For discussion on
8 November 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 September 2007, over 2.3 million employees and self-employed persons were enrolled in the MPF schemes, with total assets of the schemes amounting to over $257 billion. The MPF System is reviewed from time to time to ensure that it continues to serve the needs of the existing and potential scheme members. The present proposed amendments are recommended by the Mandatory Provident Fund Schemes Authority ("MPFA"). They cover different aspects of the operation, in particular the enforcement, of the MPF System, so as to better protect the interests of employees and scheme members.

Legislative Proposals

(a) Non-payment of mandatory contributions in non-enrolment cases

3. Under section 7(1) of the Mandatory Provident Fund Schemes Ordinance ("MPFSO"), every employer of a relevant employee is required to ensure that the 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 its employee in an MPF scheme throughout his employment. Under sections 7A(1) and 7A(2) of the MPFSO, it is the legal responsibility of the employer to make mandatory contributions to the MPF scheme for the employee.

4. However, where an employer has failed to enrol an employee in an MPF scheme and thus has not been making mandatory contributions for the employee, 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. To close this loophole and ensure that employees in non-enrolment cases will not be deprived of their entitlement to mandatory contributions, it is proposed to amend the MPF legislation to make it clear that an employer who does not enrol its relevant employee in an MPF scheme is still liable to pay mandatory contributions for the employee and such contributions become due to the MPFA by a prescribed due date. The amended legislation will provide for both criminal and civil routes of actions to deal with default contributions in respect of non-enrolled employees, similar to that stipulated under the existing legislation in respect of enrolled employees. An employer's obligation will cover mandatory contributions which would have been payable had the employee been enrolled in a registered scheme in accordance with section 7 of the MPFSO and this obligation will commence from 1 December 2000 irrespective of whether the employee is still in the employment of the same employer on the commencement date of the amendment. The legislative proposals will also introduce a mechanism to facilitate the depositing of the contributions received by the MPFA into an MPF scheme for the benefit of the employee concerned.

5. To facilitate effective enforcement, we also propose to amend the MPFSO so that in cases of non-enrolment or non-payment of mandatory contributions, the court will have a discretionary power to compel an employer to enrol its employees in an MPF scheme and to pay the outstanding contributions and contribution surcharges as appropriate. These measures are expected to enhance the deterrent effect against non-enrolment and non-payment of mandatory contributions.

(b) Increasing the maximum penalty for non-enrolment and non-payment of contributions

6. An employer who fails to enrol its employees in an MPF scheme in accordance with section 7 of the MPFSO or fails to make mandatory

contributions in accordance with section 7A of the MPFSO commits an offence under section 43B of the MPFSO and is liable, upon conviction, to a fine at level 6 ($100,000) and to imprisonment for 6 months on the first occasion, and to a fine of $200,000 and to imprisonment for 12 months on each subsequent occasion.

7. Some labour unions and legislators consider that the existing penalty provisions are not adequate in providing effective deterrence against non-compliant employers, particularly in view of the relatively low level of fines imposed by the courts in prosecution cases. They also hold the view that default in making MPF contributions is akin to default in wage payment, and hence the maximum penalty for default contributions should be adjusted upward to align with that for wage defaults under section 63C of the Employment Ordinance ("EO"), i.e. a maximum fine of $350,000 and imprisonment for three years.

8. The MPFA agrees that it is necessary to send a strong message to employers that they should enroll employees in MPF schemes and make MPF contributions on time. To achieve this purpose for providing stronger deterrence against possible breaches, we propose to increase the maximum penalty under section 43B of the MPFSO for failure to comply with the enrolment and contribution obligations to a fine of $350,000 and imprisonment for three years. After the adjustment, the maximum penalty under section 43B of the MPFSO will become on a par with that for wage defaults under section 63C of the EO.

(c) <u>Offence for failure of employers to remit the deducted wages as employee mandatory contributions</u>

9. Under section 7A(1) and (2) of the MPFSO, an employer is required to deduct from an employee's relevant income his MPF contributions, and pay the employee and employer mandatory contributions to the relevant MPF scheme before the contribution due date. However, the MPFA's enforcement experience indicates that it is not uncommon for employers to deduct mandatory contributions from the employees' relevant income without remitting the deducted sum to MPF schemes. Such act by employers severely jeopardises employees' interests, particularly if the employers later run into financial difficulties and are unable to settle the outstanding employee (and often employer) contributions. The employees not only lose the employer mandatory contributions to which they should be entitled but also the employee mandatory contributions that have been

deducted from their salaries[1].

10. The sanctions under the current MPF legislation against default contributions, however, do not distinguish between cases where an employer has deducted MPF contributions from an employee's wage for its own use and cases where no such deduction has been made. Concerns have therefore been expressed by some labour unions and legislators that, in non-payment of mandatory contribution cases, employers who have deducted employee mandatory contributions should be subject to a heavier punishment than employers who have not, so as to reflect the severity of the former type of cases which are by nature similar to illegal deduction of wages. Illegal deduction of wages is prosecutable under the EO. Section 32 of the EO prohibits employers from deducting from employee's wages except where allowed in specified circumstances. One of such circumstances is that the deductions are required or authorized to be made under any enactment.

