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The Malaysian Government Pension Scheme : Whither Its Future Direction?

Lee Kum Chee

ABSTRACT

Public sector employees in Malaysia are covered by the Government pension scheme. Benefits provided by the scheme include retirement benefits, survivor benefits and disability benefits. The financing of the scheme by the Government is a cause of concern in view of the large absolute amount of expenditure on pension benefits and the rising trend of such expenditures. This paper examines the financing of the pension scheme and the causes of its increasing costs as well as alternative options to the current system.

ABSTRAK

Kakitangan sektor awam di Malaysia adalah diliputi oleh skema pencen kerajaan. Faedah yang disediakan oleh skema itu termasuk faedah persaraan, faedah pewaris dan faedah keupayaan. Pembiayaan kos skema itu oleh kerajaan merupakan suatu isu memandangkan jumlah perbelanjaan yang besar untuk faedah pencen dan kenaikan dalam arah aliran perbelanjaan itu. Kertas ini mengkaji pembiayaan skem pencen kerajaan Malaysia dan faktor-faktor yang menyebabkan kenaikan kos itu serta opsyen lain untuk sistem yang sedia ada.

INTRODUCTION

In Malaysia, the legislation provides for a pension scheme which is financed and managed by the Government as an employer for the protection of its employees against various contingencies. Pension benefits form part of their conditions of service in the public sector. The Government pension scheme covers employees in the public sector who are on pensionable status. Employees in the private sector are not included in this scheme. They and their employers are instead required to contribute to the employees' provident fund or the social security organisation. In the case of payments of retirement or disability benefits and pensions in the private sector, the public purse is not affected as such payments come from the monthly wage deductions of employees and matching contributions from employers.

Public sector employees include those employed directly by the government, statutory bodies and local authorities. Pensionable employees in the public sector are entitled to an array of benefits that comprise: (1) retirement benefits (a monthly pension and a gratuity as well as a cash award for accumulated leave), (2) survivors' benefits (derivative pension and derivative gratuity as well as dependant's pension), and (3) disability pension. For these benefits, the amount paid is essentially a specified proportion of basic salary. Thus the Government pension scheme is a defined benefit scheme.

Retirement benefits represent the most important benefits provided by the Government pension scheme both in terms of the quantum of monetary award and the purpose of the scheme, which is the provision of income during retirement. In order to ensure some form of equity in retirement benefits, the computation of retirement benefits is based on formulae which vary the amount of benefit received with the length of pensionable service credited to the retiring employee and his last drawn salary. Combined with the pension factor, the formula effectively sets a maximum rate of monthly pension for individuals who retire after 25 years' service, and a proportionately reduced benefit for those retiring with a shorter period of service. The payment of a gratuity in the form of a substantial lump sum amount, incorporates flexibility in terms of financial planning as it enables retirees to meet urgent needs, such as investing in a business, settling a housing loan, or purchasing a house. Employees also receive a lump sum cash award for accumulated leave (Malaysia 1980a).

The payment of benefits to only those who retire under specified conditions reflects an important principle of the pension scheme. The individual should have experienced a substantial reduction of income or completely withdrawn from public service. This ensures that the recipient does not enjoy benefits from the scheme as well as salaries concurrently.

Although the Government pension scheme is created primarily for retirement, it recognises the importance of providing survivor benefits which are of immediate concern for the welfare of employees' families. The aim is to compensate dependants for the permanent loss of financial support. Eligible dependants include the surviving spouse and minor children (Malaysia 1980a).

Disability pension is granted where an officer retires due to accidents or diseases caused by his job or due to a travel accident (Malaysia, 1980b). The amount of disability pension depends on the degree of impairment.

In order to receive pension benefits, employees must have attained the compulsory retirement age of 55 years, the optional retirement age of 50 years for men and 45 years for women, or must have been medically certified unfit for work as a result of accidents or disease. The individual must have at least ten years' service in the public sector, including a probationary period of three years before qualifying for a pension.

The purpose of this paper is to discuss the problem of the rising expenditure on pension benefits in the context of the current structure of the Government pension scheme, the means of financing it, and the factors leading to the higher expenditure. Suggestions for reforms are then made in the concluding remarks.

