

**For discussion on
12 April 2007**

Legislative Council Panel on Financial Affairs

**Proposed amendments to
Mandatory Provident Fund Schemes Ordinance**

PURPOSE

This paper seeks Members' views on the proposed amendments to the Mandatory Provident Fund ("MPF") legislation to improve the MPF System in the light of operational experience.

BACKGROUND

2. The MPF System, designed to be a mandatory, privately managed, fully-funded scheme, was launched in December 2000 for retirement protection for Hong Kong's working population. As at end January 2007, over 2.35 million employees and self-employed persons had enrolled in the MPF schemes, and the total asset of the MPF constituent funds was over \$200 billion. Given the impact of the MPF System on the community, it is essential that the MPF System should be constantly reviewed to ensure that it continues to serve the needs of the existing and potential scheme members.

3. The MPF Schemes Operation Review Committee ("the Review Committee") was established by the Mandatory Provident Fund Schemes Authority ("MPFA") in August 2001 for the purpose of conducting comprehensive review of the MPF System and relevant legislation with regard to their operational and administrative aspects. Membership of the Review Committee is at the Annex. Based on the advice of the Review Committee, the MPFA has made a number of recommendations on amendments to the MPF legislation. The Administration intends to take forward the amendment proposals through the introduction of an MPF Schemes (Amendment) Bill in 2006/07 legislative session.

MAJOR LEGISLATIVE PROPOSALS

MPF treatment of housing allowance and other housing benefit

4. Under the Mandatory Provident Fund Schemes Ordinance (“MPFSO”), each employee and employer has to contribute 5% of the relevant income as mandatory contributions, subject to the minimum and maximum levels of relevant income. Housing allowance and other housing benefit are excluded from the definition of “relevant income”. It has come to our attention that some employers have intentionally restructured the remuneration package of their employees by converting a portion of salary and wages to what they claim to be a housing allowance or other housing benefit so as to reduce the amount of relevant income and to evade their responsibilities to pay mandatory contributions in respect of that portion of salary and wages.

5. The primary justification for originally excluding housing allowance from the definition of “relevant income” was that housing allowance could be quite substantial and the exclusion was needed to minimise the potentially significant contribution burden for employees who received housing allowances. Their inclusion would perhaps be a detriment to the employee’s disposable income. Hence, it was recommended to exclude housing allowance and benefit from relevant income when the legislation was first enacted in August 1995. It was also envisaged at the time that the matter would be unlikely to affect lower-paid employees, probably because they usually were not entitled to housing allowance and benefit. However, in the light of abuses that have developed in recent years, the MPFA has reconsidered the validity of such a basis for exclusion.

6. Conceptually, MPFA is of the view that there is no valid reason to treat housing allowance differently from any other types of allowance or remuneration items. The fact that an allowance is for covering a substantial expenditure item of the employee should not be a determinant in deciding whether that allowance item should be excluded from relevant income. Other types of payment and expense could also be very significant and may even be of an amount greater than housing expense. One may then argue that other types of allowance provided by an employer to an employee should also be excluded from relevant income as any employee’s mandatory contributions thereon would aggravate the contribution burden of the employee. If that rationale for excluding an amount from relevant income was extended to its logical conclusion, we might end up with a situation where mandatory contributions were only payable on an employee’s net savings (i.e. the amount of payments not expended each month) because allowances could be structured to cover all other

outgoings. To apply such rationale, mandatory contributions could be substantially reduced in many cases. Hence, the fact that housing expense is expensive in Hong Kong does not appear to fully justify its exclusion from relevant income.

7. Further, if the purpose of the application of the housing allowance exclusion were to alleviate the contribution burden of those employees who have to incur housing expense, this treatment should be extended to all employees incurring housing expense regardless of whether they are receiving housing allowance from employers. This, however, would be impractical and susceptible to manipulation.

8. We propose to amend the MPFSO by removing the specific housing allowance and benefit exclusion from the definition of “relevant income”. As a result, all remuneration items (including housing allowance/other housing benefit) will be taken into account in determining the relevant income for computation of mandatory contribution purpose.

