Volume 11 / June 2024

EPF Account Restructuring: Requirements, Opportunities and Challenges

Mohaini Ahmad Basri

Licensed Financial Planner, WealthVantage

In the context of national retirement savings, the Employees' Provident Fund (EPF) plays a crucial role in helping Malaysians prepare for their retirement. Over time, significant changes have occurred in Malaysia, especially regarding societal lifestyle, socio-economic levels, education, and population demographics, all of which impact the EPF's function. Consequently, there is a need to restructure the EPF accounts. This change presents both opportunities and challenges. From the perspective of a financial planner, it is essential to dissect the multifaceted implications of these changes.

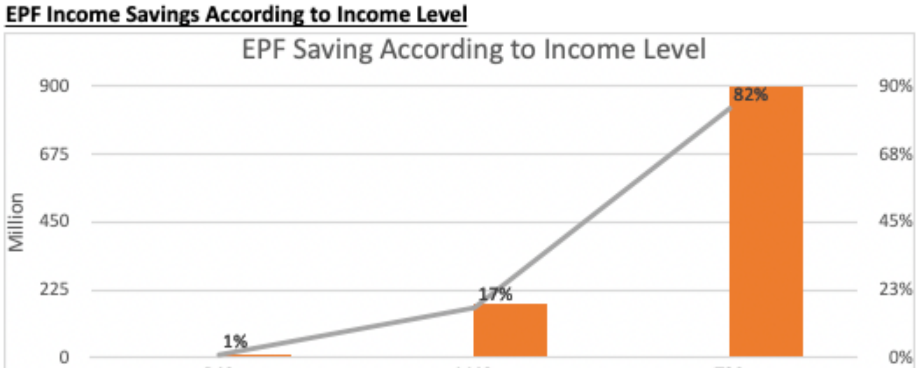
The opportunities stemming from EPF restructuring are manifold. By realigning account structures, such as transitioning from the traditional two-account model (Account 1 and Account 2) to a more diversified three-account framework, including the Retirement Account, Sejahtera Account, and Flexible Account, EPF aims to enhance flexibility and cater to a broader spectrum of financial needs.

This restructuring not only promises improved financial security during retirement through enhanced savings accumulation but also introduces avenues for more strategic financial management across various life stages. For instance, the Sejahtera Account focuses on immediate life-cycle needs like housing, education, and healthcare, providing members with targeted solutions to manage these critical expenses efficiently. Overall, we will explore various aspects of these opportunities, challenges, and proposed enhancements to optimize this transition from the viewpoint of a financial planner.

Restructuring Requirements

The EPF's changes are well-grounded, supported by several factors. Serving as a mandatory savings plan for Malaysian workers, the EPF ensures a financial safety net upon retirement, with contributions from both employees and employers managed for long-term returns. However, evolving circumstances necessitate restructuring the EPF framework to meet future challenges. A key factor is the significant demographic shift, with Malaysia's population aging alongside advancements in health technology, resulting in a higher average age of 74.8 years, according to the Department of Statistics Malaysia (DOSM). Concurrently, rising living costs, economic instability, and inflation diminish the purchasing power of retirement savings. Moreover, there's a notable shift in current financial priorities. Increased financial education initiatives highlight that needs extend beyond retirement savings to encompass healthcare, education, housing, and others.

EPF Income Savings According to Income Level



Median Savings:

- T20: RM 170,266
- M40: RM 20,660
- B40: RM 1,063

Source : EPF

Corresponding author: mohaini@wealthvantage.com.my

Recent statistics show significant differences in savings among the income groups. Both the average and median savings between the B40, M40, and T20 groups exhibit vast differences, with notable outliers within the T20 group. The median savings of the T20 group (RM 170,266) is almost 160 times that of the B40 group (RM 1,063) and 8 times that of the M40 group (RM 20,660).

The savings difference between the B40 and M40 groups is nearly 19 times. This disparity is quite alarming. Despite being the smallest group, the T20 holds 82% of the total EPF savings, while the B40 and M40 groups hold only 1% and 17% of the total savings, respectively.

It is important to understand the situation further by looking back at the time during the MCO. As a result of the MCO, it was reported that the median EPF savings for the B40 group plummeted by 70% to just RM577 from RM2,434 previously. For the M40 group, median savings fell by 34% to RM19,926 from RM30,113 previously. EPF withdrawals during this period also resulted in more than half of EPF contributors (6.7 million members) now having savings of less than RM10,000.

