

Why you should NOT use Estimated Leave Balances

The Holidays Act stipulates that *annual leave accrues on the Employee's anniversary* – anything else is an *estimated balance* and is often the subject of discussion and source of misunderstanding.

Showing *estimated leave balances* on Payslips (regardless of Employee pressure) is NOT recommended. It is possibly misleading as far as the Employee is concerned. Estimated values represent an estimate of leave that would accrue assuming the Employee stays until the next anniversary, rather than a balance that might apply should they leave. This is because it is reasonable to assume an Employee would be entitled to an estimated 2 weeks of annual leave for six months of service – which almost certainly will not be their entitlement in a final pay situation unless they earn exactly the same earnings every week (no Overtime, Allowances, absence etc).

Consider this: an Employee started 6 months ago, working a few days here and there but now works more-or-less full time. His Payslip shows an *estimated leave balance* of 2 weeks. If he were to leave, he wouldn't receive anything like 2 weeks of leave, he is entitled only to 8% of his liable earnings.

A further complication occurs when the Employee's *anniversary occurs within the current pay period*. The anniversary hasn't triggered an accrual until the pay finishes, so the estimating process works on the old accrued balance plus a proportion of the annual entitlement (based on the number of days elapsed from the last anniversary date to the current period ending date). The pay following will be based on the new accrued balance, plus 8% if it's positive, plus a proportion of the annual accrual – producing quite a different result due to the possible extra 8% on the unused balance.

Comparing an estimated balance with figures from other Reports also causes much confusion – until you understand that various Leave Reports are often intended for different purposes, or are based on totally different views (eg money valuation as opposed to time valuation). For example, the *Leave Liability Report's* purpose is to reflect the Company's liability for *final annual leave entitlements in dollar terms*, it is also based on 8% final pay entitlement calculations, whereas the *estimating process* is based on a proportion of time elapsed since last anniversary – two completely different requirements, producing two quite different outputs.

Despite that, I want to use Estimated Leave Balances

Those who require *estimated balances* to be shown on Payslips will run into numerous issues with attempting to understand the logic behind the estimating process.

This Factsheet attempts to address this issue so you have a working knowledge of how **SmoothPay** implements leave estimating.

The following examples illustrate a number of scenarios (as used by **SmoothPay**) for calculating and checking *estimated leave balances* on Payslips.

Where people tend to go wrong when trying to understand the complexities of Holidays Act entitlements is that *leave does not actually accrue per pay period* and the estimated balance does not necessarily follow a linear progression (eg you might expect the balance to increase by 0.07692 weeks per week).

You need to be fully aware of three things before starting this process:

- 1) **Leave does not accrue per pay period.** The Holidays Act prescribes that leave accrues on the Employee's anniversary. Anything else will be an *estimate*, and **SmoothPay's estimated balance** is based on the same logic as a termination pay (except it's working with time, not money). A Final Pay Calculation form is available on our [website...Forms...Final Pay Calculation](#) for your further reference.
- 2) **When leave does accrue** (as per the Act), the Employee is entitled, as part of any termination value calculation (and for the purposes of estimating entitlement), to an additional 8% on unused leave remaining from the Employee's last anniversary (this is shown clearly on the *Final Pay Calculation form*). Until that time, because the accrual hasn't yet occurred, the extra 8% liability that would occur on a positive leave accrued balance would not occur if the accrued balance is less than zero.
- 3) **Annual leave accrues in weeks** - anything else is *non-compliant*.

NOTE: All examples are based on 4 weeks annual accrual and accrual occurs on each anniversary, in accordance with the Holidays Act.

