CHAPTER 3: SOCIAL SECURITY IN MALAYSIA

3.1 Introduction

There are no better social security programmes, which can be applicable to any country. Basically, several social security programmes in Malaysia are implemented, developed and expanded by reference to the extent and importance of the problem of insecurity. In this chapter, I intend to show how EPF is developed on the basis of its own particular social, political and economic environment.

3.2 Social Security Measures Operating in Malaysia

In Malaysia, pension and provident fund is an important social security scheme, which provides a significant source of funds to finance economic development. Pension and provident fund plays a significant role in resource mobilization and allocation. Generally, we can categorize these pension and provident funds into nine types, comprising the Employees Provident Fund (EPF), the Social Security Organization (SOCSO), the Armed Forces Fund (AFF), the Pension Trust Fund (KWAP) and five other private pension funds (PPFs). The total resources continued to grow in tandem with the increase in the number of contributors and improving contributions due to the economic recovery.

3.2.1 Employees Provident Fund (EPF)

EPF is under the legislation of Employees Provident Act 1951 administered by the EPF Board, a statutory body. It is based on a provident fund principle, which is also a saving scheme.

The primary objective is to provide financial protection to its members and their beneficiaries under the contingencies of old age, disability and death. Essentially a compulsory savings scheme, employees and employers are required to make the mandatory monthly contributions to the fund where they are credited to a separate account maintained for each worker, on which **compound interest** is paid.

All amount of EPF contribution was saved with the fund until the contributors satisfy the conditions of withdrawal. The liquidity of the contributions and the deferred payments of benefits allow the fund to invest in long-term assets. A detail description on EPF will be enclosed in the latter part of this research.

3.2.2 Social Security Organization (SOCSO)

SOCSO was established under the Employees Social Security Act 1969, administered by SOCSO Board, a statutory body, to provide security benefits to workers. There is a social insurance principle of "pooling" of resources and sharing of risks. The coverage is for industries employing 5 or more employees who are earning RM500 or less per month. "Once a member always a member". Generally, there are two types of benefits covered by SOCSO: -

1) **Employment Injury**

   i) Temporary disablement benefit

   ii) Permanent disablement benefit

   iii) Dependants' benefit

   iv) Constant attendance allowance

   v) Funeral benefit

vi) Medical benefit including prosthetics benefit

vii) Physical and vocational rehabilitation

2) **Invalidity Pension Schemes**

i) Invalidity pension

ii) Invalidity of grant

iii) Constant attendance allowance

iv) Medical benefit including prosthetics benefit

v) Physical and vocational rehabilitation

3.2.3 Armed Forces Fund (AFF)

AFF was established under the Armed Forces Provident Fund Board, and based on the provident fund principle as saving scheme. The coverage included servicemen who are enlisted on or after August 1972 and who are not eligible for pensions. Cash withdrawal only allowed:-

i) on the death of the contributor;

ii) one month after the contributor is discharged or retired from service; and

iii) on the contributor attaining the age of 55 years.

During the period under review, AFF invested largely in trust funds.

3.2.4 Pension Trust Fund (KWAP)

KWAP was established under the Pension Trust Fund Act 1991 to assume the Government's obligation payments of the public sector. Total resources mobilised by KWAP rose on account of a rise in the funds contributed by the Federal and state governments as well as local authorities and statutory bodies. [Source: *Economic Report, 2000/2001*, Ministry of Finance, Malaysia] The investment portfolio of KWAP basically was in deposits and money market instruments, equity and trusts fund as well as corporate loans and bonds.

3.2.5 Private Provident and Pension Funds (PPFs)

The five private PPFs included Malaysia Estates Staff Provident Fund, MAS Malaysia Provident Fund, SECSO Employees Provident Fund, Petronas Retirement Benefit Scheme and Jendarata-Bernam Provident Fund.

Table 3.1 Provident and Pension Funds in Malaysia (RM million) (end-June)

	Total Resources		Malaysian Government Securities		Net Contribution	
	1999	2000^{p}	1999	2000^{p}	1999	2000^{p}
EPF	151,576	172,507	46,987	58,259	3,911	4,792
SOCSO	7,034	8,232	2,489	3,242	233	208
AFF	4,683	4,836	5	0	(109)	(181)
KWAP	13,563	15,126	0	0	3,956	5,455
Private PPFs	857	913	222	114	(1.7)	(11)
Total	**177,713**	**201,614**	**49,703**	**61,615**	**7,989**	**10,263**

^{p} Preliminary data.

Figures in parentheses indicate net withdrawals.

[Source: *Economic Report, 2000/2001*, Ministry of Finance, Malaysia]

Obviously, EPF is the most important pension and provident fund, which means EPF is a crucial social security scheme in Malaysia. Preliminary data of 2000 shows that the EPF accounted for 85.6% of total resources of pension and provident funds at end-June 2000.

