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Challenges of Private Retirement Scheme (PRS) in Malaysia

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Abstract

This paper intend to compare and analyse the private retirement scheme (PRS) and other retirement schemes that exists in Malaysia**.** PRS is a complementary scheme to the existing Malaysian pension schemes that are Government Pension Scheme (GPS) and Employees Provident Fund (EPF). There are many differences between the three retirement schemes such as the dividend in EPF is guaranteed, the government servant will received their pension after retirement but PRS depend solely on the investment made by contributor; EPF and GPS give death and incapacitation benefits to their members but not PRS; income tax relief are given to PRS contributor and EPF members. These differences lead to challenges in providing PRS to contributors especially during the economic downturn faced by our country today.

Keywords: Private retirement scheme; Employee provident fund; Government scheme

1. Introduction

The Government of Malaysia (The Government) encourages youth to undertake long-term investment through the Private Retirement Scheme (PRS). The PRS was introduced after suggestions made by Securities Commission Malaysia (SC) to the Government in order to accelerate development of the private pension industry in Malaysia. PRS works as a complementary scheme to the existing Malaysian pension schemes i.e Employee Provident Funds (EPF) scheme and Government Pension Scheme (GPS). It seeks to enhance choices available for all Malaysians, whether employed or self-employed, to supplement their retirement savings under a well-structured and regulated environment (Securities Commission, 2011).

Generally, PRS can be defined as a contribution pension scheme which allows people (or their employees) to voluntarily contribute into an investment vehicle for the purposes of building up

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their retirement income (Liew, 2012). According to Federation of Managers Malaysia (FIMM) (2012), PRS funds are purposely built for long term (10-15 years basis) investing to prepare the investors for a comfortable retirement years. The contributors of PRS may choose from the eight PRS providers and invest according to their expected returns and risk profile.

PRS is administered by Private Pension Administrator (PPA). It functions as a record keeping and resource centre for data on all transactions performed by contributors. The assets of each PRS will be segregated from the PRS provider and held by an independent Scheme Trustee under a trust to safeguard contributor's money. The PRS providers, the PPA, the Scheme Trustee and distributors of PRS are being regulated by SC in order to ensure the proper functioning of PRS industry and protect members through prudential and investor protection requirement (Yeoh, 2012).

Currently, there are eight providers approved by the Securities Commission under section 139B of CMSA that are Affin Hwang Asset Management Berhad, AIA Pension and Asset Management Sdn. Bhd., AmInvestment Services Berhad, CIMB-Principal Asset Management Berhad, Kenanga Investors Berhad, Manulife Asset Management Services Berhad, Public Mutual Berhad, and RHB Asset Management Sdn. Bhd. They offered PRS scheme and fund on conventional and Shariah based. The basic scheme consists of growth, moderate and conservative funds.

3.0 Comparison between PRS, GPS and EPF

3.1 Definitions of GPS, EPF and PRS

Pensions Act 1980 stated that GPS is intended to provide financial security for retired government employees. It is a defined benefit plan that is financed and managed by the Government for employees in the Government service. It shall be charged on the Federal Consolidated Fund. Officers on full-time employment in the public service or an employee of any statutory or local authority who prior to retirement or death, was service in Malaysia or in any of the territories which presently constitute Malaysia under given condition are entitled to pension benefits. The public service refer to the Judicial and Legal Service; the Parliamentary service; the General Public Service of the Federal Government; the Joint Public Services common to the Federal Government and of one or more of the states; the Education Service; the Police Force; the Public service of each state; the Railway Service and such other service as the Yang di-Pertuan Agong may determine to be public service. However GPS is not an absolute right as the Yang di-Pertuan Agong may reduce or withhold a pension if an employee has been guilty of negligence, irregularity or misconduct. The government employees must serve for at least 10 years to be eligible for a pension. They also have an option whether to take up GPS or EPF. The retirement age is 60 years old and pensions are paid for life.

The employee benefit scheme called EPF prescribed by Employee Provident Fund Act 1991 is a defined contribution plan that governed the private sector employees. It is managed by Employee

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Provident Fund. The EPF is the central pillar of retirement savings for private sector and nonpensionable public sector employees in Malaysia. All private sector employees in Malaysia who have attained the age of 16 and employed under a contract of service are required to contribute to EPF with the exception of certain categories (employees or workers holding Employment Pass or expatriates holding Visit Pass (temporary employment) ; Thai workers who enter Malaysia with a Territorial Pass; seamen; foreign domestic maids; self-employed persons; out-workers who do cleaning and alteration repair works; persons detained in custody, in prison, Henry Gurney School and mental hospital and pensioners). However, foreign workers and expatriates may opt to do so.

According to PPA 2015, PRS is a voluntary long-term investment scheme intended to help individuals accumulate savings for retirement. PRS is available for all Malaysians, whether the Government or private sector employed or self-employed, to increased their retirement savings under a well-structured and regulated environment. It is a complementary scheme to the existing Malaysian pension schemes and is governed by Capital Market and Services Act 2007 and regulated under Guidelines on Private retirement Scheme 2012.

2.2 Contributions

The GPS is a non-contributory plan. It is a way of acknowledging and appreciating the excellent service, loyalty, dedication and honesty rendered by government employees. Further it take care the life maintenance for the dependents of government employee who have passed on during the term of service with the Government or after their retirement.

