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Mandatory Provident Funds

Contents

Introduction

The Mandatory Provident Fund Schemes Ordinance (MPFSO) commenced operation in Hong Kong on 1 December 2000. Since the operation of the MPFSO, several amendment ordinances and regulations have been enacted by the Government with a view to enhancing protection for scheme members and streamlining the operation of the MPF system in Hong Kong.

The major features of MPF are:

- Mandatory – membership in an MPF scheme or MPF-Exempted ORSO scheme is mandatory. The employer has no choice and must make available an MPF scheme to its employees. Self-employed persons must join an MPF scheme.
- Portability – on changing jobs an employee does not receive benefit; his/her accrued benefits must be transferred to another scheme or retained in a master trust scheme.
- Preservation – benefits are payable at age 65. Early withdrawal of benefits is allowed only in the event of the member's death, total incapacity, terminal illness, early retirement between ages 60 and 64 and member has declared not to become employed or self-employed within the foreseeable future, permanent departure from Hong Kong, and if the member has a small balance account of HK$5,000 or less, has not made contributions to an MPF scheme for 12 months.
- Full and immediate vesting – all mandatory contributions to an MPF scheme paid by an employer become fully "vested" for the benefit of the employee immediately upon the contribution being paid – this means the employers are not entitled to the return of any monies even for employees who leave employment after a short period.
- Fixed rate of mandatory contributions – employer's contributions to MPF schemes is mandatory. These are equal to 5% of the employee's relevant income (subject to a maximum relevant income of HK$30,000 per month). Unless the employee earns less than HK$7,100 per month, he/she must make the same rate of contributions out of his/her relevant income.
- Trust – the arrangement must be created by trust. Insurance arrangements are not permitted.
- Investment choice – MPF schemes are intended to offer members choice of investments, including one choice designed for security of capital on terms specified by MPF. The Default Investment Strategy is also available for those members who do not make their own investment choice and is itself also an investment choice.
- Benefits – benefits payable under an MPF scheme are calculated solely by reference to the amount of contributions paid into the scheme and the investment return or loss on those contributions. Benefits are not linked to the final salary of an employee or his/her years of service and it is possible that benefits will be less than the contributions paid into the scheme.

There are three types of MPF schemes:

- A master trust scheme which is available to all eligible applicants
- An industry scheme which is for the catering and construction industries only
- An employer-sponsored scheme which is for the staff of the particular employer and associated employers.

MPF schemes are regulated by the MPFS Authority.

Master trust schemes

A master trust scheme is a registered scheme the membership of which is open to the employees of more than one employer, self-employed persons and persons having accrued benefits in another registered scheme: in other words, any employee or self-employed person can participate in a master trust scheme.

A trustee of this type of scheme may only be a corporate trustee; no individuals may be appointed as trustees. Provided that the trustee satisfies the requirements of the MPFS Authority, the master trust scheme will be registered and a certificate will be issued. There are extensive regulations regarding trustees of an MPF master trust but provided that the scheme is registered it will not be necessary for an employer to consider these regulations.

The trustee of a master trust scheme as well as the master trust scheme itself must be approved by the MPFS Authority. A Code on MPF Investment Funds has been published by the MPFS Authority which contains guidelines for the guidance of approved trustees, service providers and on the approval of the master trust schemes. The MPFS Authority has also published the Code on Disclosure for MPF Investment Funds regarding the disclosure of information about MPF schemes and constituent funds and in particular, information about fees, charges and performance.

The master trust schemes and the underlying pooled investment funds need to be approved by the Securities and Futures Commission (SFC) and, separately, an SFC Code on MPF Products has been issued by the SFC for this purpose.

MPF for employers

Employers in Hong Kong – whether large or small and whether carrying on business as a limited company or in another form – must ensure that all staff participate in an MPF scheme (unless they join an MPF-Exempted ORSO scheme). Exceptions are limited.

Employers may choose to join a master trust scheme offered by a trustee company approved for MPF purposes or to create their own employer-sponsored scheme. MPF schemes with special features called "industry schemes" are available for the catering and construction industries.

Employers should take account of MPF requirements in employment policies and practices as they have a material impact on personnel administration procedures. Employers who have given contractual retirement benefits may need to revise their employment contracts.

