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Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2021

Background brief

Purpose

This paper provides background information on the Mandatory Provident Fund Schemes (Amendment) Bill 2021 ("the Bill"). It also summarizes the major views and concerns expressed by Members of the Legislative Council ("LegCo") on issues relating to the development of a common electronic platform for the administration of Mandatory Provident Fund ("MPF") schemes ("eMPF Platform") in recent years.

Background

The Mandatory Provident Fund System

2. The MPF System is a mandatory, privately-managed and fully-funded pension system established under the Mandatory Provident Fund Schemes Ordinance (Cap. 485) ("MPFSO") and was launched in December 2000 to provide retirement protection to the working population, complementary to other pillars of the retirement protection framework. Employees and self-employed persons are required under MPFSO to join a registered MPF scheme selected by the employers or self-employed persons (as the case may be) and make choice from a range of constituent funds available under the scheme for investment of contributions. All provident fund schemes intend to be operated as MPF schemes must be registered with the Mandatory Provident Fund Schemes Authority ("MPFA"), and registered MPF schemes must be operated by MPF trustees approved by MPFA.

3. According to the Administration, as at May 2021, there were about 4.5 million scheme members enrolled into MPF schemes chosen by around

310 000 participating employers. The 14 approved trustees of the 27 MPF schemes administer some 10 million accounts of the scheme members either internally or through third-party administrators, involving 12 scheme administration platforms with different scheme administration processes of varying standards. The multiple business models, data standards, process designs and administration system infrastructure have made it difficult to achieve standardization and economies of scale. Moreover, among the around 30 million MPF administration transactions (e.g. enrolment of scheme members, collection and allocation of contributions, recovery of outstanding contributions, handling transfers between schemes and fund switches within schemes, and administration of withdrawals of accrued benefits) per year, more than 65% are paper-based. All these have contributed to the high administration costs of the MPF System.

<u>Development of a centralized electronic platform for the administration of Mandatory Provident Fund registered schemes</u>

4. The development of the eMPF Platform was an initiative in the Chief Executive ("CE")'s 2017 Policy Address delivered in January 2017. The Administration then considered that the eMPF Platform, which provided a common, integrated electronic platform to facilitate the standardization, streamlining and automation of MPF scheme administration processes, would enhance the operational efficiency of MPF schemes and achieve cost savings, thereby would provide more room for reduction in the administration fee of MPF funds.

5. The Administration introduced the Mandatory Provident Fund Schemes (Amendment) Bill 2019[1] into LegCo in 2019 to empower MPFA to establish a wholly-owned subsidiary (i.e. the eMPF Platform Company Limited,[2] hereafter referred to as "the Company") as a legal entity for owning and operating the eMPF Platform. The Administration has so far committed over $4.9 billion of public money to fund the hardware and software development and maintenance of the eMPF Platform, and as seed money to support the initial years of operation of the Company.

6. According to the Administration, in order to pave the way for the launch and smooth operation of the eMPF Platform, it is necessary to provide proper

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1 The Mandatory Provident Fund Schemes (Amendment) Bill 2019 was gazetted in June 2019, and passed by the Legislative Council at the meeting of 17 July 2020.

2 The eMPF Platform Company was set up in March 2021 under section 6DA of the Mandatory Provident Fund Schemes Ordinance (Cap. 485) with the primary objectives to develop, build and operate the eMPF Platform.

legal basis for the designation of the eMPF Platform as the common gateway for scheme administration processes in the MPF System, and delineate the respective roles, functions, powers, responsibilities and the interface of the Administration, MPFA, the Company, trustees and other stakeholders. Details for the implementation of the eMPF Platform have to be made through introducing legislative amendments to MPFSO and its related subsidiary legislation.

The Mandatory Provident Fund Schemes (Amendment) Bill 2021

7. The Bill was gazetted on 9 July 2021, and received its First Reading at the LegCo meeting of 14 July 2021. The key legislative proposals are summarized in the paragraphs below.