The median EPF savings also decreased by more than 50% to RM8,100 compared to RM16,600 before the COVID-19 pandemic. This highlights the severe inequality in savings among these groups. Severe inequality is detrimental to the overall economy. Those who lack funds continue to struggle, even though they constitute the majority. This situation possibly shapes the new EPF account structure, which may offer both advantages and challenges to the people

EPF Account Restructuring

Following the restructuring, member accounts will transition from two (Account 1 and Account 2) to three distinct accounts:

- Retirement Account (75%): The main account for accumulating retirement savings.

- Sejahtera Account (15%): Aims to help with current life cycle needs such as housing, education, and health.

- Flexible Account (10%): A new account providing flexibility for short-term financial needs, allowing savers to withdraw savings at any time according to their needs.

Opportunities and Challenges of EPF Account Restructuring

Although the Flexible Account provides members with the ability to make withdrawals at any time, the overall structure increases the proportion of funds allocated to retirement accounts. This shift benefits members by ensuring they have more savings during retirement. Indirectly, this restructuring promotes disciplined saving habits. As financial planners, our observations suggest that many members lack saving discipline, and this change is expected to enhance their savings behaviour. With larger savings, members will enjoy stronger financial security for retirement. This means they can cover the rising cost of living and meet other financial needs, such as healthcare, without worry.

Flexible Withdrawal Opportunities

Flexible withdrawals provide numerous opportunities for members to access essential services.

Addressing Emergency Needs

Many members face significant financial hardship. This mechanism helps address immediate needs, allowing individuals to maintain a lifestyle that suits their circumstances. According to Malaysia Department of Insolvency (MDI), personal loans account for nearly half (49.22%) of all bankruptcy cases over a five-year period, followed by business loans at 17.05%. Vehicle financing and housing loans also contribute significantly, comprising 11.11% and 8.28% of total cases, respectively. As a result, personal loan-related bankruptcies are the most prevalent in Malaysia. The restructuring of EPF accounts may help address issues related to personal financial management and reduce bankruptcy rates.

Avoid Borrowing from Loan Sharks or Unauthorized Financial Institutions

This mechanism also prevents members in need from resorting to loans from unapproved sources, thereby enhancing their economic and financial security. As financial planners, we encounter many cases of individuals seeking advice related to high-interest loans from unapproved lenders. According to Bukit Aman's Commercial Crime Investigation Department (CCID), the statistics for cases of unlicensed money lending from January to April 2024 amounted to 260 cases with a loan value of RM1.04 million.

With the changes, it can protect low- and middle-income groups from falling into debt crises over time. Loan sharks operate in communities with limited access to formal financial institutions, offering lenient borrowing requirements and fast approval processes, which attract individuals facing urgent financial needs. However, these loans come with high interest rates and unfavourable terms.

Improving General Protection

For those not struggling with basic necessities, the benefits from EPF can be used to contribute to insurance/takaful that suits their needs. Although EPF through i-Lindung offers such services, there are limited options from a few operators. Recent statistics show that only about 40% of Malaysians contribute to such insurance. This action can help members manage future health costs, which is a primary reason for the premature depletion of savings in old age.

At the same time, statistics show that a significant number of accidents involve motorcycle riders, and unfortunately, many of them are not protected by any insurance. In 2022, the nationwide road accident fatalities totalled 6,080, increasing to 6,344 in the following year. Specifically, approximately 4,000 of these fatalities involved motorcycles. Personal accident premiums are generally low, making it easier for members to subscribe to this insurance. Overall, the move is commendable, considering many individuals still lack health contributions. In addition to that, members contributing to health can reduce the financial burden on government services.

Investment Opportunity

This EPF Account restructuring allows members to plan their investments in approved avenues. For instance, if a member invests a surplus of RM 100 per month for 20 years with 8% return yearly, the accumulated amount is around RM 59,000. In addition to that, the restructuring of EPF allows funds to be invested in a more diversified portfolio, including global and alternative investments, potentially increasing the average annual return compared to current EPF offerings. This, in turn, helps increase members' final savings amounts. The T20 group could benefit the most from this scheme. Recent data shows the T20 group has savings around RM 896 billion, constituting 82% of the overall savings. Assuming 10% is withdrawn from the Flexible Account, approximately RM 8.9 billion could be invested, significantly boosting the local economy.