Example 1

Sam has a *zero accrued leave balance*. He has used up his previous accruals, or started less than 12 months ago and hasn't used any leave yet, and it's six months since his last anniversary or start date:

Opening Accrued Balance		0
Less any Leave taken this Pay		0
Balance of Accrued Leave		0
Plus 8% (if Balance is > 0)		0
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 182 (6 months)	2
Estimated Balance		2

His following Pay Period (again, has used no Leave) would calculate as:

Opening Accrued Balance		0
Less any Leave taken this Pay		0
Balance of Accrued Leave		0
Plus 8% (if Balance is > 0)		0
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 189	2.07
Estimated Balance		2.07 (increase of 0.07692)

You can see that this produces a linear increase in his *estimated leave balance*. However, things don't normally work that way, so the following examples show what happens in real life, where Employees take Leave in advance, and when their Anniversary occurs.

Example 2

Sam has *taken leave in advance* and his *accrued leave balance is negative*. He's very close to accruing his next Leave entitlement (it's 3 days away from the Period End Date):

Opening Accrued Balance		-3
Less any Leave taken this Pay		0
Balance of Accrued Leave		-3
Plus 8% (if Balance is > 0)		0
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 362	3.97
Estimated Balance		0.97

His following Pay Period (again, has used no Leave and his accrual won't trigger until the pay is completed) would calculate as:

Opening Accrued Balance		-3
Less any Leave taken this Pay		0
Balance of Accrued Leave		-3
Plus 8% (if Balance is > 0)		0
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 369	4.04
Estimated Balance		1.04 (increase of 0.07692)

His next Pay shows an *unexpected jump in his balance*, because his *annual accrual has now occurred*, and as it is now a positive balance it also attracts an extra 8%:

Opening Accrued Balance	-3 + 4	1
Less any Leave taken this Pay		0
Balance of Accrued Leave		1
Plus 8% (if Balance is > 0)		0.08
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 11	0.12
Estimated Balance		1.2 (increase of 0.16)!

Example 3

Sam has *taken lots of Leave in advance* and his *accrued leave balance is negative*. He's *very close to accruing his next leave entitlement* - it's 3 days away from the period end date:

Opening Accrued Balance		-5
Less any Leave taken this Pay		0
Balance of Accrued Leave		-5
Plus 8% (if Balance is > 0)		0
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 362	3.97
Estimated Balance		-1.03

His following Pay Period (again, he has used no Leave and his accrual won't trigger until the Pay is completed) would calculate as:

Opening Accrued Balance		-5
Less any Leave taken this Pay		0
Balance of Accrued Leave		-5
Plus 8% (if Balance is > 0)		0
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 369	4.04
Estimated Balance		-0.96 (increase of 0.07692)

His next Pay shows a *smaller than expected increase in his balance*, because his annual accrual has now occurred but it's still a negative balance:

Opening Accrued Balance	-5 + 4	-1
Less any Leave taken this Pay		0
Balance of Accrued Leave		-1
Plus 8% (if Balance is > 0)		
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 11	0.12
Estimated Balance		-0.88 (increase of 0.08)

Example 4

Sam has *lots of leave remaining*. He's very close to accruing his next leave entitlement - it's 3 days away from the period end date:

Opening Accrued Balance		5
Less any Leave taken this Pay		0
Balance of Accrued Leave		5
Plus 8% (if Balance is > 0)		0.4
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 362	3.97
Estimated Balance		8.97

His following Pay Period (again, he has used no leave and his accrual won't trigger until the Pay is completed) would calculate as:

Opening Accrued Balance		5
Less any Leave taken this Pay		0
Balance of Accrued Leave		5
Plus 8% (if Balance is > 0)		0.4
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 369	4.04
Estimated Balance		9.44 (increase of 0.47)!

His next Pay (after the anniversary has occurred) shows:

Opening Accrued Balance	5 + 4	9
Less any Leave taken this Pay		0
Balance of Accrued Leave		9
Plus 8% (if Balance is > 0)		0.72
Plus proportion of Annual Accrual (Accrual / 365 x days)	4 / 365 x 11	0.12
Estimated Balance		9.84 (increase of 0.4)!

Varying any of these factors, the number of days before or since anniversary, the annual accrual (unless otherwise set in configuration), **SmoothPay** will treat 4 weeks as 8%, 5 weeks as 10% etc, any Leave being taken, will cause changes in the values and the effect on the *estimated balance* can be significant.

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