**unit 6. accounting systems for payroll and payroll taxes**

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**6.0 aims and objectives**

This unit aims at discussing the accounting for payroll and payroll tax liabilities. The techniques and procedures used in computing personal income tax, pension contributions, and other deductions are discussed in detail. Also, the journal entries and other records necessary in accounting for payroll will be explained and illustrated based on examples. After reading and covered this unit you would be able to:

* understand the importance of payroll accounting
* define payroll related terms
* describe the components of a payroll register
* calculate income taxes, pension contribution and other deductions and net pay
* record journal entries related to payroll and payroll taxes
* prepare a payroll register

**6.1 introduction**

In the previous chapter you have discussed the basic accounting principles and practices that are useful in accounting for the acquisition, use, and disposal of plant assets, as well as the accounting for intangible assets and natural resources have also been discussed briefly.

In this chapter you will be acquainted with the basics of accounting for payroll and payroll taxes. Accounting systems for payroll and payroll taxes are concerned with the records and reports associated with the employer-employee relationship. It is important that the accounting system provide safeguard to ensure that payments are in accord with management’s general plans and its specific authorizations.

All employees of an organization expect and are entitled to receive their remuneration at regular intervals following the close of each payroll period. Regardless of the number of employees and the difficulties in computing the amounts to be paid, the payroll system must be designed to process the necessary data quickly and assure payment of the correct amount to each employee.

The system must also provide adequate safeguards against unauthorized payments to employees and other misappropriations of funds.

Various federal, state, and local laws requires employers to keep accurate payroll records and to prepare reports and submit to the appropriate governmental units. The law also require employers t remit the amounts withheld from its employees and for taxes imposed on itself. These records must be kept for specified periods of time and be available for inspection by those responsible for enforcement of the laws. Besides, payroll data may be useful in negotiations with labor unions, in settling employee grievances, and in determining rights to vacations, sick leaves, and retirement pensions.

Here, in this chapter, you are going to learn intensely and worked through the major concepts that are common to most payroll systems such as the employee’s earnings record, payroll sheet (or register), and journal entries related to payroll. Each of these concepts is illustrated and discussed by taking into account the current tax law of the country. As much as possible the chapter attempts to give you adequate knowledge about payroll systems in Ethiopia, however, if you come across any confusion or difficulties you can consult the authorities in the Ministry of Finance or Inland Revenue Administration in your locality, or refer the various proclamations especially; Proclamation No. 286 / 2002, the council of ministers regulation No. 78 / 2002. And Article 33 or proclamation No. 64 / 1975

**6. 2 importance of payroll accounting**

Accounting for payroll is particularly important because:

1. Payroll often represents the largest expense that a company incurs.
2. Both federal and state governments require that detailed payroll records be kept and
3. Employees are sensitive to payroll errors or irregularities. To maintain good employee morale payroll must be paid on a timely and accurate basis.

**6. 3 definition of payroll related terms**

***1. Salary and Wages:*** Salary and wages are usually used interchangeably. However, the term wages is more correctly used to refer to payments to unskilled-manual labor. It is usually paid based on the number of hours worked or the number of units produced. Therefore, wages are usually paid when a particular piece of work is completed or weekly.

On the other hand, salaries refers to payments to employees who render managerial, administrative or similar services, and they are usually paid to skilled labor on a monthly or yearly basis.

Both wages and salaries related to an ‘employee’ is an individual who works primarily to one organization and whose activities are under the direct supervision of employer.

A self-employed person on the other hand works (gives her services) on a fee basis to various firms.

***2. The Pay Period:*** A pay period refers to the length of time covered by each payroll payment.

***3 The Pay Day:*** The pay day- is the day on which wages or salaries are paid to employees. This is usually on the last day of the pay period.

***4. A Payroll Register (sheet):*** is the list of employees of a business along with each employee’s gross earnings; deductions and net pay (take home pay) for a particular pay period. The payroll register (sheet) is prepared based on attendance sheets, punched (clock) cards or time cards.

***5. Pay Check:*** A business can pay payroll by writing a check for the amount of the net pay. A check is prepared in the name of each employee and handed to employees. Alternatively a check for the total net pay can be prepared for employees to the paid by cash at the organization.

