Prudence ...

Monitor your investments regularly

Supervision of the Industry

The MPFA has primary responsibility for supervising approved trustees and works with other financial regulators in overseeing MPF products and MPF intermediaries to ensure safety and soundness in the operation of the MPF system. As the Registrar of Occupational Retirement Schemes, the MPFA is also responsible for overseeing the effective operation of occupational retirement schemes.

SUPERVISION OF APPROVED TRUSTEES

The approved trustees are entrusted with the overall responsibility for the administration and management of MPF schemes, including approved pooled investment funds. While they may delegate some of their functions to other service providers, they have to comply with the provisions of the MPF legislation and discharge their responsibilities with due care, and to exercise their fiduciary duties as required.

A list of the approved trustees and their background as at 31 March 2005 is at Appendix 6.

The Compliance Standards

To ensure the smooth operation of the MPF System, the MPFA seeks to promote good corporate governance, proper risk management and a strong compliance culture among the approved trustees. The MPFA commenced an initiative in 2004-05 to develop a set of standards for the guidance of trustees in establishing a structured framework for monitoring their compliance with statutory duties and responsibilities. With the help of international consultants, the compliance frameworks of selected approved trustees were reviewed to determine an appropriate set of standards for the MPF industry.

The consultants then drew up a set of draft Compliance Standards, which reflects internationally recognized compliance methodology. The fundamentals of the methodology are:

- ownership of compliance at the highest levels within an organization;
- the existence of documented procedures to facilitate the understanding throughout an organization of the statutory obligations in day-to-day operations;
- the implementation of monitoring and supervision measures to assess whether compliance has occurred; and
- the presence of review and reporting mechanisms.

The draft Compliance Standards were sent to relevant industry associations for comments in late 2004 and were revised in early 2005 based on comments received. The MPFA will consult various stakeholders before issuing the Standards in mid-2005.

Ongoing Monitoring

The MPFA continued to monitor developments in the MPF market, which has been stable, with the number of approved trustees remaining unchanged at 19 during 2004-05. The MPFA conducts on-site visits of approved trustees to assess compliance with the regulatory requirements. The latest round of on-site visits, which started in 2003-04, continued in the 2004-05 financial year. The focus was to review the valuation of investment holdings and investment compliance, as well as to ensure that weaknesses in scheme administration processes identified previously had been addressed. The visits to all the approved trustees were completed in March 2005.

The approved trustees are required to submit regular returns to MPFA. The review of these returns ensures that the approved trustees comply with the statutory requirements and relevant governing rules, and allows for early detection of issues that may call for proposals to amend overall regulatory policy settings.

As part of the ongoing monitoring, approved trustees are also required to report significant events under section 62 of the Mandatory Provident Fund Schemes (General) Regulation. The MPFA followed up these notices to ensure that the reported events did not adversely affect scheme members' interests and that rectification actions were taken as and when necessary.

During the year, the MPFA issued a number of warning and reminder letters to the approved trustees involved in breaches. These breaches were either identified by the MPFA through enquiries and complaints received, during on-site visits or reported by the trustees themselves. In addition, the MPFA issued two financial penalty notices in relation to two breaches. Details of the financial penalty notices are set out under item 8 in Part E of the Statistics section.

The analysis of complaints has been, and will continue to be, one of the major means of the ongoing monitoring of the performance of approved trustees. At the same time, it is also an effective avenue for identifying scheme administration issues and areas requiring policy development considerations. A total of 222 complaints (compared with 164 in the previous financial year) were lodged with the MPFA against approved trustees, most of which were related to scheme administration. The number of complaints has increased with the increase in scheme members' awareness of their MPF rights.

To improve the effectiveness and efficiency of the administration of MPF schemes, a Trustees Operations Liaison Group was set up during the year, comprising representatives from all approved trustees and the MPFA. Quarterly meetings were held to discuss operational issues of MPF schemes which are of interest across the industry, and to share information on the latest developments of the MPF System.

Recent Developments

During the year, an increasing number of trustees began to offer special voluntary contribution arrangements under which employee scheme members could make voluntary MPF contributions directly to the trustees without channeling through their employers. The MPFA has been working with approved trustees to address operational issues that may arise in connection with such arrangements. Several MPF Guidelines on trustees' statistical returns have also been revised to include data on special voluntary contributions to facilitate the monitoring of market development in this respect.