Proposals relating to the eMPF Platform

8. The provisions mainly seek to provide the legal backing for the operation of the eMPF Platform and related matters. The major proposed amendments include:

(a) empowering the Secretary for Financial Services and the Treasury ("SFST") to designate an electronic system (i.e. the eMPF Platform) ("designated system") administered and operated by the Company for providing services and facilities to facilitate the approved trustees of MPF schemes to perform their scheme administration functions (proposed new section 19I);

(b) specifying the general duties and powers of the Company in operating the designated system including charging fees for providing any service or facility in relation to the designated system, and requiring an approved trustee to provide information to the Company (proposed new sections 19K, 19L and 19R);

(c) providing for the mandatory use of the designated system by the approved trustees, and empowering SFST to specify by notice published in the Gazette a date from which the approved trustee of a pre-existing MPF scheme is required to use the designated system to perform their scheme administration functions (proposed new sections 19M and 19N);

(d) imposing "straight pass-on" and "corresponding fee reduction" requirements for cost savings and fee-setting[3] (proposed new sections 19T to 19ZE, and proposed new Schedules 13 to 16);

(e) providing immunity from civil liability to the Company, or a director or employee of the Company in respect of anything done, or omitted to be done, in good faith in the performance or purported performance of the Company (proposed amendments to section 42B(3)); and

(f) providing certain safeguards to trustees and relieving trustees from legal consequences, through a "safe harbor" provision, if trustees' non-compliance with the law is attributable to the failure of the Company to discharge its duties as system operator (proposed amendments to section 44B).

Other miscellaneous amendments

9. The Bill introduces a number of miscellaneous amendments not related to the eMPF Platform. The proposed amendments include:

(a) empowering the Director of Audit to conduct examination into the economy, efficiency and effectiveness with which MPFA has used its resources in performing its functions (proposed amendments to section 6C(2));

(b) empowering CE to appoint one of the directors of MPFA to be the Deputy Chairman of MPFA (proposed new section 6PA); and

[3] The purpose of the provisions is to regulate the fees charged by the approved trustees for scheme administration so as to ensure cost savings derived from the operation of the eMPF Platform will be passed directly to the scheme members. While the trustee of a Mandatory Provident Fund ("MPF") scheme may charge to a constituent fund of the scheme in relation to the use of the designated electronic system, or for the provision of scheme administration services by the system operator, the aggregate amount that may be charged to the constituent fund must not exceed the total amount of the fee payable by the trustee to the system operator for the use and provision of services. There is also a mechanism for calculating and determining the fund expense ratio and the permitted percentage for a constituent fund (other than capital preservation fund) of an MPF scheme. If the fund expense ratio of a constituent fund in a specified period exceeds the permitted percentage, the approved trustee of that constituent fund has to pay the amount calculated in accordance with the new Schedule 16 into the constituent fund as income of the fund.

(c) lowering the existing statutory cap on out-of pocket expenses of the Default Investment Strategy constituent funds from 0.2% to 0.1% per annum (proposed amendments to Schedule 11).

10. Details of the main provisions of the Bill are set out in paragraph 18 of the LegCo Brief (File Ref: MPF/2/1/43C) dated 7 July 2021), and paragraphs 4 to 17 of the Legal Service Division Report on the Bill (LC Paper No. LS96/20-21). Except for the provisions mainly in connection with the specification made under the proposed section 19N,[4] and the provisions mainly concerning establishing and maintaining certain registers as required by the Bill and the Mandatory Provident Fund Schemes (General) Regulation (Cap. 485A)[5] which will come into operation on a day to be appointed by SFST by notice published in the Gazette, the Bill, if passed, will come into operation on the day on which the enacted Ordinance is published in the Gazette.

Major views and concerns expressed by Members

11. The Administration and MPFA consulted the Panel on Financial Affairs ("FA Panel") on the legislative proposals and additional funding requirements for taking forward the eMPF Platform Project ("the Project") at the meeting on 4 January 2021. Matters relating to the implementation of the eMPF Platform were also discussed at the FA Panel meetings on 5 March 2018, 18 December 2018, 2 December 2019 and 1 March 2021, meetings of the Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2019, and relevant special meetings of the Finance Committee for examining the relevant Estimates of Expenditure. The major views and concerns expressed by Members at these meetings are summarized in the ensuing paragraphs.

