

Financial and management accounting: payroll services



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Financial and Management Accounting Case Study: Payroll Services

1. IMPACT ON THE CHARGE PER TRANSACTION:

The payroll department is incurring a total cost of £590, 000 at present. The charge per transaction is £236 (see fig 1 Appendix A) which is the charge applied each time a salary transaction is completed i. e the salary is transferred. If the lump sum is paid to the staff to switch over to the monthly payment system, it is forecasted that it will generate a saving of £20, 000 in Pay Costs while the services and supplies costs are likely to decrease by £3, 000, thereby bringing it down to £98, 000. The recalculated total or full cost will be £ 567, 000 per financial year. In the new scenario the charge per transaction is reduced to £226 thereby showing a saving of £10. On analysis of the figurework it will not be advisable to have these workers shifted over to the monthly payment system as the figures suggest that bulk of the workers are under the monthly payment system. The authority will have to pay a lump sum of £500, 000 to the workers when they shift over to the new system, however in retrspect the cost dished out now will be recovered in a very long time because the savings being made by the authority on different facets of the payroll department are not significant enough. Apart from the savings it does represent harmonisation of the company however there are other aspects to be considered. Bulk of the workers are under the monthly payment arrangement and having the weekly workers under that scheme might cause confusion in the payroll system. However there are some finer points to take into consideration. The ending of the weekly wage payment system might have an adverse effect because the workers who are being offered to shift over to the monthly payment system will still be working on <https://assignbuster.com/financial-and-management-accounting-payroll-services/>

weekly basis. The difference only being that their salaries will be paid on a monthly basis. Alongside these workers there are other workers who are employed on a monthly basis, they work on a monthly basis and receive their salaries on a monthly basis. If the authority wants to keep the weekly and the monthly workers apart and not mix up or confusion between the two, it would have to operate two different payroll departments. There would be one department keeping the records of staff working on a weekly basis but all of whom will be paid a monthly salary and the second department within the payroll section to keep record of the staff working on a monthly basis who also get paid on a monthly basis. Operating two separate departments would therefore mean that all the costs associated with the running of the payroll section will be much more than what they stand at now. The increment in the cost is therefore a major factor to consider. Considering this the weekly staff should not be asked to transfer to the monthly system. The fact that the authority will probably have to run two departments within a department complicates things and also increases the cost factor which is what the authority is geared towards saving. The government is also urging all the authorities to save on the cost side of things and make the authorities economically more viable. Therefore on the basis of the analysis and considerations it is advisable that the authority should not seek to transfer their weekly staff over to the monthly payment system.

2. FINANCIAL APPRAISAL OF OPTION 1 AND 2:

In this case we are faced with the scenario of two options having different lifespans associated with them. Option 1 has a lifespan of 4 years while

Option 2 has a life span of 6 years. Facing this situation we will carry out the financial appraisal on the basis of the equal annual cash flow method whereby the option with the lowest cost will be chosen. The Equal annual cashflow supposes that the cashflows generated as an annuity. In case of annuities we use the annuity factors rather than the individual yearly discount rates to calculate the present values of the cash flows. Whereas in the equal annual cashflow method the annuity factor is the total of all the yearly factors for the duration of the project and in this case the lifespan of the payroll system being put in place.

Equal annual cashflow = present value of costs/annuity factor for N years at R%

Therefore for option 1:

The equal annual cashflow = $916,454 / 2.3299$ (Looking at the annuity tables)

i. e = £ 393, 345 (see appendix B for figures)

and for Option 2:

The equal annual cashflow = $1,453,231 / 2.7967$

i. e = £ 519, 623

Therefore on the basis of the analysis we will chose the option 1 as it has the lowest equal annual cashflow. There are a few limitations with the calculations involving cashflows and capital costs. These cashflows do not

take into account the fluctuation of the interest rate and assume it to be constant over the lifespan. In isolation from authority B's proposal we will choose the first option as it has the lower equal annual cash flow. It is feasible on the basis of the calculations to select option 1 and put it into practice. However there are limitations to the equal annual cashflow method. This appears to be a nice idea however in reality it does not add value to what we can determine from the other methods. The other methods will also yield the same result and therefore adding no extra information for us to make a decision. The equal annual cashflow method can be used alone when other methods yield nothing and this is the last resort for carrying out a financial appraisal. As far as the arithmetic involved in this method it is no more complicated than the other methods and is no more advanced than the traditional methods. There are limitations to this method which leave a lot to be desired. This method ignores the influence of inflation and fluctuation in the interest rate. However it is possible to overcome these limitations by adjusting for these factors. The cashflows can be adjusted for inflation and the fluctuating interest rate in the real world. Firstly a discount rate should be selected that is already adjusted for the inflation and includes an allowance for the inflation. Secondly the cashflows can be expressed in real terms whereby meaning that the anticipated inflation rate can be excluded from the discount rate. In other words the first method provides us with the nominal cashflows while the second method gives us the real cashflows at a real discount rate. The second method excludes the anticipated inflation rate from the discount rate which follows the prudence concept of accounting where the costs are over estimated and the profits are underestimated so as to avoid disappointment later and to cover for the contingencies.

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3. DISCUSSION ON THE PROPOSAL:

Authority B's proposal is to transfer A's payroll function to B. The cost associated with this is £380,000 for the next financial year. Evaluating on the cost basis only the Authority A should go ahead with the transfer because the cost proposed by authority B is less than the cost calculated for authority A which is £393,345 on the equal annual cashflow method. Authority B has also suggested that in future if more authorities join in the cost would be lowered progressively in the following financial years. Based on the calculation and authority B's proposal the authority A its payroll function to authority B. In order to carry out an investment appraisal of the proposal there will be a few items other than the cost. We would need the reduction in the cost due to the shifting of the payroll. We would also require the reduction in cost due to less staff being employed. Reduction in service and supplies costs. However we would also need to know the cost incurred due to the redundancy of a number of staff due to the payroll being transferred. The knowledge of all these costs would enable us to make a much better informed decision on whether or not to transfer the payroll to authority B and whether it would be beneficial in the long run. These financial appraisals have a limitation which is that they do not incorporate inflation however inflation can be adjusted for when carrying out the financial appraisal. The net present value can be adjusted by two ways to take inflation into account. Firstly a discount rate can be used which incorporates inflation. Secondly the discount rate can exclude the inflation rate and the cash flows can be expressed in real terms.

The transferring of the payroll from one different authorities to a central one might result in too many job losses and redundancies which again will be against the government's agenda. The government would certainly not like to contribute to unemployment. In this case this can be solved by spreading the unemployment over different authorities and not increasing the burden on one authority or for that matter a few authorities. The government should also try and create more jobs so as to accomodate these redundancies.

APPENDICES

APPENDIX A:

The cost for operating the payroll section is as follows:

Payroll costs: £216, 000

Services and Supplies: £101, 000

Accomodation:£ 45, 000

Capital Charge:£228, 000

Full Cost:£ 590, 000

The charge to the Budget Holders is:

$£590, 000/2500 = £ 236/\text{Transaction. (fig1)}$

The cost for the payroll after paying the Lump sum:

Payroll Costs: £196, 000

Services and Sipplies:£ 98, 000

Accommodation:£ 45, 000

Capital charge:£ 228, 000

Full Cost:£ 567, 000

The charge now to the Budget Holders is:

£ 567, 000/2500 =£ 226/Transaction(fig2)

APPENDIX B:

OPTION1

START OF YEAR CAHSFLOWS

YRCASHFLOWPV @ 8%

1£ 830, 000 830, 000

2£ 33, 000 28, 290

3£ 36, 300 28, 815

4£ 39, 930 29, 349

TOTAL 916, 454

OPTION 2

START OF YEAR CAHSFLOWS

YRCASHFLOWPV @ 8%

1£ 1400, 000 1400, 000

2£ 22, 000 20, 369

3£ 24, 000 20, 575

4£ 24, 000 19, 051

5£ 24, 000 17, 640

6£ 24, 000 16334

TOTAL 1, 453, 231

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