The rate of contributions is 5% of the employee's relevant income (subject to a maximum relevant income of HK$30,000 per month). Employee's relevant income includes salary and bonuses/commissions/allowances. Housing allowances are also included. Contributions must be made into the scheme in respect of the full period of employment, though the first contributions can be delayed until expiry of probation (which must not exceed 60 days).

If employers wish to contribute more than the minimum rate of mandatory contributions, MPF schemes can accept voluntary top-up contributions. Alternatively, employers may establish separate retirement schemes for additional benefits. The regulations applicable to voluntary contributions within MPF schemes are different to those for mandatory contributions.

All mandatory contributions to an MPF scheme paid by an employer become fully "vested" for the benefit of the employee immediately upon the contribution being paid – this means the employer is not entitled to the return of any monies even for employees who leave employment after a short period. However, if an employer pays an employee a severance payment or long service payment, that payment can be recovered from (or off-set against) the employee's benefits derived from the employer's contributions.

MPF for employees

Unless an employee earns less than HK$7,100 per month, he/she has to contribute 5% of his/her relevant income (subject to a maximum relevant income of HK$30,000 per month) to an MPF scheme.

Benefits under an MPF scheme are payable at age 65. Early withdrawal of benefits is allowed only in the event of the member's death, total incapacity, terminal illness, early retirement between ages 60 and 64 and member has declared not to become employed or self-employed within the foreseeable future, permanent departure from Hong Kong, or if the member has a small balance account of HK$5,000 or less, has not made contributions to an MPF scheme for 12 months.

On changing jobs, an employee does not receive the benefits under his/her MPF scheme. However, the employee is given a choice as to how to handle his/her accrued benefits and may either:

- transfer the accrued benefits to a new MPF scheme operated by the new employer;
- retain the accrued benefits in the existing scheme (the benefits will stay in the personal account of that scheme); or
- transfer the accrued benefits to a personal account in another scheme.

Following the implementation of the Employee Choice Arrangement on 1 November 2012, an employee may also opt to transfer the accrued benefits derived from the employee's portion of mandatory contributions attributable to current employment to any other master trust scheme or industry scheme of his/her choice once a year.

An employee can transfer his/her accrued benefits held in a personal account to any other MPF scheme of his/her choice at any time.

Exempted schemes

Background

The MPF-Exempted Occupational Registered Schemes governed by the Occupational Retirement Schemes Ordinance (MPF-Exempted ORSO schemes) may be defined contribution schemes – that is, benefits are determined by reference to the amount of contributions made, as is the case in MPF schemes – or defined benefit schemes (often called final salary schemes). Nearly all such schemes provide benefits to members in the form of a lump sum payment payable on termination of employment.

No further applications are accepted in respect of MPF-Exempted ORSO schemes after 1 December 2000. Under the MPFS (Exemption) Regulation (Exemption Regulation), if a member of an MPF-Exempted ORSO scheme became a member of the scheme on or before 1 December 2000, he/she is deemed to be an "existing member" under the Exemption Regulation. Otherwise, he/she shall be treated as a "new member". A new member of an MPF-Exempted ORSO scheme is subject to the preservation of minimum MPF benefits requirements. With effect from 19 July 2002, an existing member can retain his/her status after a transfer from an MPF-Exempted ORSO scheme to another MPF-Exempted ORSO scheme subject to satisfying certain conditions.

Effect of MPF exemption

If entitled to MPF exemption, a scheme can continue largely as at present and allow new members to join without being subject to all MPF restrictions. Existing and new employees must be given the chance to choose between the exempted existing scheme and an MPF scheme.

Compliance with the rules for giving staff this choice requires advance planning by an employer and creates ongoing employer obligations.

The effect of MPF exemption depends on whether the MPF-Exempted ORSO scheme is itself further registered under or exempted from ORSO. In particular, it impacts differently on existing members and new members. The main effect for existing members is that if the MPF-Exempted ORSO scheme is itself registered under ORSO, they will be able to receive their benefits on leaving employment (subject to any applicable vesting scale) before reaching retirement age, free from requirements on preservation, portability and withdrawal of their benefits, which applies to new members of such scheme.

Self-employed

Under MPF, self-employed persons (including partners) are required to participate in an "MPF master trust".

