

**Legislative Council Panel on Manpower
(Meeting on 21 March 2002)**

**Proposal to Address the Financial Problem of
The Protection of Wages on Insolvency Fund**

Purpose

This paper informs Members of a proposal to increase the Business Registration Certificate (BRC) levy from \$250 to \$600 per annum to address the financial problem of the Protection of Wages on Insolvency Fund (the Fund)

Background

Income of the Fund

2. The Fund is mainly financed by a levy at the rate of \$250 per annum on each BRC issued under the Business Registration Ordinance, Cap 310. Other sources of income include money recovered from remaining assets of insolvent employers through subrogation and returns from investment and deposits. In 2000-01, of the total income of the Fund, 75% came from levy income, 14% from subrogation income and 11% from interest/investment income.

Expenditure of the Fund

3. Claims payment accounts for the largest share of the Fund's expenditure. In the last three financial years, about 96% of the Fund's expenditure were spent on claims payment while the remaining 4% was on other expenses.

Previous adjustment of BRC levy

4. After the Fund's establishment in 1985, the BRC levy has only been increased once from \$100 to \$250 in July 1991. The 1991 levy increase was to enable the Fund to meet the anticipated increase in claims payment arising from an upward revision of the payment limit for ex-gratia severance payment from \$4,000 to \$8,000 plus 50% of excess entitlement in the same year. Since then, while the Fund's coverage has improved, there was no corresponding increase in the BRC levy as a high level of reserve has been built up over the years.

Financial Position of the Fund

Upsurge in claims payment

5. However, following the Asian financial crisis in late 1997, there has been a sharp increase in claims payment, as shown in Table A.

Table A: Claims payment during 1996-97 to 2000-01

	1996-97	1997-98	1998-99	1999-00	2000-01
Claims payment	\$180.8M	\$272.4M	\$424.2M	\$456.3M	\$349.8M

6. The amount of claims payment has increased dramatically from \$180.8 million in 1996-97 to a peak level of \$456.3 million in 1999-00, i.e. an increase of 152%. In 2000-01, although claims payment has registered a drop to \$349.8 million, it was still 93% higher than that of 1996-97.

Continued depletion of the Fund since 1997-98

7. Given the upsurge in claims payment with no corresponding increase in the Fund's income, the Fund has been operating on annual deficits since 1997-98. The Fund's reserve has dropped from \$877.7 million as at end of March 1997 to \$226.8 million as at end of January 2002.

8. The changes in the financial position of the Fund is shown in Table B below:

Table B: Financial Position of the Fund

	96-97 (\$m)	97-98 (\$m)	98-99 (\$m)	99-00 (\$m)	00-01 (\$m)	Apr 2001– Jan 2002 (\$m)
Income	241.4	261.8	254.3	268.6	236.1	172.6
Expenditure	194.0	286.5	439.6	473.2	366.2	278.8
Surplus/(Deficit)	47.4	(24.7)	(185.3)	(204.6)	(130.1)	(106.2)
Reserve (Accumulated Fund)	877.7	853.0	667.7	463.1	333.0	226.8

Recent trends

9. The number of applications received by the Fund has been on the rise in the first ten months of 2001-02. During the period, 15,163 applications were recorded, representing an increase of 35% over the same period in 2000-01.

10. As indicated in the financial projection at Appendices I and II, the Fund would register a deficit of \$127 million for 2001-02 and its reserve would drop to \$206 million by the end of March 2002. As the applications received still maintains at a high level, it is estimated that claims payment for 2002-03 would reach a high

level of \$500 million.

Justifications for a Levy Increase

11. Over the years, the Fund has played an important role in maintaining harmonious labour relations and social stability. It is therefore imperative that the Fund must have sufficient reserve to provide prompt financial relief to employees of insolvency cases. To meet the needs of claims payment and to enable the Fund's reserve to return gradually to a reasonably healthy level of \$200 million, we propose to increase the BRC levy rate to \$600 per annum. The benchmark of \$200 million is adopted, as the Fund has registered a record deficit of \$204.6 million in 1999-00.

12. As indicated in Appendix III, with a levy rate of \$600, small surpluses around the level of \$24 million to \$25 million per year could be achieved for the Fund in the coming years. The reserve of the Fund could be built up gradually and reach a healthier level at \$200 million in 2006, i.e. four years after the increase takes effect.

13. It is worth reiterating that since the Fund's establishment in 1985, the BRC levy has only been increased once in 1991. The additional costs on employer, at \$350 a year amount to less than \$1 a day per establishment.

Public Consultation

14. Under section 4(1) of the Protection of Wages on Insolvency Ordinance, the Protection of Wages on Insolvency Fund Board (Fund Board) is entrusted with the function to make recommendations to the Chief Executive with respect to the BRC levy rate. At its meeting on 22 February 2002, Members of the Fund Board unanimously agreed that the BRC levy should be increased to \$600 per annum with effect from May 2002.

