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**Paper for the House Committee meeting
on 25 January 2002
Report of the Bills Committee on
Mandatory Provident Fund Schemes (Amendment) Bill 2001**

Purpose

This paper reports on the deliberations of the Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2001 (the Bill).

Background

2. In the course of preparing for the implementation of the Mandatory Provident Fund (MPF) System, the Administration has identified provisions in the Mandatory Provident Fund Schemes Ordinance (Cap. 485) (the Ordinance) and the Mandatory Provident Fund Schemes (General) Regulation (the Regulation) which can be improved to better protect the interests of scheme members and enhance the effective operation of the System.

The Bill

3. The principal objects of the Bill are -
- (a) to introduce a number of technical amendments to the Ordinance to enhance protection for scheme members and effective operation of the System; and
 - (b) to confer on the Mandatory Provident Fund Schemes Authority (MPFA) certain functions and powers to facilitate its regulation of MPF schemes.

The Bills Committee

4. Members agreed at the House Committee meeting on 25 May 2001 to form a Bills Committee to study the Bill. Hon Ambrose LAU Hon-chuen was elected Chairman of the Bills Committee and the membership list of the Committee is at **Appendix I**.

5. The Bills Committee has held a total of five meetings, including one meeting with industry groups and professional bodies to receive their views. A list of organizations which have submitted views to the Bills Committee is at **Appendix II**.

Deliberations of the Bills Committee

6. In considering the Bill, members have deliberated at length on the scope of MPFA's regulatory powers, notably its powers to borrow money; to add or amend conditions on approved trustees, MPF schemes and approved pooled investment funds (APIFs); and to require the guarantor of an APIF to maintain adequate reserves so as to provide investment guarantees.

MPFA's power to borrow - Clause 4

7. Unlike other statutory bodies such as the Securities and Futures Commission (SFC) and the Hospital Authority, MPFA is currently not empowered to borrow under the Ordinance. However, the Administration has pointed out that MPFA may need to engage in borrowing activities such as overdraft, securities settlement (in case of unexpected settlement delay) and short term banking facilities for financing working capital. It therefore proposes to allow MPFA, with the prior approval of the Financial Secretary (FS), to borrow money on such security or other conditions as it considers expedient.

8. Members of the Bills Committee do not fully subscribe to the Administration's view. As MPFA has already received a capital grant of \$5 billion from the Government at its inception, members query the justification for empowering MPFA to borrow. They are concerned that the proposed section 6QA confers on MPFA very wide powers to borrow money. To safeguard against possible abuse, members have requested that MPFA's powers should be circumscribed by stipulating the temporary nature of and the limited circumstances under which such powers can be invoked (such as for providing bridging facilities).

9. With a view to addressing members' concerns, the Administration has proposed Committee Stage Amendments (CSAs) to amend clause 4 to the effect that MPFA may, with the prior approval of FS, borrow money temporarily for the purposes of (a) the settlement of securities transactions, (b)

acquiring an overdraft banking facility, (c) dealing with an emergency, or (d) dealing with other unforeseeable circumstances.

Proposed powers for MPFA to amend existing conditions or impose new ones on approved trustees, registered MPF schemes and APIFs - Clauses 9, 10, 11 and section 2 of Schedule to the Bill

10. At present, MPFA has the power to impose conditions upon registration of MPF schemes, and approval of trustees and APIFs. However, the legislation is silent on whether new or additional conditions can be imposed after approval/registration, and whether existing conditions can be amended. According to the Administration, the proposed provisions are to put beyond doubt that MPFA has the power to impose additional conditions or amend existing ones to cater for changes in technology, legislation and best market practice, thereby enhancing protection for scheme members.

11. Some members of the Bills Committee have queried the justification for conferring the proposed regulatory powers on MPFA at this point of time since the System has only been in operation for about a year. Major changes should not be introduced until more operational experience has been gained. A member representing the labour sector however agrees that it may be necessary to strengthen the regulatory powers of MPFA, given the total value of the MPF contributions and the need to protect scheme members' interest.

12. All the deputations which have submitted views to the Bills Committee object to empowering MPFA to impose additional conditions or amend existing ones on approved trustees and MPF schemes. Representatives of the industry are of the view that prospective service providers should have been fully informed as to what requirements will be applicable to them before they apply for approval because of the substantial investment involved. The proposed powers, if enacted, will create uncertainty in the market and give scope for the arbitrary imposition of different requirements on different service providers/schemes. The MPFA will also be in a position to prescribe/amend a wide range of requirements which have not been considered by the legislature or made known to market participants. Subsequent changes or addition of conditions after approval/registration will cause confusion and incur costs.

