LC Paper No. CB(1)967/17-18(03)

Proposed Tax Deduction for Deferred Annuity Premium and MPF Voluntary Contribution (MPF VC)

Financial Services and the Treasury Bureau

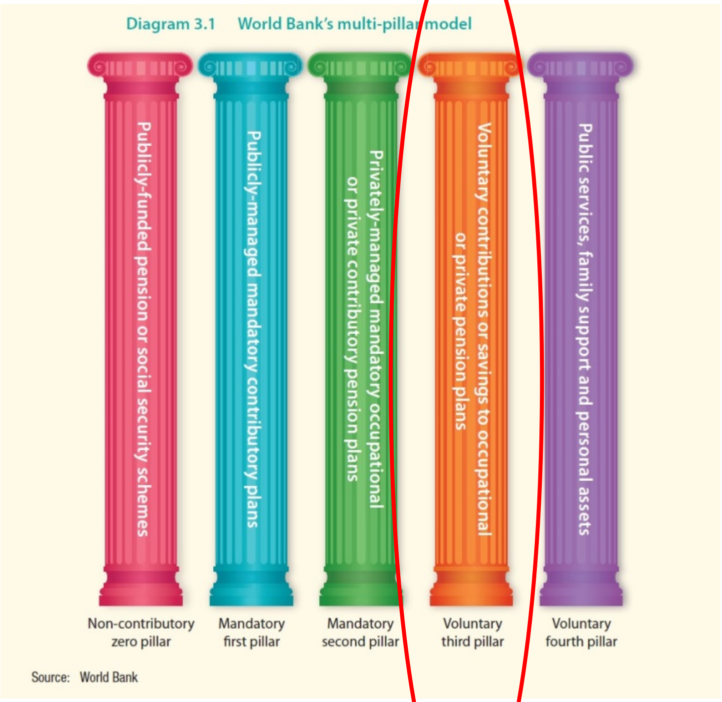
15 May 2018

The 2018-2019 Budget

- To encourage the development of the deferred annuity market, thereby **offering more options to people in making financial arrangements for retirement**, I will ask the Insurance Authority to issue guidelines, and enable all deferred annuity products available in the market meeting the guidelines to enjoy tax concessions … … the proposed tax concessions will be applicable to MPF voluntary contributions.

Policy Considerations

- MPF as 2nd pillar: mandatory, rigid
- World Bank: voluntary, flexible and discretionary 3rd pillar to compensate for rigidities in the design of other pillars
- To address old age risks:
  - financial discipline, early saving for retirement protection, and phased withdrawal of savings after retirement
  - need a basket of tools for retirement planning



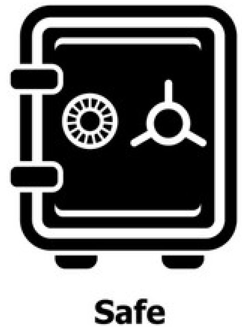
MPF VC

- 2017: out of the $68.99 billion total MPF contributions received, $3.6 billion were voluntary contributions
- Tax incentive to encourage scheme members to make more contributions for retirement planning in addition to the current mandatory contributions

Proposed Implementation Details

- Trustees will provide “Tax Deductible Voluntary Contribution Account” (TVC) under each MPF scheme
- All existing MPF Mandatory Contribution preservation requirements will apply to the accrued benefits in the TVC account
- Employees or self-employed persons can open a TVC account with any MPF trustees
- Trustees will issue TVC annual account statement to employees and self-employed persons for tax filing
- Propose to allow scheme members of Occupational Retirement Schemes (ORSO schemes) who are exempted from MPF to open TVC account
- TVC account can be opened with any MPF trustees of scheme members’ choice
- Considerations:
  - simplifying administrative work and reducing costs of employers and trustees
  - enhancing competition among trustees
  - encouraging employees and self-employed persons to make additional savings

Mandatory Contribution

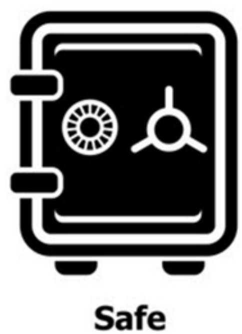


Existing tax deduction limit of $18,000

Deducted from salary

Voluntary Contribution

Tax Deductible Voluntary Contribution



Tax deduction limit of $36,000

If there is no separate **TVC** account, it will involve a lot of administrative work to allow scheme members to choose whether they would like to subject their VC to the preservation requirement for enjoying the tax deduction. Apportioning **tax deductible and non-tax deductible contributions** within one account will also create tedious administrative work

