

LEGISLATIVE COUNCIL BRIEF

MANDATORY PROVIDENT FUND SCHEMES ORDINANCE
(CHAPTER 485)

**MANDATORY PROVIDENT FUND
SCHEMES ORDINANCE
(AMENDMENT OF SCHEDULE 2) NOTICE 2011
AND
MANDATORY PROVIDENT FUND
SCHEMES ORDINANCE
(AMENDMENT OF SCHEDULE 3) NOTICE 2011**

INTRODUCTION

At the meeting of the Executive Council on 14 June 2011, the Council ADVISED and the Chief Executive ORDERED that, under section 48 of the Mandatory Provident Fund Schemes Ordinance (“MPFSO”), the Mandatory Provident Fund Schemes Ordinance (Amendment of Schedule 2) Notice 2011, at Annex A, and the Mandatory Provident Fund Schemes Ordinance (Amendment of Schedule 3) Notice 2011, at Annex B, (collectively referred to as “the Amendment Notices”), should be made, subject to the approval of the Legislative Council (“LegCo”).

JUSTIFICATIONS

Rationale of prescribing a Minimum Relevant Income Level (“Min RI”) and a Maximum Relevant Income Level (“Max RI”)

2. The purpose of setting a Min RI for Mandatory Provident Fund (“MPF”) mandatory contributions is to lessen the financial burden of MPF contributions on lower-paid employees and self-employed persons (“SEPs”). As for the prescription of a Max RI, it reflects the policy objective of encouraging the workforce to save for basic retirement needs. Higher

income employees and SEPs may decide whether to top up their retirement savings through voluntary contributions or other investment.

Statutory Considerations and Review Findings of the Mandatory Provident Fund Schemes Authority (“MPFA”)

3. Section 10A of the MPFSO requires MPFA to conduct a review on Min RI and Max RI at least once in every four years. The latest review was conducted in 2010. Section 10A¹ further requires MPFA to take into account the following statutory factors (but without limiting the factors which MPFA may take into account) in conducting the review –

- (a) for Min RI, 50% of the monthly median employment earnings prevailing at the time of the review as compiled from the General Household Survey (“GHS”) conducted by the Census and Statistics Department (“C&SD”); and
- (b) for Max RI, the monthly employment earnings at 90th percentile of the monthly employment earnings distribution prevailing at the time of the review as compiled from the GHS conducted by C&SD.

MPFA’s review findings based on the above statutory factors and statistical data for Q3 2010 are that consideration should be given to increasing Min RI from \$5,000 to \$5,500 per month, and Max RI from \$20,000 to \$30,000 per month. MPFA also drew reference to the Statutory Minimum Wage (“SMW”), among other relevant factors, in its review findings for the consideration of the Government.

4. After consultation with LegCo Panel on Financial Affairs (“FA Panel”) on the review findings on 21 February 2011, MPFA recommended in March 2011, among others, that the Government consult stakeholders on a Min RI above \$5,500, taking into account the potential impact of the implementation of the SMW; and the increase in Max RI should be implemented in two phases, i.e. from \$20,000 to \$25,000 for phase one, and then from \$25,000 to \$30,000 for phase two, with the timing for phase two dependent on a comprehensive review of the statutory adjustment mechanism in section 10A of the MPFSO (para. 5 below).

¹ The statutory factors were introduced in 2002 with a view to providing a more consistent and transparent basis for future adjustment of Min RI and Max RI.

The Recommended Levels

Min RI

5. SMW represents a wage floor to forestall excessively low wages without unduly jeopardizing the flexibility of the labour market, economic growth and competitiveness of Hong Kong or causing significant adverse impact on the employment opportunities for the vulnerable workers. Notwithstanding that SMW is expressed as an hourly rate while Min RI is attached to a monthly earnings concept, there are overwhelming views in the community that Min RI should take into account or even be linked to SMW. The main concerns include –

- (a) the existing statutory factor for the adjustment of Min RI (para. 3(a) above) takes into account historical income data in 2010 and cannot reflect the expected substantive change in wages after the implementation of SMW on 1 May 2011; and
- (b) those who are to receive SMW will be amongst the lowest income group who should be spared the burden of saving for retirement.