13. In this respect, the Bills Committee has examined whether the proposed powers for MPFA to add or amend conditions are newly created powers, or are existing powers already available to MPFA by virtue of relevant provisions in the Interpretation and General Clauses Ordinance (Cap.1). In the opinion of the legal adviser to the Bills Committee, MPFA's power under the existing Ordinance to impose conditions is only exercisable upon approving a trustee or registering a provident fund scheme. Any proposal to empower MPFA to impose new conditions after approval/registration will likely have the effect of widening the scope of MPFA's powers. As to whether the power to

amend existing conditions is already available to MPFA by virtue of section 46(a) of Cap. 1, the legal adviser considers that the power under the said section appears to be exercisable only in respect of the documents expressly mentioned therein. As approval of trustees/registration of MPF schemes are not included in section 46(a) of Cap. 1, it would appear that MPFA does not have a power under the existing Ordinance or by virtue of section 46(a) of Cap. 1 to amend existing conditions. An express provision in the legislation will be required to confer on MPFA such power.

14. On whether there is a practical need for imposing new conditions or amending existing ones, the Administration confirms that to better protect scheme members' interest, MPFA has found it necessary to impose new conditions on matters such as business consolidation of trustees, requiring the trustee to appoint a third party scheme administrator in accordance with a specified timetable etc. With the passage of time, some of the existing conditions may become outdated and require amendments. Members are informed that similar powers to impose and amend conditions after the granting of approval/licences are also available under the Banking Ordinance and the Securities Ordinance.

15. To address the Bills Committee's concerns, the Administration has proposed a CSA to provide for a definition of "conditions" to mean "reasonable conditions" so as to ensure that new conditions added/existing conditions amended must be reasonable ones. Regarding MPFA's power to impose/amend conditions in respect of the "marketing" of MPF schemes which members consider may be too arbitrary, the Administration has accepted the Bills Committee's suggestion and will introduce CSAs to the effect that such power will be limited to the ambit of the guidelines issued by MPFA after consultation with the industry.

16. Members consider that although it may be necessary for MPFA to have the power to amend existing conditions or impose new ones on approved trustees, registered schemes and APIFs, they are keen to ensure that MPFA will exercise such powers in a reasonable way. In this connection, the Administration has further advised that MPFA's decisions are subject to judicial review. The Bill, if enacted, will also enable any party aggrieved by MPFA's decision to add/amend conditions to lodge an appeal with the MPF Schemes Appeal Board. To allow more time for trustees to make the necessary adjustments resulting from new/amended conditions as decided by MPFA, the Administration has agreed to introduce a CSA to extend the time-frame for MPFA to notify the approved trustee of its decision in advance from 7 working days to 30 calendar days.

Regulations requiring the guarantor of an APIF to maintain adequate reserves - Clause 18

17. The Administration has proposed to amend section 46(1A) of the Ordinance to empower the Chief Executive in Council to make regulations requiring the guarantor of an APIF to maintain adequate reserves so as to provide the guaranteed investment returns to MPF scheme members.

18. The Bills Committee notes the industry's objection to the proposed amendments. As participation in the guaranteed fund option within a MPF scheme is voluntary, the industry considers that this investment option should be subject to the same regulatory standards applicable to guaranteed funds in the market. The industry groups are gravely concerned that there may be inconsistency in the standards adopted by various regulators (namely, MPFA, the Hong Kong Monetary Authority (HKMA), the Insurance Authority (IA) and SFC) on the reserve requirements. The Bills Committee agrees with the need to protect scheme members' interest but has also urged the Administration to work closely with the regulators and the industry to safeguard against any inconsistency in regulatory standards.

19. In response, the Administration highlights the need to protect MPF scheme members' accrued benefits. It has advised that the proposed amendments will merely enable existing guidelines issued by MPFA on the reserve requirements on guaranteed funds (whether at the constituent fund level or the APIF level) to be prescribed into regulation, if necessary. Any regulation made under the proposed provisions is subsidiary legislation and subject to approval by the Legislative Council.

20. Regarding concerns about uniformity in regulatory standards, the Administration has assured the Bills Committee that MPFA will continue to work together with HKMA, IA and SFC to ensure consistency in regulating MPF guaranteed funds taking into account the differences in product design and regulatory regimes. The Secretary for Financial Services (SFS) will also address this point during the resumption of the Second Reading debate of the Bill.

