

**Workshop on Governance of MPF Trustees
17 October 2017**

Opening Address

**Dr David Wong Yau-kar
Chairman
Mandatory Provident Fund Schemes Authority**

The Honourable Bernard Charnwut Chan, distinguished guests, ladies and gentlemen

Good morning.

2. On behalf of the Mandatory Provident Fund Schemes Authority (MPFA), I would like to express my warm welcome to all of you for attending this Workshop.

3. Today, we are very honoured to have a number of distinguished speakers, including leading figures working in different disciplines related to the MPF, as well as senior representatives from fellow regulators, to share with us their knowledge and experience on the important topic of “Governance”.

4. As you are all aware, financial regulators worldwide are increasingly focusing on the governance of financial institutions. While the financial crisis of 2008 had a significant negative impact on the financial wealth of pension funds around the world, it had also proved to be an important stress test of the governance structures and processes of pension funds, and drew attention to governance frameworks.

5. On the global front, in 2009 the Organization for Economic Co-operation and Development (OECD) issued the “OECD Guidelines for Pension

Fund Governance”, laying down a framework for strengthening pension fund governance with the objective of better serving the needs of pension fund members. And in 2015 the Basel Committee on Banking Supervision issued revised guidance on corporate governance principles for banks. Here in Hong Kong, last year the Securities and Futures Commission issued a circular introducing measures to enhance the accountability of the senior management of licensed corporations. And just a couple of months ago, the Insurance Authority updated its Guideline on Corporate Governance of Authorized Insurers. Thus regulators, both international and local, increasingly recognize the need to strengthen the governance arrangements of financial institutions and to make senior management accountable for safeguarding the interests of their customers.

6. But experience shows that mere compliance with rules and regulations is not enough to drive financial institutions to provide good services and to manage in a responsible manner other people’s money that they are entrusted with, whether in the capacity of an asset manager, broker or custodian.

7. Under the MPF System, MPF trustees assume a fundamental role in protecting scheme members’ interests and delivering “value for money” outcomes for them. With MPF assets under management reaching a record high since inception – amounting to HK\$786 billion as of 31 August 2017 and covering over 4 million scheme members – I would like to emphasize that although **MPF trustees are not “public trustees”, they are indisputably, “trustees of the public”**. MPF trustees hold the key to two main components in the delivery of good retirement saving outcomes for scheme members. First, they take charge of the administration platform and hence the operational efficiency of MPF schemes. Second, they are legally required to appoint investment managers and custodians to manage the MPF funds and assume the overall responsibility of admitting new funds or terminating funds that do not meet the overall objective of retirement protection under the MPF System.

8. Regarding the first component – ensuring operational efficiency – I am pleased to see that under the leadership of the Government, the MPFA and MPF trustees are working on a blueprint for e-MPF, which will basically provide a centralized electronic platform that will support the scheme administration of all MPF trustees. This is a major infrastructural reform, which will deliver a much better service experience for members and improve the cost efficiency of MPF administration in the years to come.

9. On the second component – governance – I believe this is the right time to engage the MPF industry and service providers in a dialogue to see what can and should be done to strengthen the capability of the boards of MPF trustees in overseeing the management of MPF assets. I believe this is the right time because, as I just mentioned, MPF assets under management have reached a record high, exceeding HK\$780 billion – equivalent to about 32% of Hong Kong’s total 2016 GDP. Compared with more mature pension systems around the world, whose asset size averages 50% of GDP, there is clearly considerable room to grow the MPF assets of our scheme members. A significant part of the growth will depend on how effectively MPF trustees deliver better “value for money” for MPF scheme members. Let me take a few moments to examine how good governance will help achieve this goal.

10. Hong Kong adopted the multi-pillar retirement protection model recommended by the World Bank; the MPF System forms the second pillar of this model. Employees are mandated to join the MPF schemes chosen by their employers, and MPF contributions are privately managed. Because of the mandatory nature of the contributions and the broad customer base, the size of MPF assets has grown steadily over the past 17 years. Out of the \$786 billion of MPF assets, \$560 billion is from contributions, while \$226 billion represents investment returns.

11. The MPF System was founded on the cornerstone that trustees manage

the investments and make sure that everything is in good order for scheme members, so that when it comes to their retirement, members can have a basic level of retirement protection based on the contributions accrued over their working life, which may span over 40 years. Therefore, good governance is particularly important for a mandatory private pension system like the MPF.