As the implementation of the SMW regime will have direct impact on the earnings of the low income group and possible rippling effect on the earnings of the rest of the workforce, MPFA plans to conduct a comprehensive review of the statutory adjustment mechanism prescribed in section 10A of the MPFSO when the actual impact of SMW on wages is available. Pending the review outcome, we have made reference to the hourly SMW rate and the median monthly working hours in determining Min RI. Assuming a 26-working day per month arrangement, if the SMW rate is applied to the median working hours of the entire working population, which is 8 hours, the monthly reference is \$5,824; and if the SMW rate is applied to the median working hours of the four low paying sectors² identified by the Provisional Minimum Wage Commission, which is 8.5 hours, the monthly reference is \$6,188. We consider increasing Min RI from \$5,000 to \$6,500 acceptable as it also reflects the broad-based consensus of the public.

² The four low paying sectors identified by the Provisional Minimum Wage Commission when deliberating the recommended initial SMW rate are: restaurants; retail; estate management, security, and cleaning services; and other low paying sectors (including elderly homes, laundry and dry cleaning services, hairdressing and other personal services, local courier services, and food processing and production).

6. With the increase of Min RI to \$6,500, and based on Q4 2010 data, an additional 180 900 employees / SEPs (or a total of 337 300) will be excluded from making mandatory contributions. This compares with the exclusion of an additional 50 600 employees / SEPs (or a total of 207 000) from the net if \$5,500 is adopted. The economic impact of increasing Min RI to \$6,500 is set out at Annex C.

Max RI

7. The existing Max RI of \$20,000 has not been amended since the implementation of the MPF System in 2000. The previous reviews in 2002 and 2006, with the application of the statutory factor (para. 3(b) above) suggesting an increase to \$30,000, have not been pursued given the economic environment at that time and the lack of consensus in the community. As mentioned in para. 3 above, MPFA's latest review findings based on Q3 2010 data show that consideration should be given for Max RI to be increased to \$30,000. We have received comments from employers' associations that businesses, especially small and medium enterprises ("SMEs"), are digesting the cost implications of SMW, and absorbing any increase in Max RI would be difficult. This should be balanced against views that Max RI has not been adjusted in the last ten years to reflect a need to increase savings for the employees. On balance, we propose to increase Max RI to \$25,000.

8. With the increase of Max RI to \$25,000, and based on Q4 2010 data, an additional 424 600 employees (and their employers who are required by the MPFSO to make mandatory contributions for their employees) and 89 900 SEPs will be required to make additional mandatory contributions. The economic impact of increasing Max RI to \$25,000 is set out at Annex C.

Daily Income Level

9. The MPFSO also specifies a daily income level for application to casual employees who are members of an industry scheme and employees (not being casual employees who are members of an industry scheme) remunerated more frequently than on a monthly basis³. Since the

³ Employees who fall under this category include causal employees under the two industry schemes (i.e. the catering and construction industries) as well as those employees who receive payment of salaries more frequently than on a monthly basis.

implementation of the MPF System in 2000, a 30-day basis has been assumed in converting the monthly Min RI and Max RI into daily rate. With reference to a 26-day basis when referencing to SMW for Min RI (para. 5 above), we see the logic of applying the same assumption in deriving the daily figure for statutory codification. With the increase of Min RI to \$6,500 per month, the daily Min RI on a 26-day basis is \$250⁴. As for the corresponding daily figure for Max RI, we propose to retain the current 30-day basis pending MPFA's review of the statutory adjustment mechanism, i.e. an increase from \$650 to \$830 per day, to avoid an overly abrupt increase.

