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Panel on Financial Affairs

Meeting on 4 April 2011

Background brief on strengthening the regulatory regime for Mandatory Provident Fund intermediaries

Purpose

This paper provides background information on the proposal to strengthen the regulatory regime for Mandatory Provident Fund ("MPF") intermediaries, and summarizes the main concerns and views expressed by Members when relevant issues were discussed at Council meetings and the Panel on Financial Affairs ("FA Panel").

Background

2. The Mandatory Provident Fund Schemes Ordinance (Cap. 485) ("MPFSO") was enacted in 1995 to provide a statutory framework for the establishment of mandatory, privately managed retirement schemes for the retirement protection of the general workforce. It is supplemented by subsidiary legislation passed in 1998, 1999 and 2000. The MPF System was launched in December 2000. Since 2000, seven sets of legislative amendments proposed by the Government have been endorsed by the Legislative Council. They include amendments to raise the penalty for default on contributions, to streamline and improve the overall operation of the MPF system, and to introduce a system for employees to choose their own schemes.

3. The Legislative Council enacted the Mandatory Provident Fund Schemes (Amendment) Bill 2009 in July 2009, which, among other things, allows employees to transfer accrued benefits derived from their employee's mandatory contributions during their current employment from a contribution account under a registered scheme on a lump-sum basis to another MPF scheme of their own choice once per calendar year, or more than once per calendar year if the governing rules of the relevant scheme as determined by the trustee concerned allow for more frequent transfers by the scheme

members. The arrangement is commonly known as the "Employee Choice Arrangement" ("ECA").

4. The Monetary Provident Fund Schemes Authority ("MPFA") announced on 30 September 2010 that in order to enhance protection of the interests of employees, the Authority proposed to reinforce the existing regulatory regime of MPF intermediaries through legislation and that the Government had agreed to the proposal. As the legislative process took time, the implementation of the ECA would have to be deferred.

Existing regulatory arrangements in respect of MPF intermediaries

5. While MPFA has a primary responsibility for supervising approved trustees, the Authority works with other financial regulators in overseeing MPF products and MPF intermediaries to ensure efficient and effective operation of the MPF System. MPFA uses a decentralized and coordinated approach in regulating MPF intermediaries, relying on the three financial regulators in Hong Kong, namely the Hong Kong Monetary Authority, the Securities and Futures Commission and the Insurance Authority, for the supervision of those MPF intermediaries falling under their respective regulatory regimes. MPFA acts as the lead regulator and coordinator in the regulation of MPF intermediaries. The four regulators have signed a Memorandum of Understanding Concerning the Regulation of MPF Intermediaries ("MOU"), which took effect on 1 January 2004, to ensure conformity and effectiveness in regulatory approach.

6. The term "MPF intermediaries" is not present in the MPFSO. According to the MOU, “MPF intermediaries” means those persons who are engaged in: (a) selling MPF schemes; or (b) advising clients on constituent funds or underlying approved pooled investment funds of MPF schemes[1]. Currently, all MPF intermediaries have to be registered with MPFA and

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[1] It is also mentioned in the MOU that –

The term "MPF intermediary" is used in the most expansive sense, including an individual (employee/agent/representative), a sole proprietor, a partnership, or a corporation and its directors who are responsible for the supervision of the selling/advising activities of MPF schemes. Unless otherwise specified, the term "MPF intermediary" refers to individual, firm, partnership, corporation and its directors.

The term "MPF intermediary" does not include certain professionals (such as lawyers, professional accountants or actuaries) whose act of giving advice is wholly incidental to the practice of their profession.