***6. Gross Earnings*:** are taxes collected from the earnings of employees by t he employer organization as per the regulations of the government. These have to be submitted (paid) to the government because3d employer organization is only acting as an agent of the government in collecting these taxes from employees.

***7. Payroll Deductions:*** are deductions from the gross earnings of an employee such as employment income taxes (with holding taxes), labor union dues, fines, credit association pays etc.

***8. Net Pay:*** Net Pay is the earning of an employee after all deductions have been deducted. This is the take home pay amount collected by an employee on the payday.

**6.4 Possible components of a Payroll Register**

**1 Employee Number**

Number assigned to employees for identification purpose when a relatively large number of employees are involved in a payroll register.

**2 Name of Employees**

**3 Earnings**

Money earned by an employee from various sources,. This may include.

1. ***Basic Salary****-* a flat monthly salary of an employee for carrying out the normal work of employment and subject to change when the employee is promoted.
2. ***Allowances-*** money paid monthly to an employee for special reasons, like:
	* + *Position allowance*- a monthly paid to an employee of earning a particular office responsibility.
		+ *Housing allowance-* a monthly allowance given to cover housing costs of the individual employee when the employment contract requires the employer to provide housing but the employer fails to do so.
		+ *Hardship allowance*- a sum of money given to an employee to compensate for an inconvenient circumstance caused by the employer. For instance, unexpected transfer to aw different and distant work area or location.
		+ *Desert allowance-* a monthly allowance given to an employee because of assignment to a relatively hot region.
		+ *Transportation (fuel) allowance-* a monthly allowance to an employee to cover cost of transportation up to her workplace if the employer has committed itself to provide transportation service.

***C. Overtime Earning:*** Overtime work is the work performed by an employee beyond the regular working hours.

Overtime earnings are the amount paid to an employee for overtime work performed.

Article 33 of proclamation No. 64/1975 discussed the following about how overtime work should be paid:

A worker shall be entitled to the paid at a rate of

* 1. one and one-quarter (1 ¼) times his ordinary hourly rate for overtime work performed before 10:00 P.M in the evening.
	2. One and one half (1 ½) times his ordinary hourly rate for overtime work performed between 10:00 P.M and six (6:00 A.M) in the morning.
	3. Two times the ordinary hourly rate for overtime work performed on weekly rest days
	4. two and one half (2 ½ ) times the ordinary hourly rate for overtime work performed on a public holiday.

All in all, the gross earnings of an employee may include the basic salary, allowance and overtime earnings.

**Check Your Progress Exercise – 1**

1. What term is frequently used to refer to the total amount paid to employees for a certain period?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………**

1. Distinguish between salaries and wages?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………**

1. An employee earns Br. 50 per hour with one and quarter (1 ¼) times than regular hourly rate for all hours in excess of 40 per week. If the employee worked 50 hours during the current week, what was the gross earning for the week?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………**

**4 Deduction:** are subtractions made from the earnings of employees required by the government or permitted by the employee himself.

* + 1. ***Employment Income Tax:*** Every citizen is required to pay employee tax to the government in almost all countries. In Ethiopia also, income tax is charged on the gross earnings of the employee at the rates indicated under schedule A of the Proclamation N. 286/2002- Income tax proclamation.

The tax rates under schedule A are Presented below:

|  |  |
| --- | --- |
| **Employment Income****(per month)** | **Income****Tax rate** |
|  Over Birr | To Birr | Exempt (Free from Tax) |
| 0 | 150 |
|  151 |  650 | 10% |
|  651 |  1400 | 15% |
| 1401 |  2350 | 20% |
| 2351 |  3550 | 25% |
| 3551 |  5000 | 30% |
| Over 5,000 |  | 35% |
|  |  |  |
|  |  |  |

\*In computing and withholding tax, the income tax proclamation dictates that income attributable to the month of Nehassie and Pagumen shall be aggregated (added) and treated as the income of one month.

Taxable income includes any payment or gains in cash or I n kind received from employment by an individual, including income from former employment or otherwise or from prospective employment.