Implementation Schedule

10. With the implementation of SMW on 1 May 2011, there is a need to increase Min RI as soon as possible such that the lower-income group who may earn more due to SMW can continue to be spared of the burden of making MPF contributions. Taking into account the time required for adjustment of systems by trustees and employers and publicity by MPFA etc., MPFA has advised us that the increase in Min RI can be implemented by 1 November 2011, if the revised Min RI can be confirmed in June 2011. Upon then, there will be more certainty on the revised level and trustees and employers may start preparing for the system adjustment as they see fit. On Max RI, we propose to defer the implementation of the increase in Max RI to 1 June 2012 to allow employees and employers a longer time to adjust to the new contribution level.

CONSEQUENTIAL AMENDMENTS

11. The Mandatory Provident Fund Schemes (Contributions for Casual Employees) Order (Cap. 485 sub. leg. E) ("the Order") prescribes the corresponding amount of MPF contributions to be made in respect of casual employees of industry schemes under different income bands with reference to Min RI and Max RI. The purpose of the Order is to provide easy reference to employers. MPFA will separately make corresponding amendments to the Order which are of technical nature. The commencement of the amendments will tie in with the implementation of the Amendment Notices.

⁴ If Min RI is increased to \$6,500, the daily minimum level of relevant income would be \$220 (rounded up to the nearest ten dollars) if a 30-day basis is adopted.

12. Section 16AA of the Inland Revenue Ordinance (“IRO”) (Cap. 112) provides for the deduction of mandatory contributions by SEPs for the purpose of calculating their tax payable under Profits Tax. Section 26G of the IRO provides for the deduction of contributions to recognized occupational retirement schemes and mandatory contributions to MPF Schemes by employees for the purposes of calculating tax payable under Salaries Tax or Personal Assessment⁵. The maximum amount of allowable deduction under section 16AA or 26G of the IRO for each assessment year is prescribed in Schedule 3B to the IRO, currently at \$12,000 (i.e. \$20,000 x 5% x 12 months). Subject to the increase of Max RI to \$25,000 per month, we aim to introduce an amendment bill to amend Schedule 3B to the IRO to increase the maximum deduction to \$15,000 (i.e. \$25,000 x 5% x 12 months) in the coming legislative year.

OTHER OPTIONS

13. As Min RI and Max RI are prescribed in Schedules 2 and 3 to the MPFSO respectively and amendments of the Schedules are to be made in accordance with section 48 of the MPFSO, there is no alternative option other than legislative amendment to effect the proposed changes.

THE AMENDMENT NOTICES

14. The main provisions of the two Amendment Notices are set out as follows –

- (a) Section 3 of the Amendment Notice at **Annex A** will –
 - (i) replace the existing Min RI of \$5,000 per month for employees (not being casual employees who are members of an industry scheme) who are remunerated on a monthly basis with \$6,500 per month;
 - (ii) replace the existing Min RI of \$160 per day with \$250 per day for employees (not being casual employees who are members of an industry scheme) who are remunerated more

⁵ The IRO provides that the amount of the deductible contributions made by an employee to a recognised occupational retirement scheme is limited to the amount of the mandatory contributions which the employee would have been required to pay if he had contributed as a participant in an MPF scheme.

frequently than on a monthly basis, as well as casual employees who are members of an industry scheme;

- (iii) replace the existing Min RI of \$5,000 per month for employees (not being casual employees who are members of an industry scheme) who are remunerated less frequently than on a monthly basis with \$6,500 per month, the amount as prorated; and
 - (iv) replace the existing Min RI of \$5,000 per month or \$60,000 per year for SEPs with \$6,500 per month or \$78,000 per year;
- (b) Section 3 of the Amendment Notice at **Annex B** will –
- (i) replace the existing Max RI of \$20,000 per month for employees (not being casual employees who are members of an industry scheme) who are remunerated on a monthly basis with \$25,000 per month;
 - (ii) replace the existing Max RI of \$650 per day with \$830 per day for employees (not being casual employees who are members of an industry scheme) who are remunerated more frequently than on a monthly basis, as well as casual employees who are members of an industry scheme;
 - (iii) replace the existing Max RI of \$20,000 per month for employees (not being casual employees who are members of an industry scheme) who are remunerated less frequently than on a monthly basis with \$25,000 per month, the amount as prorated; and
 - (iv) replace the existing Max RI of \$20,000 per month or \$240,000 per year for SEPs with \$25,000 per month or \$300,000 per year.

