Issues in incomes provision for the elderly in Malaysia

Kevin CARAHER

Department of Sociology and Social Policy
University of Durham
United Kingdom

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Kevin Caraher
Department of Sociology and Social Policy
University of Durham
United Kingdom.

This paper will discuss whether the current levels of income provision for the elderly under the auspices of the Employees Provident Fund are sufficient to meet the needs of the increasingly elderly population in contemporary Malaysia. It concludes that:
(1) Lump sum payments do not represent the best option for income security into old age;
(2) Increased accessibility to funds prior to retirement, through dedicated separate accounts, lessens the ability of the EPF to act as a reliable source of income for the elderly;
(3) Current arrangements are inadequate to meet the needs of an increasingly elderly population and thus leaves them more vulnerable to the socially exclusive aspects of poverty in old age.¹

The most important sources of non-familial support for the elderly in Malaysia are the Employees Provident Fund (EPF) and other limited pension schemes (Haaga, Peterson et al, 1990). There exists a degree of reluctance, on the part of states which rely on fully funded individual savings schemes in the form of provident funds, to develop a social insurance based pension scheme which would offer a basic guaranteed income for the elderly beyond retirement. Focussing on Malaysia, this paper seeks to highlight a number of issues raised as a result of an over reliance on the EPF to provide income beyond retirement. The processes of economic globalisation and increased urbanisation raise concerns regarding the future abilities of traditional systems of support to cater for the more vulnerable members of society. This may lead to increased demands on individual savings, which, at present are insufficient to solely meet the needs of life beyond retirement. This paper does not suggest an either or solution. Rather it acknowledges that both individuals and the state are central to the provision of adequate living standards beyond retirement. Improving current schemes and supplementing individual provision with a social insurance based pension would, it is argued, provide a greater guarantee of income for the elderly and increase the chances of avoiding the socially exclusive aspects of poverty in old age.

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Is Malaysia ageing?

There is little doubt that an increasingly ageing global population is a focus of primary concern regarding quality of life and guarantee of income provision for the elderly. Not only to those who have a dedicated academic interest in this field, but also to a great many governments, non-governmental organisations both national and transnational, and perhaps most importantly of all to individual citizens planning for life beyond retirement. It is the choices made by both individuals and organisations, which will impact upon the quality of life experienced by the elderly regardless of geography. The aim surely must be to avoid excluding from the mainstream those who have contributed to an improved quality of life enjoyed by present, and successive, generations.

The global aged population, that is those aged 60 and above, is expected to increase almost threefold between 1990 and 2030 (Williamson and Pampel, 1998). The majority of this increase, that is more than 50%, will occur in developing nations, and in particular Asia (World Bank, 1994). This paper is concerned with issues regarding the provision of income for the elderly, and taking Malaysia as its exemplar, seeks to examine the adequacy of current arrangements in meeting the needs of an increasingly aged population.

Malaysia’s total population currently stands at approximately 22.8 million of which approximately 21.5 million qualify as citizens (Mid-term Review of the Seventh Malaysia Plan (MTR7MP), 1999, Table 4.1). Classified as an upper middle income country (World Bank, 1997), the per capita income currently stands at RM 12,135. This reflects Malaysia’s swift recovery from the regional financial crisis which began in 1997, and saw GDP rate (at 1987 prices) of –7.5% in 1998 recover to stand at +5.4% in 1999 (Department of Statistics, 2000).

The population is projected to increase at an average annual rate of 2.2%, with a growth rate for those aged 65 and above estimated at 4.1% (MTR7MP, 1999, Table 4.1). Life expectancy in Malaysia has continued to increase from 68.8 years for males and 73.4 years for females in 1991 (Asher, 1994), to 69.6 years for males and 74.5 years for females in 1997 (MTR7MP, 1999, Table 12.3). The elderly share of the total population, which stood at 5.7% in 1991, is estimated to reach 14.5% by 2020 (Asher, 1998). This will be reflected in an estimated increase of elderly persons aged 60 and above from 1 million in 1991, to 3 million in 2020 in Peninsular Malaysia (Chan and Da Vanzo, 1996). It is clear from the data presented that the Malaysian elderly are living longer and are increasing as a percentage of the total population. Taking account of the fact that the normal retirement age is approximately 55 years, there is a real and contemporary need for the establishment of an adequate system of income provision beyond retirement.

