

Springing up so bright, shooting out in light



SUPERVISION OF APPROVED TRUSTEES

Inspection Visits to Approved Trustees

As the approved trustees are entrusted with the overall responsibilities for the administration and management of the MPF schemes, the supervision of their performance remains one of the core functions of the MPFA. An approved trustee may delegate part of its functions to other service providers but they are required to comply with the provisions of the MPF legislation and discharge their responsibilities with due care, and to exercise their fiduciary duties as required. A list of the approved trustees and their background as at 31 March 2003 is at Appendix 7.

After more than two years' operation, employers and self-employed persons have become familiar with the MPF System. MPF trustees have also made considerable improvements in their scheme administration process. The MPFA continues to supervise the operation of the trustees and monitor the compliance of the investment funds with regulatory requirements.

During the year, the MPFA continued with its on-site inspection programme to ensure that the approved trustees comply with the MPF legislation. The focus of the latest round of regular on-site inspections was on scheme administration, which included the processing of contributions, fund switching, benefit transfers and investment monitoring etc.

Some non-compliance issues and internal control weaknesses were identified during inspection visits. Non-compliance issues included failure to complete transfer-out and payment of accrued benefit requests within the statutory timeframe and failure or delay in sending letters to scheme members (who have ceased to be employed by a participating employer or ceased to be self-employed) informing them of the different options that they have with respect to the transfer of their accrued benefits. With regard to these cases of non-compliance, the MPFA issued a total of 26 financial penalty notices to trustees during the year. Details of the notices are set out at item 8 under Part E of the Statistics section. The MPFA monitored all the breaches and internal control weaknesses closely and in some cases, follow-up inspections were made to ensure that corrective actions had been taken by the approved trustees and/or service providers.

In preparation for the commencement in February 2003 of those provisions of the Mandatory Provident Fund Schemes (Amendment) (No.2) Ordinance 2002 which concern scheme administration and the adjustment of the minimum relevant income for contribution from \$4,000 to \$5,000 per month, a special round of on-site inspection visits was paid to approved trustees. The inspections, which took place during the period from November 2002 to January 2003, were designed to assess trustees' readiness to comply with the legislative changes. The scope of inspection included reviewing the scheme administration systems, procedures, communication plans as well as customer service facilities to ensure that relevant enhancement or revision had been made to cater for changes as required by the amended legislation. In general, the approved trustees' readiness for compliance was considered satisfactory.

Supervision of the Industry *Continued*

As part of the ongoing process to refine the MPF System and to enhance MPFA's capabilities, integrity and accountability, the MPFA conducted initial studies for the development of a risk management regime to control risks. In this respect, preparatory work was carried out to review the strategy of supervision of approved trustees. A risk-based strategy was proposed, under which emphasis will be placed on investment-related aspects of MPF schemes and funds, MPF guaranteed funds and corporate governance issues. Tailor-made inspection programmes will be designed to tackle identified weaknesses of individual trustees. The proposed strategy was endorsed by the Management Board in December 2002.

Ongoing Monitoring

To ensure that the approved trustees comply with the statutory requirements and to enable early detection of issues which call for potential legislative amendment, policy development, issuance of guidelines etc, trustees are required to submit returns, audited financial statements and reports in respect of the schemes under their trusteeship on monthly, quarterly and annual bases.

Also as part of the ongoing monitoring, approved trustees are required to report significant events under Section 62 of the Mandatory Provident Fund Schemes (General) Regulation. For protection of scheme members' interest, follow-up actions have been carried out to ensure that the issues have been rectified and that the reported events would not negatively impact scheme members' interest.

Upon the outbreak of atypical pneumonia in Hong Kong in March 2003, the MPFA requested from approved trustees their proposed contingency measures to ensure business continuity in case any member of their staff contracted the disease. After examining the trustees' proposed measures, the MPFA issued a letter to all approved trustees in April 2003 highlighting the major issues to be addressed in drawing up their contingency/business continuity plans.