LEGISLATIVE TIMETABLE

15. The Secretary for Financial Services and the Treasury is seeking the waiver of the LegCo President from complying with the procedural requirements on notice period with a view to moving the Amendment Notices

at the LegCo meeting on 22 June 2011 for approval.

IMPLICATIONS OF THE PROPOSAL

16. The legislative proposal is in conformity with the Basic Law, including the provisions concerning human rights. The Amendment Notices will not affect the current binding effect of the MPFSO. The proposal itself has no productivity, environmental and significant sustainability implications. The financial and civil service implications, as well as the economic implications are set out at **Annex C**.

PUBLIC CONSULTATION

17. MPFA consulted the MPF Schemes Advisory Committee on 11 May 2010 and the Labour Advisory Board on 5 July 2010 on its review findings⁶. The Financial Services and the Treasury Bureau and MPFA consulted the FA Panel on the review findings on 21 February 2011⁷, after the SMW rate was enacted by LegCo in January 2011. The FA Panel further conducted a public hearing on 20 April 2011 to meet with deputations and solicit views. The Min RI proposed represents the broad-based consensus at the public hearing. On Max RI, the views are quite diverse with some employers' groups requesting no change or a smaller increase, while some requesting phased implementation if the level is to be increased to \$30,000. The views of employees and other interested parties as regards the level also vary.

PUBLICITY

18. A press release will be issued on 14 June 2011. A spokesman will be available to answer media and public enquiries.

⁶ When the two advisory bodies were consulted, the then prevailing monthly median employment earnings (based on Q1 2010 statistical data) was \$10,500 and hence MPFA's review findings for Min RI for consultation was \$5,250 whereas the review findings for Max RI (i.e. pitching at 90th percentile of the monthly employment earnings) remained unchanged at \$30,000.

⁷ MPFA updated the review findings for Min RI to \$5,500 in early 2011 taking into account statistical data for Q3 2010 which became available at that time and we consulted the FA Panel in February 2011 on this basis. The review findings for Max RI remained unchanged at \$30,000.

BACKGROUND

19. The MPFSO provides that unless exempted, an employer and employee must each contribute 5% of the employee's relevant income to an MPF scheme as mandatory contribution, while an SEP must similarly contribute 5% of his relevant income. However, if the relevant income of the employee or SEP concerned is less than Min RI, he is not required to make MPF contribution himself, although his employer (in the case of an employee) still has to make MPF contribution for him. For a relevant employee or an SEP whose relevant income is above Max RI, both he and his employer (in the case of an employee) are not required to make mandatory contribution in respect of the excess relevant income. The current Min RI and Max RI are \$5,000 and \$20,000 respectively. The Min RI was last adjusted in 2002 whereas Max RI has never been adjusted since the implementation of the MPF System in 2000.

20. Section 10A of the MPFSO requires that MPFA must, not less than once in every four years, conduct a review of Min RI and Max RI to ascertain whether there are grounds to amend the levels. In accordance with the law, MPFA conducted a review and submitted its findings to FSTB in July 2010. As the objective of Min RI is to lessen the financial burden of MPF contribution on low-paid employees, FSTB considers that a credible Min RI level should take into account SMW. After the SMW rate was enacted by LegCo in January 2011, we consulted the FA Panel in February 2011 on MPFA's review findings and attended a public hearing convened by the Panel on 20 April 2011.

ENQUIRIES

21. Enquiries in relation to the LegCo Brief should be directed to Miss Emmy Wong, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) at 2527 3909.

