"The Status Quo and the Future of the Public Pension System in Japan"

Motohiko Sugiyama, Mitsunori Ide, Akira Konishi

Japan

Summary

Around 60 years has passed since the public pension system was founded in full scale. Since then, several revisions were made against problems at different times according to necessity. However, our public pension system is still challenged by various problems in the recent slump of Japanese economy, and the birth dearth and the aging society.

In this paper, we will review the present status and the problems, etc., learning lessons from the revision history of the public pension system since its foundation, and study what it should be in the future.

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In this paper, we will review the present status and the problems, etc., learning lessons from the revision history of the public pension system since its foundation, and study what it should be in the future.

1. History of Public Pension System (mainly those of the employees' pension insurance)

(1) Foundation of public pension system

○ Foundation of the employees' pension insurance plan (1942)

The employees' pension insurance plan in which the insured were male workers at factories, etc., was founded.

In 1944, the scope of the insured was enlarged to staff and female employees.

- The benefits were the old-age pension etc., only under the earnings-proportioned plan.
- It was executed according to the social insurance premium method in Japan

(2) History of major revision

○ Full revision of the employees' pension insurance plan (1954)

The system of the pension was fully revised.

- The old-age pension only under the earnings-proportioned plan was revised to the two-storied old-age pension consisting of the fixed and the earnings-proportioned benefits.
- The pensionable age for men was deferred from 55 years old to 60 years old.

○ Realization of the pension for all the Japanese (1961)

While the employees' pension insurance plan was founded for employees in private enterprises and the mutual-aid pension system was founded for the civil servants separately, any public pension systems for the individual proprietors were not founded. The needs for income security after retirement for all the people in Japan grew from the forecast on increase of nuclear families and the future grayish society. In 1961, the national pension system was founded consequently, which brought the pension for all the Japanese was realized.

- The insured were those who were 20 years or older to 60 years old below and were not covered by the mutual-aid pension system.
- According to the social insurance premium method, the premium thereof was fixed.
- The pension was defined according to the period of contribution of the premium, of which one third was born by the National Treasury.

○ Introduction of the price indexation and the wage indexation (1973)

- Price indexation

  If the year-on-year commodity prices fluctuated over 5%, the amount of pension which pensioner received was revised according to the fluctuation.
- Wage indexation

  The amount of pension which pensioner received was revised according to the increase of the wages of the active generations through re-evaluating the standard monthly salary-proportioned amount after starting the contribution to the pension system on which the earnings-proportioned benefits was calculated.

The level of benefits of the employees' pension insurance was targeted at 60% of the closest level of the standard monthly salary of men.

○ Introduction of the basic pension and optimization of the level of benefits (1985)

Preparing for the upcoming full grayish society, the following revisions were made to ensure the public pension system operated in stable.

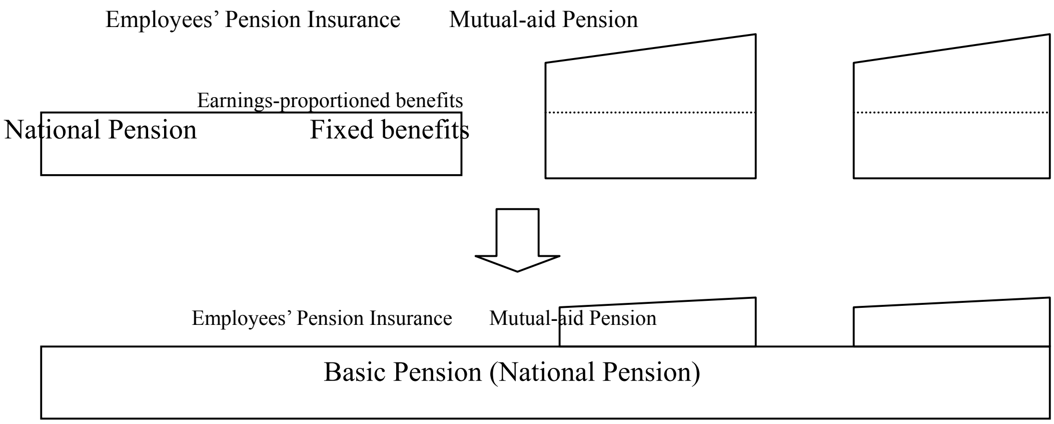
In this revision, the age when the pensioner started to receive the employees' pension was stipulated as 65 years old in the Employees' Pension Insurance Law. However, the amount equal to the earlier employees' pension benefits (the fixed benefits and the earnings-proportioned benefits) was exceptionally paid to those at their age of 60 or older.

- Introduction of the basic pension

  The public pension system in Japan was roughly divided into three, namely, the national pension plan (for individual proprietors), the employees' pension insurance plan (for the insured employees of private enterprises) and the mutual-aid pension plan (for civil servants). These three had problems that they created the imbalance among systems in contribution and payment, and their financial foundations were susceptible to the change of industrial structure.

  On account of this, the basic pension (fixed benefits) common to all the Japanese was introduced and the employees' pension insurance and the mutual-aid pension were reorganized to surmount them on the basic pension.

Incidentally, the calculation method for the earnings-proportioned amount of pension which differed from the employees' pension insurance to the mutual-aid pension was uniformed to that for the employees' pension insurance amount to balance the benefits.



- Optimization of the level of benefits

  In the revision of 1973, the level of benefits of the employees' pension insurance was targeted at 60% of the closest level of the standard monthly salary of men, whereas the rate reached 68% because the period of contribution was prolonged thereafter. The multiplier of the earning-proportioned benefits and the fixed unit premium for the fixed benefits were diminished depending on birth years to optimize the level of benefits.

- Establishment of females' pension rights

  The wives (full-time housewives) of the employees of private enterprises were covered by the pension system of their husbands (spouses' pension added amount) and they might arbitrarily purchase the national pension. If these wives who were not arbitrarily insured by the national pension divorced or got disabled, they could not receive the pension at all.

