

# Business Operations

We are an advocate of the MPF System, striving to refine it and maximize its value for scheme members.

This section summarizes major results of our efforts in the year in improving MPF products, ensuring the smooth operation of the MPF market, supervising the MPF industry, promoting the efficiency of market operations, and protecting the MPF benefits of scheme members.

This section also covers our work as the Registrar of Occupational Retirement Schemes in the year.

## MPF PRODUCTS

### The DIS

New legislation was enacted on 26 May 2016 to require that MPF trustees provide in each MPF scheme a DIS. The DIS represents a major reform of the MPF System, aiming to address scheme members' concerns about the difficulty of making investment decisions and high fees of MPF. It was launched on 1 April 2017.

### Design and development

We designed and developed the DIS with reference to international experience and the advice of OECD experts and Hong Kong industry experts on a strategy suitable for long-term retirement investment. Comments from the previous public consultation entitled "Providing Better Investment Solutions for MPF Members" and input of the industry also formed the basis for the design.

The DIS is a ready-made investment solution, designed mainly for scheme members who do not know how to choose or are not interested in managing their MPF. It uses two mixed assets funds investing in a globally diversified manner with the management fees and recurrent out-of-pocket expenses capped by law. Investment risks are automatically reduced as a scheme member approaches retirement age. The fee cap requirement for DIS is the first of its kind in the MPF System.

In collaboration with the Securities and Futures Commission ("SFC"), we approved 58 constituent funds, 26 APIFs and 9 ITCISs as building blocks of the DIS.

### Preparation and implementation

Resources are dedicated to guiding and communicating with trustees in preparation for the launch of the DIS.

We visited trustees on-site to assess their progress of preparation and review their governance, risk management, compliance framework and operational readiness of scheme administration systems. In addition, independent assessments on trustees' readiness were completed before launching the DIS.

After the launch of the DIS, we started a supervisory programme to oversee trustees' implementation of the DIS, and supervised them in carrying out transitional arrangements. On the enforcement side, we refined our strategies to support the implementation of the DIS.

For MPF intermediaries, we developed a new continuing professional development ("CPD") training activity on the DIS. Train-the-trainer sessions and briefing sessions for responsible officers were organized. We also directly delivered messages on the DIS to subsidiary intermediaries via town-hall briefings of industry associations. Moreover, we updated the study notes for the examination of intermediaries to incorporate information on the DIS.

### Communication, publicity and education

We carry out territory-wide communication, publicity and education programmes in three phases to get the messages across and raise the public's awareness, particularly of the impact of the statutory requirements on the treatment of MPF benefits.

Following the passage of the new legislation in May 2016, efforts were made to generate public awareness of the DIS and the related legislative changes. Mass media publicity was launched to get scheme members geared up for receiving DIS information from trustees.

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In the second phase which started in December 2016, we stepped up publicity to help scheme members and employers understand the DIS. Advertisements were placed in various media channels to raise awareness of the DIS and draw attention to its possible impact on scheme members. We also mobilized all MPF trustees to conduct awareness campaigns to all nine million account holders.

The third phase of publicity started in April 2017, focusing on the transitional arrangements for the existing default investment account holders and the DIS notices issued to the affected scheme members.

### Fees and charges

Lower fees can have a significant contribution to long-term investment return. The cap on the management fees of the DIS at 0.75% and the recurrent out-of-pocket expenses at 0.2%, working through market forces, is likely to place further downward pressure on fees of MPF funds, and reduce the FER of MPF funds, which was 1.56% as at 31 March 2017, over time.