**Check Your Progress Exercise – 2**

1. What is the total amount deducted as income tax for an employee who earns a basic montly salary of Br. 1800, a monthly non taxable allowance of Br. 300, and an overtime earning of Br. 400?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………**

1. Describe (i) Basic (regular) pay, (ii) Overtime pay

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………**

**Short cut to Income Tax Calculation**

|  |  |
| --- | --- |
| **Employment Income****(per month)** | **Income****Tax Payable** |
| Over Birr | To Birr |  |
|  0 | 150 | No tax |
| 151 | 650 | (10% X EI) – 15 |
| 651 |  1400 | (15% X EI) – 47.5 |
|  1401 |  2350 | (20% X EI) – 117.5 |
|  2351 |  3550 | (25% X EI) – 235 |
|  3551 |  5000 | (30% X EI) – 412.5 |
| Over 5,000 |  | (35% X EI) – 662.5 |

EI = Employment Income or taxable income

15 = (150 X 0.1) – 0

47.5 = [(150 X .15) – 0] + [(500 X 0.15) – (500 X 0.1)]and so forth

Proclamation No. 286/2002 states that the following are not taxable.

1. income from employment received by casual employees who are not regularly employed provided that they do not work for more than one month for the same employer in any twelve months period.
2. Pension contribution, provident fund and all forms of retirement benefits contributed by employers in an amount that doesn’t exceed 15% of the monthly salary of the employee.
3. Payments made to---- (an employee) as a compensation or gratitude in relation to:
	* personal injuries suffered by that person
	* the death of another person

The council of ministers regulation No. 78/2002

Regulations issued pursuant to the income tax proclamation further exempts the following from income tax.

1. Amounts paid by employers to cover the actual cost of medical treatment of employees.
2. Allowance in view of means of transportation granted to employees under contract of employment, i.e., transportation allowance.
3. Hardship allowance
4. Amounts paid by employee in reimbursement of traveling expenses incurred on duty.

***4.b. Pension Contribution***

Permanent employees a governmental organization in Ethiopia is expected to pay or contribute 4% of their basic salary to the governments’ pension trust fund.

This amount is withheld by the employer from each employee on every payroll and later be paid to the respective government body.

The employer is also expected to contribute towards this same fund 6% of the basic salary of every permanent government employee.

Therefore, the total contribution to the pension fund of the Ethiopian government is equal to 10% of the basic salary of all of its permanent employees.

That is, 4% comes from the employees and 6% comes from the employer.

This enables a permanent employee of a government organization to be entitled to the pension pay when retiring provided the employee satisfies the minimum requirements to enjoy the benefits.

Business and non-governmental not-for profit organization (NGO’s) also have this kind of a scheme to benefit their employees with some modifications. A fund known as provident fund is established and both the employer and the employee contribute towards this fund monthly. When an employee retains or leaves employment, a lump sum amount is paid to him/her.

***4.c. Other Deductions***

Apart from the above two kinds of deductions, employees may individually authorize additional deductions such as deductions to pay life insurance premiums, to repay loan from the employer, to pay for donation to charitable organization, contributions to "ldir" etc.

**Check Your Progress Exercise – 3**

* 1. Identify the federal and state taxes that most employers are required to withhold from employees?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………..**

* 1. What is the employer share of pension contributions for a government permanent employee whose regular monthly salary of Br. 2400?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………..**

**5 Net Pay**

Net pay represents the excess of gross earnings over total deductions of an employee.

*Signature*

The payroll sheet should have a column for signature of the employee to be taken when the employee collects the net pay.

**6.5 major Activities involved in accounting for payroll**

***1 Gathering the necessary data*** *-* All the relevant information about every employee should be gathered.

This requires reviewing various documents such as attendance sheets and doing some arithmetic work.

***2 Entering the names of employees*** - along with the gathered data such as earnings, deductions and net pays in the appropriate columns of the payroll register.

***3 Totaling and proving the payroll register*** -the grand total for earnings must be checked if its equal to the sum of the grand totals of deductions and net pays.

***4 The accuracy and authenticity of the information*** - summarized in the payroll should be verified by a different person from the one who prepared it.

***5 The payroll*** - should be approved by an authorized personnel (individual)

***6 Paying the payroll -*** either in cash or by writing a check.

***7 The payment of the payroll and income taxes* -** withheld from employees (withhold doing tax liability) should be recorded in journal entry form.