Sources of incomes provision for the elderly in Malaysia

There exists in Malaysia a broad spectrum of social security schemes that differ philosophically in their approach (Asher, 1994). Some schemes subscribe to the notion of social insurance, primarily legislated for under the Employees’ Social Security Act 1969
(SOCSO). Others rely on the principles of individual provision for old age under the Employees’ Provident Fund (EPF). It is the latter, which represents the dominant philosophy, and that which provides the greatest extent of cover for individuals seeking to fund life beyond retirement.

It is correct to state that the EPF plays a central role in the provision of income security for the elderly in Malaysia. However, we would be in error, if we did not at the very least acknowledge the role that the family has played and continues to play in the support of the elderly. The strength of familial support, based on concepts of filial piety has been well documented elsewhere (Jones, 1993, Lillard and Willis, 1997). However, there are concerns that westernisation, through the process of economic globalisation, will see an erosion of familial support and filial piety at present associated with Asian cultural values (Martin, 1989; Schulz, 1993).

Our main concern here is the role that intergenerational transfers play in the provision of income for the elderly beyond retirement. It can be argued that the family in Malaysia is the central welfare provider, both in monetary terms and in the provision of social care (Schulz, 1993; Da Vanzo and Chan, 1994; Lillard and Willis, 1997). At present it is common practise for adult children to co-reside with their parents. Data drawn from the Second Malaysian Family Life Survey (MFLS-2) (1993) indicates that more than two thirds of Malaysians aged over 60 co-reside with an adult child. Indeed there are economic incentives in place to encourage the continuation of this practice. Adult children who live with their parents enjoy a tax rebate of RM1000; 1991 legislation introduced a RM1000 tax deduction against medical expenses incurred by adult children for the care of elderly parents, and a further RM1000 is tax deductible against the purchase of necessary equipment for disabled parents. However, it can be argued that the dual processes of rapid industrialisation and urbanisation may have a detrimental effect on the ability of the family to offer support to those more vulnerable members. Both geographical dispersion and the growing trend for smaller family units may require an extension of formal social protection to fill the role traditionally associated with the family (Schulz, 1997).

It would be useful at this juncture to present a brief overview of the main social security schemes. We shall then turn our attention to the main focus of this paper, that is whether the current levels of income provision for the elderly under the auspices of the EPF are sufficient to meet the needs of the increasingly ageing population in contemporary Malaysia.

**Social Insurance schemes**

The Employment Injury Insurance Scheme and the Invalidity Pension Scheme were created by the Employees’ Social Security Act 1969 and implemented in 1972 and 1974 (Peninsular Malaysia) respectively. A pilot scheme was initially based in larger towns.

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2 Da Vanzo and Chan, 1994 cite private correspondence from JKC Kiet, Head of Inland Revenue Tax Dept, Sarawak Jan 1993.
and rolled out to the whole of the Peninsular in 1980 (Asher, 1994 p.23, citing Singh, 1992 p.10). As noted SOCSO operates as a social insurance system.

The Act covers all employers employing one or more persons and relates to those employees earning less than RM2000 a month. Total membership of SOCSO for 1998 stood at 8,428 589 (cumulative) while the total number of registered employers was 358 543 (Ministry of Human Resources). Once covered by the scheme employees remain insured against work-related injury, invalidity or death, even if subsequently the employees’ earnings rise above the qualifying threshold.

Employers contribute 1.25% of an employee’s monthly wage towards the Employment Injury Insurance Scheme, which covers industrial accidents, occupational diseases and commuting accidents. In the case of the Invalidity Pension scheme, both employers and employees contribute 0.5% of the monthly wage.

The Employment Injury Insurance Scheme has no minimum qualifying period and provides a temporary disability benefit equivalent to 80% of wages subject to a minimum of RM9 per day. This benefit is payable after a four-day waiting period and paid in arrears should the disability last longer than four days. Permanent disability benefit is equivalent to 90% of wages if totally disabled, subject to a minimum of RM9 per day. Up to one-fifth of contributions is payable where disability exceeds 20%. If the disability is assessed to be less than 20% the lump sum is paid to the injured party. There is provision for a constant attendance supplement, which is equal to 40% of the pension up to a maximum of RM500 per month. Medical benefits such as treatment costs, hospitalisation, medicines, artificial limbs and other prosthetic appliances, and physical and vocational rehabilitation are provided for under the scheme. As are dependants benefits in the form of a survivors pension, equivalent to 60% of the permanent disability pension payable to the widow, dependant children each receive a payment equivalent to 40% (60% if orphaned) of the permanent disability pension up to age 21. A funeral grant of up to RM1000 is payable to cover incurred expenses.