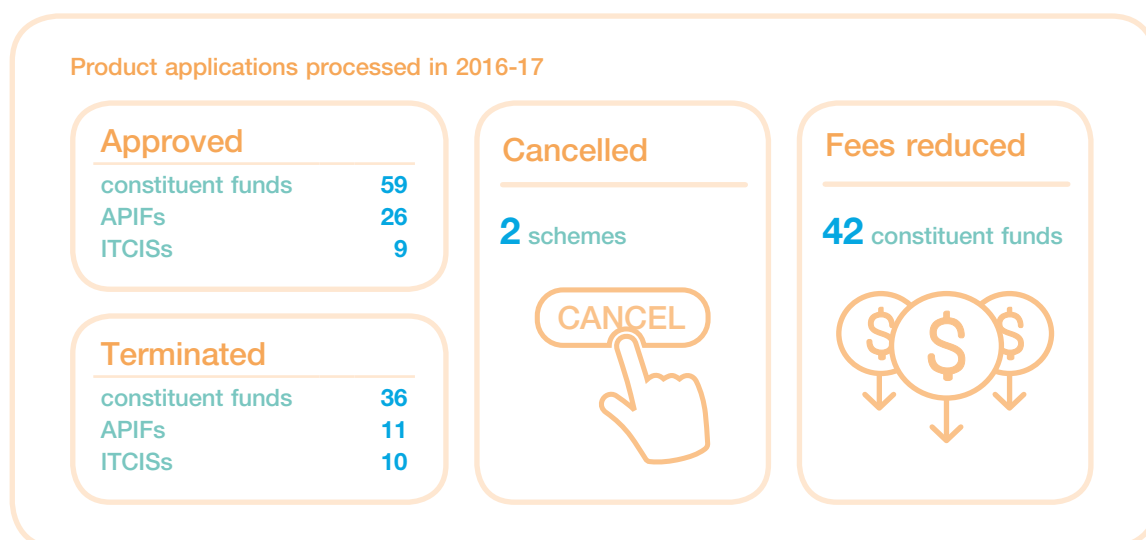
In fact, there has been a steady reduction in the average FER of MPF funds over the years. It dropped significantly by 24% from 2.06% in July 2007 (when the FER was first introduced) to a record low of 1.56% in September 2016 and stayed at this lower level as at 31 March 2017.

During the year, as the preparation of the DIS gathered momentum, 42 pre-existing MPF funds reduced their fees. As at 31 March 2017, there were 170 (41%) low-fee MPF funds (with management fee of 1% or below or FER of 1.3% or below) of different types (128 of them investing in equities and/or bonds)<sup>1</sup>.

### Product approval

We agreed with SFC on arrangements to make the approval process for new MPF funds more streamlined, efficient and focused on key risks.

For MPF product applications, we provided trustees with a reference checklist to facilitate the preparation of documentation and information.



<sup>1</sup> The number of low-fee funds includes only the constituent funds available for selection in the MPF market. The denominator for calculating the percentage of low-fee funds has been adjusted accordingly.

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### Disclosure of MPF information

We make ongoing efforts to drive improvements to the materials for disclosing MPF information to scheme members, facilitating retirement planning and decision-making on MPF schemes and funds.

Starting with DIS, we have simplified and standardized presentation in the offering documents for MPF schemes<sup>2</sup>, making them more user-friendly and easier to read. The effort will continue in the coming years.

### MPF MARKET

MPF trustees make continuous efforts to enhance the cost-effectiveness of their MPF funds. Since 2003, applications have been received for 36 schemes to be consolidated into 14 schemes.

## MPF INDUSTRY SUPERVISION

### Trustees

#### Surveillance, monitoring and enforcement

We adopt a proactive and risk-based approach in monitoring and supervising trustees.

We assess and oversee trustees' compliance and detect potential weaknesses. In respect of areas of concern, we issue circulars to provide guidance and take supervisory or enforcement actions as appropriate. We investigate suspected non-compliance cases and make regulatory responses having regard to factors including the nature and scope of the cases.

#### Market activities in 2016-17



8 MPF schemes under the trusteeship of the HSBC Provident Fund Trustee (Hong Kong) Limited comprising total assets under management of \$176.4 billion were merged into 4.

Other business activities involving the change of sponsorship for a number of MPF schemes took place:

-  Manulife (International) Limited acquired the sponsorship of MPF and ORSO schemes from the Standard Chartered Bank (Hong Kong) Limited from 1 November 2016.
-  The sponsorship of the Schroder MPF Master Trust (currently known as SunLife MPF Master Trust) was transferred to Sun Life Hong Kong Limited from 1 December 2016.
-  The Hongkong and Shanghai Banking Corporation Limited replaced HSBC Life (International) Limited to act as the Sponsor of HSBC Mandatory Provident Fund – SuperTrust Plus and HSBC Mandatory Provident Fund – ValueChoice from 22 November 2016.

#### Supervision and enforcement actions in 2016-17



3 circulars were issued to trustees on compliance, scheme administration, and other MPF issues.

184 enquiries were conducted into issues related to scheme administration, arising from inspection, monitoring, enquiries, complaints and trustees' self-reporting.

<sup>2</sup> Offering document refers to a document that invites participation in an MPF scheme.

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### Thematic programme

We pursued a focused supervisory programme to address operational risks and governance issues of trustees with key compliance issues.



We closely monitored a trustee's transformation programme to overhaul its governance, risk management, administration infrastructure and processes, through regular meetings with the trustee and with the assistance of an appointed independent consultant.

### Intermediaries

#### Registration

We process applications for registration as MPF intermediaries to engage in MPF sales and marketing activities. New applicants or applicants who have left the industry for three years or more are required to take an examination.