Therefore, it was made compulsory for the wives (full-time housewives) of the employees of private enterprises or the civil servants to be insured by the national pension in order that they could draw the basic pension.

However, as these full-time housewives did not make any earnings, the pension system to which their spouses contributed bore the premium instead of charging it individually.

- Review on the benefits to their age of early 60's (1994)

  For the pensionable age of the employees' pension insurance, the benefits thereof equal to the earlier employees' pension benefits (the fixed benefits and the earnings-proportioned benefits) was exceptionally paid to the pensioner at their age of 60 or older. The discussion was made on driving the pensionable age both for the fixed and the earnings-proportioned benefits to 65 years old.

  The pensionable age would be deferred in stages to 65 years old from 2001 to 2013 only for the fixed benefits through providing the benefits to the pensioners in early sixties to support their life in addition to their earnings and to the pensioner of 65 years or older to make their life plan primarily on the pension.

- Optimization of the level of benefits, deferment of the pensionable age, and introduction of all earnings-proportioned system (1999)

  Since the revision of the pension system in 1994, the birth dearth and the aging have been progressing faster than expected. According to the projection of Japanese population (intermediate projection), the proportion of people of 65 years or older is projected to increase from 14.6% in 1995 to 32.3% in 2050, that is, 4 contributors per pensioner will drop to 1.5 contributors per pensioner. If the level of the benefits before the revision is maintained, it is expected that the premium rate in the monthly salary for the employees' pension insurance will jump almost double from 17.35% to 35% in 2025.

The income growth of working generations slows along with the low economic growth. The premium rate of 35% may exceed the limitation, considering the increase of medical and nursing cost beside the pension. The Ministry of Health and Labor published the reform of the public pension system, "5 options" (□) and took a pole at the same time on the intellectuals.

(□) Option A:maintain the benefits before the revision (the future premium rate for the employees' pension insurance will be 26.4% of annual income)

Option B:limit the premium rate for the employees' pension insurance up to 30% of monthly income (the total benefits will be optimized around 10%).

Option C: limit the premium rate therefor up to 20% of annual income (the total benefits will be optimized around 20%).

Option D:maintain the premium rate therefor at the present rate (17.35%) (the total benefits will be optimized around 40%).

Option E:Abolish the employees' pension insurance plan (the public pension will be only the basic pension and the employees' insurance plan will be abolished.)

As the result of taking the balance between the future contribution and the total benefits amount, based on those mentioned above, the revision was made in order to limit the future premium of the employees' pension insurance around

20% of annual income as well as the future total benefits amount for this time. This is because the premium rate of 20% of annual income is considered as a limitation when reviewing the cases in European countries, which have confronted the grayish society earlier than Japan, and many the intellectuals, commented that the premium should be up to 20% (they chose Option C out of 5 Options) in the poll of them. The followings are the measures therefor.

- Optimization of the employees' pension insurance (the earnings-proportioned benefits) at 5%

  It is impossible to optimize the future total benefits amount around 20%, only if the pensionable age is deferred as described hereunder. Hence, it is also necessary to optimize the earnings-proportioned benefits 5%.

  Incidentally, the benefits from the basic pension is conventionally maintained.

  As the result of these, the level of the benefits falls in around 60% of the after-tax income of working generations.

- Review on the indexation

  The wage indexation is not applied, but only the price indexation will be applied at the age of 65 years or older.

  While the burden on the working generations is increasing, it is not considered affordable to reflect the increment of wages to the income. For the amount of the pension of the recipients, it is considered possible to keep their purchasing power through applying the price indexation.

- Review on the benefits for the working pensioner at the age of 65 years or older

  The employees' pension insurance has been drawn by the people of 65 years or older without any conditions. The premium for the employees' pension insurance will be born by those who are 65 to 70 years old and are still working. For those who earn a certain level of income or higher, full or a part of the earnings-proportioned benefits will be suspended according to their income. However, the basic pension will be fully paid.

- Deferment of the pensionable age of the employees' pension insurance (the earnings-proportioned benefits)

  For male, the pensionable age of the employees' pension insurance will be deferred to 65 years old in phase-in-method from 2013 to 2025.

  As stated above, it is crucial to defer the pensionable age as well as to optimize the benefits 5% in order to limit the future premium rate of the employees' pension insurance up to 20% of annual income and also limit the future total benefits amount around 20%.

  Forecasting the decrease of workforce in the light of the birth dearth and aging society, the grounds for this deferment of the pensionable age are that it is necessary to promote full employment of the senior people and the pensionable age of the public pension in other countries is 65 years in principle.

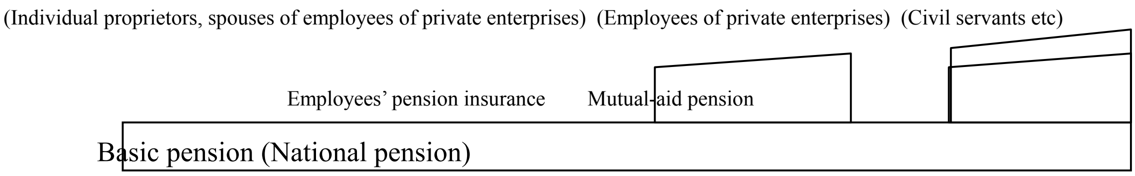
(3) The status quo

The current public pension is the two-storied old-age pension consisting of the fixed and the earnings-proportioned benefits.

1st story: the basic pension common to all the residents in Japan, which is the fixed benefits

2nd story: the employees' pension insurance (contributed by employees in private enterprises) , which is the earnings-proportioned benefits the mutual-aid pension (contributed by civil servants), which is the earnings-proportioned benefits

Accordingly, individual proprietors and the spouses of employees of private enterprises and the civil servants are only covered by the basic pension. The employees of private enterprises and the civil servants will additionally receive the earnings-proportioned benefits.



The following section will describe it in detail with emphasis on the basic pension and the employees' pension insurance.

