<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>
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<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

4th tier
- Individual Annuity (20 million)
- Property Accumulation Pension Saving (Zaikei-nenkin) (3 million)

3rd tier
- Employee’s Pension Fund (Kosei-nenkin-kikin) (12 million)
- Qualified Pension Plan (Tekikaku-nenkin) (10 million)
- Portion paid by employer

2nd tier
- National Pension Fund (0.9 million)
- Employee’s Pension Insurance (Kosei-nenkin) (33 million)

1st tier
- National Pension (Kokumin-nenkin) (70 million)

1st tier
- Self-employed (20 million) Category 1 insured persons
- Spouses of category 2 (12 million) Category 3 insured persons
- Private Employee (33 million)
- Public Employee (5 million)
### 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>
<tr>
<td><strong>Substitution of Social Security</strong></td>
<td>Yes A portion of Employee’s Pension Insurance (social security) benefits which are proportional to your pay is provided by Employee’s Pension Fund</td>
<td>No</td>
</tr>
<tr>
<td><strong>Plan Management</strong></td>
<td>Plan sponsors must establish a separate entity, Employee’s Pension Fund, to manage plans</td>
<td>Plan sponsors make a contract with providers, such as life insurance companies and trust banks, to manage plans</td>
</tr>
<tr>
<td><strong>Form of Benefit</strong></td>
<td>Life annuities must be provided</td>
<td>Life annuities are not necessarily required</td>
</tr>
<tr>
<td><strong>Contribution</strong></td>
<td>- Employer contribution : deductible (no limit)</td>
<td>- Employer contribution : deductible (no limit)</td>
</tr>
<tr>
<td></td>
<td>- Employee contribution : deductible as Social Security Premium Deduction (no limit)</td>
<td>- Employee contribution : deductible as Life Insurance Premium Deduction (¥ 50,000 annual limit)</td>
</tr>
<tr>
<td><strong>Taxation</strong></td>
<td>- No tax on investment earnings</td>
<td>- No tax on investment earnings</td>
</tr>
<tr>
<td></td>
<td>- Special Corporate Tax is NOT imposed on the asset balance up to the certain limit</td>
<td>- Special Corporate Tax (1.173%) is imposed on the asset balance.</td>
</tr>
<tr>
<td></td>
<td>&lt;Taxation is suspended until March 2003&gt;</td>
<td>&lt;Taxation is suspended until March 2003&gt;</td>
</tr>
<tr>
<td><strong>Benefit</strong></td>
<td>- Annuity : taxable, but Deduction for Annuity Payments applies</td>
<td>- Lump-sum : taxable, but Deduction for Lump-sum Payment applies &amp; separately taxed</td>
</tr>
<tr>
<td></td>
<td>- Lump-sum : taxable, but Deduction for Lump-sum Payment applies &amp; separately taxed</td>
<td></td>
</tr>
</tbody>
</table>
## 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>Individual Type DC</strong></td>
</tr>
<tr>
<td>Contributions are fixed regardless of company profits.</td>
<td>Contributions are fixed regardless of company profits.</td>
</tr>
<tr>
<td>Employees cannot make contributions.</td>
<td>Employees choose whether to participate and how much to contribute from their pay.</td>
</tr>
<tr>
<td>Employers make matching contributions.</td>
<td>Employers cannot make matching contributions.</td>
</tr>
<tr>
<td>Individuals make contributions at their discretion.</td>
<td>Individuals make contributions at their discretion.</td>
</tr>
</tbody>
</table>
Figure 4: Eligibility and Contribution Limits

- **Individual Type DC**
  - Self-employed
  - Contribution Limit: 68,000 yen/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: 36,000 yen/month
  - Employee of the company with DB plan
  - Contribution Limit: 18,000 yen/month
  - DB Plan (Employees Pension Fund & Qualified Pension Plan, etc.)

- **Employee’s Pension Insurance**

- **National Pension**

- **Not eligible for DC**

- **Category#1 insured**
  - Self-employed and other individuals

- **Category#2 insured**
  - Employee of private corporation, etc

- **Category#3 insured**
  - Employee of public employee

- **National Pension Fund**

- **Portion Paid by employer**

- **Mutual Aid Pension**
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:
        - <Contribution Limit>:
          - 18,000 yen/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:
    - Employer DOES NOT run Employer-Sponsored DC:
      - Eligible for Individual DC:
        - 15,000 yen/month
  - Self-employed:
    - <less than 60 years old>
      - Eligible for Individual DC:
        - 68,000 yen/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
  - 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 Manager** A
- **Investment Manager** B
- **Investment Manager** C
- **Investment Manager** D
- **Investment Manager** E

- **Beneficiary**
- **Benefit Claim Forms**
- **Benefit Payment**

- **Plan Administrator**
  - Contributions
  - Recordkeeping
  - Gather each Investment Directions
  - Provide Plan Information
  - Provide Information related to Investment Products
  - Investment Direction

- **Trustee**

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**
- **Individual Investment Direction**
  - **Plan Administrator A**
  - **Plan Administrator B**
  - **Plan Administrator C**
- **Beneficiaries**
  - Benefit Claim Forms
  - Benefit Payment
- **National Pension Fund Association**
  - Application / contribution
  - Selection
  - Gather investment directions
  - Recordkeeping
  - Present investment options line-up
  - Provide information of investment options
  - Gather investment directions
  - Present investment options line-up
  - Provide information of investment options
- **Outsourced Financial Institutions**
  - 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

**Rollover**

- Tax-free

**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

**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>Amount of Annuities</th>
<th>Deductions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 2.6 mil yen</td>
<td>1.4 mil yen</td>
</tr>
<tr>
<td>2.6mil - 4.6mil yen</td>
<td>Amount times 25%+0.75mil yen</td>
</tr>
<tr>
<td>4.6mil – 8.2mil yen</td>
<td>Amount times 15%+1.21mil yen</td>
</tr>
<tr>
<td>More than 8.2mil yen</td>
<td>Amount times 5%+ 203mil yen</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Age 65 or more</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Years of Service</strong></td>
</tr>
<tr>
<td>Up to 20 years</td>
</tr>
<tr>
<td>Beyond 20 years</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)

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.
### 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.

Percentage of the average total retirement benefits per employee (28 Million Yen)
## Appendix 3: Comparison of U.S. 401(k) and Japanese Employer-Sponsored DC

<table>
<thead>
<tr>
<th>Who May Contribute</th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employees &amp; Employers (matching contributions / discretionary contributions)</td>
<td>Employers Only</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Annual Contribution Limit</th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Pre-tax Employee Contribution Limit: $10,500 (in 2001)</td>
<td>Employer Contribution Limit: 432,000 yen for employer without DB plan 216,000 yen for employer with DB plan</td>
</tr>
<tr>
<td></td>
<td>Aggregate DC Contribution Limit: Lower of $35,000 or 25% of pay</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Eligibility</th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
<tbody>
<tr>
<td></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 Participants must be less than 60 years old</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Vesting</th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employee contributions: immediately 100% vested Minimum requirement for employer contributions: 100% vesting after 5 years or graded vesting in 20% increments from 3rd through 7th year)</td>
<td>Minimum requirement: 100% vesting after 3 years.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Investment Options</th>
<th>United States 401(k)</th>
<th>Japanese Employer-Sponsored DC</th>
</tr>
</thead>
<tbody>
<tr>
<td></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
- Trust Banks
- 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

Direction for Benefit Payment

Benefit Payment

Contribution

Contract

Benefit Payment
Figure 10: Plan Sponsors can Switch among New Pension Schemes