



Extra Lifesavers Ma Kwan Ching, aged 5
Extra lifesavers can not only keep us afloat, Kwan Ching makes sure that they also keep her in style and fashion.



In the first full year of operation of the MPF System, MPF trustees and other service providers made significant improvements in familiarizing themselves with the full details of the System and smoothing the scheme administration process. In the course of discharging its supervisory functions, the MPFA provided assistance to the industry in overcoming the teething problems in scheme administration, which arose in the initial months of MPF launch.

Supervision of the Industry

Supervision of Trustees

The trustee of a MPF scheme is the central party having overall responsibility for the administration and management of the scheme. A trustee may delegate part of its functions to other service providers but the trustee has the duty to supervise and exercise proper control over these service providers.

In the initial months of MPF contributions, MPF trustees experienced some operational problems and encountered substantial numbers of discrepancies in contribution data and payments, which were mainly attributable to the unfamiliarity of employers and self-employed persons with the MPF System. After having accumulated operational experience, the trustees showed significant improvements in the accuracy and efficiency in processing contributions during the year. By increasing staff resources, streamlining procedures, enhancing their internal systems and providing appropriate assistance to the employers, they managed to substantially reduce processing backlogs and increase the operational efficiency in various stages of contributions processing.

Inspection Visits to Trustees

In year 2000-01, the MPFA carried out on-site inspections of the approved trustees mainly to assess their readiness for the commencement of MPF contributions on 1 December 2000. In the past year, the on-site inspection programme was refocused to ensure the trustees' on-going compliance with various aspects of the MPF legislation. All aspects of the trustees' operations, including the processing of contributions, fund switching and benefit transfers, were scrutinized.

Some non-compliance issues were discovered during inspection visits, including failure to complete transfer-out and payment of benefit requests within the statutory timeframe, late reporting of events of a significant nature, technical breaches of the 10% investment rule (the rule prohibiting the investment of more than 10% of total scheme assets in any single investment) and acquisition of non-permissible investments. With regard to these cases of non-compliance, the MPFA issued a total of four financial penalty notices to trustees during the year. The MPFA monitored all the breaches closely and made sure that remedial actions were taken by the service providers. Subsequent improvements were found in the operations of scheme administrators and the monitoring mechanisms of the trustees over other service providers.

Ongoing Monitoring

To ensure that the approved trustees comply with the statutory requirements and to enable early detection of deficiencies, 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. For the protection of scheme members' interests, necessary follow-up actions and special investigations will be carried out if deficiencies or contravention of the MPF legislation are identified.

The MPFA is also responsible for processing changes of officers and other information of the approved trustees to ensure that they comply with the MPF legislation and the conditions of approval. New appointment of directors or chief executive officers of approved trustees must have the prior consent of the MPFA based on the same approval requirements as adopted in the initial approval process. During the current financial year, the MPFA gave consent to the appointment of 45 directors or chief executive officers.

Meetings and Workshops

Apart from inspection visits, the MPFA started regular meetings with individual trustees in June 2001 to keep abreast of the trustees' MPF operations and provide a channel for the trustees to raise their concerns and other issues with a view to addressing those issues more promptly. The meetings were very constructive as they facilitated direct communication between the trustees and the MPFA.

In the early months of the reporting year, the MPFA organized a series of workshops for trustees and other service providers to clarify the procedures relating to such issues as contribution arrangements and benefit transfers. These briefings helped the MPF intermediaries and the frontline staff of the trustees in familiarizing with scheme administration issues and in smoothening their operations.

Complaints Against Trustees

A total of 1 329 complaints received by the MPFA in the year were lodged against trustees. Most of them were related to scheme administration. Considering the massive numbers of accounts involved in the MPF System (about three million in total), the number of complaints was relatively small. The majority of the complaints were lodged in the early months of the reporting year. The number of complaints decreased over the year as the operation of most trustees continued to stabilize and improve.

Resignation of Trustees

The MPFA approved two cases of application for resignation as the approved trustee of MPF schemes. The resignations took effect between January and March 2002. In both cases, as the resigned trustees' functions were taken over by existing approved trustees and as the resignation did not involve a change of scheme administrators, the changeover of business went smoothly. The two trustees retained their approval status for the purposes of managing MPF approved pooled investment funds.

A list of the approved trustees and their background as at 31 March 2002 is at Appendix 7.

Monitoring of MPF Investments

With the implementation of the MPF System, the emphasis of the MPFA's work in respect of the regulation of MPF investment was shifted from the registration and approval of schemes and funds to the monitoring of compliance with investment requirements. Efforts were made during the year to strengthen the MPFA's capabilities in this respect.

