First edition

# INTRODUCTION TO FINANCIAL PLANNING


**Prepared By**

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# Introduction to Financial Planning

First edition 2024

## COMMERCE DEPARTMENT

JABATAN PENDIDIKAN POLITEKNIK DAN KOLEJ KOMUNITI
KEMENTERIAN PENDIDIKAN TINGGI

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# Introduction to Financial Planning

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# PREFACE

This e-book is written to give readers an overview of financial planning. In today's fast-paced world, managing personal finances has become more critical than ever. The ability to plan, save, and invest wisely can be the difference between financial security and uncertainty.  This e-book aims to demystify the financial planning process and give readers the tools and knowledge needed to take control of their financial future.

This e-book is designed to guide readers through the essentials of financial planning, regardless of their starting point. It cover budgeting, saving, investing, risk management, tax planning, and retirement planning — a comprehensive financial plan tailored to client needs and goals.

The financial landscape can often feel overwhelming, but anyone can achieve financial freedom with the proper knowledge and a clear plan. This e-book empowers readers to make confident financial decisions and build a secure future for themselves and their families by breaking complex concepts into simple, actionable steps.

May this e-book be a trusted guide to a more prosperous and secure financial future.

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# About Us

## FAIRUZ SOFIA BINTI KAHARUDDIN

Ms. Fairuz Sofia is a lecturer at Politeknik Sultan Salahuddin Abdul Aziz Shah and has more than 10 years of experience in teaching and learning in the field of finance. She holds a Bachelor's degree in Business Management from IIUM and a Master of Science (Finance) from UUM.

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WHY FINANCIAL PLANNING IS VERY IMPORTANT?

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# "It's about creating a **roadmap for your life** that balances dreams with reality"

COMMERCE DEPARTMENT, PSA

# Chapter 1: Overview of the Financial Planning Industry

## 01 | DEFINE FINANCIAL PLANNING

Financial planning is a systematic approach to managing one's financial resources to achieve life goals. It involves setting clear objectives, analyzing the current financial situation, and implementing strategies to meet those goals.

Financial planning is not just about budgeting or saving; it encompasses various aspects of managing finances to ensure long-term financial security and stability.

> **Financial planning is a systematic approach to managing one's financial resources to achieve life goals.**

## 02 | THE OBJECTIVES OF FINANCIAL PLANNING

- **Budgeting and Managing Expenses:** Ensuring that income is allocated efficiently to cover necessary expenses and savings.
- **Asset Management:** Building and maintaining a portfolio of assets that appreciates over time.
- **Risk Management:** Protecting against potential financial losses through insurance and other mechanisms.
- **Investment Planning:** Growing wealth through strategic investments.
- **Tax Planning:** Minimizing tax liabilities through legal means.
- **Retirement and Estate Planning:** Ensuring financial stability during retirement and the efficient transfer of wealth.

## 1.1.3 | FINANCIAL PLANNING PROCESS

**The financial planning process involves several key steps:**

- **Budget Planning:** Creating a plan for allocating income towards expenses, savings, and investments. Effective budget planning ensures that financial resources are used efficiently.
- **Managing Cash Flow and Basic Assets:** Monitoring and controlling the inflow and outflow of money to maintain financial stability. Basic assets include savings, checking accounts, and liquid investments.
- **Risk Management and Insurance Planning:** Identifying potential financial risks and finding ways to mitigate them. This often involves purchasing insurance policies to cover health, life, property, and other assets.
- **Investment Planning:** Developing a strategy to grow wealth over time through investments in stocks, bonds, mutual funds, real estate, and other vehicles.
- **Tax Planning:** Structuring financial activities to reduce tax liabilities. This includes taking advantage of tax deductions, credits, and other incentives.
- **Retirement/Estate Planning:** Preparing for retirement by building a financial cushion that will support one's lifestyle. Estate planning involves managing and distributing assets after death in accordance with the individual's wishes.
- **Islamic Estate Planning:** Ensuring that the distribution of assets after death complies with Islamic law (Shariah), which includes principles like the division of inheritance and charitable giving.

**Always store your property taxes, maintenance bills, insurance, permits.**

## 1.1.4 | THE TRADE-OFF CONCEPT

The trade-off concept in financial planning involves making decisions that balance competing financial priorities. For instance, an individual might need to decide between saving for retirement and investing in their child's education. Understanding trade-offs helps in making informed decisions that align with long-term financial goals.

## 1.1.5 | THE MARKETING OF FINANCIAL PLANNING SERVICES

Marketing financial planning services involves promoting the value of comprehensive financial advice to potential clients. It includes building trust, demonstrating expertise, and communicating how tailored financial strategies can help clients achieve their financial goals. Channels for marketing may include digital advertising, social media, seminars, and networking.

## 1.1.6 | THE RISK PROFILE INVESTOR

Investor risk profiles vary based on their financial goals, timelines, and risk tolerance. Generally, investors are categorized as:

- **Conservative:** prefer low-risk investments and prioritize capital preservation.
- **Moderate:** willing to take some risk for moderate returns.
- **Aggressive:** ready to take significant risks for higher potential returns. Understanding an investor's risk profile is crucial to creating a financial plan that aligns with their comfort level and objectives.

# THE ANALYTICAL TOOLS FOR FINANCIAL PLANNING

## 1.2.1 | TYPES OF CONCEPTS AND APPLICATIONS IN RELATION TO THE TIME VALUE OF MONEY

The concept of the time value of money (TVM) is central to financial planning, as it reflects the idea that a dollar today is worth more than a dollar in the future due to its potential earning capacity. Here, we'll explore both rudimentary and advanced concepts and applications

a. **Rudimentary Concepts and Applications:** Rudimentary concepts of the time value of money include understanding basic calculations such as present value (PV) and future value (FV). These are used to determine the value of money at different points in time. For example:

- Present Value (PV): The current value of a future sum of money or stream of cash flows given a specified rate of return.
- Future Value (FV): The value of a current asset at a future date based on an assumed rate of growth.

b. **Advanced Concepts and Applications:** Advanced applications of the time value of money involve more complex scenarios, such as:

- **Net Present Value (NPV):** Used in capital budgeting to assess the profitability of an investment or project. NPV is the difference between the present value of cash inflows and outflows over a period of time.
- **Internal Rate of Return (IRR):** The discount rate that makes the NPV of all cash flows from a particular project equal to zero. It's a metric used to evaluate the attractiveness of a project or investment.
- **Annuities and Perpetuities:** Calculating the present or future value of a series of payments (annuities) or endless payments (perpetuities).

## 1.2.2 | RISK TOLERANCE IN FINANCIAL DECISIONS.

Risk tolerance refers to the degree of variability in investment returns that an individual is willing to withstand in their financial plan. .

- **Conservative:** prefers minimal risk and is satisfied with lower returns.
- **Moderate:** balances risk with moderate returns.
- **Aggressive:** willing to accept significant risks for potentially higher returns.

# THE FINANCIAL PLANNING INDUSTRY IN MALAYSIA

## 1.3.1 | THE LOCAL AND GLOBAL DEVELOPMENT OF FINANCIAL PLANNING

**Global Development:** The financial planning industry has grown significantly worldwide, influenced by the increasing complexity of financial products, regulatory changes, and the rise of the middle class seeking financial security. Key developments include the professionalization of financial planners, the adoption of technology in financial services (fintech), and the globalization of financial markets.

**Local Development in Malaysia:** In Malaysia, the financial planning industry has evolved in response to economic growth, rising income levels, and regulatory advancements. The Securities Commission Malaysia (SC) and Bank Negara Malaysia (BNM) have been instrumental in setting standards and regulations to ensure that financial planning services are accessible and reliable. The establishment of professional bodies like the Financial Planning Association of Malaysia (FPAM) has further driven the industry's credibility and growth.

## 1.3.2 | THE LOCAL AND GLOBAL DEVELOPMENT OF FINANCIAL PLANNING

- **Banks and financial institutions:** Offer comprehensive financial planning services as part of their wealth management portfolios.
- **Independent Financial Advisors (IFAs):** Provide unbiased advice tailored to clients' specific needs without being tied to any particular financial institution.
- **Insurance companies:** offer financial planning services with a focus on risk management, retirement planning, and wealth protection.
- **Investment firms:** specialize in investment planning and portfolio management as part of their financial planning services.
- **Certified Financial Planners (CFPs):** are professionals who have obtained certification from recognized bodies and offer personalized financial advice.

## 1.3.3| THE RANGE OF FINANCIAL SERVICES AVAILABLE.

In Malaysia, financial planners offer a wide range of services, including:

- **Investment Planning:** Crafting investment strategies that align with clients' goals and risk tolerance.
- **Retirement Planning:** Developing plans to ensure sufficient income during retirement.
- **Insurance and Risk Management:** Assessing and advising on insurance needs to protect against unforeseen events.
- **Estate Planning:** Helping clients plan for the distribution of their wealth upon death, including Islamic estate planning (Faraid).
- **Tax Planning:** Advising on strategies to minimize tax liabilities while remaining compliant with Malaysian tax laws.
- **Education Planning:** Assisting clients in saving for their children's education through tailored investment plans.

