

All Relevant Topics on LSP Valuation click to learn more

 valtech-valuation.com/lsp-valuation-hkas19

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Long Service Payments (LSP) Actuarial Valuation under the New Legislations

Hong Kong Accounting Standard 19 (HKAS 19)

LSP Valuation Services by Valtech

Valtech provides Long Service Payment (LSP) valuation services in accordance with HKAS 19 and auditors' requirements. Our approach ensures consistency, transparency, and audit-readiness through comprehensive documentation of all valuation inputs, sources, and assumptions.

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- 1
Multinational corporation's (MNC's) Hong Kong office in publication sector
- 2
MNC's Hong Kong office in production sector
- 3
MNC's Hong Kong office in telecommunication sector
- 4
An international law firm's Hong Kong office
- 5
A company with approximately ten thousands of staff in Hong Kong
- 6
A famous medical group in Hong Kong
- 7
MNC's Hong Kong business in clothing and baby products

- 8
MNC's Hong Kong business in building product
- 9
The Hong Kong office of a MNC, with headquartered in USA
- 10
A MNC headquartered in Austria in electronics trading industry
- 11
A hotel group in Hong Kong
- 12
Non-governmental Organisations (NGOs) in Hong Kong
- 13
An organisation with both voluntary MPF and ORSO scheme (a complex case that requires consideration of complicated offsetting issues)
- 14
The list above is non-exhaustive.

Why is Valtech's services attractive to many employers?

The Whole Process and Valtech's Approach

Our process begins with a customised data collection template tailored to the client's organisation. Valtech coordinates the entire valuation process, addressing technical queries from auditors and client representatives to ensure alignment throughout. Our support continues until auditors confirm that no further clarification is required.

We also provide technical explanations on accounting implications under HKAS 19 and offer professional guidance to help management interpret and apply the results appropriately.

Our advanced model accommodates ORSO schemes, voluntary MPF contributions, severance payments, and gratuities — offering a flexible and accurate solution for both permanent and contract staff arrangements.

Long Service Payment Valuation Process Overview:

1. Formal appointment of Valtech as the valuation advisor
2. Valtech will provide of **a customised data collection template** fitting the situation of your organisation
3. Technical assistance during data completion by phone or email
4. Preparation of **valuation summary and report** with supporting documentation for audit review
5. Ongoing support for auditor inquiries until audit completion

Long Service Payment Valuation (LSP Valuation) after Abolition of MPF Offsetting Mechanism

The abolition of the MPF offsetting mechanism, effective **1 May 2025**, marks a significant shift for employers in Hong Kong. Companies and non-governmental organizations (NGOs) must now prepare for the new requirements in calculating **Long Service Payment (LSP)** obligations. This legislative change will impact both current-year expenses and long-term liabilities related to LSP.

At **Valtech Valuation**, we specialize in providing **reliable, accurate, and compliant long service payment valuation services (LSP valuation services)** tailored to the unique needs of businesses in Hong Kong. With a proven track record in LSP valuation, we ensure your organization is fully prepared for the upcoming changes.

Impact of MPF Offsetting Abolition on LSP Valuation

The abolition of the MPF offsetting mechanism introduces new complexities in LSP valuation for calculating LSP obligations. Employers must now account for:

- **Increased Liabilities:** The removal of MPF offsetting will lead to higher LSP liabilities for employers.
- **Past Service Costs:** These must be recorded in the year the Amendment Ordinance is enacted.
- **Future Obligations:** Employers need to project LSP liabilities accurately to ensure compliance and financial preparedness.

Valtech's LSP valuation services are designed to help businesses navigate these changes seamlessly. Our team of experts ensures that your calculations are not only compliant but also optimized for financial planning and reporting.

Get Prepared for 1 May 2025

The abolition of the MPF offsetting mechanism is a game-changer for employers in Hong Kong. Don't wait until the last minute to address your LSP obligations. Partner with Valtech Valuation to ensure a smooth transition and compliance with the new legislation.

