



OECD/IOPS Conference Private Pensions in Asia

“Individual Choice in Retirement Arrangements”

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27 April 2005



The Regulation of Choice under Hong Kong MPF

- 1. Background to Retirement Saving System in Hong Kong**
- 2. Policy and Legal Framework**
- 3. MPF Scheme Structures**
- 4. Regulation of Intermediaries**
- 5. Disclosure Regulation**
- 6. Is member choice a good idea?**



1. Background to Retirement Saving System in Hong Kong

Prior to December 2000 -

Occupational Retirement Schemes

- Voluntary System
- Sponsored by employers
- Defined benefit or defined contribution
- Trust-based or insurance arrangement
- Regulatory focus on funding



1. Background to Retirement Saving System in Hong Kong

(cont'd)

Since December 2000 -

Mandatory Provident Fund Schemes (MPF)

- 2nd pillar of World Bank's suggested 3 pillar approach
- Employment based, mandatory system
- Privately managed
- Defined contribution
- Trust-based



2. Policy and Legal Framework

Policy Tensions

- Employer selects trustee and scheme, enrolls employee and remits contributions to trustee
- Inconvenient and expensive to deal with multiple trustees
- Employees are the primary stakeholders of benefits and better able to assess needs and risk appetite
- Employees wanted a low/no risk option



2. Policy and Legal Framework (cont'd)

Policy Tensions (cont'd)

- Employers also opposed to choice because of severance/long service payment offset
 - Employers may bear loss for bad investment decision
- Limited financial resources of small employers
 - More concerned with lack of control over investment choice and admin burden



2. Policy and Legal Framework

(cont'd)

Compromise solution

- Maximum choice within practical limits
 - Employers choose trustee and scheme
 - Employees choose funds within scheme
 - Self employed persons choose trustee and fund
 - Employees can also choose trustee and fund for preserved a/c and for some voluntary contributions



2. Policy and Legal Framework (cont'd)

Compromise solution (cont'd)

- Few rules about structure or range of choice
- Essentially regulated by
 - giving members information so they can make a choice (disclosure regulation)
 - minimizing fee obstacles
 - regulating the giving of advice (intermediaries)
 - educating the members
 - market forces re range of choice



2. Policy and Legal Framework (cont'd)

- **Law does not require > 1 fund per scheme**
 - Mandatory to offer “capital preservation fund”
 - Practical minimum choice is capital preservation fund and at least one other
 - Average is 7 choices of fund
 - Min 2; Max 29 funds to choose from
 - Any “default” choice left to scheme rules but generally CPF or money market



2. Policy and Legal Framework

(cont'd)

- **Single or multi manager choice**
 - No rules
 - Most schemes (42) only offer funds by one manager
 - Only 2 schemes offer choice across different managers



2. Policy and Legal Framework (cont'd)

- **Types of funds offered**
 - No rules except requirement for capital preservation fund
 - Around half offer only pre-mixed fund range (growth, stable growth, balanced, guaranteed etc.)
 - Around half offer pre-mixed plus some asset class choice (regional equity, global equity, bond, money market etc.)
- **Currently no fee for switching choice of fund**



3. MPF Scheme Structure

- **MPF Schemes set up under trust**
- **Each scheme provides fund options**

Example of an MPF scheme

MPF Scheme				
Capital Preservation Fund	Equity Fund	Bond Fund	Balanced Fund



3. MPF Scheme Structure (cont'd)

Common Types of Funds

- **Capital Preservation Fund**
 - Invests exclusively in short-term Hong Kong Dollar bank deposits and high quality bonds
 - Administrative fees can only be deducted when returns for the month exceed the banks' savings rate
- **Money Market Fund**
 - Invests generally in short-term high quality interest bearing instruments



3. MPF Scheme Structure (cont'd)

Common Types of Funds (cont'd)

- **Guaranteed Fund**

- Provides a guarantee on the capital, or a minimum rate of return
- Usually subject to certain qualifying conditions (e.g., stay in the fund for a min.period)

- **Bond Fund**

- Invests in bonds or debt instruments issued by governments / public organizations / large corporations that meet certain minimum credit rating requirements



