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New Development in Corporate Pension Schemes in Japan

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1. Introduction

Japanese retirement plan world is facing a big change because of the two sets of upcoming legislation. One is Defined Contribution (DC) bill that will introduce DC plans into Japan for the first time, and the other is Defined Benefit (DB) Corporate Pension bill that will re-organize DB plan schemes in Japan. The purpose of this paper is to explain the reason why these change will be brought about and the contents of the new DC bill and DB Corporate Pension bill.

2. The Current Japanese Retirement Systems

The current Japanese retirement system consists of the four-tiered systems as is shown in the figure 1. The first and the second tiers are the social security system. The third tier is employer-sponsored retirement plans. The forth tier is individual savings and annuities.

The first tier, National Pension, covers all people and offers the fixed benefits regardless of your pre-retirement income. If you continue to pay premiums for 40 years, you can receive the maximum benefit (the current level is 65,000 yen per month). The current premiums are 13,300 yen per month. Although Japanese social security is operated as pay-as-you-go system, there are some accumulated assets. National Pension has the assets of 8.6 trillion yen. (Exchange rate these days are around 120 yen per U.S. dollar.)

The second tier, Employee’s Pension Insurance, offers benefits which are proportional to your pre-retirement income. This is the second-tier social security system for private employees, and the premiums depend on their income. It has the assets of 118.5 trillion yen. The second tier for public employees, Mutual Aid Pension, is operated separately from Employee’s Pension Insurance. It has the assets of 45.1 trillion yen. There is the dedicated second tier retirement system for self-employed, National Pension Fund, with the assets of 800 million yen. Participation in National Pension Fund is voluntary.

The third tier is employer-sponsored retirement plans. Historically Japanese companies have paid lump-sum retirement money when employees leave companies. This lump-sum retirement plans are book-reserved system. When DB plans were introduced during the mid 1960’s in Japan, many companies transferred a part or all portion of the lump-sum retirement plan benefits into DB plans for the purpose of taking advantage of the tax benefits of DB plans as well as of averaging cash outflows. Currently there are two kinds of DB plans in Japan, Employee’s Pension Fund and
Qualified Pension Plan. Both are different in terms of regulatory body, plan management, benefits requirement, taxation, and so on. The comparison of the two DB plans appears in the figure 2. Employee’s Pension Fund has the assets of 51.3 trillion yen and Qualified Pension Plan has the assets of 20 trillion yen.

The forth tier is individual savings and annuities, which are sold mainly by life insurance companies and post offices. Property Accumulated Pension Saving Plan is a kind of employee benefit plans provided by employers for their employees where employees can contribute after-tax money up to the certain limits.


DC bill has gone through a rough route so far. It was supposed to pass in the ordinary Diet session in June 2000, and DC plans were expected to be introduced in Japan in January 2001. However, following the sudden death of then Prime Minister Keizo Obuchi, the diet was dissolved before DC bill was discussed. The bill was submitted again in the fall of 2000 in the extraordinary session of the Diet. However, it died again because of the shortage of discussion time.

The latest schedule for legislation is as follows: DC bill and DB Corporate Pension bill are to be discussed and enacted in the current ordinary Diet Session. The session began January and lasts until June 29th, 2001. Then regulations of DC Act will be made public a few month later, probably around July. Following that, DC Act will take effect and employers can establish DC plans as soon as November 1st. Regulations of DB Corporate Pension Act will be made public sometime in 2001 and the act will take effect April 1st, 2002. These schedules can change if bills do not pass in the current Diet session.

4. Background for DC Plan Introduction to Japan

The discussion that DC plans are needed in Japan began from the side of employers around 1996 or 1997. Due to the poor investment environments these days in Japan, employers have had to make additional contributions to existing DB plans to cover promised benefits to employees. But most employers have difficulties in doing so in the sluggish Japanese economy.