REGISTRATION AND APPROVAL OF MPF SCHEMES AND FUNDS

The registration and approval of MPF schemes and funds involves a detailed review of various aspects of the application, including the scheme rules, their operations and disclosure, particularly in respect of compliance with MPF legislation and protection of scheme members' interests. Table 1 sets out the processing statistics of these applications during the year, and Table 2 shows an analysis of the structure of approved pooled investment funds. As at the end of March 2005, there were 47 registered MPF schemes, 324 approved

Table 1. Processing statistics on registration and approval of MPF schemes and funds

	Number as at 31 March 2004	De-registration/ Revocation during the year	Registration/ Approval during the year	Number as at 31 March 2005
Registered Schemes	**48**	**2**	**1**	**47**
Master Trust Schemes	44	2	1	43
Industry Schemes	2	0	0	2
Employer Sponsored Schemes	2	0	0	2
Approved Constituent Funds	**321**	**9**	**12**	**324**
Approved Pooled Investment Funds	**253**	**2**	**23**	**274**
Approved Index-Tracking Collective Investment Schemes	**76**	**1**	**8**	**83**

Table 2. Analysis of approved pooled investment funds

	Unit Trust		Insurance Policy		Total	
	as at 31 March 2004	as at 31 March 2005	as at 31 March 2004	as at 31 March 2005	as at 31 March 2004	as at 31 March 2005
By fund valuation bases						
Unitized	187	204	63	67	250	271
Non-unitized	0	0	3	3	3	3
Total	**187**	**204**	**66**	**70**	**253**	**274**
By fund structures						
Umbrella funds	22	23	4	4	26	27
Internal portfolios	130	150	29	29	159	179
Feeder funds	6	6	22	22	28	28
Portfolio management funds	29	25	11	15	40	40
Total	**187**	**204**	**66**	**70**	**253**	**274**

constituent funds and 274 approved pooled investment funds. A full list of the registered schemes and their underlying constituent funds is available at Appendix 7.

As can be seen from Table 1 above, there was an increase in the number of funds during the year as compared with the last. This was due to the introduction of new products in response to changes in the global financial markets, so as to provide members with a wider range of investment options. The decrease in the number of schemes was due to the consolidation of the MPF System through merger of MPF schemes.

Apart from the registration and approval of new applications, the MPFA also approves amendments to governing rules of MPF schemes and funds on an ongoing basis. Following the publication of the Code on Disclosure for MPF Investment Funds in June 2004, the MPFA also approved fee tables and reviewed Fund Fact Sheets of MPF schemes, which are required to be provided to scheme members under the Code.

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

SUPERVISION OF MPF INTERMEDIARIES

MPF intermediaries play an important role within the MPF System through serving MPF scheme members and providing advice on scheme and fund selection. The MPFA is responsible for registering and supervising MPF intermediaries. It also coordinates the efforts of other regulators, i.e. the Securities and Futures Commission (SFC), the Insurance Authority (IA) and the Hong Kong Monetary Authority (HKMA), in supervising MPF intermediaries with a view to ensuring regulatory consistency and minimizing regulatory overlap. Whilst the MPFA is mainly responsible for daily monitoring and handling of complaints against MPF intermediaries, the HKMA, the IA and the SFC are responsible for supervising those MPF intermediaries falling under their regulatory regimes.

During the year, the work in respect of supervision of intermediaries continued to focus on monitoring their compliance with the Code of Conduct for MPF Intermediaries and improving their professional standard through the Continuing Professional Development (CPD) requirement.

Registration of MPF Intermediaries

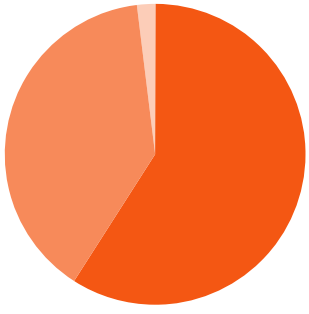
During the year, the MPFA processed around 3 700 applications for registration as MPF intermediaries and 1 700 applications for renewal of registration. The number of MPF intermediaries remained about the same during the past two years at around 25 000. As at 31 March 2005, there was a total of 24 502 registered MPF intermediaries, comprising 433 corporations and 24 069 individuals (see Table 3).

Table 3. Number of Registered MPF Intermediaries *(as at 31 March 2005)*

Total number of registered MPF intermediaries	24 502
Corporate intermediaries	433
Individual intermediaries	24 069
Permitted to advise on insurance policies	12 918
Permitted to advise on securities	5 707
Permitted to advise on both securities and insurance policies	4 014
Permitted to sell MPF schemes without rendering specific investment advice	1 430

Figure 1 shows the distribution of individual intermediaries among three industries (banking, insurance and securities), classified by the major line of business of the intermediary's primary sponsoring corporation. The distribution of MPF intermediaries among the three industries has been quite stable over the past few years.