Review of Investment Regulation

The MPFA is responsible for regulating all relevant parties under the MPF System and protecting the interests of members of MPF schemes. Investment regulation is therefore very important in the regulatory framework. A panel of international experts on risk management and investment was commissioned, with the assistance of the Securities and Futures Commission, in May 2001 to conduct a review on risks associated with MPF operations. Issues related to investment regulation reviewed included the risk of diversion of funds from MPF schemes, potential for inflated fees and charges, conflicts of interest among service providers, and the adequacy of regulatory arrangements to address operational risks and disclosure requirements.

Based on the findings of the review, the panel made a number of recommendations which primarily focused on the MPF legislation, the existing regulatory arrangements, the development of technical expertise at the MPFA and the disclosure of information to scheme members. In the light of those recommendations, MPFA has taken steps to enhance its capabilities in investment regulation and supervision. It is also examining those recommendations relating to streamlining of MPF scheme administration, in consultation with the industry and other stakeholders.

Registration and Approval of Schemes and Funds

MPF products include schemes, constituent funds and pooled investment funds. Following the implementation of the MPF System at the end of year 2000, the amount of work related to the registration of schemes and approval of funds was largely reduced. Isolated applications for registration were received and processed. 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 2001	De-registration/ Revocation during the year	Registration/ Approval during the year	Number as at 31 March 2002
Registered Schemes	51	0	0	51
<i>Master Trust Schemes</i>	47	0	0	47
<i>Industry Schemes</i>	2	0	0	2
<i>Employer Sponsored Schemes</i>	2	0	0	2
Approved Constituent Funds	299	0	12	311
Approved Pooled Investment Funds	231	14	3	220

Table 2. Analysis of approved pooled investment funds

	Unit Trust		Insurance Policy		Total	
	as at 31 March 2001	as at 31 March 2002	as at 31 March 2001	as at 31 March 2002	as at 31 March 2001	as at 31 March 2002
By fund valuation bases						
<i>Unitized</i>	167	156	61	61	228	217
<i>Non-unitized</i>	0	0	3	3	3	3
Total	167	156	64	64	231	220
By fund structures						
<i>Umbrella funds</i>	22	21	4	4	26	25
<i>Internal portfolios</i>	113	107	36	36	149	143
<i>Feeder funds</i>	5	5	15	15	20	20
<i>Portfolio management Funds</i>	27	23	9	9	36	32
Total	167	156	64	64	231	220

In the past year, various changes to the structures of MPF schemes and approved pooled investment funds were made by the service providers, including changes in fees and charges and adjustments in the administrative aspects of the schemes. These changes were made in response to market demand and/or in view of operational needs. The statistics of amendments processed are summarized in Table 3.

Table 3. Statistics of processing amendments to registered schemes and approved funds as at 31 March 2002

	Completed	In Progress	Total
Registered Schemes	80	19	99
Approved Pooled Investment Funds	41	6	47
Total	121	25	146

Monitoring of Investment Compliance

The MPFA monitored MPF investment compliance by periodically conducting on-site inspection visits to the trustees and regularly reviewing the various types of returns and reports submitted by the service providers. No substantive problems or irregularities were noted, other than certain technical breaches of the diversification rule and acquisitions of non-permissible investments.

Market Developments

A number of developments in the market affecting MPF funds were notable during the year.

PRESCRIBED SAVINGS RATE

According to the Mandatory Provident Fund Schemes (General) Regulation, administrative expenses (other than the Compensation Fund levy) may be deducted from the capital preservation fund of a MPF scheme in each month. The expenses may be deducted only if the investment income of the fund for that month exceeds the amount of interest that would be earned if the fund has been placed on deposit in a Hong Kong dollar savings account at the prescribed savings rate determined by the MPFA. Where such deduction is made from the capital preservation fund, the amount is limited to the actual return in excess of the interests earned at the prescribed savings rate.

The basis for determining the prescribed savings rate for each month is specified in the Guidelines on Capital Preservation Funds. This set of guidelines was revised in June 2001 in anticipation of the de-regulation of the Interest Rate Rule applicable to Hong Kong Dollar Savings Accounts in July 2001. The revised guidelines specify that the prescribed savings rate is to be determined by taking the simple average of the interest rates on savings deposits of \$120,000 offered by the three note-issuing banks in Hong Kong.

