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Payroll Issues

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What are we looking at today?

1. **Marginal Rates – bonuses, back pays, termination**
2. **Allowances**
3. **Recovering Overpayments**
4. **Death of an Employee**
5. **Retirement**
6. **Superannuation Thresholds**
7. **Transitional and Non-Transitional ETPs**

Marginal Rates

Many calculations in payroll are done using what is known as a Marginal Rates calculation:

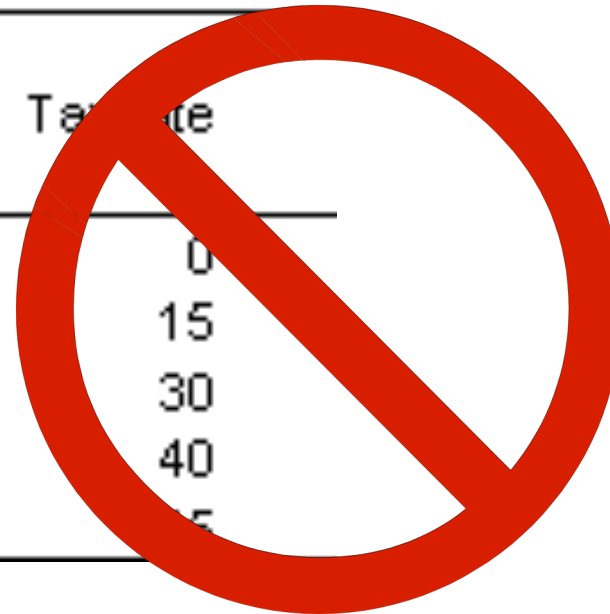
For example

- Bonus Payments
- Back Pays
- Leave paid on termination
- Leave being cashed in

Marginal Rates

A Marginal Rate tax calculation is not a flat percentage amount, therefore this table should not be used to calculate tax on termination payments

Newtax threshold from 1 July 2007	Tax rate
Income range (\$)	
0 - 6,000	0
6,001 - 30,000	15
30,001 - 75,000	30
75,001 - 150,000	40
150,001 +	45



Marginal Rates

Marginal Rates could be said to be a “notional” calculation – that is, how much extra tax would the person pay on top of their normal pay IF they received their normal pay every pay period for a full year and they got a portion of this lump sum each pay for a whole year instead of being paid once a year?

Marginal Rates – taxing an annual bonus or lump sums of leave on termination

1. using the relevant PAYG withholding tax table, work out the amount to withhold from the payee's normal gross earnings for a regular pay period.
2. divide the amount of the payment by the number of normal pay periods in 12 months (12 monthly payments, 26 fortnightly payments or 52 weekly payments).
3. disregard any cents.
4. Add the amount at step 3 to the normal gross earnings for a single pay period.
5. use the same PAYG withholding tax tables used at step 1 to work out the amount to withhold from the amount at step 4.
6. subtract the amount at step 1 from the amount at step 5.
7. multiply the amount obtained at step 6 by the number of normal pay periods in 12 months (12 monthly payments, 26 fortnightly payments or 52 weekly payments).

Marginal Rates

****Normal gross earnings**

Normal gross earnings include all payments, except those relating to termination payments, received in the last full period of employment (this includes taxable allowances, overtime, bonuses etc). Therefore, a payee's normal gross earnings is those earnings relating to the last full pay period worked.

Where a payee's pay fluctuates significantly over a number of pay periods, we will accept an average of gross taxable earnings for the financial year to date over the number of pays received.

NAT 3032-09.2006

Marginal Rates

Example:

Weekly paid Employee

Claiming Tax Free Threshold No Leave Loading

Normal Weekly Pay \$1200

Post 17/08/93 Annual Leave being paid on termination

\$7675.47

Using Steps from previous slide

1. \$1200 per week = \$275 tax
2. \$7675.47 divided by 52 weeks = \$147.61
3. \$147.00 (cents ignored)
4. \$1200 + \$147 = \$1347
5. \$1347 per week = \$321 tax
6. \$321 - \$275 = \$46
7. \$46 x 52 = \$2392 – this is the tax to withhold on the \$7675.47 on the leave.

