

Panel on Financial Affairs

Special meeting to be held on 1 February 2007

Follow-up questions on Meeting of 5 January 2007

“Review of the Minimum and Maximum Relevant Income Levels for Mandatory Provident Fund Contributions”

The following information sets out our response to issues raised by the Panel on Financial Affairs on the above subject at its meeting held on 5 January 2007 –

1. *To enable Members to have a better picture on the retirement protection provided by Mandatory Provident Fund (MPF), the Mandatory Provident Fund Schemes Authority (MPFA) is requested to provide various modellings on the accrued benefits to employees upon retirement based on the real MPF investment return rates over the past few years.*

Response

The MPFA has provided for Members’ reference the following modellings:

- (a) Scenario 1 - Employee works continuously for 20 years from 2007

Projected accrued benefits available to employees upon retirement under different monthly income:

Monthly Relevant Income (RI) of Employee	Accrued Benefits upon retirement if Min RI = \$5,000 Max RI = \$20,000 (a)	Accrued Benefits upon retirement if Min RI = \$5,000 Max RI = \$30,000 (b)	Accrued Benefits upon retirement if Min RI = \$6,000 Max RI = \$20,000 (c)	Accrued Benefits upon retirement if Min RI = \$6,000 Max RI = \$30,000 (d)
HK\$4,000	HK\$206,000	HK\$206,000	HK\$206,000	HK\$206,000
HK\$5,000	HK\$442,000	HK\$442,000	HK\$312,000	HK\$312,000
HK\$6,000	HK\$531,000	HK\$531,000	HK\$531,000	HK\$531,000
HK\$10,000	HK\$885,000	HK\$885,000	HK\$885,000	HK\$885,000
HK\$20,000	HK\$1,769,000	HK\$1,769,000	HK\$1,769,000	HK\$1,769,000
HK\$25,000	HK\$1,769,000	HK\$2,031,000	HK\$1,769,000	HK\$2,031,000
≥ HK\$30,000	HK\$1,769,000	HK\$2,293,000	HK\$1,769,000	HK\$2,293,000

(b) Scenario 2 - Employee works continuously for 30 years from 2007

Projected accrued benefits available to employees upon retirement under different monthly income:

Monthly Relevant Income (RI) of Employee	Accrued Benefits upon retirement if Min RI = \$5,000 Max RI = \$20,000 (a)	Accrued Benefits upon retirement if Min RI = \$5,000 Max RI = \$30,000 (b)	Accrued Benefits upon retirement if Min RI = \$6,000 Max RI = \$20,000 (c)	Accrued Benefits upon retirement if Min RI = \$6,000 Max RI = \$30,000 (d)
HK\$4,000	HK\$447,000	HK\$447,000	HK\$447,000	HK\$447,000
HK\$5,000	HK\$975,000	HK\$975,000	HK\$669,000	HK\$669,000
HK\$6,000	HK\$1,170,000	HK\$1,170,000	HK\$1,170,000	HK\$1,170,000
HK\$10,000	HK\$1,950,000	HK\$1,950,000	HK\$1,950,000	HK\$1,950,000
HK\$20,000	HK\$3,900,000	HK\$3,900,000	HK\$3,900,000	HK\$3,900,000
HK\$25,000	HK\$3,900,000	HK\$4,513,000	HK\$3,900,000	HK\$4,513,000
≥ HK\$30,000	HK\$3,900,000	HK\$5,125,000	HK\$3,900,000	HK\$5,125,000

(c) Scenario 3 - Employee works continuously for 40 years from 2007

Projected accrued benefits available to employees upon retirement under different monthly income:

Monthly Relevant Income (RI) of Employee	Accrued Benefits upon retirement if Min RI = \$5,000 Max RI = \$20,000 (a)	Accrued Benefits upon retirement if Min RI = \$5,000 Max RI = \$30,000 (b)	Accrued Benefits upon retirement if Min RI = \$6,000 Max RI = \$20,000 (c)	Accrued Benefits upon retirement if Min RI = \$6,000 Max RI = \$30,000 (d)
HK\$4,000	HK\$933,000	HK\$933,000	HK\$933,000	HK\$933,000
HK\$5,000	HK\$2,045,000	HK\$2,045,000	HK\$1,386,000	HK\$1,386,000
HK\$6,000	HK\$2,454,000	HK\$2,454,000	HK\$2,454,000	HK\$2,454,000
HK\$10,000	HK\$4,089,000	HK\$4,089,000	HK\$4,089,000	HK\$4,089,000
HK\$20,000	HK\$8,178,000	HK\$8,178,000	HK\$8,178,000	HK\$8,178,000
HK\$25,000	HK\$8,178,000	HK\$9,495,000	HK\$8,178,000	HK\$9,495,000
≥ HK\$30,000	HK\$8,178,000	HK\$10,811,000	HK\$8,178,000	HK\$10,811,000