In contrast, EPF is publicly managed and financed through contributions amounting to 23% of the employees' payroll. The employee contributes 11% of their salaries and the employer is obliged to contribute at least 12% but can voluntarily pay a higher rate.

As for PRS, the contributions depend on the type of scheme policies choose by the contributors. PRS have a growth fund, moderate fund and conservative fund which is selected based on age factors or preferred choice by the contributors.

2.3 Benefits

2.3.1 GPS

The government employees who retires are entitled to pension that is paid monthly; gratuity which is paid lump sum; accumulated leave; cash award in lieu of leave; disability pension may be granted where an officer, other than a contract officer is required to retire as a result of sustaining an injury in the course and arising out of performing his official duty or due to a travel

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accident or contracting a disease to which he is exposed by the nature of his duty; dependent's pension, medical benefits in and after service for spouse and children.

2.3.2 EPF

As a member of EPF, the private sector employee will receive retirement benefit that is their EPF saving, dividend that is guaranteed by the Government at the minimum rate of 2.5%, however (EPF, 2015) has declared 6.75% dividend in 2014. Other benefits are incapacitation and death benefits and tax exemption up to maximum amount of RM6,000 which can be withdrawn the whole amount. A member account is divided into two sub-accounts. Account I consists of seventy percent of monthly contributions can only be withdrawn when the account holder reaches the age of 55, becomes incapacitated or leaves the country. Until January 31, 2008, EPF members with savings of more than MR 55,000 in their Account I were able to invest part of the excess saving in products of approved investment institutions. The remaining 30% of monthly contributions allocated to the Account II can be used for medical expenses, housing loans, settling the balance of housing loan, financing education, purchasing computer, performing Hajj or it can be used for any other purposes after the members attain age of 50

2.3.3 PRS

The main objective of PRS is to help individual saves for their retirement. The Malaysian Government is also providing a tax relief of up to RM3,000 per annum on PRS contributions until Year 2022. Additionally, incomes generated via PRS are also exempted from tax. Compared to the EPF, PRS offers more flexibility in that there is no fixed amount or intervals of contribution required. PRS contributors are free to contribute whatever they can afford within their limits although PRS providers may set a minimum or maximum limit on their plans. PRS also allows the contributors to switch between plans and providers once a year subject to conditions imposed by the providers which give a certain liberty to turn to more promising plans should the need arise. Since PRS is administered by PPA who keeps track of all PRS providers and contributors, it is able to control the communications process more effectively and generally protect the interests of all parties better.

3.0 Challenges

From the above comparison, it could be observed that GPS is mandatory for government employee and EPF on the private sectors employees. As PRS is a complementary scheme and on voluntary basis, the government employee and private sector employee may not be interested in applying PRS as they already have a pension scheme when they retired. Further they might not have enough money for other investment as the cost of living is high now days especially during the economic downturn.

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Unlike EPF which is mandated by EPF Act 1991 to declared dividend of at least 2.5%, PRS does not give such a guarantee. This is another factor that makes people shun from PRS. Perhaps they might lose their investment if their PRS fund does not perform well. Further, since PRS is an investment scheme, the PRS contributors need to be aware of the quality of the fund assets, the management experience and quality of service offered by fund providers. They need to learn new knowledge about investments. However, to ensure the safety of the contributor's fund, SC Malaysia has come out with specific requirements for these funds such as experience of fund manager, the equity exposure and proof of stability based on historical performance of existing funds. These will contribute in ensuring the consistency and stability of the fund performance and thus suitable for retirement saving.

Apart from the tax exemption of RM3000, there are not many other benefits that can be derived from PRS. The amount of RM3000 exemption is too little compared to the exemption granted to savings in the EPF. The duration of tax relief is also only for ten years. The Government should reconsider regarding the amount and duration of tax exemption for PRS providers.

Further, the fees imposed by SC on the scheme and funds of PRS offered by the providers are very high. They need to pay RM5000 for establishment of any scheme whether Shariah or conventional. RM3000 must be paid for each of growth, moderate and conservative funds offered under the scheme. This is a problem to the PRS providers especially during the economic downturn. SC ought to review the fees charged to the PRS providers.

Asher and Bali, (2012, p. 65) suggest Malaysia to reform the current pension system in order to improve fairness and sustainability. The differences in the designs of the pension schemes for the government employees and private sector workers have significant implications for fairness. Malaysia needs an integrated pension system that includes publicly financed social pensions and better management of inflation, longevity, and survivors' benefits. It would be good if the Government can convince the Malaysian people that even though each pension scheme is different, however they work together and not against one another. All of them create opportunities for Malaysian people to save for their retirement.

4.0 Conclusion

It is a good effort by Malaysian government to introduce PRS which is available to all Malaysians to supplement their retirement savings under a well structured and regulated environment. However, there are several issues that need to be addressed in order to strenghten the existence of PRS. Since PRS is still new compared to other retirement scheme and it is only on voluntary basis, the Government should take proactive measures to help the development of PRS. Many incentives such as prolong the duration period of tax exemption, increased the amount of tax exemption and reduced the fees charge to PRS providers can be given to contributors and providers of PRS. This is important to enhance the quality of PRS and to promote confidence amongst contributors and future investors.

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