The complaint mechanism has been and will continue to be one of the major means of the ongoing monitoring of the performance of approved trustees. At the same time, it is also an effective avenue for identifying scheme administration issues and policy development areas. A total of 226 complaints received by the MPFA in the year were lodged against approved trustees, mostly related to scheme administration. The number of complaints has dropped significantly compared to a year ago as most approved trustees have continued to streamline and improve their operations.

Registration and Approval of MPF Schemes and Funds

The registration and approval of MPF schemes and funds involved a detailed review of various aspects, including scheme rules, operations, and disclosure focusing on compliance with MPF legislation and protection of scheme members' interest. Table 1 sets out the processing statistics during the year, and Table 2 shows an analysis of the structure of approved pooled investment funds. A full list of the registered schemes and their underlying constituent funds is at Appendix 8.

Table 1. Processing statistics at scheme and fund levels

	Number as at 31 March 2002	De-registration/ Revocation during the year	Registration/ Approval during the year	Number as at 31 March 2003
Registered Schemes	51	2	0	49
Master Trust Schemes	47	2	0	45
Industry Schemes	2	0	0	2
Employer Sponsored Schemes	2	0	0	2
Approved Constituent Funds	311	7	14	318
Approved Pooled Investment Funds	220	3	32	249
Approved Index-Tracking Collective Investment Schemes	0	0	39	39

Table 2. Analysis of approved pooled investment funds

	Unit Trust		Insurance Policy		Total	
	as at 31 March 2002	as at 31 March 2003	as at 31 March 2002	as at 31 March 2003	as at 31 March 2002	as at 31 March 2003
By fund valuation bases						
Unitized	156	185	61	61	217	246
Non-unitized	0	0	3	3	3	3
Total	156	185	64	64	220	249
By fund structures						
Umbrella funds	21	23	4	4	25	27
Internal portfolios	107	126	36	36	143	162
Feeder funds	5	7	15	15	20	22
Portfolio management Funds	23	29	9	9	32	38
Total	156	185	64	64	220	249

Supervision of the Industry *Continued*

In the past year, considerable amendments were made to the constitutive and offering documents of MPF schemes and approved pooled investment funds by the approved trustees and service providers. These amendments included consequential changes due to legislative amendments, scheme/business restructuring, changes in fees and charges etc. Statistics on MPF schemes and funds are included in Part B of the Statistics section.

SUPERVISION OF INTERMEDIARIES

Registration of MPF Intermediaries

Part of the MPFA's regulatory effort is devoted to supervising MPF intermediaries who engage in selling MPF schemes or advising clients on the funds of MPF schemes. The MPFA cooperates with the Hong Kong Monetary Authority (HKMA), the Insurance Authority (IA) and the Securities and Futures Commission (SFC) in regulating MPF intermediaries. During the year, the work in respect of supervision of intermediaries focused on renewal of registration of MPF intermediaries, monitoring intermediaries' compliance with the Code of Conduct for MPF Intermediaries and improving the professional standard of MPF intermediaries.

During the year, the MPFA processed a total of 4 674 new applications for registration as MPF intermediaries. As at 31 March 2003, there was a total of 26 193 registered MPF intermediaries, comprising 428 corporations and 25 765 individuals respectively.

Following the enactment of the Securities and Futures Ordinance and the Banking Ordinance 2002, the MPFA has issued a new type of MPF intermediaries card to staff of authorized institutions who are permitted to sell MPF schemes without rendering specific investment advice.

Table 3 sets out the number of MPF intermediaries and Figure 1 shows the percentage share of individual registered intermediaries by the major line of business of the intermediary's primary sponsoring corporation.

Table 3. Number of Registered MPF Intermediaries as at 31 March 2003

Total number of registered MPF intermediaries	26 193
Corporate intermediaries	428
Individual intermediaries	25 765
Permitted to advise on insurance policies	14 015
Permitted to advise on securities	5 782
Permitted to advise on both securities and insurance policies	3 891
Permitted to sell MPF schemes without rendering specific investment advice	2 077

Figure 1. MPF Intermediaries by Industry* as at 31 March 2003



Ongoing Monitoring

Under the existing regulatory framework, the MPFA acts as the lead regulator in the regulation of MPF intermediaries, coordinating the regulatory efforts of the other three regulators with a view to ensuring regulatory consistency and minimizing regulatory overlap. Whilst the MPFA is mainly responsible for daily monitoring and handling of complaints, the HKMA, the IA and the SFC are responsible for supervising those MPF intermediaries falling under their regulatory regimes, including conducting inspections and taking enforcement/disciplinary actions where necessary on MPF intermediaries under their respective supervision.