□Benefits

Basic pension:

paid at the age of 65 years or older

The amount of pension is the fixed benefits according to the period of contribution. (In the case of full contribution period from 20 to 60 years old, the amount is 804,200 yen)

Employees' pension insurance:

paid at the age of 65 years or older

The amount of pension is calculated through multiplying average standard earnings-proportioned monthly salary by multiplier by the contribution period by the sliding commodity price indices (the standard monthly salary has been scaled by the wage indexation and the multiplier is from 7.125/1000 to 9.625/1000 according to birth years).

Nonetheless, as the phase-in deferment of the pensionable age for the exceptional payment of the employees' pension insurance (the fixed and the earnings-proportioned benefits) is on going, the followings will be paid to the applicable pensioners from 60 to 64 years old and 65 years old.

Fixed benefits: the fixed amount according to the contribution period

Earnings-proportioned benefits: the annual amount calculated similar to the employees' pension insurance at the age of 65 years or older.

For the mutual-aid pension, the benefits calculated by the following equation will be added to the above-mentioned earnings-proportioned benefits.

Average standard monthly salary × (0.5/1000 to 1.5/1000) × contribution period × the price indexation

□Premiums

Basic pension: 13,300 yen per month

Employees' pension insurance: 17.35% of the standard monthly salary (including the premium for the basic pension)

For the pension system for the insured of the employees' pension insurance, when the employees are employed by the enterprises to which the employees' pension insurance system is applied, they will be automatically covered by the pension system and the premium will be withheld from their employment income.

For the national pension, the residents in Japan shall voluntarily be insured by the national pension system at the age of 20 years or older and pay the premium. For the wives of the insured employees, their premium is included in their spouses' premium for the employees' pension insurance. This shall be reported to the municipal government.

Every employee and every spouse of theirs are insured, and every premium is collected without omission thereby. On the other hand, there are the non-insured and defaulters in the national pension system owing to the formalities to be done on a voluntary basis.

(4) Integration of public pension plans

We have reviewed the history of the past revisions focusing on the employees' pension insurance in the preceding sections. We will summarize the integration of the mutual-aid pension, which is one of the public pension plans, the employees' pension insurance and the national pension in this section.

For the mutual-aid pension system, it was founded from the system for veterans and bureaucrats in the beginning. Following this, various types of systems per business field were established and consolidated. In 1985, there were 7 systems before introducing the basic pension.

□National Public Service Mutual-aid Association

□Local Public Service Mutual-aid Association

□Private School Teachers & Employees Mutual-aid Association

□Agricultural, Foresters and Fisheries Institutions Employees Mutual-aid Association

□Japan Railway Mutual-aid Association

□Japan Tobacco Industry Mutual-aid Association

□Japan Telegraph and Telephone Mutual-aid Association

The calculation methods for the premium and the benefits are with no wonder different each other.

With independent pension systems, the operation of the systems went instable due to the declining number of the current contributors associated with the change of the industrial structures, which might cause the imbalance between contributions and benefits among the systems. For example, at the Japan Railway Mutual-aid Association in spite of the past record of 480,000 contributors, the number of contributors plummeted to 360,000 until 1983 due to the decline of demand for railways, whereby they faced financial difficulties.

In these circumferences, the integration of the public pension systems including the employees' pension insurance was progressed through balancing the contributions and the benefits among the individual systems.

In 1985, the benefits were leveled first through introducing the basic pension, employing the fixed amount system common nationwide, and applying the benefits calculation method common to the employees' pension insurance plan, even though the earnings-proportioned payment system was separated.

In 1989, the premiums for the earnings-proportioned plan were adjusted among the systems. The Japan Railway and the Japan Tobacco Mutual-aid Associations of which financial state especially declined were subsidized therefor.

In 1997, the Japan Railway, the Japan Tobacco, and the Japan Telegraph and Telephone Mutual-aid Association were united with the employees' pension insurance plan. The current mutual-aid pensions are thereby as follows.

- National Public Service Mutual-aid Association
- Local Public Service Mutual-aid Association
- Private School Teachers & Employees Mutual-aid Association
- Agricultural, Foresters and Fisheries Institutions Employees Mutual-aid Association d

2. Peculiarities in the Public Pension System in Japan

- Pension for all residents in Japan

In 1961, the national pension plan for individual proprietors was found and the pension for all the Japanese was realized. After that, the basic pension common to all the people in Japan was introduced in 1985, and the employees' pension insurance and the mutual-aid pension were reorganized to add them to the basic pension.

As stated above, the stable insured group was formed by the pension system to all the residents in Japan, which enabled a whole society to assure the old-age life.

Since the benefits of the basic pension is common to all the people in Japan in order to assure the basic part of their life after retirement, the cost therefor are born equitably by all the people in Japan.

- Social Insurance Premium Method

The public pension is operated in the social insurance premium method in Japan.

The employees in the private enterprises bear the premium proportion to their earnings, and they will receive the fixed amount of the basic pension and the employees' pension insurance proportioned to their earnings.

Since the amount of the basic pension is fixed, the method has a function to allot the income from the people of high-income to those of low-income in the same generation.

The public pension is compulsory and is the government-run.

For the private insurance systems, insurance companies can not precisely understand the risk of each one's life expectancy. They set the premiums according to an average risk of the insured. In this case, people who feel it comparatively expensive (who believe their life expectancy is short) may not purchase the insurance. Consequently, the premium for the left group will be relatively expensive. To avoid such case, the risk from the longevity is dispersed among all the people in Japan through compulsory insurance.

The fund of the public pension is basically from the income from the premiums and the management of the reserve fund. On the other hand, one third of the benefits of the basic pension are subsidized by the National Treasury (tax).

The public pension system of Japan was founded as a German type social insurance system. While the pension system for all the residents in Japan was materialized in 1961 and the basic pension system common to the all the people in Japan was introduced in 1985, an British type social insurance system was also introduced.

German type: Covered the employees according to job categories
Benefits proportioned to earnings
Funded by the social insurance premium
Savings and insurance
British type: Covered all the residents
Fixed benefits
Funded primarily by taxes
Re-allotment of income

The social insurance premium method is strongly featured with a saving element for the insured centering on employees, while the pension system in Japan incorporates an element of re-allotting income to assure the lives of all the Japanese with the fixed benefits through combining the basic and the employees' pension insurance.