## 1.3.4 | THE PROFILE OF A COMPETENT FINANCIAL PLANNER

A competent financial planner in Malaysia should possess the following attributes:

- **Certification and Credentials:** Holding certifications such as Certified Financial Planner (CFP), Registered Financial Planner (RFP), or Shariah Registered Financial Planner (Shariah RFP) indicates a high level of knowledge and professionalism.
- **Experience:** demonstrated experience in providing financial advice and managing client portfolios.
- **Ethical Standards:** Adhering to a strict code of ethics, including transparency, honesty, and acting in the client's best interest.
- **Communication skills:** the ability to explain complex financial concepts in a clear and understandable manner.
- **Client-Centric Approach:** Focusing on the needs, goals, and circumstances of the client, offering personalized advice rather than one-size-fits-all solutions.

HOW DO CHANGES IN THE ECONOMIC ENVIRONMENT, SUCH AS GOVERNMENT POLICIES INFLUENCE OUR FINANCIAL DECISIONS?

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# "The economic environment affects everything **we do financially**”

COMMERCE DEPARTMENT, PSA

# Chapter 2: The Economic Environment and Its Implication

## 2.1.1 | THE ROLE OF GOVERNMENT IN AN ECONOMIC SECTOR

### REGULATION AND OVERSIGHT

Enforcing laws and regulations that govern economic activities, such as labor laws, environmental standards, and consumer protection

### FISCAL POLICY

Governments use taxation and public spending to influence the economy. This includes collecting taxes, spending on public goods and services, and managing budget deficits or surpluses.

### MONETARY POLICY

Through central banks, the government controls the money supply and interest rates to manage economic stability and growth.

### ECONOMIC STABILIZATION:

During economic downturns, governments can use stimulus measures, such as increased public spending or tax cuts, to help stabilize the economy.

## 2.1.1 | THE ROLE OF PRIVATE SECTOR IN AN ECONOMIC SECTOR

### PRODUCTION OF GOODS AND SERVICES

Businesses create products and services that meet consumer needs, driving economic activity.

### INVESTMENT AND INNOVATION

Private companies invest in new technologies, research and development, and infrastructure, contributing to long-term economic growth.

### JOB CREATION

The private sector is the largest employer, providing opportunities for individuals to earn income and improve their standard of living.

### TAX REVENUE

Private businesses contribute to government revenue through taxes. This revenue is critical for funding public services and infrastructure development.

## 2.1.2 | THE INFLUENCE OF DEMOGRAPHIC STRUCTURE AND INVESTMENT INCENTIVES

- **Demographic Structure Influence:** The demographic structure of a population, including age, gender, and income distribution, has significant implications for an economic system. For example:
  - **Aging Population:** An aging population may lead to increased demand for healthcare services, pensions, and retirement planning, while potentially reducing the labor force and economic productivity.
  - **Youthful Population:** A younger demographic might increase the demand for education, housing, and job creation, fostering economic growth but also requiring significant investment in infrastructure and services.
- **Investment Incentives Influence:** Investment incentives, such as tax breaks, subsidies, and grants, can stimulate economic growth by encouraging both domestic and foreign investment.


  - Attract Foreign Direct Investment (FDI): Countries offer incentives to attract foreign companies, which bring capital, technology, and jobs.
  - Encourage Entrepreneurship: By reducing the cost of starting and running a business, incentives can promote entrepreneurship and innovation.
  - Boost Specific Sectors: Targeted incentives can help develop key industries, such as renewable energy or technology, contributing to a diversified and resilient economy.

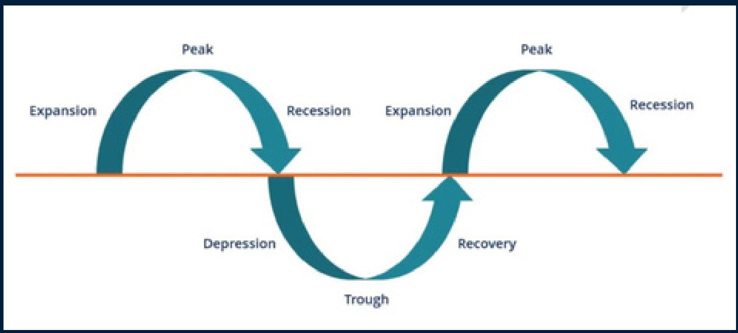
## ANALYZE THE ECONOMIC ENVIRONMENT

## 2.1.3 | COMPARE BETWEEN GROWTH AND BUSINESS CYCLE

**Economic Growth:**
Economic growth refers to the increase in the production of goods and services in an economy over time. It is measured by the growth rate of a country's Gross Domestic Product (GDP). Sustained economic growth leads to higher income levels, improved standards of living, and increased employment opportunities. Growth is driven by factors such as technological advancements, capital accumulation, and labor force expansion.

**Business Cycle:**
The business cycle describes the fluctuations in economic activity that an economy experiences over a period, characterized by phases of expansion and contraction. The key phases include:

- **Expansion:** A period of rising economic activity, increasing GDP, employment, and consumer spending.
- **Peak:** The point at which economic growth reaches its maximum rate before starting to decline.
- **Recession:** A period of declining economic activity, falling GDP, rising unemployment, and reduced consumer spending.
- **Trough:** The lowest point in the business cycle, marking the end of a recession before the economy begins to recover.




- **Gross Domestic Product (GDP):** Measures the total value of goods and services produced in an economy. It is the most comprehensive indicator of economic activity.
- **Unemployment Rate:** Indicates the percentage of the labor force that is unemployed and actively seeking work. A rising unemployment rate can signal economic distress.
- **Inflation Rate:** Measures the rate at which the general level of prices for goods and services is rising, eroding purchasing power.
- **Consumer Confidence Index (CCI):** Reflects consumers' optimism or pessimism about the state of the economy, influencing their spending behavior.
- **Interest Rates:** Set by central banks, interest rates influence borrowing costs, consumer spending, and investment decisions.

## 2.2.2 | THE ROLES OF ECONOMIC INDICATOR

Economic indicators are statistical measures that provide insights into the health of an economy.

- **Gross Domestic Product (GDP):** Measures the total value of goods and services produced in an economy. It is the most comprehensive indicator of economic activity.
- **Unemployment Rate:** Indicates the percentage of the labor force that is unemployed and actively seeking work. A rising unemployment rate can signal economic distress.

## 2.2.3 | THE EFFECTS OF INFLATION

- **Decrease of Purchasing Power:** As prices rise, the value of money decreases, meaning consumers can buy less with the same amount of money. This can lead to a decrease in the standard of living, especially if wages do not keep pace with inflation.
- **Impact on Savings and Investments:** Inflation erodes the real value of savings and fixed-income investments. For example, if the inflation rate is higher than the interest rate on a savings account, the real value of the saved money decreases over time.

- **Redistribution of Income:** Inflation can benefit borrowers (who repay loans with money that is worth less than when they borrowed it) and hurt lenders and fixed-income earners, such as retirees.
- **Uncertainty and Reduced Investment:** High or unpredictable inflation can create uncertainty about future costs and returns, leading to reduced investment by businesses and individuals.
- **Wage-Price Spiral:** Inflation can lead to a cycle where rising prices lead to demands for higher wages, which in turn lead to higher production costs and further price increases.

## ANALYZE THE IMPLICATIONS OF GOVERNMENT POLICIES

## 2.3.1 | THE IMPLICATIONS OF GOVERNMENT POLICIES IN CONTROLLING THE ECONOMIC SYSTEM

**a. National Savings**

National savings represent the total savings of a nation, including both private savings (from households and businesses) and public savings (from the government). Government policies that influence national savings include:

- Implications:
    - **Encouraging Savings:** Policies such as tax incentives for retirement savings accounts (e.g., EPF in Malaysia) or reducing taxation on interest income can boost national savings by encouraging individuals and businesses to save more.
    - **Investment Growth:** Higher national savings increase the pool of available capital for investment, promoting economic growth and development.
    - **Economic Stability:** Higher savings rates can help reduce reliance on foreign capital and improve economic stability, especially during economic downturns.

b. **Exchange Rate Policy**

Exchange rate policy involves government actions to influence the value of the national currency relative to other currencies. This can be done through fixed, floating, or managed exchange rate systems.

- Implications:
    - **Trade Balance:** By influencing exchange rates, the government can impact the competitiveness of exports and imports. A lower exchange rate can make exports cheaper and imports more expensive, improving the trade balance.
    - **Inflation Control:** Exchange rate policies can also affect inflation. A stronger currency can reduce the cost of imported goods, helping to control inflation, while a weaker currency can increase import costs, potentially leading to higher inflation.
    - **Foreign Investment:** Exchange rate stability is crucial for attracting foreign investment. Investors are more likely to invest in countries with stable and predictable exchange rates.