Marginal Rates

What would have happened if we had used the “table” everyone thinks is the marginal rates table?

People usually do the following:

$$\$1200 \times 52 = \$62400$$

$$\$62400 + 7675.47 = \$70075.47$$

This puts them in the 31.5% bracket

$$\$7675.47 \times 31.5\% = \$2418 \text{ tax}$$

$$\$2418 - \$2392 = \$26 \text{ too much tax withheld}$$

This is pretty close – so let’s change the scenario a little and see what happens

Marginal Rates

Weekly paid Employee
Claiming Tax Free Threshold No Leave Loading
Normal Weekly Pay \$1200

Post 17/08/93 Annual Leave being paid on termination \$7200
Post 17/08/93 Long Service Leave \$9600

1. 1200 per week = \$275 tax
2. \$16800 divided by 52 weeks = \$323.08
3. \$323.00 (cents ignored)
4. \$1200 + \$323 = \$1523
5. \$1523 per week = \$385 tax
6. \$385 - \$275 = \$110
7. 110 x 52 = \$5720 – this is the tax to withhold on the \$16800 bonus.

Marginal Rates

What would have happened if we had used the “table” everyone thinks is the marginal rates table?

$$\$1200 \times 52 = \$62400$$

$$\$62400 + 16800 = \$79200$$

This puts them in the 41.5% bracket

$$\$16800 \times 41.5\% = \$6972 \text{ tax}$$

This is \$1252 too much tax!

Back Pays (lump sum payments in arrears)

Back pays need to be split into 3 categories

1. Type A – Salary and Wages or Other Payments relating to the current financial year
2. Type B – Salary and Wages relating to the previous financial year – but less than 12 months prior to the date of payment
3. Type C – Salary and Wages relating to previous financial years and older than 12 months prior to the date of payment OR Other Payments relating to a previous financial year

Back Pays (lump sum payments in arrears)

salary or wages (including salary or wages to a person after their reinstatement to duty following a period of suspension, and the amount during the period of suspension) – you split into Types A, B and C

other amounts such as allowances, compensation, sickness or accident pay relating to incapacity for work calculated at a weekly or other periodical rate, excluding payments under a person's own policy and payments to a company director – these you just split into Types A and C

Back Pays

Type A

For this payment all you need to do is rework the pays the person did receive with the amount they should have received work out the difference in tax and pay them the nett difference.



Back Pays

Type B

For this payment you need to tax the payment at marginal rates over the number of pays it relates to

The information in the ATO tax table on lump sum payments in arrears says to use the **CURRENT PAY** when calculating the marginal rate tax not the **NORMAL GROSS EARNINGS**

Back Pays

Type C

For this payment you need to tax the payment at marginal rates over the number of pays in a year

Use the **NORMAL GROSS EARNINGS** to work out the marginal rate tax

Back Pays

Example:

Lisa has been granted a raise of \$20 per week it goes back to the beginning of April 2007 and ending August 24, 2007.

She is paid weekly.

Pay periods end on Fridays.

She is paid the last day of the period.

Her back pay will be processed with the normal pay for period ending August 31, 2007.

Split the payment into Type A and B

Back Pays

Type A – work out the difference between what she was paid and what she should have been paid.

For each of the 7 pay periods this financial year she was paid \$680 per week gross tax was \$111 nett was \$569

Her pay should have been \$700 less tax \$118 equalling net \$582

She is owed \$140 gross less tax \$49 = \$91

Back Pays

Type B – divide the lump sum by the number of pays the payment relates to.
Calculate tax at marginal rates using
CURRENT PAY.

