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STATE OF AND PROBLEMS WITH NON-GOVERNMENT PENSIONS IN JAPAN

by

Noriaki Niwata

I. The Position of Non-Government Pensions in the Pension System

In Japan, the term "non-government pension" and its concept correspond to the more widely used term "private pension". In other words, "government pension" is often called "public pension," while "non-government pension" is referred to as "private pension". Naturally, the major part of public pension is represented by the various types of pensions in the social security system, and it is not altogether incorrect to define public pension as social security pension. Likewise, it is possible to define private pension as personal pension. In addition, there is a group of pension systems called "corporate pension", which is positioned somewhere between public pension/social security pension and private pension/personal pension. Corporate pension is considered semi-public, semi-private pension or quasi-public pension. In recent years, new measures have been introduced to invigorate the corporate pension and its functions and management, promoting a trend toward viewing this type of pension as being more private in nature. As a result, there are strong expectations for corporate pension to have the characteristics and effects of a private pension in addition to its qualities and goals as a public pension.

This trend can be attributed to the changes taking place in the Japanese government pension system. As in most advanced government pension systems in the world, the Japanese government pensions are either financially distressed or anticipating financial difficulties in the near future, as the Japanese population ages rapidly. The Japanese government has responded to this situation by changing its pension policies. Such changes include restrictions on the amount of government pension benefits (not a reduction of benefits but prevention of further increase) and adjustment through combined benefits. On the other hand, public pension insurance premiums continue to increase, giving rise to such statements as: "We should no longer expect to be able to live on government pension benefits alone in our old age", and "The welfare trend is changing. It is reasonable now to depart from the traditional goal of continuous increase in government pension benefits, and limit the scope of pension-based national welfare system, in order to avoid large increases in pension insurance premiums and the resultant excessive burden". Thus, non-government pension, i.e., private pension or personal pension, came to receive high marks and expectations. Even before this trend started, the effectiveness of corporate pension as semi-public, semi-private or quasi-public pension had been re-evaluated and the demand for functional corporate pension had greatly increased.

Today, the importance of self-reliant efforts is being emphasized in Japan because of the inadequacy of the social security system in responding to the increasingly serious conditions of the aging society. Now, Japanese people must make their own efforts to maintain their standard of living at every stage of their life cycle, at their own responsibility, throughout their long lives. When people with such self-reliant attitudes get together and cooperate to establish various voluntary but social systems to achieve the goal of self-reliance through interdependence, they establish a system of mutual aid. The social security system, which can be defined as public aid, completes the picture of guaranteed standard of living, when supported by self-reliance and mutual aid. "Self-reliant efforts" consist of self-reliance and mutual aid described above, and are the conceptual opposite of "public aid". Public aid takes concrete form in the various social security systems. If we limit the discussion to guaranteed standard of living in old age, then public aid can be represented by government pension. The concrete form of mutual aid in Japan is corporate pension insurance, which is established, implemented and utilized by individual corporations.

It naturally follows that this self-reliance takes concrete form in the various types of personal pension. Personal pension as self-reliance and corporate pension as mutual aid are lumped together as pension insurance or pension system as self-reliant efforts. Although they are both part of such efforts, personal pension and corporate pension differ in their details, characteristics, or functions. It is, however, possible to lump these pensions together as non-government/private pensions, as opposed to government/public pensions. Even if we define corporate pension as semi-public, semi private or quasi-public pension, the general practice is to categorize corporate pension as non-government/private pension. Such non-government/private pensions (personal pension and corporate pension) are said to complement the functions of government/public pensions. In the past, non-government/private pensions were not fully developed nor yet proliferated. Consequently, they were defined as merely supplementary (filling in as much as possible where government/public/social security pensions were lacking). In today's Japan, however, they are rated higher as a means to complement and complete the government/public/social security pensions (i.e., to fill in where the others are lacking, to completely, or nearly, guarantee a certain standard of living in old age). The status of non-government/private pensions has been elevated, and more is expected of them. The transition from "supplement" to "complement" indicates the qualitative and quantitative progress of non-government/private pensions.