**c. Fiscal Policy and Taxation**

Fiscal policy involves government spending and taxation decisions to influence the economy. Taxation, a key component of fiscal policy, directly affects the disposable income of consumers and the profitability of businesses.

- Implications:
  - **Economic Growth:** Government spending on infrastructure, education, and health can stimulate economic growth by improving productivity and creating jobs. Conversely, higher taxes can reduce disposable income and consumption, potentially slowing down the economy.
  - **Income Redistribution:** Progressive taxation policies can help reduce income inequality by redistributing wealth from higher-income groups to lower-income groups through social welfare programs.
  - **Public Debt:** Excessive government spending without corresponding revenue can lead to high levels of public debt, which may require higher future taxes or spending cuts, potentially hindering long-term economic growth.

d. **Monetary Policy and Interest Rates**

Monetary policy refers to the actions of a central bank (such as Bank Negara Malaysia) to control the money supply and interest rates in the economy.

- Implications:
  - **Inflation Control:** By adjusting interest rates, the central bank can influence inflation. Higher interest rates typically reduce inflation by decreasing consumer spending and borrowing, while lower rates can stimulate economic activity but may lead to higher inflation.
  - **Economic Growth:** Lower interest rates make borrowing cheaper for consumers and businesses, encouraging investment and consumption, which can spur economic growth.
  - **Exchange Rates:** Interest rate adjustments can also impact exchange rates. Higher interest rates attract foreign investment, leading to an appreciation of the national currency, while lower rates can lead to depreciation.
  - **Employment Levels:** Lower interest rates can stimulate business investment and expansion, leading to job creation and lower unemployment rates. Conversely, higher interest rates may lead to reduced investment and consumer spending, which can slow down economic activity and result in higher unemployment levels.

### e. Wages Policy

Wages policy refers to government regulations and interventions that influence wage levels, such as minimum wage laws or collective bargaining agreements.

- Implications:

## INCOME DISTRIBUTION:

Minimum wage laws help ensure that workers earn a livable income, reducing poverty and income inequality. However, excessively high minimum wages can lead to unemployment if businesses cannot afford to pay higher wages.

## COST-PUSH INFLATION:

Increases in wages can lead to higher production costs for businesses, which may pass on these costs to consumers in the form of higher prices, contributing to inflation.


## LABOR MARKET EFFICIENCY

Wages policy can influence the allocation of labor across industries and regions. For example, higher wages in a particular sector may attract more workers to that industry, potentially leading to labor shortages in other sectors.

WHY LEGISLATION AND REGULATORY CONTROL IS VERY IMPORTANT IN FINANCIAL PLANNING?

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"It **protects consumers** and navigating complex financial landscapes."

COMMERCE DEPARTMENT,PSA

# Chapter 3: Legislation and Regulatory Control Affecting Financial Planning

## 3.1 | THE ROLES OF THE FOLLOWING AUTHORITIES IN REGULATING FINANCIAL PLANNING

**Bank Negara Malaysia (BNM)**
Bank Negara Malaysia (BNM) is the central bank of Malaysia and plays a crucial role in regulating the financial sector, including financial planning services. Its key responsibilities include:

- **Monetary Policy:** The BNM controls inflation and ensures economic stability by managing interest rates and the money supply.
- **Supervision and Regulation:** BNM oversees banks, insurance companies, and financial institutions to ensure they comply with regulations and operate soundly.
- **Consumer Protection:** BNM promotes transparency and fairness in financial services, ensuring that consumers are well-informed and treated fairly by financial institutions.
- **Development of Financial Markets:** BNM works to develop and enhance Malaysia's financial markets, making them more robust and competitive globally.

**In 2023, BNM hiked the Overnight Rate Policy (OPR) to 3% due to slowing economy and "tamed" inflation**

3% OPR remains unchanged until end of 2024

**Securities Commission (SC):** The SC is the regulatory authority responsible for overseeing Malaysia's capital markets. It ensures that the securities industry operates in a fair and transparent manner. Its roles include:

- **Regulating Securities and Futures Markets:** The SC sets rules and guidelines for market participants to ensure market integrity.
- **Protecting Investors:** The SC enforces regulations that protect investors from fraud and malpractice.
- **Facilitating Market Development:** The SC promotes the development of a vibrant and efficient capital market.

**Bursa Malaysia:** Bursa Malaysia is the Malaysian stock exchange where securities are traded. It plays a key role in financial planning by providing a platform for investment and capital raising. Its responsibilities include:

- **Market Regulation:** Ensuring that listed companies comply with listing requirements and that trading activities are conducted in an orderly manner.
- **Providing Market Access:** Facilitating the buying and selling of securities, including stocks, bonds, and derivatives, which are critical components of many financial plans.

**Labuan Offshore Financial Services Authority (LOFSA):** The Labuan Offshore Financial Services Authority (LOFSA), also known as Labuan FSA, is the regulatory body for the Labuan International Business and Financial Centre (IBFC). It oversees and regulates offshore financial activities, including banking, insurance, and investment services. Key roles include:

- **Regulating Offshore Financial Activities:** Ensuring that offshore entities comply with international standards and local regulations.
- **Promoting Labuan IBFC:** Developing Labuan as a premier offshore financial center, attracting international business and investment.
- **Supervising Compliance:** Monitoring the activities of offshore entities to prevent illegal activities such as money laundering and terrorism financing.

**Financial Mediation Bureau (FMB):** The Financial Mediation Bureau (FMB) provides a dispute resolution service for consumers and financial institutions in Malaysia. It helps resolve conflicts that arise from financial services in a fair and efficient manner. The FMB's roles include:

- **Mediation Services:** acting as a neutral party to help resolve disputes between consumers and financial institutions, such as banks and insurance companies.
- **Consumer Protection:** Ensuring that consumers have access to a fair process for resolving financial disputes without the need for costly and time-consuming legal proceedings.
- **Public awareness:** educating consumers about their rights and the mediation process, helping them make informed decisions in financial planning.

**Perbadanan Insurans Deposit Malaysia (PIDM):** PIDM is the deposit insurance corporation in Malaysia. It protects depositors by insuring their savings in the event of a bank failure. Its key roles include:

- **Deposit Protection:** PIDM insures deposits up to a certain limit, ensuring that depositors are compensated if their bank fails.
- **Financial Stability:** PIDM contributes to the stability of the financial system by maintaining public confidence in the banking system.
- **Risk Management:** PIDM assesses and monitors the risks faced by member institutions to prevent failures and ensure the protection of depositors

## THE LEGISLATION APPLICABLE TO FINANCIAL PLANNING.

### 3.2.1 | THE IMPORTANCE OF THE ACTS WITH REGARDS TO FINANCIAL PLANNING

**Financial Services Act, 2013 (FSA):** The Financial Services Act, 2013 (FSA) is a comprehensive piece of legislation that governs the regulation of financial institutions in Malaysia. Its importance in financial planning includes:

- **Regulation of Financial Services:** The FSA provides the framework for regulating financial institutions, ensuring they operate in a safe and sound manner.
- **Consumer Protection:** The Act includes provisions to protect consumers from unfair practices and ensure transparency in financial services.
- **Market Integrity:** The FSA promotes the stability and integrity of Malaysia's financial system, which is crucial for effective financial planning.

**Personal Data Protection Act, 2010 (PDPA):** The Personal Data Protection Act, 2010 (PDPA) is designed to protect the personal data of individuals in commercial transactions. Its relevance to financial planning includes:

- **Data Security:** The PDPA ensures that financial planners handle clients' personal data responsibly and securely, preventing unauthorized access and misuse.
- **Client Trust:** Compliance with the PDPA helps build trust between financial planners and clients, as clients are assured that their personal information is protected.
- **Legal Compliance:** Financial planners must adhere to the PDPA's regulations to avoid legal penalties and maintain their professional reputation.

**Anti-Money Laundering, Anti-Terrorism Financing, and Proceeds of Unlawful Activities Act, 2001 (AMLA):**
The Anti-Money Laundering Act, 2001 (AMLA) is aimed at preventing money laundering, terrorism financing, and other illegal financial activities. Its importance in financial planning includes:

- **Risk Management:** Financial planners must comply with AMLA to prevent being involved in or facilitating illegal activities, which can have serious legal and reputational consequences.
- **Due Diligence:** The Act requires financial planners to conduct thorough due diligence on their clients to ensure that they are not involved in money laundering or terrorism financing.
- **Compliance Requirements:** Financial planners must implement internal controls and reporting systems to detect and report suspicious activities as mandated by AMLA.

