<table>
<thead>
<tr>
<th>Title</th>
<th>New Development in Corporate Pension Schemes in Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Author(s)</td>
<td>Urata, Haruka</td>
</tr>
<tr>
<td>Citation</td>
<td></td>
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<td>URL</td>
<td><a href="http://hdl.handle.net/10086/14525">http://hdl.handle.net/10086/14525</a></td>
</tr>
</tbody>
</table>
**Figure 1: Current Retirement Systems in Japan**

*Number of participants in parentheses*

<table>
<thead>
<tr>
<th>4th tier</th>
<th>Individual Annuity (20 million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual Savings</td>
<td>Property Accumulation Pension Saving <em>(Zaikei-nenkin)</em> (3 million)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>3rd tier</th>
<th>Employee’s Pension Fund <em>(Kosei-nenkin-kikin)</em> (12 million)</th>
<th>Qualified Pension Plan <em>(Tekikaku-nenkin)</em> (10 million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate-Sponsored</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>2nd tier</th>
<th>National Pension Fund (0.9 million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Portion proportional to compensation</td>
<td>Employee’s Pension Insurance <em>(Kosei-nenkin)</em> (33 million)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>1st tier</th>
<th>National Pension <em>(Kokumin-nenkin)</em> (70 million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic Portion</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Self-employed (20 million)</th>
<th>Spouses of category 2 (12 million)</th>
<th>Private Employee (33 million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category 1 insured persons</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>Spouses of category 3 insured persons</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Employee (5 million)</td>
<td>(特約労働者・就労代行労働者)</td>
</tr>
</tbody>
</table>
### Figure 2: Existing DB Schemes in Japan

<table>
<thead>
<tr>
<th></th>
<th>Employee’s Pension Fund</th>
<th>Qualified Pension Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Regulatory Body</strong></td>
<td>Ministry of Health, Labor and Welfare</td>
<td>Ministry of Finance</td>
</tr>
</tbody>
</table>
| **Substitution of Social Security** | Yes  
A portion of Employee’s Pension Insurance (social security) benefits which are proportional to your pay is provided by Employee’s Pension Fund | No                                                   |
| **Plan Management**      | Plan sponsors must establish a separate entity, Employee's Pension Fund, to manage plans | Plan sponsors make a contract with providers, such as life insurance companies and trust banks, to manage plans |
| **Form of Benefit**      | Life annuities must be provided                               | Life annuities are not necessarily required            |
| **Contribution**         | - Employer contribution : deductible (no limit)  
- Employee contribution : deductible as Social Security Premium Deduction (no limit) | - Employer contribution : deductible (no limit)  
- Employee contribution : deductible as Life Insurance Premium Deduction (¥ 50,000 annual limit) |
| **Taxation**             | **Investment**                                                |                                                       |
|                          | - No tax on investment earnings                              | - No tax on investment earnings                        |
|                          | - Special Corporate Tax is NOT imposed on the asset balance up to the certain limit  
<Taxation is suspended until March 2003> | - Special Corporate Tax (1.173%) is imposed on the asset balance.  
<Taxation is suspended until March 2003> |
| **Benefit**              | - Annuity : taxable, but Deduction for Annuity Payments applies | - Lump-sum : taxable, but Deduction for Lump-sum Payment applies & separately taxed |
### Money Purchase Plans
Contributions are fixed regardless of company profits.

### Profit Sharing Plans
Contributions can be changed at employers’ discretion.

### 401(k) Plans
Employees choose whether to participate and how much to contribute from their pay.

Employers make matching contributions.

