the expense using a reasonable basis. For this example, we'll assume we have two categories of pay (Nursing wages and Administrative salaries), and we'll assume our payroll system cannot give us the exact expense for those two days.

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Nursing Wages

Our nursing staff works seven days per week, and there is no substantial difference in staffing among the days of the week. Note that while no single nurse works more than five days, the nursing position is staffed around the clock, every day. For our accrual calculation, we can use a ratio of 2/7; we'll accrue 2 of the 7 days (28.57%) of the nursing wages paid on the November 9th payroll, plus 100% of the nursing wages paid on the November 2nd payroll. (To keep our example simple, we are ignoring payroll tax expense and other related costs.)

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Administrative Salaries

Our administrative staff works 5 days per week, and there is no substantial difference in staffing among the days of the week. For our accrual calculation, we can use a ratio of 2/5; we'll accrue 2 of the 5 days (40%) of the administrative salaries paid on the November 9th payroll, plus 100% of the administrative salaries paid on the November 2nd payroll. (To keep our example simple, we are ignoring payroll tax expense and other related costs.)

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A14		fx		
	A	B	C	D
1		Nursing	Admin	
2				
3	Week ended 11/9/xx	27,632.00	9,200.00	
4	Percentage to accrue	28.57%	40.00%	
5		7,894.46	3,680.00	
6	Week ended 11/2/xx	28,432.50	9,170.00	
7		36,326.96	12,850.00	
8				
9				
10				

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5		7,894.46	3,680.00	
6	Week ended 11/2/xx	28,432.50	9,170.00	
7		36,326.96	12,850.00	
8				
9				
10				

2 days out of 7 = 28.57%

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5			3,680.00	
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7		36,326.96	12,850.00	
8				
9				
10				

2 days out of 5 = 40%

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6	Week ended 11/2/xx	28,432.50	9,170.00	
7		36,326.96	12,850.00	
8				
9				
10				

Add the full prior week to the 2 days to get the 9 day accrual amount.

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Journal Entry #: 02		Date: 10/31/XX		
Description: Payroll Accrual				
Account	Description	Ref.	Debit	Credit
65100	Nursing Wages		36326.96	
41100	Administrative Salaries		12850.00	
02350	Accrued Payroll			49176.96

Here is our accrual entry

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The debits equal the credit.

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65100	Nursing Wages		36326.96	
41100	Administrative Salaries		12850.00	
02350	Accrued Payroll			49176.96

The \$49176.96 that we paid for salaries and wages in the last 9 days of October is now an October expense, even though it was not disbursed until November.

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Reversing the Accrual

When we accrue an expense, we are moving the transaction from one accounting period to another. In this example, we have moved payroll paid in November to the month where the payroll was earned by the employees (October). The normal November payroll posting will still include all payroll checks written in November, including wages paid for the last 9 days of October. If we do not reverse our October payroll accrual in November, that expense will be posted twice (in the October accrual and in the November payroll totals). By reversing our October accrual in November, we solve this.

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Journal Entry #: 02 Date: 11/30/XX
Description: Reverse Payroll Accrual

Account	Description	Ref.	Debit	Credit
65100	Nursing Wages			36326.96
41100	Administrative Salaries			12850.00
02350	Accrued Payroll		49176.96	

The amounts are the same as in the accrual entry. Every debit from that entry is now a credit.

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Journal Entry #: 02 Date: 11/30/XX
Description: Reverse Payroll Accrual

Account	Description	Ref.	Debit	Credit
65100	Nursing Wages			36326.96
41100	Administrative Salaries			12850.00
02350	Accrued Payroll		49176.96	

and every credit is now a debit

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41100	Administrative Salaries			12850.00
02350	Accrued Payroll		49176.96	

The accrual and the reversal, when added together, do not change the expense totals. They do move some of the expense from one accounting period to another, which is the whole idea.

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Summary

Payroll is a cash basis system, and it is being recorded in an accrual based accounting system. Payroll is posted on the date the paychecks are written, which seldom matches the period when the money was earned by the employees. An accrual entry moves the expense from the period it was paid to the period where it "belongs". This accrual entry must be reversed in the next period to avoid "doubling up" on the expense. The net effect of the accrual and reversal is zero for all accounting periods combined, with the benefit of recording the expense in the period where it belongs.

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by Jim Halpin

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