- Support between generations

The Japan's pension system used to take the reserve funding method. During the inflation economy, the premium was set lower than the benefits after World War II.

Since then, the phase-in-method to raise the premium according to the forecast in consideration of cost bearing ability has been adopted.

Subsequently, the higher level of the benefits was paid to the insured at the foundation of the pension system whose contribution period was short and the shortage of the fund were compensated by the premiums paid by the future pensioner through introducing the price indexation and the wage indexation. The element of pay-as-you-go system was emphasized thereby, although the system owned a certain reserve fund.

3. Current Challenges

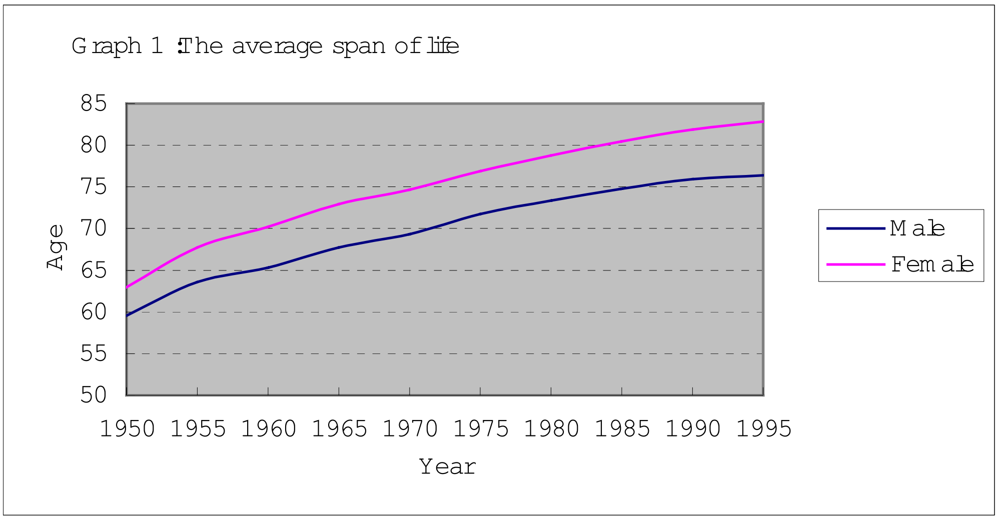
(1) Financial pressure on the pension associated with the birth dearth and the aging society

A. Financing method for the public pension

The financing method for the public pension in Japan is a kind of assessment insurance method referred as "corrective reserve fund method" in the paragraph 2. (3). The difference from the assessment insurance method is that the employees' pension insurance has its reserve fund around 5 times of the annual benefits and the national pension has it around 3 times of the same. It is possible to ease the premium fluctuation, if the reserve fund is amortized. Meanwhile, since the level of the reserve fund is insufficient and the assessment insurance method is basically applied, the financing method has a structure that the decrease of the current contributors who bear the premiums and the increase of the senior people who receive the benefits, that is to say, the population risk, may directly squeeze the budget and raise the premiums.

B. Birth Dearth

The birth rate has lowered the estimation on it in the future by the Government for the year 1992 to 1997 and the future level of the birth dearth is likely to be more serious according the estimation. When taking the estimation in 2025 for an example, the birth rate drops 11% from 1.80 to 1.61 in the mid range estimation and it drops 5% from 1.45 to 1.38 in the lower range estimation.

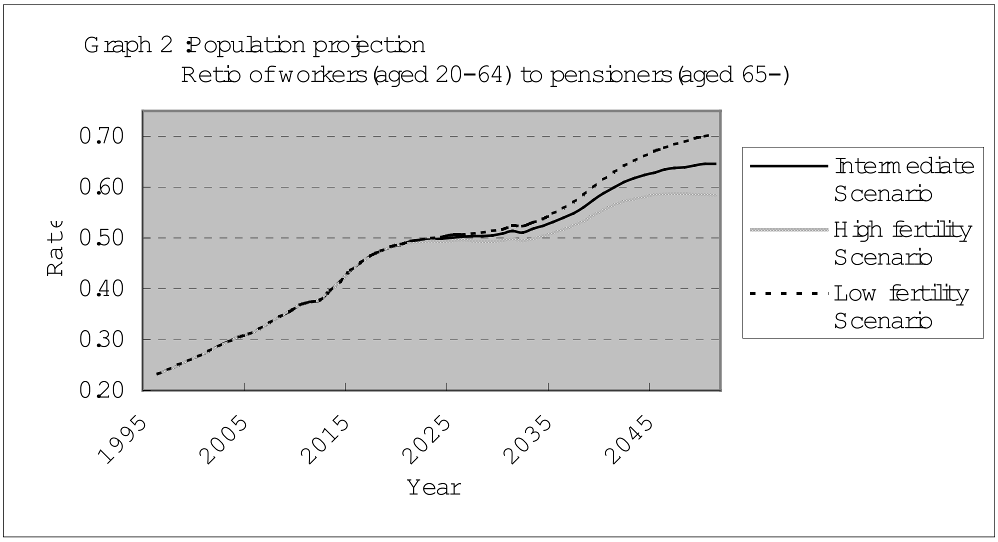


C. Graying

On the other hand, as a peculiarity, Japan has become a country of the world longest-life span (see the Graph 1), and furthermore, it is predicted we will face a considerably rapid aging society due to the rapid growth of population at the age of 65 years or alder in the next 20 years when the baby boomers generation born after World War II will turns into the pensioner generation.