11. In order to deter such unscrupulous acts by employers, we propose to impose a higher penalty on employers who do not remit the deducted employee mandatory contributions from employees' wages to the relevant MPF schemes. It is proposed that upon conviction, the employer will be liable to *a fine of $450,000* and to *imprisonment for four years*. The higher maximum penalty level proposed compared to that for default contributions where the employers have not made deduction from their employees' wages (i.e. *a fine of $350,000* and *imprisonment for three years* as explained in para.8 above) is prepared with reference to the maximum penalty for breaching section 32 of the EO (i.e. *a fine of $100,000* and *imprisonment for one year*).

(d) <u>Offence for providing false pay-records to employees</u>

12. Section 139 of the Mandatory Provident Fund Schemes (General) Regulation ("General Regulation") requires an employer to give monthly pay-records to its employees who are MPF scheme members. The pay-record should be given to the employee not later than 7 working days after the payment, or the last payment if there is more than one payment, of mandatory contributions during the month concerned.

[1] Where the insolvent employers deduct employees' wages for making employees' MPF contributions and default on these sums, such arrears of wages are already covered by the Protection of Wages on Insolvency Fund.

13. The pay-record contains information on the amount of relevant income of the employee, the amount of employer mandatory/voluntary contributions paid by the employer and the amount of employee mandatory/voluntary contributions deducted from the income of the employee, and the date on which these contributions are paid to the trustee of the MPF scheme. The contribution details contained in the pay-record can be used by the employee to verify if the employer has properly ascertained the amount of relevant income and correctly calculated the amount of employer contributions and the amount of employee contributions. It is also intended to serve as an evidence of payment of contributions by the employer to the trustee concerned.

14. There is concern that some employers, though giving monthly pay-records as required under the law, could deliberately provide false or misleading contribution details (e.g. by stating that contributions have been duly paid on a certain date when in fact no such payment has been made) to deceive their employees. To protect the interests of scheme members, it is proposed to create a new offence against the employer which, in a pay-record given to an employee, provides any information that it knows to be false or misleading in a material respect, or recklessly provides any information that is false or misleading in a material respect. The employer, upon conviction, is liable to a fine at level 6 and to imprisonment for one year on the first occasion and to a fine of $200,000 and to imprisonment for 2 years on each subsequent occasion. The new provision is modeled on section 43E of the MPFSO which sanctions a person for making a false or misleading statement in any document given to certain prescribed persons (i.e. the MPFA, a trustee, an auditor of a trustee or an auditor of a MPF scheme), but not including an employee.

(e) <u>Approval of controllers of approved trustees</u>

15. Trustees of MPF schemes play an important role in ensuring that MPF schemes are operated in compliance with the law and that the interests of scheme members are well protected. The MPF legislation provides that a trustee must first be approved by the MPFA if it intends to conduct MPF business. One of the eligibility requirements for a trustee company applying to conduct MPF business is that the MPFA is satisfied that the controllers of the company are suitable.

16. According to section 2 of the MPFSO, the following persons are controllers of an approved trustee:

(a) the chief executive officer and directors of the company;

(b) a person in accordance with whose instructions those directors are accustomed to act ("indirect controller"); and

(c) a natural person or another company who, directly or indirectly, controls at least 15% of the voting shares of the trustee ("minority shareholder controller").

17. Indirect controller and minority shareholder controllers are required to satisfy the same criteria as the chief executive officer and directors when a trustee company is first approved to carry on MPF business. Subsequent to the approval of the trustee, section 28 of the General Regulation provides that any new appointment of chief executive officer and directors in respect of the trustee requires the prior consent of the MPFA. However, no similar requirement for prior consent in respect of subsequent appointment of indirect controllers and minority shareholder controllers is stipulated in the MPF legislation. It is inconsistent and unreasonable that persons who become indirect controllers or minority shareholder controllers after initial approval of the trustee are not subject to scrutiny to ensure that they are suitable.

18. Moreover, once the MPFA has given consent to the appointment of a chief executive officer or director of the company under section 28 of the General Regulation, the MPFA is not empowered to withdraw the consent even if the person is no longer suitable to continue performing such role. For the better supervision of the trustees, the MPFA should be empowered to withdraw the consent previously given to any chief executive officers or directors as well as other types of controllers from continuing holding such positions if such persons are no longer suitable.

19. It is also envisaged that a person may have unknowingly become the controller of a trustee by virtue of his acquiring voting shares of an approved trustee exceeding the threshold of 15%. In that case, the person should be prohibited from exercising the voting rights conferred by the shares until and unless consent is given by the MPFA to the person to be a controller of the trustee.

20. To address the above issues, it is proposed to amend the MPF legislation to set out clearly the approval requirements in respect of indirect controller and minority shareholder controllers and the withdrawal of approval of controllers under specified circumstances. This seeks to

enhance the supervision of the trustees so as to better protect scheme members' interests.

Legislative timetable

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

Financial Services and the Treasury Bureau
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