



# OECD/IOPS Global Forum on Private Pensions

## **Supervision of DC Schemes - Conflicts of Interest**

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# Conflicts of Interest in DC Schemes



# Theoretical Framework

- Refers to those circumstances where there is a misalignment of interests between an operator and a scheme beneficiary
- Usually relates to risk of transferring monetary or other opportunity from member to operator



# Theoretical Framework (cont'd)

- Control mechanisms typically
  - Direct prohibition in the law
  - Changing the nature of the relationship to import equitable / fiduciary duties (e.g. to require the operator to place member interests above their own and to avoid conflicts of interest where possible)
  - Direct imposition of fiduciary like duties through law either in relation to specific issues / transactions or in managing conflicts of interest
  - Disclosure of the conflict of interest
  - Procedural safeguards such as approvals, compliance arrangements, record keeping, etc.



# Theoretical Framework (cont'd)

## The usual suspects

- In-house assets
- Related party transactions
- Best execution on trades
- Collateral benefits / soft commissions

## Not such 'usual' suspects

- Fees and charges
- Plan design



## A. Fees as a Conflict Issue

- A fairly obvious conflict of interest
- How does fiduciary duty apply in context? Does putting member first mean that:
  - providers should charge no fee?
  - ... or perhaps just enough to survive?
  - or as much as they want provided the parties 'agree' to it or it is disclosed?
- Some jurisdictions therefore regulate fee levels
- Most leave it to market forces but with intervention to ensure that the market has full information



# Supervision – Fund Fees in Hong Kong

- The level of fees and charges has been much discussed since disclosure improved in 2003 / 2004
- General position is to let market forces set fee levels – strategy therefore to help market forces work better

## **Demand Side**

- ▶ improve disclosure – make it consistent, prominent, easy to understand and compare

# Supervision – Fund Fees in Hong Kong (cont'd)



## Fees of all MPF Funds

### Criteria for Filtering the List of Funds

Fund Type  Trustee   
 Scheme

456 funds selected / Average FER = 1.89% / Median risk indicator = 16.09%

MPF Trustee	Scheme	Constituent Fund	Fund Type	Latest FER	OCI 1 Year	OCI 3 Year	OCI 5 Year	Fund Risk Indicator	Details
HSBC	Schroder MPF Master Trust	Schroder MPF Asian Portfolio - Class B	Equity Fund	1.73%	\$18	\$56	\$97	30.14%	<a href="#">More</a>
MassMutual	Mass Mandatory Provident Fund Scheme	Global Growth Fund	Mixed Assets Fund	1.73%	\$67	\$103	\$142	17.01%	<a href="#">More</a>
MassMutual	Mass Mandatory Provident Fund Scheme	Hong Kong Equities Fund	Equity Fund	1.73%	\$67	\$103	\$142	28.86%	<a href="#">More</a>
BCT	Bank Consortium MPF Plan	Bank Consortium Asian Equity Fund	Equity Fund	1.74%	\$18	\$57	\$97	30.39%	<a href="#">More</a>
BOCIP	BOC-Prudential Easy-Choice Mandatory Provident Fund Scheme	BOC-Prudential Asia Equity Fund	Equity Fund	1.74%	\$18	\$57	\$97	26.84%	<a href="#">More</a>
MassMutual	Mass Mandatory Provident Fund Scheme	Global Stable Fund	Mixed Assets Fund	1.74%	\$67	\$104	\$142	12.33%	<a href="#">More</a>
Sun Life	Sun Life Rainbow MPF Scheme	Sun Life First State MPF Stable Income Fund - B	Mixed Assets Fund	1.74%	\$18	\$57	\$97	9.31%	<a href="#">More</a>
BCT	RCM MPF Plan	RCM Balanced Fund - Class A	Mixed Assets Fund	1.75%	\$18	\$57	\$98	17.23%	<a href="#">More</a>
BCT	RCM MPF Plan	RCM Growth Fund - Class A	Mixed Assets Fund	1.75%	\$18	\$57	\$98	21.21%	<a href="#">More</a>