"MPF intermediaries" includes those supervised by one or more of the following regimes:

(a) Securities and Futures Commission regime – as licensed corporations or licensed representatives licensed/deemed to have been licensed to carry on Type 1 (dealing in securities) and/or Type 4 (advising on securities) regulated activities;

(b) Insurance Authority regime – as authorized insurers eligible to carry on long term business or their employees, authorized insurance brokers or appointed insurance agents eligible to engage in long term business, or their registered Chief Executives/registered Responsible Officers/Technical Representatives; and

(c) Monetary Authority regime – as authorized institutions or their staff.

who are involved in selling MPF schemes or advising clients on constituent funds or underlying approved pooled investment funds of MPF schemes.

comply with the Code of Conduct for MPF Intermediaries made by the MPFA. As specified in the Code of Conduct, breach of any of the requirements of this Code will, in the absence of any extenuating circumstances, reflect adversely on the fitness and properness/suitability of the representative and/or the corporation concerned to remain as an MPF intermediary. A description of the existing regulatory framework for MPF intermediaries is available in the Code of Conduct and is reproduced in **Appendix I**.

Concerns and views expressed by Members

Council meetings

7. At the Council meeting on 9 June 2010, Hon WONG Kwok-kin raised an oral question about the ECA, enquiring, among others, whether and how the relevant authorities would strengthen the regulation of MPF investment products as well as the regulation of MPF intermediaries to safeguard the interests of employees in view of the implementation of the ECA scheduled for 2011. In reply, the Secretary for Financial Services and the Treasury (SFST) advised that in preparing for the implementation of the ECA, MPFA was drawing up relevant guidelines for intermediaries, which would require them to explain clearly to clients the contents of different schemes and fund types, including fees, investment objectives, the risk levels, and so on, when selling MPF schemes or funds and assist the latter in choosing appropriate schemes and funds for making the transfer based on their investment objectives and risk tolerance level after taking into account all the relevant information. Furthermore, MPFA had made the Best Practice Note for MPF Trustees to guide trustees on how the promoters of their MPF schemes should be supervised, in order to ensure that their MPF intermediaries would market and sell MPF schemes and products properly.

8. At the Council meeting on 1 December 2010, a motion moved by Hon WONG Kwok-kin on "Comprehensively reviewing the Mandatory Provident Fund Scheme" was passed with amendments. As per the terms of the motion passed (**Appendix II**), the Council urged the authorities to comprehensively review the MPF System and further improve the relevant mechanisms, so as to protect the retirement life of all people; and the relevant review should seek to, among others, strengthen the regulation of MPF investment products and regularly review the sales practices adopted by intermediaries.

9. At the Council meeting on 16 March 2011, Hon KAM Nai-wai raised an oral question on the MPF System, enquiring about the number of approved trustees, the regulation of the management and administrative fees of MPF Schemes, the progress of the preparatory work for the implementation of the

ECA, and the Government's consideration of the establishment of a universal retirement protection scheme. According to SFST's reply, the Administration and the MPFA are preparing legislative proposals to strengthen the regulation of MPF intermediaries and will brief the FA Panel and commence consultation work in April 2011. The Administration expects to introduce the relevant Bill into the Legislative Council in 2011 with a view that the ECA can be implemented as soon as possible in 2012. In addition, the MPFA have commenced the preparatory work for implementation of the ECA, and this includes ensuring the alignment of the various systems of MPFA and trustees, strengthening MPF investment education to assist employees to make choices that suit their needs, and strengthening the training and regulation of MPF intermediaries.

Panel on Financial Affairs

10. When the FA Panel discussed the policy initiatives for 2010-2011 on 21 October 2010, SFST advised that as the ECA would put employees as the direct targets of marketing and sale activities by MPF intermediaries in future, the Administration would take forward MPFA's proposal to put in place a statutory framework for the regulation of MPF intermediaries, with a view to better protecting the interest of MPF scheme members. Some Members expressed concern about the delay in implementing the ECA, but there was a view that the initiative was important in providing a legal basis for instigating disciplinary actions against practitioners' misconduct.

Latest development

11. The Administration will brief the FA Panel on the proposal to strengthen the regulatory regime for MPF intermediaries at the Panel meeting on 4 April 2011.