Assumptions used for the purpose of these models

- (1) Annualised MPF investment return = 6.99% (the annualised rate of return of the MPF System over the five years to 31 March 2006).
- (2) The employee does not have any early withdrawal of MPF accrued benefits, including any offsetting of severance payment or long service payment.
- (3) The minimum and maximum relevant income levels will remain the same for the following years.
- (4) The employee has accumulated MPF accrued benefits for 6 years as at 31 December 2006 and has achieved investment returns of 6.99% and the employee is earning the same monthly income during the past 6 years.
- (5) Effect of inflation not modelled, hence all figures are expressed in today's dollar term. Salary increment rate assumed to be identical to inflation rate.

2. ***Some Members express concern about the problem of working poverty faced by many low income earners and doubt whether the MPF System can provide sufficient protection to lower income workers upon their retirement. In this connection, some Members consider that the Administration should actively explore other retirement protection schemes (such as the Old Pension Scheme or Central Provident Fund) to supplement the MPF System.***

Response

The Central Policy Unit is conducting a study on "Sustainability of the Three Pillars of Retirement Protection in Hong Kong" ("the Study"), which assesses the sustainability of the three pillars of retirement protection in the next 30 years. The Study is expected to be completed in 2007. The Administration will consider and draw reference to the findings of the Study.

3. ***Some Members point out that employees earning a monthly income below \$6,000 can barely make ends meet and may have difficulties in making MPF contributions. In this connection, MPFA/the Administration is requested to re-consider whether the minimum level of relevant income should be set at 50% of the monthly median employment earnings; and whether it should be raised to say, 60% of the monthly median employment earnings.***

Response

In accordance with the requirement of section 10A(1) of the Mandatory Provident Fund Schemes Ordinance (“MPFSO”), the MPFA has conducted a review of the minimum relevant income according to the statutory methodology. The mechanism of using 50% of the monthly income median was proposed in the Report of the Consultancy on the Mandatory Provident Funds System in 1995 and has been adopted since that time. This mechanism was also endorsed by the Legislative Council in 2002 after thorough deliberation and prescribed in section 10A(2) of the MPFSO.

The Administration has noted the proposal of the MPFA that the minimum relevant income level be kept at the current level of \$5,000. We note from the information provided by the MPFA that if 60% of median income methodology is used as the minimum relevant income level, it is estimated that about 129,000 employees would be excluded from the MPF contribution net and the amount of accrued benefits available for their retirement would also be reduced substantially (please see response to Q1 above).

In considering the proposal, the Administration would take into account the views of LegCo Members and the public, including employers’ and employees’ representatives, as well as other relevant factors.

4. ***Given that the tax concessions are granted for MPF contributions made by employees and employers, there will be an impact on the tax revenue of the Government if the maximum level of relevant income is to be adjusted. In this connection, MPFA / the Administration is requested to provide information on the possible impact on tax revenue if the maximum level of relevant income is increased from \$20,000 to \$30,000.***

Response

If the maximum level of relevant income is to be increased from \$20,000 to \$30,000 and a corresponding amendment is to be made to the Inland Revenue Ordinance in respect of tax deductions for MPF contributions, self-employed persons and employers under Profits Tax and employees under Salaries Tax could claim a higher amount of deduction. It is estimated that Profits Tax and Salaries Tax revenue would decrease by \$300 million and \$250 million respectively.

5. *Members note that employees with monthly earnings of more than \$20,000 may be making other investments on top of their mandatory MPF contributions in preparation for retirement. To enable Members to consider the need for increasing the maximum level of relevant income from \$20,000 to \$30,000, MPFA/the Administration is requested to provide information, where practicable, on the investment behaviour of employees in the income bands between \$20,000 and \$30,000 per month and those who have monthly earnings in excess of \$30,000 per month.*

Response

The MPFA has looked at some research studies conducted by financial institutions on retirement planning, which however do not contain any specific information on the investment behaviour of employees in the income bands between \$20,000 and \$30,000 per month and those who have monthly earnings in excess of \$30,000 per month. Statistics relating to the investment behaviour of employees are also not available from surveys conducted by the Census and Statistics Department.

The Hong Kong Exchanges and Clearing Limited (“HKEx”) and the Securities and Futures Commission (“SFC”) conducted two separate retail investor surveys in 2005 which may perhaps help shed light on the characteristics of retail participation in the investment market in Hong Kong, although these surveys did not give income distribution information on the survey respondents. They might not be strictly comparable because of the differences in survey design, concepts and definitions.