Benefits of the eMPF Platform for scheme members

12. Members noted that the industry-wide fund expense ratio was around 1.44% out of the asset under management ("AUM"), and it was estimated that the eMPF Platform fee to be charged by the Company would be in a range of 0.3% to 0.4% of AUM in the transitional stage, and would further drop to 0.2%

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4 Those provisions are proposed sections 14, 15(2), 16 to 18, 20, 21,23, 25, 40, 45, 48 (in so far as it relates to the proposed Schedule 17), 52, 55, 57(1) and (2), 59 to 61, 63, 64, 66, 67, 70 to 73, 77,78, 80, 83, 87(2), 88(2) and (3), 92, 94, 96, 100, 101(2), (3), (4),(6),(7), (9) to (11), (13), (14), (17)and (20), and 102.

5 Those provisions are proposed new sections 19 (in so far as it relates to the proposed section 19S), 79, 84, 91, 93, 99 and 105.

to 0.25% in about ten years' time. They enquired how the Administration would ensure scheme members could benefit from the cost savings after the implementation of the eMPF Platform, and trustees would not charge fees on other pretexts.

13. The Administration reiterated that currently, MPF schemes were operated by 14 approved trustees under a decentralized landscape involving 12 scheme administration platforms with different standards. The multiple business models, data standards, process designs and administration system infrastructure of the MPF System had contributed to the high administration costs of the System. The policy objective of the Project was to achieve cost savings from the enhanced operational efficiency of the MPF System, thereby creating room for fee reduction for the benefit of scheme members through the switching from the current predominantly paper-based MPF-related transactions to electronic transactions. To achieve the policy objective and ensure that any cost savings derived from the Platform operation would be passed directly to scheme members, two statutory requirements were proposed as follows:

(a) there should be a statutory requirement that no fee on scheme administration exceeding the eMPF Platform fee payable by trustees to the Company could be charged, whether in whole or in part, to the scheme, a constituent fund of the scheme, or a member of the scheme (i.e. the "straight pass-on" requirement); and

(b) with the lowered scheme administration costs due to the eMPF Platform, there should be corresponding reduction in the topline fees of MPF schemes.

The eMPF Platform fee to be charged by the Company in the transitional stage would be in a range of 0.3% to 0.4% of AUM. This represented the first stage of fee reduction to scheme members upfront by a possible 30% cut in scheme administration costs on average. Depending on the rate of digital take-up and consequential improvement to operational efficiency, it was expected that the eMPF Platform fee would further drop in a gradual and steady manner to 0.2% to 0.25% in about 10 years' time.

14. Some Members expressed concern that the magnitude of cost savings might not be fully realized in the early stage of transition given that trustees needed to incur additional costs and make investment in system adjustment for moving to the eMPF Platform. They urged the Administration to provide a timetable for realizing fee reduction and continue to engage MPF trustees with a view to ensuring that trustees would lower their scheme administration fees as early as possible after the implementation of the eMPF Platform.

15. The Administration advised that in formulating the proposals on the eMPF Platform fee, one of the most important guiding principles was to maximize the room for fee reduction for the benefit of scheme members. Assuming a high level of digital take-up rate and with economies of scale, it was estimated that the total cumulative quantifiable cost savings to scheme members would possibly be in a range of $30 billion to $40 billion over a ten-year period. Moreover, it was expected that after the trustees got onboard the eMPF Platform during the two-year transitional stage, scheme members could enjoy upfront a fee cut of around 30% on average in scheme administration (i.e. from 0.58% to about 0.3% to 0.4%).

16. Members enquired how the eMPF Platform could help expedite the introduction of "Full Portability" of MPF benefits and abolition of the arrangement of offsetting severance payments ("SP") and long service payments ("LSP") against MPF accrued benefits ("the offsetting arrangement").

17. The Administration advised that the eMPF Platform would improve efficiency, reliability and accuracy of the MPF System and facilitate MPFA's enforcement actions. MPFA would also ensure a level playing field for the healthy and sustainable development of the MPF System for the benefit of scheme members and Hong Kong. The eMPF Platform might also pave way for future MPF reform initiatives such as "Full Portability".