In addition to this, new accounting rules similar to Financial Accounting Standard No. 87 in the U.S. took effect March, 2001. Under-funded DB plans and liabilities of book reserve lump-sum
retirement plans have negative effects on the company’s balance sheet, which can lead to
downgrade of credit ratings and fall of stock prices of the companies. As a result, many employers wanted to replace current DB plans with DC plans because they thought DC can solve these problems. They do not intend to implement DC plans on top of the existing DB plans. They look upon DC plans as replacement of DB plans. All that employers want to do is just to shift investment risks from employers to employees. They have intention to continue to be a major contributor to retirement plans. As a result of these employers requests, Japanese DC plans look like money purchase plans in the U.S., not 401(k) plans with employee contributions a major source of funds. The comparison between U.S. and Japanese DC plans is illustrated in the figure 3.

Although the discussion that DC is necessary in Japan came from financial and accounting aspects of employers, these days some employers look DC plans from a different angle, human resource standpoint. More companies gave up seniority-pay systems these days and switched to performance-based pay systems. Traditional retirement plans which favors long-time workers are not in line with them. Labor market is getting mobile these days even in Japan, but employees with short-term services lose with the traditional retirement plans which favors longtime workers. Employers need new measures to attract workers in a liquid labor market. DC plans are regarded as suitable retirement plans for these changes.

Some say that DC plan introduction is good especially for small-to-medium companies. Old-age benefits of the social security system are expected to be decreased because of the rapid aging and the declining labor force of Japanese society. Larger companies can compensate for the shortfalls in the social security system by making their retirement plans rich, but many small-to-medium companies have no pension plans. DC plans are easy for small-to-medium companies to adopt because the cost of maintaining DC plans are predictable and because employers will not suffer from additional funding requirements in the adverse investment environments with DC plans. DC plans are expected to be adopted by small-to-medium companies. This is another reason leading to DC plan introduction in Japan.

5. Japanese DC plans.

Japanese media call DC plans Japanese-version of 401(k) plans, but they are different as is shown in the figure 3. There will be two types of DC plans in Japan, one is Employer-sponsored Type, and the other is Individual Type. One person can participate in either of them. You cannot
participate in both of them at the same time.
Employer-sponsored Type is similar to money purchase plans in the U.S.. Contributions come only from employers, and the amounts of contributions are fixed regardless of employers’ profits. Employees cannot contribute to the plan from their pay.

On the other hand, in Individual Type, employees or self-employed can contribute to the plan from their pocket money at their discretion. It is similar to 401(k) plans or IRA in the U.S.. But employers cannot make matching contributions to Individual Type DC plans. This is the different feature from 401(k) plans.

Figure 4 shows eligibility and contribution limits of Japanese DC plans. Not all Japanese can participate in DC plans. Public employees and housewives (to be precise, dependent spouses of employees) are not eligible for participation.

Private employees are eligible for Employer-sponsored Type if their employer sponsors DC plan. There are two kinds of contribution limits for Employer-sponsored Type DC plans. If your employer sponsors DB plans at the same time, individual limits are 18 thousand yen per month. Otherwise limits are doubled, 36 thousand yen per month.
If your employer does not sponsor a DB plan nor an Employer-sponsored Type DC plan, you are eligible to participate in Individual Type DC plans. The limit then is 15 thousand yen per month. Self-employed can participate in Individual Type DC plans, too, and their limit is 68 thousand yen per month. But this limit is aggregated with the premiums to National Pension Fund explained above.

Figure 5 is a summary flow-chart explaining which type you are eligible for and how much the contribution limits are.

6. Employer-sponsored Type DC Plans

Figure 6 shows who play what kind of roles in Employer-sponsored Type DC plans. The operation of Employer-sponsored Type DC plans is handled by “plan administrator”, “trustee”, and “investment managers”. Employers (plan sponsors) can handle plan administrative jobs by themselves if they wish. But they can hire registered plan administrators and outsource to them such functions as record-keeping and providing various information to participants.
Plan administrator functions are defined in the DC bill as follows:
**Recordkeeping related Function**
- Recordkeeping participants’ individual data and inform participants of their account balances periodically
- Receiving each participant’s investment direction
- Making decisions on whether to pay benefits

**Investment related Function**
- Selecting investment options for the plan
- Providing information about investment options to participants

Trust banks and insurance companies become trustees. Agricultural Cooperative Association and Employee's Pension Fund can be trustees, too.