< Outline of Japanese Pension System >

1. Government Pension/Public Pension/Social Security Pension

A. National Pension

(1) National Pension (Contributory)

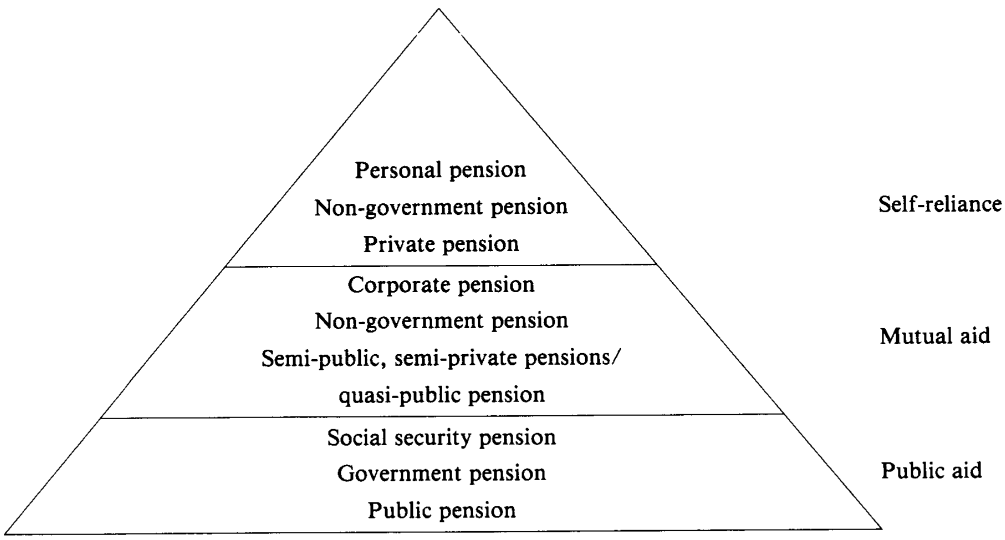
(2) Welfare Pension (Non-Contributory)

B. Welfare Pension
C. Mutual Pension (Public)
 (1) Government Employees Mutual Pension
 (2) Local Government Employees Mutual Pension
 (3) Agriculture, Forestry and Fishery Organization Employees Mutual Pension
 (4) Private School Faculty and Staff Mutual Pension
 (5) Japan Railways Mutual Pension
 (6) Japan Tobacco Mutual Pension
 (7) Nippon Telegraph and Telephone Mutual Pension

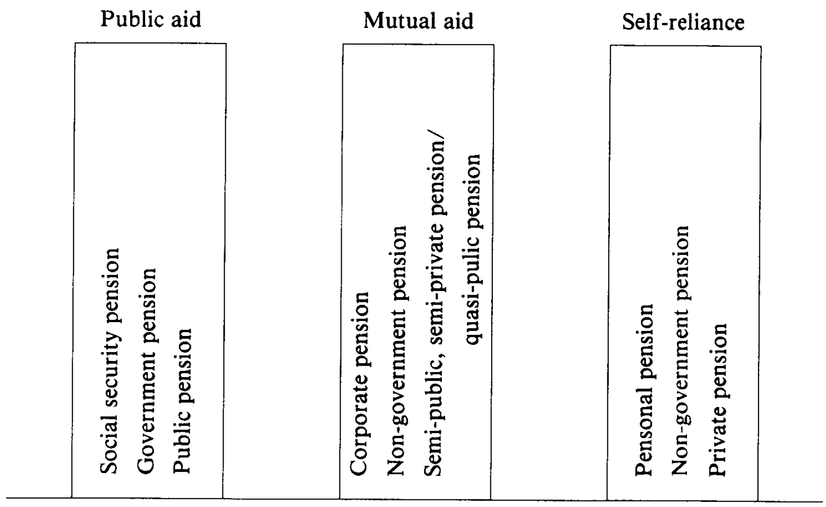
2. Non-Government Pension/Private Pension