Eligibility of delegate of custodian and subcustodial agreement - Sections 6 and 7 of Schedule to the Bill

21. The proposed provisions seek to require the approved trustee to ensure that the custodian's functions will not be delegated to a non-eligible person. Non-compliance of the requirement by the trustee without reasonable excuse is an offence liable on conviction to a fine of \$ 50,000 (level 5). The industry disagrees that penalty provisions should be introduced and suggests that it would be more appropriate to require the custodian concerned to indemnify the scheme against all losses arising from its use of subcustodians who are non-eligible persons.

22. In response, the Administration maintains its policy intent that trustees are the key party responsible for administering a MPF scheme in compliance with the MPF legislation. Given the important bearing of custodians and subcustodians on the security of scheme assets, it is necessary for approved trustees to ensure that such persons are eligible to act as custodians/subcustodians. The MPFA needs certain sanctioning measures as under existing legislation, the only way for MPFA to enforce the relevant requirements is to revoke the approval granted to the trustee. This should be used as a last resort as it may disrupt the smooth operation of a MPF scheme and may not be in the interest of scheme members.

Definition of governing rules", "offering document" and "participation agreement" - Clause 2(a)(iv) and (x)

23. There are three major documents relating to a MPF scheme. The trust deed governs the establishment of the scheme; the offering document sets out details such as benefit payment, benefit transfer and investment options etc; and the participation agreement contains the terms and conditions agreed between a participating employer and the scheme trustee. The Administration has proposed to amend the existing definition of "governing rules" to include, inter alia, those rules and provisions contained in the offering document and participation agreement so as to enable MPFA to forestall any changes to terms which may adversely affect scheme members' interests.

24. As trustees have to act in accordance with the "governing rules" of a scheme, the scope of the proposed definition is of concern. The industry and the Law Society of Hong Kong have submitted to the Bills Committee that the proposed definition is unduly wide and may even include documents such as software agreements. As participation agreements relate primarily to vesting and voluntary contributions which may vary between employers, the industry considers it inappropriate for MPFA to approve amendments thereto.

25. In response, the Administration has advised that its intention is to ensure consistency between the provisions in the offering documents/participation agreements and those in the trust instrument which in turn must comply with the provisions of the Ordinance. Having considered the concerns of the industry and the Bills Committee, the Administration will propose CSAs to reinstate the existing definition of "governing rules" and add a new definition for "offering document" and "participation document" in the Regulation. The Administration has confirmed to the Bills Committee that the industry is agreeable to the proposed changes.

26. At present, the SFC is responsible for approving offering documents. Some members share the industry's concern that requiring the same documents to be approved by MPFA may result in a duplication of function between MPFA and SFC. In response, the Administration has confirmed that MPFA will work closely with SFC to ensure that dual monitoring will not arise.

SFS will reflect this point in his speech during the resumption of the Second Reading debate of the Bill.

Other concerns

27. In the course of deliberation, some members have raised a number of MPF-related issues which are outside the scope of the Bill but are of widespread concern. These include measures to deal with default in making MPF contributions, payment of accrued benefits, the retirement age of self-employed persons and the feasibility of consolidating an employee's separate accounts resulting from changes in employment. While members may pursue these policy issues through other channels, they have also noted that a MPF Schemes Operation Review Committee set up under the MPFA is reviewing the implementation of the System and will recommend improvements, where necessary.

Committee Stage Amendments

28. The Administration has proposed a number of CSAs to address the concerns raised by members. Some technical amendments and textual improvements have also been proposed. The full set of CSAs to be moved by the Administration is in **Appendix III**. The Bills Committee has not proposed any CSAs.

Recommendation

29. The Bills Committee notes the Administration's intention to resume the Second Reading debate on the Bill on 6 February 2002.

