Private Retirement Scheme as a Financial Protection of Old-Age in Malaysia from the Perspective of PRS Providers

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Abstract: The government has recognized the importance of savings from an early age to ensure sufficient savings after retirement. To further increase savings, the government encourages youth to take a long-term investment through the Private Retirement Scheme (PRS). This study was designed to discuss the drawbacks of PRS according to the perspective of PRS providers. This study applied the qualitative research methodology by conducting interviews with the PRS providers. Thematic data analysis was used to deduce the findings gained from the PRS respondents. The findings of the research revealed that majority of the respondents agree PRS is a beneficial scheme to protect investors after retirement. However, there are a few recommendations proposed to improve the PRS, such as more tax incentives by the government, raise people awareness, etc.

Keywords: Private retirement scheme, financial protection for old-age, private pension scheme, private retirement scheme providers

Paper type: Research paper

1. Introduction

The world is experiencing rapid demographic changes in terms of population due to the increase of life expectancy in many regions. This would increase the number of elderly people which can easily fall into the poor or hard core poor group. It would cause a huge impact on the national development economically and socially especially during an acute and prominent economic crisis. Many countries have introduced social protection policies including formalizing the pension system for the old. Samad and Mansor (2013) stated that Malaysia is predicted to have 15% old-age population by the year 2030. Currently, households headed by old-age person are facing high level of poverty (8th Malaysia Plan). Therefore, the Malaysian government has emerged with better solutions in providing a social security for the poor elderly people in the coming years.

Malaysia has an old-age financial protection system which is based on the multi-pillar of World Bank framework (Security Commission). It provides assistance based on the non-contributory “zero pillar”, mandatory public pension plans, mandatory occupational or personal pension plans, voluntary “third-pillar” pension plan, and non-financial “fourth pillar”. There are three mandatory occupational pension plans and one social insurance program in Malaysia to sustain life after retirement which are Government Pension Scheme (GPS), Employees Provident Fund (EPF), *Lembaga Tabung Angkatan Tentera*/Armed Forces Fund Board (LTAT), and Social Security Organisation (SOCSO). Malaysia also has 1 Malaysia Retirement Savings Scheme (1MRSS) and the Private Retirement Scheme (PRS) for voluntary pension plan. The non-financial “fourth pillar” is a social protection given by the family, neighbours, or non-government organisations.

A survey on 2000 retirees in Malaysia has revealed that the benefits provided by EPF are not sufficient to support their retirement life. The average EPF balance for men retired in 2010 is RM160,000 while for women is RM100,000, but 50% of the EPF members retired in 2010 received balance less than RM50,000 (Syed Hamadah Othman, 2010). To overcome the problem, the EPF system has allowed its members to invest part of their savings with approved external fund managers. 30% of labour force who are mostly self-employed have no EPF/SOCSO coverage. These are the reasons why the government introduced PRS as a complement to EPF and GPS (Nur Asyikin Jamaluddin, 2012).

According to section 139A of Capital Markets and Services Act 2007 (CMSA), PRS is defined as a retirement scheme governed by a trust, offered or provided to the public for the sole purpose, or having the effect, of building up long term savings for retirement for members where the amount of the benefits is to be determined solely by reference to the contributions made to the scheme and any declared income, gains, and losses. There are eight providers of PRS, namely AIA Pension and Asset Management Sdn. Bhd., AmInvestment Management Sdn. Bhd., CIMB-Principal Asset Management Berhad, Hwang Investment Management Berhad, Kenanga Investors Berhad, Manulife Asset Management Services Berhad, Public Mutual Berhad, and RHB Asset Management Sdn. Bhd.

2. Literature Review

Malaysia applies the World Bank five-pillar pension scheme which are:

(i) The non-contributory “zero pillar” which is the social support to provide a minimum level of protection in the form of social assistance that is funded by the local, regional, or national government. The Department of Social Welfare, under the Ministry of Women, Family, and Community Development is the party responsible for providing social protection for the elderly in Malaysia (Samad and Mansor, 2013). There are three main schemes available under the Department of Social Welfare. The programs such as *Bantuan Orang Tua*, *Rumah Seri Kenangan* (retirement homes), and *Pusat Jagaan Harian Warga Emas (*elder daycare center) are under this pillar. The expenditures for these programs have been increasing but its exposure remains limited and many shortcomings have occurred, for example many poor people have not received the contribution while the people who received it are not poor (Robert Holzmann, 2015).

(ii) The “second pillar” is a mandatory public pension plan that is publicly managed. However, no program has been established under this pillar.

(iii) The third pillar is a mandatory occupational or personal pension plan. There are three occupational pension plans and one social insurance program in Malaysia. The main objective of these programs is to sustain life after retirement. It provides protection in the form of forced savings through the deduction of employees’ salary and contribution from the employers.

