

Council Resolution 1267 (Act No. 124 of November 27, 2014); *MTA*  
(20) Act for Establishment of the Financial Services Agency (Act No. 130  
of October 16, 1998); 2 (5)

## 4. Labor/Social Security Law

### **An Act of the Partial Revision of the Defined Contribution Pension Act and other Private Pension Acts**

Law No. 66, June 3, 2016 (Effective on January 1, 2017)

#### **Background:**

(1) Income Security Schemes among the elderly in Japan consist mainly of two-tiered Public Pension Schemes composed of the Basic Pension and Employees pension. Private Pension Schemes complement Public Pension Schemes as being the “third tier.”

(2) The Defined Benefit Corporate Pension Act (Law No. 50, 2001) and the Defined Contribution Pension Act (Law No. 88, 2001) have regulated Private Pension schemes.

1) The Defined Benefit Corporate Pension Act (DBA) deals with defined benefit-type pension plans in which the benefit rate (ie. calculating formula) is preliminarily defined. Two types of governing system for the defined-benefit corporate pension are provided in the DBA: Bylaws-type Defined Benefit pension plan (BDB) and Fund-type Defined Benefit pension plan (FDB). The BDB shall be governed by an employer based on the bylaws, which have been drawn up between an employer and a labor union organized by a majority of the workers at the workplace - in cases where such a union does not exist, a person representing a majority of the workers - and recognized by the Minister of Health, Labour and Welfare. The FDB shall be governed by the board of directors set up in the Approval Fund (approved by the Minister of Health, Labour and Welfare), in which directors should be elected from representatives directed by both employer and employees respectively.

2) The Defined Contribution Pension Act (DCA) prepares only the pension plans defined the contribution rate but not the benefit rate.

Because benefit-defined pension plans as stated above require employers to fund a reserve for the pension benefits in the future, employers, especially of small and tiny companies, have to bear the burden charge, so that few Private Pension Schemes cover workers employed in small and tiny companies and self-employed persons. The Contribution-based pension scheme made by the DCA is designed to resolve these issues.

The DCA provides two types of governing system: Corporation-type Defined Contribution Pension plan (CDC) and Individual-type Defined Contribution pension plan (commonly called as 'iDeCo'). CDC shall be governed by an employer based on the bylaws, which have been drawn up between an employer and workers and recognized by the Minister of Health, Labour and Welfare. The iDeCo, different from other pension plans, which are based on employment relationship between employer and employees, is intended to cover self-employed and other persons who do not enter into any other pension plans. The latter shall be governed by the National Pension Fund Association - the body corporate established based on article 137-4 of the National Pension Act - based on the bylaws, which have been drawn up by this Association and recognized by the Minister of Health, Labour and Welfare.

(3) Recently, issues surrounding the income security schemes among the elderly have become serious, so that more expectations are being placed on the Private Pension scheme. First, legislations were enacted to plan a long-term reduction of the public pension benefit rate. Acceleration of demographic aging has become increasingly a controversial issue: the question is the intergenerational equity and the sustainability of the Public Pension scheme. As a result, laws to reform the public pension system (Law No. 104, 2004) introduced measures to control recipients' future benefits (corresponds to about 50% of the income levels in active years) by raising and locking in pension premiums on certain levels and automatically adjusting the benefit rate according to the birth rate and variance of the average length of life. Secondly, the government decided that the 'Employees' Pension Fund' will be liquidated, which was introduced by (the revision of) the Employees Pension Act in 1966 and has remained to the present, so participants in the fund will be lose chance to take part in any private pension schemes (see the Act to Reform of the Public Pension System, Law No. 63, 2013). Thirdly, it was pointed out that,

while the number of subscribers to those pension plans has increased as a whole, the implementation of pension plans in small and tiny companies and the participation of the 'iDeCo' have not been as good as was expected.

### **Main Provisions:**

(1) *The intent and purpose of this revision* is to create favorable environments for people, regardless of their lifestyles, preparing for old age on a voluntary basis. There are predictions that the role of the private pension schemes complementing the public schemes will expand as a diversification in lifestyle spreads. Whilst there are a variety of amendments with this revision, this paper mainly explains three measures: *measures for diffusing the use of the private pension schemes; measures for improving the "portability" of pension assets; and measures for dealing with a shortage of reserve funds in a defined benefit type pension.*

(2) *Measures for diffusing the use of private pension schemes in small companies* contain: 1) Measures for spreading private schemes to workers employed in small and tiny companies and 2) Measures for relaxing the eligibility criteria of the iDeCo plan.