Self-employed persons need to make payment of contributions of 5% of their "relevant income" – "relevant income" is to be calculated in accordance with "assessable profits" for profits tax purposes.

Contributions may be on a monthly or yearly basis

If the level of income earned by a self-employed person is below HK$7,100 per month or HK$85,200 per annum (depending on whether monthly or yearly contributions are made), he/she does not need to make contributions.

There is a maximum level of mandatory contributions of HK$1,500 per month or HK$18,000 per annum (this may be paid regardless of actual "relevant income").

Partners

Partners (who are not employees) are self-employed for the purposes of MPF.

To calculate the "relevant income" of a partner, proportional adjustments are made according to the person's share of the profits of the business for a relevant financial period.

Expatriates

Few exemptions apply. Expatriates who are members of home country schemes may be exempted. Expatriates entering Hong Kong for work for a limited period not exceeding 13 months may also be exempted. Those not exempted must participate in an MPF scheme or an MPF-Exempted ORSO scheme and will be entitled to benefits under the relevant scheme on permanent departure from Hong Kong.

Taxation

Employers

An employer's contributions to an MPF scheme or MPF-Exempted ORSO scheme are generally deductible, as revenue expenses, for profits tax purposes up to 15% of the total emoluments of the employees.

Where the employer operates both an MPF scheme and MPF-Exempted ORSO scheme, payments made to both schemes are aggregated to calculate the 15% limit.

Employees

No salaries tax is payable on benefits received from an MPF scheme or an MPF-Exempted ORSO scheme which are derived from the employee’s own contributions. On the other hand, exemption from salaries tax for benefits received which are derived from employer’s contributions depends on the reason why the employee left employment. For example, they will be exempted if the employee left due to retirement.

A deduction for salaries tax purposes with respect to the mandatory contributions into an MPF scheme of up to HK$18,000 per annum in the year of assessment 2019 – 2020 and after (subject to further changes in case of change in relevant income cap) is allowed. Contributions into an MPF-Exempted ORSO scheme are also deductible for salaries tax purposes, but the maximum amount deductible is the lesser of (i) the employee’s contributions; or (ii) the amount of the mandatory contributions that the employee would have been required to pay if he had contributed as an employee to an MPF scheme; but subject to a maximum of HK$18,000 per annum and subject to further changes also.

Commencing from the year of assessment 2019 – 2020, employees who are members of an MPF scheme or an MPF exempted ORSO scheme can claim tax deductions under salaries tax and personal assessment for making voluntary contributions to tax deductible voluntary contribution accounts. The aggregate maximum tax deductible limit for each taxpayer is set at HK$60,000 per year.

Self-employed

Self-employed persons are eligible for a deduction of up to HK$18,000 per annum in the year of assessment 2019 – 2020 and thereafter (subject to further changes in case of change in relevant income cap) in respect of assessable profits for their contributions to an MPF scheme.

Industry schemes

Industry schemes are designed to address the problem of bringing the large number of casual labourers who may work with one employer for only a few days into the MPF regime. Casual labourers are those who are employed on a day-to-day basis or for a fixed period of less than 60 days.

Two industry schemes have been established and approved in respect of the construction and catering industries.

The key features of industry schemes are:

- Enrolment is optional for employers and employees/casual employees in the relevant industries (though if they do not enrol, they must enrol in a master trust scheme).
- Scales of contributions by reference to the amounts of relevant income for employees who are casual employees are prescribed by the MPFS Authority and published in the Gazette from time to time. The flat 5% contribution will not apply.
- The minimum level of income in relation to employees who are casual employees for contribution purposes is HK$280 per day and the maximum is HK$950 per day.
- Employers can either remit contributions directly to the trustee of the industry scheme in the same way as under other MPF schemes, or they can choose to pay the contributions to the trustee at the same time as the employees'/casual employees' wages through the use of smart cards. This is known as the "instant payment method". Where the instant payment method is used, employers are not required to remit contributions to the trustee, issue monthly payslips to the employees/casual employees or prepare, submit or keep remittance statements.
- Unlike other types of MPF schemes, (where the employer must arrange for the employees to join 60 days within commencement of employment), there is no 60-day period before an employee who is a casual employee is required to join an industry scheme; contributions must be made immediately on commencement of employment.

