EPF: Lump-sum or partial withdrawals at 55?

5 questions to ask and answer

by Celine Tan

UPON reaching 55, most people prefer to withdraw all their savings in the Employees Provident Fund (EPF) but more and more people are opting for flexible withdrawals (partial or monthly payments). According to the EPF, last year, 235,931 employees made withdrawals at age 55 and 70% of the withdrawals were full withdrawals. The number of flexible withdrawals increased by 41.67% to 82,690, compared with 2009 (see table).

Choosing between withdrawing a lump sum and making a partial withdrawal depends on many factors. Financial planners say you can ask five questions when crunching the numbers for your retirement plan, not at 55.

1 What is your behaviour towards money?

Your EPF savings can be the single largest disbursement of money you will see in your lifetime. "It is something that most individuals look forward to throughout their working life. It gives them a sense of fulfilment when they receive it since they believe that it is then possible

BREAKDOWN OF WITHDRAWALS AT 55

	AMOUNT WITHDRAWN (RM)	FLEXIBLE WITHDRAWALS (PARTIAL AND MONTHLY)		LUMP-SUM WITHDRAWALS		TOTAL NUMBER OF WITHDRAWALS
		NO. OF WITHDRAWALS	%	NO OF WITHDRAWALS	%	
2009	8,343,367,709	58,368	25	150,718	75	209,086
2010	8,516,380,059	82,690	30	152,971	70	235,931

Source: EPF

to achieve their life goals," says K Gunasegaran, founder and licensed financial planner of Wealth Street Sdn Bhd.

If you are quick to spend money without a plan, think twice before withdrawing the whole. "Those who are not used to having large sums of money tend to get emotionally charged. It can lead to splurges on big-ticket items such as luxury cars. While the money is rightfully yours and it is not entirely wrong to benefit from your retirement savings, be aware of the consequences. If you know that you are an emotional spender, it is best to drop the idea of a lump-sum withdrawal because you have to make smart choices with the money," says Gunasegaran.

2 Can you generate higher returns at a higher risk?

The primary concern of retirees is whether their retirement savings can sustain them throughout their golden years and generate sufficient returns to outpace inflation.

Headline inflation, as measured by the Consumer Price Index (CPI), increased to 3.3% on an annual basis in May, according to Bank Negara Malaysia (BNM). From 2005 to 2010, the average inflation rate in the country was 2.77%, reaching a historical high of 8.5% in July 2008 and a record low of -2.4% in July 2009.

For the past 59 years, from 1952 to 2010, the EPF has declared annual dividend rates of between 2.5% and 8.5%. In the past 10 years, the highest dividend payout from the EPF was 6% in 2000 and the lowest dividend payout was 4.25% in 2002. "If you are conservative and expect the EPF to continue providing decent annual dividends, opt for flexible withdrawals," says Wong Keng Leong, practice manager and licensed financial adviser representative at Standard Financial Planner Sdn Bhd.

Headline inflation, however, is not necessarily a reflection of the rise in a household's real cost of living. This means that the returns on your retirement savings should far exceed the reported CPI figures. "Also, the EPF promises a minimum dividend of 2.5% per annum. If you think that you or your financial adviser or fund manager can surpass the average returns made by the EPF, consider a lump-sump withdrawal to boost your retirement nest egg," says Gunasegaran.

When doing so, observe the associated costs such as sales charges or management fees levied by the financial professionals and financial institutions. If you decide to retain your retirement savings with the EPF, there will be a small charge that differs from year to year.

3 Would you still be paying debts at age 55?

If you will still be servicing high-interest debts at age 55, consider using your EPF savings to pare down or settle the loans. This is especially so if the interest levied is higher than the returns generated by your savings. "High-interest debt includes credit cards [interest rate ranges from 13.5% to 17.5% a year] and personal loans [interest rate ranges from 8% to 12%]. Holding any of these debts negates any investment gains unless you are able to get superior returns on your investment over the years. Withdrawing your retirement savings, be it in a lump sum or partially, to settle your high-interest debt is a smart option but ensure that there is still some money left for your retirement, says Wong.

There is no fixed rule on how much debt you should settle. "How much you should pay off depends on the quantum of your savings.

WONG: Withdraw your retirement savings to settle your high-interest debt ... but ensure that there is still some money left for your retirement

GUNASEGARAN: Put retirement savings into annuity-like insurance plans

Also, it is good to check whether your debt can be restructured to reduce the interest you have to pay. If so, evaluate the financial benefit of settling this debt with a lump sum withdrawal of your EPF savings," says Gunasegaran.

4 Do you want to control your retirement funds?

Contributors have little control over how their savings are managed and invested by the EPF, which has sole discretion on how to invest the money that they receive and the dividend (over the minimum amount guaranteed) to declare.

"If you want to take full charge of your retirement savings [either on your own or with professional help], you can do so at 55. When you take a lump-sum payment, you are able to invest in investments that may not be available to you if you were to retain your savings in the EPF [withdrawals can be made to EPF-approved local equity funds]," says Wong, who observes that most of his retired clients withdrew all their EPF monies at 55 as they were comfortable with managing their own money.

A key benefit of withdrawing your retirement savings in a lump sum is that it allows you to expose your loved ones to managing money with a long-term perspective. "At the point of death, most of us will not want to leave a large sum of money to loved ones who cannot manage it. In all likelihood, the money will be spent sooner than planned. Withdrawing your retirement savings in a lump sum at the point of retirement allows you to slowly educate your young-adult children on how to manage a big sum of money. Let them know where you keep your savings and what you are doing with it. This is an alternative to receiving a lump sum from the EPF when you are no longer around," says Gunasegaran.

5 Do you have a plan to access your money?

If you are 55, under the EPF's monthly payment withdrawal scheme, the board will transfer the total amount into a special account and put monthly payments into your bank account.

If you opt for a lump-sum withdrawal, how will you draw down your money to fund your lifestyle? There are two options to evaluate. Wong suggests that you should plan a draw-down strategy that includes either a quarterly or half-yearly redemption. "Note that some instruments allow you to make periodical withdrawals but may impose charges."

On the other hand, Gunasegaran thinks that it is more advisable for retirees to put their retirement savings into annuity-like insurance plans, under which they will receive annual payments after a certain number of years. ▪

COMMON MISTAKES MADE WITH LUMP-SUM WITHDRAWALS

Preparing to retire is sometimes likened to preparing for a marathon. This is why: It requires one to accumulate assets that will last decades. Running a marathon needs you to train for a 42km run. "When retiring and at the start of a marathon, both individuals want to reach the end. For the former, this translates to sufficient savings. However, many do not know what to do when they receive their EPF savings and do not know how to generate returns that surpass inflation," says Wong Keng Leong, practice manager and licensed financial adviser representative at Standard Financial Planner Sdn Bhd.

Many retirees want to live their dreams and goals, but have limited resources. "This increases the tendency to fall for 'get-rich-quick schemes' in the hopes of 'boosting' their income and fulfilling their life goals," says K Gunasegaran, founder and licensed financial planner at Wealth Street Sdn Bhd.

An old statistic from the EPF is frequently quoted: 70% of contributors who withdraw their EPF savings at the age of 55 spend all of it within three years. "While it is fine to reward yourself and your spouse during retirement years, be moderate in your approach. For instance, if you need a new car, choose one that suits your requirements and that you can afford. Instead of going for a yearly holiday, go every five years. This allows your returns to compound," says Gunasegaran.

Another common mistake is to use the lump sum to fund your children's education. "Funding your own retirement is more important that your children's education because your children can take a study loan and repay the amount after they start working. This option is not available to you as a retiree," says Wong. ▪