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Panel on Financial Affairs

Meeting on 1 February 2007

Updated Background Brief on Review of the Minimum and Maximum Relevant Income Levels for Mandatory Provident Fund Contributions

Purpose

This paper sets out the background of the review of the minimum and maximum relevant income levels for Mandatory Provident Fund (MPF) contributions; and summarizes Members' concerns on the subject.

The Mandatory Provident Fund Schemes (Amendment) Bill 2002

2. When the MPF system was first launched in December 2000, a relevant employee or self-employed person (SEP) whose relevant income was less than $4,000 per month was not required to make MPF contributions, although his employer (if any) had to make contributions in respect of him. If the relevant income of the relevant employee or SEP was above $20,000 per month, he was not required to contribute to the MPF scheme in respect of the amount in excess of $20,000. The minimum and maximum levels of $4,000 and $20,000 respectively were adopted in 1995 when the Mandatory Provident Fund Schemes Ordinance (Cap. 485) (MPFSO) was enacted. According to the Administration, the $4,000 was derived from 50% of the then monthly median employment earnings (monthly median income); and the $20,000 was based on the target to cover the entire earnings of 90% of the working population.

3. With a view to reviewing the operation of the MPF system, the Mandatory Provident Fund Schemes Authority (MPFA) set up the MPF Schemes Operation Review Committee (the Review Committee) in August 2001. It completed the first phase of its work in end 2001 and put forward a number of proposals. The Administration agreed with the proposals and introduced the Mandatory Provident Fund Schemes (Amendment) Bill 2002 (the 2002 Bill) which proposed, inter alia, a mechanism for future adjustment of the minimum and maximum levels of relevant income for MPF contribution purposes. It was proposed that MPFA must conduct

a review of the minimum and maximum levels of relevant income **not less than once in every four years**. Without limiting the factors which MPFA might take into consideration, MPFA must take into account the following findings prevailing at the time of the review as compiled from the General Household Survey conducted by the Census and Statistics Department :

(a) in respect of the minimum level of relevant income, 50% of the monthly median employment earnings; and

(b) in respect of the maximum level of relevant income, monthly employment earnings at 90th percentile of the monthly employment earnings distribution.

4. Accordingly, the Administration proposed in the 2002 Bill to revise the minimum level of relevant income from $4,000 to $5,000 per month. However, having regard to the prevailing economic conditions at that time, the Administration proposed to retain $20,000 per month as the maximum level of relevant income instead of raising it to $30,000 in accordance with the relevant findings. The 2002 Bill was passed by the Legislative Council on 12 July 2002. To allow time for service providers and employers to make adjustments to their systems and administration procedures, the raising of the minimum level of relevant income for MPF contributions (as well as some other changes) became effective on 1 February 2003.

5. A summary of the major views and concerns expressed by Members in the course of scrutinizing the 2002 Bill is in **Appendix I**.

Review by MPFA

6. The MPFA conducted a review of the minimum and maximum relevant income levels in mid-2006, which was the first such review conducted since the commencement of section 10A of MPFSO. Based on the adjustment mechanism under the said section, MPFA has put forward the following recommendations for the Government's consideration :

(a) **maintaining** the minimum level of relevant income at **$5,000 per month**; and

(b) **increasing** the maximum level of relevant income from $20,000 to **$30,000 per month**.

The Administration has indicated that it will consider the community's views before making a decision on the matter.

7. When the MPFA briefed the Panel on Financial Affairs (FA Panel) on its recommendations at the meeting on 5 January 2007, some Panel members indicated support for MPFA's recommendations. Some Members expressed reservation on

the proposal of increasing the maximum level of relevant income from $20,000 to $30,000 per month while some Members were of the view that the minimum relevant income level should be raised to $6,000 instead of remaining unchanged. Question was raised as to whether the existing adjustment mechanism under section 10A should also be reviewed. The major views and concerns expressed by Members are as follows:

(a) Consideration should be given to raising the minimum relevant income level from $5,000 to $6,000 per month for the purpose of making MPF contributions. This would relieve low-income workers of the financial burden of making MPF contributions and enable them to have more disposable income to make their ends meet.

(b) Pending a full recovery of the economy, increasing the maximum relevant income level for making MPF contributions would inevitably increase the operating costs of employers, in particular small and medium enterprises which had been hard hit during the economic downturn.

(c) There might not be a strong need to extend the requirements to make MPF contributions to employees earning over $20,000 a month as these higher income earners might have made other investments for their retirement.

(d) Given the changes in circumstances since the enactment of the 2002 Bill, it might be opportune for the Administration/MPFA to examine whether the existing adjustment mechanism for determining the minimum and maximum relevant income levels should be reviewed.

(e) The efficacy of the MPF system in providing adequate retirement protection was questionable as its investment return had not been very impressive. To cater for the retirement needs of the workforce, in particular low-income earners, the Administration was asked to re-consider whether the MPF System should be supplemented by other retirement benefit schemes such as old-age pension scheme or Central Provident Fund.

(f) It was pointed out that employers might choose to withhold wage increases if they were required to increase their MPF contributions as a result of raising the maximum relevant income level.