A. Semi-Public, Semi-Private Pension/Quasi-Public Pension
 (1) Welfare Pension Fund Pension (Adjustment Pension)
 (2) Tax Qualified Pension
 (3) Farmers Pension
 (4) National Pension Fund Pension
  (a) Regional national pension fund pension
  (b) Functional national pension fund pension
B. Personal Pension
 (1) Group Pension (Company pension)
 (2) Personal Pension
 (3) Post-office Pension
 (4) Asset-building Pension
 (5) Mutual-aid Pension (ex. private/cooperative association pension mutual aid)

K-1 Diagram of Japanese Pension System



K-2



II. Types of Personal Pension and Their Development

Personal pensions in Japan can be classified as follows, according to several criteria.

A. Classification by Term of Benefit

1. Term Annuity or Terminable Annuity
   Pension benefits are received during the contract period. Benefits are terminated at the end of that period.
2. Perpetual Annuity, existence annuity, or life pension
   Pension benefits are received as long as the insured is alive or his/her life is sustained.

The former, the term annuity, is often used as a "stopgap" pension, to sustain a standard of living during the period following the employee's retirement, when he/she no longer has an income, but is not yet eligible for public welfare pension or mutual pension. On the other hand, the latter (perpetual annuity) is purchased and used in most cases as an "additional" pension, to supplement the public pensions such as the welfare pension and non-welfare pension (mostly national pension), which tend to be insufficient to maintain a standard of living in one's old age.

B. Classification by Method of Determining the Benefit Amount

1. Fixed-amount Pension
   The benefits continue to be paid in the constant amount determined in the contract.
2. Progressive Pension
   The amount of benefits is increased at a certain rate over time.

The former is straightforward and convenient to include in one's life plan, since the amount of pension benefits is fixed. The latter can, to some extent, counter the erosion of security due to inflation, which is the No. 1 enemy of pension recipients. If the inflation rate stays at the level observed in recent years in Japan, progressive pension can sufficiently counter the effects of inflation. If the inflation rate increases, progressive pension can hardly make up for the erosion caused by inflation. Progressive pension as a sliding scale pension does not exist in Japan.

C. Classification by Premium Payment Method

1. Reserve financing plan
   Type of pension in which a person starts to pay the pension premium as early as possible in his/her life, continuing to pay for a long period of time. The total of these payments and the total of the interest are the source of pension funds, and the amount of pension benefits is determined accordingly.
2. Paid-up Premium Pension
   Type of personal pension in which a person pays a lump sum pension insurance contribution at one point in life, usually at an advanced age.

The former is considered more practical for the general population, since it enables them to receive pension benefits that include the interest on the paid premium, without being an undue burden for them. The longer the payment period or the contribution period, the lower the relative cost of monthly or annual premium, but the long time it takes before receiving the pension benefits almost guarantees a considerable erosion of security, even at the current inflation rate in Japan. Should the scenario of the past oil crisis and the resulting wild inflation be repeated, the damage will be extensive. Even at the current inflation rate, it is predicted that the value of pensions will be reduced to 1/3 to 1/2 in 30 years. The latter, the paid-up premium pension, is relatively safe against erosion due to inflation. It is, however, not affordable for everyone, since its purchase requires a considerable amount of available cash. In many cases, paid-up premium pension plans in Japan are purchased by retired company employees, since employees retiring after reaching the retirement age receive a relatively large sum of retirement allowance. In other cases, this type of pension plan is purchased with the large proceeds from a land sale, reflecting the unusually high land prices in Japan.

D. Classification by Presence or Absence of Payment Guarantee Period

1. Pension Without Payment Guarantee Period
   Payment of pension benefits is terminated at the time of insured's death. This type of pension is called pension without payment guarantee period in Japan, and is the regular, ordinary type of pension.
2. Pension with Payment Guarantee Period
   It may be reasonable to terminate pension benefits payment at the time of insured's death, but if the death is premature, occurring shortly after the payment began, it gives the impression of losing out. Pension with payment guarantee period provides a lump sum payment of the remaining pension fund (paid premium minus paid pension benefits) to the survivors or allows the survivors to use the remaining fund as their own pension fund, for a limited period of time.

