

# WORLD FINANCE

THE VOICE OF THE MARKET

## A revolution in retirement planning for the Philippines

By World Finance – July 16, 2023

<https://www.worldfinance.com/wealth-management/a-revolution-in-retirement-planning-for-the-philippines>

Family is the foundation of social life in the Philippines and a high priority among Filipinos. Ask any parent if they have invested or saved for their children's future and the answer is almost always a resounding yes. However, the same cannot be said when asked about how they are preparing for their own eventual retirement

Almost everyone has a clear idea on what they will be doing after retirement from work. Unfortunately, most have not taken any concrete steps to prepare for retirement. As is often the case, planning for retirement takes a backseat compared to taking care of other members of the family and even the extended family. Filipinos tend not to actively prepare for eventual retirement and greatly depend on either the mandatory company retirement payout or through the state-sponsored retirement systems, the Social Security Services (SSS) for private citizens or the Government Service Insurance System (GSIS) for government employees. A good number depend on their children to help them with their finances upon retirement. Unfortunately, dependence on any one, or even all three, methods is not sustainable in the long run.

In a recent survey, Filipinos believe that savings equivalent to 2.1 years' worth of personal income is enough for their retirement, which is way below the regional average of 2.9 years. If you consider that the average current life expectancy of Filipinos is 72 and the standard retirement age is 60, retirement savings could be short by up to 10 years, maybe more.

The lack of retirement planning is exacerbated by the general gaps in financial knowledge among Filipinos to manage their retirement finance. Either the funds are left in savings accounts, which produce near zero income, or they are depleted due to bad business decisions or spent on unnecessary extravagance. The lack of financial literacy, discipline and annuity type of pension payout can contribute to early depletion of retirement funds.

### **The state of pension funds**

The Philippine Institute for Development Studies conducted a study in 2018 showing that the Philippines will be an aging population by 2032, when at least seven percent of its population will be 65 years and older. This only means that more people will be relying on pension benefits, whether through private or public pension systems. The Philippines, unfortunately, has much to improve upon when it comes to retirement systems. According to Mercer CFA Institution Global Pension Index, the Philippines has the second worst retirement income system among 44 nations.

Today, the Philippines has around 7.6 million Filipinos aged 60 and above. The SSS provides a monthly pension of approximately PHP 5,000–18,000 (\$90–\$320) to retirees. Considering the increasing cost of living, expected medical costs and other lifestyle expenses, it is safe to say that the pension provided by the state is insufficient.

Republic Act Nos. 4917 and 7641 enacted a corporate pension system for the private sector, designed to augment SSS benefits. Under the law, private companies can establish their own retirement plans that enjoy certain tax benefits including exemptions from investment income and compensation taxes. Currently however, the creation of a retirement fund is not mandatory and oftentimes only the large companies establish such retirement plans for the benefit of their employees. Most SMEs or traditional family-owned corporations still use the 'pay as you go' scheme to provide retirement pay as their employees retire.

Considering that these payments are not pre-funded, it places employees' retirement pay at risk during

difficult times for businesses where many employers are in financial straits. Simply put, the current state-sponsored and private pension plans are oftentimes not adequate to provide for 10 years' worth of living expenses for retirement especially if additional income is lacking.

### **Revolutionising pension funds**

Both the government and private sector have acknowledged that there are serious flaws in the current pension system that need to be addressed. For one, current corporate pension funds are not portable, leaving the burden of retirement planning solely to the last employer. As funding of corporate retirement funds is not mandatory, the majority of companies just provide the minimum mandatory retirement pay on a 'pay as you go' basis or in some cases no retirement payments are made. Many companies cite cumbersome and expensive processes to establish formal retirement plans, thus negating the tax benefits granted to formally established retirement programmes. The result is companies fall back to these 'pay as you go' schemes. The unfortunate consequence is that retirees are forced to either continue working for additional income, change their lifestyle to reduce their expenses, or depend on family members to finance their retirement years. The worst-case scenario is when retirees are unable to fund their expenses and fall into poverty.

The Capital Markets Development Act of 2021 aims to change all that. The bill has already passed Congress and is currently awaiting the Senate's approval. If passed, the law will help improve private pension plans and compel companies to redesign current retirement systems to adapt to the law. The objective of the bill is to establish a private retirement and pension system that is fully funded, portable, and more actuarially fair for employees.

One significant change is that the responsibility of deciding and funding for the employee's retirement benefit will now be shared by both the employer and the employee. Currently, investment decisions and pension payouts are decided and shouldered solely by the employer whether the pension is based on the mandatory retirement pay or based on a defined benefit arrangement. The pending bill allows for the creation of a mandatory, fully funded and portable Employee Pension and Retirement Income (EPRI) account under the name of the employee, created at the start of employment. The EPRI account shall be permanent, owned and managed by the employee regardless of changes in employment or transfer of employer until their eventual retirement. As a benefit of establishing EPRI, employer contributions are allowed as a deductible expense and shall not be considered as part of the employee's compensation subject to income tax. In addition, all income and gains earned from investments of the EPRI assets, and all benefits and distributions received by the employee upon his retirement shall be exempt from all taxes.