(a) GPS is one of the largest and the earliest protection schemes for old-age in Malaysia provided by the government under the Public Service Department (PSD). It is a non-contributory plan. However, it only covers civil servants or government employees who opted for the pension scheme. There are several types of benefits such as service pension (monthly payment), service gratuity (lump sum payment), cash award in lieu of leave (lump-sum payment), medical benefits, disability pension, dependant's pension, and derivative pension (pension benefits to a deceased pensioner's dependant who died either while still in service or after retirement) (GPS, 2016).

(b) EPF is established under the Ministry of Finance and provides social protection coverage for all private sector employees regardless of their status, as well as for government employees who opt for the EPF scheme. This is regulated under the EPF Act 1991. Both employees and employers are required to make monthly contributions, made up of 8% deduction from the monthly salary for employees below the age 60 and 5.5% to 4% for those age 60 and above, effective March 2016 until December 2017 salary, and 13% contribution from the employers. The fund is maintained in two accounts; termed Account I and Account II. For Account I, contributors can make full withdrawal upon retirement at the age of 55. The fund can also be withdrawn whenever a contributor is incapacitated, decides to leave the country, makes an investment, or deceased. The second account (Account II) is the preparation for a comfortable retirement after reaching 50 years of age. Money can be withdrawn to purchase or build a house, to reduce/redeem housing loan, for flexible housing withdrawal, to finance the education of a contributor or that of their children, to pay for medical expenses of a contributor and that of their children, and to perform the hajj (EPF, 2016))

(c) LTAT requires monthly contributions from the employees and employers of the armed forces. The LTAT has two schemes for its members. The first scheme is mandatory for the members of the armed forces who are not commissioned officers in which they have to contribute 10% of their monthly salary and 15% contribution are from the government monthly. The second scheme is on voluntary basis in which the armed forces officers may contribute a minimum of RM25 to a maximum of RM750 monthly; this is without any contribution from the government. Among the benefits are partial withdrawal to buy a house or join a retraining program for the retiring and retired members, a lump sum withdrawal, and death and disablement benefits scheme (LTAT, 2016)

(d) SOCSO is responsible for the safety and welfare of all private sector workers whether they are temporary, probation, or contract workers. The protection schemes cover death or premature death and health. SOCSO has two schemes which are the employment injury scheme (EIS) and the invalidity pension scheme (IPS). The purpose of the schemes is to give cash benefits to the workers in the case of injuries and accidents. However, the coverage does not include self-employed workers, domestic workers, civil servants, and foreign workers.

(i) EIS offers protection in terms of occupational disease, commuting accidents, emergency accidents, and accidents while in employment. Basically, EIS covers accidents that take place in the workplace or related to the job. The benefits include permanent disablement benefits, temporary disablement benefits, funeral benefits, dependants benefits, constant attendance allowance, and education loan.

(ii) IPS covers all accidents happen to the workers. It is a 24-hour coverage scheme for accidents, injuries, death, or disease occur at the workplace and do not need to be work related. The benefits given include constant attendance allowance, education loan, rehabilitation benefits, invalidity benefits, invalidity pension benefits, survivor's pension scheme, and funeral benefits (SOCSO, 2016)

(iv) The voluntary "third-pillar" pension plan. Two new programs were introduced, namely the 1Malaysia Retirement Savings Scheme (1MRSS) and the Private Retirement Scheme (PRS).

(a) 1MRSS was introduced in 2010 by the government through the EPF scheme for the self-employed workers and informal sector employees. The scheme is for those without a fixed monthly income. The contribution is voluntary for informal sector workers. A minimum contribution of RM50 monthly and the government will contribute 5% of the total contribution, subject to RM60 or a maximum amount per year until 2014. EPF manages the scheme and dividend will be given based on their savings (Samad and Mansor, 2013)

(b) Private Retirement Scheme (PRS) was introduced by the government in July 2012. This is a voluntary long-term investment and it aims to help foreign and self-employed workers to accumulate savings for retirement. The scheme has been approved by the Securities Commission. 49 funds are being offered by eight PRS providers comprised of local and international financial institutions in Malaysia (Affin Hwang Asset Management Berhad, AIA Pension and Asset Management Sdn. Bhd., Am Funds Management Berhad, CIMB Principal Asset Management Berhad, Kenanga Investors berhad, Manulife Asset Maanagement Services Bhd, Public Mutual Berhad, and RHB Asset Management Sdn. Bhd.). Contributors are free to choose any fund and they can contribute to more than one fund if they can afford to do so. Two separate accounts are maintained in which the accounts will be divided into 70% and 30%. Withdrawal of the 70% account is upon retirement while withdrawal of the 30% account is allowed once a year. Government has given incentives such as tax relief of up to RM3,000.00 for the first 10 years and tax deduction for employers if the contribution is 19% of employer's remuneration for 10 years to encourage participation in the PRS

(v) The non-financial "fourth pillar" is a social protection given by the family, neighbours, or non-government organisations. Among the formal social programs are health care or housing and other individual assets such as home ownership and reverse mortgages to serve as a source of income for the elderly.

