

**Revenue Ruling  
No. 02- 006  
May 17, 2002  
Corporation Franchise Tax**

**Accrued Vacation Pay**

**Purpose:** The purpose of this Revenue Ruling is to determine whether accrued vacation pay should be included in the computation of surplus and undivided profits for franchise tax purposes.

**Analysis/Discussion:** La. Rev. Stat. Ann. / 47:605(A)(West 2001), provides that in computing surplus and undivided profits there shall be included all reserves other than those for definitely fixed liabilities . . . .

According to Kieso and Weygandt, Intermediate Accounting, 635-637 (8<sup>th</sup> ed.), an employer is required to accrue a liability for employees compensation for future absences if all of the following conditions are met: (1) the employer's obligation relating to employees rights to receive compensation for future absences is attributable to employees services already rendered; (2) the obligation relates to rights that vest or accumulate; (3) payment of the compensation is probable; and, (4) the amount can be reasonably estimated.

If an employee is at risk of losing his or her accrued vacation pay for any reason, the accrued vacation pay cannot be thought of as a definitely fixed liability.

In the situation addressed by this Revenue Ruling, which is the most common scenario, an estimated vacation pay accrual is made at the end of the year based upon the amount of average employee experience with the company and the various vacation policies for different types of employees. If during the subsequent year, an employee doesn't take the vacation pay that has been earned, such accrued vacation pay is lost. If an employee resigns, such employee is not paid for the vacation time they have earned.

The vacation pay accrual account is evaluated at the end of each year based upon changes in the number of employees, variations in the experience level of the employees, and increases or decreases in the salary level of the employees. The account is not maintained in a manner which details specific employees. As such, it is neither debited nor credited as employees earn and use vacation pay.

**Conclusion:** Due to the risk of loss in the situation addressed by this Revenue Ruling, accrued vacation pay cannot be thought of as a definitely fixed liability. Therefore, such accrued vacation pay should properly be included in the computation of surplus and undivided profits for franchise tax purposes. However, if accrued vacation pay is accounted for by employee, debited and credited as each employee uses and earns vacation and an employee is certain to be compensated for the accrued vacation pay in addition to the employee's regular pay when the employee fails to take an earned vacation, such accrued vacation pay should properly be considered a definitely fixed liability and therefore indebtedness. If the accrued vacation pay is

indebtedness, then the provisions of La. Rev. Stat. Ann./47:603 (West 2001) must be employed to determine to what extent it is included in taxable capital.

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