Figure 1. MPF Intermediaries by Industry* *(as at 31 March 2005)*



Insurance 59%
Banking 39%
Securities 2%

* *classified by principal's major line of business*

The MPFA started a review on the registration of MPF intermediaries with a view to streamlining the registration process and tightening CPD compliance. Proposed reforms include replacing MPF intermediaries cards with MPF intermediary certificates and stipulating CPD compliance as one of the criteria in assessing the fitness and properness of applicants and registrants. The recommended changes will be introduced in 2005-06 after industry consultation.

Ongoing Monitoring

During the year, the MPFA processed around 6 000 changes of information relating to MPF intermediaries. As in the past years, most of the changes were related to change of employment of individual intermediaries and change of name of their sponsoring corporations as a result of corporate mergers and restructuring.

Complaints against MPF intermediaries remained at a low level, with less than 10 complaints lodged in the year, accounting for less than 1% of the total number of complaints received by the MPFA.

Continuing Professional Development

The CPD requirement for MPF intermediaries has been implemented since January 2002. The objectives are to enhance the technical knowledge and professional expertise of individual intermediaries and to provide reasonable assurance to MPF scheme participants and the public at large that individual intermediaries remain fit and proper to be registered. MPF intermediaries are required to undertake a minimum of 10 hours of CPD activities in each calendar year, with at least 20% of the minimum CPD hour requirement devoted to core subject areas such as MPF or related legislation, relevant codes and guidelines, and up-to-date developments of the MPF System.

As at 31 March 2005, six institutions/professional bodies have been recognized by the MPFA for the provision of training activities for CPD subjects. They are Caritas Adult & Higher Education Service, Hong Kong Securities Institute, Management and Executive Development Centre of The Hong Kong Polytechnic University, The Hong Kong Retirement Schemes Association, School of Professional and Continuing Education of The University of Hong Kong, and Financial Services Development Centre of Vocational Training Council. The MPFA continued to assess whether certain programmes or courses were eligible to be qualified as core CPD activities. In 2004-05, a total of 16 programmes/courses were recognized as core CPD courses.

REGULATION OF OCCUPATIONAL RETIREMENT SCHEMES

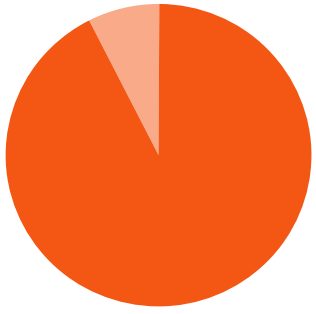
The MPFA is the Registrar of Occupational Retirement Schemes (RORS) and has the functions conferred on it by ORSO. It is responsible for regulating occupational retirement schemes (ORSO schemes) established voluntarily by employers. As at 31 March 2005, there were a total of 7 913 ORSO schemes, with a total asset size of $179.38 billion. The work of the RORS during the year is reported below.

Withdrawal of Exemption Certificate

Prior to the launch of the MPF System, the employers operating 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 an MPF scheme.

Employers of MPF-exempted ORSO schemes may withdraw their MPF exemption certificates. During the year, 255 MPF-exempted ORSO schemes, covering about 3 000 members, had relinquished their exemption status. The number of remaining MPF exempted ORSO schemes as at 31 March 2005 was 5 261, covering about 7 000 employers and 500 000 scheme members. A breakdown of the number of MPF exempted ORSO schemes is shown in Figure 2.

Figure 2. Number of MPF-Exempted ORSO Schemes *(as at 31 March 2005)*



ORSO Registered Schemes	4862
ORSO Exempted Schemes	399
Total Number of MPF-Exempted ORSO Schemes	**5261**

Winding Up of ORSO Schemes

For those ORSO schemes which have not obtained MPF exemption status, the relevant employers may choose amongst the options of making an interface arrangement to retain them as top-up schemes, freeze the schemes or terminate the schemes. During the year, 363 ORSO schemes (comprising 228 MPF-exempted schemes and 135 non MPF-exempted schemes) had been wound up. As at 31 March 2005, 130 ORSO schemes were in the process of being terminated, pending the transfer of scheme assets and/or provision of the necessary information to the MPFA. After the termination of these schemes, the number of remaining ORSO schemes would be 7 783, including 5 206 MPF-exempted schemes (covering about 500 000 scheme members) and 2 577 non MPF-exempted schemes (covering about 60 000 employees). The number of termination notices received by the MPFA has shown a decreasing trend towards the end of the financial year.