3.3 Methods of Social Security Protection in Malaysia

In general, the four main methods of providing organized social security protection in Malaysia are: [Karto, D. (1986)]

3.3.1 Employer's Liability Scheme

Employer's liability scheme covers the employment injury compensation under the **Workmen's Compensation Ordinance 1952**; and sickness and maternity benefits under the **Employment Ordinance 1955**. These schemes are entirely the employers' responsibility in that they are legally bound to meet the cost and to give the benefits directly to those of their workers who are "qualify".

3.3.2 Social Insurance System

Social insurance system covers the employment injury and invalidity benefits under the **Employees' Social Security Act 1969**. These schemes are based on the principle of the pooling risks and finances. A central fund is set up in order to pay the benefits in the form of periodical payments on an earning-related basis.

3.3.3 Statutory Provident Fund

Statutory provident fund includes benefits for the old age under the **Employee Provident Fund (EPF) Act 1951** and the old age benefit scheme under the **Armed Forces Fund Act 1973.** These schemes consist of individual and entirely separate accounts into which the contributions of the employee and his employer are accumulated to earn interest until withdrawn to meet his financial needs.

3.3.4 Non-Contributory Scheme

An example for this non-contributory scheme is the old age pension scheme under the **Government Pension Ordinance 1951**, which affords income protection out of public funds.

3.4 Employees Provident Fund (EPF) in Malaysia

EPF is a mandatory defined-contribution type of social security protections, which use national social security mechanisms, with both record-keeping, and investment functions undertaken centrally by the statutory board.

For simplicity, we focus on **Employees Provident Fund (EPF)** as representing a **Pay-As-You-Go (PAYG)** social security system. Specifically, it is a savings scheme where individual or the contributor provides for his own retirement. EPF is not financed primarily out of general revenues of the government, but are financed entirely or meagerly by special contribution from employers and employees.

3.4.1 Background Of Establishment

The Employees Provident Fund (EPF) was established on 1 October 1951 under the EPF Ordinance 1951 which was subsequently known as the EPF

Act 1951. The EPF Act 1951 has, since then, been replaced by the **EPF Act 1991** in June 1991.

The EPF is a statutory body and a **trustee fund**, which was set up for the purpose of **providing retirement benefits** to its members to enable them to lead a comfortable retired-life. The main role of EPF is to provide **financial security** to its members, especially after retirement, through a **compulsory savings scheme**.

The EPF is under the jurisdiction of a Board, which consists of 20 members who are appointed by the **Minister of Finance**. The EPF Board is made up of a Chairman, a Deputy Chairman and 18 other members which comprise of: -

a. 5 Government Representatives

b. 5 Employer Representatives

c. 5 Employee Representatives

d. 3 Professional Representatives

The EPF Board is responsible for formulating EPF policies and to ensure implementation of these policies. Since EPF is a compulsory savings scheme, it is the responsibility of the government and EPF Board Members to ensure that EPF provides good and fair services for the contributors. Apart from the Board, the EPF also has an **Investment Panel**, which is responsible to formulate EPF investment policies. The members of the Investment Panel are also appointed by the Minister of Finance. The Panel is made up of a Chairman, a representative of the Governor of Bank Negara Malaysia, a representative from the Ministry of Finance and three others who are experts in financial, business and investment related matters.

Under the EPF Act, the employer and employee are required to contribute to EPF based on the rate of contribution set by the EPF Act. The EPF headquarter is situated in the EPF building in Kuala Lumpur. Apart from the Headquarters, the EPF has 14 State Offices and 33 Local Offices throughout the country. The EPF is a national social security organization operating through a Provident Fund scheme in Malaysia. The primary members of EPF are the private and non-pensionable public sector employees.

3.4.2 Functions of the EPF

i) To receive and recover contributions

Every employer is liable to contribute on behalf of every employee who is employed under a contract of service or apprenticeship. Every month, the employer deducts **11% of the employee's wages** and together with the **employer's share of 12%** pays to the EPF by way of Form A before or on the 21st day of the following month. Employers and employees are, however, allowed to elect to contribute at rates higher than the statutory rates.

ii) To invest all EPF moneys (members' savings)

EPF funds are invested in: -

a. *Long term investments:-*

- Malaysian / Federal Government Securities inclusive of advanced deposits with Bank Negara Malaysia
- Foreign Securities
- Debenture Loans
- Loans that are guaranteed by the Government

b. *Equities*

c. *Short term investments:-*

- Time Deposits
- Non Negotiable Certificates of Deposits
- Other short term deposits.

iii) **To return members' savings to them or their beneficiaries (next-of-kin) through the process of withdrawals savings.**