3. Research Design

Qualitative research method was used in this study. Interviews were conducted with the PRS providers and the data were analysed according to the thematic data analysis to deduce the findings obtained from the respondents. The analysis was sorted out according to the contributions, benefits, tax deductions, profits, knowledge, and awareness of fund performance of the PRS.

The interview was conducted with five PRS providers and one PPA officer. The PRS providers were Affin Hwang Asset Management Berhad, AIA Pension and Asset Management Sdn. Bhd AmFunds Management Berhad, Kenanga Investors Berhad, and Manulife Asset Management Services Berhad. The respondents involved were the officers in charge of PRS in their organizations. Their age range is between 26 and 56 years old. They were 6 male and 1 female. The respondents' designation, inter alia, as Head of the PRS product, Senior Manager, PRS Specialist, and Senior Clerk. Most of them have experienced managing the PRS since the introduction of the scheme in 2012. The respondents have been working in the unit trust industry around 2 to 20 years. The PPA officer is the chief operating officer of PPA.

4. Results

A. Contributions

The contributions of PRS depend on the type of PRS scheme policies chosen by the contributors. PRS has growth fund, moderate fund, and conservative fund which is selected based on the age factors or contributors' preference. Some PRS providers offer zero sales charge and the account can be activated with only RM10; only if the application is done during their road show campaign. As mentioned by R4; *"We do waive a lot of fees during our campaign and road show."* PRS contributors are free to contribute whatever they can afford within their limits although the PRS providers may set a minimum or a maximum limit on their plans. It is a flexible contribution as there is no fixed amount or interval of contribution required. It also allows the contributors to switch between plans and providers once a year, subject to the conditions imposed by the providers. This gives a certain liberty to the contributors to turn to more promising plans should the need arise. All the providers agreed. R3(b) viewed it as a healthy competition between the providers and said that *"The provider must make sure that the performance is good, so the contributors stay with them."* Furthermore, this was supported by R4 who said *"We want them to have an option and to make a decision. That is why we have disclosure documents, marketing materials to ensure that they are well prepared and they are also knowledgeable enough to make a choice."* Since PRS is administered by PPA who keeps track of all PRS providers and contributors, the communication process can be controlled, it is more effective, and it protects the interests of all parties better.

PRS is a long-term investment which can only be withdrawn when a contributor reach 55 years old. It is under the strict supervision of the government. According to the PPA officer, *"The government would not let PRS fail because even though PRS is run by the private sector, it is governed by the government through the framework set by the Security Commission (SC). The PRS provider must be approved by the SC, and there is a trustee that actually looks after the investment. The provider is just the fund manager, and even the agent must be a licensed person through proper programs set up by the SC through The Federation of Investment Managers Malaysia (FIMM)".*

So the agents or distributors who sell their products must be licensed by the FIMM and subject to the approval of SC. PPA is also supervised by the SC because PPA is the central administrator. As for the providers, they are supervised and monitored through the terms and conditions of an individual license, not as an organization.

The PPA is the central administrator that manages all providers that manage the members. According to the officer of PPA; *"The investor can also subscribe or invest in more than one providers. At least the members know if there is any problem, they can just call the PPA".*

B. Benefits and tax deductions

There are many benefits for the contributors who invest in PRS for their future retirement. According to the Prime Minister of Malaysia when announcing the Malaysian Budget 2013, among the incentives given are;

a) personal tax relief up to RM3,000 for contributions by individuals to PRS approved by SC;
b) tax deductions to employers for contributions above the statutory rate up to 19% of employees' remuneration; R2 explained that; *"…if the employer pay an EPF, 12% will be deducted for tax relief and the additional 7% tax will be given to the employers that participate in the PRS. So the total is up to 19%." R5 added that"…this tax deduction is only up to 10 years…. 2012 up to 2021, not forever"*
c) tax exemption on income received by funds within the scheme;
d) proposed tax deduction on employers' contributions to the scheme for their employees (Malaysia's Private Retiement Scheme (2012).

In the 2014 Budget presented on 25 October 2013, the Prime Minister announced an incentive of RM500 as a one-off contribution to young PRS members (aged between 20-30 years) to purchase units of PRS fund, whom have accumulated a minimum gross contribution of RM1,000 within a year. This incentive is available for a period of 5 years from 2014 to 2018 (Security Commision, 2016).