The former, also called "Tonchin" pension, closely matches the true definition and principles of pension. The Japanese, however, have a strong aversion to insurance or pension plans that require them to pay the premium or contribution without recovering any portion of it. Instead, they prefer to look at pension insurance as a form of savings. Consequently, they tend to avoid pensions without a payment guarantee period, and instead purchase pension plans with a payment guarantee period. In other words, by purchasing the latter, the insured acquires a savings plan and a pension insurance plan that incorporates mortality rate and survival rate. Even under the plan with payment guarantee period, the payment is terminated at the time of insured's death after the expiration of the guarantee period.

E. Classification by Inclusion of Principal in Pension Fund

1. Principal Inclusive Pension
   Pension benefits are paid from the pension fund, which consists of the principal or the source of pension and the interest it generates. This type of pension is popular in Japan and most pension plans sold by life insurance companies belong to this category.
2. Principal Deferred Pension
   The so-called interest payment pension. The total insurance premiums (i.e., pension fund), whether by installment or lump sum payment, is left intact, and pension benefits are calculated and paid based on the investment interest the fund generates. Many pension plans handled by trust banks are of this type.

In the former, the principal will eventually vanish. In the latter, in the event of the insured's death or termination or recipient eligibility period, the principal amount is paid to the insured (in the case of term annuity) or to the spouse or survivor (in the case of perpetual annuity). Not yet being familiar with the principal deferred pension, most Japanese purchase and utilize the principal inclusive pension. The benefit of interest payment pension is maximized when the interest rate is high.

F. Classification by Whether or Not the Characteristics of the Financial Institution Handling the Pension Are Incorporated

1. Insurance Pension (Life Insurance Pension)
   Pensions handled by life insurance companies, post offices or agricultural cooperatives. They combine life insurance (including life mutual aid) and personal pension (including pension mutual aid). The plan incorporates mortality rate and survival rate. If the insured dies while paying premiums toward the pension fund, a prescribed amount of death benefit is paid. In case of the insured's death after the benefit payment starts, the benefit payment is terminated at that time.
2. Savings Pension (Pension Handled by Financial Institutions Other Than Insurance Companies)
   Pension plans sold generally by city banks, local banks, trust banks, securities firms, etc. If the insured dies while paying pension installments, the total amount of installments plus interest is paid to the survivors. In case of the insured's death while receiving the pension benefits, the balance of the pension fund is paid to the survivors in the form of lump sum payment or their own pension benefits.

In the former, if the insured dies while receiving pension benefits, the balance of the pension fund is distributed to other surviving pension recipients. In this sense, this type of pension has the characteristics of an insurance plan. The latter may be considered as "long-term fixed amount accumulation and fixed-term fixed-amount withdrawal". Since it can be interpreted as a type of money in trust, some call this a "trust pension".

Generally, personal pensions can be classified according to the criteria mentioned above, but there are some personal pensions that do not belong to any of these categories, thus complicating the picture.

a. Asset Building Pension

This pension plan is available to hourly or salaried employees of a company, only if the business owner or the company implements this pension system. This system originated as a long-term installment savings plan with built-in tax incentives to encourage workers to save for purchase of a home, for which funds were lacking in Japan. The original purpose of this system was to encourage property accumulation among workers. This system was converted and expanded into a worker's property accumulation pension savings plan in an attempt to ensure financial security in salaried workers' old age. This was a response to the rapid aging of the Japanese society. The underlying concept is that an property accumulation pension can be of great help in providing financial security in one's old age, just as home ownership greatly improves the standard of living in one's old age. Property accumulation pension savings plans come with a tax incentive in which the interest earned on the principal is exempt from income tax, until the total of the principal (or the paid premiums) and the interest reach 5 million yen (tax exempt interest). In a property accumulation pension insurance plan, the interest earned on the paid premiums is exempt from income tax until the total paid premium amount reaches 3.5 million yen. Over the years of premium payment, the interest earned can reach an astonishingly large amount, which is tax exempt. This is one of the very few tax incentives available to salaried workers, who in general are victims of tax inequality. This type of pension was devised since most salaried workers must retire at a fixed age.