D. Impact from the birth dearth and the aging on the pension finance

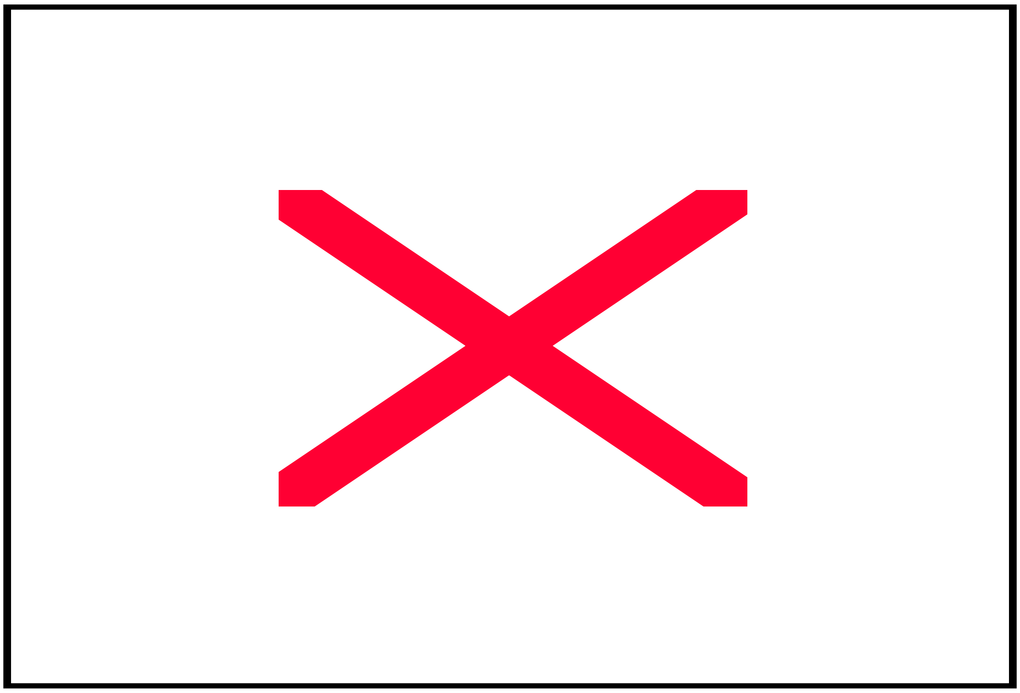
The increase of the senior people (i.e., pensioners) in the aging after adding the decrease of the current working generation (i.e., the premium bearer or contributor) in the birth dearth is simply represented by the population of senior people per the population of working generation. At the peak time of 2050, we will face the fact that the ratio of the senior generation to the current working generation may reach 60% (see Graph 2).

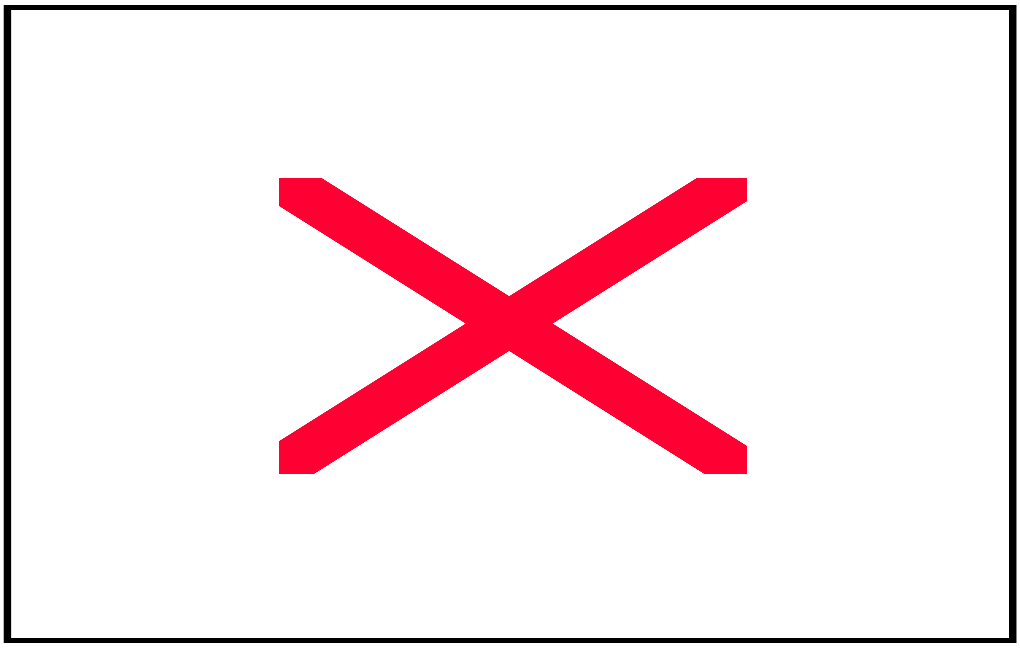


This ratio simply expresses the possible impact on the pension finance based on the assessment method, that is, “two workers support one pensioner” in image.

The birth dearth and the aging are apparently progressing much faster than any other countries. It is acknowledged that we have little time to prepare for it.

According to the result of re-calculation of the budget, if the current benefits level is maintained and it is raised in a phase-in-method, the contribution rates will be 27.6% for the employees’ pension insurance in 2025 or later (see Graph 3), and the premium for the basic pension will be 24,800 yen in 2020 or later (see Graph 4).





(2) Budget Easing Associated with the Economic Slump

A. Freeze on the Hike of Premium

In the re-calculation of 1994, it was assumed that the premium would be raised

2.15% in 1999 to 19.5%. However, the Japan economy stampeded to the prolonged recession after the bubble burst economy in 1990, the Government decided to freeze the hike of the premium for the present as an economic policy.

This freeze simply defer the premium revenues of around 15 trillion yen for the following 5 years. This deferment of the premium revenue means the deferment of debt in the future. Even though it was discounted in the future prediction of the Government, it might cause of further hike of the premium in the future as a consequent.

B. Abolishment of the Downward Slide Associated with Prices Fluctuation

The deflation caused by the economic slump rolls back the standard prices. If the pension system was operated as it goes, the benefit would be lowered for it was linked with the prices.

As a rule of the system, it was necessary to be indexed the benefit amount lower with no wonder. However, considering the public opinion and the state of Japanese economy, to lower the pension amount was abandoned according to the resolution that "the lower indexation for this fiscal year will be discounted into the next indexation" as a economy policy by the Government.