#### 295 complaint cases against trustees were received:

-  235 cases relating to service quality were referred to the trustees concerned to address the issues<sup>3</sup>; and
-  60 other cases were enquired into with the trustees concerned.

#### 25 cases of suspected non-compliance were investigated.

Supervisory compliance letters were issued to trustees in 93 closed cases in relation to internal controls, regulatory obligations, record keeping, investment compliance, and scheme administration. 6 independent reviews were subsequently engaged by trustees to undertake improvement measures.

23 financial penalty notices were issued to trustees<sup>4</sup> (fined \$695,000 in total) for non-compliance.

Members of the public can check MPF intermediaries' registration through MPFA's website or hotline.

### Training

To maintain professional competencies in MPF business, subsidiary intermediaries must undertake a minimum of 10 hours of CPD activities on MPF each year.

Non-compliance may result in suspension or revocation of registration.

As at 31 March 2017, 38 activities in the form of courses, seminars, lectures or conferences were recognized as core CPD activities for MPF intermediaries. We carry out quality assurance checks on these activities, which include vetting the materials used, visiting classes and reviewing participants' evaluation.

### Supervision

MPF intermediaries are required to submit annual returns to MPFA within one month after the end of a calendar year. An "eService" platform is provided on MPFA's website for electronic filing of these returns. 73% of principal intermediaries and 60% of subsidiary intermediaries have made use of the platform to submit their returns for 2016. We will continue to promote wider use of this electronic platform.

We communicate regularly with intermediaries on regulatory requirements and legislative changes that impact on them. This year, two circulars were issued to them on regulatory issues, covering matters relating to personal account enquiries by intermediaries on behalf of scheme members. Five circulars were issued on administration issues, such as information about the DIS.

<sup>3</sup> 4 out of 235 cases were related to the DIS concerning trustees' handling of DIS enquiries.

<sup>4</sup> The non-compliance was in relation to scheme administration, including late reporting of default contributions to MPFA, late processing of transfer or payment of MPF benefits and failure to submit various returns or reports to MPFA, etc.

## Business Operations

### Enforcement

We regulate MPF intermediaries in conjunction with the frontline regulators (i.e. the Insurance Authority ("IA"), Monetary Authority and SFC) under a multi-regulator model. During the year, 10 on-site inspections were conducted by the frontline regulators.

Where intermediaries or unlicensed persons are suspected to have conducted regulated activities in contravention of the law, we will refer the cases to the relevant frontline regulator(s) for investigation, and impose disciplinary sanctions or take other enforcement actions where appropriate.

**In 2016-17,**



**28 complaints and referral cases against MPF intermediaries were received, mainly concerning failure to comply with the statutory conduct requirements.**

**8 cases concerning MPF intermediaries were referred to frontline regulators for investigation.**

**36 compliance advice or reminder letters were issued to principal or subsidiary intermediaries in 23 cases.**

**A disciplinary order of two-month suspension was made against an MPF intermediary, after the MPF Schemes Appeal Board upheld MPFA's decision.**

## MARKET EFFICIENCY

### Standardization, streamlining and automation of scheme administration

Administrative complexity is one of the challenges to maintaining cost-efficiency and effectiveness of the MPF System. A high percentage of scheme administration matters are still paper-based and processed manually by trustees, each with its own procedures and systems. Such phenomenon has added extra complexity and costs to the System.

Simplified and automated administration would enhance user experience by bringing more flexibility and higher quality services to employers and scheme members. High on MPFA's work agenda is to explore fundamental measures to standardize, streamline and automate MPF scheme administration in the long run with the help of technology.

To this end, we completed consultancy studies on the feasibility, cost-benefit and operational considerations of a preliminary conceptual model of infrastructure and processes for MPF scheme administration.

Along the same vision, the Chief Executive announced in the 2017 Policy Address that the next work target of MPFA is to put in place eMPF, a centralized electronic platform, to facilitate the standardization, streamlining and automation of MPF scheme administration. In this regard, we will work closely with the Government in pursuing the initiative.

### Financial Technology ("Fintech")

Fintech is driving innovation and is now commonly considered to cover areas such as payments, big data analytics, applications, etc. Fintech will change the nature of commerce and end-user expectations for financial services.

We are in close liaison with the stakeholders concerned and keeping in view the development of Fintech to understand the benefits and risks that it will bring about, as well as its possible application to enhance the MPF system.

# Business Operations

## Cybersecurity

With growing concern over cybersecurity issues, we shared views with Hong Kong Monetary Authority (“HKMA”) and briefed trustees on the importance of cybersecurity risk management.