**Employees Provident Fund (EPF) Act, 1991:**
The EPF Act governs the Employees Provident Fund, which is a mandatory retirement savings scheme for Malaysian workers. Its code of ethics and rules include the following:

- **Responsibility:** Employers and employees are responsible for contributing to the EPF, ensuring that workers have savings for retirement.
- **Compliance:** Both employers and employees must comply with the regulations set out in the EPF Act, including timely and accurate contributions.

## THE CODE OF ETHICS AND RULES IN FINANCIAL PLANNING

## 3.3.1 | DESCRIBE THE CODE OF ETHICS AND RULES IN FINANCIAL PLANNING

**Persatuan Insurans Am Malaysia (PIAM):** PIAM is the General Insurance Association of Malaysia, representing all general insurers in the country. Its code of ethics emphasizes:

- **Professional Conduct:** Members must maintain high ethical standards and act in the best interest of clients.
- **Transparency:** ensuring that clients are fully informed about the terms and conditions of insurance products.
- **Accountability:** Members must be accountable for their actions and adhere to the laws and regulations governing the insurance industry.


**The Life Insurance Association of Malaysia (LIAM):** LIAM represents life insurance companies in Malaysia. Its code of ethics includes the following:

- **Integrity:** Life insurance agents and companies must conduct their business with honesty and integrity.
- **Client-Centric Approach:** The interests of clients must always come first, with products and advice tailored to their needs.
- **Confidentiality:** Maintaining the confidentiality of client information is paramount in life insurance practices.

**PIAM supports new standards vehicle repair for motor vehicles involved in accidents in compliance with the Road Transport Act 1987.**

It is to ensure the use of quality and safe repair methods

**Malaysian Takaful Association (MTA):** MTA is the association representing the takaful (Islamic insurance) industry in Malaysia. Its code of ethics focuses on:

- **Shariah Compliance:** All takaful products and practices must adhere to Shariah principles.
- **Fairness:** Takaful operators must treat all participants fairly and ensure that the benefits of takaful are equitably distributed.
- **Transparency:** ensuring that participants fully understand the terms and conditions of takaful products.
- **Confidentiality:** Not to disclose or utilize personal information, trademark, correspondence and member companies' accounts or business

**Malaysian Takaful Association (MTA) ensuring that all practices and products comply with Shariah (Islamic law) principles. MTA also plays a role in developing the takaful industry.**

**The Federation of Investment Managers Malaysia (FIMM):** FIMM regulates the unit trust and asset management industry in Malaysia. Its code of ethics includes the following:

- **Fiduciary Responsibility:** Investment managers must act in the best interest of their clients, with a duty of care and loyalty.
- **Professionalism:** maintaining high standards of professionalism and competence in managing clients' investments.
- **Transparency:** providing clear and accurate information to clients regarding their investments and the risks involved.

WHY ARE RISK MANAGEMENT AND INSURANCE PLANNING CONSIDERED ESSENTIAL?

# "Risk management and insurance planning are the **cornerstones of financial security**

COMMERCE DEPARTMENT, PSA

# Chapter 4: Risk Management and Insurance Planning

## THE CONCEPT AND MANAGEMENT OF RISK

### 4.1.1 | DESCRIBE THE CONCEPT OF RISK.

Risk refers to the uncertainty regarding potential outcomes, especially concerning the possibility of loss or damage.

In financial planning, risk is the possibility that an event or action will negatively impact an individual's financial goals. Understanding risk is crucial, as it helps individuals and businesses make informed decisions to protect their financial interests.

### 4.1.1 | THE MANAGEMENT OF RISK

**a. Risk Avoidance**

- **Definition:** Risk avoidance involves taking steps to eliminate the chance of a particular risk occurring. This strategy is used when the potential negative consequences are deemed too significant to tolerate.
- **Application:** For example, a business might avoid entering a market with high political instability to eliminate the risk of financial loss due to unpredictable regulations or unrest.

**b. Risk Control**

- **Definition:** Risk control involves taking measures to reduce the likelihood or impact of a risk. This can include both preventative and corrective actions.
- **Application:** Installing safety equipment in a factory reduces the risk of accidents (preventative), while having a disaster recovery plan in place helps mitigate the impact of a data breach (corrective).

**c. Risk Transfer Through Insurance**

- **Definition:** Risk transfer involves shifting the financial burden of a risk to another party, typically through insurance. By paying premiums, individuals or businesses transfer the risk to an insurance company, which assumes the financial responsibility in the event of a loss.
- **Application:** Purchasing health insurance transfers the risk of large medical bills from the individual to the insurance provider, ensuring financial protection in case of illness or injury.

## 4.2 | THE INSURANCE COVERAGE IN FINANCIAL PLANNING

**a. Life Assurance**

- **Purpose:** Life insurance provides financial security to beneficiaries in the event of a policyholder's death. It is a critical component of financial planning, ensuring that dependents are financially protected.
- **Types:** include term life insurance, whole life insurance, and endowment policies, each offering with varying benefits and coverage durations.

**b. Health and Liability Insurance**

- **Health Insurance:** provides coverage for medical expenses such as hospitalization, surgeries, and other healthcare bills. It reduces the financial burden on individuals and families during health crises.
- **Liability Insurance:** protects the policyholder against legal liabilities resulting from accidents, injuries, or damages caused to others. It is essential for both individuals and businesses to protect against potential lawsuits and financial losses.

**c. General Insurance**

- **Definition:** General insurance covers non-life assets and risks, including property, vehicles, and other possessions. It protects against damage or loss caused by incidents such as accidents, theft, natural disasters, and fire.
- **Application:** Homeowners insurance, auto insurance, and travel insurance are common examples of general insurance.

**d. Commercial Insurance**

- **Purpose:** Commercial insurance protects firms against a variety of hazards, such as property damage, liability claims, and business disruption. It ensures the continuity and financial stability of a business.
- **Types:** include product liability insurance, professional indemnity insurance, and business interruption insurance, among others.

## 4.2 | THE INSURANCE COVERAGE IN FINANCIAL PLANNING

**e. Takaful**

- **Definition:** Takaful is a type of Islamic insurance in which members contribute to a pool of cash that are used to compensate participants who experience losses. It functions on the ideas of mutual help and shared accountability, which are consistent with Shariah law.
- **Application:** Takaful, like conventional insurance, covers a wide range of risks, including life, health, and general insurance, but with an emphasis on ethical and religious conformity.

**The Malaysian Takaful Association (MTA) anticipates the takaful industry is expected to see better performance in 2024**

It is reflecting the overall economic growth projection of four percent compared to 3.7 percent in 2023.


**f. Education Policy**

- **Purpose:** An education policy is a savings plan designed to accumulate funds for a child's education. It provides financial security and ensures that the rising costs of education can be managed without financial strain.
- **Types:** These policies can be traditional savings plans or linked to investment products, offering both security and the potential growth of funds over time.

# ACTIVITY

## QUESTION 1

Ameena decided to purchase an insurance for her car but she has to take in account the deductible and excess insurance. Determine the amount payable by insurer and Ameena for the following claims.

| | Sum Insured RM600 | | Sum Insured RM1500 | |
|---|---|---|---|---|
| | Insurer | Ameena | Insurer | Ameena |
| Deductible (RM700) | | | | |
| Excess (RM400) | | | | |

## QUESTION 2

Nur Raffah Studio decided to purchase insurance for her premise. One day, the premise caught fire and the loss incurred by Nur Raffah Studio was RM26000. Determine the amount payable by the insurer and Nur Raffah Studio by filling out Table 1 below.

| | Sum Insured RM20,000 | | Sum Insured RM100,000 | |
|---|---|---|---|---|
| | Insurer | Ayesha Studio | Insurer | Ayesha studio |
| Deductible(RM5000) | | | | |
| Excess (RM2000) | | | | |
| Franchise (RM10000) | | | | |

HOW DOES INVESTMENT PLANNING BALANCE RISK AND REWARD TO ACHIEVE YOUR FINANCIAL GOALS?

5

"Investment planning is the **blueprint** for turning financial goals into reality

COMMERCE DEPARTMENT, PSA

# Chapter 5: Investment Planning

## THE CONCEPT OF INVESTMENT

### 5.1.1 | THE OBJECTIVES AND REWARDS OF INVESTING

Investment is the act of allocating resources, typically money, in order to generate an income or profit. The primary objectives and rewards of investing are as follows:

- **Capital Growth:** Investors aim to increase the value of their initial investment over time. This growth in capital provides the potential for wealth accumulation.
- **Income Generation:** Investments can generate regular income through dividends, interest, or rental income, providing a steady cash flow.
- **Inflation Protection:** Investing in assets that appreciate over time helps protect against inflation, preserving the purchasing power of money.
- **Retirement Planning:** Investments are often used to build a financial cushion for retirement, ensuring financial security in later years.
- **Wealth Preservation:** Strategic investments help conserve wealth and pass it on to future generations.