***8 The withholding******tax* -** must be paid to the relevant government authority in time (promptly) and this is recorded in journal entry form.

**Check Your Progress Exercise – 4**

1. How is Net Pay computed?

**………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………………**

1. Assume an employee's regular hourly pay is Br. 16, with a time and a half for every hour worked in excess of 48 during a week. The following data are available:

Hours worked during current month Br. 200

 Regular monthly salary Br. 3072

 Allowance (transportation) Br. 300

Assume that according to company policy transportation allowance in excess of Br. 200 is subject to employment income tax.

Based on the above data, compute the amount of the employee's:

* 1. net pay for the current month;
	2. employment income tax,
	3. total deductions, assuming the employee is permanent civil servant.

**6.6 Illustration of a payroll register**

Godanaye is a government agency recently organized to rehabilitate street children. It has five employees whose salaries are paid according to the Ethiopian calendar month. The following data relates to the month of Yekatit, 1995.

***Serial Name of Employee Basic Transp. Overtime Duration of***

***No. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ Salary Allowance worked(hr) OT Work***

01 Aregash Shewa Br. 730 200 4 6:00-10:00 P.M

02 Paulos Chala 1020 \_\_\_ 8 Sunday(8:30-5:30)

03 Mohammed Modesir 5300 \_\_\_ \_\_\_ \_\_\_

04 Tensay Belay 1470 \_\_\_ \_\_\_ \_\_\_

05 Haile Olango 950 \_\_\_ 6 Public Holiday

***Additional Information***

* The management of the agency usually expects a worker to work 40 hours in a week and during Yekatit there are four weeks.
* There were no absentees during the month
* All employees are permanent except Tenssay and Haile
* Paulos agreed to contribute monthly Br. 300 from his salary as a monthly saving in the credit association of the agency.

***Required***

1. Prepare a payroll register (sheet) for the agency for the month of Yekatit, 1995.
2. Record the payment of salary as of yekatit 30,1995 using check stub No. 0123.
3. Record the payment of the claim of the credit Association of their agency on Megabit 1, 1995 use check stub No. 0124.
4. Record the payment of the withholding taxes and pension contribution to the concerned government body on Megabit 7,1995.
5. Compute and recognize the total payroll tax expense for the month of Yekatit, 1995.

***Computation of Earnings, Deductions and Net Pay***

Gross Earnings = Basic salary + Allowance + Overtime Earning

***Overtime Earning***

Overtime earning = OT hrs worked X (ordinary hourly rate X relevant OT rate)

1. **AREGASH:**

* OT Earning = 4 hours X br. 730 X 1.25 = br. 22.81

 160 hours

 NB Every employee is expected to work 160 hours per month

 (i.e. 40 hours x 4 weeks)

* You should compute the regular hourly rate first:

 Regular Hourly Rate = Monthly salary (Basic Salary)

 Total Hours worked in the Month

 = br. 730

 160 Hours

* Therefore, the regular Hourly payment = br. 4.56

 The regular hourly payment must be multiplied by the appropriate OT rate as

 follows:

 br. (4.56 x 1.25) x 4 hours-------------------br. 22.81

2. PAULOS

* OT Earning = 8 hours X br. 1020 x 2 ----------------br. 102.00

 160 hours

3. HAILE

* OT Earnings = 6 hours X br. 950 x 2.5 -------------br. 89.06

 160 hours

*GROSS EARNINGS*

 Gross Earnings = Basic salary + Allowance + OT Earnings

1. AGEGASH
	* Gross Earnings = br. 730 + br. 200 + br. 22.81 = br. 952 .81
	* Remember taxable income in this case is br. 752.81 because the transportation allowance of br. 200 is not subject to taxation.
2. PAULOS
	* + Gross Earning = br. 1020 + br. 102 = br. 1122
		+ The Gross Total Earnings of Paulos consists of the br. 1020 basic salary plus the overtime earnings of br. 102, which is br. 1122.
3. MOHAMMED
	* + Gross Total Earnings = br. 5300, which include the basic salary alone
4. TENSAY
	* + Gross Total Earnings = br. 1470, which is the basic salary.
5. HAILE
	* + Gross Total Eanings = br. 950 + 89.06 = br. 1039.06