Relevant papers

12. The relevant papers are available at the following links:

Oral question raised by Hon KAM Nai-wai at the Council meeting on 16 March 2011
http://www.info.gov.hk/gia/general/201103/16/P201103160200.htm

Motion debate on "Comprehensively reviewing the Mandatory Provident Fund Scheme" at the Council meeting on 1 December 2010 (Hansard, page 136-234)
http://www.legco.gov.hk/yr10-11/english/counmtg/hansard/cm1201-translate-e.pdf

Minutes of FA Panel Meeting on 21 October 2010 (paragraphs 1-4)
http://www.legco.gov.hk/yr10-11/english/panels/fa/minutes/fa20101021.pdf

Press Release by MPFA on 30 September 2010
http://www.mpfa.org.hk/english/quicklinks/quicklinks_pr/press_release_detail.asp?press_id=2271

Oral question raised by Hon WONG Kwok-kin at the Council Meeting on 9 June 2010 (Hansard, page 42-47)
http://www.legco.gov.hk/yr09-10/english/counmtg/hansard/cm0609-translate-e.pdf

Research Paper by the Research Division of the Secretariat on "Comprehensively reviewing the Mandatory Provident Fund Scheme" (Chinese version only)
http://www.legco.gov.hk/yr10-11/chinese/sec/library/1011rn11-c.pdf

Report of the Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2009
http://www.legco.gov.hk/yr08-09/english/bc/bc03/reports/bc030708cb1-2025-e.pdf

Code of Conduct for MFP Intermediaries
http://www.mpfa.org.hk/english/leg_reg/leg_reg_cod/files/code_of_conduct-eng.pdf

Memorandum of Understanding Concerning the Regulation of MPF Intermediaries
http://www.mpfa.org.hk/english/leg_reg/leg_reg_mous/files/mou_int.pdf

Website of MPFA on supervision of intermediaries
http://www.mpfa.org.hk/english/super/super_si/super_si.html

Council Business Division 1
Legislative Council Secretariat
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Extract from the Mandatory Provident Fund Schemes Authority's Code of Conduct for MPF Intermediaries

2. Regulatory Framework

2.1 This Code is developed based on the decentralized approach to the regulation of MPF intermediaries. The MPFA, rather than licensing MPF intermediaries directly, relies on the existing regulatory regimes, i.e. the MA, the IA (including the SROs) and the SFC, as far as practicable for the licensing and supervision of MPF intermediaries, with the MPFA acting as the lead regulator and coordinator.

2.2 The MPFA, in approving an application as an approved trustee, would impose the following conditions on the approval of the trustee (pursuant to section 20(8) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485) ("the Ordinance"):

(a) In relation to the administration of any registered scheme by an approved trustee -

(i) the trustee shall take all reasonable steps in the circumstances to ensure that no person other than a registered MPF intermediary should induce or seek to induce another to become a participating employer or a member of the scheme;

(ii) the trustee must immediately report to the MPFA any breach of this condition of which it becomes aware;

(iii) in response to any breach of this condition, the MPFA may require the trustee to take such steps as the MPFA shall deem appropriate;

(iv) this condition does not apply to the publishing of any such inducement through advertisements or marketing materials to which the Securities and Futures Ordinance (Cap. 571) applies or to any inducement that is made outside the course of employment or without the prospect of reward for such inducement.

(b) The trustee must obtain undertakings from the promoters of those MPF schemes under its trusteeship. The promoter of an MPF scheme is to undertake to the trustee that it will, as far as reasonably practicable, ensure that MPF intermediaries selling/advising on the MPF scheme will comply with this Code.

2.3 In addition, the MPFA, in registering an MPF scheme (pursuant to section 21 or 21A of the Ordinance), would require the promoter of the scheme to provide an undertaking to the MPFA that it would only use registered MPF intermediaries to sell/advise on the scheme.

2.4 Under the Ordinance, the MPFA is responsible for supervising the activities of approved trustees. Being the central party to an MPF scheme, the approved trustee has a duty to use its best endeavours to supervise and exercise proper control over the persons appointed or engaged for the purposes of selling or advising on the MPF scheme (pursuant to section 43 of the Mandatory Provident Fund Schemes (General) Regulation).

2.5 The promoter, in turn, is responsible for monitoring and supervising the activities of MPF intermediaries appointed or engaged by the promoter for the purposes of selling or advising on the MPF scheme. Promoters breaching the undertaking would be required to rectify any deficiencies in their systems and controls. For those who fail to do so, the relevant trustee should take steps to terminate the contractual relationship with the promoter.