b. Fixed Pension

Technically, this type of pension is both a term pension and a fixed-amount pension. It is one of the most popular types of pension in Japan.

c. Pensions with Various Special Contracts

A variety of special contracts can be added to personal pensions. Special contracts grant benefits in the event of accidents that are covered by the insurance; they include accident security, benefits for injuries and for accidents, indemnity against traffic accidents, and benefits for hospitalization due to accidents, diseases or geriatric diseases. Among these, the most widely used in Japan is the special contract covering hospitalization for diseases.

d. Insurance Money Pension System Payment

In this system, the money of a matured life insurance or a death benefit is held by the insurance company, who acts as a proxy and invests the money. The insured person or the bereaved family members receive payment from the principal and its accrued interests in a pension-like manner over an extended period. Surprisingly, some insurance companies have recently begun paying the insurance money from a nonlife insurance in a pension-like manner also. This is not an eccentric idea, however, because precedents already exist in which the pension system applies to the insurance money of a workmen's compensation insurance as a government insurance, public insurance or social insurance.

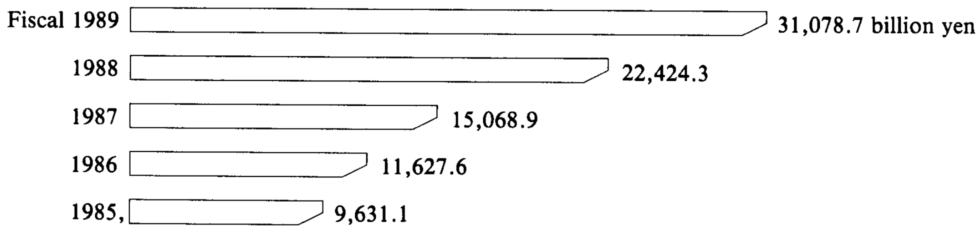
e. **Group Pension (Company Pension)**

There may be some disagreement whether this pension should technically be regarded as a personal pension or a corporate pension. It can be called a corporate pension, since companies adopt this pension. On the other hand, it can certainly be called a personal pension because it is left entirely to the judgment of each company whether the company adopts it or not. Accordingly, this type of pension may fall into the personal pension category by a slight stretch of the interpretation (in other words, when the corporate pension is defined as a semi-public, semi-private, quasi-public pension). Most group pensions are carried out according to the insurance system. This means that they are handled through life insurance companies. There is a domestic pension, a kind of domestic insurance, which resembles the group pension. The domestic pension is implemented in a manner similar to that for domestic insurance, but in a company which functions as an economic entity. This is another domestic pension which also serves as a company pension, and it is also popular in Japan. This type of pension hardly falls in the semi-public, semi-private, quasi-public type, or the governmental type.

In Japan, personal pension insurance began to appear around 1955. After that, awareness of the need for retirement security grew stronger with the rapidly aging society, and personal pensions sold by private insurance companies proliferated remarkably after 1976. In fiscal 1989, the sales amount of personal pensions increased 32.7% over the preceding year. Two other types of insurance have also shown extremely smooth growth; one is property accumulation pension insurances for building up property, and the other is group pension insurance for the welfare of hourly and salaried employees. Most of the latter types of insurance are eligible retirement pensions and welfare pension fund pensions, which will be discussed later.