The impact of over-expenditure was likely to reach 260 billion yen until the next review on the level. No budget was kept for it, which also meant the deferment of the debt to the current working generation.

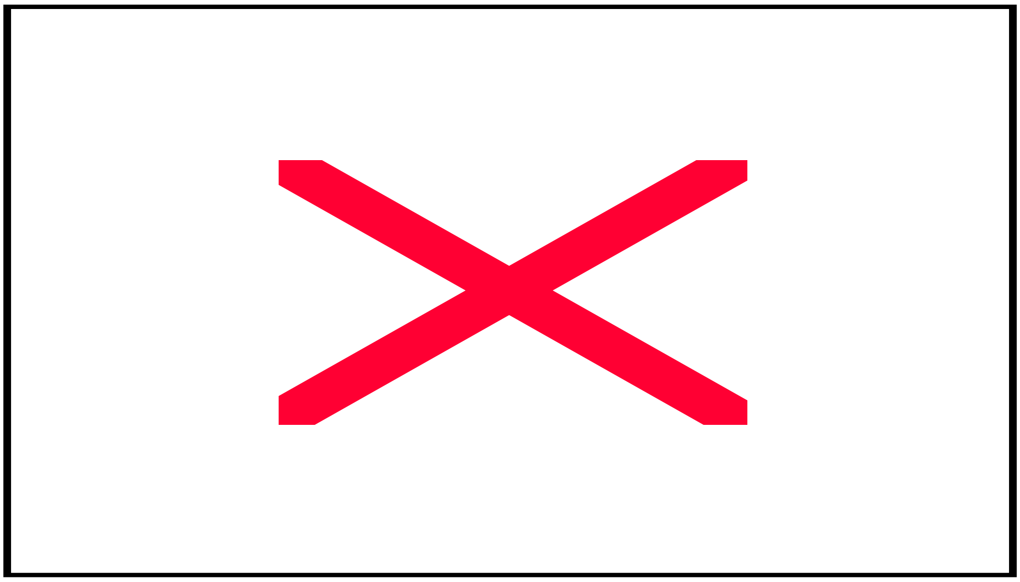
(3) Complaint from the Current Contributors Attributable to the Incredible Pension System

A. Anxiety for the roll-back of the future benefit

The revision history of the benefits is as stated in the paragraph 1. (1). Looking back the last 20 years, three major revisions on the benefit were made in 1985, 1994 and 1999 respectively during the last 15 years.

"The continuation of the system" is crucial to the credibility on the pension system. In the light of this, there is no doubt that the people feel the pension system incredible owing to these frequent revisions of the benefits.

Particularly in the youths, feeling of unfairness arises that "the benefits they receive will be smaller than their contribution" (see Graph 5), attributing to the frequent rollback of the benefits and the potential increase in the future premium.



Some comment that the mass media agitates people excessively. However, it is acknowledged that it is extremely difficult to completely remove the feeling of unfairness, even if the people in Japan understand the social and mutual support systems that are based on "the pro-rata benefits according to the pro-rata contributions."

B. Insufficient Understanding by the Japanese on the Policy

Some point out that the policy making process for revising the system not so open to the youths create their complaint. The Government makes an advertisement effort strongly to solve it, whereas another pointed out that they can not feel, "we participate in the policy decision making."

(4) Increase of Non-insured and Defaulters

There is a tendency of increase of the non-insured and defaulters of the national pension, influenced by incredibility as mentioned previously.

It is said that there are 2.7 million non-insured and defaulters. The monthly premium for the national pension is 13,300 yen. The unpaid amount of the premium is amounted to around 36 billion yen per year.

Some point out that these will not always impose a negative impact on the pension finance, because the amount of benefits will be reduced because of a short contribution period. However, from the viewpoint on the entire social assurance, the number of public assistance recipients may increase in the future, which may also increase the total expenditure.

(5) Aging of the Pension System

A. Variable Employment

In Japan, “people are employed by one company until their retirement age”, that is, life-long employment has been common. This system has supported Japan’s economic growth for a long time, forming “loyalties to a company.” In this rapidly metamorphosing information society, it is considered a factor that impairs proper competition and growth. In the circumferences, this life-long employment has been gradually collapsed in the course of “restructuring” by Japanese enterprises and the increase of the enterprises which adopt the performance-oriented human resource system.

A new working style, referred as “Freeter(s)” has been created. These Freeters do not work as a regular employee but as a part timer or a temporary staff, wondering company to company. The number of these Freeters is increasing. It is seemed to be the extension of moratorium of the youth, whereas it may be considered as a structural change in the employment owing to the demand for cheaper workforce including part-timers than the regular employees.

As either the cases may be, the current framework of the pension system does not cover them. There is apprehension that the number of non-pensioners will increase against "the pension for all the residents in Japan" in near future.

B. Assimilation of Women in Working Place

The pension system in Japan is organized based on a "family unit" basis not on an "individual unit" basis. In other words, full-time housewives (whose annual income is less than 1.3 million yen) are categorized as "the Category-3 insured" who will receive the basic pension without paying its premium.

This system is based on the assumption in the old life style that "women will work at full-time housekeeping and will not divorce for all their lives." However, the women's life style has been diversified drastically, whereby this system is getting outmoded.

(a) Feeling of unfairness of working women

i. The housekeeping is acknowledged as a job, while working wives who do both their jobs and housekeeping feel it unfair that the equal amount of benefits are paid overlooking non-contributors or contributors.

ii. In the pension budget wise, the singles bear the benefits for the Category 3 insured.

iii. The full-time housekeepers live on the income of their spouses, which means the full-time housekeepers belong to high-income families. In other words, these high-income and relatively rich families receive the benefits from the premiums contributed by the double-income families, which amplifies the feeling of unfairness

(b) Decrease of benefits by divorce

i. The valuation on the housekeeping effort until divorce is ceased at the time when they have divorced. In the case of divorce at around retirement age, many of them may not receive the benefits.

ii. This arises along with the increasing divorce rate nowadays. The portion of the pension was ordered in some cases by a judicial court. The beneficiary rights of such wives are not firmly established and the legal support is insufficient at the present time.