If your company is a public company in Hong Kong, you will also need to get prepared for possible enquiry from the Stock Exchange of Hong Kong on LSP valuation disclosures. This is possible as the new law has significant impact on labour costs for those companies having large labour force in Hong Kong. It is expected that regulators in Hong Kong will closely monitor the quality the public companies' disclosures on the obligations from LSP.

Our Methodology: Projected Unit Credit Method

Valtech employs the **Projected Unit Credit Method**, a widely recognized actuarial technique, to calculate LSP obligations. This method ensures:

- Accurate projection of future liabilities.

- Incorporation of workforce demographics and turnover rates.
- Alignment with international accounting standards and local regulations.

Why Choose Valtech for LSP Valuation?

1. Specialized Expertise:

Valtech focuses exclusively on **LSP valuation** and related services, ensuring unparalleled accuracy and compliance. Unlike general valuation firms, our expertise is directly aligned with the complexities of LSP calculations under the new legislation.

2. Actuarial-Driven Approach:

Our LSP valuation model incorporates **actuarial assumptions** and the **Projected Unit Credit Method** to calculate LSP obligations, including the anticipated effects of the MPF offsetting abolition.

3. Comprehensive Support:

Beyond LSP valuation, we provide additional services such as:

- **Sensitivity testing** and **discount rate reviews** for accounting disclosures.
- **Severance Payment (SP)** and **Gratuity Payment** valuations.
- Assistance in recording **past service costs** in the year of enactment of the Amendment Ordinance.

4. Trusted by Leading Employers:

Valtech has been appointed by **multinational corporations** and prominent employers in Hong Kong to handle their LSP obligations. We are currently assisting clients with workforces of **several thousand employees**, ensuring detailed and accurate calculations that account for diverse workforce scenarios.

5. Certified Actuarial Models:

Our core actuarial valuation program is certified by a **qualified actuary (Fellow)**, ensuring the a high standard of accuracy and reliability. We continuously improve our models to stay ahead of regulatory changes and industry best practices.

Why are you encouraged to hire a valuation specialist to perform the calculation?

The calculation is not too complicated for one single employee. Following the practical example provided by HKICPA, you can calculate the result and project the impact for a single employee under simplified assumptions using a single worksheet of a spreadsheet program. However, when the number of employees increase from 1 to hundreds or even to thousands, the complexity will increase significantly. Programming technique will be required to handle massive data. On the other hand, according to HKAS 19, actuarial assumptions should be used. For example, staff turnover rate should be considered and turnover rate should be different for staff in different age groups. Combining the impact of actuarial assumptions and the large pool of employees, involvement of valuation specialist can support company in using a proper framework and perform a level review on the input data.

Can I Use Excel Spreadsheet to Calculate LSP?

The projected unit credit method is an actuarial valuation method that views each period of service as giving rise to an additional “unit” of LSP and measures each unit separately to build up the final obligation. In HKICPA’s guidance note, the example is based on a predefined year of service for a particular employee, that would give you a complete table of each unit that sum up to the total LSP. In practice, we have a lot of employees. Also an employee may leave before they retire and he/she may be dismissed such that LSP may be paid before his/her retirement. In our opinion, unless a company has only less than 10 employees, otherwise, calculating by excel is not a feasible solution. Programme will be required to calculate for a larger workforce.

Valtech have conducted telephone interview with over 20 employers in Hong Kong including public and private companies. We understand that some companies have been using simple excel template in estimating LSP obligation. Some excel template or simple estimation method make use of “time to retirement” concept by assuming that all existing employees will not resign or be dismissed until 65 years ago, then a discount or probability adjustment is applied to consider many employees would leave before retirement. Before enactment of the new legislation, the error caused by such simple estimation will be less material given the overall exposure is much less significant with MPF offsetting mechanism. Many simple excel template is not applying the projected unit credit method as suggested by the accounting standard. Some excel templates try to apply “prudence first” approach, which also cannot provide a fair or comprehensive estimate of SP and LSP.

Accounting and Financial Reporting Implications under HKAS 19

HKICPA issued comprehensive guidance for the accounting for the impact arising from the abolition of the Mandatory Provident Fund (MPF)-Long Service Payment (LSP) offsetting mechanism (the “Abolition”) on entities in Hong Kong.