FINANCING THE GOVERNMENT PENSION SCHEME

In terms of financing, the Government pension scheme, like salaries of public sector employees, is basically funded by the general revenue of the Government. It thus represents a substantial operating cost. Indeed the difficulties faced in the recession years of 1985-86 led to the proposal of the Government to abolish the scheme as a move to reduce the financial pressure on the general budget. This was however met with objections by public sector employees and representatives of trade unions as it would mean the loss of an important source of old-age income. The proposal was hence later withdrawn. Nevertheless, a basic issue that remains is that of financing the rising cost of the pension scheme. The problems of financial viability are compounded by the inherent structure of the pension scheme which at present subscribes to merely partial contributions from statutory bodies and local authorities.

FINANCING FROM GENERAL REVENUE

Pension benefits in the public sector represent a reward for services rendered to the Government in its role as an employer and its payment has always been the prerogative of the Government (Malaysia 1951). The pension scheme is essentially financed by the general revenue of the Government, with contributions coming partly from statutory bodies and local authorities, which are required to contribute 17 1/2 percent of their employees' salaries with 10 years' service. Up to 1991 all contributions of statutory bodies and local authorities were channelled into the Consolidated Fund as revenue and all pension benefits were paid out of this Fund without any conscious effort to balance annual income and expenditures. This precarious financial situation manifested itself during the recession years of the country.

Thus the Government pension scheme was not funded up to 1991 for several reasons. First, since pre-independence times of the country, the pension scheme for public sector employees has traditionally been financed from general taxation. Second, the programme is expected to continue indefinitely and will not be easily terminated as it is a law enacted in Parliament and protected by the Federal Constitution of Malaysia. Thus the solvency of the scheme is guaranteed by the Government. Third, the taxing and borrowing powers of the Federal Government can be used to raise additional revenues if the scheme faces financing problems (Rejda 1988). Fourth, being mainly non-contributory in nature there are in fact no financial contributions to be accumulated from employees. Moreover, coverage is extensive as the scheme covers all current and future employees in the civil service as well as statutory bodies and local authorities.

In 1991 a major initial step was taken to rectify the situation by ensuring the financial viability of the pension scheme. A pension fund was established with an initial contribution of $500 million from the Government. The function of the fund is to collect, invest and manage contributions of the Government as well as statutory bodies and local authorities, and returns from any investment of the fund (Malaysia 1991). Its ultimate goal is to pay all forms of pension benefits to current and future pensioners without incurring any additional costs to the Government. Until it is self-financing, benefits would continue to be paid from current revenue.

PARTIAL NON-CONTRIBUTORY NATURE

Until employees in the public sector are placed on the pension scheme, contributions are made to the Employees Provident Fund at the rate of 10 percent of their salaries by employees and 12 percent by employers. Once employees become pensionable, both parties stop contributing to the Employees Provident Fund. Contributions of employees would be returned to them on their retirement while those of employers would be retained by them accordingly. This means that the pension scheme is fully non-contributory for both parties for the initial period of employees' service. The non-contributory nature of the scheme still applies to employees of the public sector after they are pensionable. For statutory bodies and local authorities, they contribute 17 1/2 of their employees' salaries from the period the employees are pensionable until their retirement. Thus the pension scheme is partially non-contributory for statutory bodies and local authorities as long as their employees are not yet pensionable. It is totally non-contributory for employees.

A pension scheme without any contributions at all from employees and only partial contributions from employers throughout the entire period of their service would be bound to encounter difficulties in accumulating financial resources for investment if it is required to yield sufficient returns to pay retirement benefits. Indeed converting the scheme to a fully contributory one constitutes a vital step to making the fund totally financially viable.

FINANCIAL VIABILITY

Since the Government pension scheme provides an important source of income for public sector employees in the event of any contingency, it is important that the scheme be financially viable. Indeed it must be properly financed if it is to continue paying the expected benefits as stipulated in the pension laws.

Besides its structure, the present financial viability of the government pension scheme also depends on economic and demographic factors. Economic growth affects revenue and hence taxability of the Government. Inflation would create a pressure on the Government as an employer to raise salary levels in the public sector, which in turn would increase the pensions of future retirees. Demographic factors, such as life expectancy and mortality rates have an impact on the number of beneficiaries in relation to the size of the working population. The size of the public sector is also important as it directly determines the size of pension expenditures.