1) The state of implementation of the private pension in small companies employing 30-99 workers has hovered at 18.6% (in 2013). Additionally, it has been expected to dissolve Employees' Pension Funds mainly in such companies by laws to reform the public pension system (Law No. 104, 2004) as stated above. In this context, the 'Simplified Defined Contribution Pension' plan is put in place [Art. 3 (5) in the DCA], and thus CDC plans can be started through simple procedures by this arrangement. This revision additionally allows an employer in the small companies, especially with 100 or fewer employees in which it would be difficult to conduct the CDC, to pay a pension premium to their workers' iDeCo plan in addition to the premium paid by workers ("Special Premiums paid by Small Businessmen scheme" [Art. 55 (2) (4), 68-2, 69, 70-2 in the DCA]).

2) Because the iDeCo plan had limited the eligibility criteria to the members who were self-employed and not able to participate in other corporate-type pension plans so far, the diffusion rate of the iDeCo plan among them remained very low (0.5% of all the eligible participants). In

this revision, all insured person aged 60 or below covered by the public pension schemes could participate in the iDeCo plan [Art. 64 of the DCA], so that such people as being stay-at-home mums (dads), civil servants and workers participating in other corporate-type pension plans could make a choice of the iDeCo plan [see Art. 62 (1) of the DCA].

(3) *Measures for improving the “portability” of pension assets* amended in this revision allow ones’ assets funded to transfer to another pension plan after a job change and to aggregate pension reserve, in light of ‘modification to diversification of life course.’ While there has been a certain framework to be able to transfer between Defined Benefit-type Pension plans (DBs), between Defined Contribution Pension plans (DCs) and from the DBs to the DCs, this revision provides a provision enabling the transfer from the DCs to the DBs [Art. 54-4 of the DCA, Art. 82-5 of the DBA etc.]. Other amendments are made concerning transfers between each pension plan in case workers will change their jobs [Art. 80 of the DCA etc.].

(4) *Measures for dealing with a shortage of reserve funds in defined benefit-type pensions* are also provided in this revision. Under the Defined Benefit-type Pension plans, employers must pay a contribution and invest assets to maintain the requisite pension benefit for workers according to benefit conditions and calculating formula based on agreement between workers and employers. The employer must pay a contribution additionally if the investment performance is not enough to guarantee the expected amount and then a shortage of reserve funds actually exists. Such a scheme imposes operational risks on the side of employers. This revision creates the “Risk Sharing-type Defined Benefit Corporate Pension” plan, which contains a mechanism enabling operational risks to be shared by participants (ie. workers). The DBA requires that the premium rate shall be calculated based on the expected rate of interest, of death, of contingencies, and so on [reg. 43 of the DBA]. This revision, when calculating the premium rate, requires considering a “fixed amount of financial deterioration risk,” which shall be estimated as the amount of shortage in case the investment performance becomes worse [reg. 46-2 of the DBA]. On the other hand, this revision also prepares the mechanism to impose a risk on the side of the participants by fixing the benefit automatically in case of a disruption of the balanced budget. If the

prescribed amount of benefits exceeds the fund reserve, it would be multiplied by a certain “adjustment rate” in order to maintain a balance with the fund reserve and would be automatically adjusted. Therefore, it is the risk sharing mechanism that while employers bear a certain risk at the time of the contribution of premium, participants (workers) also bear a certain risk at the time of the determination of benefit.

### **Editorial Note:**

Both the DBA and the DCA stated as their aim that ‘supporting citizens’ self-help efforts to maintain each income in older age, thereby helping to contribute to the stability of the lives and the welfare of citizens, coupled with benefits from the Public Pension’ [Art. 1]. Private Pension Schemes have a role to complement Public Pension Schemes, and this role is becoming more important.

Private Pension Schemes in Japan have their roots in the retirement benefits having been paid voluntarily by corporations to their employees and have developed by special tax treatment. Therefore, they have been developed based on the employment relationship, especially a life-time employment practice, having been perceived as one of the important factors of the prosperity of the Japanese economy. In contrast, we can recognize moving toward the new framework based on the “individual” from several measures introduced by these revisions such as measures for diffusing the use of the iDeCo plan and measures for improving the “portability” in light of ‘modification to diversification of life course.’ In such a context, policies for supporting individuals to participate in the private pension plans and the protections of their benefit have become more important.

## **5. International Law and Organizations**

### **Multilateral:**

Date Coming into Force with Respect to Japan	Date of Adoption	Title of Treaties and Agreements