(c) Impact on wages of part-timers

i. The merit for being "the Category 3 insured" is significant. Many part-timers control their annual income below 1.3 million yen.

ii. It is the fact that they are required to bear the premium of 17.35% if the annual income exceeds 1.3 million yen. Without 1.5 million yen or higher income, the actual income will not increase.

iii. There is a voice that these are the cause for lowering the wages for part-timers.

4. Future Directions

(1) Roll-back of the Benefits

In 1999, the system was revised for the purposes of (□) avoiding overloading onto the next generations, and (□) limiting the future premium in the bearable range and trim the increase of the lump sum benefits within the range.

There is apprehension that the public pension finance will not be able to keep the system if the birth rate drops further, taking the recent trend of the birth dearth into account, while the Government forecast on the birth rate is based solely on the "intermediate level."

To avoid such event, a more direct approach is taken, that is, the rollback of the benefits level.

The current benefits level is targeted at "60% of the income in the working ages" as a standard. This level is relatively high when comparing with those in the other countries, owing to the tax preference. The rollback of the benefits is roughly classified into three as stated below.

A. Benefits Cut

The benefits cut is one of direct and effective approaches to control the excess of the expenditures with no doubt. However, for (□) the level of cut and (□) the scope of targets (if the beneficiaries be included?), it is considerably difficult to unify the public opinion.

B. Deferment of the Pensionable Age

As one of the legal revisions in 1999, the pensionable age was deferred by 5 years from 60 years old to 65 years old. This deferment of the actual pensionable age to 65 years old has been finalized after 25 years of processing term.

It is too early to discuss the deferment of the pensionable age to 70 years further, considering the current employment picture. It is the fact that it is also necessary to study how to keep the workforce in Japan as well from the points of (□) filling the future shortage of the workers population with senior people and (□) taking time to unify the public opinion.

C. Change of the Tax System

In Japan, the pension is given a tax preference. The actual benefits level after tax deduction is relatively high, comparing with the other countries.

Some commented therefor that it is necessary to rectify the pension budget by increasing the revenue through establishing earmarked tax for social assurance to the pension.

The characteristics of this method are that not only the contributors but also the pensioners will share the bearing through actual benefits cut.

Many perceive it impractical to reduce the benefits of the pensioners who have already made their living plan on them. On the other hand, it seems to be possible to reduce the burden on the pensioners who live largely on the public pension through devising the system as far as the revision of the tax system concerns.

However, in the tax system for the Japanese occupational pension system, the tax on the taxable deferment is imposed on the reserve fund in return for lighter tax on the benefits. There is a challenge to harmonize the entire tax system through reviewing it on the pension including the occupational pension for taxation on the pension.

(2) Premium Method to Tax Method

To solve the problems, that is, (□) increase of the non-insured by the public pension and the defaulters of the premiums, (□) imbalance between contribution and benefits, and (□) feeling of unfairness to the Category 3 insured who receive the pension without paying the premiums, there is an opinion to change the funding method of the pension system from the premium method to the taxation method represented by the earmarked tax for example.

The current pension system is established on the philosophy "pro-rata benefits to pro-rata contribution" in which the benefits are proportioned to the paid premiums. If the taxation method is applied, this point will be nullified, that is, paying the premiums will not always have link with receiving the benefits.

When applying the taxation method, the fairness is required for distribution. For this purpose, a means test (asset investigation) will be rendered. As the result of it, the assumption, "the pension for all the residents in Japan" will collapse and the pensioners will not be able to receive the pension even if they make savings for their life after retirement. It is predicted that the saving rate will drop thereby.

For the operation of the system, many problems are pointed out for the taxation method, that is, (□) there is an inhibitation among the people in Japan to obtain their understanding, because the financial source is only be secured by the hike of the tax rate to keep the level of benefits, and (□) some problems attributing to the unpaid consumption tax and the reverse graduation are predicted.

The current financial resource of the pension in Japan places a foot on the premium method while it actually relies on the tax revenue through the injection from the tax as “National Treasury.” The finance resources are a kind of “hybrid” of the rule of matching the contributors to the benefits and wide financing from taxes.

In the main stream of the “small government” to minimize the involvement by the Government, there is a suggestion that the rolls of benefits should be consolidated and then connect the related financial resources with them. This is the suggestion that the “taxation method” is applied to the necessary level for the basic living cost (the part of the basic pension) and the premium method preconditioned by self-help efforts is applied to the additional part (the earnings-proportioned part).

(3) Assessment method to reserve fund method

A. Reserve Fund Method to Solve the Population Risk

To surmount the financial pressure associated with the birth dearth and the aging, many commented that the assessment method should be switched to the reserve fund method. For the opposition to it, the others commented that it is not able to compensate the loss in the pension by inflation.

On the contrary to it, there is another view that the financial pressure may be solved by the swelling interests to the reserve fund along with the escalation of the interest rate in inflation.

A problem is also pointed out that the contributors would be forced to bear the reserve fund for both the pensioners' and own benefits when shifting the reserve fund method.

From the other point of view, it is possible to solve this problem through rollback of the benefits and effectively using the existing reserve fund. As either the cases may be, it is necessary to deliberate the shift and also review the entire framework including the financial resources is crucial.

B. Shift from Defined Benefit Plan toward Defined Contribution Plan

Some commented that the earnings-proportioned benefits should shift to the defined contribution plan at the individual account. The contribution quote is not always efficient method in the operation cost wise. However it can solve the problems associated with the increase of non-insured and defaulters, variable employment styles and "the Category 3 insured" etc at the same time.

Meanwhile, it is necessary to deliberate how to develop the individual account and which systems to be established, when shifting from the current "life-long defined benefit without assurance" system.

It is also pointed out that the system in which the benefit is not defined will not be a social safety net.