Non-payment of mandatory contribution in non-enrolment cases

9. Under section 7(1) of MPFSO, every employer of a relevant employee is required to ensure that his employee becomes a member of an MPF scheme within a prescribed period. Section 7(1A) further stipulates that an employer is required to ensure the enrolment of his employee in an MPF scheme throughout his employment. A breach of section 7(1A) is a continuous offence where an employer could be prosecuted more than once for his failure to enrol an employee and is liable to a daily penalty of \$500 for each day on which the offence is committed. Under section 7A(1)(a) and 7A(2)(a), it is the legal responsibility of the employer to make mandatory contributions to an MPF scheme. Section 7A(8) further stipulates that mandatory contributions should be paid to the approved trustee of an MPF scheme of which the employee is a member within a prescribed period and in a prescribed manner.

10. However, where an employer has failed to enrol an employee into an MPF scheme, while criminal prosecution could be brought against the employer for non-enrolment, no legal action could be taken against the employer for its non-payment of mandatory contributions under the existing MPF legislation. We therefore propose to amend the MPFSO to provide that in non-enrolment cases, the MPFA can bring criminal proceedings against the employer for non-enrolment and non-payment of mandatory contributions at the same time. To facilitate effective enforcement, we also propose to amend the MPFSO so that upon conviction for non-enrolment or non-payment of

mandatory contributions, the Court will have a discretionary power to compel an employer to enrol his employee into an MPF scheme and to pay the outstanding contributions and contribution surcharges as appropriate. These measures could enhance the deterrent effect against non-enrolment.

Improvement of arrears recovery mechanism

11. Sections 132-136 of the Mandatory Provident Fund Schemes (General) Regulation (“General Regulation”) prescribe in detail the procedure for recovering arrears of contribution¹. Concerns have been expressed that the current arrears recovery process is too cumbersome, thus affecting the ability to recover default contribution in a timely manner from employers, especially in cases where an employer enters into bankruptcy or liquidation.

12. At present, an employer is required to pay the mandatory contributions by the contribution day, and the trustee would issue a reminder notice to the employer requiring it to settle the default contribution by the end of the 30-day settlement period². There are concerns that some employers may take advantage of the 30-day settlement period to delay payment as long as possible and settle the mandatory contributions with the trustee only towards the end of the 30-day settlement period.

13. The MPFA could impose contribution surcharge and institute civil proceedings against an employer to recover the default contribution and contribution surcharge by virtue of section 18 of the MPFSO only after all the

¹ Where an employer fails to pay the mandatory contributions by the contribution day, the approved trustee needs to issue a reminder notice to the employer requiring it to settle the default contributions by the end of the settlement period (i.e. a 30-day statutory period immediately following the contribution day). If the employer fails to do so, the trustee must make a first report of such fact to the MPFA within the immediately following 7 days. The MPFA will then send a notice to the employer imposing a contribution surcharge and requiring rectification within a specified period. Should the employer still fail to rectify, the trustee will make a second report to the MPFA within the immediately following 10 days. If warranted, the MPFA may institute legal action to recover as a debt due to the MPFA from the employer the default contribution and contribution surcharge.

² The purpose of the 30-day settlement period is to allow some time for the trustees to help employers resolve default cases, particularly those caused by inadvertent omissions or other unintentional reasons. During the 30-day period, upon notification by the trustees, the employers can, for example, rectify careless mistakes made in the computation of contributions and make up for differences in the amounts of contributions due to those mistakes. Those cases that can be resolved during the 30-day period do not need to be reported by the trustees to the MPFA and will therefore allow resources of the MPFA to be focused on genuine default cases. This settlement period was useful during initial implementation of the MPF System because many employers were not familiar with the calculation of MPF contributions then. However, the calculation method was simplified in 2002 and, by now, most employers are familiar with it. On the other hand, some employers are taking it for granted that they do not need to contribute until the end of the settlement period since these cases will not be reported to the MPFA.

recovery procedures have been complied with. However, it is not possible to comply with the detailed recovery mechanism in full in some cases. An example would be an employer who did not enrol employees in an MPF scheme for a period of several years after employment and did not make contributions for those years. Due to the passage of time, the reporting period for each of the monthly contribution periods has already passed, rendering it impossible for the trustee concerned and MPFA to comply with all the recovery steps. There is uncertainty about the authority of the MPFA to impose contribution surcharge and institute civil proceedings against defaulting employers in case where the recovery procedures prescribed in sections 132-136 have not been complied with.

14. The General Regulation requires the MPFA to issue a surcharge notice to an employer after the MPFA receives a first report on default contribution on that employer from the trustee. In cases such as those where it is clear that the employer cannot be contacted at the address on record or that employers have already been wound up, issuance of surcharge notices would inevitably lead to wastage of enforcement resources.