She is owed \$260 – it relates to 13 pays.

$$\$260/13 = \$20$$

Current pay \$700 per week

$$\$700 + \$20 = \$720$$

$$\text{Tax on } \$720 = \$124$$

$$\text{Tax on } \$700 = \$118$$

$$\text{Difference} = \$6.00$$

$$\$6.00 \times 13 = \$78$$

Back Pays

Both Type A and B payments will go in the gross income box of the payment summary



Back Pays

Now suppose Lisa was also owed a car allowance for January and February 2007 which we only just realised we hadn't paid – so it will be paid with the normal pay for period ending 01/09/07

She is owed \$250 per month – totalling \$500

As the payment is for an Allowance, this is a back pay for OTHER amounts and not Salary and Wages – we must use TYPE C to work out the tax. (Using the Normal pay to work out Marginal Rate Tax)

Back Pays

Normal Earnings \$700 – tax is \$118

$\$500 / 52 = \9.62 (ignore cents)

$\$700 + \$9 = \$709$ – tax is \$120

$\$120 - \$118 = \$2$

$\$2 \times 52 = \104

$\$500 - \$104 = \$396$

As Type C payment is more than \$400 it will go in Lump Sum E on the payment summary and the payment summary must include an explanation in relation to the payment. (If under \$400 would also go in Gross Income)

ALLOWANCES

A good rule of thumb is this – anything you pay your employees should be treated as taxable income unless the Commissioner for Taxation allows otherwise.




ALLOWANCES

Despite its name, a **living away from home allowance** is NOT an allowance, it is a fringe benefit.

It should not be shown on the payment summary (except perhaps as part of the reportable fringe benefits amount)


ALLOWANCES



If you make a **cents per kilometre** payment to cover work-related use of an employee's private car, for **PAYG** purposes you are **paying an allowance and not making a reimbursement** - it is made to cover a notional expense not an actual expense

(note that under the definition of ordinary earnings in Superannuation Guarantee Ruling 94/4 this payment is deemed to be a reimbursement and is not considered ordinary time earnings for the calculation of your superannuation payment obligations)

ALLOWANCES



ATO PAYG Bulletin No. 1 lists allowances by “type”, whether or not they are taxable and where they go on the payment summary

ALLOWANCES

ALLOWANCE TYPE	WITHHOLD PAYG?	SHOW ON PAYMENT SUMMARY?
Cents per kilometre car expense payments using Tax Office rates (1) <ul style="list-style-type: none"> For payments made up to 5000 business kilometres by applying the Tax Office rate to the number of kilometres travelled. For payments made in excess of 5000 business kilometres by applying the Tax Office rate to the number of kilometres travelled. 	<p>No</p> <p>Yes (from the payment for the excess over 5000 kms)</p>	<p>Yes (show total allowance separately in allowance box)</p> <p>Yes (show total allowance separately in allowance box)</p>

NON-ROTARY ENGINE	ROTARY ENGINE	RATE PER KM
Up to 1600 cc	Up to 800 cc	58 cents
1601 cc – 2600 cc	801 cc – 1300 cc	69 cents
Above 2601 cc	Above 1301 cc	70 cents

This table says “using Tax Office rates” – ATO have advised that amounts paid UP TO their rates can use this part of the schedule

ALLOWANCES

ALLOWANCE TYPE	WITHHOLD PAYG?	SHOW ON <i>PAYMENT SUMMARY</i> ?
<p>Award overtime meal allowances (4)</p> <ul style="list-style-type: none"> Up to reasonable allowances amount Over reasonable allowances amount <p>The allowance must be paid under an industrial instrument in connection with overtime worked</p>	<p>No</p> <p>Yes (from excess over reasonable allowances amount)</p>	<p>No</p> <p>Yes (show total allowance separately in allowance box)</p>
<p>Domestic or overseas travel allowance involving an overnight absence from payee's ordinary place of residence (4)</p> <ul style="list-style-type: none"> up to reasonable allowances amount over reasonable allowances amount <p>An allowance for overseas accommodation must be subject to PAYG and be shown in the allowance box on the <i>Payment Summary</i></p>	<p>No</p> <p>Yes (from excess over reasonable allowances amount)</p>	<p>No</p> <p>Yes (show total allowance separately in allowance box)</p>