Annuities

- An annuity is a long-term insurance contract under which accumulated savings will provide stable stream of income to policyholders over a period of time
- "Class A - Life and annuity" of Classes of Long Term Business in the Insurance Ordinance (Cap. 41)
- Turning assets into a stable stream of cashflow, usually in monthly payments. Part of each payout comes from the principal
- The number of annuity policies in force has increased 88.16% from 63,420 in 2012 to 119,334 in 2016 and the amount of premiums has increased 189.83% from HK$2,941.2 million in 2012 to HK$8,524.6 million in 2016

Annuities

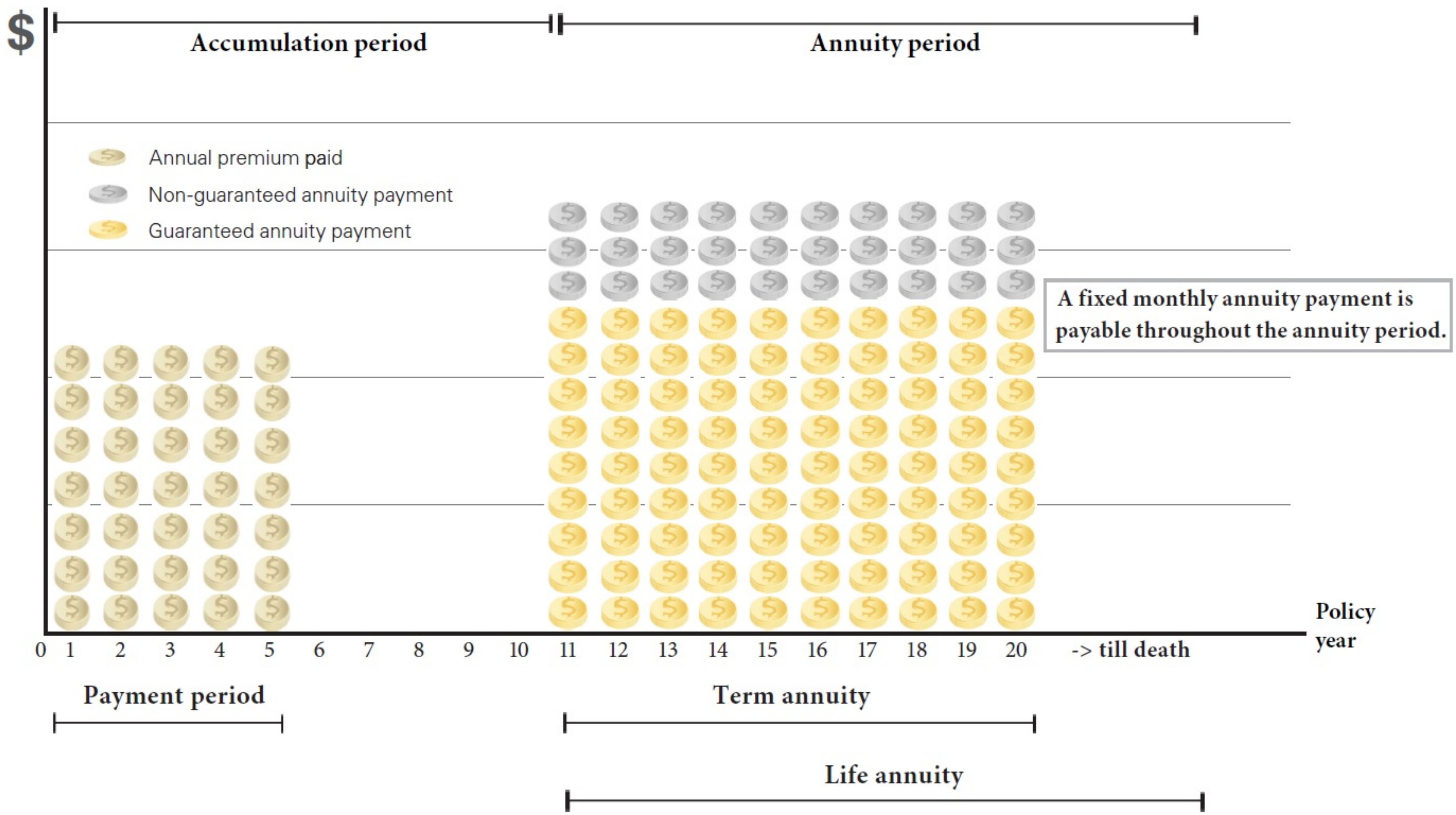
- Life annuity: annuity period until death
- Term annuity: limited annuity period such as 15 or 20 years
- Immediate annuity: insurance companies receive a lump sum payment from policyholders in return for immediate regular payouts from the next month
- Deferred annuity: premium payments and accumulation of the capital during the accumulation period, cash payouts afterwards