Financial Services and the Treasury Bureau
14 June 2011

**Mandatory Provident Fund Schemes Ordinance
(Amendment of Schedule 2) Notice 2011**

(Made by the Chief Executive in Council under section 48 of the
Mandatory Provident Fund Schemes Ordinance (Cap. 485) subject to the
approval of the Legislative Council)

1. **Commencement**
This Notice comes into operation on 1 November 2011.
2. **Mandatory Provident Fund Schemes Ordinance amended**
The Mandatory Provident Fund Schemes Ordinance (Cap. 485) is
amended as set out in section 3.
3. **Schedule 2 amended (Minimum level of relevant income per
contribution period)**
 - (1) Schedule 2, section 1(a)—
Repeal
"\$5,000"
Substitute
"\$6,500".
 - (2) Schedule 2, section 1(b)—
Repeal
"\$160"
Substitute
"\$250".
 - (3) Schedule 2, section 1(c)—
Repeal
"\$5,000"

- Substitute**
"\$6,500".
- (4) Schedule 2, section 2—
Repeal
"\$160"
Substitute
"\$250".
- (5) Schedule 2, section 3—
Repeal
"\$5,000"
Substitute
"\$6,500".
- (6) Schedule 2, section 3—
Repeal
"\$60,000"
Substitute
"\$78,000".
4. **Application of Schedule 2 as amended**
Schedule 2 to the Mandatory Provident Fund Schemes Ordinance
(Cap. 485) as amended by section 3 applies in relation to a
contribution period that begins on or after the commencement date
of that section.

Explanatory Note

The purpose of this Notice is to amend Schedule 2 to the Mandatory Provident Fund Schemes Ordinance (Cap. 485) so as to adjust the minimum level of relevant income for contribution purposes under that Ordinance.

Clerk to the Executive Council

COUNCIL CHAMBER

2011

**Mandatory Provident Fund Schemes Ordinance
(Amendment of Schedule 3) Notice 2011**

(Made by the Chief Executive in Council under section 48 of the
Mandatory Provident Fund Schemes Ordinance (Cap. 485) subject to the
approval of the Legislative Council)

1. **Commencement**
This Notice comes into operation on 1 June 2012.
2. **Mandatory Provident Fund Schemes Ordinance amended**
The Mandatory Provident Fund Schemes Ordinance (Cap. 485) is amended as set out in section 3.
3. **Schedule 3 amended (Maximum level of relevant income per contribution period)**
 - (1) Schedule 3, section 1(a)—
Repeal
"\$20,000"
Substitute
"\$25,000".
 - (2) Schedule 3, section 1(b)—
Repeal
"\$650"
Substitute
"\$830".
 - (3) Schedule 3, section 1(c)—
Repeal
"\$20,000"

- Substitute**
"\$25,000".
- (4) Schedule 3, section 2—
Repeal
"\$650"
Substitute
"\$830".
- (5) Schedule 3, section 3—
Repeal
"\$20,000"
Substitute
"\$25,000".
- (6) Schedule 3, section 3—
Repeal
"\$240,000"
Substitute
"\$300,000".
4. **Application of Schedule 3 as amended**
Schedule 3 to the Mandatory Provident Fund Schemes Ordinance (Cap. 485) as amended by section 3 applies in relation to a contribution period that begins on or after the commencement date of that section.

Explanatory Note

The purpose of this Notice is to amend Schedule 3 to the Mandatory Provident Fund Schemes Ordinance (Cap. 485) so as to adjust the maximum level of relevant income for contribution purposes under that Ordinance.

Clerk to the Executive Council

COUNCIL CHAMBER

2011

Financial and Civil Service Implications and Economic Implications

Financial and Civil Service implications

Staffing Implications

The proposal to increase the minimum level of relevant income (“Min RI”) and the maximum level of relevant income (“Max RI”) will have no staffing implications for the Government.

Expenditure Implications

2. The proposal to increase Min RI from \$5,000 per month to \$6,500 per month will not affect the obligations of the Government as an employer.

3. As for the proposed increase of Max RI to \$25,000, the Government would need to make additional Mandatory Provident Fund (“MPF”) mandatory contributions in respect of Government employees earning a monthly income of \$20,000 or above and who currently only receive mandatory contributions from the Government. Government contribution for about 13 700 members of the civil service will not be affected as the amount of their MPF contributions are not linked to the maximum relevant income level.