Advice sought

30. Members are invited to note the recommendation of the Bills Committee in paragraph 29 above.

Legislative Council Secretariat

23 January 2002

**Bills Committee on
Mandatory Provident Fund Schemes (Amendment) Bill 2001**

Membership list

Chairman Hon Ambrose LAU Hon-chuen, GBS, JP

Members Hon James TIEN Pei-chun, GBS, JP
Hon NG Leung-sing, JP
Dr Hon David CHU Yu-lin, JP
Hon LEE Cheuk-yan
Hon Eric LI Ka-cheung, JP
Hon Margaret NG
Hon CHAN Yuen-han, JP
Hon Bernard CHAN
Hon CHAN Kam-lam
Hon SIN Chung-kai
Hon Andrew CHENG Kar-foo
Hon TAM Yiu-chung, GBS, JP
Hon Abraham SHEK Lai-him, JP
Hon Tommy CHEUNG Yu-yan, JP
Hon LEUNG Fu-wah, MH, JP
Hon Audrey EU Yuet-mee, SC, JP

(Total: 17 members)

Clerk Miss Polly YEUNG

Legal Adviser Miss Connie FUNG

Date 11 July 2001

**Bills Committee on
Mandatory Provident Fund Schemes (Amendment) Bill 2001**

List of organizations which have submitted views to the Bills Committee

1. Law Society of Hong Kong
2. Hong Kong Retirement Schemes Association
3. Retirement Schemes Industry Group (representing Hong Kong Trustees' Association Ltd., Hong Kong Investment Funds Association and the Hong Kong Federation of Insurers)

Written submissions only

4. The Hong Kong Association of Banks
5. The Deposit Taking Companies Association

GFOX:DMA#44411v8
1st draft: 26.6.2001
2nd draft: 3.12.2001
3rd draft: 5.12.2001
4th draft: 7.12.2001
5th draft: 10.12.2001
6th draft: 11.12.2001
7th draft: 19.12.2001
8th draft: 11.1.2002
9th draft: 14.1.2002

MANDATORY PROVIDENT FUND SCHEMES (AMENDMENT) BILL 2001

COMMITTEE STAGE

Amendments to be moved by the Secretary for
Financial Services

<u>Clause</u>	<u>Amendment Proposed</u>
2(a)	<p>(a) In subparagraph (ii), in the proposed definition of "company", in paragraph (b)(i), by deleting "oversea company", "</p> <p>(b) By deleting subparagraph (iv).</p> <p>(c) In subparagraph (v), in the proposed definition of "mandatory contribution" -</p> <p>(i) in paragraph (a), by deleting "paid or payable" and substituting "required to be paid";</p> <p>(ii) in paragraph (b), by deleting "section 5(1)(b)" and substituting "section 5(1)".</p> <p>(d) By deleting subparagraph (vii).</p>

(e) In subparagraph (x) -

(i) by adding -

““conditions” () means
reasonable conditions;”;

(ii) by deleting the definitions of “offering
document” and “participation agreement”.

2(b) By deleting the proposed section 2(3) and (4) and
substituting -

“(3) For the avoidance of doubt, it is hereby
declared that an amount that is paid as a contribution
to a registered scheme contingently on the basis that
the amount will later constitute a mandatory
contribution to the scheme shall for all purposes be
treated as a mandatory contribution to the scheme (and
the provisions of this Ordinance shall apply
accordingly) unless and until it is certain that the
amount will not constitute a mandatory contribution
to the scheme.”.

New By adding -

“2A. Exemptions

Section 4(3) is amended by adding “and section 11(1)
and (2)” after “subsections (4) and (5)”.

4

By deleting the proposed section 6QA and substituting -

"6QA. Authority may borrow money

The Authority may, with the approval of the Financial Secretary, borrow money temporarily, on such security or other conditions as it considers expedient, for the purposes of -

- (a) the settlement of transactions in securities;
- (b) acquiring an overdraft banking facility;
- (c) dealing with an emergency; or
- (d) dealing with any other circumstances which could not have been foreseen."

7(a)

By deleting "subject to" and substituting "in accordance with"

8

(a) In paragraph (a) -

- (i) in the proposed section 11(1), by adding "or is exempted under section 4(3)" after -
 - (A) "retirement age"; and
 - (B) "that age";
- (ii) in the proposed section 11(2), by adding "or is exempted under section 4(3)" after "retirement age".

- (b) In paragraph (b), in the proposed section 11(7)(b), by deleting "section 5(1)(b)" and substituting "section 5(1)".

9

In the proposed section 20(12) -

- (a) in paragraph (b)(i), by deleting "7 working" and substituting "30";
- (b) by deleting everything after "then the" and substituting -

"Authority may by written notice served on the approved trustee -

- (c) amend any conditions imposed under subsection (8) or this subsection with respect to the conduct of the approved trustee's business; or

- (d) impose conditions with respect to the conduct of the approved trustee's business."