Built-in resiliency against these factors could be developed by accelerating the growth of the pension fund and pursuing an aggressive diversified investment policy in both the private and public sectors, domestically as well as internationally.

TRENDS OF BENEFIT EXPENDITURE

Table 1 shows the annual amount and growth rate of expenditure on pensions and gratuities for 1971-1995. Over a period of ten years (1971-1980) pension expenditure increased more than six-fold from RM87.3 to RM552.7 million while over the next decade (1981-1990) the amount doubled to RM1154 million in 1990 and further doubling again to RM2755 million in 1995. Figure 1 shows the rising trend of pension expenditure for the 25-year period. This trend is also reflected in Figure 2 which shows the cost of pension benefits as a percentage of GNP had increased gradually but steadily over this period. For example, it increased from 0.7 percent of GNP in 1971 to 1.0 percent of GNP in 1980 and then to more than 1.3 percent in 1995. It can be deduced that the upward trend would most likely continue in the coming years.

Each salary revision causes a sharp increase in expenditure on pensions and gratuities. For example, an additional expenditure of about RM93 million was incurred in 1980 while another RM29 million was paid in 1990 to finance pension arrears as a result of a salary revision in the respective years. Furthermore, in 1990 the first allocation of RM500 million was made to the Pension Fund.

The increases depicted above raises the question of whether they could continue to be financed by the Government in terms of its current revenue. The rates of growth of pension payment for the period 1971-1995 fluctuated between 2.7 percent and 83.3 percent, as shown in Table 1. Comparing these with the annual growth rates of GNP and current revenue in Table 2, it can be seen that the growth rate of pension expenditure outpaced that of general revenue and GNP in several years. Indeed if left unchecked the persistent upward trend of pension expenditure raises the problem of ensuring the long-term survival of the pension scheme.