18. As regards the abolition of the offsetting arrangement, the Administration responded that it involved preparation at various fronts such as establishing the proposed designated saving accounts ("DSA") to which each employer would need to contribute 1% of his/her employees' relevant income so as to save up in advance to meet the employer's SP/LSP liabilities after the abolition of the offsetting arrangement. MPFA had been assisting the Administration to incorporate the DSA component into the eMPF Platform. The eMPF Platform would facilitate the abolition of the offsetting arrangement, which was one of the pre-requisites for allowing "Full Portability" of MPF benefits.

<u>Views and concerns of MPF trustees</u>

19. Members noted from a joint submission from 14 MPF trustees[6] that trustees' main concerns over the Project included (a) the scheme administration functions that would be performed by the eMPF Platform; (b) the 0.58% scheme administration costs adopted for estimating the possible cost savings of

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[6] The written submission has been circulated to Members vide LC Paper No. CB(1)440/20-21(01) on 31 December 2020.

$30 billion to $40 billion in ten years of the operation; (c) immunity and liability of the Platform, and (d) safeguards to trustees if non-compliance with the statutory requirements was due to the partial (instead of sole) failure of the eMPF Platform or the Company. Members urged the Administration and MPFA to meet with the MPF industry to discuss and clarify the issues raised with a view to addressing trustees' concerns.

20. As MPF trustees would incur costs in upgrading their IT systems for getting onboard the eMPF Platform, some Members enquired if the Administration would consider providing financial assistance to trustees for this purpose, and what measures the Administration and MPFA would take to encourage trustees to support the full operation of the eMPF Platform.

21. The Administration responded that the concerted effort of the Government, MPFA and MPF trustees was pivotal to the successful implementation and smooth operation of the eMPF Platform. To this end, the Government and MPFA had set up the Working Group on eMPF in 2017 to steer the development of the Platform in collaboration with the MPF trustees. Amongst other things, the Working Group had formulated a set of common standards and technical specifications covering most areas of MPF scheme administration processes, which formed the scope of the tender documents of the eMPF Platform. Noting that trustees would incur expenditure for data cleansing and migration in order to transfer to the eMPF Platform, the Government had proposed an additional funding provision of $210 million to facilitate trustees' boarding onto the eMPF Platform and managing the associated risks. Details of the assistance to be provided to trustees, particularly the first batch for boarding onto the eMPF Platform, would be worked out between MPFA, the Company and trustees during discussions on the transitional arrangements.

22. The Administration stressed that the implementation of the eMPF Platform would not change the existing relationship between MPFA as a regulator and the trustees as regulatees. Therefore, trustees should continue to owe fiduciary duties to scheme members and would remain legally responsible for the administration of MPF schemes after the implementation of the eMPF Platform. For other services currently provided by trustees which were not directly relevant to their obligations under MPF legislation (e.g. customer service hotline), or were more personalized or "add-on" services to tailor to different customers' experience or needs, the eMPF Platform would not take up these functions as they were not core scheme administration functions. Trustees or their group companies might continue to provide such services as part of their business. The Administration assured Members that the Government and MPFA would have on-going dialogue with the MPF industry to

ensure smooth and secure transition from the existing system to the new eMPF Platform.

Reform of the Mandatory Provident Fund System

23. Some Members considered that the Administration and MPFA should reform the MPF System to address issues including poor investment performance of many MPF funds and restrictive requirements for early withdrawal of MPF benefits by scheme members. These Members noted that some members of the public had urged for abolishing the MPF System or permitting early withdrawal of the MPF benefits by scheme members to cope with financial hardship during adverse economic situations like those arising from the coronavirus disease 2019 ("COVID-19") epidemic.

24. The Administration advised that MPFA had taken a number of measures, such as introducing the Employee Choice Arrangement in 2012 and the Default Investment Strategy in 2017, to create more room to reduce the administration fee of MPF funds. It was envisaged that the implementation of the eMPF Platform would further reduce the administration cost of the MPF System and enhance competition, thus providing further room for trustees to lower the administration fee. Moreover, the implementation of the eMPF Platform could lower the threshold for potential trustees to enter the MPF market as the Platform could automatically and electronically handle many MPF scheme administration processes currently performed by trustees, thus reducing the cost barrier for them in entering the market and increase competition in the market.

