

LegCo Panel on Financial Affairs

Meeting to be held on 6 November 2000

Progress of the Implementation of the MPF System

Introduction

The Mandatory Provident Fund (MPF) System will be launched in Hong Kong on 1 December 2000 after years of meticulous preparation, to provide the workforce with additional retirement protection. The Mandatory Provident Fund Schemes Authority (MPFA) was set up under the Mandatory Provident Fund Schemes Ordinance (Chapter 485) (MPFSO). Responsible to the Management Board and advised by the statutory Mandatory Provident Fund Schemes Advisory Committee, the MPFA's main functions are to regulate MPF trustees and protect MPF scheme members' interests.

2. This paper gives a brief account of the implementation of the MPF System.

Coverage

3. Statistics from the Census and Statistics Department indicate that, as at mid 2000, the total population of Hong Kong was 6.72 million¹. There are around three million members in our workforce, of which about 830 000 are covered by different forms of retirement protection. Against such a new

¹ The population includes 321 300 employers, 2 881 300 employees and 307 300 self-employed persons.

estimate, the MPFA re-assessed the number of persons² that will be covered by the MPF System. The estimate shows that there are 251 000 employers, 2 014 200 relevant employees and 280 500 self-employed persons (SEPs) under the MPF System.

4. Except for the exempt persons stipulated in the MPF legislation, employees aged between 18 and 65 and SEPs aged below 65 are required to participate as members of MPF schemes. Also, in order to provide daily-waged casual employees in the construction and catering industries with retirement protection, the “Industry Schemes” have been set up in accordance with the law to facilitate the enrolment of such employees.

Preparation by the MPFA

5. The MPFA is pressing ahead in full steam in preparation for the commencement of the MPF System on 1 December 2000³. The Authority’s Information Management System is now in place to meet operational needs. In respect of human resources, the professional staff members under various divisions are now ready to take the regulatory and monitoring duties on board. A team of inspectors has been set up to carry out inspection, investigation and

² The estimate is based on the information obtained from the General Household Survey and the Central Register of Establishments. Relevant adjustments have been made to take account of the number of employers not covered by MPF (e.g. companies without employees) and MPF exempt employees (e.g. civil servants and teachers in subsidised schools covered by pension systems, domestic employees, employees who have attained the age of 64 or under the age of 18, and employees employed for a period of less than 60 days, etc.).

³ The following critical dates are relevant for the purpose of MPF implementation. They include:

- a) 1 December 2000, the commencement date of the MPF System, which is also the first contribution day for casual employees in Industry Schemes whose contribution day is the day on which the relevant income for the relevant contribution is paid to employees;
- b) 31 December 2000, the first calculation day of mandatory contribution by employees;
- c) 29 January 2001, last day of the permitted period for employers to ensure its employees become members of an MPF scheme; and
- d) 10 February 2001, for an employee who is remunerated on a calendar month basis, the last day for the first contribution.

enforcement functions. A structured training for the inspectors is well underway.

6. Four rounds of inspections have been conducted to ensure service providers' capability in handling mass applications. During the inspections, operation details of the service providers have been examined. The competency of the trustees in handling large number of registrations in the next few months, in respect of the areas such as manpower, training of staff and the adequacy of facilities, has also been fully assessed. During the initial stage of the implementation of the MPF System, the trustees may need to handle many enquiries, or even complaints. Therefore, the MPFA has scrutinized the trustees' contingency measures and complaint handling mechanisms. The MPFA is satisfied that all trustees are ready for the launch of the MPF System on 1 December as scheduled.

Compliance by Employers and Employees

7. As at 31 October 2000, about 95 000 employers and 66 000 SEPs have enrolled in MPF schemes. This represents about 38% and 24% of the total relevant population respectively. As the making of contributions has yet to start, it is not possible to ascertain the compliance rate of employees at this stage. It is roughly estimated that about one million employees may have enrolled, representing 50% of the total relevant population.

8. The above statistics may be on the low side. This is partly because some employers and employees are still taking a wait-and-see stance, waiting for better offers from service providers. Some SEPs may also worry

that once they enrol in an MPF scheme, their existing tax arrangement will be affected.

9. Nevertheless, the MPFA anticipates that the compliance rate will significantly improve in the coming month. Owing to extensive publicity efforts made by the MPFA and the service providers, the awareness of the MPF System by the community has been raised to a satisfactory level⁴. Since the end of October, the MPFA has been issuing letters to remind employers who have not yet signed up of the 1 December Launch Day and the penalties provisions in the law. It should be noted that failure to enrol could, if convicted, result in a fine of HK\$100,000 and imprisonment of six months. Employers who delay enrolment or contributions, if found, are liable to pay contribution surcharges and financial penalties, plus all contributions in arrears. Contributions by such employers will be backdated to the commencement day (i.e. 1 December 2000).

Industry Schemes - Compliance of Construction and Catering Industries

10. The MPFA has registered two MPF Industry Schemes. Daily-rated casual employees in the construction and catering industries may opt to join either industry scheme. However, the response has been poorer than expected. Statistics at the end of October 2000 show that only about 600 employers, 4 000 to 5 000 employees and about 440 SEPs have signed up. Such compliance rate is a cause for concern.

⁴ A sampling survey conducted by the MPFA shows that 98% of the local population aged between 18 and 65 is aware of the MPF System. The rate is higher than that in the February (92%) and the June (96%) surveys.

11. The MPFA faces quite a number of difficulties, such as structural problems, in the implementation of the Industry Schemes. Many people in the construction and catering industries have reservations about revealing their workplace and income to the authorities concerned. Some also worry that the enrolment will affect their tax arrangement. As a result, employers and employees may tend to delay or simply avoid joining the MPF schemes altogether.