We discussed with trustees international principles and guidelines on cybersecurity and the steps they should take to protect their technological assets and customer information against cybersecurity threats.

We also reminded trustees to set cybersecurity strategies and urged them to conduct regular self-assessment and testing on cyber-resilience for withstanding and recovering from disruption caused by cyber attacks.

## PROTECTING MPF BENEFITS

### Non-compliant employers

One of MPFA’s primary missions is to protect the rights and interests of MPF scheme members. We take enforcement actions against non-complying employers, including filing civil claims to recover default contributions on behalf of affected employees and initiating criminal prosecutions to instil deterrent effect. In the year, we reviewed our strategies and measures of working with trustees to enhance efficiency of operation in tackling default contributions.

In 2016-17,



2 067 employment establishments were visited under proactive inspection (major targets included catering establishments, retail outlets and construction sites).

278 900 payment notices were issued in respect of default contribution under MPF schemes<sup>5</sup>.

60 049 cases were investigated<sup>Δ</sup>

#### breakdown of alleged offences

Default contribution	59 666 cases
Non-enrolment	1 339 cases
Forced change to self-employed person	20 cases
Others <sup>6</sup>	559 cases

<sup>Δ</sup> as one case may be related to several types of alleged offences, the total number of alleged offences may exceed the total number of complaints

In respect of substantiated non-compliance, civil claims were filed with:

Small Claims Tribunal	538 cases
District Court	61 cases
High Court	1 cases
Bailiff	26 cases
Liquidators	143 cases

36 Garnishee Orders were granted by court to freeze employers’ bank accounts.

9 court orders were granted by court to compel convicted employers to rectify non-compliance with contribution requirements.

\$136.9 million outstanding contributions in MPF schemes were recovered on behalf of employees.



<sup>5</sup> A surcharge calculated at 5% of the amount of MPF contributions in arrears is imposed on employers who failed to make MPF contributions for their employees within the prescribed period. The surcharges received are credited into the MPF accounts of the employees concerned.

<sup>6</sup> Others include failure to notify trustees of termination of employment, failure to issue monthly pay record, etc.

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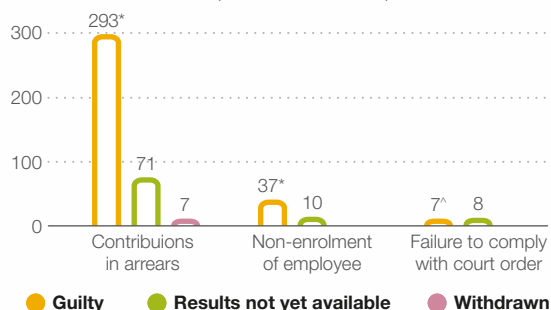
### Prosecution actions taken in 2016-17



**433 summonses were issued to employers and directors/managers of limited companies for prosecution in respect of their suspected non-compliance.**

In a landmark case, the Department of Justice applied to the High Court for leave to commence criminal proceedings against an employer for failing to arrange MPF enrolment and make contributions for its employees, notwithstanding that the company was in the process of winding-up and a provisional liquidator had been appointed. The employer was later convicted and fined \$147,500 by the court.

### Prosecution Status (as at 31.3.2017)



\* involving 53 employers (total fine: \$1,110,700)

^ involving 5 employers and 2 directors of limited companies (fined between \$6,000 and \$30,000 each). One of the directors was also sentenced to 4 months' imprisonment suspended for 2 years in addition to the court fine imposed.



**71 financial penalty notices were issued to repeat defaulters for breach of section 7A(8) of the MPFSO<sup>7</sup> (involving 69 employers and a total penalty of \$790,108).**

**We maintain a Non-Compliant Employer and Officer Records section on MPFA's website. From the database, members of the public can view and search for information on employers and officers with MPF non-compliance records.**

**As at 31.3.2017**



**2 546 non-compliance records were kept in the database, including:**

- 1 907 civil awards or judgments
- 639 criminal conviction records

## Non-compliant members of MPF schemes

Permanent departure from Hong Kong is one of the grounds on which scheme members may withdraw their MPF benefits before attaining retirement age. Some scheme members abuse the arrangement and make false claims to withdraw their MPF benefits on this ground. This affects the amount of savings available to them for retirement. We take prosecution actions in respect of substantiated cases.

Moreover, to tackle syndicate crime in arranging scheme members to make false claims in MPF withdrawal, MPFA refers cases to the Police for investigation from time to time. Four scheme members were charged in 2016-17 and sentenced to 81 to 160 hours of community service.