K-3 Trend of Personal Pension Insurance Policies Sold

(by the end of each fiscal year)



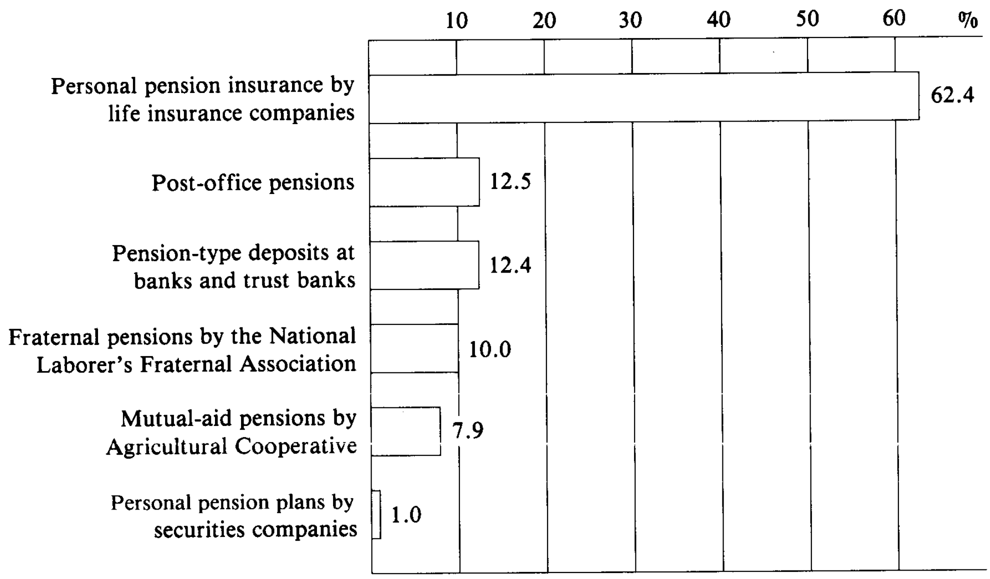
* From "Life isnsurace — 1990" p.13, issued by life Insurance Association (Sept. 11, 1990)

K-4 Newly Sold Post-Office Pensions by Type (in fiscal 1989)

Type of pension	Number	Percentage	Pension Amount	Percentage
Total	405,000	100.0%	¥82,621 million	100.0%
Perpetual pension	112,000	27.7	25,547	30.9
Personal pension	96,000	23.8	21,344	25.8
Married-couple pension	16,000	3.9	4,187	5.1
Property accumulation & perpetual pension	0	0.0	16	0.0
Term annuity	293,000	72.3	57,074	69.1

*Origin: "Present State of Post-Office Insurance and Pensions 1990" pages 11, by the Ministry of Posts and Telecommunications.

K-5 Types of Personal Pensions Bought (based on multiple responses)
(Surveyed by Life Insurance Culture Center)



* Origin: "Pension Guide for a Secure Future" p.15, by Life Insurance Culture Center (Jan. 1991)

III. Special Problems Involved in Personal Pensions

It is logical that the demand for personal pensions rises with the aging of society. Then what groups of people are particularly in need of personal pensions?

1. **Those who expect to receive lower benefits from governmental pensions, public pensions or social security pensions:**
   People who cannot expect to receive much in annual benefits from welfare pensions and/or various mutual aid pensions should purchase personal pensions at their own expense to compensate for the expected shortfall. Those people whose length of service

was short (which means that the period for which they paid premiums was short, and the period for which they participated in pension programs was also short) must plan to supplement their funds for the retirement years by purchasing personal pensions. This, however, raises something of a conflict, in that those who had a shorter length of service and/or lower wages are rather unlikely to be able to afford personal pensions. But on the other hand, they definitely need to purchase personal pensions because the benefits from the national pension for non-employees is almost always lower than that from the welfare pension benefit or mutual aid pension benefit for employees. Those people insured by the national pension who are self-employed or free-lance need to buy personal pensions.

2. **Those who are likely to reach the uppermost limit of public pension benefits:**
People with higher salaries naturally receive a higher pension benefits, however, a public pension benefit has an upper limit. Accordingly, they will not receive benefits which exceed that upper limit. The amount of that benefit should be sufficient for them to live in their retirement days, but they may find it uncomfortable because of the need to lower their previous living standard. To avoid such a reduction, they need to purchase personal pensions in line with their own judgment and expenses.