12. Trustees in a mandatory system are expected to have a higher duty of care compared with those of retail products, where investors are free to choose their own service providers and whether or not to invest. MPF Scheme members place their trust in and rely on the integrity and professional judgment of MPF trustees to manage the schemes responsibly and safeguard their retirement savings. Therefore, it is absolutely vital for trustees to act in the best interests of scheme members and take all possible measures to ensure the delivery of appropriate member outcomes through high quality, value-for-money benefits and services, despite possible conflicts that may arise from their own profit objectives.

13. The impact of good governance on enhancing the performance of pension funds and providing increased protection of members' benefits is considered to be substantial. International best practices indicate that appropriate governance structures, well-defined accountability, policies and procedures, and suitable processes for selecting and operating governing bodies are some of the key factors in good governance of pension funds.

14. I know most of you realize that the pension business has a number of unique features which may not be found in retail fund distribution or securities brokerage. MPF trustees may have a client relationship with scheme members for some 40 years. Should the member decide to make phased withdrawals, the relationship may even last 50 years or more. Obviously, a good decision by the trustee in picking diligent, well-performing asset managers can make a huge difference to a retiree's income over a period of 40 years or more. The same is

true if MPF trustees fight hard in negotiating contracts for services with asset managers or custodians at a rate that is competitive so that whatever savings can be negotiated on the fees to service providers can go into investments for members.

15. Governance structures establish the architecture for decision-making processes in pension funds, and the accountability of pension funds' governing bodies strongly influences the incentive for sound, judicious decision making.

16. Good governance also calls for clear identification and separation of the operational and oversight responsibilities in a pension fund. Generally, the governing body of a pension fund focuses on strategic decisions and oversight functions, while operational tasks are delegated to executive staff or external service providers. The governance framework should facilitate two-way communication between the board level and the operational level in the governing body, with the governing body retaining ultimate responsibility for the fund.

17. The governing body of a pension fund should be accountable to members and beneficiaries. Appointing independent directors or members to the board is one way to enhance accountability of the governing body. Independent directors can provide the board with access to a wider range of skills and experience and thus enhance decision-making. Having independent directors, however, is not enough. All directors must bring appropriate experience to the board, understand their fiduciary responsibility, be prepared to challenge the decisions of the management team and act in a manner that is not influenced by any conflict of interest. To achieve this, the industry should look broadly to identify directors who will bring the right level of expertise and capability to the board, and ensure that sound appointment and renewal policies are instituted.

18. While MPF trustees have no legal obligation to have scheme member

representation on their boards, the board should nevertheless seek ways to gauge the views of these ultimate beneficiaries to support its decisions.

19. Last but not least, policies and procedures are the mechanisms that ensure the proper functioning of a pensions fund's governing body. They form the means by which incentives for prudent behaviour are operationalized, and are conducive to sound judgment and decision making. In my experience, key policies and procedures include those that support good governance structures, accountability, transparency, independent oversight, a clear investment policy, and risk identification, control and monitoring. An important aspect of governance mechanisms is a risk-based internal control system to regularly assess the performance of persons and entities (such as appointed service providers) involved in the operation and oversight of the pension fund, and to ensure compliance with the law.

20. Promoting a high standard of governance among all MPF trustees has always been a key regulatory objective of the Authority. Good governance breeds good behaviour, which in the long run, will bring about positive results in protecting the retirement savings of scheme members.

21. No doubt, the governance of pension trustees is a vast and important topic. I hope that through the interactive sessions in this Workshop with our fellow financial regulators in Hong Kong and leading experts on risk management, pension designs and corporate governance, we can all learn more about, and together help generate ideas to improve, the MPF System for working people in Hong Kong.

22. Now, it is my pleasure to introduce our Guest of Honour, the Honourable Bernard Charnwut Chan, who is the Convenor of the Executive Council of the Hong Kong SAR and a Hong Kong Deputy to the National People's Congress of the People's Republic of China. He is currently the

President of a listed company, and sits on the boards of a number of local and overseas companies. With his longstanding experience as a board member and chairman of various companies and NGOs, I am sure Mr Chan will have much to share with us on today's topic, and enlighten us on public expectations of the MPF System.

23. Please join me in welcoming Mr Chan.