The Hong Kong Federation of Insurers
香港保險業聯會

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By Fax (2978 7569) and Email (bc_03_15@legco.gov.hk)

The Hon. TAM Yiu-chung, GBS, JP
Chairman
Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2015

Dear The Hon. Tam

Mandatory Provident Fund Schemes ("MPF") (Amendment) Bill 2015

Thank you for inviting The Hong Kong Federation of Insurers ("HKFI") to provide comments on the subject Bill.

The HKFI, together with our 15 Member Companies who are MPF Administrators constituting about 90% of market share, is supportive of the introduction of Default Investment Strategy ("DIS") in principle. However, the HKFI cautions that the "opt-out" approach to DIS will affect 554,200 default scheme members (20% of 2.8 million scheme members) contributing $620 million to MPF annually, with an aggregate net asset value of $6 billion (as at 31 March 2015).

Under the current default arrangement offered by various providers, over 50% of the default funds are invested in conservative funds with low risk. Taking an "opt-out" approach will expose the affected scheme members to market risks without their **explicit** consent. It is also noteworthy that some of the providers are not 100% certain as to who the active or passive default scheme members are because the member records were not required to be retained systematically in that way when the MPF System was launched in 2000.

In this regard, the insurance industry would like to explain to your Committee the risks of the "opt-out" approach. Alternatively, we propose an "opt-in" approach which can give a better, safer and fairer option for all parties concerned.

Background

1. The LegCo Brief provides that "for an existing default scheme member who has not given investment instructions for all his accrued benefits, a trustee is required to notify him in writing that, if no reply has been received from the member for all or part of those benefits after the expiry of a 42-day opt-out period, such benefits will be transferred to and invested into the DIS within 14 days after the opt-out period…"

Risks of "opt-out" approach

2. As we all know, most Hong Kong people including scheme members are incredibly busy and may overlook the trustee's notice on the opt-out option before the expiry period. For those scheme members who have originally invested in conservative funds but have not opted out from DIS, they would be exposed to the market risks in the absence of his/her **explicit** consent. Such arrangement would be highly controversial and may be subject to 'outcry' later on once implemented, which would put the trustee in a very difficult situation although they are following the approved process in accordance with the law (if passed).

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For example, a scheme member Mr Chan has all along invested all his accrued benefits $200,000 in an MPF Money Market Fund with lowest risk and also lowest return. After the Bill has been enacted, Mr Chan who, for whatever reasons, has overlooked the notice from the trustee and his accrued benefits are subsequently transferred to a DIS Fund with 60% of underlying investment in equity. Due to unforeseen market volatility, the average equity price has dropped by 40% and the net asset value of his accrued benefits has subsequently dropped by 24% to $152,000.

3. Not until these scheme members have suffered from financial losses, would they start to realize that they are required to opt out from DIS if they choose to continue with the conservative funds. But that would be too late for them to do anything to avoid the loss.
4. The industry considers that the Government should not be empowered to take money out of funds actively without scheme members' **explicit** consent to prevent substantive potential losses for the latter which will inevitably lead to massive complaints.

Merits of "opt-in approach"

5. The insurance industry recommends that an "opt in" approach to DIS be adopted. With "opt-in" approach in place, the trustee(s) will be obliged to seek the **explicit** consent of the scheme members to transfer and invest their accrued benefits in the DIS.
6. As such, scheme members will have the opportunity to make an **informed** decision after considering the pros and cons of DIS prior to opting in, or not, to transfer their accrued benefits and invest into the DIS.
7. Even if individual scheme members may eventually suffer from financial losses due to market volatility, the opt-in option is based on an **informed** decision of the scheme members made.
8. The key element to the success of DIS is public education by the MPF Authority, in collaboration with industry associations. More transparency on how the DIS works, the pros and cons of opting-in/-out and the possible outcome will be welcomed by the scheme members. And it may help arouse their interest in taking up more ownership of their MPF schemes. After all, DIS should follow the free choice of scheme members.

We once again thank you for the opportunity to share with you our genuine concerns on this subject and to suggest a practical solution. And we look forward to further dialogue with the MPF Authority and the Government on the proper way forward. In the meantime, if there is any further information we can provide, please do not hesitate to let us know.

Yours sincerely

Wim Hekstra
Chairman
Retirement Schemes Working Group
Life Insurance Council ("LIC")

cc: The Hon. K P Chan, JP
Mr John Leung, JP, Commissioner of Insurance
LIC Councillors
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