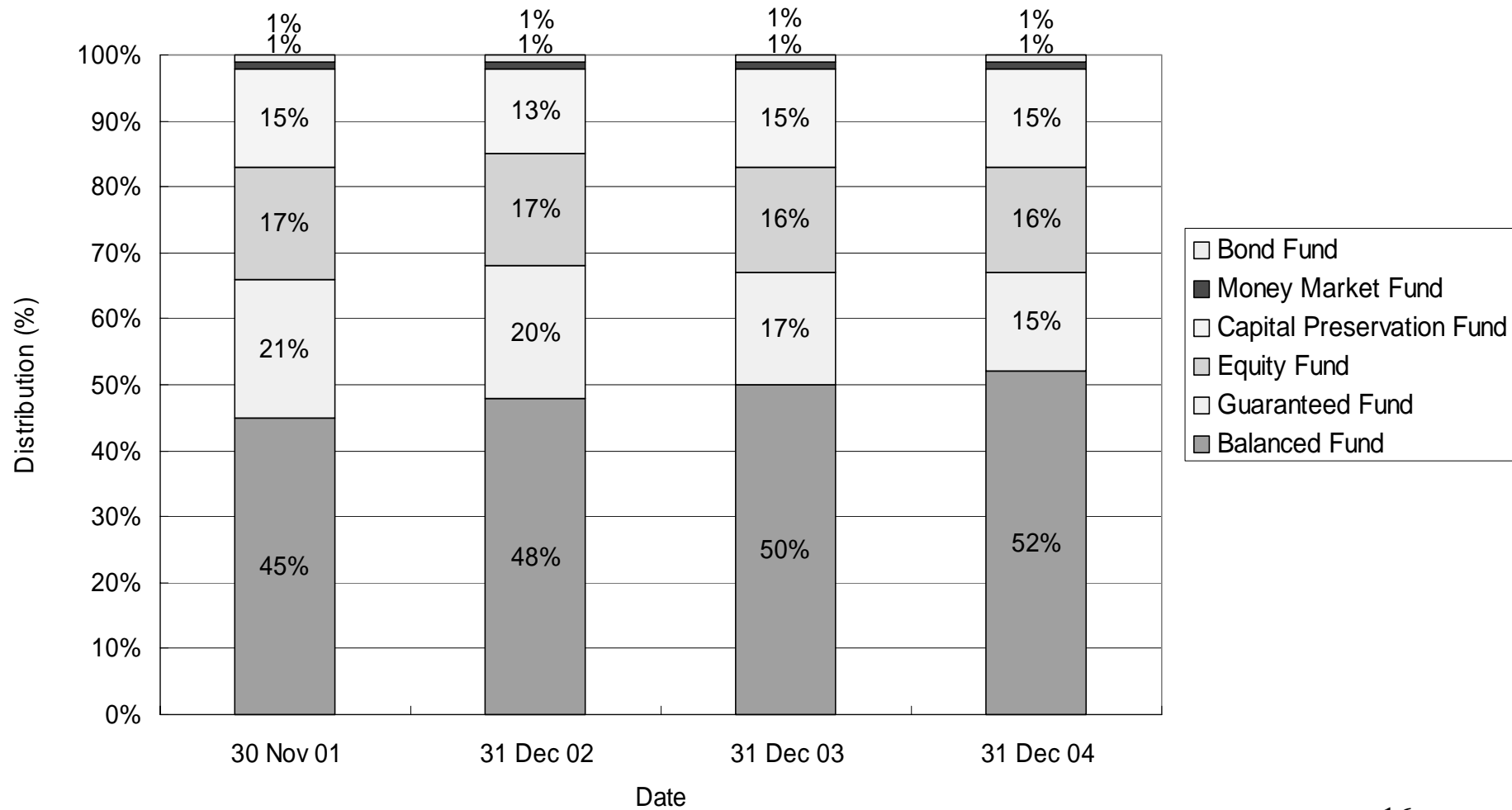
3. MPF Scheme Structure (cont'd)

Common Types of Funds (cont'd)

- **Balanced Fund (or “Mixed Asset” Fund)**
 - Invests in both equities and bonds, either globally or regionally
- **Equity Fund**
 - Sometimes called aggressive fund or growth fund, primarily invests in equities traded on recognized stock exchanges