2.6 No person shall engage in selling MPF schemes or advising clients on constituent funds or underlying approved pooled investment funds of MPF schemes unless he is registered with the MPFA as an MPF intermediary.

2.7 To meet basic registration requirements, an applicant must be supervised by one or more of the three financial regulatory regimes – the MA, the IA and the SFC. An individual applicant must pass an MPF intermediaries examination recognized by the MPFA. In addition, the applicant must satisfy the MPFA that he is fit and proper to be registered as an MPF intermediary.

2.8 Generally speaking, the MPFA, in registering MPF intermediaries, is not likely to be satisfied that an applicant is a fit and proper person, if the person (whether in Hong Kong or elsewhere):

(a) has been found by a court to have acted fraudulently or dishonestly, has been convicted of a criminal offence, or is the subject of unresolved criminal charges which are of direct relevance to fitness and properness;

(b) is an undischarged bankrupt, is currently subject to bankruptcy proceedings, or is a bankrupt who has recently been discharged;

(c) has been denied membership/registration of any professional/regulatory body due to reasons other than insufficient qualification/experience, or disqualified/censured/disciplined by any professional/regulatory body due to serious misconduct;

(d) has failed to comply with the Continuing Professional Development ("CPD") requirement during his period of registration as an MPF intermediary.

2.9 For MPF corporate intermediaries intending to give advice on securities, they would need to be licensed by the SFC or registered with the SFC to carry on Type 1 (dealing in securities) and/or Type 4 (advising on securities) regulated activities.

2.10 For MPF individual intermediaries intending to give advice on securities, they would need to be licensed representatives licensed by the SFC (if they are engaged by a licensed corporation) or their names have been entered in the Register maintained by the HKMA (if they are engaged by an authorized institution) to carry on Type 1 (dealing in securities) and/or Type 4 (advising on securities) regulated activities.

2.11 For MPF intermediaries (corporate and individual) intending to give advice on insurance policies, they or their employers would need to be registered or authorized under the IA regime.

2.12 Upon registration with the MPFA, MPF intermediaries are issued with Mandatory Provident Fund intermediary certificates ("MPF certificates"). Prior to issuing MPF certificates, Mandatory Provident Fund intermediaries cards ("MPF cards") would be issued.

2.13 MPF certificates will only be issued to MPF individual intermediaries who are sponsored by MPF corporate intermediaries.

2.14 There is clear identification on the MPF card/certificate indicating whether the MPF intermediary is:

- permitted to sell MPF schemes without rendering specific investment advice;
- permitted to advise on securities;
- permitted to advise on insurance policies; or
- permitted to advise on securities and insurance policies.

2.15 A register bearing particulars of registered MPF intermediaries ("MPF intermediaries register") is available for inspection at the office of the MPFA. Enquiries can also be made through an enquiry hotline.

2.16 An MPF corporate intermediary should lodge with the MPFA an annual return within the stipulated timeframe.

2.17 Upon registration with the MPFA, all MPF intermediaries, whether corporate or individual, are required to fulfill the requirement in respect of CPD as stipulated in the Guide to Continuing Professional Development for MPF Intermediaries in order to remain fit and proper to be registered as MPF intermediaries.

2.18 A committee ("MPF Intermediaries Regulation Coordinating Committee"), consisting of representatives from the HKMA, the IA, the SFC, the MPFA (together "four regulators") and the Financial Services and the Treasury Bureau, is established to coordinate the regulation of MPF intermediaries. The main functions of the Committee are to define the boundaries and delineate the responsibilities of the four regulators; to help coordinate inspection and enforcement actions; to discuss risk issues; to advise on disciplinary actions; and, generally, to keep the regulatory framework under constant review.

2.19 To ensure compliance with the Code, the MA, the IA and the SFC will carry out routine inspection visits to MPF corporate intermediaries that are supervised by them.