SUSPENSION OF DEALINGS OF MPF FUNDS

Due to the suspension of trading of the US stock exchanges during 11-14 September 2001 inclusive, the 20 approved trustees declared suspension of dealing in the constituent funds of their MPF schemes and the associated approved pooled investment funds. As a result, 267 constituent funds and 172 approved pooled investment funds were affected. The decision to suspend trading was promptly reported to the MPFA and communicated to scheme members via announcements in the press. Trading in all of the funds was resumed by 18 September 2001.

Statistics

Statistics on MPF schemes and funds are included in Part B of the Statistics section.

Supervision of Intermediaries

MPF scheme members are directly served by intermediaries who sell MPF products and advise on the schemes and funds that they sell. The MPFA works closely 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 monitoring compliance with the Code of Conduct for MPF Intermediaries and improving the professional standard of MPF intermediaries.

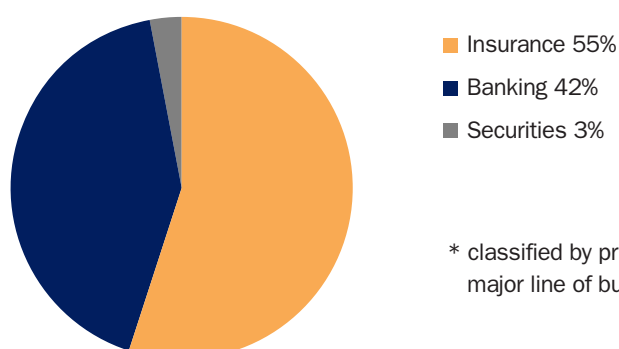
Registration of MPF Intermediaries

During the year, the MPFA processed a total of 4 140 new applications for registration as MPF intermediaries. As at 31 March 2002, there was a total of 28 637 registered MPF intermediaries, comprising 474 corporations and 28 163 individuals respectively. Table 4 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 4. Number of Registered MPF Intermediaries *as at 31 March 2002*

Total number of registered MPF intermediaries	28 637
Corporate intermediaries	474
Individual intermediaries	28 163
<i>Permitted to advise on insurance policies</i>	13 820
<i>Permitted to advise on securities</i>	9 343
<i>Permitted to advise on securities & insurance policies</i>	5 000

Figure 1. **MPF Intermediaries by Industry*** *as at 31 March 2002*



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 7 726 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 HKMA, IA and SFC conducted a number of inspections on corporate intermediaries falling under their respective regulatory regimes. So far, no major irregularities or serious breaches of the Code of Conduct for MPF Intermediaries were noted.

In the past year, there were 38 complaints against MPF intermediaries. This accounted for less than 1% of the total complaints received by the MPFA. Three complaint cases were referred to the other regulators for information and consideration of follow-up action.



Forum to introduce the CPD requirements for MPF intermediaries

Continuing Professional Development

In order to help MPF intermediaries maintain their professional competence, the Continuing Professional Development (CPD) requirement was introduced with effect from January 2002. MPF intermediaries were required to undertake a minimum of 10 hours of CPD activities in each calendar year. Four institutions, namely Hong Kong Securities Institute, Caritas Adult & Higher Education Service, the Financial Services Development Centre of the Vocational Training Council, and the Management and Executive Centre of the Hong Kong Polytechnic University have been recognized by the MPFA for the provision of training activities for CPD core subjects.

A guide to the CPD requirement was issued in October 2001.

In addition, a forum on the CPD requirement was held by the MPFA on 1 February 2002 at the Hong Kong Convention and Exhibition Centre, where industry practitioners were briefed on the CPD requirement and details of the relevant courses offered by the recognized institutions.

Regulation of Occupational Retirement Schemes

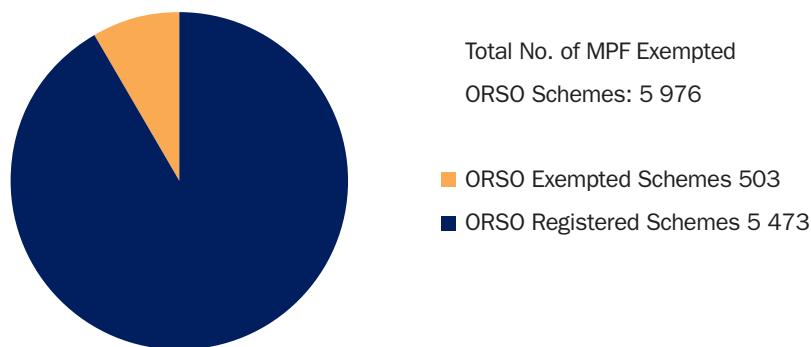
Occupational retirement schemes (ORSO schemes) are voluntarily established by employers under the Occupational Retirement Schemes Ordinance (Cap.426) (ORSO). The number of ORSO schemes has been decreasing since the implementation of the MPF System.

