

# **LegCo Panel on Financial Affairs Meeting to be held on 7 March 2001**

## **Amendments to the Mandatory Provident Fund Schemes Ordinance and the Mandatory Provident Fund Schemes (General) Regulation**

### **Introduction**

In the course of preparing for the implementation of the Mandatory Provident Fund (MPF) System, we have identified a number of areas in the MPF legislation which could be improved to facilitate the operation of the System, to better protect the interests of scheme members, or to enhance the effectiveness of the regulation of MPF schemes by the Mandatory Provident Fund Schemes Authority (MPFA). There are also some anomalies or ambiguities in the MPF legislation which need to be removed. We have also taken the opportunity to review the functions of the MPFA with a view to ensuring that it fulfils more effectively its statutory responsibilities for overseeing and monitoring the operation of the retirement protection systems in Hong Kong, including the retirement scheme industry. This paper sets out the main areas of, and reasons for, the proposed amendments to the MPF legislation.

### **Amendments to the Mandatory Provident Fund Schemes Ordinance (MPFSO)**

#### ***(A) Enhance Protection for Scheme Members***

##### *Conditions for approval of trustees*

2. Section 20(8) of the MPFSO provides that in approving an applicant as an approved trustee, MPFA may impose such conditions with respect to the conduct of the applicant's business as it considers appropriate. The section is silent on whether MPFA could amend existing conditions or add new ones upon the approved trustees. It is proposed that a new subsection should be added in section 20 to put it beyond doubt that, after giving notice to a trustee and providing the trustee with an opportunity to make representations, MPFA may impose further or additional conditions or amend existing conditions with respect to the conduct of the trustee's

business as it considers appropriate. An appeal mechanism against MPFA's decision would be provided.

*Conditions for scheme registration*

3. Sections 21 and 21A of the MPFSO specify that an application for the registration of a provident fund scheme as an employer sponsored scheme/master trust scheme and industry scheme may be made to the MPFA. However, they are silent on whether additional conditions could be imposed after the scheme has become registered. In view of the need to enhance members' protection, MPFA would need the flexibility to be able to impose and amend registration conditions. We now propose to empower MPFA to impose conditions in registering a scheme, and to impose further or additional conditions or amend the existing conditions, after giving notice to a trustee and providing the trustee with an opportunity to make representations. Again, an appeal mechanism would be provided.

*De-registration of scheme*

4. Section 34A of the MPFSO stipulates that except for the voluntary winding up of an employer sponsored scheme, a registered scheme can only be wound up by the Court. However, there may be a situation in which there is no scheme members nor scheme assets. In such a situation, it may not be necessary to wind up such a scheme by application to court. A simple de-registration would suffice. It is proposed that a new section should be added to provide MPFA with the power to de-register a registered scheme upon application from the relevant trustee, provided that the scheme has no scheme members and no scheme assets.

*Adequate reserves for guarantor of an approved pooled investment fund*

5. Section 46(1A)(r) of the MPFSO provides that regulation may be made for the purpose of requiring the approved trustee of registered schemes to maintain adequate reserves so as to provide investment guarantee. However, a majority of schemes would structure their investment arrangements by investing in approved pooled investment funds. For prudential regulatory purposes, it is considered necessary for guarantor of approved pooled investment funds to maintain adequate reserves to support the investment guarantee. We therefore propose that a new provision

should be added under section 46(1A) to provide for regulation making power to achieve such effect.

***(B) Definition of Terms***

6. Several terms used in the MPFSO have to be amended or added to clarify their respective meaning. Examples are set out below.

*Governing rules*

7. Trust deed and offering document are two major documents of an MPF scheme. Trust deed is the document governing the formation of a trust and is thus part of the governing rules. It is market practice that a trust deed would only set out a framework for the establishment of a scheme. The details of the scheme, including fees, investment options, etc., can only be found in the offering document. Separately, a participation agreement contains the terms and conditions agreed between a participating employer and the scheme trustee, including the rules in relation to voluntary contribution arrangement. It is proposed that the definition of “governing rules” in section 2 should be amended to cover offering document and participation agreement so that any change to those documents would constitute a change of governing rules and would need prior approval from MPFA under section 63 of the General Regulation. This would give MPFA greater control on changes of scheme features and terms which may have an adverse impact on scheme members’ interest.