**Malaysia's foreign portfolio inflows of RM7bil in May 2024 was the largest in 10 months**

Inflows into equities saw a strong turnaround at RM1.5bil in May, while debt securities flows surged to RM5.5bil

### 5.1.2 | THE CONCEPT AND ADVANTAGES OF PORTFOLIO INVESTMENT

Concepts of Portfolio Investment:

- Portfolio investment involves diversifying investments across asset types, such as equities, bonds, and real estate, helps reduce risk and produce balanced returns.
- Instead of investing all funds in a single asset, investors spread their investments across various assets to minimize risk and increase potential returns.

Advantages of Portfolio Investment:

- **Risk Diversification:** Portfolio investment decreases overall risk by diversifying assets and mitigating the impact of poor performance on a single investment.
- **Potential for Higher Returns:** A well-diversified portfolio can achieve higher returns by capitalizing on the strengths of different asset classes.
- **Flexibility:** Portfolios can be tailored to meet specific investment goals, risk tolerance, and time horizons, offering flexibility to investors.
- **Stability:** Diversification gives the portfolio stability by allowing gains in one area to offset losses in another, resulting in smoother performance over time.

## THE PRIMARY INVESTMENT MARKET

## 5.2.1 | THE OVERVIEW OF VARIOUS PRIMARY INVESTMENT MARKETS

**a. Equity Market**

- **Overview:** Investors buy and sell shares of companies on the equity market, also referred to as the stock market. Investors purchase equity to gain ownership in a company and benefit from its growth through capital appreciation and dividends.
- **Characteristics:** Equity investments are typically higher-risk but offer higher potential returns. They are suitable for long-term investors seeking growth.

**b. Debt Market:**

- **Overview:** The debt market, or bond market, is where investors lend money to entities (governments, corporations) in exchange for periodic interest payments and the principal's return at maturity.
- **Characteristics:** Bonds offer constant income and are less risky than equities, making them ideal for conservative investors

**c. Foreign Exchange Market:**

- **Overview:** The Foreign Exchange (Forex) market is where currencies are traded. It is the world's largest financial market, with participants trading currencies for a number of purposes, including speculation, hedging, and international trade.
- **Characteristics:** The Forex market is highly liquid and operates 24/7. However, it is also volatile, requiring a deep understanding of global economic factors.

**d. Islamic Financial Products:**

- **Overview:** Islamic financial products, including banking, takaful (Islamic insurance), investment-linked products, and sukuk (Islamic bonds), adhere to Shariah principles, which prohibit interest (riba) and emphasize ethical investing.
- **Characteristics:** These products offer opportunities for Muslim investors to participate in the financial markets while adhering to their religious beliefs. They are also gaining popularity among non-Muslim investors seeking ethical investment options.

**e. Property Market:**

- **Overview:** The property market entails buying, selling, and renting real estate properties. This market includes residential, commercial, and industrial properties.
- **Characteristics:** Property investments can provide capital appreciation and rental income. They are considered relatively stable and can offer protection against inflation, but they require significant capital and involve liquidity risk.

## 5.2.2 | THE FACTORS TAKEN INTO CONSIDERATION WHEN COMPARING PRIMARY INVESTMENTS

When comparing primary investments, several factors must be considered:

- **Risk Level:** Different markets carry different levels of risk. For example, equities are generally riskier than bonds, while real estate may have liquidity risks.
- **Potential Return:** The potential return varies across asset classes. Equities may offer higher returns, while bonds and real estate may provide more stable, lower returns.
- **Time Horizon:** The investment duration has an impact on the asset choice. Longer time horizons allow for riskier investments, whereas shorter horizons may favor more conservative assets.
- **Liquidity:** The ability to convert an investment to cash without considerable loss of value is vital. For example, stocks are typically more liquid than real estate.
- **Economic Conditions:** Economic factors such as interest rates, inflation, and economic growth influence market performance. Understanding these conditions helps in making informed investment decisions.
- **Ethical Considerations:** For some investors, the ethical impact of their investments, such as adherence to Islamic principles or social responsibility, is a critical factor.

## MANAGED INVESTMENTS

Managed investments involve the professional management of investment portfolios on behalf of investors.

These can include mutual funds, unit trusts, and managed portfolios, where fund managers make decisions on asset allocation and security selection based on the investor’s goals and risk tolerance.

- Advantages:
  - **Expert Management:** Access to professional fund managers who have the expertise and resources to make informed investment decisions.
  - **Diversification:** Managed investments often provide instant diversification across different asset classes and geographies.
  - **Convenience:** Managed funds offer a hands-off approach to investing, where the investor does not need to actively manage their portfolio

## 5.3.1 | THE TYPES OF MANAGED INVESTMENTS

**a. Unit Trust**

- **Definition:** A unit trust is a type of collective investment scheme where investors pool their money together to invest in a diversified portfolio of securities, such as stocks, bonds, or other assets. The portfolio is managed by professional fund managers.
- **Key Features:** Investors purchase "units" in the trust, and their value fluctuates based on the performance of the underlying assets.

**b. Property Trust**

- **Definition:** A property trust, also known as a real estate investment trust (REIT), enables investors to combine assets and invest in real estate properties such commercial buildings, shopping centers, and residential complexes.
- **Key Features:** Investors benefit from rental income and capital appreciation on properties in the trust's portfolio.

> **The trustees of Amanah Saham Bumiputera (ASB) bought 27.76 million shares in Malayan Banking Bhd. ASB remains Maybank's largest shareholder with its 30.49% stake.**

**c. Equity Trust**

- **Definition:** An equity trust is a managed investment fund that primarily invests in stocks or equities. The goal is to achieve capital growth by investing in a diversified portfolio of shares in different companies.
- **Key Features:** Equity trusts are generally suited for investors with a higher risk tolerance, as the value of stocks can be volatile.

**d. Mortgage Trust**

- **Definition:** A mortgage trust is a type of managed investment that uses pooled funds to provide loans secured by mortgages on real estate properties. The trust earns returns on these loans' interest payments.
- **Key Features:** Mortgage trusts are typically considered lower risk than equity trusts, but they offer lower returns, focusing on income generation through interest.

**e. Life Insurance**

- **Definition:** Life insurance, particularly investment-linked life insurance, combines a death benefit with an investment component. The policyholder invests part of the premium in a managed fund, which has the potential to grow over time.
- **Key Features:** The investment component of life insurance can provide policyholders with a potential return, in addition to the protection offered by the death benefit.

## 5.3.2 | THE ADVANTAGES AND DISADVANTAGES OF MANAGED INVESTMENTS COMPARED TO PRIMARY INVESTMENTS.

### Advantages of Managed Investments:

- **Professional fund managers** oversee managed investments, leveraging their expertise in selecting and managing a diversified portfolio of assets. This reduces the need for individual investors to actively manage their investments.
- **Diversification:** Managed funds typically invest in a wide range of assets, which spreads risk and can lead to more stable returns over time.
- **Accessibility:** Managed investments often have lower entry costs than direct investments in primary markets, making them accessible to a broader range of investors.
- **Convenience:** Fund managers handle the day-to-day decision-making, allowing investors to participate in complex investment strategies.
- **Liquidity:** Many managed investments, such as unit trusts, offer greater liquidity than some primary investments, like real estate, allowing investors to buy and sell units more easily.

### Disadvantages of Managed Investments:

- **Management Fees:** Managed investments typically charge fees for the fund's professional management, which can lower overall returns. These fees may include management fees, performance fees, and other administrative expenses.
- **Lack of Control:** Investors in managed funds have limited control over the specific assets in which their money is invested, as decisions are made by the fund managers.
- **Potential for Lower Returns:** While managed investments provide diversification and professional management, they may not achieve the same high returns as more concentrated investments in individual assets, especially in a rising market.
- **Market Risk:** Managed investments are still subject to market risks, and the value of the fund can fluctuate based on the performance of the underlying assets, just like primary investments.
- **Diluted Returns:** The diversification that managed investments offer can sometimes dilute restoration, particularly in strong-performing sectors or assets where a concentrated investment might have yielded higher gains.

# ACTIVITY

## QUESTION 1

Doug invested $2,500 into a Certificate of Deposit earning a 6.5% interest rate. How long will it take Doug's investment to double?

## QUESTION 2

Jessica has a $2,200 balance on her credit card with an 18% interest rate. If Jessica chooses to not make any payments and does not receive late charges, how long will it take for her balance to double?

## QUESTION 3

Jacob currently has $5,000 to invest in a car after graduation in 4 years. What interest rate is required for him to double his investment?

## QUESTION 4

Rhonda is 22 years old and would like to invest $2,500 into a U.S. Treasury Note earning 7.5% interest. How many times will Rhonda's investment double before she withdraws it at age 70?

## QUESTION 5

George is in the 33% tax bracket. He would like to invest $100,000. George is comparing two accounts that have a 6% interest rate. The first is a taxable account charging interest earned. The second account is tax deferred until he withdraws the money. Which account should George invest his money into?

WHAT ARE THE KEY BENEFITS OF EFFECTIVE TAX PLANNING FOR INDIVIDUALS AND BUSINESSES?