DEDUCTIONS AND NET PAY

1. AREGASH:
	* Gross Total Earnings-----------------------------------------br. 952.81
	* Gross Taxable Income (br. 952.81 – br. 200)-----------------752.81

 *Employee Income Tax:*

 *Earnings X Income Tax Rate = Income Tax*

 0 – 150---------150 0 br. 00.00

 151 – 650 on 500 10% 50.00

 651 – 752.81 on 102.81 15% 15.42

 TOTAL br. 752.81-----------------------------------------------br. 65.42

 Pension contribution:

 Basic salary x 4%

 = br. 730 x 0.04-------------------------------------------------29.20

 ⇒ Total Deduction (br. 65.42 + br. 29.20)-----------------br. 94.62

NB. The income tax to be deducted from the employee could have been computed by using the short-cut method as follows:

 = (Taxable Income x 15%) – br. 47.5

 = (br. 752.81 x 0.15) – br. 47.5 = br. 65.42

1. PAULOS:
	* Gross Total Earning-----br. 1122.
	* Employee Income tax

 *Earning X Income Tax Rate = Income Tax*

 0 – 150 (150) 0 br. 00.00

 151 – 650 on 500 10% 50.00

 651 – 1122 on 472 15% 70.80

 TOTAL br.1122---------------------------------------------br. 120.80

* Pension Contribution (br. 1020 x 0.04)---------------------40.80
* Credit Association--------------------------------------------300.00
	+ Total Deduction---------------------------------------------br. 461.60
1. MOHAMMED:
	* Gross Total Earnings------------------------------------br. 5300.00
	* *Employee Income Tax*

 *Earning X Income Tax Rate = Income Tax*

 0 – 150-------150 0 br. 00.00

 151 – 650 on 500 10% 50.00

 651 – 1400 on 750 15% 112.50

 1401 – 2350 on 950 20% 190.00

 2351 – 3550 on 1200 25% 300.00

 3551 – 5000 on 1450 30% 435.00

 Over 5000 on 300 35% 105.00

 Total br. 5300.00-----------------------------------------------br. 1192.50

* + Pension contribution (br. 5300 x 0.04)---------------------- 212.00
		- Total Deductions------------------------------------------br. 1404.50
1. TENSAY:
	* Gross Total Earnings------------------------------------br. 1470.00
	* Gross Taxable Income--------------------------------------1470.00

 Employee Income Tax:

 *Earning X Income Tax Rate = Income Tax*

 0 – 150-----150 0 br. 00.00

 151 – 650 on 500 10% 50.00

 651 – 1400 on 750 15% 112.50

 1401 – 1470 on 70 20% 14.00

 Total br. 1470---------------------------------------------------- br. 176.50

*NB. No pension contributions because she is not permanent employee of the organization. Therefore, total deduction is the same as Employee Income Tax, br. 176.50.*

1. HAILE:
	* Gross Total Earnings--------------------------------------br. 1039.06

 Employee Income Tax:

 Earnings X Income Tax Rate = Income Tax

 0 – 150----150 0 br. 00.00

 151 – 650 on 500 10% 50.00

651 – 1039.66 on 389.06 15% 58.36

 Total br. 1039.06----------------------------------------------------br. 108.36

* + Pension contribution should not be computed for Haile because he is not permanent employee of the agency. Thus, the only deduction from Haile’s earnings is the employee income tax.

 NB. It is also possible to compute income tax by using the short-cut method:

 Total Income Tax = (Taxable Income x 15%) – 47.5

 = (br. 1039.06 x 0.15) – 47.5

 = br. 108.36

*NET PAY:*

Net pay = Gross Total Earnings – Total Deductions

1. AREGASH:

 Net pay = br. 952.81 – br. (94.62)

 Net pay = br. 858.19

1. PAULOS:

 Net pay = br. 1122 – br. (461.60)

 Net pay = br. 660.40

1. MOHAMMED:

 Net pay = br. 5300 – br. (1404.50)

 Net pay = br. 3895.50

1. TENSAY:

 Net pay = br. 1470 – br. (176.50)

 Net pay = br. 1293.50

1. HAILE:

 Net pay = br. 1039.06 – br. 108.36

 Net pay = br. 930.70

*PROVING THE PAYROLL:*

 Total Earnings:

 Basic salary-----------------------------------------------br. 9470.00

 Allowances-----------------------------------------------------200.00

 Overtime--------------------------------------------------------213.87

 Grand Total---------------------------------------br. 9883.87

 Deductions:

 Employee Income Taxes--------------------------------br. 1663.58

 Pension Contributions----------------------------------------282.00

 Other Deductions----------------------------------------------300.00 =

 Total Deductions------------------------------br. 2245.58

Net Pay Total------------------------------------------------------br. 7638.29

Total Deductions plus Net pay----------------------------------br. 9883.87

The payroll register (or sheet) for Godanaye Rehabilitation Agency prepared for the Month of Yekatit, 1995 is shown below.

6.7 SUMMARY

The term payroll is used to refer to the total amount paid to employees for a certain period. Payroll includes amounts paid for salaries to managerial or administrative employees as well as wages paid for manual labor.

Accounting systems for payroll and payroll taxes are concerned with the records and reports associated with the employer-employee relationship. It is important that the accounting system provide safeguards to ensure that payments are accord with management’s general plans and its specific authorizations.

Various federal, state, and local laws require employers to keep accurate payroll records and to prepare reports and submit to the appropriate governmental units. The law also requires employees and for taxes imposed on itself. These record must be kept for specified periods of time and be available for inspection by those responsible for enforcement of the laws.

Payroll data may also be useful in negotiations with labor unions, in settling employee grievances, and in determining rights to vacations , sick leaves, and retirement pensions.

Salary and wages are usually used interchangeably. However, the term wage is more correctly used to refer to payments to unskilled manual labor. It is usually paid based on the number of hours worked or the number of units produced. Therefore, wages are usually paid when a particular piece of work is completed or on a weekly basis. On the other hand, salaries refer to payments to employees who render managerial, administrative, or similar services. Salaries are usually paid to skilled labor on a monthly or yearly basis.

A payroll register is the list of employees of a business along with each employee’s gross earnings, deductions, and net pay (take-home-pay) for a particular pay period. The payroll register (sheet) is prepared based on attendance sheets, punched (clock) cards or time cards.

Components of a payroll register include Employee number, Employee name, Earnings (usually Basic or regular salary, Allowances, and overtime), Deductions, Net pay, and Signature.

Earnings are money earned by an employee of an organization from various sources. It may include: (1) the basic salary which is a flat monthly salary of an employee that is paid for carrying out the normal work or employment, (2) allowances which represents money paid monthly to an employee for special reasons, which may include: position allowance, housing allowance, hardship allowance, desert allowance, and transportation (or fuel) allowance, etc, and (3) overtime earnings – the amount payable to employees for overtime work performed.

Deductions are subtractions made from the earnings of employees. Deductions are either required by law or permitted by the employee himself. The principal deductions in Ethiopia are: Employee Income tax, pension contribution, and other deductions like deductions to pay life insurance premiums, to repay loans from the employer, for credit association, to pay for donation to charitable organization, contribution to ‘Idir’, etc.

Net pay or take-home-pay represents the excess of gross earnings over total deductions of an employee.

The payroll sheet should have a column for signature of the employee to be taken when the employee collects the net pay. In general, a payroll register (sheet) should at least show the total earnings of each employee, deductions, and the net pay together with the names and signatures of employees.

***Todanaye***

***Payroll Register(sheet)***

***For the month of Yekatit,1995***

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| Ser. No. | Name ofEmployee | Earnings | GrossEarning | Deductions | TotalDeduc. | NetPay | Sign. |
| Basic salary | Allo-wance | OverTime | IncomeTax | PensionContr. | OtherDeduc. |
| 01 | Aregash Shewa | 730 | 200 | 22.81 | 952.81 | 65.42 | 29.2 |  \_\_\_ | 94.62 | 858.19 |  |
| 02 | Paulos Chala | 1020 | \_\_\_ | 102 | 1122 | 120.8 | 40.8 | 300 | 461.6 | 660.4 |  |
| 03 | Mohammed Mudesir | 5300 | \_\_\_ | \_\_\_ | 5300 | 1192.5 | 212 | \_\_\_ | 1404.5 | 3895.5 |  |
| 04 | Tensay Belay | 1470 | \_\_\_ | \_\_\_ | 1470 | 176.5 |  \_\_\_ | \_\_\_ | 176.5 | 1293.5 |  |
| 05 | Haile Olango | 950 | \_\_\_ | 89.06 | 1039.06 | 108.35 |  \_\_\_ | \_\_\_ | 108.35 | 930.71 |  |
|  |  |  |  |  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |  |  |  |  |
| Totals |  |  |  |  |  |  |  |  |  |  |
| 9470 | 200 | 213.87 | 9883.87 | 1663.57 | 282 | 300 | 2245.57 | 7638.3 |  |