Employer-sponsored schemes

Employer-sponsored schemes are those established by a specific employer and whose members may only be the employees of that employer and, if that employer is a company, employees of any associated companies of that employer.

An employer-sponsored scheme may have trustees who are natural persons, though such persons can only be trustees if they are approved by the MPFS Authority and they are either members of the scheme or independent trustees (as the case may be). To be independent, a trustee must not be a controller (such as a director or chief executive), employee or shareholder of the employer or its associates or have any association (financial or otherwise) with the employer, its associates or controllers.

Such employer-sponsored schemes must also be approved by the MPFS Authority.

Eligible investment funds for MPF

The MPF regulations provide investment restrictions and limits on investment of the money in an MPF scheme.

Generally an MPF trustee are required to appoint an eligible investment manager to manage the investment of the funds of an MPF scheme and the legislation sets provisions for the eligibility of such an investment manager and the terms of the required investment management contract. However, if the MPF trustee decides to invest only in approved pooled investment funds, there is no requirement to appoint a separate investment manager. "Approved pooled investment fund" means that the fund is an arrangement approved by the SFC under the Protection of Investors Ordinance and by the MPFS Authority under the MPF regulations.

Applications for approval of these arrangements must comply with the Codes issued by the MPFS Authority and the SFC as referred to in the section under "Master Trust Schemes" above.

An eligible investment manager must meet the MPF requirements; if the MPF scheme invests in a fund which is an approved pooled investment fund, the investment manager of that fund must also meet those requirements. These are in addition to the qualifications set out in the Code on MPF Products issued by the SFC. There is also a requirement for the independence of the manager from other parties. For approved pooled investment funds which are also offered to the retail public, the manager is required to also comply with the Code on Unit Trusts and Mutual Funds issued by the SFC.

The rules permit monies of an MPF scheme to be invested in a unit trust or mutual fund which is an approved pooled investment fund. However, the trust or fund must be approved by the MPFS Authority and authorised under the Securities and Futures Ordinance by the SFC. If the fund includes provision for a guaranteed amount then additional provisions apply to the guarantor. The relevant unit trust or mutual fund need to comply with the restrictions governing the investment of monies under the MPF as well as those applied to other trusts and funds authorised under the MPF Products issued by the SFC. In addition, where the approved pooled investment fund is also offered to the retail public, the requirements of the Code on Unit Trusts and Mutual Funds also apply.

A separate booklet is available on unit trusts and mutual funds which explains the procedures for authorisation of funds by the SFC.

Compensation fund

The MPFS Authority has set up a compensation fund for the purpose of compensating any scheme member for any losses to his/her accrued benefits caused by the misfeasance or illegal conduct of a person concerned with the administration of the relevant MPF scheme. However, the compensation fund is to be used only in the event that the losses cannot be totally compensated by the resources of the trustee and other service providers or their insurance. All benefits arising from both mandatory and voluntary contributions made by employers and scheme members will be covered without any limit.

The compensation fund had been established with an initial government injection of HK$600 million. Further moneys are collected by levy payable by the approved trustee of the MPF registered scheme. When in need, the MPFS Authority may apply to the court to use the compensation fund.

Although there is a compensation fund, the person whose act or omission causes the loss would still be liable for his/her default. He/she would also be required to reimburse the fund with interest if payment to an aggrieved member has been made.

Default Investment Strategy

From 1 April 2017, each of the existing MPF schemes has been required by law to offer the Default Investment Strategy (DIS). The contributions of scheme members who do not make their own choice of constituent funds will be invested through the DIS. Scheme members can also choose to invest through the DIS.

The DIS uses two constituent funds called the Core Accumulation Fund (CAF) and the Age 65 Plus Fund (A65F). Around 60% of the CAF is held in higher risk assets and 40% in lower risk assets. The A65F holds 20% higher risk assets and 80% lower risk assets.

The contributions of scheme members below the age of 50 will be fully invested into the CAF. After a scheme member reaches age 50, assets will gradually be moved from the CAF to the A65F every year. This process will continue until the scheme member reaches age 65 when all assets will be held in the A65F. As such, the DIS aims to balance risk and return based on the needs of average MPF scheme members depending on their age.

The amount of service fees and recurrent out-of-pocket expenses charged to the constituent funds in the DIS is set at no more than 0.95% of the net asset value.

Want to know more?

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