The following pages describe requirements of plan designs of Employer-sponsored Type DC plans under the DC bill.

**Eligibility**
Those who are 60 years old or younger and who are covered by Employee’s Pension Insurance (social security system) should be participants if employers implement DC plans. Being a participant means receiving contributions. Insured of Employee’s Pension Insurance whose age is over 60 years old is not eligible to participate in DC plans. Employees who are not insured of Employee’s Pension Insurance are also not eligible to participate in DC plans even though they are under 60 years old. The latter includes part-time workers. Employers can cover a limited group of employees with DC plans if it is not discriminatory. For example, the new DC plan covers only newly-hired employees while the existing DB plan covers current employees. This treatment is regarded as non-discriminatory. The overall standard for non-discrimination rule is unknown as of this writing. It will be provided in regulations, or it will be examined case-by-case by the regulatory body when companies prepare plan documents.

**Contribution formula**
Contribution formula must be fixed percentage of participants’ pay or fixed amount for every participant. In any case the amount of contributions for every participant must be within the contribution limits (18,000 or 36,000 yen per month).

**Investment Options**
There are some requirements for investment options. There must be at least three investment options for diversification purpose. Bank deposits, bonds, stocks, mutual funds (investment
trusts), insurance products will be used as investment options. One of the investment options must be a capital guaranteed product. However, the definition of a capital guaranteed product is not decided yet and is expected to be stipulated in the regulation. Participants must be given opportunities to change investment direction every three months. Plan administrators have to provide information on account balances to participants at least once a year.

**Participant Education**
As is the case with DC plans where investment decision are made by participants, it is important to give enough information for participants to make a sound investment decision. Japanese DC bill categorizes such information into three types, “Explanation about DC Plans”, “Basic Investment Theory” and “Information of Investment Options”.

DC bill stipulates who are responsible for giving such information. Providing “Explanation about DC Plans” is plan sponsors’ legal obligation. They have to explain how DC plans work and what the contents of the plan documents of the company are.

Plan sponsors should provide “Basic Investment Theory” on the best efforts basis, but it is not their legal obligation. Such knowledge as relationship between risks and returns, diversification, and dollar-cost-averaging will be given to participants.

Providing “Information of Investment Options” is plan administrators’ legal obligation. Information on each option’s structure, historical performances, risk/return profiles, and so on will be given to participants.

No regulation is schedule to be made in the near future regarding the distinction between investment education and investment advice.

**Benefit Events**
One of the controversial issues in Japanese DC plans is benefit events. As is explained above, most employers consider DC plans as replacement of current retirement plans. They do not intend to add a DC plan on top of the current plan. They think DB plan or DC plan, not DB plan and DC plan. But benefit events are different between the two plans.

You cannot receive benefits from DC plans until you reach 60 years old with over 10 years of participation. This means that when you leave the company, you cannot receive benefits unless you are 60 years old or more. You just rollover your account balance to new employer’s DC plan or to Individual Type DC plan before you attain the age of 60. As it were, this is a mandatory rollover. You have no choice whether to receive cash or rollover them to another plan at termination of employment. This characteristics completely differs from the U.S. DC plans where participants have discretion on whether to receive cash or rollover them to another plans or IRA
when they leave companies.
This mandatory rollover rule might be inconvenient to some employees who want to receive cash payments when they quit jobs. With the current DB plans, they can receive cash when they leave. However, if their employer switches from the current plan to a DC plan, it is no longer possible. This difference in benefit events between the existing plan and a DC plan would make labor negotiation in introducing DC plans very difficult.
The reason why participants cannot receive benefits until age 60 is because the tax authority required distinction between savings and old age benefits as a condition to give tax benefits to DC plans. DC plans look like savings to the tax authority because individual accounts exist in DC plans. They think that if you can receive cash at your 40’s or 50’s when you leave companies, it is just a savings. The history of Japanese taxation is a history of taking incentives away from savings in order to stimulate spending. They conclude that if you start receiving benefits at 60 years old, it is not savings but old age benefits. As a result, tax benefits can be provided.