*Master trust schemes and employer sponsored schemes*

8. The present definition of “master trust scheme” in section 2 of the MPFSO specifies the membership of a master trust scheme, which does not include a person who has minimum MPF benefits transferred from an occupational retirement scheme (ORSO scheme) to an MPF scheme as required under section 5(3) of Schedule 2 to the MPF Schemes (Exemption) Regulation (the Exemption Regulation). Besides, those employees of age 65 or above or below 18 whose employers wish to enrol them (and they agreed to be so enrolled) in an MPF scheme to make voluntary contributions are not included as well. It is proposed that the definition of “master trust scheme” in section 2 should be amended such that its membership will also be opened to such persons as mentioned above. Similar amendments to the

definition of “employed sponsored scheme” would also be made.

### *Relevant time*

9. Under section 7(3)(b)(ii) and section 7C(2)(b) of the MPFSO, the “relevant time” for an employee (or a self-employed person) who commences employment (or self-employment) after the commencement of those sections on 1 December 2000 is defined as *the date* on which the person becomes employed (or self-employed). Furthermore, under section 7(1) and 7C(2), an employee (or a self-employed person) must become a member of a registered scheme within the permitted period after the relevant time. Taken together, the permitted period for such persons will begin on the second day of employment (or self-employment). There is therefore a one day time lag which has caused unnecessary complication to scheme administration and this is not our policy intent. We propose to remove the ambiguity by specifying that the relevant time should be the beginning of the date on which the employment (or self-employment) begins.

### *(C) Powers of MPFA*

#### *Prosecution of Offences*

10. Under the MPFSO, the MPFA is responsible for ensuring compliance with the legislation. Sections 30A and 32 of the MPFSO give MPFA the general power of inspection and investigation relating to the contravention of the MPFSO. However, MPFA does not have the power of prosecution, and has to initiate such action through the Police and the Department of Justice.

11. Given that ensuring compliance with MPFSO is one of the essential functions of MPFA and that law enforcement forms an integral part of the MPF system to ensure compliance, we propose to add a new section to the MPFSO to empower MPFA to prosecute offences under the MPFSO in its own name. The proposed arrangement can streamline the existing prosecution process and speed up the handling of MPF-related cases, and tie in with MPFA's law enforcement effort against non-compliance with the MPFSO. The Securities and Futures Commission (SFC), as a regulator, also has this power and experience indicates that this arrangement works well.

*MPFA's power to borrow*

12. MPFSO does not provide MPFA with the power to borrow. For efficient financial management, borrowing is necessary to enable an organization to set up bank overdraft facilities to enhance cashflow management capabilities and to avoid setting aside excessive idle cash to make allowance for unexpected events. It is proposed that a new section be added in the MPFSO to provide that MPFA may, with the approval of the Financial Secretary, borrow money on such security or other conditions as it considers expedient. Other statutory bodies like the SFC are also conferred with such powers.

***(D) Other amendments***

13. We propose to amend section 6E of the MPFSO to better reflect MPFA's functions including the enforcement of the compliance of the MPFSO, the promotion of proper standards of conduct and sound and prudent business practices among trustees and service providers; the responsibilities to review the relevant legislation from the operational perspective; and promoting the professional standards and the overall development of the retirement industry in Hong Kong. We also propose to make other technical amendments to the MPFSO relating to the transfer of benefits from ORSO schemes; clarification that only self-employed persons of age 18 or above but below 65 are required to join MPF schemes; clarification that no mandatory contribution is required to be made in respect of relevant income earned by the employee during the first 30 days of employment after the implementation of MPF; adding an immunity provision to provide that no civil liability shall be incurred by the directors or any staff of MPFA as a result of anything done or omitted to be done by such persons bona fide in the exercise or purported exercise of any functions conferred or imposed by or under the MPFSO; amendment of the definition of "company" to include "corporation" as the present restricted definition has created difficulties for body corporates incorporated overseas and not registered under Part XI of the Companies Ordinance, and making consequential amendments to other sections of the MPFSO.

**Consequential and other technical amendments to the General Regulation**

### ***Approval of pooled investment funds***

14. To provide flexibility to MPFA for amending approval conditions of pooled investment funds in view of changes in operation and documentation and amendments to the MPF legislation and guidelines, we propose to amend the General Regulation to allow MPFA to impose further or additional conditions for an approved pooled investment fund. Where MPFA varies or imposes further or additional conditions, MPFA should give written notice to the trustee, investment manager or the insurer, where appropriate, of the approved pooled investment fund.