FIGURE 1. Pension expenditure 1971-1995

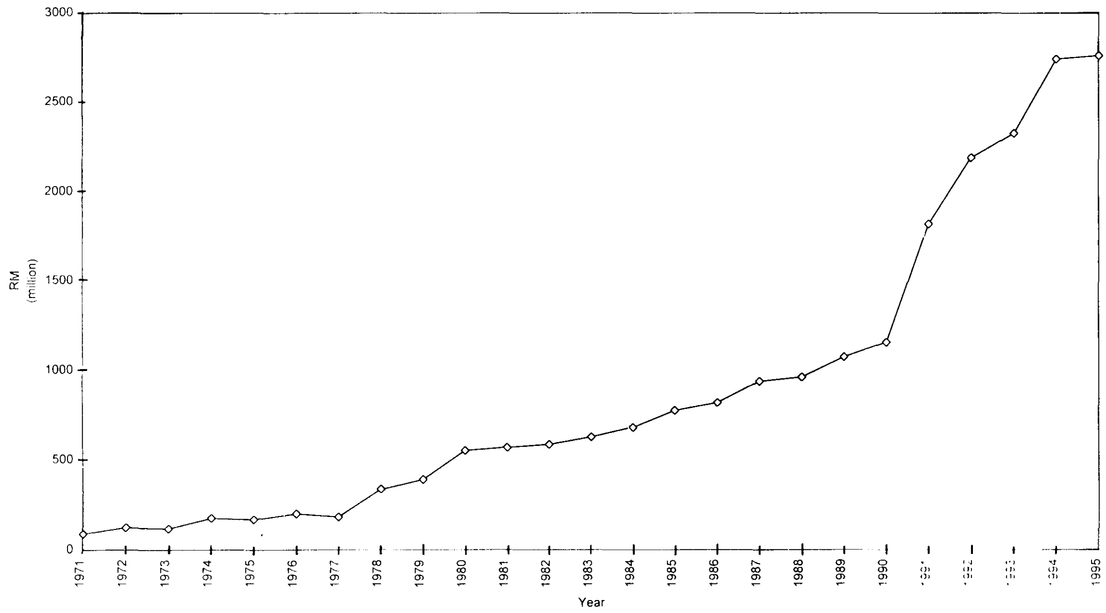

FIGURE 2. Pension cost as % of GNP

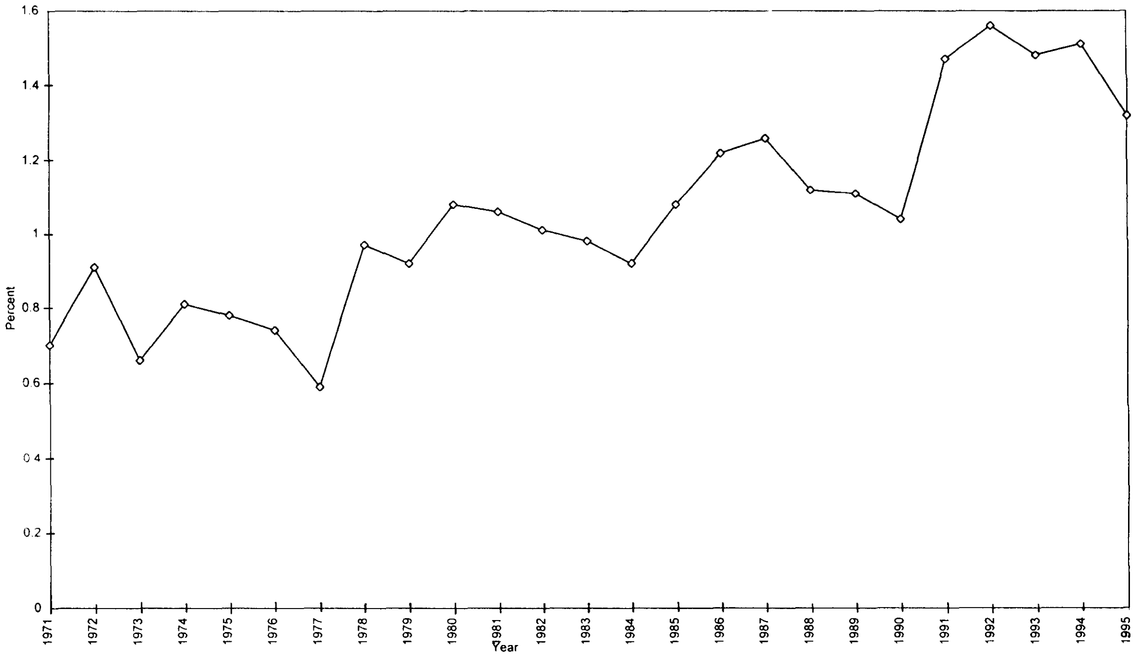

TABLE 1: Expenditure on pensions and gratuities 1971-1995

Year	Expenditures (RM million)	Growth Rate (%)
1971	87.3	–
1972	124.5	42.6
1973	118.6	-0.5
1974	176.8	49.1
1975	168.6	-4.6
1976	201.9	19.8
1977	185.1	-8.3
1978	339.3	83.3
1979	393.3	15.9
1980	552.7	40.5
1981	571.5	3.4
1982	587.0	2.7
1983	629.0	7.2
1984	681.0	8.3
1985	775.0	13.8
1986	817.0	5.4
1987	938.0	14.8
1988	961.0	2.5
1989	1073.0	11.7
1990	1154.0	7.5
1991	1815.0	57.3
1992	2183.0	20.3
1993	2320.0	6.3
1994	2737.0	18.0
1995	2755.0	0.66

Source: Economic Reports, Malaysia

FACTORS THAT CONTRIBUTE TO THE RISING COST OF THE GOVERNMENT PENSION SCHEME

The increasing cost of the Government pension scheme could be attributed to several factors. They include: (1) the benefit structure, (2) the salary component of the benefit formulae, (3) implementation of the Pensions Adjustment Act, 1980, (4) large size of the public sector, (5) increase in life expectancy, (6) increase in number of pensioners demanding benefits, (7) retirement provisions.