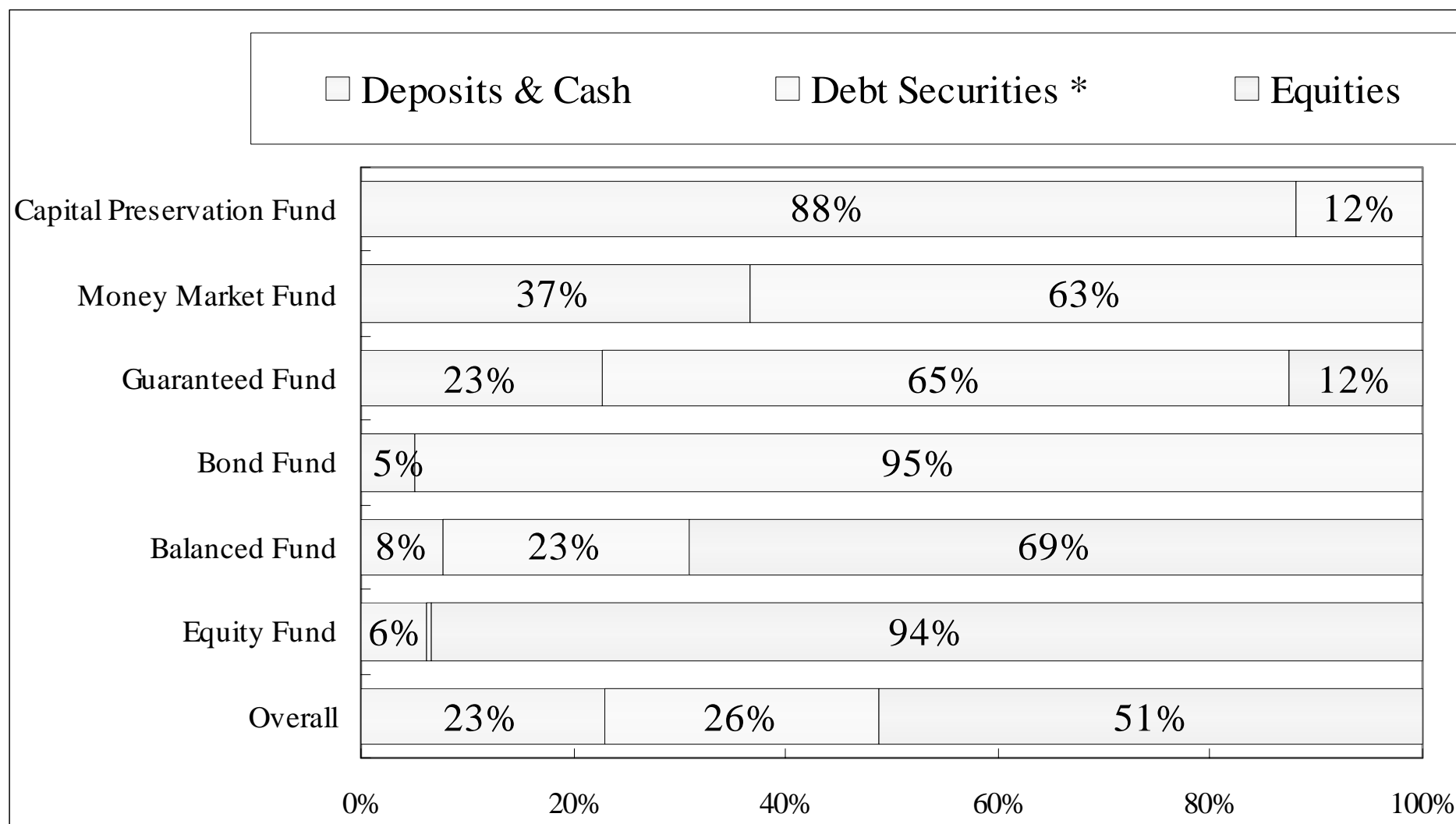
Asset Distribution by Fund Types





Asset Allocation by Asset Class

- as at 30 September 2004



* Including convertible debt securities



4. Regulation of Intermediaries

- **Jointly regulated with 3 frontline regulators**
 - Securities and Futures Commission
 - Hong Kong Monetary Authority, and
 - Insurance Authority
- **Intermediary must be registered with MPFA**
 - Supervised by one of frontline regulators
 - Pass MPFA exam
 - Be fit and proper



4. Regulation of Intermediaries

(cont'd)

- **MPFA Code of Conduct for MPF Intermediaries**
 - Regulatory arrangements
 - Registration requirements
 - Principles of conduct



5. Disclosure Regulation

- **Quality disclosure is critical if members are to make informed choices**
- **Disclosure jointly regulated by MPFA and SFC**
 - Both have a role re offering documents
- **MPFA major project in 2003/2004 to improve disclosure of**
 - Fees and charges
 - Performance information



5. Disclosure Regulation (cont'd)

- **“Code on Disclosure for MPF Investment Funds” issued 30 June 2004**
 - Five ‘good disclosure principles’ (facilitate decision making, timely, promote comparability, consistent, clear & concise)
 - Standard form fee table
 - Ongoing cost illustration
 - Fund fact sheets
 - Expense ratios



5. Disclosure Regulation (cont'd)

- **Next phase is to improve ‘after the event’ disclosure**
 - Less relevant to choice
 - More relevant to personal financial planning
 - Focussed on benefit statements and similar information
 - Focus on performance, fees and charges
- **Later phase is to develop a platform for comparison to facilitate choice of fund**



6. Is Member Choice a Good Idea?

Is it sensible to leave asset allocation decisions to members?

- Matching asset allocation to needs is extremely difficult
- Sub-optimal choices will increase social/economic stresses on governments
- Sub-optimal choice by members is almost certain

on the other hand ...

- Individuals best placed to assess own needs
- Members want control



6. Is Member Choice a Good Idea? (cont'd)

Is there any point in allowing choice across providers?

- Performance comparison almost impossible
- Fee comparison difficult
- Services comparison difficult

How many choices are too many?

- Research suggests that consumers can't handle decision making across > 6 items



6. Is Member Choice a Good Idea? **(cont'd)**

Liability for choice?

- Where provider has some discretion, could they be liable for offering inappropriate choices?
- US litigation - WorldCom, Dynergy, Polaroid, Enron



Thank you