Based on the information obtained from termination notices submitted and the latest annual returns of ORSO registered schemes, the asset arrangements of the terminated ORSO registered schemes (including those schemes undergoing termination processes) are set out in Table 4.

Table 4. Asset arrangements for terminated ORSO registered schemes for the period from 1 April 2004 to 31 March 2005

Asset Arrangement	Number of Schemes	%	Asset Size (HK$ million)	%
Transferred to MPF Scheme	94	28	413	20
Transferred to another ORSO Scheme	30	9	1,133	55
Paid out to scheme members	212	63	515	25
Total	**336**	**100**	**2,061**	**100**

Funding of ORSO Schemes

According to the ORSO, employers operating ORSO schemes should ensure proper funding of the schemes to meet the scheme members' benefit claims. The MPFA monitors the funding situation of the schemes by examining the annual returns and audited financial statements in respect of the schemes. In the case of defined benefit schemes, actuarial certificates have to be supplied to the MPFA at least every three years. The certificate may be a full certificate certifying that the scheme's assets are sufficient to meet the scheme's aggregate vested liabilities, or a qualified certificate showing that the scheme assets are not sufficient to meet the vested liabilities. Where a qualified certificate is supplied, the actuary shall make recommendations as to the amount of contributions to be made by the employer in order to make up the shortfall in funding within three years. Under such circumstances, actuarial certificates will have to be supplied more frequently, every year instead of every three years, until the assets of the scheme have returned to a level sufficient to meet the scheme's aggregate vested liabilities.

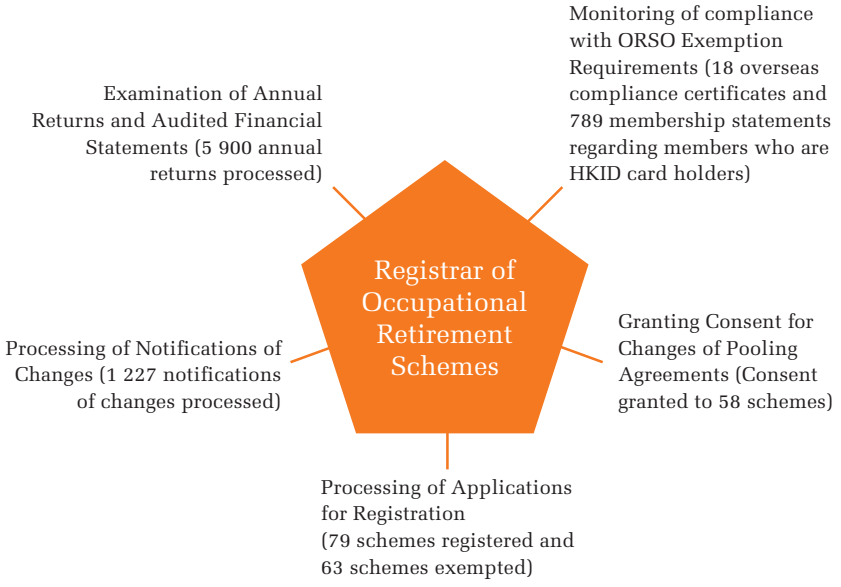
As indicated in the actuarial certificates received as at 31 March 2005, 23 ORSO schemes (7.4% of the total of 311 defined benefit schemes) were insolvent. The total asset size of these schemes was $5,969 million and the total shortfall was $277 million. The amount of shortfall involved represented about 4.6% of the aggregate assets of the 23 under-funded schemes. This is a marked improvement over the situation a year ago, when the number of insolvent defined benefit schemes was 48, with a total shortfall of $753 million (5.9% of the aggregate assets of the underfunded schemes). The MPFA has been monitoring the situation closely by seeing to it that contributions are made according to scheme terms and rules, and in accordance with the actuarial recommendations.

Other Work of the Registrar of Occupational Retirement Schemes

In addition to handling the withdrawal of exemption certificates and applications for winding up, and monitoring the funding of defined benefit schemes, the MPFA, as the Registrar of Occupational Retirement Schemes (RORS), is also responsible for ongoing monitoring of ORSO registered/ exempted schemes. The work of the RORS in this aspect includes ensuring the effective administration of such schemes and processing of changes to the schemes. Statistics on some major areas of the RORS' work are summarized in Figure 3.

Figure 3. Work of Registrar of Occupational Retirement Schemes

Note: Figures denote workload for the year ended 31 March 2005



A list of the corporate administrators who administer pooling agreements for ORSO schemes is in Appendix 8.

Statistics

Statistics on ORSO schemes are set out in Part C of the Statistics section.