# Supervision – Fund Fees in Hong Kong (cont'd)



Average, Highest and Lowest FER of All Constituent Funds							
Fund Type	No. of Funds	Average FER	Name of Constituent Fund	Highest FER	Name of Constituent Fund	Lowest FER	Details
		%		%		%	
<a href="#">Mixed Assets Fund</a>	196	2.03	<i>BEA (MPF) Japan Growth Fund - BEA</i>	3.38	<i>Capital Stable Fund - BCT</i> <i>Balanced Fund - BCT</i>	1.26	<a href="#">More</a>
<a href="#">Bond Fund</a>	33	1.82	<i>Multi-Manager Global Bond Fund - AXA</i>	2.49	<i>Global Bond Fund - AIAT</i> <i>Global Bond Fund - AIAT</i>	0.13	<a href="#">More</a>
<a href="#">Equity Fund</a>	142	1.94	<i>Taifook Global Diversification Fund - HTHK</i>	3.90	<i>World Equity Fund - AIAT</i>	0.21	<a href="#">More</a>
<a href="#">Guaranteed Fund</a>	30	2.36	<i>Guaranteed Fund - MassMutual</i>	3.92	<i>Principal Capital Guaranteed Fund - Principal</i>	1.35	<a href="#">More</a>
<a href="#">Money Market Fund - MPF Conservative Fund</a>	48	0.92	<i>Manulife MPF Conservative Fund - Manulife</i> <i>Manulife MPF Conservative Fund - Manulife</i>	1.77	<i>MPF Conservative Fund - HTHK</i>	0.45	<a href="#">More</a>
<a href="#">Money Market Fund - non MPF Conservative Fund</a>	1	1.10	<i>Double Easy Cash Fund - AXA</i>	1.10	<i>Double Easy Cash Fund - AXA</i>	1.10	<a href="#">More</a>
<a href="#">Others</a>	6	1.56	<i>Principal HK Dollar Savings Fund - Principal</i>	1.60	<i>Principal US Dollar Savings Fund - Principal</i> <i>Principal HK Dollar Savings Fund - Principal</i>	1.35	<a href="#">More</a>
<b>Overall</b>	<b>456</b>	<b>1.89</b>		<b>3.92</b>		<b>0.13</b>	

# Supervision – Fund Fees in Hong Kong (cont'd)



## **Demand Side**

- improve disclosure – make it consistent, prominent, easy to understand and compare
- help focus members on importance of fees
- portability

## **Supply side**

- encourage greater use of simple low cost products and discouraging product proliferation
  - reduce scheme operation costs / complexity where possible
  - facilitate entry / exit in market
  - achieve scale benefits by facilitating voluntary contributions
- Improvements are gradual, around a 10% drop in last 2 years
  - Expectations of more significant reductions



## B. Plan Design as a conflicts issue

- Ensuring that funds are structured in members' best interests is also a conflict of interest issue
- Provider's motives in scheme / fund design are not always aligned with the best interest of members

**Example 1** – greater use of passive investment structures

- Given evidence about relative merits of active vs passive management there should be greater use of index strategies
- If not for whole of fund then at least to gain core market exposure
- Should still be scope for those who genuinely believe they can add alpha



# Plan Design as a conflicts issue (cont'd)

- Supervisory strategy
  - Requiring providers to actively consider issue
  - Requiring providers to document their consideration of the issue
  - Providing evidence to the industry about active vs passive management outcomes

## **Example 2** – using 3<sup>rd</sup> party investment products

- Several connected issues
  - Using existing underlying funds rather than creating new ones
  - Looking outside proprietary arrangements
  - Aggressive review of manager performance
- Supervisory strategy
  - Requiring providers to actively consider issue
  - Requiring providers to document their consideration of the issue



# Plan Design as a conflicts issue (cont'd)

## Example 3 – range of investment options

- Is it in members' interests to offer an ever expanding number of fund choices?
- Is it in members' interests to offer higher and higher levels of investment risk?
- MPFA has consulted industry on whether number and range of investment options should be limited
- Proposal 1 – no explicit limit on number of funds but no type replication allowed and applicant required to justify how addition is in members' interests
- Proposal 2 – funds with investment risk greater than regional equity fund should not be approved (except Hong Kong / Greater China equity funds)
- Diversity of views expressed



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