ALLOWANCES

ALLOWANCE TYPE	WITHHOLD PAYG?	SHOW ON <i>PAYMENT SUMMARY</i> ?
Allowances paid for working conditions, qualifications, special duties For example: <ul style="list-style-type: none"> • crib, danger, dirt, height, site, shift, travelling time; • trade, first aid certificate, safety officer. 	Yes	Yes (include total allowance in gross payment)
Allowances for non deductible expenses For example: <ul style="list-style-type: none"> • part day travel (no overnight absence from payee's ordinary place of residence); • meals (not award overtime meal allowance or overnight travel allowance); • motor vehicle for non deductible travel, e.g. home to work, including cents per kilometre payments 	Yes	Yes (include total allowance in gross payment)
Allowances for expected deductible expenses For example: <ul style="list-style-type: none"> • tools; • compulsory uniform; dry cleaning; • motor vehicle for work related travel, including cents per kilometre payments in excess of Tax Office rate (1); • overseas accommodation for deductible travel 	Yes	Yes (show total allowance separately in the allowance box with an explanation)

Recovering Overpayments

When an amount is overpaid and it is recovered in the same financial year, you reverse the full payment in the payroll (as if it had never happened) – the employee repays you the NETT amount of the overpayment. You will recover the overpaid tax from the ATO by offsetting the reversing entry against other tax you are paying to the ATO.

Whether you can recover any overpaid superannuation may be up to the super fund trustee – but a recent ruling suggests you may be able to do this

Recovering Overpayments

However, when you recover an overpayment in a financial year other than the one it was paid in, you cannot do this. Instead you must recover the GROSS amount of the overpayment from the employee's nett salary. It cannot affect the taxable income of the new financial year. Once repaid you send a letter to the ATO advising that monies reported on the xx/yy payment summary have since been repaid and the new gross is now \$zz.* The employee will ask the ATO for an amended tax return and the ATO will give them any applicable tax refund.

Recovering Overpayments - Example

You wrote and advised Jane of an overpayment and asked her to repay it. Gross \$2000 less tax \$630 = \$1370

Jane has requested to repay it over 5 pays. She was overpaid in June, her letter did not come into the office until June 29th (after the payroll cut off date for that period) so the repayment will not start until the 1st pay in July.

Recovering Overpayments

Jane must repay the \$2000 GROSS amount of the overpayment from her NETT pay, not the \$1370

This is because the overpayment that occurred and was reported on the 06/07 payment summary cannot affect income that is earned and will be reported on the 07/08 payment summary.

In each of the 5 weekly pays in July and August, Jane earns \$1188 gross.

$\$1188.00 - \$271.00 = \text{Nett } \$917.00$ from this you will deduct \$400 and pay \$517 into her bank account.

Recovering Overpayments

After the \$2000 is recovered you will send a letter to the ATO (with a copy for Jane) saying that some of the gross income on the 06/07 payment summary has been repaid and the new gross amount is now \$zz.**

Jane will ask the ATO for an amended tax return - if she has already done it – or declare the revised gross on her tax return if she has not – and the ATO will give her any applicable tax refund (which will be based on her full income situation and not just the income she received from you)

Recovering Overpayments

One last thing to note

Where you allow the employee time to repay the overpayment (which is usually the case) you may be liable for fringe benefits tax as this will then be classed as a low interest loan fringe benefit.



Recovering Overpayments

**

For the 07/08 financial year onwards, instead of writing letters, we will be able to issue Amended Payment Summaries

Format O = original

Format A = amended

Death of an Employee

Avoid the impulse to immediately pay the entitlements in the ordinary manner (i.e. in to the deceased's bank account) as you may be deemed to be intermeddling with the Estate.

Shortly after the death, make written contact with the next of kin, advising them of the company's desire to pay the unpaid entitlements and requesting details of the executor or administrator.

It may also be necessary to seek the return of company property such as security keys, mobile phone, pager, etc



Death of an Employee

Once the executor or administrator's details are known, make written contact and again advise of the company's desire to pay the unpaid entitlements. It is prudent to request evidence of the executor's or administrator's authority.

Once authority is established, make the payment as directed and provide full details of the payment by way of a letter including any applicable paperwork.



Death of an Employee

Outstanding payments for ordinary wages salary and wages

No tax needs to be deducted from the employee's last pay, covering pay for the period up to the date of death, including back pays and bonus payments.