The Invalidity Pension Scheme provides coverage against invalidity or death from whatever cause. Qualifying criteria apply to this scheme, namely that a minimum of 24 contributions from the previous 40 month period should have been made prior to the incidence of invalidity. The full pension is set at 50%, plus 1% for every 12 contributions made in addition to the basic 24, subject to a maximum of 65% of earnings and a minimum pension of RM171.43 per month (as at January 1995). Similar additional benefits to those mentioned above are applicable under this scheme in the form of survivors’ pension (widow and orphan) and a funeral grant.

The Workmen’s Compensation Scheme is in effect an employer’s liability scheme. Based on the 1952 Workmen’s Compensation Ordinance, the scheme covers employment injury and occupational diseases. Those covered by SOCSO are excluded from the scheme,
which is applicable to both manual (unrestricted) and non-manual workers (subject to a wage limit), including foreign workers.  

The Old Age Pension Scheme (OAPS), which is a non-contributory retirement benefit, is available to those permanent officers who have completed not less than three years service. In line with the changes made through the establishment of the Pension Trust Fund, those public sector employees appointed on or after the 12 April 1991 can make a choice between the pension scheme or alternatively the EPF. Employer contributions to the EPF, made by the public sector, are returned to it once an employee joins the pensionable category or retires, or in the case of death. Employee’s personal contributions remain within the EPF scheme. On retirement public sector employees covered by the OAPS receive a gratuity and a pension up to a maximum of 50% of last drawn salary, the scheme also provides survivor and disability pensions. Due to the increasing burden of retirement benefits payable to public sector employees, the Malaysian government established the Pension Trust Fund (PTF) in 1991. A figure equivalent to 5% of the annual civil service bill is met by the PTF. Contributions to the PTF are made at a rate of 17.5% of the salary of pensionable employees by statutory and local authorities. Asher (1998) notes that as at the end of 1996 the total resources of the PTF stood at M$7,600 million.

The Armed Forces Fund (AFF) was established through the Armed Forces Act (1973) to provide superannuation benefits for members of the armed forces who are not eligible for pensions. Mid year calculations for 1996 saw the total resources of the AFF stand at RM3.587 billion (The Star, 1996). In addition to the AFF there exists the non-contributory Regular Armed Forces Pension Scheme, the National Defense Fund, a non-contributory additional assistance fund and the National Heroes Donation Trust Fund designed to assist the survivors of armed forces personnel who died on active service.

**The Employees Provident Fund**

The EPF, as is common with other national provident funds, is a publicly mandated savings plan with contributions shared between employers and employees. Originally set up by the former colonial power to cater for expatriate workers, this type of scheme is particularly common in Asia, notably India, Malaysia, Singapore and more recently in Thailand and Indonesia. The Malaysian EPF is the oldest such provident fund dating back to the EPF Act 1951 and currently operates under the 1991 Act, amended 1995. As expected, this type of scheme is fully funded and as such differs from other pay-as-you-go social insurance based scheme such as SOCSO. The main role of the EPF is to provide financial security to its members beyond retirement. However the nature of provident funds, reliant as they are on long term contributions, the relatively young age at which funds are accessible, the nature of this access and the sub-division of contributions into dedicated accounts calls into question the ability of the EPF to meet its central raison d’être.

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3 Unless otherwise noted, the description of the Malaysian schemes, excluding those of SOCSO and the EPF, draws upon Asher 1994, 1998.
All employees, irrespective of the size of their employer’s business, are covered by the scheme and as noted above both employees and employers contribute to the EPF at a current rate of 11% and 12% of wages respectively. Each member’s contributions are separated into three dedicated accounts, each with specific withdrawal requirements. At present, 60% of contributions are deposited into Account I and cannot be withdrawn until the member reaches age 55. At age 55, members can withdraw their funds either as a single lump sum, part lump sum with balance paid in periodical payments, periodical withdrawal or withdraw the dividend annually leaving the balance within the account. A further 30% is deposited in Account II and withdrawals are permitted for the purchase or building of a house, or the payment of housing loans. The balance of this account, that is total contributions plus compound interest, may be withdrawn at age 50. The final 10% is held in Account III and may only be withdrawn to meet the costs of defined critical medical conditions.

It should be noted that the framework of the fund is not rigid and is regularly amended and developed. For instance, with effect from November 1996 it has been possible for an individual aged below 55 years and with a balance in excess of RM55000 in Account I to invest up to 20% of their funds in approved unit trusts. Similarly, Dr Chan Chee Khoon from the Citizens’ Health Initiative, writing in the electronic version of Aliran Monthly, noted that on January 18 2000 it was announced that the EPF had entered into an agreement with the Life Insurers Association of Malaysia to enable “…the estimated five million active EPF members to use their savings [to] sign up for a health insurance scheme [beginning] this June. Under [this] scheme contributors can authorise EPF to pay the premiums from their Account III (health) annually…”.