### ***Contribution surcharge***

15. Section 18(2) of the MPFSO provides that, subject to the General Regulation, a contribution surcharge up to 20% per annum on the arrears shall be imposed on the employer. Section 134 of the General Regulation sets out the mechanism of charging contribution surcharge, and the surcharge is only charged up to the end of the second payment period. To deter further delay by the defaulter in repaying the default contributions, it is proposed to empower MPFA to issue further notices to defaulter, specifying payment periods after the second payment period, and to charge contribution surcharge on any outstanding arrears at 20% per annum for the payment periods specified in notices issues by MPFA.

### ***Constituent funds***

16. At present, apart from the requirement of including a capital preservation fund, the MPF legislation does not specify the number of constituent funds within an MPF scheme. To ensure that each MPF scheme contains more than one investment option for scheme members, we propose that the General Regulation should be amended to require a registered scheme to contain more than one constituent fund. For the avoidance of doubt, we also propose to make it explicit that every constituent fund of an MPF scheme must be made available for scheme members to choose where to invest their accrued benefits.

### ***Delegate of custodian and subcustodial agreement***

17. Section 71 of the General Regulation imposes requirements on

delegate of custodian and section 72 prescribes the elements to be included in subcustodial agreements. However, the General Regulation is silent on the penalty for non-compliance. In respect of delegation of investment management function under section 45 and investment management contract under section 47 of the General Regulation, the approved trustee is required to ensure compliance with the provisions, and related penalty provisions are set out in section 67 for non-compliance. To provide parity treatment, it is proposed that sections 71 and 72 should be amended to impose obligations on the approved trustees to ensure compliance with the provisions, and to impose a penalty on non-compliance similar to section 67.

***Same day contribution for casual employee***

18. Section 122(1)(b) of the General Regulation defines the contribution day applicable to a casual employee to be either the day on which the relevant income for the relevant contribution period is paid to the casual employee, or the 10<sup>th</sup> day after the last day of the relevant contribution period. The approved trustee and the employer will agree on which of the two days to be the contribution day. The General Regulation provides that if employers are making contributions for their casual employees on the day when the relevant income is paid to the casual employees, such employers do not have to provide remittance statements to the approved trustees, and to prepare pay-record for each month in respect of each relevant employee. These exemptions from the requirement are to ease the administrative burden of employers.

19. It has now come to MPFA's attention that in practice, it may not be feasible for some employers to make contributions for casual employees on the same day when the relevant income is paid, for example, when the casual employees are paid very late at night or outside office hours.

20. To overcome the above operational difficulties, we now propose to give some flexibility to employers by amending the definition of the contribution day applicable to a casual employee to the effect that it would mean either the 10<sup>th</sup> day after the last day of the relevant contribution period, or the next working day immediately subsequent to the payment of the relevant income. This would mean that employers who make the contributions within the next working day after the payment of the relevant

income would also be eligible to enjoy the exemptions mentioned in paragraph 18 above.

***Exemption for persons entering Hong Kong for the purposes of employment***

21. The MPF legislation exempts a person who is being given permission to land or remain in Hong Kong for the purposes of employment for a period of 12 months or less under the conditions of stay imposed in accordance with section 11 of the Immigration Ordinance. The purpose is to exempt the people from outside Hong Kong who are employed under short term employment contracts.

22. It has come to MPFA's attention that, as a matter of departmental practice, the employment visa given by an Immigration Officer to a person from outside Hong Kong to enable him/her to land and remain in Hong Kong usually covers a period of 1 year plus 1 day, i.e. more than 12 months. To remove this discrepancy, we now propose that the reference to "12 months" in section 203(1)(b) of the General Regulation should be amended to "13 months".

**Legislative Timetable**

23. The draft for the proposed legislative amendments is being finalized. It is expected that the Amendment Bill will be introduced into the Legislative Council in the current session.

**Other Amendments**

24. MPFA is also considering other amendments to the MPF legislation to enable MPFA to properly regulate voluntary contributions and to deter late enrolment of employees by employers, and is consulting employer groups and industry organizations. Relevant proposals, if any, for amendment to the MPF legislation will be included in the Amendment Bill.