### IRA (Individual Retirement Account)
Individuals make contributions at their discretion.

---

**Figure 3: U.S. DC Plans vs. Japanese DC Plans**

<table>
<thead>
<tr>
<th>U.S.</th>
<th>Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Employer-sponsored Type DC</strong></td>
<td><strong>Employee</strong></td>
</tr>
<tr>
<td>Contributions are fixed regardless of company profits.</td>
<td>Employees cannot make contributions.</td>
</tr>
<tr>
<td>Employees choose whether to participate and how much to contribute from their pay.</td>
<td>Employees make contributions at their discretion.</td>
</tr>
<tr>
<td>Employers cannot make matching contributions.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Individual Type DC</strong></th>
<th><strong>Employer</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Employees choose whether to participate and how much to contribute from their pay.</td>
<td>Employees make contributions at their discretion.</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Figure 4: Eligibility and Contribution Limits

- **Individual Type DC**
  - Self-employed
  - Contribution Limit: 68,000yen/month minus contribution to National Pension Fund

- **Employer-sponsored Type DC**
  - Employee of the company without DB plan nor Employer-sponsored DC plan
  - Contribution Limit: 36,000yen/month
  - Employee of the company without DB plan
  - Contribution Limit: 15,000yen/month
  - Employee of the company with DB plan
  - Contribution Limit: 18,000yen/month

- **National Pension**
  - Portion Paid by employer
  - Mutual Aid Pension

- **Not eligible for DC**
  - Employee of the company without DB plan
  - Employee of the company with DB plan

- **Eligibility and Contribution Limits**
  - Spouses of category 2
    - Category#3 insured
  - Self-employed and other individuals
    - Category#1 insured
  - Employee of private corporation, etc
  - Public Employee

- **Employee’s Pension Insurance**
**Figure 5: Eligibility of DC Plan -Flow-chart-**

- **Employee of Private Corporation**
  - **<less than 60 years old>**
    - Employer DOES run any DB Plan
      - Employer DOES run Employer-Sponsored DC
        - Participate in Employer-Sponsored DC
          - **18,000yen/month**
      - Employer DOES NOT run Employer-Sponsored DC
        - Not Eligible for either Employer-sponsored DC or Individual DC
          - **No Eligibility**
    - Employer DOES NOT run any DB Plan
      - Employer DOES run Employer-Sponsored DC
        - Participate in Employer-Sponsored DC
          - **36,000yen/month**
      - Employer DOES NOT run Employer-Sponsored DC
        - Eligible for Individual DC
          - **15,000yen/month**

- **Self-employed**
  - **<less than 60 years old>**
    - Eligible for Individual DC
      - **68,000yen/month**
      - Net of the contribution to National Pension Fund

- **Public Employee**
  - House-wives
    - Not Eligible for either Employer-sponsored DC or Individual DC
      - **No Eligibility**
Figure 6: Who Play What Kind of Roles in Employer-sponsored Type DC?

Plan Sponsor

Employee A
Employee B
Employee C

Investment Direction by each Employee

Plan Administrator

Gather each Investment Directions
Provide Plan Information
Provide Information related to Investment Products

Investment Manager A
Investment Manager B
Investment Manager C
Investment Manager D
Investment Manager E

Trustee

Contributions

Recordkeeping

Beneficiary

Benefit Claim Forms
Benefit Payment

Benefit Payment Instructions

Either all or part of plan administrator's role could be handled by plan sponsor.
Figure 7: Who Play What Kind of Roles in Individual Type DC?

- Self-employed A
- Self-employed B
- Plan Sponsor
- Payroll Deduction (Basic Arrangement)
- Employee A
- Employee B
- Beneficiaries

National Pension Fund Association

Selection

- Application / contribution
- Benefit Payment
- Benefit Claim Forms

Outsourced Financial Institutions

Plan Administrator A
- Gather investment directions
- Recordkeeping

Plan Administrator B
- Present investment options line-up
- Provide information of investment options

Plan Administrator C

Investment Directions

Investment Manager “A”

Investment Manager “B”

Investment Manager “C”

Investment Manager “D”

Investment Manager “E”
**Figure 8: Tax on Defined Contribution Plans**

**Contributions**

- **Employer-sponsored Type**
  - Employers can deduct contributions
  - Employees are not taxed on contributions

- **Individual Type**
  - Individuals can deduct contributions from their taxable income