<https://www.hkicpa.org.hk/-/media/HKICPA-Website/New-HKICPA/Standards-and-regulation/SSD/gMPFLSP.pdf>

It should be noted that the Government Subsidy does not yet meet the recognition criteria of any element of the financial statements based on an assessment of relevant facts and circumstances at the time of writing of the above publication.

Hong Kong Accounting Standard 19 (HKAS 19) requires businesses to compute and report their defined benefit obligations (DBO) and related expenses. Thus, Hong Kong companies need to have present value assessments on DBO. The most commonly adopted method in valuation of DBO is the projected unit credit method.

The projected unit credit method is a valuation method using actuarial assumptions that considers each period of service as generating an additional unit of benefit entitlement and measures each unit separately to build up the final obligation.

The main technical issue in determining the present value of DBO is to deal with the actuarial assumptions. We need to consider the following issues:

To estimate the present value of DBO, businesses normally need assistance by professional valuers or actuaries. The following parameters have to be considered during the valuation procedures:

- 1
The probability that employees live until the statutory retirement age
- 2
The probability that employees stay in position in retirement year
- 3
The impact brought by the new abolition of MPF offsetting arrangement

Under the new legislations, significant differences could be found in the calculations of MPF offsetting arrangement. Overall, the related obligations will increase. In the calculation process, the related issues rise from pre- and post-transition have to be solved.

The Hong Kong Government will put in place two supporting measures to assist businesses to adapt to the new policy. The first measure is a 25-year refined subsidy scheme. The Government will subsidize a certain proportion of the total amount of severance payments (SP) and LSP payable by employers under this scheme, in order to lower the burden of employers brought by rising obligations.

Valtech's valuation team includes Master of Finance, Master of Statistics and valuation experts with background in quantitative finance and financial engineering. In the context of LSP valuation, Valtech also works with qualified fellow actuary to improve model accuracy and prevent errors. In addition, Valtech's valuation services are ISO 9001 certified. If companies' auditors do not require an actuary to be responsible for the calculations, our valuation team are capable of providing opinion on DBO for financial reporting purposes. Our qualified actuary can provide advice in truly complicated project upon request.

Common Problems Identified in Many LSP Calculation Models

Valtech has conducted review of common models, Excel worksheets, and methodologies used for recording liabilities related to the abolition of the Mandatory Provident Fund (MPF) offsetting mechanism during our provision of advice on valuation or review opinion to auditors. We have identified several areas for improvement, applicable regardless of whether an external valuer is engaged. We strongly recommend companies and auditors to evaluate the impact and risk from the issues.

A prevalent issue is the oversimplified assumption that LSP is only payable upon an employee's retirement at age 65 (or the defined retirement age). This approach assumes a binary outcome—either LSP is paid upon retirement, or no payment is made if the employee

resigns before that age. In reality, employees are entitled to LSP not only at retirement but also in cases of dismissal or death, provided they have been with the company for five years or more.

Another key concern we observed is the potential underestimation of LSP liabilities, primarily due to the practice of applying a global turnover rate or age-specific turnover rates that fail to account for “loyalty.” Typically, more experienced employees exhibit greater loyalty, leading to lower turnover rates. Inaccurate estimations can arise when a generalized turnover rate is applied to employees over the age of 50, particularly when their accumulated LSP balance is significant. This could result in an overestimation of resignation probabilities for loyal, long-serving employees, which in turn could lead to a significant underestimation of LSP liabilities.

Tailored Solutions for Diverse Organizations | Experience Really Matters in LSP and SP Valuation

Drawing on extensive experience with public and private companies, multinational corporations (MNCs), and non-governmental organizations (NGOs), Valtech designs actuarial programs that cater to various employee benefit schemes (including MPF, ORSO, voluntary contributions, vested portions, gratuities, and withdrawals).

Many employers have voluntary contribution and some even have a vesting scheme for the voluntary contribution. Since voluntary contribution can still be used to offset LSP or SP, such contribution should be considered carefully in the actuarial model. Some companies may have experienced volatile turnover in the past few years, posing a challenge in LSP estimation. Experienced valuer and actuary will be able to provide a fairer estimate.