As at the end of 1997 the EPF had 8.3 million members, and currently includes an estimated five million active contributors (The Star, 1999; Aliran, 2000). Asher (1998) illustrates that the coverage as measured by the ratio of active contributors to labour force as at end of 1995 stood at 49.5%. If we extrapolate from current figures using the same calculation, then we can show that the coverage has increased to approximately 55%. Thereby implying that 45% of the labour force, or just less than one in two workers does not enjoy the basic EPF coverage.

Under the 1991 Act, the EPF can only utilise approved investments. These include Malaysian Government Securities (MGS), debenture loans, money market instruments, equities and property. Investment strategies are determined by both the Investment Department and the Investment and Economic Research Department employing economists, fund managers and investment analysts. The Act stipulates that the EPF is required to invest at least 50% of its annual surplus funds in MGS, provided the total invested in government securities is not less than 70% of the total value of investments. However, due to favourable economic performances in the mid-1990s, resulting in a marked reduction in the issuing of new MGS, the government allowed the EPF to

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4 See bibliography for the full www citation; original parentheses.
5 Labour force figures obtained from Ministry of Human Resources.
diversify its range of investments. The Fund is restricted from investing more than 25% of its total funds in equities. As at the end of August 1998, the EPF investments in MGS amounted to approximately 47% of its total funds, compared to 73.6% in 1991. The former figure is expected to show an increase in the wake of the large budget deficit for 1999 of some RM16.6billion, part of which is to be met by the EPF. Investments in equities for the same periods stood at 19% and 11.9% respectively (The Star, 1999; Asher, 1998).

Dividends are calculated on a compound basis and are paid annually. The rate of dividend is determined by the EPF board, subject to approval from the Minister of Finance, under the EPF Act the dividend cannot be less than 2.5%. The real rate of return, that which has exceeded the increase in the consumer price index, has consistently been positive. That is, the rate of dividend has exceeded the rate of inflation for 43 out of its 47 years in existence form 1951 to 1998. Asher (1998) has noted that the shift in investments away from MGS to alternative investment destinations has affected the ability of the EPF to maintain its accustomed high rate of return. This is evidenced by a reduction in the level of dividend payable on balances from 8.0% to 7.5% in 1995 (Asher, 1998). Part of this shift away from MGS can be attributed to the role that the EPF has played in promoting home ownership. Asher comments that the 1996 amendment to the 1991 Act enabled the EPF not only to encourage private home ownership through access to funds in Account II, but to act as a source of finance for housing provision through the offices of its subsidiary MBSB.

Whilst it is relevant to highlight the developments of the EPF investment strategy, and the possible impact of this upon the level of dividend payments to its members, it should also be noted that the EPF maintains a high degree of efficiency in the management of accounts. A common criticism of national provident funds has been the often high administrative burden associated with such schemes. As far as the EPF is concerned however, this has been demonstrated not to be the case with operating costs amounting to less than 3% of total income (The Star 1999).

Discussion

There are a number of concerns regarding the efficacy of national provident funds in meeting their main aim, that being the provision of income for the elderly beyond retirement. In the first instance the ability of provident funds to provide an adequate income for the elderly is reliant on regular long-term contributions from individual account holders. Individual savings schemes are not equal to the task of providing adequate income for those workers forced to leave the labour force through ill health/disability, or the provision of social/child care in the case of women. The nature of the globalised economy, on which so much is pinned in the case of Malaysia, reduces the certainty of life long employment, as evidenced by the sharp economic downturn in 1997. The recent trend away from MGS will also affect the ability of the EPF to maintain its

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6 See Asher, 1998 (International Social Security Review, Vol. 51, 1/98, p13) for discussion of alternative use of EPF funds with regards to government led infrastructure projects and contributions to a fund established to reverse sharp declines on the KLSE following the economic downturn in 1997.
regularly high dividends, Asher (1998) argues that greater volatility of returns is to be expected.

