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CENTRAL PROVIDENT FUND CHANGES

Several changes to the Central Provident Fund ("CPF") system were recommended by The Economic Review Committee's ("ERC's") subcommittee on taxation, CPF, wages and land on 15 July 2002. Some of the main recommendations are summarised below:

Central Provident Fund

The CPF contribution rates will gradually be restored to 40%. The current and proposed CPF contribution rates and the rates for the respective accounts and age groups are listed below:

Table 1

	Ordinary Account		Medisave Account		Special Account		Total	
Age	Current %	Proposed %	Current %	Proposed %	Current %	Proposed %	Current %	Proposed %
35 and under	26	28	6	7	4	5	36	40
Above 35-45	23	25	7	8	6	7	36	40
Above 45-50	22	22	8	9	6	9	36	40
Above 50-55	22	14	8	9	6	9	36	32
Above 55-60	10.5	11	8	9	0	0	18.5	20
Above 60-65	2.5	2.5	8.5	9	0	0	11	11.5
Above 65	0	0	8.5	9	0	0	8.5	9

The ERC's subcommittee recommended for the new rates to take effect in tandem with the restoration of the total contribution to 40%. This will take several years.

Labour Market Flexibility

a. CPF contribution for monthly ordinary wages will be capped at $5,000 instead of the current $6,000. The reduction in mandatory contributions also helps to enhance wage flexibility. The ERC view workers in the higher salary scale to be better in managing their finances and hence should not be compelled to contribute any higher proportion of their pay into CPF. Employers are in fact urged to compensate these workers for the loss of employers' CPF contribution with higher wages to reflect their market value.

b. Workers between the age of 50-55 years will have their employers' and employees' contribution cut from 20% to 16% as the CPF contribution is restored for the other age group. The committee emphasised that this is not a cost cutting measure but a way to increase wage flexibility to help these workers keep their jobs or to secure new ones.

c. The minimum salary for employee CPF contributions will be raised from $200-$363 to $500-$750. This will lead to higher take home pay for those earning less than $750 monthly.

Financial Security in Retirement

The CPF Special Account contribution rates will be increased by a further 1% to 3% (for workers age 55 and below) to enable workers reach the minimum sum requirement which will be $80,000 from 1 July 2003. The minimum sum will also be raised beyond $80,000 effective from the year 2003 to cater for their retirement needs. Please refer to Table 1 for the proposed rates for different categories of age group.

Healthcare Needs

The CPF Medisave Account contribution rates will be increased by 0.5% to 1% to cater for healthcare needs in retirement. Please refer to Table 1 for the proposed rates for different categories of age group.

Home Ownership

CPF withdrawals for new properties bought with the exception of Housing & Development Board ("HDB") subsidised loans will be capped at 150% of the property value with effect from 1 September 2002 and brought down further to 120% over the next five years. This is to prevent CPF members from over borrowing to buy property.

Some possible impact of the ERC's Recommendations

Higher personal income tax and lower overall income but take-home pay will increase

CPF contributions up to the statutory amount from the employer is not subject to income tax and contribution by the employee is deducted as a relief against his assessable income. Lowering the contribution rate and the CPF ceiling will increase the tax burden of an individual. This is particularly so for the high-income earners between the age of 50-55 years.

Lower loan for housing and the reluctance of banks to lend to persons approaching their 50s

The capping of the home mortgage financing using CPF funds to 150% of property value and eventually to 120% would affect homebuyers.

A Goldman Sachs analyst quoted "These buyers will have to lower their loan durations and pay more cash towards their mortgages monthly". Although this move could affect demand and prices of properties but in the long run, this should put the property market on a sounder footing. As Mr Tharman Shanmugaratnam, chairman of the ERC's subcommittee on taxation, CPF, wages and land, said " We did not want to destabilise the property market".

Immediately after the ERC's recommendations, the government announced several measures to boost the banking sector and mitigate potential negative impact on the property market. Banks will be allowed to provide mortgage loans for HDB flats currently financed by HDB at market rates. CPF can be used for up to half of the 20% cash deposit for new residential purchases with effect from 1 September 2002.

Another likely impact of the ERC's recommendations is that banks may now be less willing to extend housing loan to those nearing or in their 50s as their CPF contributions will be reduced.

Conclusion

The aim of these recommendations is to fine tune the CPF system which remains as an important and integral part of our wage structure providing Singaporean with home ownership and retirement funds.

Amongst other benefits, the ERC's recommendations will provide flexibility to our wage structure especially those in the older age group, which are bearing the brunt of the current recession.

The proposals will also bring down the amount of CPF withdrawal for repayment of housing loan to a more reasonable level, so that homeowners will not purchase houses that are beyond their means. This will leave more CPF balance for retirement. Increase in the contribution rates for special account and raising the minimum sum requirement will also lead to more funds available for retirement. Increase in Medisave will address the healthcare needs in retirement.

The parliament has since approved the ERC's recommendations.

This article is contributed by Mr Foo Teck Leong, a director of Total Business Solution Pte Ltd ("TBS"), a company providing one-stop professional solutions to SMEs and individuals. Solutions provided by TBS include:

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