These payments do not get shown on a payment summary



Death of an Employee

Superannuation still needs to be paid – but if the super fund won't accept it (some won't after the employee has passed away), paying the trustee of the estate the equivalent amount is acceptable

SUPERANNUATION GUARANTEE (ADMINISTRATION) ACT 1992 PART 3 SECTION 23

23(9A) Contributions to estate of deceased employee.

If:

- (a) an employee has died; and
- (b) the employer would, if the employee had not died, have made a contribution to a complying superannuation fund or RSA for the benefit of the employee; and
- (c) the employer pays to the legal personal representative of the employee an amount equal to the amount of the contribution that would have been paid; the amount paid is taken for the purposes of this section to have been a contribution made by the employer to a complying superannuation fund or RSA for the benefit of the employee.

Death of an Employee

Payments for unused Annual and Long Service Leave.

Payments for unused annual and long service leave made after the death of an employee are not taxed.

They also do not show the payment on a payment summary.

Death of an Employee

NOTE

While these payments don't go on a payment summary and are not taxed, they should still be processed through payroll as in most States you will need to pick up these payments for Payroll Tax.

Death of an Employee

Other payments

Any ETP (e.g. outstanding RDOs, sick leave paid on termination etc) is taxed (or not taxed) according to who it goes to.

All ETP payments made after death go on an ETP payment summary

Death of an Employee

Dependant of the deceased

Payment	Tax rate
Amount which accrued before 1 July 1983	Tax-free
Amount up to \$140,000 which accrued after 1 July 1983	Tax-free
Amount over \$140,000 which accrued after 1 July 1983	46.5%

Death of an Employee

Non-Dependant of the deceased

Payment	Tax rate
Amount which accrued before 1 July 1983	Tax-free
Amount up to \$140,000 which accrued after 1 July 1983	31.5%
Amount over \$140,000 which accrued after 1 July 1983	46.5%

Death of an Employee

Trustee

These payments are not taxed by the employer, however, when the trustee eventually pays out the benefits from the estate, the trustee pays tax on the death benefit termination payment in the same way it would have been taxed if the payment was made directly to a dependant or non-dependant.



Retirement

The standard retirement age, defined on the basis of age pension eligibility, is currently 65 years for men and being phased in to age 65 for women. Early retirement is defined as retirement from the full-time labour force before the standard retirement age.

For tax purposes there is no difference between resignation and retirement except when the employer puts an “early retirement scheme” in place with the ATO.

When the employer has an “approved” “early retirement scheme”, then the payments under that scheme are treated for tax purposes in the same way as a bona fide redundancy

Superannuation

As a minimum superannuation should be paid quarterly

Deadlines are:

28 July, 28 October, 28 January and 28 April

However, if you have become a “contributing employer” to a fund, you may have to pay more regularly (usually monthly)

If an employee has AFTER TAX deductions to super, they have to be sent to the fund
MONTHLY

Superannuation

If you miss your quarterly deadline, you usually have to complete a Superannuation Guarantee Charge Statement and send the payment along with interest and admin fees to the ATO instead of to the fund



Superannuation

What income do you have to pay super on?

There are currently 3 “earnings bases” you could use:

1. Super Fund Trust Deed
2. Award Super Clause
3. ATO’s definition of Ordinary Time Earnings (SGR 94/4 and 94/4a lays out full details of what is considered to be OTE)

From 1 July 2008 you will all have to use option 3

Superannuation

What income do you have to pay super on when an employee is sacrificing to super?

1st thing to note is that a salary sacrifice to super is counted by the ATO to be an EMPLOYER contribution, not an employee one.



Superannuation

Q/ I have a bit confusion with salary sacrifice and super calculation.

Base salary \$100,000

Salary sacrifice 10% means taxable gross of 90,000

When we calculating the super which figure will have to consider as correct base according to the law) either

a/ $100,000 \times 9\% = 9000$ or

b/ $90,000 \times 9\% = 8100$?