# 6

# "Income tax planning **minimizes taxes** and **maximizes savings**."

COMMERCE DEPARTMENT, PSA

# Chapter 6: Income Tax Planning

## THE BASIC TAX CONCEPT

## 6.1.1 | DESCRIBE THE FOLLOWING TAXATION TERMINOLOGIES:

**a. Basis of Assessment**

- **Definition:** The basis of assessment refers to the method and period used by tax authorities to determine the taxable income for an individual or business. It typically involves assessing income earned during a specific tax year or period.
- **Application:** In Malaysia, the basis period for income tax is usually the calendar year, with taxes assessed on income earned within that year.

**b. Residency**

- **Definition:** Residency status determines how an individual or entity is taxed in a particular country. A resident is normally taxed on worldwide income, but a non-resident may only be taxed on income earned within the country.
- **Application:** In Malaysia, an individual's residency status for tax purposes is determined by the number of days spent in the country during a tax year, with residents enjoying certain tax benefits and lower tax rates compared to non-residents.

**SSPN depositors will continue to enjoy income tax relief of up to RM8,000 for the assessment year 2014**

Simpan SSPN is a choice for Malaysian looking to save for a higher education.

**c. Calculation of Gross Income**

- **Definition:** Gross income refers to the total income earned by an individual or entity before any deductions, exemptions, or taxes are applied. It includes income from various sources such as salary, business profits, rental income, dividends, and interest.
- **Application:** Gross income is the starting point for calculating taxable income, and all potential income sources must be accurately reported to the tax authorities.

**d. Deductions**

- **Definition:** Deductions are specific expenses or allowances that can be subtracted from gross income to reduce taxable income. Common deductions include business expenses, charitable donations, and specific allowances granted by the tax authorities.
- **Application:** In Malaysia, deductions might include expenses like medical costs, education fees, and contributions to approved retirement schemes, which help lower the overall tax liability.

**e. Reliefs**

- **Definition:** Reliefs are specific amounts or reductions provided by the tax law to lessen the tax burden on individuals and entities. These may include personal reliefs, spouse reliefs, and child reliefs.
- **Application:** For example, in Malaysia, individual taxpayers can claim reliefs for personal expenses such as life insurance premiums, EPF contributions, and expenses related to the education of children.



**f. Tax Computation**

- **Definition:** Tax computation is the process of calculating the amount of tax owed by applying the relevant tax rates to the taxable income after all deductions and reliefs have been taken into account.
- **Application:** In Malaysia, tax is computed using a progressive tax rate, where higher income levels are taxed at higher rates, culminating in the determination of the final tax payable or refundable.

**g. Real Property Gains Tax (RPGT)**

- **Definition:** RPGT is a tax imposed on the gains arising from the disposal of real property, such as land or buildings, within a specified period. It is a form of capital gains tax.
- **Application:** In Malaysia, RPGT is charged on the profit made from the sale of property, with different rates depending on the holding period and the type of property sold.

## 6.2.1| FACTORS OF CONSIDERATION IN INCOME TAX PLANNING:

**a. Income Splitting**

- **Definition:** Income splitting involves distributing income among different family members or entities to reduce the overall tax burden. By spreading income across individuals or entities taxed at lower rates, the total tax liability can be minimized.
- **Application:** In Malaysia, income splitting might involve transferring assets or income-producing investments to a spouse or children, who may have a lower tax rate, thus reducing the family's overall tax burden.

**b. Income Deferment**

- **Definition:** Income deferment is the practice of delaying the receipt of income to a later tax year when the taxpayer expects to be in a lower tax bracket, thus reducing the tax payable on that income.
- **Application**: For example, a business owner in Malaysia might defer invoicing clients until the next tax year if they anticipate being in a lower tax bracket or if tax rates are expected to decrease.


**c. Acceleration of Deductible Claims**

- **Definition:** This involves bringing forward deductible expenses into the current tax year to reduce taxable income and, therefore, the tax liability for that year.
- **Application:** In Malaysia, taxpayers might accelerate payments for expenses like rent, insurance, or business-related costs to claim the deduction in the current year, thereby reducing the current year's taxable income.

# ACTIVITY

## QUESTION 1

The information about Mr. Wong is as follows:

- Age: 32 years old
- Annual income: RM 57,000
- Dependents: Wife (unemployed), 1 child
- Approved contribution:
    i. Insurance premium: RM 2,500
    ii. Education and MHI premium: RM 1,800

He owns an apartment, collects a rental of RM3,600 a year, and pays RM600 a year for the management fees. He bought books for RM400 and a tablet for RM1,800. He also donated RM2,000 to an approved charity. Assume EPF at 11% of gross salary, and figure out the tax payable for Mr. Wong for the year of assessment of 2023.

## QUESTION 2

Azim purchased a house on 5th November 2017 for RM210,000 and sold it on 10th November 2022 for RM300,000. He also incurred an additional cost of RM24,000 for the first renovation of the house.

| YEAR OF DISPOSAL | TAX RATE |
|---|---|
| Within 3 years | 30% |
| $4^{th}$ year | 20% |
| $5^{th}$ year | 15% |
| After $5^{th}$ year | 0 |

Based on the Real Property Gain Tax (RPGT) schedule above, find the RPGT tax payable.

"HOW CAN THE PRINCIPLES OF PROACTIVE PLANNING AND THOUGHTFUL LEGACY-BUILDING, AS HIGHLIGHTED IN THESE QUOTES, BE APPLIED TO ENSURE BOTH A FULFILLING RETIREMENT AND A MEANINGFUL ESTATE PLAN?"

7

"**Creating money on a daily basis** is the finest approach to forecast your future".

COMMERCE DEPARTMENT, PSA

# Chapter 7: Retirement Planning/ Estate Planning

## THE RETIREMENT PLANNING

### 7.1.1 | DESCRIBE THE METHODS TO CALCULATE RETIREMENT INCOME

Retirement planning refers to financial strategies of saving, investments and ultimately distributing money meant to sustain oneself during retirement.

There are two ways to estimate the funds needed for a comfortable retirement: Income Replacement Ratio Method Adjusted Expense Method

**a. Income Replacement Ratio**

- **Definition:** This method recognises that most people will be spending less on certain expenses during retirement. As a guide, aim for two-thirds to three-quarters of your income to live comfortably.
- **Example:** Say Ali want to replace 75% of his current income. If he currently earn RM60,000 per year, and his desired retirement age is 62.

Annual retirement income needed
75% x RM60,000 = RM45,000
**Men:** 83-62 = 21
**Women:** 88-62 = 26 Years in retirement (life expectancy - retirement age)
Total retirement income needed
**Men:** RM45,000 x 21 = RM945,000
**Women**: RM45,000 x 26 = RM1,170,000

**b. Expense Method**

- **Definition:** This method may increase, or some decrease, while others vary as the people grow older. So, it is important to review expenses before and during retirement.
- **Example:** If you need RM3,000 per month at retirement, and your desired retirement age is 62.

Annual retirement income needed
RM3,000 x 12 = RM36,000
**Years in retirement** (life expectancy - retirement age)
**Men:** 83-62 = 21
**Women:** 88-62 = 26
Total retirement income needed
**Men:** RM36,000 x 21 = RM756,000
**Women:** RM36,000 x 26 = RM936,000


### 7.1.2 | THE AMOUNT OF INCOME NEEDED DURING RETIREMENT

The general rule of thumb is that the person needs two-thirds of their last drawn income to maintain the same standard of living which is have pre-retirement. Meaning if Azmir earn RM7,500 a month during his last year of work, he will need RM5,000 a month when he retire otherwise, he will have to downsize y lifestyle.

## 7.1.3 | IDENTIFY THE CURRENT INCOME SOURCES

- **Employees Provident Funds (EPF) Savings:** a crucial component of retirement planning in many countries, particularly in Malaysia and Singapore. It's a savings plan where both employees and employers contribute a portion of the employee’s salary to a fund, which is then used to provide financial security during retirement.

- **Private Retirement Schemes (PRS) :** a voluntary long-term savings and investment scheme designed to help the people save more for your retirement.

## 7.1.4 | STRATEGIES FOR FILLING RETIREMENT INCOME DEFICIT

- Use the bucket strategy to divide retirement savings, ensuring funds are available when needed.
- Systematic withdrawals, like the 4% rule, can adjust based on performance and inflation.
- Consider annuities for guaranteed income; evaluate fees and potential returns first.


## 7.2 | DETERMINE THE ESTATE PLANNING PROCESS

## 7.2.1 | THE FUNCTION OF ESTATE PLANNING

The preparation of tasks that serve to manage an individual's asset base in the event of their incapacitation or death. The planning includes the bequest of assets to heirs and the settlement of estate taxes. Most estate plans are set up with the help of an attorney experienced in estate law.