Prepared by\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_Checked by\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_Approved by\_\_\_\_\_\_\_\_\_\_\_

6.8 answers to check your progress questions

*Check Your progress Exercise - 1*

1. Payroll

2. *(a) Salaries* – represent payment for employees who are paid at a monthly or yearly rate. Salary is usually applied to payment for managerial, administrative, or similar services.

*(b) Wages* – represent payment for services of employees at an hourly rate or on a piece work basis. Wage is usually applied payment for a manual labor.

 (*c) Gross Earnings* = Basic Salary + Overtime earning for the week

Weekly Basic Salary = regular hourly rate x weekly regular working hours.

 = br. 50 x 40 hrs. = br. 2000

* + Therefore, weekly regular salary of the employee is br. 2000
	+ Overtime Earning = Overtime Hours worked x (Regular Hourly rate x OT rate)

 OE = 16 x (br. 50 x 1.25)

 OE = 16 x (62.50)

 Overtime Earning = br. 1000.

* Thus, total earnings of the week = br. 2000 + Br. 1000 = br. 3000

*Check Your progress Exercise – 1*

1. Gross total Earnings of the employee = Basic Salary + Allowance +

 Overtime earning

 Gross total Earnings = br. 1800 + br. 300 + br. 400

 Gross Total Earnings = br. 2500

Taxable Income of the employee = br. 2200, which does not include the allowance of br. 300, because it is non-taxable.

 *Earnings X Income Tax Rate = Income Tax*

 0 – 150 150 0 00.00

 151 – 650 on 500 10% 50.00

 651 – 1400 on 750 15% 112.50

 1401 – 2200 on 800 20% 160.00

 Total br. 2200 322.50

* Total Employee Income Tax is therefore, br. 322.50

 (b) *(i) Basic (Regular) pay* – is a flat monthly salary of an employee that is paid

 for carrying out the normal work of employment and subject to change

 when the employee is promoted.

 (ii) *Overtime pay* – is the amount payable to an employee for overtime work

 done.

*Check Your progress Exercise - 3*

 1. Employee income tax

 - employee pension contribution (if any)

2. Pension contribution is the amount of money that each government permanent employee contributes towards a fund which up on the employees retirement, will be drawn upon to finance the participant’s welfare.

* The employer’s share of pension contribution is 6% of the regular monthly salary of the permanent civil employee. Thus; 0.06 x br. 2400 = br. 144.00

*Check your progress Exercise - 4*

 1. Net pay is computed using the following formula:

 Net pay = Gross total Earnings – Total Deductions

2. Gross Total Earnings = Basic Salary + Allowance + Overtime earning

 Gross Total Earning = br. 3072 + br. 300 + (8 hrs x (br. 16 x 1.50)

 = br. 3072 + br. 300 (8 x br. 24)

 = br. 3072 + br. 300 + br. 192

 = br. 3564.00

* Net pay = Total Earnings – Total Deductions
* Total Deductions = Income Tax + pension contribution
* Income Tax: Taxable Income (br. 3564 – br. 200) ---br. 3364.

 *Earnings X Income Tax Rate = Income Tax*

 0 – 150 on 150 0 00.00

 151 – 650 on 500 10% 50.00

 651 – 1400 on 750 15% 112.00

 1401 – 2350 on 950 20% 190.00

 235 – 3364 on 1014 25% 253.50

 Total br. 3364--------------------------------------------------- br. 606.00

* Pension contribution = 4% of basic salary

 Pension contribution = 0.04 x br. 3072 = br. 122.88

 Total Deductions -----------------------------br. 728.88

* (i) Net pay = br. 3564 – br. 728,88

 Net pay = br. 2835.12

* (ii) Employee Income Tax = br. 606.00
* (iii) Total Deductions = br. 606 + br. 122.88 = br. 728.88

6.9 model examination questions

*problem – 1*

chilalo Retail Enterprise, a government owned business, pays its employees salaries according to the Ethiopian calendar Month. The following data relate to the month of Meskerem, 1995 E.C.