**Investment Earnings**

- Deferred until benefit payments
- Special Corporate Tax (1.173%) on the assets balance is levied
  - However, it is suspended through March 31, 2003

**Rollover**

- Tax-free

**Benefit Payments**

- Old Age Benefit
  - Taxable
  - However, different deductions apply respectively for annuity payments and lump sum payment in calculating taxable income.
- Disability Benefit
  - Tax-free
- Survivors Lump Sum
  - Subject to inheritance tax
- Early Withdrawal Lump Sum
  - Subject to income tax
Appendix 1: Deductions for Benefits

1. **Deductions for annuity payments**

   - When receiving in the form of annuities, the following deductions apply.
   - All annuities from social securities, DB plans, DC plans are combined before applying the deductions.

<table>
<thead>
<tr>
<th>Age 65 or more</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount of Annuities</td>
</tr>
<tr>
<td>Less than 2.6 mil yen</td>
</tr>
<tr>
<td>2.6mil - 4.6mil yen</td>
</tr>
<tr>
<td>4.6mil – 8.2mil yen</td>
</tr>
<tr>
<td>More than 8.2mil yen</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Less than 65 Years Old</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount of Annuities</td>
</tr>
<tr>
<td>Less than 1.3 mil yen</td>
</tr>
<tr>
<td>1.3mil - 4.1mil yen</td>
</tr>
<tr>
<td>4.1mil – 7.7mil yen</td>
</tr>
<tr>
<td>More than 7.7mil yen</td>
</tr>
</tbody>
</table>

2. **Deductions for lump-sum payment**

   - When receiving lump-sum payment, the following deductions apply.
   - All lump-sum money from retirement benefits, DB plans, DC plans are combined before applying the deductions.

   - The amount remaining after the deductions should be divided by 2 to reach the taxable income.
   - Separately taxed.

<table>
<thead>
<tr>
<th>Years of Service</th>
<th>Deductions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to 20 years</td>
<td>Years times 0.4mil yen</td>
</tr>
<tr>
<td>Beyond 20 years</td>
<td>Years over 20 times 0.7mil yen + 8mil yen</td>
</tr>
</tbody>
</table>

<Examples>
- If you work for 10 years  4 mil yen (10 x 0.4mil)
- If you work for 20 years  8 mil yen (20 x 0.4 mil)
- If you work for 30 years  15 mil yen ((30-20)x0.7+8 mil yen)
### Appendix 2: Benefit Projection

**Assumptions:**
You receive the maximum contributions from the start of your employment (age 22) until age 60.

<table>
<thead>
<tr>
<th>Contribution Amount</th>
<th>Investment Return</th>
<th>Assets at Age 60</th>
<th>Comparison with the average benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>18,000 Yen per Month</td>
<td>3%</td>
<td>15.28 Million Yen</td>
<td>55%</td>
</tr>
<tr>
<td>(216,000 Yen per Year)</td>
<td>4%</td>
<td>19.23 Million Yen</td>
<td>69%</td>
</tr>
<tr>
<td></td>
<td>5%</td>
<td>24.45 Million Yen</td>
<td>87%</td>
</tr>
</tbody>
</table>

Note: Salary and retirement benefit data is from Japan Federation of Employers Associations research of September 1998.
## Appendix 3: Comparison of U.S. 401(k) and Japanese Employer-Sponsored DC