## 7.2.2 | THE ROLE PLAYED BY AN ESTATE PLANNER

- **Executor-** someone who carries out the directions in the will.
- **Guardian-** A Guardian needs to be appointed to raise the child in the event both parents die before the child becomes an adult.
- **Agent (DPOA)-** A durable power of attorney (DPOA), you give authorization to a certain person, or people, to make decisions on your behalf when you are not physically or mentally capable.
- **Agent (Health Care)-** The health care agent receives a durable power of attorney for health care, which gives your agent the power to make medical decisions if you are incapacitated or unable to make medical decisions.
- **Trustee-** If you create a revocable living trust, you will name a trustee, or co-trustees, to manage your assets.

## 7.2.3 | DESCRIBE THE TECHNIQUES FOR PRESERVING WEALTH

1) Prepare a will
2) Use estate tax exclusion
3) Title all assets to avoid probate
4) Monitor retirement plan assets
5) Gift assets that whose do not need to family members
6) Keep enough assets liquid to satisfy y estate taxes
7) Refrain from naming estate as the beneficiary for life insurance
8) Know what assets you have and where you have them
9) Meet with a financial advisor

## 7.2.4 | EXPLAIN THE ROLE OF LIFE INSURANCE IN ESTATE PLANNING

1 . To provide liquidity in an estate to pay off liabilities such as taxes or mortgages. This will ensure that non-liquid assets, such as a cottage or business, do not have to be sold, but can be left to beneficiaries.

2 . To establish a fund to provide income for an individual wish to support.

3 . To make a donation to charity.

## 7.2.5 | THE TYPES OF TRUSTS

**Asset Protection trust:** a legal arrangement designed to shield assets from creditors, lawsuits, or other financial threats. It's often used to safeguard wealth from potential future claims while allowing the trust creator to retain some level of control or benefit from the assets.

**Insurance trust:** An insurance trust is an irrevocable trust set up with a life insurance policy as the asset, allowing the grantor of the policy to exempt assets away from his or her taxable estate.

**Insurance trust:** An irrevocable trust set up with a life insurance policy as the asset, allowing the grantor of the policy to exempt assets away from his or her taxable estate

**Ecucational trust:** A type of trust specifically designed to fund educational expenses for beneficiaries, such as children or grandchildren.

## 7.2.6 | THE ROLES OF VARIOUS PARTY IN WILL WRITING

1**) Attorney:** takes care of the complicated legal rules, to ensure that your spouse retains a certain amount of property after your death.
2) **Professional will writing company:** specializes in drafting, preparing, and managing wills and related estate planning documents and also focus on ensuring that clients' wishes are legally documented and that their estates are handled according to their desires.
3) **Amanah Raya Berhad:** If the person die without leaving a valid Will, the estate may not be distributed. It makes financial sense. It gives the opportunity to help those less fortunate to intended beneficiaries.
4) **Islamic will writing:** involves creating a will that complies with Islamic principles and Sharia law, ensuring that a Muslim's estate is distributed according to their religious beliefs and legal requirements.

## 7.2.7 | EXPLAIN THE ROLE OF SYARIAH LAW IN RELATION TO ESTATE PLANNING

**a. Faraid:**

- Islamic laws of inheritance, as prescribed by the Quran and Hadith, which dictate how a deceased person's estate should be distributed among their heirs.
- The term comes from the Arabic word "fard," meaning obligation, and is a crucial part of Islamic estate planning.

**b. Calculation Of Faraid**

- **Spouse:**
- 1/8 if the deceased has children.
- 1/4 if there are no children.

- **Parents:**
- Each parent receives 1/6 if there are children.
- If no children, the mother receives 1/3, and the father receives the remainder.

- **Children:**
- Sons receive twice the share of daughters.

**c. The agnatic heirs**

- relatives who inherit under Islamic inheritance laws through the male line.

- This concept is central to Islamic inheritance law and ensures that property is distributed among relatives who share a common paternal ancestry.

**d. The Asabah- remainder man**

- a group of heirs who inherit the remainder of the estate after the fixed shares have been distributed to other heirs.
- The term “Asabah” translates to “those who are entitled to inherit due to their kinship” and primarily includes male relatives who inherit based on their close relationship to the deceased.

e. Baitulmal

- "House of Wealth" or "Treasury" in Arabic.
- The state treasury responsible for managing public finances and distributing resources according to Islamic principles.

# ACTIVITY

## QUESTION 1

Explain **TWO (2)** objectives of retirement.

## QUESTION 2

Describe the steps to be taken to set up a retirement plan.

## QUESTION 3

When Azwan wants to plan for a retirement, he should start as early as possible. Discuss this statement.

## QUESTION 4

EPF and PRS are isntitutions that provide members and their dependent with the form for retirement in the future age. Describe THREE (3) differences between these two institution.

## QUESTION 5

Explain the distinction between a Will made by a Muslim and a non- Muslim.

## QUESTION 6

Define **THREE (3)** causes for inheritance under Faraid.

## QUESTION 7

Estate planning is a way to save your heirs' money and headaches. Do you agree with this statement. Justify your answer.

HOW CAN YOU DESIGN FOR A FINANCIAL PLAN IN YOUR LIFE?

# 8

"**Fortune favors** the prepared mind."

COMMERCE DEPARTMENT, PSA

# Chapter 8: Designing a Financial Plan

## THE PROCESS IN DESIGNING A FINANCIAL PLAN

## 8.1.1 | DESCRIBE THE FINANCIAL PLANNING PROCESS

a. **Understanding the client:**

- a crucial step in designing a personalized financial plan.
- It involves gathering and analyzing information about the client's financial situation, goals, preferences, and values to create a strategy that is tailored to their specific needs.

There are several steps as below:

1. **Conduct a comprehensive financial assessment**

- Objective: obtain a thorough understanding of the client's current financial situation.

**2. Identify financial goals and objectives**

- Objective: Understand what the client wants to achieve with their financial plan.

**3. Assess risk tolerance on customer profile**

- Objective: Gauge how much risk the client is willing to take with their investments and their preferences.

**4. Know all client values and lifestyle.**

- Objective: Align the financial plan with the client's personal values and lifestyle preferences.

**b. Data gathering:**

- The process where you gather all of your financial statements and personal documents that will, together, form the basis of your personalized financial plan.

- a critical first step in designing a financial plan. It involves collecting detailed information about the client's financial situation, goals, and preferences to ensure that the plan is accurate and tailored to their needs.

c. **Analysis of financial data**

- a critical step in developing a sound financial plan. This process involves interpreting the information gathered about a client's financial situation to understand their financial health, identify areas for improvement, and develop strategies to meet their goals.

Steps:

- Net Worth Calculation:

Formula: Net Worth = Total Assets - Total Liabilities

**Analysis:** A positive net worth indicates financial stability, while a negative net worth suggests that liabilities exceed assets.

Cash Flow Analysis:

- **Formula: Cash Flow** = Total Income - Total Expenses

Tools:

- **Financial Statements:** Use balance sheets to calculate net worth and cash flow statements to track income and expenses.

- **Financial Ratios:** Apply ratios like the savings rate (savings/income) and debt-to-income ratio (total debt/income) for a detailed analysis.

**d. Understanding strategies to meet needs**

- Understanding and implementing strategies to meet a client's financial needs involves developing a comprehensive plan that addresses their specific goals, circumstances, and preferences. There are several strategies as below:

- **Set Clear Goals:** Identify what you want to achieve, like saving for retirement or buying a home.
- **Create a Budget:** Track your income and expenses to ensure you're living within your means and saving for your goals.
- **Save and Invest:** Build an emergency fund, save regularly, and invest wisely according to your risk tolerance and goals.
- **Manage Debt:** Pay off high-interest debt first and consider consolidating if it helps.
- **Get Adequate Insurance:** Ensure you have the right insurance to protect against financial risks, like health or life insurance.
- **Plan for Taxes:** Use strategies to minimize your tax bill and make the most of deductions and credits.
- **Prepare for the Future:** Update your will and estate plan to ensure your assets are distributed according to your wishes.
- **Plan for Retirement:** Save and invest for retirement to ensure you can support yourself when you stop working.
- **Review Regularly:** Check your financial plan often and make adjustments as needed based on changes in your life or goals.

e. **Preparation of plan:**

1. **Gather Information**
   - Collect Data: Gather detailed information about income, expenses, assets, liabilities, insurance, tax situation, and financial goals.
   - Understand Goals: Discuss and define the client's short-term, medium-term, and long-term financial goals.
2. **Analyze the Data**
   - Assess Financial Health: Calculate net worth and evaluate cash flow to understand financial stability.
   - Review Budget: Analyze spending patterns and budgeting habits to identify areas for improvement.
   - Evaluate Investments: Assess the performance, risk, and alignment of current investments with the client's goals.
   - Examine Debt: Review debt obligations and create a strategy for managing and reducing debt.
3. **Develop Strategies**
   - Budget and Cash Flow Management: Create or adjust a budget to ensure savings and investment goals are met.
4. **Prepare the Plan Document**
   - Draft the Plan: Create a detailed document that outlines the financial analysis, strategies, and action steps.
   - Include Recommendations: Provide specific recommendations for budgeting, saving, investing, debt management, and other financial areas.
   - Set Goals and Timelines: Define clear objectives and timelines for achieving the client's financial goals.