However, there is an exception to “age 60 requirement”. When you lose eligibility within 3 years or less of becoming a participant for such reasons as becoming a housewife, you can receive cash payment from a DC plan at termination of employment. The purpose of this exception is to eliminate burdens of keeping records and holding assets of short-time participants with small amounts of account balances for long time. This rule is similar to the small amount provision of the U.S. pension rule although Japanese rule defines in terms of length of participation, not an amount of benefits.

Participants can start receiving benefits any time between 60 and 70 years old. When they reach age 70 years old, they have to receive benefits. Benefits are paid in the form of installment. However, all or parts of benefits can be paid as lump-sum if it is allowed in the plan documents.

Other than attaining age 60, there are two benefit events, severe disability and death. In the case of severe disability, participants start receiving benefits any time between the day becoming severe disability and 70 years age. Benefits are paid in the form of installment. However, all or parts of benefits can be paid as lump-sum if it is allowed in the plan documents. In the case of death, benefits are paid to survivors of participants in the form of lump-sum.

**Vesting Rules**
Vesting Rules are defined for the first time in Japanese retirement plan history. With 3 years of service, participants are 100% vested in Employer-sponsored Type DC plans. Participants can be partially vested within 3 years if the plan documents provide so, like 50% vested after 1 year of
service, 75% vested after 2 years of service, and 100% vested after 3 years of service. Employers are not allowed to forfeit once employees attain at least 3 years of service. In other words employers are allowed to forfeit the accumulated assets of employees who leave the company with 3 years or less service.

Some employers feel uneasy with this vesting rule because currently employers can change the amount of benefits depending on the reason why employees leave the company. If employees did bad thing and leave the company, employers can reduce benefits or pay nothing at their discretion. Employers no longer have this kind of “free-hand” on benefits with DC plans.

7. Individual Type DC Plans

In Individual Type DC plans, you decide whether to participate in DC plans, how much to contribute to plans, and which plan administrator you choose. Figure 7 shows who play what kind of roles in Individual Type DC plans. Each plan administrator prepares a packaged product with certain investment options selected in advance. National Pension Fund Association, government agency, play a role of the trustee of Individual Type DC plans. If you are an employee, your employer deducts contributions from your pay and remits to National Pension Fund Association. If you are a self-employed, paying premiums to National Pension (social security system) is a condition to participate in Individual Type DC plans. Although National Pension is mandatory for a self-employed, one-third of them are said not to be paying premiums to National Pension. National Pension Fund Association will decide the eligibility for your participation in DC plans by checking whether you are paying premiums to National Pension or not. Once you are deemed to be eligible, you remit DC plan contributions directly to the Association by yourself.

8. Portability & Rollover

As is explained above, rollover is mandatory unless you are over 60. When participants in Employer-sponsored Type DC plans change jobs, their account balances must be rolled over to a DC plan of a new employer. If there are no DC plan with a new employer or if participants become self-employed, their account balances are rolled over to Individual Type DC plans. When participants in Individual Type DC plans change jobs to become an employee, their account balances must be rolled over to a DC plan of a new employer. If there are no DC plan with a new employer, their account balances remains with Individual Type DC plans.
9. Taxation on DC Plans

Figure 8 describes taxation on Japanese DC plans. Contributions are deductible. With Employer-sponsored Type DC plans employers can deduct contributions in preparing tax returns and employees are not taxed on contributions. With Individual Type DC plans individuals can deduct contributions from their taxable income.