Enhanced EPF Investment Planning

From an economic standpoint, the Flexible Account, which offers flexible withdrawals, enables EPF to strategize and develop more effective investment approaches, resulting in higher returns for members compared to the ad hoc withdrawals seen during the MCO period. With a structured mechanism in place, EPF can also improve its forecasting of new investments aligned with anticipated withdrawal amounts. At the same time, higher savings in the Retirement Account enable EPF to build a more diversified investment portfolio, yielding better returns for members. During the MCO, the government introduced schemes like i-Citra and i-Lestari, resulting in RM 145.1 billion in withdrawals. Such significant withdrawals can affect EPF's long-term investment plans.

Challenges

While these changes offer numerous opportunities and benefits to EPF members, they also present financial challenges that need careful consideration. Recent reports state there have been three million applicants for the Flexible Account, resulting in withdrawal applications amounting to RM 8.78 billion. One of the primary challenges is ensuring that the flexibility of the Flexible Account does not lead to premature depletion of retirement savings. The ability to withdraw funds at any time for short-term needs could tempt members to prioritize immediate consumption over long-term financial security. Without proper financial planning and education, members might find themselves with insufficient savings during retirement, which could undermine the primary purpose of the EPF.

Educating Members for Optimal Use

First and foremost, members need to be educated about using their EPF savings effectively. For instance, consider a scenario where an individual uses their EPF savings to cover basic necessities such as food, shelter, and transportation. This is crucial because it ensures that the funds serve their primary purpose of providing financial security. Misusing these funds for less beneficial expenditures, such as luxury goods or non-essential services, could undermine the long-term benefits of the EPF restructuring.

According to a survey by the Financial Education Network (FEN) in 2023, only 36% of Malaysians have a clear understanding of basic financial concepts. Therefore, targeted educational campaigns should be implemented to inform members about prudent spending and saving practices. According to FEN, financial literacy is a combination of financial awareness, knowledge, skills, attitudes and behaviours necessary to make sound financial decisions and ultimately achieve individual financial well-being.

Lack of Investment Knowledge

For members who do not need immediate withdrawals from their Flexible Account for daily expenses, optimizing it for investment is advantageous. However, learning to invest is essential. Investment can significantly enhance their retirement funds, but it requires knowledge and strategic planning. Members without comprehensive investment knowledge should seek guidance from licensed financial planners. Professional advice can help them navigate the complexities of the investment landscape, ensuring they make informed decisions that align with their financial goals and risk tolerance.

Streamlining the Withdrawal Process

Efficient management of the withdrawal process is critical to the success of the EPF restructuring. Ensuring that members can quickly and seamlessly access their funds when needed is paramount. Enhancing IT facilities is a key component of this, as it can streamline transactions and reduce delays. For example, the introduction of the EPF i-Akaun has significantly improved the speed and efficiency of transactions, with over seven million members registered as of 2021. Additionally, special assistance programmes for the elderly should be established to help them navigate the withdrawal process. This includes providing clear instructions, dedicated support services, and possibly in-person assistance to ensure they can access their funds without undue hardship.

Awareness of Investment Risks

While the option to use Flexible Account savings for investment can be advantageous, members must be aware of the associated risks. Investments are inherently tied to market conditions, and in volatile periods, there is a risk of loss. For example, during the 2020 market downturn due to the COVID-19 pandemic, many investors saw significant losses in their portfolios. At the same time, it is crucial to educate members about the potential dangers of investing in unapproved schemes or falling victim to scams.

According to the Malaysia Securities Commission (SC), nearly one-third of Malaysians are at risk of falling victim to investment scams. More than RM1.34bil was lost to scams in 2023 compared with RM804mil in 2022 involving 33,235 cases. Members should be encouraged to conduct thorough research and only engage with credible and licensed investment opportunities. The relevant authorities must continuously monitor, while regulatory oversight can further protect members from fraudulent activities.

Addressing Financial Literacy Challenges

The effectiveness of financial education initiatives is often limited by the varying levels of financial literacy among EPF members. Those with lower financial literacy may struggle to understand and benefit from the restructuring fully. To address this, tailored educational programmes that cater to different literacy levels are necessary. These programmes should employ a range of teaching methods, from simple guides and workshops to one-on-one financial counselling sessions. Additionally, leveraging technology such as mobile apps and online resources can provide accessible and user-friendly educational tools for all members.