**5. Review and Finalize**

- Present the Plan: Share the draft plan with the client, explaining each section and recommendation.
- Gather Feedback: Address any questions or concerns the client may have and make necessary adjustments.
- Finalize the Plan: Make final revisions based on client feedback and provide a completed financial plan.

**6. Implement and Monitor**

- Implement Strategies: Assist the client in taking action on the plan's recommendations, such as setting up savings accounts, adjusting investments, or updating insurance.
- Monitor Progress: Regularly review the plan's progress and make adjustments as needed to stay on track with goals.

**7. Communicate Regularly**

- Schedule Reviews: Set up periodic meetings to review the plan, assess progress, and make adjustments based on any changes in the client's circumstances or goals.

**f. Implementation of plan**

- a financial plan involves putting the strategies and recommendations outlined in the plan into action.

There are several steps as following below:

- Defining and agreeing your financial objectives and goals.
- Gathering your financial and personal information.
- Analysing your financial and personal information.
- Development and presentation of the financial plan

**g. Process review**

A process review is essential for evaluating the effectiveness of a financial plan and making necessary adjustments. It involves assessing how well the plan is performing and ensuring that it remains aligned with the client's goals and changing circumstances. Here's a simplified guide to conducting a process review:

**1. Schedule Regular Reviews**

- **Set Review Dates: Plan periodic reviews based on the client's needs, typically quarterly or annually.**
- **Prepare Documentation: Gather relevant financial documents and performance reports before the review meeting.**

**2. Assess Performance**

- Review Goals: Check if the client's financial goals are being met. Compare current progress with the objectives set in the plan.

**3. Update Financial Information**

- Gather New Data: Collect updated information about income, expenses, assets, liabilities, and any changes in personal circumstances.

**4. Identify Issues and Opportunities**

- Spot Issues: Look for any discrepancies or areas where the plan is not performing as expected.
- Find Opportunities: Identify new opportunities for improving financial performance, such as investment adjustments or tax-saving strategies.

**5. Adjust the Plan**

- Modify Strategies: Update investment strategies, savings plans, or debt repayment approaches based on the review findings.
- Revise Goals: Adjust financial goals if there have been significant changes in the client's circumstances or objectives.

## 8.2 | DETERMINE A FINANCIAL PLAN FOR A GIVEN SITUATION

Mei, who is 30 years old, married with one child, and lives in Kuala Lumpur. Mei earns RM8,000 per month and has some debts, a mortgage, and various financial goals.

Scenario

- Income: RM8,000 per month
- Expenses: Monthly expenses include mortgage (RM1,500), utilities (RM300), groceries (RM600), credit card payments (RM400), personal loan (RM200), and other expenses (RM500).
- Assets: Emergency fund (RM5,000), savings account (RM15,000), investments (RM20,000)
- Liabilities: Mortgage balance (RM250,000), personal loan (RM15,000), credit card debt (RM5,000)
- Financial Goals:
    - Short-Term Goals: Save RM10,000 for a family vacation within 2 years.
    - Medium-Term Goals: Save RM40,000 for child’s education by the time the child is 18 years old.
    - Long-Term Goals: Build a retirement fund with a target of RM500,000 by age 60.

. Gather and Analyze Information

A. Financial Data Collection

- Income: RM8,000 per month
- Expenses: Total monthly expenses = RM1,500 (mortgage) + RM300 (utilities) + RM600 (groceries) + RM400 (credit cards) + RM200 (personal loan) + RM500 (other) = RM3,500
- Monthly Surplus: RM8,000 - RM3,500 = RM4,500

B. Financial Goals

- Short-Term: Save RM10,000 in 2 years (approx. RM417 per month)
- Medium-Term: Save RM40,000 in 18 years (approx. RM185 per month)
- Long-Term: Save for retirement target of RM500,000

2. Assess Financial Health

A. Net Worth Calculation

- Assets: RM5,000 (emergency fund) + RM15,000 (savings) + RM20,000 (investments) = RM40,000
- Liabilities: RM250,000 (mortgage) + RM15,000 (personal loan) + RM5,000 (credit cards) = RM270,000
- Net Worth: RM40,000 - RM270,000 = -RM230,000 (negative net worth)

B. Cash Flow Analysis

- Monthly Surplus: RM4,500 (positive cash flow available for saving and investing)

3. Develop a Budget and Savings Plan

A. Create a Budget

- Essential Expenses: RM3,500 per month
- Savings Allocation: Prioritize saving and debt repayment from the RM4,500 surplus
    - Emergency Fund: Increase to RM10,000
    - Vacation Savings: RM10,000 target in 2 years (approx. RM417 per month)
    - Child’s Education: RM40,000 target (approx. RM185 per month)

B. Allocate Savings

- Emergency Fund: Save RM500 per month until reaching RM10,000
- Vacation Fund: Save RM417 per month
- Child's Education: Save RM185 per month

4. Investment Strategy

A. Retirement Savings

- Current Contribution: If not contributing, start with 10% of salary (RM800 monthly)
- Investment Accounts: Utilize EPF (Employees Provident Fund) contributions, and consider additional investments in mutual funds or unit trusts.

B. Investment Allocation

- Emergency Fund: Keep in a high-yield savings account or short-term fixed deposits.
- Retirement Accounts: Contribute to EPF and explore private retirement schemes.
- Education Savings: Consider a trust fund or an education savings plan for better growth and tax benefits.

5. Debt Management

A. Prioritize Debt Repayment

- Credit Cards: Focus on paying off the RM5,000 balance quickly, allocating an additional RM500 per month towards it.
- Personal Loan: Continue making minimum payments or consider refinancing options to lower interest rates.
- Debt Repayment Plan
- Credit Card Payments: Allocate RM500 per month towards credit card debt.
- Personal Loan: Maintain current payment schedule or increase payments as debt decreases.

6. Insurance and Risk Management

A. Evaluate Coverage

- Health Insurance: Ensure adequate coverage for the family through private health insurance or employer-provided plans.
- Life Insurance: Obtain a policy with sufficient coverage, such as term life insurance.
- Disability Insurance: Consider if not already in place to protect against loss of income.

7. Tax Planning

A. Optimize Tax Strategies

- EPF Contributions: Maximize contributions to EPF to benefit from tax relief.
- Tax Reliefs: Take advantage of available tax reliefs for education, insurance, and savings.

B. Adjust Withholdings

- Review tax withholdings to ensure they align with projected tax liabilities.

8. Estate Planning

A. Prepare Documents

- Will: Create or update a will to specify the distribution of assets.
- Trusts: Consider setting up a trust if necessary for estate planning and asset protection.

B. Review Beneficiaries

- Update beneficiary designations on insurance policies and EPF accounts.

9. Monitor and Review

A. Regular Check-ins

- Schedule Reviews: Set up annual or semi-annual meetings to review financial progress and make necessary adjustments.
- Track Performance: Monitor savings, investments, and debt reduction progress.

# ACTIVITY

## QUESTION 1

Alex, 40 years old, is married with two children. He earns RM12,000 per month and has a mortgage with a balance of RM400,000. His total debt includes RM15,000 in personal loans and RM5,000 in credit card debt. Alex wants to save RM20,000 for a family vacation in 3 years, RM100,000 for his children's education in 10 years, and build a retirement fund with a target of RM1,000,000 by age 65. He currently has RM10,000 in savings and RM30,000 in investments. His monthly expenses total RM6,000. Develop a comprehensive financial plan including goal setting, savings, investment, debt management, and review strategies.

## QUESTION 2

The Tay family consists of Mr. Tan, 45 years old, his spouse, Ms. Mei, 43 years old, and their two children, aged 12 and 8. They live in Kuala Lumpur and both are employed full-time. Mr. Tan earns RM15,000 per month as a senior manager, while Ms. Mei earns RM8,000 per month as a marketing executive.

Financial Situation:

- Income:
  - Mr. Tan: RM15,000 per month
  - Ms. Mei: RM8,000 per month
  - Total Household Income: RM23,000 per month

Additional Information:

- Mr. Tan and Ms. Mei have a combined retirement savings of RM80,000 in their EPF accounts.
- They are considering purchasing a new car in 3 years, which they estimate will cost RM60,000.
- Mr. Tan has a term life insurance policy with RM500,000 coverage, and Ms. Mei has a policy with RM300,000 coverage.
- They are both covered under their employer's health insurance plans.

Questions:

- Calculate the Tay family's monthly surplus or deficit based on their income and expenses.
- Determine their current net worth by assessing their assets and liabilities.

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