Withdrawal of Exemption Certificate

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, 345 MPF exempted ORSO schemes had relinquished their exemption status covering about 7 000 members, who had to be enrolled in MPF schemes subsequently. The number of MPF exempted ORSO schemes as at 31 March 2002 was 5 976 covering about 8 400 employers and 524 000 scheme members. A breakdown of the number of schemes is shown in Figure 2.

Figure 2. **Number of MPF Exempted ORSO Schemes** as at 31 March 2002



Winding Up of ORSO Schemes

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, 7 447 ORSO schemes (comprising 422 MPF exempted schemes and 7 025 non-MPF exempted schemes) were wound up. As at 31 March 2002, there were 768 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 8 660, including 5 895 MPF exempted schemes (covering about 522 000 scheme members) and 2 765 non-MPF exempted schemes (covering about 83 000 employees).

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 5.

Table 5. Asset arrangements for terminated ORSO registered schemes for the period from 1 April 2001 to 31 March 2002

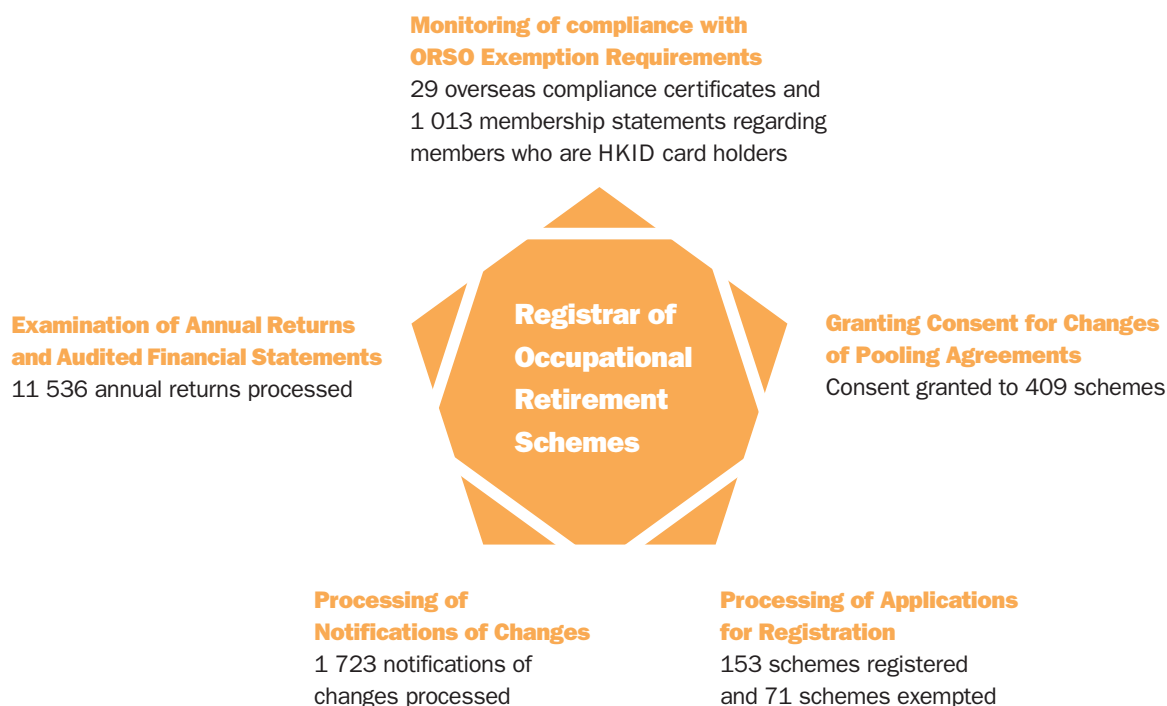
ORSO Asset Arrangement	NO. of Schemes	%	Asset Size (HK\$million)	%
Transferred to MPF Scheme	6 205	85	11,297	72
Transferred to another ORSO Scheme	313	4	3,654	24
Paid out to scheme members	801	11	686	4
Total	7 319	100	15,637	100

Work of the Registrar of Occupational Retirement Schemes

As the Registrar of Occupational Retirement Schemes (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.