According to the SFC survey¹, 36.8% of Hong Kong people aged 18 and above traded investment products². The most popular investments are Hong Kong stocks (28.3%), followed by managed funds (excluding MPF investments). Retail participation in different investment products in 2005 are as follows:

¹ The SFC survey was conducted from September to November 2005.

² They were retail investors who had traded one or more investment products (including Hong Kong, Mainland or foreign stocks, managed funds and derivatives) in the past 24 months.

Table 1: Retail Participation in Different Investment Products

<u>Investment products</u>	<u>Retail participation* (%)</u>
(1) Stocks traded on the Stock Exchange of Hong Kong	28.3
(2) Managed funds (excluding MPF investments)	18.1
(3) Plain vanilla bonds	4.9
(4) Warrants traded on the Stock Exchange of Hong Kong	4.7
(5) Stocks traded in Mainland or other foreign markets	4.1
(6) Structured products (e.g. equity/credit linked notes)	2.8
(7) Other derivatives traded on the Stock Exchange of Hong Kong or the Hong Kong Futures Exchange (e.g. futures, options)	1.5
(8) Leveraged foreign exchange contracts (excluding foreign currency deposits)	1.2
<i>Any of the above</i>	<i>36.8</i>
<p><i>Note: * Since respondents might have traded more than one investment product, the sum of all investment products is greater than the overall participation rate (36.8%).</i></p> <p><i>(Base: all respondents)</i></p>	

Table extracted from Retail Investor Survey Report 2005 conducted by the Securities and Futures Commission.

According to the HKEx survey³, a typical Hong Kong retail stock investor⁴ was a 42-year-old white-collar worker, with upper secondary or above education, a monthly personal income of about \$18,750 and a monthly household income of about \$35,000. Detailed profiles of different investors⁵ are given in the table below:

³ The HKEx survey was conducted in December 2005.

⁴ Stock investors were defined as those who were holding Hong Kong stocks or had traded Hong Kong stocks in the past 12 months.

⁵ Please see (4) for the definition of stock investors. Definitions of the other types of investors were as follows: (a) stock traders were those who had traded Hong Kong stocks in the past 12 months; (b) derivatives investors were those who were holding derivatives (futures and options traded on HKEx) or had traded derivatives in the past 12 months; and (c) non-investors were those who were neither stocks investors nor derivatives investors.

Table 5. Profile of different investor types (2005)					
(%)	Adult population	Stock investors	Stock traders	Derivatives investors	Non-investors
Sex					
Male	47.2	55.1	56.4	63.1	44.0
Female	52.8	45.0	43.6	36.9	56.0
Age					
18 – 19	3.1	0.3	0.4	1.5	4.2
20 – 29	16.5	10.9	11.6	18.8	18.8
30 – 39	21.0	25.7	25.7	27.3	19.1
40 – 49	24.2	31.5	32.0	35.2	21.3
50 – 59	16.2	20.6	19.6	10.6	14.4
60 or over	19.0	11.1	10.8	6.7	22.1
<i>Median</i>	<i>42</i>	<i>42</i>	<i>42</i>	<i>42</i>	<i>42</i>
Education level					
No schooling / kindergarten	7.5	1.2	0.8	0.0	10.1
Primary	13.9	7.0	6.5	4.8	16.6
Lower secondary	15.9	13.7	12.2	9.0	16.7
Upper secondary	29.4	29.4	29.3	18.7	29.5
Matriculation	6.7	7.5	8.1	11.4	6.3
Tertiary or above	26.1	40.7	42.6	56.1	20.2
Refusals	0.6	0.5	0.6	0.0	0.6
Occupation					
Managers / administrators / professionals	12.4	23.7	24.6	35.7	7.8
White collar	20.6	30.1	32.1	27.3	16.9
Blue collar	17.9	15.0	13.9	15.7	19.0
Homemakers	17.2	12.0	10.5	8.5	19.4
Retirees	17.4	11.4	11.3	8.1	19.7
Students	5.1	0.6	0.7	0.0	6.9
Unemployed persons	6.3	3.5	3.5	0.0	7.4
Others	0.0	0.0	0.0	0.0	0.0
Refusals	3.2	3.7	3.4	4.7	2.9
Median monthly personal income (HK\$)*	13,750	18,750	18,750	22,500	11,250
Median monthly household income (HK\$)	18,750	35,000	35,000	45,000	16,250
* Among those who were engaged in full-time or part-time employment. Note: Numbers may not add up to 100% due to rounding.					

Table extracted from Retail Investor Survey Report 2005 conducted by the Hong Kong Exchanges and Clearing Limited.

Financial Services and the Treasury Bureau/
Mandatory Provident Fund Schemes Authority

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