(4) Others

A. Systems of Policymaking and Resolution

Since the complaint among the young generations attributes to misunderstanding the facts, it is also suggested that the system to encourage the youth to participate in the process of resolution to remove feeling of alienation.

B. Addressing the variable employment

There is a suggestion that a clear orientation for working should be included in the school education.

It is not considered that the young generations are interested in the pension system and it is impossible to stop this trend even if the importance of full-employment through education.

We acknowledge that it is necessary to revise the system according to the change of employment in this regard.

C. Addressing “the Category 3 insured” problem

It is suggested that the contribution by women workers should be evaluated through shifting the family basis pension to the individual basis pension.

As an opposite opinion, if people of low-income are forced to pay the premium, the number of defaulters may increase.

5. Review on Financing Method

Next, we will review the finance control methods which we should select in the employees’ pension insurance plan through the prediction for the movement of the future premium rate.

(1) Premises

To review the financing methods, the premises to render a forecast are as follows. For the projection of the future population, we have simulated it in three cases of intermediate, lower and higher. We will review the change of level of impact from difference of financing methods.

- We will review the superiority between the reserve fund method and the assessment method considering how the future premium rate will change in a pure comparison of the financing methods.
- The premium will be reviewed every 5 years

- Price increases and interest rate will be tied with no delay.
- The benefits are fixed at the level of the current employees' pension insurance.
- Suppose the full earnings-proportioned plan does not significantly influence the relation between the benefits and the premiums, this is not taken into consideration for these simulations.
- The rate in the basic pension born by the National Treasury remains one third as it is.
- The forecasts on the insured will be simulated in the respective intermediate, lower and higher cases of the projection of the future population published by the Government.
- The premises other than the insured forecast are similar to those for the recalculation of the budget of the employees' pension insurance as follows.
    - Wage increase: 2.5%
    - Price increase: 1.5%
    - Yield: 4.0%
    - Revised pension rate (for the newly awarded per year) 2.5%.

(2) Results of Simulations

<In the case of intermediate estimation>

Firstly we reviewed the intermediate estimation as for the projection of the future population.

Where the reserve fund is estimated using the estimation of the future premium rate resulted from the recalculation of the budget of the employees' pension insurance, it is acknowledged that the fund will level off after around 40 years from now (See Graph 6, "Fund (1)").

(Graph 6)

Fund (1): shows the case that the premium rate is hiked every 5 years.

Fund (2): shows the case that the premium is kept constant.

For the present reserve fund method for the employees' pension insurance, it is planned to hike the future premiums in a phase-in-method. This is the assessment method (corrective assessment method) on the premises that a certain reserve fund is always held. If it is switched to the reserve fund method on the premises that the reserve fund enough to keep the future premium constant is held, the premium rate will be around 25.1% through the estimation in order that the pension fund level off after around 40 years from now (see Graph 7).

In this case, the movement of the pension fund is expressed as the legend, Fund (2) in Graph 6.

(Graph 7)

This is the level lower by around 10% than the final premium rate of 27.6% in the assessment method.

The pension fund is estimated as around 400 trillion yen 40 to 60 years after in the case of the assessment method, whereas it will jump to 650 trillion yen in the case of the reserve fund. The difference between them is 250 trillion yen. It is possible to cap the upper limitation of the future premium.

The total premium is small and the reserve fund is large. This is because the revenue created from the reserve fund by the premium reserved in advance. This indicates that reserving the premiums preliminarily through the reserve fund method will reduce the burden later.

<In the case of higher estimation>

Secondly, we reviewed the higher estimation where the decrease of the future population is smaller than the intermediate estimation.

In this simulation, we also calculated the premium rate in order that the pension fund almost level off after around 40 years from now (see Graph 8).

(Graph 8)

Fund (1): shows the case that the premium rate is hiked every 5 years.

Fund (2): shows the case that the premium is kept constant.

In the above simulation, provided the premium rate is hiked every 5 years (in the assessment method), the premium rate after 40 years is estimated to be around 25.5%.
On the other hand, provided the premium rate is kept constant in the future (in the reserve fund method), the premium rate of around 23.9% is estimated.
There is difference less than 10 %. For the pension fund, the fund in the reserve fund method is larger by around 100 trillion yen.
Comparing with the intermediate estimation, the population is estimated larger. When comparing the assessment method to the reserve fund method, the difference between them is small and the difference in the reserve fund is also small.

(Graph 9)

<In the case of lower estimation>

Thirdly, we reviewed the lower estimation where the decrease of the future population is larger than the intermediate estimation.

In this simulation, we also calculated the premium rate in order that the pension fund almost level off after around 40 years from now (see Graph 10).

(Graph 10)

Fund (1): shows the case that the premium rate is hiked every 5 years.

Fund (2): shows the case that the premium is kept constant.

In the above simulation, provided the premium rate is hiked every 5 years (in the assessment method), the premium rate after 40 years is estimated to be around 30.0%. On the other hand, provided the premium rate is kept constant in the future (in the reserve fund method), the premium rate of around 26.1% is estimated (see Graph 11)

There is difference over 10%. For the pension fund, the fund in the reserve fund method is larger by around 100 trillion yen.

Comparing with the intermediate estimation, the population is estimated smaller. When comparing the assessment method to the reserve fund method, the difference between them is large and the difference in the reserve fund is also large.

This indicates that the impact on the premium rate per worker is large, where the population of workers who support a pensioner decreases.

(Graph 11)

(3) Conclusion

Referring to the recent population movement statistic, the life expectancy still prolongs, while the birth dearth trend is ongoing. Therefore, it is highly possible that the projection of the future population movement will lower than the intermediate estimation of the population.

If the projection of the population lowers, the superiority of the reserve fund method will be highlighted, for necessary total premium is small as aforementioned. There are many obstacles to hike the premium rate in the reserve fund method from the current premium rate at a stroke. We acknowledge many challenges to solve before realization, while it is the fact that the future premium rate will be limited through hiking the premium rate, desirably forwarding it as far as possible. We believe that the equitability among the generations will be kept by doing that.