Table 2. Growth rates of GNP and government current revenue

Year	Expenditures of GNP (%)	Growth Rate Current Revenue (%)
1971	–	–
1972	9.1	20.8
1973	32.4	16.4
1974	21.0	41.0
1975	-1.2	6.8
1976	99.1	20.3
1977	16.1	26.0
1978	8.3	13.9
1979	-17.9	18.8
1980	15.9	32.6
1981	8.2	13.5
1982	7.4	5.6
1983	9.8	11.5
1984	13.2	11.8
1985	-3.0	1.5
1986	-7.1	-7.6
1987	11.8	-7.0
1988	14.9	21.1
1989	12.7	15.0
1990	14.6	16.8
1991	11.5	15.4
1992	11.9	15.3
1993	11.7	6.2
1994	15.2	18.6
1995	15.1	3.1

Source: Economic Reports, Malaysia

THE BENEFIT STRUCTURE

Pension expenditure is directly related to the structure and level of benefits provided as they determine the amount that each pensioner is paid. Thus an analysis of the problem of rising pension expenditure must take into account the features of the Government pension scheme. It has been said that the pension scheme of the Malaysian public sector is "one of the best in the world" because of its comprehensive structure that covers a wide range of contingencies, including old age, disability, occupational disease, death and travel accident. Besides paying monthly pension for the rest of a pensioner's life, the gratuity paid on retirement could be a substantial sum, particularly for employees on higher salary scales, as no maximum is imposed on the amount that one is eligible for.

The pension and gratuity payable are based on the following formulae:

Pension 1/600 x number of months of service x last drawn salary.

Gratuity 1/20 x number of months of service x last drawn salary.

The amount of monthly pension paid to an employee is subject to a maximum of one-half of the individual's last drawn salary. Thus the limit imposed by the formula is 300 months or 25 years. Employees must work until the optional retirement age of 50 years for men or 45 years for women or the compulsory retirement age of 55 years before they are eligible to receive pension benefits. If they resign before reaching the retirement age or are dismissed, then their pensions are forfeited.

A recent development was the payment of gratuities and cash benefits in lieu of annual leave to those who opt to retire at the age of 40 years. Such ad hoc improvements in the benefit structure through various amendments of the pension laws have also partly resulted in increasing pension expenditure. This reflects the attempt of the Government to accommodate the changing needs of public sector employees. Maintaining a dynamic and an attractive scheme must include efforts to develop it into one that is highly resilient to external forces.

THE SALARY COMPONENT OF THE BENEFIT FORMULAE

Inflation has a direct effect on the cost of the Government pension scheme as it leads to demands for higher salaries, which in turn influence the total amount of pension benefits. Benefits are computed based on predetermined formulae as set out in the rules and regulations of the Government pension scheme. The salary component of the formulae, that is, the salary drawn by an officer in his last confirmed appointment immediately prior to retirement (the last drawn salary), implies that future retirement benefits of the currently employed would increase whenever their salary increases. These increases in salary are subject to the seniority and job performance of an individual as well as across-the-board revisions as mandated by the Salary Reports adopted by the Government from time to time. Salary increases are important for current employees as they would raise the last drawn salary and hence the quantum of benefits drawn by a retiring officer.

In the Malaysian public service, salary increases are effected through the various Salary Reports recommended by the Committees that are commissioned by the Government to examine the salaries and terms and conditions of service for its employees. They are usually conducted on an ad hoc basis in response to rises in the cost of living. The payment of salary increments and arrears associated with the salary revisions are as follows: 8.4% of the total wage bill borne by the public sector in 1977, 10.9% in 1980, 7% in 1989 and 4.5% in 1991. These salary increases in turn generated increases in pension expenditures as new retirees are paid higher pensions and existing pensioners are paid their pension arrears. Their long-term effect on the financial obligation of the Government is obvious as they lead to a corresponding rise in pension costs of current as well as future retirees.

IMPLEMENTATION OF THE PENSIONS ADJUSTMENT ACT, 1980

Recognition is given to the principle of compensating existing pensioners to take into account inflation and rising earnings of the currently employed. With the implementation of the Pensions Adjustment Act, 1980, any revisions of existing salary schemes in the public sector means that corresponding revisions would be made to pension benefits of current pensioners. The adjustments are calculated based on the last drawn salary at the equivalent salary grades that the pensioners would have been on had they not retired. This reflects the efforts of the Government to protect the purchasing power of pensioners' income and to ensure them an opportunity to share in the fruits of any economic growth enjoyed by those still working.