3. **Those who are not covered by any corporate pension:**
Not every company provides a corporate pension such as company pension, tax eligible pension plan, and welfare pension fund pension. Further, those people insured by the national pension, which is a pension for non-employees, are not covered by corporate pensions. For this reason, this group of people also should purchase personal pensions to prepare for their retirement.

4. **Those who will receive smaller benefits from their corporate pension:**
Even when a company provides a corporate pension, the employees should enroll in a personal pension if they can expect only small benefits from the corporate pension because of low corporate pension benefits, a short period of service or lower earnings.

5. **A corporate pension that includes a pension for survivor(s):**
If, for instance, a corporate pension may function so that the benefit to a husband, an ex-employee who begins receiving his corporate pension benefit following retirement from the company upon reaching retirement age, is discontinued when he dies. If so, then his wife or other survivors will suffer from economic distress. For this reason, wives and children should purchase their own personal pensions ahead of time to prepare for their retirement years. If the position of the husband and wife is switched, making the wife the chief breadwinner of the family, then the need for the husband to obtain a personal pension is greater.

6. **Those who retire at a younger age:**
People who retire at a younger age naturally have more retirement years ahead of them. And what could be worse than the benfit amount from a public pension being lower because of their shorter period of participation in the pension. Therefore, they must not avoid considering the joining of a personal pension to compensate for the difference. In the past, many female employees or insured females tended to suffer

from this problem in Japan.

7. **Those with no child:**
It is a rapidly increasing trend that children are not interested in taking care of their elderly parents. This is also true in Japan. This means that aged parents have to depend on personal pensions.

8. **Married couples with a wide difference in ages:**
Married couples with a large age difference are more likely to have one partner living considerably longer than the other and living alone in his or her golden years. Therefore, an easier way to prevent their standard of living from falling after one of the partners dies, each partner should think of purchasing a personal pension to prepare for future living expenses.

9. **Single females or males:**
It is strongly suggested that single females or males should purchase such personal pensions because of the widely accepted principle that living alone costs more per person than two people living together.

10. **Those who expect to live or have lived outside Japan for an extended period of time:**
The public or governmental pensions do not yet fully or extensively take into account the period of time spent outside Japan. Accordingly, those people who work for foreign companies and work in a foreign country should prepare for their retirement days by at least purchasing personal pensions. The situation is the same for Japanese as for people in any other country.

11. **Those with unstable social standing:**
There are people who can expect only a limited benefit from public or governmental pensions. Such people include, for instance, a wife whose husband has deserted her, and although very rare, national public service personnel or local public service employees who have been sentenced to imprisonment or other heavy punishment, punished for delinquency, or sentenced to administrative punishment. These people need to make up for the limited amount of benefits by purchasing personal pensions at their own expense.

The following section discusses the special personal pensions that have recently been introduced and other personal pensions that are expected in the future.

(a) **Variable-Amount Pension:** Variable-amount insurance has already been released, and as the next step, a variable-amount pension is being planned for release. The variable-amount pension system is expected to be nearly the same as that of variable-amount insurance except that it is designed to pay pension benefits that will change in the future, while death benefits or matured insurance is paid in fixed amounts. The popularity of variable-amount insurance was explosive when it was first released, but it quickly lost popularity in Japan after Blue Monday, when investment yields suddenly fell. A similar risk is attached to the variable-amount pension. It will be a high-risk, high-return personal pension designed to prevent reduced pension security. It is unavoidably accompanied by a risk from fund investments.

(b) **Pension with automatically increasing benefits:** This pension is designed to increase the amount of pension benefits automatically by adopting a credit-like system for paid premiums or by adopting a payment system that takes bonuses into account.

(c) **Pension insurance for existence security:** This pension does not include a death benefit or a guaranteed pension benefit paying term. It may be referred to as a Japanese version of the so-called Tonchin pension. This type of pension is considered better suited for women (who have longer average life expectancy longer average remaining years than their husbands, and who do not need to leave any inheritance or assets to their surviving spouses), single persons or people who have sufficient assets or expensive life insurance for covering death security.