15. In view of the concerns and problems with the existing default contribution recovery procedure, we propose to amend the General Regulation to streamline the procedure by removing the settlement period and providing the MPFA with the discretion to issue notices to employers, and clarifying the uncertainty in the law to facilitate the recovery of default contribution by the MPFA even if some recovery steps could not be complied with.

OTHER LEGISLATIVE PROPOSALS

16. The other legislative proposals could be broadly classified into three categories: (A) to enhance the enforcement of the MPF System; (B) to improve administration and regulation of MPF schemes; and (C) other technical and miscellaneous amendments. The proposals are summarised in the following paragraphs.

(A) Enhance the enforcement of the MPF System

Greater effectiveness of service of MPF summonses

17. Service of a summons on a body corporate under MPFSO is governed by the Companies Ordinance which provides that a summons may be served on a company by leaving it or sending it by post to the registered office of

the company. However, the service would not be effective if the registered address of a company is not valid and there is nobody to acknowledge receipt. We propose to provide for an alternative mechanism for the service of summons on the employer's business address so as to increase the chance of successful service of summons.

Expansion of power to require production of records

18. Currently, the MPFA does not have the general power to request production of records from employers and self-employed persons except during on-site inspections. We propose to introduce a new provision in the MPFSO to confer the MPFA with an explicit power to request employers or self-employed persons to produce records to the MPFA within a specified period, irrespective of whether during on-site inspections or not, for the purpose of ensuring compliance with the provisions of the MPF legislation. The employer or self-employed person who, without reasonable excuse, fails to comply with the request commits an offence and is liable on summary conviction to a fine.

Extension of the prosecution time bar

19. The time limit for instigating criminal proceedings for an offence under sections 43C and 43E of the MPFSO and section 26 of the Mandatory Provident Fund Schemes (Exemption) Regulation is now governed by section 26 of the Magistrates Ordinance which is six months after the occurrence of the offence. To facilitate the MPFA to take enforcement action more effectively, we propose to amend the relevant sections to the effect that criminal proceedings may be instigated for an offence under these sections within six months after the offence is discovered by, or comes to the notice of, the MPFA.

(B) Improve administration and regulation of MPF scheme

Content requirement of annual benefit statement

20. At present, the General Regulation does not provide any mechanism for adjustments to the content requirements for the Annual Benefit Statement other than through amendments to the General Regulation. To enable the content requirements for the Annual Benefit Statement to be changed in line with market developments in a timely manner, we propose that section 56 of the General Regulation be amended to allow for the addition of further content requirements to Annual Benefit Statement as prescribed by the MPFA.

Transfer of accrued benefits on cessation of employment

21. The General Regulation requires an employer to notify the trustee of the cessation of employment of an employee within 30 days. Failure of the employer to do so might hinder the trustee to process the transfer of accrued benefits as requested by the employee. We propose to allow an employee to submit a notice of cessation of employment by statutory declaration where his employer cannot be located or refuses to submit the notice by the prescribed date so that his accrued benefit could still be transferred despite the failure of the employer to notify the cessation of employment.

Withdrawal of accrued benefits of a deceased member

22. In the context of withdrawal of MPF accrued benefits, it is unclear as to whether the Official Administrator, who summarily administers the small estate of a deceased member, could be considered as the “personal representative” as permitted under section 161 of the General Regulation, and therefore can lodge an application for payment of the deceased’s accrued benefits with the trustee of the scheme. We propose to clarify that the Official Administrator could be considered as a “personal representative” for the purpose.

Claiming of accrued benefits by scheme members

23. At present, a scheme member could withdraw his MPF benefits on the ground of permanent departure from Hong Kong by lodging a claim accompanied by a statutory declaration that he departed, or will depart, from Hong Kong permanently on a specified date; and no mandatory contributions were paid or were required to be paid by or in respect of the member to any MPF scheme since the specified date. A scheme member with small balance accounts of \$5,000 or less could withdraw his accrued benefits in the MPF scheme³, provided that no mandatory contributions were paid or required to be paid by or in respect of the member to that scheme, or to any other registered scheme during the 12 months immediately preceding the lodgement of a claim for payment of accrued benefits.

³ The current legislation allows scheme members with small balance accounts of \$5,000 or less and who have permanently left the workforce to withdraw their accrued benefits. This is because such small balances run the risk of erosion by fees and expenses (in case of flat fees in addition to percentage-based fees). Based on the quarterly statistical returns submitted by the trustees, an amount of \$21 million has been withdrawn from the MPF System on the ground of small balance account since the inception of the MPF System to 31 December 2006.