Investment earnings are tax-deferred. However, Special Corporate Tax applies on participants’ asset balances regardless of whether they gain or lose on investment. Tax rate is 1.173% on asset balances. This tax has a huge negative impact on retirement asset accumulation, considering the current adverse investment environments in Japan. Taking this situation into account, Special Corporate Tax is politically suspended until March 31, 2003. There is a strong voice among employers that Special Corporate Tax should be abolished. However, it is unclear at present whether this tax survives beyond March 31, 2003.

Rollover is tax-free. When you receive benefits, benefits are taxable. But some deductions apply before you reach taxable income. Appendix 1 shows these deductions. You will find that lump-sum payment is very advantageous in Japan.

10. DC Market Activities & Outlook

Many financial institutions are forming joint ventures to offer DC-related services in Japan. There are two companies developing recordkeeping system, NRK-Nippon Record Keeping- and JIS&T - Japan Investment Service & Technology-. Due to large capital investments, most financial institutions have joined either of the two recordkeeping companies. For example, Mitsubishi group, Sumitomo group, Nippon Life, Daiwa Securities, and Nikko Securities will use NRK’s recordkeeping system. Nomura Securities, Mizuho group, Mitsui group, UFJ group, and Daiichi Life will use JIS&T’s recordkeeping system.

Another type of joint ventures offers employee education and plan design consulting services.

Japanese DC plans will grow in the long run, but the short time prospects for the market growth is expected to be moderate. The reasons why rapid growth is not expected are as follows;

As to Employer-sponsored Type DC plans, low contribution limits (18,000 or 36,000 yen per month per capita) as well as the fact that no employee contributions are allowed will lead to slow asset accumulation. It will be possible to transfer accumulated assets from the existing DB plans or book reserve retirement plans to DC plans, but there would be tight restrictions in doing so although the
conditions for the transfer are not yet made public.

Individual Type DC plans will grow even more slowly. Few people show interests in Individual Type DC plans. The discussion of introducing DC plans in Japan came from employers who suffered from adverse investment environments. That is why we foresee demands for Employer-sponsored Type DC plans. However, we have never heard self-employed say “Yes, we want DC plans.” It seems that self-employed can enjoy the largest contribution limits (68,000 yen per month). The truth is that contribution limits for self-employed are aggregated with premiums to National Pension Fund. Self-employed with high income level like doctors and accountants are said to be paying premiums to National Pension Fund up to the limits. As a result, there are no rooms for them to make contributions to DC plans. Self-employed with medium-to-low income level are not interested in either the existing National Pension Fund nor maybe DC plans because tax benefits are not attractive at all for them who are not paying income taxes. One third of self-employed are said not to be paying premiums to social security system which is the condition for them to participate in DC plans. This condition will reduce the potential number of self-employed participants.

Employees with no DB plans or Employer-sponsored Type DC plans can join Individual Type DC plans. However, the contribution limits are the lowest, 15,000 per month per capita. Considering all these facts, Individual Type DC plans will show very slow growth.

Individual Type DC plans accept rollover money, but only from DC plans not from DB plans. It is just money transfer among DC plans and does not contribute to the DC asset growth.

Nippon Life Insurance Company, the largest insurance company in Japan, foresees that DC assets for both types combined will be 16.5 trillion yen and participants will be 8.6 million in 10 years. Daiichi Life Insurance Company, the second largest insurance company in Japan, foresees that DC asset for both types combined will be 18.0 trillion yen in 10 years.

11. Problems with Japanese DC Plans

There are some obstacles for Japanese DC plans to grow rapidly in the future. The following describes these issues.

Contributions
The appendix 2 explains the reason why contribution limit is said to be low, using actual figures. The assumption is that you receive the maximum contributions, 18 thousand yen, from the start of
your employment (age 22) until age 60 with investment returns of 3%, 4%, and 5% each. These investment returns are realistic now in Japan. With 3% investment returns, your DC assets at age 60 will be about 15 million yen. The average amount of lump sum retirement benefits for undergraduate degrees is around 28 million yen in Japan. DC plans cover only 55% of them. Even with higher investment return scenarios, 4% and 5%, DC plans cannot cover 100% of the current level of retirement benefits.

