Form for Responding to Consultation Questions

Q1. Do you support the direction of introducing a core fund in the manner set out in paragraph 36 (a) to (d) above?

Comments:

The objective of the MPF system reform is to allow scheme members to have an investment that will generate into retirement savings at a low cost.

At present, there are a very limited number of MPF service providers in the market, serving around 2.7 million employees in Hong Kong. As a result, there is a lack of incentive for these service providers to engage in a competition on price in order to attract customers.

We welcome the introduction of a core fund, whereby the cost is going to be low. For the service providers to be able to offer a new core fund at a fee of 0.75% or less, their costs have to be lower than the fees. It appears that it will be a challenging feat to accomplish. Service providers are not very likely going to operate a fund that does not yield too much of a profit to them, as there needs to be a strong reason for them to be offering a fund for 0.75% only when compared to 1.75% that they have normally been charging. For example, the service providers must offer such a fund because the relevant laws so require. On the other hand, in general, there needs to be sufficient volume in order for the fees to stay low, which would only be possible if there is a single service provider offering such a fund for all the scheme members.

In order to create a low fee environment, the Mandatory Provident Fund Schemes Authority ("MPFA") has the following options:

1. Introducing more service providers to the market

MPFA may introduce more players in the market so as to create more competition, which would have an overall effect of fees being kept at a competitive rate. As of this moment in time, however, the barrier to entry is high, which makes it difficult for institutions that have a great potential to provide better services and solutions at lower rates to enter the market. We are of the suggestion that MPFA review the current requirements for firms and institutions to become service providers and see if the barrier to entry can be lowered while maintaining a certain standard.

2. Offering the scheme members the freedom to choose on the fund(s) to invest in across a board of all available MPF funds offered by all the service providers

We are also of the opinion that MPF scheme members should have the freedom to choose from all the available funds instead of just the funds provided by a single service provider.

Since 1 November 2012, the MPF Employee Choice Arrangement (ECA) has come into effect, whereby employees have been given more autonomy to handle their own MPF investments. Employees may transfer accrued benefits from former employment or self-employment in the employees' contribution accounts to a service provider and scheme of their own choice.

While the ECA has given scheme members more freedom and autonomy over their investments, according to surveys conducted by institutions, close to 90% of scheme members have not made any switch in service providers since its introduction. The corresponding procedures in making switches appear to be complicated to most scheme members, and most scheme members are also feeling that the associated fees have not been reduced since the introduction of the ECA.

To address the issues, there needs to be a mechanism whereby it would be easy for the scheme members in making switches from one service provider to the next, and also that there needs to be a more effective way in driving the costs down from the scheme members' perspectives.

When scheme members have the ability to choose from all the funds provided by all the service providers, in order to remain competitive and to attract more customers, the service providers would need to offer funds at relatively lower rates.

At present, the service providers have been administering the records of the scheme members. This is the result of either that the employer has chosen to enroll in a scheme offered by a service provider, or that the employee has chosen to enrol with a service provider since the introduction of the ECA.

In order to facilitate the administration of the records of the scheme members, complete with their employment details and investment choices, a centralized administration system would be necessary. The MPFA may take on the role of a central administrator. Each scheme member may select from the different lines of funds provided by the different service providers as he/she wishes, and he/she can switch from fund to fund at any given time. Each time when a scheme member changes his/her investment selection(s), MPFA as the central administrator would make the corresponding updates on the database.

Under this model, when a scheme member changes job, he/she would only need to update his/her employment details with MPFA and continue on with his/her existing investment selections, without the need to enroll in a new scheme offered by another service provider and to worry about the investment left over from the scheme in his/her previous employment.

Q2. Do you agree that the CF that is the default fund should be substantially the same in all MPF schemes?

Comments:

If the CF is substantially the same in all MPF schemes, it will just be the same kind of investment for all the service providers, without much variation. The result is that there will not be much comparison from the consumer's perspective. When all the service providers are offering the same product, the lack of variation and niche among the funds would reduce competition over time, and the need for service providers to lower their fees to remain competitive.

Q3. Do you agree that it is appropriate that the core fund be based on a standardized default fund? Comments: We agree that the core fund may be used as a default fund for those scheme members who are not going to choose their own funds. Standardizing the fund would have the effect of a lack of uniqueness to attract customers, and hence a lack of competition over time.
Q4. Do you agree that the appropriate investment approach of the core fund is one that automatically reduces risk over time as the member gets closer to age 65? If not, what other option would you propose? Comments: We generally agree that the investment approach of the core fund would automatically reduce risk over time as the scheme member approaches the age of 65, in line with the investment attitude of the majority of the population.
Q5. Do you have any preliminary views on the technical issues set out in paragraph 48, in particular whether consistency is required on all aspects of default fund design in all schemes or can some elements be left to the decision of individual product providers? Comments: We are in general neutral on the technical issues set out in paragraph 48 of the Consultation Paper.
Q6. Do you agree that keeping total fee impact for the core fund at or under 0.75% is a reasonable initial approach? Comments: While scheme members would welcome a fund with a low fee, ultimately there needs to be incentives for scheme members to be able to have an investment that presents a reasonable savings return for their retirement in a cost effective manner. On the other hand, in order for service providers to be able to offer a core fund at or under 0.75%, in general they will need to see the benefits of doing so. When offering a core fund at such a rate is not enforceable by law, there is no obligation for service providers to create a fund whose profit margin is much less than what they have been earning, and given the amount of administrative costs involved. MPFA may consider sponsoring a centralized core fund itself, and have the Core Fund to be included in the product range of the service providers. Service providers would generally be in favour of outsourcing low-fee bonds to other product manufacturers.

Offering a centralized core fund will pave the way for MPFA in becoming the central administrator for the scheme members. If the scheme members are able to freely choose their own funds from a board of different service providers along with the core fund, eventually service providers would have to keep their fees at a relatively low level while offering a high return in order to remain competitive.

Q7. Do you agree that keeping total expense impact (i.e. FER) for the core fund at or under 1.0% over the medium term is a reasonable approach?

Comments:

We generally agree that the expenses for the scheme members should be kept at a minimum. Having a medium term approach would have the same effect as not having one. The existing service providers are more than likely going to create a new fund at a low fee only if there are enough benefits for them (for example, a very high volume). The MPFA sponsoring the new core fund and taking over the administration role would be the more reasonable approach.

Q8. Do you agree that passive, index based, investment strategies should be the predominant investment approach in the MPF core fund?

Comments:

We are of the opinion that the MPF core fund should present a low risk investment to the scheme members.

Q9. Are there particular asset classes which you think would not appropriately be invested on a passive, index based approach?

Comments:

We have no opinion in this area.

Q10. Do you agree that the name of the core fund should be standardized across schemes? If so, do you have any preference amongst the possibilities set out in paragraph 77 above?

Yes No

Your preference:

"MPF Core Fund" (having regard to its use as a core investment approach for retirement savings)

Comments:

Q11. Do you agree with the general principle for dealing with implementation and transitional issues as set out in paragraphs 78 and 79? Comments: Existing scheme members should be notified of the availability of a new core fund in place, but should not be forced to have their accrued benefits and future contributions to be invested in the new fund unless they have made a positive indication of their intention to do so.
Q12. Do you agree with the proposal in paragraph 81 as to how to deal with the transition for existing MPF members of default funds? Comments: Scheme members should not be forced into investing in a new core fund unless they have made a positive indication that they are intending to do so.

Information of Respondent

(Please refer to the Personal Information Collection Statement on pages 47 and 48 of this Consultation Paper)

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