Superannuation

Here's another option - perfectly acceptable under the legislation:

As an employer you must send 9% of Ordinary Time Earnings as super. Amounts subject to FBT are not superable, but salary sacrifice to superannuation is not a fringe benefit. This would mean that as a minimum you have to send \$9000 as an employer contribution to super.

BUT.... salary sacrifice to super is an employer contribution to super not an employee contribution. So technically you do not have to send anything more than the employee's \$10,000 sacrificed amount to super to meet your "minimum obligation". (i.e. as an employer you have to send \$9000, you've sent as an employer \$10,000, so you don't have to send anything else.)

Superannuation

However, this is not in the "spirit" of what an employee believes he will get from the employer - and most will be extremely unhappy if you follow this "legal" interpretation of the SGC legislation.

Most employers therefore choose to either send super on the full package (the \$9000) - because this is what they would have had to send if the employee didn't salary sacrifice - or they send super on the amount after sacrifice (the \$8100) - treating it the same way as other fringe benefits.

Because both will be more (when added to the sacrificed amount) than the minimum you have to send as an employer the ATO will be happy.

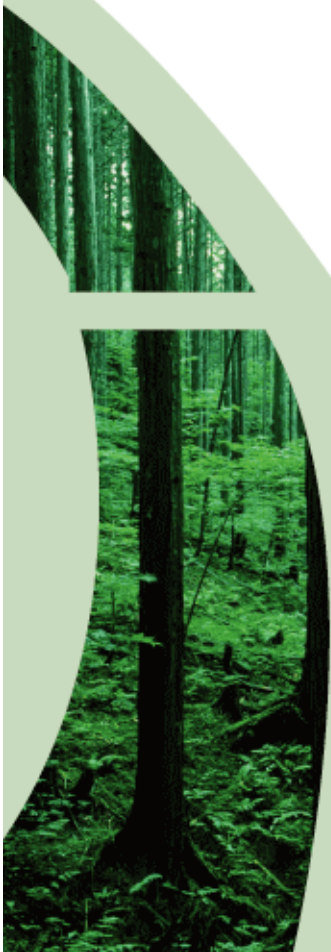
Superannuation

Q/ Can an employee salary sacrifice to their spouse's superannuation account?

It is possible for an employee to enter into an effective SSA where the employer makes a superannuation contribution in respect of someone other than the employee, e.g., spouse.

However, any such superannuation contribution will be a fringe benefit.

A much better option is to sacrifice into their own account and ask the SUPER FUND to split the contribution to the spouse



Superannuation

Q/ How much can an employee sacrifice into superannuation?

In theory most employees can sacrifice 100% of their pay to super. The ATO has no problem with this as long as it is done “effectively” (prior to the income being earned)

However from the 07/08 fin year onwards there are thresholds to the amount of **CONCESSIONAL CONTRIBUTIONS** (employer contributions) that can go into a person’s super fund/s before it attracts extra tax (which will be billed by the ATO straight to the employee)

Age at the end of the financial year of the contribution:

Under 50 \$50,000

50 and over \$100,000 (transitional to 30/6/2012)

Superannuation

Q/ Can an employee salary sacrifice unused leave being paid out on termination?

In theory yes, but most likely no.

Salary sacrifices must be done “effectively” – that is before the payment is earned, accrued or due. On termination, the leave is already accrued. This means it is too late to enter into a new agreement to sacrifice lump sums of unused leave on termination (even if the employee had a normal pay salary sacrifice in place).

To sacrifice lump sums of unused leave requires pre-planning

This also applies where employees are able to “cash in” leave while still employed



ETPs

ETPs are now split into two types of benefits:

Life Benefits and
Death Benefits

Life Benefits are also split into two types:

Transitional and
Non-Transitional

Transitional ETPs can be “directed” (rolled over)
until 30/6/2012

Non-Transitional ETPs cannot be rolled over

ETPs

Transitional arrangements may apply to payments made between 1 July 2007 and 30 June 2012 if your employee was entitled, as at 9 May 2006, to such a payment specified under:

- a written contract
- an Australian or foreign law (or an instrument under such a law), or
- a workplace agreement under the *Workplace Relations Act 1996*.