During the year, the MPFA processed a total of 7 872 changes of information relating to MPF intermediaries. Most of the changes were related to change of employment of individual intermediaries and change of name of their sponsoring corporation as a result of corporate mergers and restructuring.

The registration of a MPF intermediary is valid for a period of three years. MPF intermediaries wishing to remain registered must apply to the MPFA for renewal prior to their expiry dates. The MPFA has started the renewal process in the latter part of 2002. As at 31 March 2003, registrations of 16 311 intermediaries have been renewed.

In the past year, there were three complaints against MPF intermediaries. This accounted for less than 1% of the total complaints received by the MPFA. One complaint case was referred to another regulator for information and consideration of follow-up action.

**Continuing
Professional
Development**

The Continuing Professional Development (CPD) requirement for MPF intermediaries has been implemented since January 2002 to ensure that intermediaries maintain their professional competence. MPF intermediaries are required to undertake a minimum of 10 hours of CPD activities in each calendar year. As at 31 March 2003, five institutions have been recognized by the MPFA for the provision of training activities for CPD subjects. They are Caritas Adult & Higher Education Service, the Financial Services Development Centre of the Vocational Training Council, Hong Kong Securities Institute, the Management and Executive Centre of the Hong Kong Polytechnic University, and the School of Professional and Continuing Education of the University of Hong Kong.

Following the enactment of the legislative amendments during the year, the salient points of the amended legislation have been set out in the study notes for MPF intermediaries' examinations to ensure that MPF intermediaries are apprised of the changes. Seminars on the legislative amendments were also given to instructors of the recognized CPD institutions and MPF intermediaries.

**REGULATION OF
OCCUPATIONAL
RETIREMENT
SCHEMES**

**Withdrawal of
Exemption
Certificate**

The MPFA is the Registrar of Occupational Retirement Schemes (RORS) and has the functions conferred on it by the Occupational Retirement Schemes Ordinance (Cap. 426) (ORSO). It is responsible for regulating occupational retirement schemes (ORSO schemes) voluntarily established by employers. Since the implementation of the MPF System, the number of ORSO schemes has been decreasing.

Prior to the launch of the MPF System, existing ORSO schemes might choose to apply for exemption from MPF requirements. Members of MPF-exempted ORSO schemes had a one-off option to choose between the existing scheme and a MPF scheme.

Owing to the additional costs of running two schemes (MPF and ORSO schemes) simultaneously and other reasons, employers of MPF exempted ORSO schemes may withdraw their MPF exemption certificates. During the year, 270 MPF exempted ORSO schemes had relinquished their exemption status covering about 4 200 members. The number of MPF exempted ORSO schemes as at 31 March 2003 was 5 720 covering about 8 100 employers and 567 000 scheme members. A breakdown of the number of schemes is shown in Figure 2.

Winding Up of ORSO Schemes

Figure 2. Number of MPF Exempted ORSO Schemes as at 31 March 2003



For those ORSO schemes which have not obtained MPF exemption status, the relevant employers may choose an interface arrangement to retain them as top-up schemes, freeze the schemes or terminate the schemes. During the year, 928 ORSO schemes (comprising 328 MPF exempted schemes and 600 non-MPF exempted schemes) were wound up. As at 31 March 2003, there were 307 termination notices still pending the MPFA's processing due to incomplete information or assets pending transfer. After completion of the processing of these notices, the number of ORSO schemes would be 8 268, including 5 650 MPF exempted schemes (covering about 566 000 scheme members) and 2 618 non-MPF exempted schemes (covering about 68 000 employees). The number of termination notices received by the MPFA has reduced towards the end of the financial year.

Based on the termination notices submitted and the latest annual returns of the respective ORSO registered schemes, the asset arrangements for the terminated ORSO registered schemes (including those schemes undergoing termination process) are set out in Table 4.