Furthermore, the establishment of the Private Pension Administrator (PPA) that was set up in July 2012 to protect investors' interests is viewed as a positive development for the pension fund industry. Among other functions, this statutory body supports investors in switching PRS providers. The rules allow investors to switch provider once a year, so that consumers have the choice to switch to another PRS provider when they are not happy with their current provider (PPA, 2016).

C. Profits

There is no rule or regulation that guarantees the profit for PRS funds. The contributors' interest is not secure. All of the return is totally depending on the funds. This is admitted by R2, *"In investment they don't* *apply this law (compensation)."* This is confirmed by R3(a) "*...It is disallowed by the SC to guarantee the profit of PRS funds."*

D. Knowledge and awareness of fund performance

The contributors of PRS providers need to be aware of the quality of the funds, the management experience, and the quality of service offered by the providers. It is the duty of the providers to educate their customers in regard to the position of the funds. R1 (a) stated that they educate their contributors by providing them with an annual report and contributors can also get the knowledge from the PPA website. Some providers would require their contributors to do the risk profiling assessment in order to know the level of risk appetite that the investors prefer. As mentioned by R2, *"…when you sign up the PRS; you have to undergo the risk profiling. Meaning you will be asked the appetite of the risk and its weight. So if we found a conservative client, we cannot propose very high risk of funds. That is a way in educating our client."* It is also agreed by R5 that having the list of questions, known as the risk profiling, would make them know more about their contributors and this would also educate their contributors better.

E. Strict legislations

Malaysia has a firm and strict legislation regarding the PRS. R2 confirmed that "*Based on the feedback that FIMM received, Malaysia belongs to the group of regulators that have a very tight and stringent requirement. Firstly is from the contributor protection and also from the prospective of the PRS provider, they are actually increasing their operating cost. Many procedures need to be followed".*

F. Publicity

Many Malaysians are not aware of the existence of PRS. This is agreed by the PRS providers themselves. R1 (a) and R1 (b) suggested that the PPA as the administrator must arrange some activities and attractive approaches to market the PRS among Malaysians. As mentioned by R1 (a), "*I think PPA has to do more on the awareness and educate people. But, of course we do our part but not much we can do. I think 50% of the people we talk to don't know about PRS. Especially the working people, the target market is young adults and working adults. So aggressive awareness has to be done*". This is also supported by R1 (b), "*We really hope that PPA could be more aggressive after this in the sense of promoting and arranging activities*".

5. Conclusion

Even though, the introduction of PRS is an exciting milestone for Malaysia's pension industry and a long awaited savings opportunity for the middle-income earners, there are also some flaws in the scheme as it is still in the introductory phase. Among the flaws are contributors must be knowledgeable in the PRS funds, the incentives given to the PRS contributors are not adequate, the PRS funds are not protected or guaranteed, and minimum publicity on the PRS funds.

The contributors must be knowledgeable in their PRS investment especially during the economic downturn. They need to be educated regarding the pros and cons of the PRS products in order to choose the funds that match their retirement goals and risk appetites. In this regard, contributors should bear in their mind the five key points which include the quality of a fund's assets, compare sales charges, management experience, ease of switching, and quality of servicing. Not many contributors have the ample time to learn about these. It is suggested that a standard form such as risk profiling is used by all PRS providers to educate the PRS contributors.

To further strengthen the confidence of PRS contributors, some of the PRS providers have recommended the government to insured PRS funds as bank insured their funds through Malaysia Deposit Insurance Corporation (MDIC). Another factor that can encourage people to take PRS is increasing the tax incentives. FIMM has proposed to the government to increase the tax incentives up to RM6000. However, it has been rejected due to the economic downturn. The duration of tax relief must also be prolonged.

Another challenge is regarding creating the awareness of PRS. People in the rural area are not aware of PRS. As for those in the urban areas, although they know about PRS, they are not really convinced in PRS because it is not a compulsory scheme. More approaches need to be done in creating the awareness of PRS among us. Malaysian public and private employees already have the EPF and GPS for their retirement savings, only the remaining income can be placed in the PRS funds if they want to as it is only voluntary. They need to be educated that EPF, GPS, and other investments are not enough for a secure retirement. Besides, PPA should play a vital role in promoting and have an aggressive approach in attracting people to invest in the PRS.

Furthermore, the government needs to soften the law and procedures on PRS so that it will not burden the contributors and the PRS providers; especially the fees impose to the PRS providers.

In conclusion, as an alternative pension scheme to Malaysian citizens, several issues related to PRS need to be addressed. This is to make the alternative pension schemes available more comprehensive to all Malaysians to supplement their retirement savings.

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