These documents must do this by referring to the amount of the payment or a method or formula to work it out.

ETPs

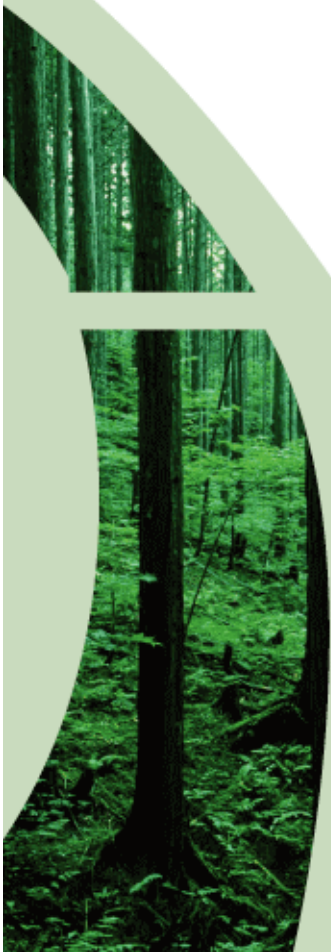
According to a recent ATO Interpretive Decision, (ATO ID 2007/163), if you enter into a new AWA with an employee on or after 10/05/2006 any ETP paid will be non-transitional even if the termination provisions are identical to the ones in the previous AWA.

TAPS has written to the ATO and to Peter Costello about this interpretation as it is the opposite to the advice we receive both on the ATO help line and from the Assistant Commissioner (and others) at our recent Breakfast Briefing Series on Super Simplification

ETPs

Is the following payment transitional or non-transitional?

On termination the Company will pay the employee the value of his/her unused sick leave entitlements.



ETPs

What about now?

On termination the Company will pay the employee sick leave according to the following scale:

Years of Service	No. of Weeks
Up to 4 years	1 week
4 years up to 8 years	2 weeks
8 years up to 12 years	3 weeks
12 years and over	4 weeks

ETPs

ETPs must be paid within 12 months of the termination of employment – with certain exceptions:

- The arrangement for a longer period of payment must have been in place prior to 10/05/2006
- The Commissioner of Taxation considers 12 months too short in the circumstances
- Must be rolled over by 30/06/2012
- Genuine Redundancy payments are exempt from the 12 month rule

ETPs

ETPs are now taxed according to their PRESERVATION AGE at the end of the income year in which the payment is made:

DATE OF BIRTH	AGE	Year of effect
Before 01/07/60	55	
01/07/60 – 30/06/61	56	2016
01/07/61 – 30/06/62	57	2018
01/07/62 – 30/06/63	58	2020
01/07/63 – 30/06/64	59	2022
After 30/06/64	60	2024

ETPs

ETPs are split into pre and post 01 July 1983 components.

For both transitional and non-transitional ETPs, the amount relating to the Pre 01 July '83 service will be tax-free (The Tax Free component)

Note: While Lump Sum D is tax-free, it is not an ETP payment and is not part of the tax-free component of an ETP – it gets reported on a “normal Payment Summary” and not an ETP Payment Summary

ETPs

Transitional ETPs – Taxable Component (post July '83)

1. Employees under the Preservation Age:
1st \$140,000 taxed at 31.5%
Next \$860,000 also taxed at 31.5%
Rest taxed at 46.5%
2. Employees at or over Preservation Age:
1st \$140,000 taxed at 16.5%
Next \$860,000 taxed at 31.5%
Rest taxed at 46.5%

ETPs

Non-Transitional ETPs – Taxable Component (post July '83)

1. Employees under the Preservation Age:
1st \$140,000 taxed at 31.5%
Rest taxed at 46.5%
2. Employees at or over Preservation Age:
1st \$140,000 taxed at 16.5%
Rest taxed at 46.5%

HINT

Understanding the concepts covered in this presentation will help you pass the C.P.S. exam!

Don't forget to collect your 100 C.P.S. points for today's breakfast.

Where to find this presentation:

<http://www.payroll.com.au/briefings/speaker.html>





QUESTIONS?