Another problem with DC contributions is that employee contributions are not allowed in Employer-sponsored Type DC plans. Since some DB plans allow employee contributions, this fact discourages some employers to adopt DC plans.

In the U.S. matching contributions have contributed to the increase in employee contributions, thus leading to the growth of 401(k) plans. However, matching contributions are not allowed in Individual Type DC plans in Japan although they are strongly requested.

**Benefit & Rollover**

Limited benefit events coupled with mandatory rollover is not a good news as is explained before. If you work for a company with a DC plan and then move to a company with only a DB plan, all you can do is just to rollover your account balance to Individual Type DC plans. You cannot withdraw money from them. You cannot even contribute to Individual Type DC plans because you are covered with DB plans (Self-employed or employees without DB plans and Employer-sponsored Type DC plans are eligible for Individual Type DC plans). Your account balance grows only with investment earnings until age 60. If you become a housewife or a public employee, the same thing happens. Your money are rolled over to Individual Type DC plans and grow only with investment returns.

Individual Type DC plans accept rollover money only from Employer-sponsored Type DC plans, not from DB plans or book-reserve lump-sum retirement plans. If DC plans are expected to become a major retirement vehicle in the upcoming mobile society where people often change jobs and take retirement money with them, Individual Type DC plans should have a function as a temporary parking lot like the U.S. IRA that accepts rollover money from both DB and DC plans.

All these features with Japanese DC plans are very user-unfriendly. Some improvements have to be made for Japanese DC plans to become a major retirement plan in the future.

**Japanese Attitude toward Investment**

Most Japanese are risk averse. It is said that Japanese are generous with low interest rates, but not generous with negative investment returns. For example, Japanese get angry when their 100 yen
becomes 99 yen, but they do not get angry when their 100 yen earns only 1 yen per year. Some employers are hesitant in adopting DC plans because they fear that employees might complain to employers about their investment failures even though employees make investment directions. It takes much time to change Japanese from savers to investors. Investment education will play a big role here. Others say that teaching Japanese about investment is easy because Japanese educational level is uniformly high. They say that Japanese just lack opportunities to make decisions on their money so far. According to them, once Japanese learn how to do with it, Japanese can easily become good investors.

**Economic Environment**
Current low interest rates and sluggish stock market result in few attractive investment options for DC plans in Japan. The U.S. 401(k) plan growth have come with the strong comeback of the U.S. industries in the 90’s. Japanese economic recovery is necessary for DC plans to grow and for Japanese to retire with enough retirement provision in the future.

**Limited Participants**
Public employees and housewives are not eligible to participate in DC plans. There are currently few job changes between public sector and private sector in Japan. But in the future this will change, and public employees should be able to participate in DC plans.

**Special Corporate Tax**
Special Corporate Tax is peculiar to Japan. It is unrealistic to levy 1.173% tax on the assets, considering the current 10-year government bond yield is only around 1.4%. That is why the tax is temporarily suspended for another two years. However, with Japanese government’s budget deficits, it is not easy to eliminate Special Corporate Tax forever. Eliminating Special Corporate Tax will be discussed in conjunction with eliminating the existing generous tax deductions for retirement benefits that are shown in Appendix 1. However, eliminating the existing tax deductions for retirement benefits is another tough job because there are already retired people who are enjoying these tax deductions. The number of retired people will be increasing as baby boomers will retire in the near future. They will oppose to eliminating tax deductions for retirement benefits. Thorough examination and restructuring of Japanese taxation system on retirement money is necessary.

Appendix 3 is a comparison sheet between U.S. 401(k) plan and Japanese employer-sponsored DC plan.
12. Defined Benefit Corporate Pension Bill

Now we switch the topic from DC bill to DB Corporate Pension bill. The purpose of the DB Corporate Pension bill is to unify regulations and taxation for DB plans and to enhance protection of vested benefits for participants. There are currently two DB schemes in Japan, Employee’s Pension Fund and Qualified Pension Plans. They are different in many ways as are shown in the figure 2. Both schemes have some problems at present.