Early withdrawals from individual member’s account will take their toll, not only on the final balance but also on the divided yield. In the case of the EPF early withdrawals from Accounts II and III for housing and health care, a possible 40% of all contributions and dividends, will result in lower returns (Williamson and Pampel, 1998). The relatively young age at which lump sum withdrawals can be made from the EPF (age 55) casts serious doubt on the ability of the accumulated balance lasting the required length of time. The increasing life expectancy combined with inexperience in individual private investments could leave the elderly vulnerable to an increased risk of poverty. The preference for a lump-sum payment, rather than a phased withdrawal scheme is evidenced by Beattie (1998), citing figures relating to the EPF he states that in 1995, only 120 persons opted for a phased withdrawal. Those opting for the lump sum found that their balances were inadequate to providing a life long income. In the majority of instances; “…the benefits were exhausted within three years of receipt at age 55.” (Beattie, 1998 p.70 citing a study carried out by Professor Mokhtar Abdullah for the EPF in 1995). In cases were lump sums are managed appropriately to give a longer lasting source of income, inflation will inevitably affect the level of income return. Therefore lump sum payments cannot be relied upon as an efficient means for the provision of income beyond retirement.

A greater degree of income guarantee lasting the required period is essential if the elderly are not to suffer the socially exclusive aspects of poverty. This is particularly the case in countries, such as Malaysia, in which the population is ageing. With an increased life expectancy, individual expenditure on health and social care is likely to increase. If the benefits accrued under life long saving through membership of the EPF are seen to be inadequate to the task of income provision in old age, it is highly probable that such benefits will be unable to cope with a possible increased expenditure on health care. The recent agreement between the EPF and the Life Insurers Association of Malaysia to set up a health insurance scheme under which premiums can be paid from Account III highlights this predicament. Premiums are graded according to age and range from RM30 annually at age 35 to RM200 at age 65-70 years (Chan Chee Khoon, 2000). As noted above there are concerns that traditional familial support will be eroded due to geographical migration, thereby placing a greater emphasis on self-reliance for the elderly left behind in often rural locations.

Concluding remarks

Providing adequate income beyond retirement and thereby lessening the socially exclusive aspects of poverty is not simply a question of individual versus state provision. Improving the current schemes and supplementing individual provision with a social insurance based pension would provide a greater guarantee of acceptable living standards beyond retirement. This paper argues that the amelioration of the negative effects of poverty in old age can be achieved through the instigation of twin reforms. In the first instance the introduction of a social insurance based pension, similar in form to that
currently operated under SOCSO, would ensure at the very least access to a basic minimum level of income. Secondly, amendments to the current structure of the EPF would enable the scheme to act as a supplement to the basic pension. The EPF, as an individual savings scheme, is designed to offer some social protection in old age through the provision of an adequate income. To fulfil this criteria greater emphasis needs to be placed on its core activity rather than expanding its remit to cover the costs of health and social care. Access to funds with regards to retirement ages will need to be addressed. The withdrawal of a lump sum at age 55 is no guarantee of income for the remaining life time. The need to introduce periodical benefits has been acknowledged by Malaysia (Beattie, 1998) although given the data presented above, a degree of compulsion with attendant benefits may be required.

At present the low paid, those forced to leave the labour force early through ill health or disability, or women taking a career break to fulfil social care obligations are placed at a disadvantage in a scheme which depends upon a high level of long term contributions. Women in particular are likely to suffer the adverse effects of poverty in old age due in part to earlier retirement combined with greater life expectancy. An increase in the level of contributions would go some way towards addressing this problem for the low paid. This could be achieved through the introduction of a minimum wage, thereby going some way towards guaranteeing a defined level of saving. The Malaysian Trades Union Congress, which represents approximately 500,000 workers, has repeatedly called for the establishment of a minimum wage and is currently petitioning the government to implement legislation introducing a guaranteed minimum wage of RM1200 by the end of this year (Malaysiakini, 2000).

An increase in the mandatory retirement age and thus access to Account I would at the very least increase the period of contribution. This could be made more acceptable if carried out incrementally over an extended period of time. This paper is not assuming that those who reach age 55 retire from work altogether, research proves this not to be the case (Chen and Jones, 1989). However, a government led initiative towards flexible retirement could facilitate the continued employment of older workers and lessen the incidence of poverty and social exclusion experienced by the elderly.

Demographic, social and economic changes in Malaysia will increase the need for a more adequate system of income provision for the elderly. Reliance on traditional means of support combined with individual savings may well lead to an increase of the incidence of poverty and social exclusion among the elderly. To prevent such a scenario, action needs to be taken to ensure that all workers are covered by a system that offers a minimum guaranteed income through periodical payments. However, any such reforms are dependent upon the political will of government to address such concerns. In the current economic climate and with the ability of the EPF to contribute to the cost of state initiated infrastructure projects through low cost loans, the required political will appears, at present, to be absent.
Bibliography