 *S.No Employee Name Basic Salary*

 001 Animut Anley birr 2500

 002 Nebiyat Girma 1880

 003 Erecha Megersa 1790

 004 Bekuretsion G/Tensae 1565

*Additional information*

* All workers are expected to work 40 hours per week and during Meskerem there are 4 weeks. The workers have done as they have been expected.
* Nebiyat Girma has worked 10 hours of overtime during Meskerem: 3 hours during ‘Meskel’ and the other 7 hours before 10 p.m.
* Erecha Megersa has also worked 5 hours of overtime: 2 hours during weekly rest days and 3 hours between 10 p.m. – 6 a.m.
* Animut and Nebiyat received a monthly position allowance of br. 350 and br 300 respectively which are both taxable.
* Animut Anley agreed to have a monthly deduction of br. 250 for credit association.
* All workers are permanent except Bekuretsion G/Tesnae.

*Required:*

1. Compute the total deductions and net pay for each employee.
2. Compute (calculate) the total:
	1. Withholding Taxes
	2. Payroll Tax
	3. Record the payment of salary as of Meskerem 30,1995.
3. Pass the entry to pay the withholding taxes to the appropriate government unit.

*Problem – 2*

Habesha Trading co. is a private business enterprise. The company pays the salary of its employees according to the Ethiopian calendar month. The following data relates to the month of Hidar, 1995.

 Serial No. Name Basic Salary

 A 101 Abeje Belew br. 2710

 P 102 Haragua Delelegn 2500

 P 103 Zeleke Belayneh 1800

 M 104 Zinash Manahlot 4200

Additional information

* The organization expects every worker to work 48 hours in a week and during Hidar there are four weeks and all workers have done as they have been expected.
* Ato, Abeje Belew and W/r, Haregua Delelegn are entitled to get a monthly allowance of birr 500 and br. 400 respectively.
* All workers are permanent except W/t, Zinash Manahlot, and they are entitled to a total of 15% provident fund of which 10% from the employer and 5% from the employee.
* Ato Zeleke Belayneh and W/t Zinash Manahlot have worked 12 hours of overtime each on public holidays.
* According to the company rule, any allowance more than birr 200 is subject to income tax.

*Required:* based on the information given above:

1. Compute the income tax for each employee.
2. Compute the total deductions for each employee.
3. Determine the net pay (take-home-pay) for each employee.
4. Compute the total withholding tax for the month.
5. Compute the total payroll tax expense.
6. Pass the journal entry to record the payment of salary as of Hidar 30,1995.

*Problem – 3*

The following data relates to the payroll of the employees of a privately owned business organization known as”ALAZAR Retail Enterprise”, for the month of Megabit, 1995 E.C.

 *Serial Name Basic Overtime Worked*

 *No. Salary Hours Duration*

 01 Aleme T. br. 4300 4 up to 10 PM

 02 Banchayehu S. 960 12 b/n 10PM to 6 AM

 03 Chemdessa N. 1450 8 weekly rest days

 04 Deniel T. 632 10 public holiday

 05 Leilena A. 2000 \_\_\_ \_\_\_\_

*Additional Information*

* The management of the business organization usually expects a woker to work 40 hours in a week.
* There were no absentees during Megabit.

*Required:*

1. Prepare a payroll sheet for the month of Megabit
2. Record the payment of salary as of Miazia 1, 1995
3. Record the recognition of the payroll tax expense as of Miazia 1, 1995
4. Record the payment of withholding taxes to the proper government units as of Miazia 15, 1995

6. 10 GLOSSARY

Payroll- total amount paid to employees for a certain period.

Salary – amount paid to work performed for skilled labor

Wages – amount paid to a piece of work by unskilled labor

Payroll Register (sheet) – a list of employees of a business along with their earnings, deductions and net pay.