However, the large numbers of pensioners, estimated as around 230,000 at 1992, means that any increases in benefits per head as a result of salary revisions would entail a large amount of expenditure. This is difficult to be shouldered by Government revenue if its growth is slower than that of pension expenditure.

THE LARGE SIZE OF THE PUBLIC SECTOR

The financial situation of the pension scheme is largely affected by the size of the public sector employment which in turns affects the future number of retirees. Total public sector employment has expanded tremendously over the past 20 years, from merely 420,000 in 1971 to 692,000 in 1980 and subsequently to 850,000 in 1990. With a strength of 859,000 staff by 1992 or 12.8 percent of the total work force of 6,685,000 million (Malaysia 1993), the Government is the largest employer in the country.

The rapid expansion of public sector employment resulted from several factors. These included the implementation of the Harun Report which brought 60,000 employees of statutory bodies and local authorities under the coverage of the Government pension scheme in 1976 and an intensive programme, *Operasi Isi Penuh*, carried out to fill all vacant positions as a move to reinforce the Government administration machinery, resulting in the recruitment of about 135,000 members in 1980 and 1981. By reason of the sheer size of its membership, the pension scheme cannot simply depend solely on Government revenue in the long run.

The privatisation programme introduced by the government in 1983 and subsequently intensified in later years, resulted in the scaling down of the average growth rates of public sector employment to between 0.9 and 1 percent in the early 1980s, as compared to between 5.4 and 5.6 percent in the early 1970s. By the 1990s the growth rates of the size of the public sector have been reduced to between 0.35 and 0.64 percent. Such minimal growth rates would in turn limit the expansion in the number of pensioners when these cohorts retire in the future.

INCREASE IN LIFE EXPECTANCY

There has been a considerable improvement in life expectancy of the population of Malaysia. Table 3 shows that average life expectancy at birth of males has increased from 55.8 years in 1957 to 69.5 years in 1995, representing an improvement of 13.7 years, while that of females has risen from 58.2 years to 74.1 years, a lengthening of 15.9 years.

The rising average number of years remaining for persons of retirement age represents an additional factor to be reckoned with in examining expenditure on pension benefits. Table 4 shows the average life expectancy from the age of 40 years, the permissible optional retirement age for pension payment, has been gradually rising since 1970. As 55 years is the compulsory retirement age for officers in the public service, males who retire at that age in 1995 would receive benefits for an average duration of 20.1 years and females for 22.7 years. The average period of pension payment is even longer for those who opt to retire earlier. Payment of pension to male officers on optional retirement would start on attaining the

TABLE 3. Life expectancy at birth by sex, Peninsular Malaysia

Year	Life Expectancy (years) Male	Female
1957	55.8	58.2
1970	61.6	65.6
1975	64.3	68.7
1980	66.4	70.5
1985	67.7	72.4
1990	68.9	73.5
1995	69.5	74.1

Source: Malaysia, Department of Statistics

TABLE 4. Life expectancy at different ages by sex, Peninsular Malaysia

Age	Life Expectancy (years) 1970		1985		1995	
	Male	Female	Male	Female	Male	Female
40	29.6	33.2	31.8	35.3	32.9	36.3
45	25.3	28.9	27.3	30.7	28.4	31.6
50	21.3	24.7	23.1	26.2	24.1	27.1
55	17.7	20.9	19.2	22.0	20.1	22.7
60	14.4	17.3	15.6	18.0	16.4	18.5
65	11.8	14.3	12.6	14.5	13.1	14.7
70	9.5	11.7	9.7	11.1	10.1	11.2
75	7.0	9.6	7.6	8.6	7.8	8.5

Source: Malaysia, Department of Statistics age of 50 years, for women when they reach the age of 45 years. Hence the average payment period is extended to 24.1 years and 31.6 years, respectively in 1995. The link between the duration of payment of pension and life expectancy at the retirement age is due to the lifetime perspective of the Government pension scheme. Pensions are paid for the rest of the retiree's life; in the event of his death, the pension is paid to his widow and dependant children, if any, in the form of a derivative pension.

The longer life expectancy of the population in general and the pensioners (or their dependants) in particular tends to increase the number of recipients of retirement pension since more pensioners would be paid for a longer period of time.