4. The Government has to make additional mandatory contribution for about 11 200 employees which amount to around \$28.9 million per annum. Such increase would be ‘offset’ by the reduction in gratuity payments for about 5 500 employees who are entitled to a contract gratuity. Thus, the net additional mandatory contributions to be made by the Government would be around \$13.4 million per annum.

5. Subvented bodies with staff earning more than \$20,000 a month and receiving mandatory contributions from these bodies under the MPF Scheme will be affected by the increase in Max RI. Bureaux / departments will deal with the implications according to individual subvention agreements.

6. Likewise, contractors for Government services will be affected if they engage workers with monthly income above \$20,000 and receiving mandatory contributions from them under the MPF Scheme. Bureaux and

departments will deal with the implications in accordance with the contract terms.

Revenue Implications

7. Under the Inland Revenue Ordinance (Cap. 112) (“IRO”), employers can claim both mandatory and voluntary contributions that they have made in respect of their employees as allowable business expenses for calculating Profits Tax. The maximum deduction amount is 15% of the total emoluments of the employees.

8. Also under the IRO, employees and self-employed persons (“SEPs”) can claim mandatory MPF contributions as a concessionary deduction item for calculating tax payable under Salaries Tax, Profits Tax or Personal Assessment, as the case may be. If the maximum relevant income level is adjusted to \$25,000 per month, the corresponding maximum tax deduction amount should be increased from \$12,000 to \$15,000 for each year of assessment.

9. If Max RI is adjusted to \$25,000 per month and the corresponding maximum tax reduction amount is increased to \$15,000, the Treasury Branch estimates that the total amount of tax under Salaries Tax, Profits Tax and Personal Assessment to be received by the Government would decrease by \$360 million per annum.

Economic implications

10. Based on the data of Q4 2010, the proposed adjustment of Min RI from \$5,000 to \$6,500 per month would exclude an additional 162 000 employees and 18 900 SEPs from contributing 5% of their income into MPF Schemes. The reduction in MPF contribution would amount to about \$51 million per month. There should be no impact on business operating cost as employers’ share of MPF contribution will not be affected by the level of Min RI. On the other hand, the total disposable income of the employees and SEPs concerned would increase by \$51 million per month, or equivalent to around 1.6% of the estimated monthly contribution based on Q4 2010 data, which is likely to increase consumer spending. Given the relatively small amount involved, the effect is expected to be small in overall terms.

11. The proposed adjustment of Max RI from \$20,000 to \$25,000 per

month would increase the monthly contribution of 424 600 employees (and their employers) and 89 900 SEPs. The increase in total MPF contribution is around \$217 million per month, or equivalent to around 7% of the estimated monthly contribution based on Q4 2010 data. Some small and medium enterprises express that this will further increase their costs on top of SMW. Given their relatively small number of high-paid employees and the maximum additional contribution required for each employee will not be more than \$250 per month, the impact should not be unmanageable. On the other hand, the proposal will reduce the disposable income of each affected relevant employee and SEP by up to \$250 per month. However, since the affected scheme members belong to the better-off group, we do not expect it will seriously affect their expenditure pattern.

12. Longer term, the increase of Min RI will, on average, reduce the accrued benefits by \$262,000 per affected employee and \$257,000 per affected SEP respectively¹. This will reduce their accrued benefits upon retirement and may increase the pressure on welfare services in the long run. In contrast, the increase of Max RI will, on average, increase the accrued benefits by \$422,000 per affected employee and \$209,000 per affected SEP respectively upon their retirement².

13. The proposed adjustment of Min RI and Max RI will bring about a net increase of MPF contribution of \$166 million per month to the pool of retirement savings in MPF Schemes.

¹ The estimations are based on the assumptions that the member makes MPF contributions for 30 years and the MPF investment return (net of fees) is 5.5% per annum (i.e. the same rate as the annualized rate of return of MPF since the implementation of the MPF System in December 2000 to 31 December 2010).

² Same assumptions as per Footnote 1.