2.20 The public will be encouraged to refer all complaints to the MPFA.

2.21 The IA (and the SROs), the MA and the SFC will be responsible for carrying out enforcement and disciplinary actions on MPF intermediaries supervised by them. In respect of MPF intermediaries who are employees of authorized insurers or authorized institutions, the IA and the MA will rely on the authorized insurers and the authorized institutions respectively to ensure suitability of their employees who are involved in the selling/advising activities of MPF schemes and to carry out enforcement and disciplinary actions on MPF intermediaries that are acting on their behalf.

2.22 All MPF intermediaries must be fit and proper to remain registered with the MPFA.

Source:

http://www.mpfa.org.hk/english/leg_reg/leg_reg_cod/files/code_of_conduct-eng.pdf

Appendix II

(Translation)

Motion on
"Comprehensively reviewing the Mandatory Provident Fund Scheme"
moved by Hon WONG Kwok-kin
at the Legislative Council meeting
of Wednesday, 1 December 2010

Motion as amended by Hon CHAN Kin-por, Hon Ronny TONG Ka-wah and Hon Paul CHAN Mo-po

That, enormous changes will occur to the population structure of Hong Kong in the future, and the ratio of persons who are aged 65 and above to the population will substantially increase to 26% by 2036; this not only indicates the gravity of population ageing in Hong Kong in the future, but also foretells the public's urgent demand for comprehensive retirement protection; yet, there is at present no retirement protection system in Hong Kong that benefit all people, and after nearly 10 years since its implementation, the Mandatory Provident Fund ('MPF') Scheme is still unable to achieve the objective of protecting people's retirement life; in this connection, this Council urges the authorities to comprehensively review the MPF Scheme and further improve the relevant mechanisms, so as to protect the retirement life of all people; the relevant review should include:

(a) to implement universal retirement protection, with tripartite contributions from the Government, employers and employees, so as to extend the coverage of protection to all Hong Kong people;

(b) to abolish the mechanism whereby employers' contributions under the MPF Scheme are used to offset severance payments and long service payments, and retain Hong Kong employees' rights to severance payments or long service payments under the relevant provisions of the Employment Ordinance, so as to provide employees with better retirement protection;

(c) to implement a system of 'one lifelong account', establish portability of MPF accounts, and require trustees to introduce a simple and easy to understand method to inspect accounts similar to that of 'bank books', so as to enable employees to peruse information on contributions, returns, etc. at any time;

(d) to lower MPF management fees and administration fees by, for example, streamlining the management and administrative procedures of MPF schemes and reducing the operating costs of MPF on the premise of not affecting MPF scheme members' interests, so as to create room for lowering administration fees, and at the same time enact legislation to require trustees to set out the actual amounts of management fees in the annual reports of the years concerned, so as to protect the actual amounts of MPFs received by employees upon retirement from not being drastically eroded;

(e) to implement totally unrestricted choices for employees under the MPF Scheme, allowing employees to choose trustees for both employers' and employees' MPF contributions, and at the same time, through publicity and education, enable employees to understand that they may transfer their MPF contributions according to the levels of risks they can bear;

(f) to strengthen the regulation of MPF investment products and regularly review the sales practices adopted by intermediaries;

(g) to review the appropriateness of the existing minimum and maximum levels of income, including that the minimum level of income should be higher than the minimum wage, as well as the percentages of contributions, so as to ensure that the amounts of MPFs are adequate to meet post-retirement expenditure;

(h) to step up law enforcement to combat the situation of default in contributions, including sentencing employers who default on contributions to immediate imprisonment, and considering blacklisting the companies concerned in the tendering exercises for government services as a form of penalty, etc.; and

(i) to reform the Occupational Retirement Schemes ('ORSO') system, requiring employers adopting ORSO schemes to provide their employees with accrued benefits not less than those under the MPF Scheme;

(j) to conduct comprehensive public consultation on the effectiveness and various aspects of the MPF Scheme, given that it has already been implemented for 10 years; and

(k) when implementing universal retirement protection, to conduct public consultation on the specific proposal;

(l) to increase the ceiling of employers' monthly contributions to employees' MPFs to HK$2,500 a month per person, so that employers can make more active commitment to employees' retirement life; and

(m) to correspondingly increase the maximum tax deduction for employees' mandatory contributions to MPF schemes to HK$30,000 each tax year, so as to strengthen employees' protection.