INCREASE IN THE NUMBER OF BENEFICIARIES RECEIVING BENEFITS

The increasing number of pensioners (and their dependants) could be attributed mainly to the expansion of the public sector and the higher average life expectancy of the general population.

Hence, there was a steadily rising trend in the total annual number of beneficiaries from 1970 to 1992. The growth rate was particularly tremendous in 1981, that is, 66,013 in 1980 to 105,695 in 1981, that is an increase of 60.1 per cent.[1] By the end of 1992, that is, within a decade, the figure had more than doubled to about 230,000.

Thus as the scheme matures, the Government is obligated to pay increasing levels of benefits as successive cohorts of new beneficiaries are added to current ones, drawing benefits over a longer period as their life expectancy improves.

RETIREMENT AGE AND EARLY RETIREMENT PROVISIONS

Another factor is a reduction in the permissible retirement age for payment of pension. These include a reduction of the compulsory retirement age from 60 years to 55 years in 1967 and the optional retirement age from 45 to 40 years in 1991, although payment of monthly pension commences only at 50 years for men and 45 for women. Although this facilitates those who wish to retire early for various reasons, such as alternative employment, many may be actually discouraged from doing so. It could also indirectly reduce the size of the public sector and thus the pension expenditure, as well as encourage removal of any "deadwood". However, an employee who takes advantage of an early retirement provision may not have earned maximum pension. The effects of retirement age on the cost of pension is partly offset by the computation formula which has a built-in adjustment for the length of service of an officer so that those opt to retire earlier would receive a reduced monthly pension. Nevertheless, a lowering of the retirement age would increase the number of pensioners at any one time who would be paid for a longer period of time, thus contributing to a higher pension expenditure.

The cost of providing pensions is partly borne by the productive sector of the economy in the form of taxes. The loss of the productivity of officers who are required or influenced to stop working while they are still capablė or willing to work would impose a substantial loss both to individuals themselves and to society in general. Moreover, a low retirement age means a larger number of pensioners and hence a higher pension cost. This could alter the ratio between pension beneficiaries and the number of tax-payers.

On the other hand, encouraging people to continue working will not necessarily overcome the problem of pension costs. Earlier retirement is likely to add to pension costs, but deferment of retirement does not correspondingly reduce them, because those who defer retirement would earn a higher monthly pension.

Job requirements could mean that beyond a certain cut-off point, age poses as a disadvantage to one's job performance. This could explain why uniformed occupations, such as certain ranks of police officers, prison officers and fire service officers, are allowed optional retirement and paid their monthly pensions at an earlier age, that is, 45 instead of 50 years (Malaysia 1980a).

The retirement age exerts a crucial influence on the cost of the pension scheme. A lowering of the retirement age would result in a corresponding increase in the average number of years over which each pensioner will receive benefits. Existing early retirement provisions also contribute to the escalating pension costs.

Thus a choice has to be made between encouraging old workers to withdraw from public service earlier so as to allow vacancies for younger staff and delaying retirement with a view to improving the financial position of the scheme. The choice would require coherent decisions concerning conditions of award of benefits and methods of calculating them, and the age at which they become payable.

CONCLUDING REMARKS AND ALTERNATIVE OPTIONS

It is clear that the upward trend in benefit expenditure is continuing. The financing of pension benefits has grown at a rate much higher than the growth of GNP. It is a cause of concern and various efforts have been undertaken to check this upward trend, such as non-payment of pension for those who retire before 45 years for women and 50 years for men, and exclusion of allowances from salary (that is, only basic salary is used) for computation of an individual's benefit. Although pensions may seem attractive, the irony is that public employees may in effect be underpaid since they encounter salary ceilings non-existent in the private sector. Thus the Government faces the dilemma of continuing the payment of pensions in the future since they are not actually privileges, but represent a form of compensation for other components that are lacking in the public sector package, such as higher salaries and fringe benefits in the private sector. However, to succumb to any potential demands for excessive generous benefits would result in even higher future expenditures and financing requirements.