8. As changes in the minimum and maximum relevant income levels for MPF contributions will have implications on employers, employees and the retirement scheme industry, the FA Panel has decided to hold a special meeting on 1 February 2007 to receive deputations' views. To facilitate discussion, the Administration/MPFA have also been requested to provide further information :

(a) various modellings on the accrued benefits to employees upon retirement based on the real MPF investment return rates over the past few years;

(b) given that tax concessions are granted for employers' and employees' MPF contributions, the possible impact on tax revenue if the maximum relevant income level is raised to $30,000 per month; and

(c) 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.

Relevant papers

9. A list of relevant papers is in **Appendix II**.

Council Business Division 1
Legislative Council Secretariat
29 January 2007

Appendix I

Major views and concerns expressed by Members on the 2002 Bill

Time-frame for review

Members raised no objection to the four-year time-frame but were concerned about the transparency of future reviews conducted by MPFA. To address the concern, the Administration undertook to report to the Panel on Financial Affairs on each review conducted by MPFA under section 10A of MPFSO. The Administration also took note of members' concern about the need to enhance publicity on the outcomes of future reviews by MPFA.

Minimum and maximum levels of relevant income

2. In proposing to raise the minimum level of relevant income from $4,000 to $5,000 per month in the 2002 Bill (i.e. adopting the threshold of 50% of the monthly median income), the Administration sought to strike a balance between avoiding to burden lower income workers and protecting their retirement needs.

3. While most members of the Bills Committee did not have any strong view against the Administration's proposal, a few members were of the view that the minimum level should be raised to $6,000 per month so as to relieve low income workers of the financial burden of making MPF contributions and to enable them to retain more disposable income which could help boost private consumption. For this purpose, Hon Andrew CHENG moved Committee Stage amendments (CSAs) to the Bill in his name stipulating that not less than 60% of the monthly median income should be adopted as the minimum relevant income level for MPF contributions.

4. The Administration objected to the member's CSAs and pointed out during the Second Reading debate on the Bill that some 130 000 employed persons would be excluded from the MPF contribution net if the proposed 60% level was adopted, thereby defeating the purpose of helping lower income workers to prepare for retirement. Furthermore, this would also mean a reduction in the amount of MPF benefits that would be accrued for scheme members upon retirement. According to the Administration, based on the 2001 statistics, it was estimated that increasing the minimum relevant income level from $5,000 to $6,000 per month would increase private consumption expenditure by a mere 0.009% which was not significant.

5. Given the economic conditions prevailing at that time, the Administration considered it appropriate to retain the maximum relevant income level at $20,000 per month, instead of raising it to $30,000 in accordance with the existing adjustment mechanism, to avoid increasing the burden on employers/employees. According to MPFA, many employees in the higher income bands were members

of MPF schemes receiving voluntary contributions on top of mandatory contributions. Therefore, proposing no change to the maximum level at that time would unlikely affect the retirement protection for these employees.

6. Some members queried the Administration for adopting a double standard in not adjusting the maximum level of relevant income in accordance with the relevant findings as in the case of the minimum level of relevant income. In this connection, Hon Andrew CHENG considered that a lower percentile of the monthly employment earnings distribution should be stipulated in the legislation so as to obviate the need to deviate from the agreed principle every now and then and to rely on the discretion of the MPFA/Administration to determine the appropriate level. He had therefore moved CSAs to the effect that the monthly employment earnings at a percentile not exceeding 80^{th} of the monthly employment earnings distribution should be adopted as the maximum level of relevant income.

7. The Administration advised that the objective of its proposal on the maximum relevant income level was to extend as far as possible the coverage of the MPF system. It considered that lowering the percentile would run contrary to the aforesaid objective and did not support the member's CSAs.

8. The CSAs moved by Hon Andrew CHENG relating to the minimum and maximum levels of relevant income were negatived. The Administration's proposals were passed and have been in force since 1 February 2003.

Appendix II

List of relevant papers

Committee	Paper	LC Paper No.
--	✧ Legislative Council Brief on Mandatory Provident Fund Schemes (Amendment) Bill 2002 issued by the Financial Services Bureau on 17 April 2002 http://www.legco.gov.hk/yr01-02/english/bills/brief/b53_brf.pdf	--
Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2002	✧ Report of the Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2002 http://www.legco.gov.hk/yr01-02/english/hc/papers/hc0628cb1-2114.pdf	CB(1)2114/01-02
--	✧ Hansard of the Legislative Council meeting on 12 July 2002 http://www.legco.gov.hk/yr01-02/english/counmtg/hansard/cm0712ti-translate-e.pdf	--
Meeting of Panel on Financial Affairs on 5 January 2007	✧ Paper on Adjustment of the Minimum and Maximum Levels of Relevant Income http://www.legco.gov.hk/yr06-07/english/panels/fa/papers/fa0105cb1-602-3-e.pdf	CB(1)602/06-07(03)
	✧ Background Brief on Review of the Minimum and Maximum Relevant Income Levels for Mandatory Provident Fund Contributions http://www.legco.gov.hk/yr06-07/english/panels/fa/papers/fa0105cb1-603-e.pdf	CB(1)603/06-07
	✧ Power-point presentation on review of the minimum and maximum relevant income levels for Mandatory Provident Fund contributions http://www.legco.gov.hk/yr06-07/chinese/panels/fa/papers/fa0105cb1-646-1-ec.pdf	CB(1)646/06-07(01)