12. The structure of the construction industry also creates difficulties for the implementation of the Industry Schemes. Numerous trades and the multi-layer structure of the sub-contracting system in the industry cause ambiguity in employer-employee relations. Workers recruited by middlemen or agents often have no knowledge about the identity of their own employers, not to mention the obligations under the MPF. This may lead to some people taking the risk of evading or delaying the enrolment. Since the establishment of the Industry Schemes in April, the MPFA has organized 48 seminars for the construction industry to explain to employers and employees about their obligations and rights. The MPFA has also submitted a detailed report to the Construction Industry Review Committee under the Works Bureau, pointing out that unless the structure of the construction industry undergoes a fundamental reform, the implementation of the MPF System will be obstructed. In addition, the Labour Department is drawing up a sample employment contract and an easy-to-fill wage record for both employers and employees in the construction industry to use as from 2001. This new measure should facilitate the operation of Industry Schemes.

13. Not fully realizing the convenience the Industry Schemes bring, some employers may choose to enrol their casual employees in Master Trust Schemes (MTSs) merely out of business considerations. Against such a background, the MPFA expects the compliance rate of the Industry Schemes to be low at the initial stage of the MPF implementation. Nevertheless, from the MPF angle, as long as daily-waged employees are enrolled in MTSs, they are provided with the retirement protection they deserve.

14. To encourage the compliance rate of Industry Schemes, the MPFA has used different channels to introduce such schemes to employees in the catering and construction industries. The MPFA has also been working closely with relevant unions and trade associations on direct publicity. The MPFA is considering a suitable enforcement plan to deal with deliberate non-compliance in the two industries.

Compliance of Small and Medium Enterprises (SMEs)

15. One of the major challenges in the implementation of the MPF System is to persuade employers of SMEs⁵ to perform their legal obligations with respect to the MPF System. Some employers and employees of SMEs are not familiar with the mode of operation of provident funds. They may tend to defer joining the MPF System, especially so when their profit margins are yet to see signs of improvement.

⁵ Small and medium enterprises are manufacturing companies with less than 100 employees or non-manufacturing companies with less than 50 workers. According to the Trade and Industry Department, there were over 290 000 SMEs in March 2000, representing 98% of the local business establishments, and employing over 1 380 000 workers. It should be noted that many of these SMEs only have 1 employee (i.e. the employer himself), whose status under the MPF System is an SEP.

Problems Faced by SMEs

16. Generally, we estimate that local enterprises may see a mild 0.7% increase in total operating cost after the implementation of MPF. The local economy is picking up at a steady pace and China is about to join the WTO. Hong Kong businessmen, with their adaptability to changes and ability of catching opportunities, should be able to absorb the mild impact of the MPF contributions on their operating costs.

17. It is difficult to ascertain the compliance rate of SMEs from information obtained from trustees at this stage. However, it can be assumed that the majority of employers who have signed up are SMEs as most of the local enterprises are SMEs. In practice, it is easier for SMEs with a smaller size of employees to choose trustees, to manage the administration of the fund as well as to communicate with their employees. The MPFA will continue to hold seminars and through direct communication to further promote MPF to the employers' associations and HR managers of SMEs. Apart from organizing MPF talks for individual employers' associations, the MPFA has set up an "MPF SME Resource Centre" in its office to provide SMEs' employers and SEPs with timely consultation services.

Protection of Employers and Employees' Benefits

18. Special arrangements are made to protect the interests of the employers and employees. First, keen market competition and high transparency have helped keeping the scheme fees at a reasonable level. Besides, the MPF legislation prohibits the refusal of membership by a trustee. This ensures every employer is able to join a scheme that suits his needs. The

legislation also provides for the setting up of a simple and efficient mechanism for the transfer of MPF accrued benefit to minimize the administrative expense.

19. Investment products under the MPF System are based on prudence. The MPF legislation prohibits the gearing of MPF investment funds and the speculation of funds in derivatives. Besides, investments must be well diversified, with certain restrictions on the investment in certain types of securities and bonds. All investment managers of MPF constituent funds are qualified professionals and are under the supervision of the Securities and Futures Commission.

20. To give scheme members a better picture of the effectiveness of their investment products, all trustees are required to issue on a regular basis investment reports and announce the price of their funds to scheme members. Employers will also help scheme members seek necessary information from the trustees.

21. As many employees may lack knowledge in investment products, the MPFA publishes some easy-to-understand booklets and an “Investment Guide for MPF Scheme Members” for the public. In October 2000, experts in the financial and investment sectors have been invited to give open seminars on investment in different districts. Other media will also be used to enhance the general public’s knowledge on investment products.

22. There are four layers of protection for scheme members’ assets. First, all MPF schemes must be established under trust. The scheme assets will

therefore be more secure. Second, the trustees, custodians and investment managers of all MPF schemes are subject to capital adequacy requirements. This ensures the financial soundness of the service providers. Third, MPF trustees are required to take out professional indemnity insurance to cover losses that MPF scheme assets might sustain from fraud or negligence on the part of the trustee or other service providers of the schemes. Fourth, the Compensation Fund is set up by law to compensate MPF scheme members for any loss in MPF benefits caused by misfeasance or illegal conduct committed by trustees and other service providers.

Conclusion

23. The MPF is a brand new system in Hong Kong. It may have to operate for some time before the desirable enrolment rate can be achieved. However, the MPFA is confident that the overall MPF enrolment rate will reach a reasonable level after the implementation of the System. The MPFA will closely monitor the situation and adjust its publicity and enforcement strategies accordingly.

Financial Services Bureau
Mandatory Provident Fund Schemes Authority

1 November 2000