The saving of an EPF member is returned to the member under the following EPF withdrawal schemes.

a. ***Age 55 Years Retirement Withdrawal Scheme.***

This Scheme consists of: -

i. **Lump Sum** Withdrawal Scheme

ii. **Periodical** Payment Withdrawal Scheme

iii. **Annual Dividend** Withdrawal Scheme

iv. **Part Lump Sum** Payment and Balance in Periodical Payment Withdrawal Scheme.

b. ***Housing Withdrawal Scheme*** which consists of:-

i. Withdrawal to buy or build a house; and

ii. Withdrawal to reduce or settle the balance of housing loan.

c. *Age 50 Years Withdrawal Scheme*

d. *Medical Withdrawal Scheme*

e. *Physical or Mental Incapacitation Withdrawal Scheme*

f. *Leaving Country Withdrawal Scheme*

g. *Death Withdrawal Scheme* - The member's savings will be returned to his next-of-kin or beneficiaries

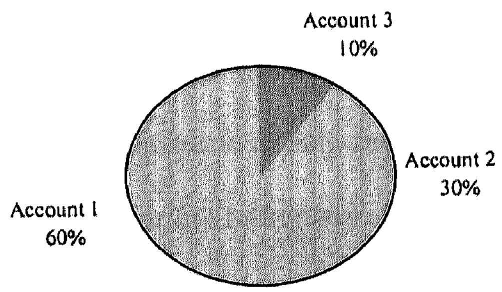
h. *Member's Savings Investment Scheme*

Apart from paying the savings back to the member or his next-of-kin in case of a member's death, EPF also provides an **additional benefit** to the deceased member's beneficiaries and to members who are incapacitated from further employment. This additional benefit is not part of the member's savings. It is from the **EPF's revenue** and is paid out to the members or their beneficiaries as a **sympathetic gesture** on the part of the EPF. The benefits are death benefit and incapacitation benefit.

3.5 Type of EPF Members' Accounts

With effect from **1 November 1994**, every EPF member will be provided with three accounts, that is, Account I, Account II and Account III. With effect from this date, all contributions with the fund together with subsequent contributions will be divided into three accounts according to the following percentage:

Chart 3.1 EPF Members' Accounts



[Source: http://www.yellowpages.com.my/financial/epf.htm]

60% of contributions for Account 1 (for retirement purposes at age 55)

A major portion of the EPF contributions, that is 60% of it will be kept in Account I. The intention of keeping the 60% of the member's savings is for retirement which is in line with the EPF's primary objective, that is to ensure that every member has sufficient cash savings for his retirement. These savings cannot be withdrawn before the member attains 55 years of age unless if he dies, leaves Malaysia permanently (for non-Malaysians) or is incapacitated from further employment. With effect from 1 November 1996 a portion of the member's savings in this account can be withdrawn for investment with Fund Managers approved by the Ministry of Finance. When a member attains 55 years of age, he can withdraw his savings in Account I together with the balance of savings in Account II and Account III (if any). It has recently been announced that contributors below the age of 55 years with more than RM50,000.00 under Account I will be allowed to invest up to 20% of their funds in unit trusts beginning from 1997.

30% of contributions for Account 2 (for housing and withdrawal at age 50)

Savings in this account comprise of 30% of an EPF member's savings. The purpose of having this account is to help members to own a house and to make early preparations for his retirement. Under the housing withdrawal scheme, a member can withdraw his savings once for buying or building a house or for purposes of reducing a housing mortgage on satisfying the prescribed conditions. Withdrawal to reduce or settle the balance of the housing loan is allowed once every five years from the date of the previous withdrawal until the member attains 55 years of age. A member can also use part of the savings to plan his retirement by withdrawing the savings from this account when he attains 50 years of age but before age 55 years, if there is still a balance of savings in this account.

<u>10% of contributions for Account 3 (for health and medical costs)</u>

The savings in Account III can be used to pay for **the medical expenses of critical illnesses.** This facility is provided to help members whose medical expenses are not covered or is partly covered by their employers. This medical treatment is not only limited to the member but also to the member's spouse, children, parents and siblings.

Source: Employee Provident Fund WebPages (See Bibliography)

3.6 Services provided by the EPF to Members

Presently, apart from registering all employees as members, EPF provides a wide range of services to its members. From day-to-day operation, EPF handles all complaints and inquiries from the public, and provides counter services to members and employers. This includes processing withdrawal of member's savings when a member fulfills the withdrawal conditions, and enforcing the law on employers who do not contribute. Occasionally, EPF has produced several leaflets and guide-books for this purpose. Statement of Accounts will be sent automatically to the members if they are currently contributing to EPF. Sometimes, EPF is also responsible in conducting courses on preparation for retirement for future retirees.