Table 4. Asset arrangements for terminated ORSO registered schemes for the period from 1 April 2002 to 31 March 2003

ORSO Asset Arrangement	No of Schemes		Asset Size (HK\$ million)	
		%		%
Transferred to MPF Scheme	394	46	765	44
Transferred to another ORSO Scheme	37	4	465	26
Paid out to scheme members	432	50	518	30
Total	863	100	1,748	100

**Funding of
ORSO Schemes**

According to the ORSO, employers operating ORSO schemes should ensure proper funding of the schemes to meet the scheme members' benefit claims. The MPFA monitors the funding situation of the schemes by examining the annual returns and audited financial statements in respect of the schemes. In the case of defined benefit schemes, actuarial certificates have to be supplied to the MPFA at least every three years. The certificate may be a full certificate certifying that the scheme's assets are sufficient to meet the scheme's aggregate vested liabilities, or a qualified certificate showing that the scheme assets are not sufficient to meet the vested liabilities. Where a qualified certificate is supplied, the actuary shall make recommendations as to the amount of contributions to be made by the employer in order to make up the shortfall in funding within three years. The frequency of supplying the actuarial certificate will also be increased to annual submission until a full certificate is supplied.

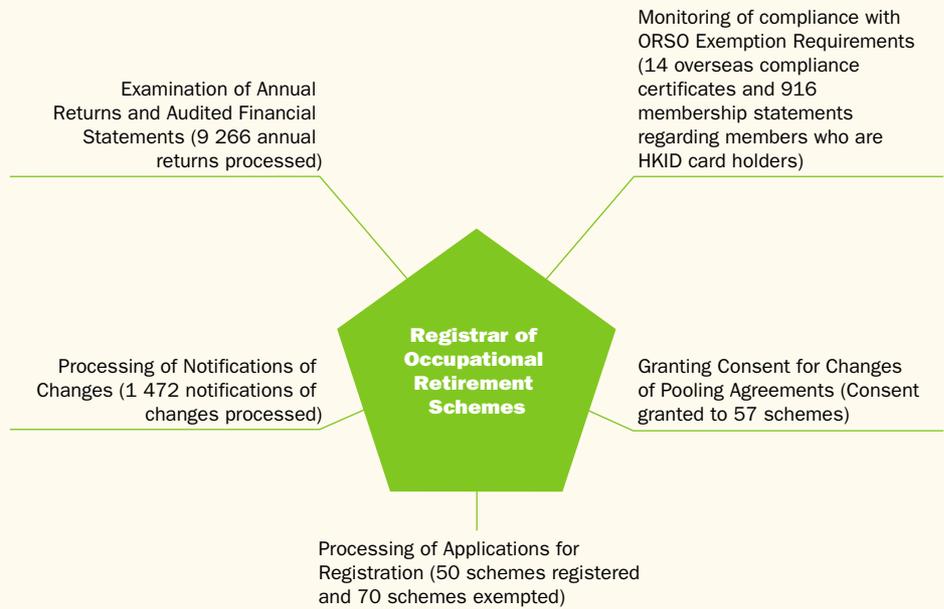
Due to poor investment performance, a small percentage of ORSO schemes were under-funded during the year. As at 31 March 2003, 22 defined benefit schemes were under-funded, with a total asset size of \$5,071 million and a total shortfall of \$287 million. The amount of shortfall involved represents about 5.7% of the aggregate assets of the 22 under-funded schemes. The MPFA has been monitoring the situation closely by seeing to it that contributions are made according to scheme terms and rules or in accordance with actuarial recommendations.

**Other Work of the
Registrar of
Occupational
Retirement Schemes**

As the RORS, the MPFA is also responsible for the effective administration of ORSO schemes. The work of the RORS in this aspect includes monitoring of ORSO registered/exempted schemes and processing of changes to the schemes. Statistics of some major work of the RORS are summarized in Figure 3.

Figure 3. Work of Registrar of Occupational Retirement Schemes

Note: Figures denote workload for the year



A list of the corporate administrators who administer pooling agreements for ORSO schemes is in Appendix 9.

Statistics

Statistics on ORSO schemes are set out in Part C of the Statistics section.