

**LegCo Panel on Manpower
(For Meeting on 23.12.1998)**

**Information Paper
Proposed amendments to the
Protection of Wages on Insolvency Ordinance**

**Revision of payment limits
and calculation of ex-gratia payment of severance payment**

Introduction

This paper informs members of the following two legislative proposals to improve the protection of employees under the Protection of Wages on Insolvency Ordinance (PWIO) :

- (a) to increase the existing limit of severance payment (SP) to \$50,000 (from existing \$36,000) plus 50% of the excess entitlement.
- (b) to amend the PWIO to the effect that the amount of ex-gratia payment for SP would be calculated according to an employee's wage level before wage reduction provided that his employer has given such an undertaking **in writing** at the time of and before implementation of the wage reduction proposal and that the wage reduction took place within the 12 months immediately before the date of termination of employment. If an employee's wage level has been reduced for more than once during the past 12 months and before implementation of each wage reduction the employer has made such an undertaking in writing, the latest undertaking shall prevail for the purposes of calculating the amount of ex-gratia payment of SP. The proposal will include a transitional arrangement to provide that where prior to the commencement of the amendment, an employer has given a verbal undertaking to pay SP on the basis of an employee's wage level before wage reduction, if the employer makes such undertaking in writing within two months from the

commencement of the amendment bill, the written undertaking shall be valid for the purposes of the proposed amendment.

Existing limits of ex-gratia payments made by the Protection of Wages on Insolvency Fund (PWIF)

2. At present, the limits of ex-gratia payments are as follows:
 - (a) arrears of wages (AW) for services rendered during the four-month period prior to the last day of service up to \$36,000;
 - (b) wages in lieu of notice (WILON) up to one month's wages or \$22,500, whichever is the less; and
 - (c) SP up to \$36,000, plus 50% of that part of the employee's entitlement to SP in excess of \$36,000.

The maximum amount of ex-gratia payment an applicant can now receive from the Fund is \$221,500.

Calculation of severance payment under PWIO

3. Under the PWIO, the PWIF follows the provisions of the Employment Ordinance (EO) in calculating the SP entitlement. In other words, SP will be calculated on the basis of the wage level immediately before termination of employment. An employee may elect to take the average wage over the preceding 12-month period. Any agreement more favourable than those provided under the EO between employers and employees would be binding on the concerned parties.

4. There has been public concern that the present trend of wage reductions would have significant implications on the amount of an employee's SP if his employer should become insolvent subsequently. It has also been suggested that employees would be more willing to accept wage reduction proposals if the PWIF should calculate the amount of ex-gratia payment for SP on the basis of an employee's wage level before wage reduction if his employer had made such an assurance.

Review by the PWIF Board (Board)

5. The Board has recently reviewed the payment limits and has concluded that there is no need to revise the limits of AW and WILON as about 94% and 98% of the applicants could recover their full entitlements respectively in 1997. However, noting that only 75% of applicants could get their entitled SP in full in 1997, the Board considered that the limit of SP should be revised. After very careful consideration and having regard to the financial position of the PWIF, the Board arrived at the view that the limit should be increased to \$50,000 (from existing \$36,000) plus 50% of excess entitlement. The Board has agreed to review the position in mid-1999.

6. The Board has also agreed that the amount of ex-gratia payment of SP under the PWIO may be calculated on the basis of an employee's wage level before wage reduction if his employer has given such an undertaking in writing at the time of and before implementation of the wage reduction proposal.

Consultation with the Labour Advisory Board

7. At its meeting held on 21 December 1998, the LAB endorsed the proposals set out in para. 1 above.

Financial implications of the proposals on the PWIF

8. On the basis of the cases approved during 1997/98, we estimate that under the proposal to increase the payment limit of SP, some 84% of the applicants will be able to get their entitled SP in full under this proposal. The additional pay-outs from the PWIF is about \$19 million. Although the PWIF will incur a deficit in 1998, its financial position is still healthy and should be able to bear the additional payment arising from this proposal.

9. As for the other proposal, the financial implications on the PWIF would likely to be insignificant as only when an employer has given a written undertaking of paying SP on the basis of the pre-reduced wage level and subsequently become insolvent will his employees be covered by the proposal.

Financial position of the PWIF

10. In November 1998, the claims payments reached a high level of \$49 million. This, together with decreased interest income as a result of reduced interest rates, brought about a deficit of around \$32 million for the month, bringing the total deficit from April to November 1998 to \$75 million. Although there are a few major applications such as the KPS Retail Stores and the Ming Fung Group still being processed, the total accumulated fund, as at 30 November 1998, stood at a healthy level of \$777 million. It is estimated that the total accumulated fund will deplete further in December 1998 when the major outstanding cases are paid out. As at 30 November 1998, the PWIF has contingent liabilities, i.e. claims received but being processed, amounting to around \$200 million.

Legislative timetable

11. We intend to implement the two proposals as soon as possible.

Labour Department
22 December 1998