<table>
<thead>
<tr>
<th></th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Who May Contribute</strong></td>
<td>Employees &amp; Employers (matching contributions / discretionary contributions)</td>
<td>Employers Only</td>
</tr>
<tr>
<td><strong>Annual Contribution Limit</strong></td>
<td>Pre-tax Employee Contribution Limit: $10,500 (in 2001)</td>
<td>Employer Contribution Limit: 432,000 yen for employer without DB plan</td>
</tr>
<tr>
<td></td>
<td>Aggregate DC Contribution Limit: Lower of $35,000 or 25% of pay</td>
<td>216,000 yen for employer with DB plan</td>
</tr>
<tr>
<td><strong>Eligibility</strong></td>
<td>All employees 21 years or older with at least 1 year of service must be allowed to join a plan. Maximum age requirements are prohibited</td>
<td>To be determined by plan rules</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Participants must be less than 60 years old</td>
</tr>
<tr>
<td><strong>Vesting</strong></td>
<td>Employee contributions: immediately 100% vested</td>
<td>Minimum requirement: 100% vesting after 3 years.</td>
</tr>
<tr>
<td></td>
<td>Minimum requirement for employer contributions: 100% vesting after 5 years or graded vesting in 20% increments from 3rd through 7th year)</td>
<td></td>
</tr>
<tr>
<td><strong>Investment Options</strong></td>
<td>ERISA 404(c) plans require minimum of 3 options with different risk/return (company stock may also be an option but does not count toward one of the 3 options) &amp; Switching among investment options must be allowed at least every three months.</td>
<td>Minimum of 3 options (company stock may also be an option but does not count toward one of the 3 options) Switching among investment options must be allowed at least every three months At least one option must be a capital guaranteed product.</td>
</tr>
</tbody>
</table>
**Appendix 3: Comparison of U.S. 401(k) and Japanese Employer-Sponsored DC (continued)**

<table>
<thead>
<tr>
<th></th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
</table>
| **Benefits Distribution**      | • Separation from service, Normal retirement age, At 59.5 years old, Death, and Disability.  
                                | • Minimum distribution rule: You must begin receiving benefits when you reach 70.5 years old (unless continue working) | • At 60 years old, Death, and Disability  
                                |                                                                                     | • You cannot receive benefits when you leave company unless you are 60 years old or older.  
                                |                                                                                     | • You must begin receiving benefits at 70 years old. |
| **Loans and Financial Hardship Withdrawals** | • Yes (hardship withdrawal subject to income tax and 10% penalty tax)          | • Not allowed                                                                             |
| **Portability & Rollover**     | • Discretionary rollover to new employer’s 401(k) plan or IRA.  
                                | • You may leave your assets with the old employer’s plan.  
                                | • No tax on rollover assets.                                                             | • Mandatory rollover to new employer’s DC plan or Individual Type DC.  
                                |                                                                                     | • You cannot leave your assets with the old employer’s plan.  
                                |                                                                                     | • No tax on rollover assets                                                             |
| **Tax**                        | • Contributions: tax deductible  
                                | • Investment Earnings: not taxed  
                                | • Benefits: subject to income tax                                                        | • Contributions: tax deductible  
                                |                                                                                     | • Investment Earnings: not taxed                                                        |
                                |                                                                                     | • Special Corporate Tax: 1.173% on account balances                                      |
                                |                                                                                     | • Old age benefits: taxable but some deductions apply                                   |
                                |                                                                                     | • Disability benefits: tax-free                                                         |
                                |                                                                                     | • Death benefits: subject to inheritance tax                                           |
Figure 9: Two New DB Plans Introduced by DB Bill

Contract Type

Employer

Plan Document

Union
<Or anyone representing 50% or more employees>

Beneficiary

Contribution

Contract

Direction for Benefit Payment

Benefit Claim Forms

Life Insurance Companies etc

Fund Type

Employer

Agreement

Union
<Or anyone representing 50% or more employees>

Beneficiary

Employee’s Pension Fund

Executive Committee

Board

Plan Document

Benefit Claim Forms

Benefit Payment

Benefit Payment

Trust Banks

Life Insurance Companies etc
Figure 10: Plan Sponsors can Switch among New Pension Schemes

Current Pension System

Employees Pension Fund

Qualified Pension Plan

New Pension System

Employee’s Pension Fund

Fund type Pension
- Employee’s Pension Fund without substitutions component-

Contract type Pension
- More strict protection on vesting rights compare to existing Qualified Pension Plan-

Defined Contribution Plan