The real cost of resources used in providing pensions would be expected to rise over the long term as salary levels in the public sector move broadly in line with those in the rest of the economy as well as with the general rise in GNP. Hence provision for an increasing number of pensioners would consume a correspondingly higher share of GNP and general revenue. Thus the future payment of pensions and gratuities would impose a heavier burden on the national budget, implying that a greater proportion of national wealth would be channelled for the purpose. The ability of the Government to continue bearing this financial responsibility depends mainly on the rate of economic growth as additional resources are necessary to finance it. Moreover, productivity growth in the public sector, partly due to its labour-intensive nature, tends to be lower than that in the industrial sector. Nevertheless, in view of the future rising expenditure, it is would not be unreasonable to consider some reforms of the whole system of pensions in the public sector. Many cases have proven that the introduction of the privatisation programme in 1983 has helped to reduce the growth rate of public sector employment.

Pension benefits should be viewed as closely related to other aspects of public service management and policy. The provision of adequate retirement benefits is one of the most effective ways of improving conditions of service for employees and a contented work force, vital for the smooth and efficient functioning of public organisations.

It cannot be denied that a State pension scheme could provide effective financial protection for its employees; it is also in the position to improve the rate of benefits in line with economic growth and maintenance of purchasing power. Nevertheless, the basic principle that should be adhered to is that social security should not be deemed a function of the Government alone. Individuals should be encouraged to participate in the provision of their future retirement needs, such as through private saving and asset ownership. The role of the Government in providing for the retired and consequently the reliance of the retired on the Government could then be gradually but significantly reduced.

The longer a pension scheme has been implemented, the greater the number of benefits provided. Once benefits and conditions have been enacted, they are difficult to be withdrawn; hence it is important that the cost implications of any improvements in the benefit structure should be carefully studied.

ALTERNATIVE OPTIONS

During times of economic prosperity, the State undoubtedly has the capacity to meet the financial obligations of pensioners. However, there is a likelihood that both current and future retirees may be disillusioned if at any time their long-term interests are at stake when the Government pension scheme is unable to deliver the promised benefits. Indeed in the face of inevitable rising pension expenditure in the next decade, the cost issue cannot be evaded. The need to re-examine the existing pension structure in the light of changing economic, social and demographic factors or even to search for alternative benefit structures thus still remains.

In this context alternative options need to be considered by policy-makers concerned about the problem. Any review of the existing structure of the pension scheme would necessitate a prior assessment of the role of the Government in providing retirement income to its former employees.

Hindered by the stark realities of strong objections from all interested parties to any drastic actions, such as the abolition of the Government pension scheme, and the unlikely eagerness of members beckoning a scheme to which they have to contribute, policy-makers are faced with limited options. If the existing non-contributory principle for public sector employees is to be adhered to, then there is limited room to manoeuvre with the issue at hand, except to consider the possibility of adopting a benefit formulae that give more weightage to lower salary grades as compared to higher grades. This will, at the same time, meet the objective of providing an income to all its members (and their dependants) against the various contingencies.

If the objective of promoting loyalty and long service among its employees is to be fulfilled, benefits can be calculated by applying a progressive formula that comprises a specified percentage of salary for each of the first 10 or 15 years of service, with subsequently higher percentages for each of the subsequent years.

Amidst formidable obstacles, such as the initial uproar that can be expected and yet for the sake of moderating the cost escalation as well as greater bureaucratic and income distributional efficiencies, another alternative is to contemplate overhauling the existing government pension scheme by transforming it into a contributory one that is privately managed and financed. This has been carried out in Chile where the public pension scheme has been converted into a savings-annuity system. To gain gradual acceptance, such a move can be initiated with low contribution rates.

In formulating any private scheme, the issue of whether a defined-contribution plan should be compulsory or voluntary has to be settled. Although mandatory membership will go a long way towards providing for their own retirement, individuals should be discouraged from relying on their pensions as the sole means of old-age income. Instead they should be expected to provide additional income for their retirement, such as through individual savings, asset ownership, private insurance and intergenerational transfers from their working children and relatives. While the financial obligations of the State can be relieved and in fact replaced by the private scheme, its regulatory role remains to ensure the smooth functioning of private schemes and the protection of members' rights such as solvency controls.

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Faculty of Economics
Universiti Malaya
59100 Kuala Lumpur