24. However, in practice, some employers may have deferred or delayed in making mandatory contributions beyond the specified date (in the permanent departure case) or beyond the date of cessation of employment of the scheme member (in the small balance account case). The scheme members would therefore not be able to claim the accrued benefit. We propose to revise this arrangement so that claimants will be able to withdraw their accrued benefits even if there were outstanding contributions by the specified date or after cessation of employment.

Unclaimed benefits

25. We propose to amend section 166 of the General Regulation to provide that if a benefit cheque remains un-presented for a certain period after issuance, the trustee, should, at the end of that period, treat the benefits as unclaimed benefits. The trustee then can trigger the procedures in dealing with the unclaimed benefits. This includes reporting of the information to the MPFA for inclusion in the unclaimed benefits register, which is available for public inspection to enable scheme members to locate their benefits.

26. A trustee is now required to publish newspaper notices to invite the member to lodge a claim if a scheme member who is entitled to be paid accrued benefits cannot be located. If no claim is made after publication of the notices, the benefits may be treated as unclaimed benefits. It is, however, silent on when the trustee should publish such a notice and henceforth the benefits could never become unclaimed benefits even if the trustee could not locate the member for a long time. A trustee is also required to publish a notice in newspapers listing the names of those members who have unclaimed benefits as at the end of the yearly financial period of the scheme and report the same to the MPFA within six months after the end of that period. The reporting period may therefore cover cases from six to 18 months and is considered to be too long both for monitoring by the MPFA and for the details of unclaimed benefits to be updated in the register maintained by the MPFA.

27. As mentioned in paragraph 26 above, the trustee is now required to publish notices in newspaper to invite eligible members who cannot be located to claim their benefits. However, publishing newspaper notices is not an effective means to invite members to take the prescribed action. The cost for publication of the newspaper notices will also be borne by the scheme members.

28. The trustee must serve a notice on a scheme member who has attained the retirement age of 65 but has not applied for claiming his accrued benefits. If the member responds to the approved trustee's notice and informs the

trustee that he would like to keep the benefits in the scheme, the trustee, when sending the Annual Benefit Statement, needs to request the member to indicate whether he wants to keep the benefits in the scheme in the following financial period and a copy of the statement has to be sent to the member again if he fails to reply. This is burdensome as members have to actively respond to the trustee of their preference on the treatment of their benefits annually.

29. In view of the issues highlighted above, we propose to clarify and streamline the processes by which benefits become treated as “unclaimed benefits” by –

- (a) setting out clearly the timeframe for MPF benefits to become unclaimed benefits (i.e. if the trustee cannot locate the scheme members concerned for six months);
- (b) removing the requirement for trustees to publish newspaper notices to locate the lost members while the MPFA will take steps through advertising and educational material to increase members’ awareness of the availability and content of the register maintained by MPFA, and the process for claiming unclaimed benefits;
- (c) requiring the trustees to report any newly identified unclaimed benefits and those unclaimed benefits that have been claimed by members to the MPFA on a quarterly basis; and
- (d) requiring the trustees to remind scheme members who have reached retirement age that they can apply for withdrawal of benefits and the trustee concerned should continue to retain the benefits for the member until the member applies for withdrawal of the benefits.

Disclosure of information by the MPFA

30. At present, the MPFA is not allowed to disclose to any person information it has obtained in the exercise and performance of functions except under certain specified circumstances. A review of the relevant provisions suggests that in certain circumstances the restriction may not be in the interest of the information subject or the public.

31. The general public, particularly prospective and existing scheme members, need certain information (e.g. fees and charges of the MPF constituent

funds) to help them to make investment decisions. The MPFSO at present does not specifically allow the MPFA to compile and disclose any comparative information to assist members for the purpose. Furthermore, on occasions, the MPFA has been requested by some parties (e.g. employees) to release their information to certain parties (e.g. the Labour Tribunal) to facilitate the processing of their cases for different purposes but such requests could not be entertained even if consent from the information subject has been obtained. The MPFA is also not able to disclose information which is already in the public domain (including court proceedings) or disclose information to the Official Receiver or liquidator to facilitate their discharge of duties. We propose to amend the MPFSO to enable the MPFA to disclose information in the above circumstances.