### In 2016-17

**78 summonses were issued to scheme members.**

Prosecution status (as at 31.3.2017)



<sup>#</sup> involving 42 MPF scheme members (average fine imposed: about \$6,100)

<sup>7</sup> Failure to pay MPF contributions in respect of an employee to the approved trustee within the prescribed period.

<sup>8</sup> MPF scheme members made a false statement in order to withdraw their MPF benefits on the ground of permanent departure from Hong Kong.



ORSO SCHEMES

Work of the Registrar of Occupational Retirement Schemes

The MPFA is the Registrar of Occupational Retirement Schemes. We process applications and notifications of changes, monitor compliance, recover default contributions, collect periodic fees, handle enquiries and complaints, and maintain a public register of ORSO schemes.

In 2016-17,

Approved the registration of 39 ORSO schemes.

Approved ORSO exemption in respect of 9 schemes.

Approved MPF exemption in respect of 5 registered schemes<sup>9</sup>.

Processed 4 250 annual returns and financial statements of ORSO registered schemes.

Granted consent to 9 ORSO registered schemes for cessation of application of pooling agreements to the schemes.

Processed 21 overseas compliance certificates and 556 membership statements of ORSO exempted schemes.

Approved 106 applications for change of trustees for MPF exempted ORSO registered schemes.

Processed 991 notifications of changes in relation to scheme name, administrator, employer and address.

Approved withdrawal of MPF exemption in respect of 112 ORSO registered schemes and 27 ORSO exempted schemes.

Processed notices of termination given by 139 ORSO registered schemes and 87 ORSO exempted schemes.

Granted consent to 78 applications for consent for disclosure of information in compliance with the US Foreign Account Tax Compliance Act.



9 MPF exemption refers to an exemption under section 5 of the MPFSO. Members, or a class of members, of an MPF exempted ORSO scheme and their employer are exempt from the operation of all or any specified provisions of the MPFSO. This is an interface arrangement with the MPF System when the System was launched in 2000.



## Business Operations

### Funding status of ORSO registered schemes

We monitor the funding status of ORSO registered schemes by examining annual returns and audited financial statements. For defined benefit schemes, actuarial certificates must be supplied by designated persons at least once every three years.

According to the relevant reports received up to 31 March 2017,



17 out of 211 defined-benefit ORSO schemes were under-funded, covering around 7 800 scheme members.

Total asset size of these under-funded schemes amounted to \$11,542 million.

Total shortfall of these under-funded schemes was \$662 million (about 5.7% of their total assets). The shortfall was caused by investment loss and/or salary increase higher than the assumption used by actuaries.

The relevant employers have to make up the shortfall in funding by a lump sum contribution or monthly contributions within three years and to submit actuarial certificates annually until the schemes were fully funded. We closely monitor the situation, and the process of making up the shortfall by the relevant employers is smooth.

### Relinquishing of MPF exemption status of ORSO schemes

During the year, 139 MPF exempted ORSO schemes, covering about 500 scheme members, relinquished their exemption status. The employers subsequently terminated these schemes and had to enrol the employees in MPF schemes.

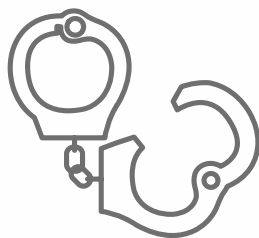
Non-compliance under ORSO

In 2016-17, the following actions were taken to recover default contributions on behalf of affected employees:

233 payment notices were issued in respect of default contribution under MPF exempted ORSO registered schemes<sup>10</sup>.

1 civil claim was filed with Small Claims Tribunal.

\$2.2 million outstanding contributions in MPF exempted ORSO registered schemes were recovered on behalf of employees.



We took the following actions in 2016-17 to deal with members of MPF exempted ORSO schemes who made false statements in order to withdraw their minimum MPF benefits on the ground of permanent departure from Hong Kong before attaining retirement age:

2 cases were referred to the Police for investigation.

The prosecution results of 3 cases<sup>11</sup> were reported from the Police.

Prosecution Status (as at 31.3.2017)



**● Guilty ● Acquitted ● Results not yet available**

# 1 case was referred to the Police before 2016-17, and 1 case was referred to the Police in 2016-17. The cases involved 2 ORSO scheme members (sentenced to 80 hours of community service and three weeks' imprisonment respectively).

10 A surcharge calculated at 15% or 20% of the amount of ORSO contributions in arrears is imposed on employers who failed to make ORSO contributions for their employees. No surcharge will be imposed in the first payment notice in respect of ORSO contributions.

11 Including 2 cases referred to the Police before 2016-17.