Abolition of SP/LSP offsetting arrangement

Before abolition of the offsetting arrangement

Employers must make Long Service Payment (LSP) or Severance Payment (SP) per these conditions:

LSP with at least 5 years of service, upon following termination types:

- Dismissal (not due to misconduct/ redundancy)
- Fixed-term contract expiry without renewal
- Death
- Resignation due to ill health
- Retirement at age 65 or after

SP with no less than 24 months of service when the employee is dismissed due to redundancy

The offsetting arrangement allows employers to reduce the amount of SP/LSP by the benefits derived from the employer's contributions under:

- The MPF scheme: the mandatory and voluntary contribution by the employer
- The Occupational Retirement Schemes Ordinance (ORSO)
- Any contractual gratuity payable to an employee

After abolition of the offsetting arrangement

On 9 June 2022, the Legislative Council passed a bill to remove the offsetting arrangement by 2025 (transition date). This means that employers can no longer use the accrued benefits of employers' mandatory contributions under MPF or ORSO arrangements to reduce the SP/LSP payable to an employee. The following notes explain further.

No retrospective effect
Where an employee's employment commenced before the transition date, the employer can continue to use the MPF scheme, ORSO benefit and gratuity to reduce the SP/LSP earned before the transition date.

No change for voluntary contributions
Employers can continue to use voluntary contributions in the MPF/ORSO, and gratuity to reduce the SP/LSP earned at any time.

Definition of pre-transition LSP wage
The pre-transition SP/LSP will be calculated based on the monthly wages immediately preceding the transition date to reduce the risk of deliberate dismissals before the transition date.

Government subsidy
To reduce the financial impact on employers, the government has pledged HK$33.2 billion in a subsidy scheme over 25 years from the transition date.

Designated Savings Accounts (DSA)
The government will introduce a new bill to help employers set up savings accounts for their contingent SP/LSP obligations.

Implications for employers and employees

Employees will receive higher SP/LSP

SP/LSP arising from service after 2025 will no longer be offset by the employer mandatory contribution (ERMC) or by a certain portion under ORSO.

- **Special situations will be compensated**

Some employees may be made worse off by the new rules, because the pre-transition SP/LSP would be calculated based only on the monthly wages immediately preceding the transition date. However, the government has undertaken to make up for any shortfall. This may imply more complicated SP/LSP administration work by the employers.

Employers will likely have a higher long-term financial cost

The additional cost will be alleviated by the government subsidy over 25 years.

- **Complexity and operation effort** Computation involves pre- and post-transition data records, plus a 2-tier government subsidy structure. It will inevitably increase the operational efforts of employers and retirement scheme providers.
- **Employers that are more impacted** The effect on employers depends on demographics and their companies' special events. Employers with a large population of older workers, a high rate of involuntary terminations, and more contract workers will see bigger financial costs.

How Mercer can support you

Cost assessment
Forecasting and budgeting for cost increases in SP/LSP pre- and post-transition, and for cost management and strategy planning

Retirement benefit design reassessment
Feasibility study on revamping voluntary contribution scale against setting up the 1% DSA, for best efficiency in costs spent on employee benefits while fulfilling regulatory requirements

Education and tools
Support HR with training on the new calculations, data for record-keeping and cost assessments to facilitate handling of member enquiries and reduce operational risk

Update HR policy/member booklet
Ensure compliance with all regulatory changes

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