Consent to restructuring of MPF schemes

32. In scheme restructuring, some trustees may encounter difficulties in obtaining consent of scheme members, particularly when there are untraceable members. At present, the trustee will apply to the MPFA for consent by virtue of section 34B of MPFSO. However, the existing legislation is unclear as to whether the consent given by MPFA⁴ overrides the requirements to obtain members' consent and is binding on all parties concerned. We propose to amend the MPFSO to put that beyond doubt.

Enrolment and contribution requirements for persons who cease to be exempt from MPF legislation

33. Some persons who are exempt from the MPF legislation may cease to be exempt even though they remain in the same employment or as a self-employed person⁵. We propose to clarify that the enrolment and contribution requirements under sections 7, 7A and 7B of the MPFSO apply to the person as if his employment has begun on the first day he is no longer an exempt person. Similar arrangements are proposed in respect of exempt person who is a self-employed person.

⁴ Before consent is given to any application for restructuring of MPF schemes, the MPFA is required to be satisfied, amongst other things, that there are proper arrangements in place for transferring the accrued benefits of scheme members into the new schemes and that the interest of scheme members will be adequately protected.

⁵ For example, a person attaining the age of 18 whilst in the same employment/being self-employed; ceasing to be a member of an overseas retirement scheme whilst in the same employment/being self-employed; or ceasing to be a member of an MPF exempted ORSO scheme whilst in the same employment.

Serving of membership certificates and participation certificates

34. At present, if the trustees send membership certificates or participation certificates to the scheme members or employers by post, it must be of registered form. Ordinary post is much cheaper than registered post. Besides, ordinary post provides convenience to employees and employers as compared to registered post since they do not have to pick up any undelivered registered mail from the post office. We therefore propose to provide that membership certificates or participation certificates could also be sent by ordinary post to provide convenience to employees and employers and reduce administration cost of the MPF schemes.

(C) Other Technical and miscellaneous amendments

35. We propose to make a number of technical amendments to the MPF legislation relating to the approval of controllers of approved trustees; appointment of investment manager; minimum credit rating requirement for debt securities; eligibility of sub-custodians; undertakings given by trustees; non-refusal requirement of the trustees; encumbrance of scheme assets; the cancellation of approval of constituent funds and approved pooled investment funds; specification of purposes of public registers established under the MPFSO and rectification of the provisions regarding the eligibility conditions for MPF exemption for ORSO registered schemes. We also propose to make other miscellaneous amendments to rectify the inconsistencies between the Chinese and English texts of certain provisions and clarify the meaning of some provisions of the MPFSO.

LEGISLATIVE TIMETABLE

36. Subject to Members' views, we plan to finalise the Bill and introduce the Bill within the current legislative session.

**Financial Services Branch
Financial Services and the Treasury Bureau
March 2007**

MEMBERSHIP OF MPF SCHEMES OPERATION REVIEW COMMITTEE
(As at end 2006)

Chairman	Mr. Ronald ARCULLI	
MPFA		
Non-Executive Director	Mr. LEE Kai-ming #	
Chief Operating Officer (Enforcement)	Ms. Hendena YU	
Executive Director (Regulation & Policy)	Mr. Darren MCSHANE	
		<u>Alternate</u>
	Representative	
Employee Representatives		
The Federation of Hong Kong & Kowloon Labour Unions	Mr. LEE Kai-ming	Mr. SIN Kai Ming
Hong Kong Federation of Trade Unions	Mr. TING Kam Yuen	Mr. C.K. KWONG
Hong Kong Confederation of Trade Unions	Ms. CHEUNG Lai Ha	Ms. Mandy LI
Employer Representatives		
Employers' Federation of Hong Kong	Ms. Mary TUNG	Mr. Louis PONG
Hong Kong Institute of Human Resource Management	Ms. Edith LEE	Mrs. Monisa TAM
MPF Industry Representatives		
Hong Kong Trustees' Association	Ms. LAU Ka-shi	Ms. Rachel TSANG
The Hong Kong Association of Banks	Mr. Mark BAIN	Ms. FU Cindy Man Yee
The Hong Kong Federation of Insurers	Mr. Terry LO	Mr. Michael HUDDART
Hong Kong Investment Funds Association	Mr. Ken TAM	Ms. Sally WONG
The Law Society of Hong Kong	Mr. Duncan ABATE	
HKSAR Government		
Financial Services and The Treasury Bureau	Mr. Albert LAM	Mr. Ryan CHIU
Labour Department	Mr. Alan WONG Kwok-lun	
Secretary	Ms. Gabriella YEE	

Mr Lee Kai-ming ceased to be a non-executive director of the MPFA with effect from 17 March 2007.