Annuities

- Annuity is not suitable for all persons. The following factors should be considered :

  - liquidity needs
  - bequest motive
  - financial discipline
  - other alternatives

Illustration of Deferred Annuities



Deferred Annuities

- Allow policyholders to transfer investment risk and longevity risk (if the annuitization phase is sufficiently long) to insurance companies

- Considerations:
  - financial discipline
  - choice for tax incentivized savings
  - no overlapping with HKMC's immediate annuity

Deferred Annuities

- Premiums paid for deferred annuity products that satisfy a set of criteria set out in the guidelines to be issued by the Insurance Authority (IA) will be eligible for tax deduction

- Criteria:
  - minimum total premium of $180,000 and minimum payment period of 5 years
  - minimum annuity period of 10 years
  - annuitization at the age of 50 or beyond
  - disclosure requirements
    - ✓ Internal Rate of Return
    - ✓ clear presentation of the guaranteed payment (minimum at 70%) and variable payment
    - ✓ clear separation of premiums of all riders (e.g. premium waiver for death or disability during payment period) from eligible annuity premiums

Tax Deduction

- Maximum tax deductible limit per year:
  - $36,000 per taxpayer
  - aggregate limit for MPF VC and deferred annuity premium

- Public education and point-of-sale conduct:
  - IA to publish a list of eligible deferred annuity products on its website
  - IA and MPFA to collaborate with the Investor Education Centre and the industry on public education campaigns
  - IA and MPFA to continue to closely monitor the point-of-sale conduct of intermediaries.

Illustrations using new salary tax bands

	A Single, monthly salary $15,000	B Single, monthly salary $20,000	C Single, monthly salary $30,000	D Single, monthly salary $60,000	E Married, 1 child, monthly salary $60,000 Spouse not working
Income	180,000	240,000	360,000	720,000	720,000
Less: deduction (MPF mandatory contribution)	9,000	12,000	18,000	18,000	18,000
Less: Allowances	132,000	132,000	132,000	132,000	264,000 120,000
Net Chargeable Income	39,000	96,000	210,000	570,000	318,000
Tax payable (A)	780	3,760	17,700	78,900	36,060

	A Single, monthly salary $15,000	B Single, monthly salary $20,000	C Single, monthly salary $30,000	D Single, monthly salary $60,000	E Married, 1 child, monthly salary $60,000 Spouse not working
Income	180,000	240,000	360,000	720,000	720,000
Less: deduction (MPF mandatory contribution)	9,000	12,000	18,000	18,000	18,000
Less: deduction (MPF VC or premiums for deferred annuities)	9,000*	12,000*	18,000*	36,000	36,000
Less: Allowances	132,000	132,000	132,000	132,000	264,000 120,000
Net Chargeable Income	30,000	84,000	192,000	534,000	282,000
Tax payable (B)	600	3,040	14,880	72,780	29,940
Tax savings (A) – (B)	**180**	**720**	**2,820**	**6,120**	**6,120**

* For scenarios A, B and C, it is assumed that given his relatively low income, the income earner will not make claims with the full tax deductible amount for MPF VC or deferred annuity premium.

Implementation Timetable

Time frame	Remarks
May 2018	Consultation with LegCo Panel on Financial Affairs
Q4 2018	Introduction of the amendment bill into LegCo
Early 2019	Passage of the bill / publication of the list of eligible products on IA's website
From early 2019	Publicity and education programmes by IA/MPFA and the industry
From assessment year 2019/20	Tax deduction to take effect

Q&A