15. The Labour Advisory Board was also consulted on 27 February 2002. The proposed increase was endorsed by the majority of the LAB members with the condition that a review of the new levy rate be conducted one year later.

Implementation Plan

16. The BRC levy rate as set out in Schedule 2 of the Business Registration Ordinance has to be amended by order published in the Gazette. The Administration plans to gazette the Order in early April 2002 for the new levy rate to take effect from May 2002 following the negative vetting period.

Education and Manpower Bureau
March 2002

Protection of Wages on Insolvency Fund
Analysis of Income and Expenditure

	Actual <u>1996-97</u> \$M	Actual <u>1997-98</u> \$M	Actual <u>1998-99</u> \$M	Actual <u>1999-00</u> \$M	Actual <u>2000-01</u> \$M	Actual Apr 2001 - Jan 2002 \$M	Revised Estimate 2001-02 \$M
INCOME							
Levy on Business Registration Certificates	177.6	181.2	172.8	174.2	176.9	145.4	171.6
Subrogation Income	10.9	14.0	17.6	57.7	32.7	18.5	22.0
Interest and Investment	52.9	66.6	63.9	36.7	26.5	8.7	9.3
	<u>241.4</u>	<u>261.8</u>	<u>254.3</u>	<u>268.6</u>	<u>236.1</u>	<u>172.6</u>	<u>202.9</u>
EXPENDITURE							
Payment of Claims	180.8	272.4	424.2	456.3	349.8	264.7	312.6
Supervision Fee	12.6	13.3	14.6	15.4	15.5	13.5	16.2
Miscellaneous	0.6	0.8	0.8	1.5	0.9	0.6	1.1
	<u>194.0</u>	<u>286.5</u>	<u>439.6</u>	<u>473.2</u>	<u>366.2</u>	<u>278.8</u>	<u>329.9</u>
Excess/(Deficit) of Income over Expenditure	<u>47.4</u>	<u>(24.7)</u>	<u>(185.3)</u>	<u>(204.6)</u>	<u>(130.1)</u>	<u>(106.2)</u>	<u>(127.0)</u>
Total Accumulated Fund as at end of Financial Year	<u>877.7</u>	<u>853.0</u>	<u>667.7</u>	<u>463.1</u>	<u>333.0</u>	<u>226.8</u> (as at 31.1.2002)	<u>206.0</u> (as at 31.3.2002)

**Protection of Wages on Insolvency Fund
Cashflow Projection**

Levy rate remains at	\$250	per annum
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Cash flow			Year 1	Year 2	Year 3	Year 4	Year 5
Levy Rate	\$250	\$250	\$250	\$250	\$250	\$250	\$250
		Revised					
	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
Year Starting from 1 April	<u>2000-01</u>	<u>2001-02</u>	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>
	\$M	\$M	\$M	\$M	\$M	\$M	\$M
<u>Cash Inflow</u>							
Levy on BRC	177.000	171.600	172.500	172.500	172.500	172.500	172.500
Subrogation Income	33.000	22.000	24.000	24.000	24.000	24.000	24.000
Other Income	26.000	9.280	1.100	(4.200)	(8.700)	(13.300)	(18.100)
Total Income	236.000	202.880	197.600	192.300	187.800	183.200	178.400
<u>Cash Outflow</u>							
Total Expenditure	366.000	329.880	500.000	417.000	417.000	417.000	417.000
Net Cash Inflow / (Outflow) from Operation	(130.000)	(127.000)	(302.400)	(224.700)	(229.200)	(233.800)	(238.600)
Cash Available at end of financial year		206.000	(96.400)	(321.100)	(550.300)	(784.100)	(1,022.700)

**Protection of Wages on Insolvency Fund
Cashflow Projection**

Levy rate at \$600 per annum with effect from May 2002
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Cash flow			Year 1	Year 2	Year 3	Year 4	Year 5
Levy Rate		\$250	\$250	\$600	\$600	\$600	\$600
			Revised				
		Actual	Estimate	Estimate	Estimate	Estimate	Estimate
Year Starting from 1 April		<u>2000-01</u>	<u>2001-02</u>	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>
		\$M	\$M	\$M	\$M	\$M	\$M
<u>Cash Inflow</u>							
Levy on BRC		177.000	171.600	393.875	414.000	414.000	414.000
Subrogation Income		33.000	22.000	24.000	24.000	24.000	24.000
Other Income		26.000	9.280	3.300	2.800	3.300	4.300
Total Income		<u>236.000</u>	<u>202.880</u>	<u>421.175</u>	<u>440.800</u>	<u>441.300</u>	<u>441.800</u>
<u>Cash Outflow</u>							
Total Expenditure		366.000	329.880	500.000	417.000	417.000	417.000
Net Cash Inflow / (Outflow) from Operation		(130.000)	(127.000)	(78.825)	23.800	24.300	25.300
Cash Available at end of financial year			<u>206.000</u>	<u>127.175</u>	<u>150.975</u>	<u>175.275</u>	<u>200.075</u>
			<u>225.375</u>				