Given the great shift in the age of the population, the corporate pension law as well as the retirement mindset of Filipinos, much more thought must be given to this. Not only do employers need to prepare for and study how to transform their existing retirement plans, but it is just as important to include the beneficiaries of their retirement plan, their employees, in the transformation process.

### **Finding ways to redefine retirement**

We at BDO have been finding ways of reimagining retirement plans in the country. BDO believes in a holistic approach to attain sustainable retirement plans by supplementing corporate retirement programmes with a personal stake in one's own retirement journey.

BDO is redefining corporate retirement planning through an integrated retirement plan solution, Pension 360. It is designed to assist companies to fulfil their retirement obligations more efficiently, while helping it attract and retain the best talent. Pension 360 combines our core pension services with personal wealth-building programmes to offer a comprehensive approach. Pension 360 consists of four main services: Corporate Pension Programme, Employee Education Programme, Personal Pension Plan, and Personal Annuity Plan.

*Corporate Pension Programme:* Companies can fulfil their retirement benefit obligations without the complexities of planning and intricacies of day-to-day administration with our Corporate Pension Programme. BDO helps companies design and optimise their retirement plan, whether it's defined benefit, defined contribution or hybrid plan, to deliver long-term value with prudent governance management for their business.

*Employee Education Programme:* To empower employees to take charge of their retirement future, BDO provides complimentary financial literacy seminars to employees. The goal is to equip employees with knowledge, information and insights through learning modules designed to help them manage their finances and grow their wealth through investments. Employee education is a crucial step in improving the long-term sustainable financial wellbeing of Filipinos especially in preparation for their eventual retirement. There are currently four financial education modules that match the employees' level of investment knowledge. One of the four modules is dedicated to retirement planning. A team of professional trainers is assigned to fulfil this notable task.

*Personal Pension Plan:* Empower employees to take charge of their finances through wealth-building programmes such as the Easy Investment Plan (EIP) and Personal Equity and Retirement Account (PERA). The EIP helps individuals get into the twin habits of regular saving and investing automatically and regularly in various investment funds. PERA, on the other hand, is a long-term voluntary tax-exempt retirement programme provided by law to encourage Filipinos to invest towards their own retirement. Either employees, employers or both can contribute to an employees' PERA. Moreover, there are tax advantages which are only available with PERA such as exemption from taxes on investments, estate taxes, and five percent tax credits from the annual PERA contribution. Employees can start their investment journey for as low as PHP 1,000 (approx \$18) or \$500 for dollar-denominated investment funds.

*Personal Annuity Plan:* Lastly, upon retirement, assure employees' peace of mind with an income payout scheme with Easy Pension Pay. The plan lets retirees enjoy the fruits of their hard work with proper management and disbursements of their funds as if the retirees are still receiving regular semi-monthly salaries. With this, the retired employees' retirement funds are safeguarded against unnecessary expenditures and are made productive by investing to earn investment income. Pension 360 includes employees as an integral part of the programme and not just as beneficiaries of the company's pension plan, thus enabling a truly sustainable retirement programme.

### **Reaching the retirement goal**

For individual clients who have decided to plan for their retirement ahead of time, BDO offers a fiduciary service that allows clients to dedicate a specific investment portfolio for a defined need. The Money Manager is a personal management trust arrangement that allows clients to set amounts for each life goal, such as retirement, and define specific dispositive conditions unique to each client and portfolio. Having a dedicated portfolio for each life goal, whether for retirement, education or wealth accumulation, helps clients deliberately plan for its achievement in the long term.

By allocating funds for life goals, it sets the path for the achievement of such purpose. In addition, the ability to create dispositive clauses under a personal management trust makes this trust arrangement unique and personalised, thus able to address the very specific needs of the client and/or their beneficiaries. The Money Manager is available to clients with different risk profiles and asset allocations. Clients can invest in either Philippine Peso or US Dollars, giving clients the flexibility to invest in local or global assets.

Now more than ever, planning for one's own retirement must be a deliberate endeavour and a personal engagement. A carefully crafted long-term plan is key to ensuring a comfortable retirement in the future. With the availability of information at one's fingertips, there are many options and routes to achieve a comfortable retirement, but one must take action to arm themselves with knowledge and tools to help chart the best course of action.

Corporate retirement plans and the government-sponsored pension are good to have, but these should not be the only source of funds at retirement. BDO's goal is to help build, design and execute a sustainable retirement fund both at the corporate and personal level. We don't always know what the future will bring, but to paraphrase the poet William Ernest Henley, we must each be the master of our fate and the captain of our soul.