Employee’s Pension Funds must substitute a portion of social security old-age benefits, which are proportional to your pay. Employers with this plan want to eliminate this substitution and to return it to Government. Because of adverse investment environments most Employee’s Pension Funds are under-funded. Although this substitution is actually a part of social security system, employers have to pay additional money to compensate for the under-funded substituted portion. Many employers and trade groups have been lobbying for introducing new Employee’s Pension Funds which have no substituted portion of social security system. DB Corporate Pension Bill will create a new DB scheme, Fund Type Defined Benefit Plan. Fund Type DB plan is the same as Employee’s Pension Fund except that there is no substituted portion.

In terms of protecting vested benefits, Qualified Pension Plans have problems because plan operation is not strictly regulated. There are no rules to check the funding status with this plan. Most Qualified Pension Plans are said to be under-funded, but there are no rules to examine funding status numerically. Many Qualified Pension Plans have been terminated these days without enough assets to pay benefits. Government considered that they have to strengthen the operational rules of Qualified Pension Plans to enhance protection of rights of participants and beneficiaries. DB Corporate Pension Bill will create another new DB scheme, Contract Type Defined Benefit Plan, to replace existing Qualified Pension Plans. Qualified Pension Plans have to be terminated within 10 years from the date the DB Corporate Pension Act take effect. DB Corporate Pension Act is scheduled to take effect on April 1, 2002.

To protect vested benefits of participants and beneficiaries, DB Corporate Pension bill borrows some provisions from Employees Retirement Income Security Act (ERISA) of the U.S.
First of all, minimum funding rules will be introduced. Funding status of plans must be checked every year, and additional contributions must be made if plans are regarded as under-funded. On the other hand, contributions have to be suspended if plans are over-funded over certain limits. Fiduciary duties will be defined and disclosure of plan operations to participants will be required in DB Corporate Pension bill.

However, plan termination insurance will not be introduced soon because larger employers have been opposing to its introduction saying that they do not want to pay extra money to save unhealthy company’s pension plans.

Figure 9 illustrates the operation of the two new types. The main difference between the two types is whether Employee’s Pension Fund, separate entity from employers, exists or not. However, rules of plan design will be the same as follows:

Contributions
Employers make contributions to fund plan assets. Employees can contribute to the plans at their discretion if plan documents allow them to do so.

Benefits
Form of benefits are lump-sum or installments that will have to be paid over the period of 5 years. Benefit payments begins between age 60 and 65. Plan sponsors must provide installment payment options for employees who works over certain years. This number must not be over 20 years. If employees work over 3 years, some benefits must be paid from the plans.

Taxation
The taxation of the two new DB schemes are almost the same as DC plans. Employers can deduct contributions and employees are not taxed on contributions. If employees contribute to the plans, Life Insurance Premiums Deduction (up to 50 thousand yen per year) will apply for employee contributions to reduce taxable income of employees. Investment earnings are tax-deferred. However, Special Corporate Tax applies on the plan assets regardless of whether they gain or lose on investment. Benefits are taxable, but the same deductions apply as is the case with DC plans.

Switching among different schemes
Currently plan sponsors can switch from Qualified Pension Plan to Employee’s Pension Fund, but not vice versa. DB Corporate Pension bill will allow plan sponsors to switch among several different schemes including DC plans as is shown in the figure 10.
From the standpoint of employers DB Corporate Pension bill will bring in more regulations in operating DB plans and increase the costs of maintaining the plans. For employees the bill will strengthen their rights for benefits. The history of the U.S. with ERISA tells us that the more rules and regulations, the more terminations of DB plans. It is too soon to predict what will become of Japanese DB plan world after DB Corporate Pension Act take effect, but DB bill might become a driving force for the growth of DC plans even in Japan.

As of this writing, both DC bill and DB Corporate Pension bill have not been enacted nor regulations are not made public. Readers are urged to collect the latest information on these bills.