25. As regards allowing scheme members to withdraw their MPF benefits for relieving financial hardship, the Administration stressed that the MPF System was designed as a long-term saving scheme for retirement. Any proposals allowing early withdrawal of accrued benefits from MPF System must take into consideration the corresponding reduction of scheme members' accrued benefits meant for their retirement. If the preservation requirement on accrued benefits was relaxed and scheme members were allowed to make early withdrawal to meet short-term financial needs or contingency, the accrued benefits would be leaked from the System from time to time and the function of accumulation for value growth would be weakened, thereby undermining the integrity of the MPF System and rendering it difficult to achieve the purpose of assisting the working population to save for their retirement. Hence, after detailed deliberation within the Government and thorough consideration of relevant policy objectives and long-term implications, it was considered not appropriate to allow early withdrawal of MPF accrued benefits by scheme members for addressing their imminent needs. The Administration had already launched a number of relief measures including the Employment Support

Scheme and the Cash Payout Scheme to help the public cope with the difficulties arising from the COVID-19 epidemic.

Relevant question raised at Council meeting

26. At the LegCo meeting of 2 May 2018, Hon CHAN Kin-por raised a written question on the work of the Working Group on eMPF. The question covers the work progress of the Working Group, the latest timetable for launching the eMPF Platform, and the Administration's plan to apply various types of financial technologies to enhance the effectiveness of the Platform. Details of the question and the Administration's reply are provided in the hyperlink in the **Appendix**.

Latest development

27. At the House Committee meeting on 16 July 2021, Members agreed to form a Bills Committee to study the Bill.

Relevant papers

28. A list of relevant papers is set out in the **Appendix**.

Council Business Division 1
Legislative Council Secretariat
2 August 2021

Appendix

List of relevant papers

Date	Event	Paper
3 April 2017	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2017-2018 (session on financial services)	Speaking note of the Secretary for Financial Services and the Treasury Report on the examination of the Estimates of Expenditure 2017-2018
5 March 2018	Meeting of the FA Panel	Administration's paper (LC Paper No. CB(1)625/17-18(07)) Background brief (LC Paper No. CB(1)625/17-18(08)) Minutes (paragraphs 43-49) (LC Paper No. CB(1)924/17-18)
17 April 2018	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2018-2019 (session on financial services)	Speaking note of the Secretary for Financial Services and the Treasury Report on the examination of the Estimates of Expenditure 2018-2019
2 May 2018	Hon CHAN Kin-por raised a written question on Work of the Working Group on eMPF	Hansard (pages 9011- 9012)
18 December 2018	FA Panel meeting	Administration's paper (LC Paper No. CB(1)309/18-19(04)) Minutes (paragraphs 46-59) (LC Paper No. CB(1)806/18-19)

Date	Event	Paper
9 April 2019	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2019-2020 (session on financial services)	Speaking note of the Secretary for Financial Services and the Treasury Report on the examination of the Estimates of Expenditure 2019-2020
2 December 2019	FA Panel meeting	Administration's paper (LC Paper No. CB(1)175/19-20(08)) Background brief (LC Paper No. CB(1)199/19-20(01)) Minutes (paragraphs 96-107) (LC Paper No. CB(1)376/19-20)
6 April 2020	Special meetings of the Finance Committee to examine the Estimates of Expenditure 2020-2021 (session on financial services)	Speaking note of the Secretary for Financial Services and the Treasury Report on the examination of the Estimates of Expenditure 2020-2021
12 June 2020	Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2019	The Bill Background brief (LC Paper No. CB(1)631/19-20(03)) Report to House Committee (LC Paper No. CB(1)740/19-20)
4 January 2021	FA Panel meeting	Administration's paper (LC Paper No. CB(1)417/20-21(03)) Background brief (LC Paper No. CB(1)417/20-21(04)) Minutes (paragraphs 4-24) (LC Paper No. CB(1)674/20-21)

Date	Event	Paper
1 March 2021	FA Panel discussed the proposed budget of MPFA for 2021-2022	Administration's paper (LC Paper No. CB(1)604/20-21(03)) Minutes (paragraphs 7-25) (LC Paper No. CB(1)883/20-21)
21 July 2021	The Mandatory Provident Fund Schemes (Amendment) Bill 2021 was introduced into the Legislative Council	The Bill Legislative Council Brief (File Ref: MPF/2/1/43C) Legal Service Division Report (LC Paper No. LS96/20-21)