Implementing Change Effectively

To ensure the careful and safe implementation of EPF restructuring while achieving the goal of improving societal well-being, comprehensive financial education is essential. Financial agencies and those involved in financial management must be equally engaged. With the restructuring of EPF accounts, the role of financial planners becomes increasingly significant. Financial planners can assist members in the following ways:

a) Meeting with clients to discuss their current financial situations, set goals, and assess potential risks: Financial planners can help members understand their financial standing and set realistic goals, ensuring they are prepared for future challenges.

b) Helping clients create personal budgets to achieve their savings goals: Financial planners can guide members in creating and maintaining budgets that align with their financial objectives, promoting disciplined saving habits.

c) Assisting clients with retirement planning, mortgages, properties, estate management, and other financial needs: Comprehensive financial planning services can ensure that members are well-prepared for all aspects of their financial lives, from retirement to property management.

d) Providing investment advice to avoid dubious investment activities: Financial planners can help members navigate the investment landscape, steering them away from risky or fraudulent schemes and towards sound investment opportunities.

In general, a comprehensive public awareness campaign is crucial to educate stakeholders about the benefits and necessity of the restructuring. Involving stakeholders in the decision-making process can foster a sense of ownership and acceptance. Providing support and resources during the transition can help reduce anxiety. Continuous monitoring is necessary to ensure that the restructuring of EPF accounts truly benefits members.

Conclusion

The restructuring of EPF accounts presents both opportunities and challenges, but overall, the potential benefits are significant. This restructuring promises greater financial flexibility for members. Despite the challenges, effective mitigation measures can ensure that this transition is beneficial for all parties involved. To achieve careful and safe implementation while improving societal well-being, financial education must be prioritized. The restructuring of EPF accounts in Malaysia signifies a substantial change with opportunities and challenges that necessitate involvement from financial agencies and those engaged in financial management, particularly financial planners. Financial planners can assist members in maximizing the benefits of these changes while mitigating associated risks.

They play a vital role in educating members about financial management – how to use their funds wisely, invest prudently, and be aware of the risks involved.

At the same time, by leveraging technological advancements, improvements can be made to the withdrawal process and addressing financial literacy challenges. Most importantly, members can reap the maximum benefits from the restructuring and secure a stable financial future.

While EPF's restructuring presents both challenges and opportunities, its ultimate goal remains clear: to optimize retirement savings mechanisms in Malaysia. Financial planners, equipped with expertise and dedication, are pivotal to facilitating this transition by empowering EPF members with the knowledge and strategies needed to navigate the complexities of modern financial landscapes effectively. By embracing these changes thoughtfully and collaboratively, EPF and its stakeholders can forge a path towards sustainable financial security and prosperity for all Malaysians.

References

The Star. (2024, February 29). *One death every two hours due to motorbike accidents in Malaysia, says JPJ.* https://www.thestar.com.my/news/nation/2024/02/29/one-death-every-two-hours-due-to-motorbike-accidents-in-malaysia-says-jpj#:~:text=Its%20senior%20enforcement%20director%20Datuk,deaths%20are%20those%20involving%20motorcycles

OECD International Network on Financial Education (INFE). (2023, December). *Financial literacy in Malaysia* [PDF]. Financial Education Network. https://www.fenetwork.my/wp-content/uploads/2023/12/OECD-INFE-2023.pdf

Sinar Harian. (n.d.). *RM145 bilion simpanan KWSP dikeluarkan sejak pandemik*. https://www.sinarharian.com.my/article/215359/berita/nasional/rm145-bilion-simpanankwsp-dikeluarkan-sejak-pandemik

Berita Harian. (2023, March). *Kawal pengeluaran caruman KWSP elak implikasi jangka panjang.* https://www.bharian.com.my/rencana/lain-lain/2023/03/1079528/kawal-pengeluaran-caruman-kwsp-elak-implikasi-jangka-panjang

Sinar Daily. (n.d.). *Only 40 per cent of Malaysians have insurance protection.* https://www.sinardaily.my/article/212355/focus/national/only-40-per-cent-of-malaysians-have-insurance-protection

MalaysiaNow. (2022, August 8). *RM145 billion EPF savings withdrawn under COVID-related programmes.* https://www.malaysianow.com/news/2022/08/08/rm145-billion-epf-savings-withdrawn-under-covid-related-programmes

Malaysia Department of Insolvency. (2022). *Bankruptcy statistic 2022*. https://www.mdi.gov.my/index.php/legislation/statistics/75-bankruptcy/1983-bankruptcy-statistic-2022

The Malaysian Reserve. (2024, May 6). *Loan sharks: Malaysia's battle against unethical lending practices.* https://themalaysianreserve.com/2024/05/06/loan-sharks-malaysias-battle-against-unethical-lending-practices/#google_vignette