10(d)

(a) In the proposed section 21(12) -

- (i) in paragraph (b)(i), by deleting "7 working" and substituting "30";
- (ii) by deleting everything after "then the" and substituting -

"Authority may by written notice served
on the approved trustee -

(c) amend any conditions
imposed under
subsection (8A) or
this subsection with
respect to the
administration or
marketing of the
scheme; or

(d) impose conditions with
respect to the
administration or
marketing of the
scheme."

(b) By adding after the proposed section 21(13) -

"(14) The Authority shall not impose under this
section any conditions with respect to the
marketing of a registered scheme, or amend any
conditions imposed under this section with
respect to the marketing of the scheme, unless
the imposition or amendment, as the case may be,
falls within the ambit of the guidelines."

11(d)

(a) In the proposed section 21A(12) -

(i) in paragraph (b)(i), by deleting "7 working"
and substituting "30";

(ii) by deleting everything after "then the" and substituting -

"Authority may by written notice served on the approved trustee -

(c) amend any conditions imposed under subsection (8A) or this subsection with respect to the administration or marketing of the scheme; or

(d) impose conditions with respect to the administration or marketing of the scheme."

(b) By adding after the proposed section 21A(13) -

"(14) The Authority shall not impose under this section any conditions with respect to the marketing of a registered scheme, or amend any conditions imposed under this section with respect to the marketing of the scheme, unless the imposition or amendment, as the case may be, falls within the ambit of the guidelines."

By deleting the clause.

Schedule

(a) In section 1(d), by adding -

“offering document” (), in relation to
a registered scheme, means a document -

(a) inviting participation in the
scheme by prospective
participating employers or
prospective members of the scheme;
and

(b) containing information relating
to the establishment or
administration of the scheme;”;

“participation agreement” (), in
relation to a registered scheme, means an
agreement -

(a) between a participating employer
and the approved trustee of the
scheme for the employer and his
employees to participate in the
scheme;

(b) between a self-employed person
and the approved trustee of the
scheme for the self-employed
person to participate in the
scheme;

(c) between a person intending to maintain a preserved account in the scheme and the approved trustee of the scheme;".

(b) In section 2(b), in the proposed section 6(3)(b)(i), by deleting "7 working" and substituting "30".

(c) In section 5(b), by deleting the proposed section 63(2A) and substituting -

"(2A) In respect of an amendment proposed to be made or made to the governing rules in respect of or by a participation agreement of a registered scheme -

(a) subject to paragraph (b), subsections (1) and (2) shall not apply unless the amendment relates to mandatory contributions or voluntary contribution;

(b) subsections (1) and (2) shall not apply if the amendment is in a form approved by the Authority for the purposes of this section."

(d) By adding -

"5A. Section added

The following is added -

"63A. Amendments to offering

**documents require
Authority's approval**

(1) An approved trustee of a registered scheme must notify the Authority in writing of any amendment proposed to be made to the offering document of the scheme and lodge with the Authority a copy of the proposed amendment.

(2) Any amendment to the offering document of the scheme should not be made available to scheme members, prospective scheme members, participating employers or prospective participating employers until the Authority has given written notice to the trustee that the Authority has approved it.

(3) In this section, a reference to an amendment to the offering document of a registered scheme includes a reference to addition of new provisions, or substitution or omission of existing provisions, of the document."."

(e) In section 8 -

(i) in paragraph (a), in the proposed section 78(6)(a)(iii), (b)(iii), (c)(ii), (d)(ii), (e)(ii) and (f)(ii), by deleting "section 5(1)(b)" and substituting "section 5(1)";

(ii) in paragraph (b), in the proposed section 78(7)(b)(ii) and (d)(ii), by deleting "section 5(1)(b)" and substituting "section 5(1)";

(iii) in paragraph (c) -

(A) in the proposed section 78(8)(a)(ii) and (b)(ii), by deleting "section 5(1)(b)" and substituting "section 5(1)";

(B) by deleting the full stop and substituting a semicolon;

(iv) by adding -

"(d) by adding -

"(10) For the avoidance of doubt, it is hereby declared that this section does not operate to require the trustee to divide a member's sub-account into any further sub-accounts."

(f) By deleting section 17 and substituting -

"17. Circumstances in which persons are exempted from operation of the Ordinance

Section 203(1)(b) and (2) are amended by repealing "12" wherever it appears and substituting "13"."

(g) In section 18, by adding before paragraph (a) -

"(aa) by adding after item 23 -

"23A. 63A Amendments 10,000 20,000 50,000".".

to offering

documents

require

Authority's

approval