KHAZANAH RESEARCH INSTITUTE

VIEWS 8/24 | 10 MAY 2024

Make EPF account restructuring a step towards a more comprehensive pension reform

Hawati Abdul Hamid and Puteri Marjan Megat Muzafar

Introduction

The Employees Provident Fund's (EPF) recent announcement on restructuring members' accounts from two to three, namely Akaun Persaraan, Akaun Sejahtera and Akaun Fleksibel, represent a refinement to Malaysia's retirement saving scheme[1]. The restructuring exercise appears to take a middle approach in striking a balance between meeting the contributors' short-term needs and long-term financial security for retirement. The newly created Akaun Fleksibel provides flexibility for members to utilise savings as and when needed, contrary to the other two accounts that have age and use limitations for withdrawals.

Views are short opinion pieces by the author(s) to encourage the exchange of ideas on current issues. They may not necessarily represent the official views of KRI. All errors remain the authors' own.

This view was prepared by Hawati Abdul Hamid and Puteri Marjan Megat Muzafar, researchers at the Khazanah Research Institute (KRI). The authors are grateful for the valuable comments from Azfar Hanif Azizi.

Author's email address:
hawati.hamid@krinstitute.org
marjan.muzafar@krinstitute.org

A version of this article was published in Free Malaysia Today, Malay Mail, The Star, The Edge Malaysia Weekly, News Strait Times, and Free Malaysia Today.

Information on Khazanah Research Institute publications and digital products can be found at www.KRInstitute.org.

[1] EPF (2024)

Meanwhile, the 5% increase in the Akaun Persaraan's contribution to 75% underscores EPF's commitment to prioritising adequate retirement income (see Table 1 to compare the current and previous structure of the accounts and their distribution rate). The 75% translates to an 18% contribution rate (from 24% of employer and employee contribution), a rate relatively higher compared to some neighbouring countries.

Table 1: Structure and distribution rate of EPF accounts

	Account 1	Account 2
Previous	70%	30%

	Akaun Persaraan	Akaun Sejahtera	Akaun Fleksibel
New	75%	15%	10%

Source: EPF (2024)

Akaun Fleksibel—a double-edged sword

The initiative reflects EPF's greater goal of addressing Malaysia's social security coverage gap which is still wide among Malaysia's workforce. The Akaun Fleksibel aims to encourage participation among non-contributors, such as the self-employed and informal workers. The account offers an option for those who wish to save for retirement yet need flexibility in dealing with cashflow issues— particularly those with variable and irregular income.

Findings from EPF's public consultations indicate that as high as 83% preferred empowerment through a flexible withdrawal, while 63% are willing to trade off increasing allocation to Akaun Persaraan (Account 1) for flexibility.

However, there is a high likelihood of EPF members making full or continuous withdrawals from Akaun Fleksibel, resulting in a zero balance and worsening saving inadequacy issues. To minimise this risk, comprehensive educational initiatives should accompany these changes to ensure that contributors make informed decisions that support their overall financial well-being. For example, while the new account makes withdrawals easier for members, they should be made aware of the consequences on their long-term savings and missing out on the compounding effect. Overall, the coming months will be crucial in evaluating the impact of the restructuring on attracting new members, reallocation of savings and withdrawal patterns from members.

A more comprehensive reform is needed

In light of Malaysia's rapid ageing and serious old-age income security adequacy, this initiative should mark a step towards a broader reform of the retirement ecosystem. It is timely to review the EPF's existing withdrawal age policies considering that some were determined since the 1950s, at a time when our life expectancies were much lower[2].

[2] EPF (2023)

For example, the full withdrawal age at 55 years was set in 1952 when life expectancy was 54.2 years[3]. Our life expectancy has now increased to 75 years. This means that the retirement saving needs to be adequate to sustain life for at least 20 years after full withdrawal age. Other potential initiatives could also include deepening progressive contributions and introducing progressive dividends. Khazanah Research Institute's (KRI) analysis indicates that increasing contribution period through a higher retirement age is expected to have the largest impact on members' savings, followed by progressive dividends and progressive contributions[4].

Beyond these, it is essential to emphasise that Malaysia's multi-tiered retirement ecosystem has yet to fully achieve its intended objectives and continues to grapple with coverage gaps, inadequate benefits and unsustainable financing. The tax-funded old-age pensions only cover civil service retirees (via the civil service pension) and selected poor elders (via the Bantuan Warga Emas).

Funding these pensions is challenging, particularly with the looming ageing population. Additionally, while EPF is meant to cover private sector workers, many remain unregistered—and among those who do, many have low savings that are insufficient for a comfortable retirement.

Pension floor for all

Given fiscal constraints and rapid ageing, we need to seriously explore other financing options as old-age poverty is expected to be higher in the future. One alternative that can be considered is a contributory pension within EPF schemes i.e. a hybrid of defined benefit (DB) and defined contribution (DC) scheme[5]. Through this, retirement savings are done collectively rather than individually, with everyone contributing a small amount while they are working into a collective fund. By a certain age, say 60 or 65, the fund can be dispersed to all as an old-age pension until their end of life (an annuity). The government plays an important role in ensuring continuity of contribution across a lifetime when we are unable to contribute e.g. having illness or disability, being laid off, and performing childcare or elderly care.

However, one of the main setbacks of building this collective fund is that we will not reap the rewards immediately. The fund needs time to grow, and it will be a slow process as we are only planting the seeds now if such a fund is created. Ultimately, Malaysia must seriously consider moving towards a model where we **minimise our individual risks** and **maximise our collective potential** as we move towards a more ageing society.

[3] UN (2022)

[4] KRI (2021)

[5] In KRI's report titled Building Resilience: Towards Inclusive Social Protection in Malaysia, we unpack the proposal with several options on how to make the scheme feasible. This might entail earmarking or ring-fencing a share of EPF contribution to the collective fund.

References

EPF. 2024. Press release: EPF Account Restructuring Set to Address Members' Life Cycle Needs. https://www.kwsp.gov.my/w/epf-account-restructuring-

EPF. 2023. Integrated Annual Report 2022: Shaping Sustainable Futures.

KRI. 2021. Building Resilience: Towards Inclusive Social Protection in Malaysia. Kuala Lumpur: Khazanah Research Institute. https://krinstitute.org/Publications-@-Building_Resilience-;_Towards_Inclusive_Social_Protection_in_Malaysia.aspx

UN. 2022. *World Population Prospects 2022, Online Edition*. United Nations, Department of Economic and Social Affairs, Population Division.