(d) **Personal pension with special contract for retirement home:** This type of pension enables the contractors or insured people to enter and spend the rest of their life in a retirement home by applying the pension benefit to the rent of the home. There are people with enormous assets resulting from the rapidly soaring prices of homes with land, the trend of which is peculiar to Japan, but who can neither afford to buy a pension nor pay to enter a retirement home. Those people can stay in their own homes until they reach a certain age, then move into the retirement homes using the pensions they have purchased with the funds borrowed against their own homes as security. "Musashino-City" system which is already in use in Japan has some aspects in common with the personal pension, and it may be considered a public precedent because it is handled by the city.

(e) **Pension with house as security:** This pension is for people who have assets such as houses and lands. These persons can receive benefits for the rest of their lives by using their assets as security. In terms of system, it is almost the same as the personal pension with a special contract on a retirement home, except for one difference; this pension is designed only to finance the purchase of the pension. In this way it provides a living for the rest of the buyer's life with the purchased pension. The personal pension with special contract for a retirement home is designed to provide the buyer with a retirement home or introduce them to a retirement home so that they can move in. When the insured dies, the insurance company will dispose of the houses or lands to collect the loaned funds. This type of pension is not likely to become popular in Japan where the family system still remains strong and many people still respect the parent-child relationship.

(f) **Pension for nursing the aged (Pension that includes supply of actual articles):** In the aging society, the number of aged suffering from senility or who are bedridden is increasing. This presents a serious nursing problem. It has been decided that pensions for merely supplying financial support are inadequate to solve the problem. Based on the need for a solution, a personal pension which supplies both financial support and actual articles, including nursing services has been discussed and released in some areas. Specifically, the nursing services include referral or dispatching of visiting maids, home helpers and nurses. Although this type of pension may present insurance managerial problems, social demand seems to be high.

(g) **Joint pension:** This pension has already been prepared as a personal pension and placed on the market. However, it has not been fully understood because of its complicated system. It is anticipated, however, that this pension will become popular in Japan where the average life span and remaining days are expected to be further prolonged, especially those of women and wives.

Pension is designed not only to provide security but also to incorporate the operation of funds and other financial activities. More specifically, the mathematical principle of pension for calculating the premium and benefit takes into account the operating profits, i.e., the interests accruing from such financial activities. Accordingly, an expected interest rate on which such calculation is based becomes a concern. In general insurance companies, the pension premiums are combined with the premiums of other insurances to form a large fund pool to take advantage of a huge amount of funds with an interest rate ranging from 5.5% to 5.75%. (The expected interest rate will probably be about 4.5% when the variable-amount insurance, i.e., the variable-amount pension appears.)

The Japanese insurance industry is under strict government control in many aspects by the Ministry of Finance. This is because personal pension insurance must be public by nature, placing a special importance on the connection with welfare. In addition to guidance, supervision, regulation and control, the insurance industry also receives administrative measures for protecting and nurturing the industry. Particularly noteworthy are the high, thick wall that blocks new companies trying to enter the insurance market, and "fleet administration". The insurance premium is publicly calculated based on an insurance company with the poorest managerial efficiency, and all other insurance companies determine the prices or values of the insurance and pension insurances by that particular premium, and they sell their products at the calculated price. Therefore, large companies with a bigger managerial scale frequently "make a great profit", and even "make too much profit" from time to time. To improve the situation, administrative measures were changed to emphasize enhancement of service quality. This benefits citizens by introducing the competition principle inside and outside the insurance industry, thus activating their management.

First, competition among the insurance companies in Japan was started. Then, entry into Japan of overseas insurance companies to develop sales activities was allowed (although the number of such foreign companies is still very small). Further, the insurance companies were allowed to develop fullscale financial activities, while at the same time, various other types of financial agencies were also allowed to begin full-scale security business activities. The personal pension was the first highly competitive product to result from all those administrative efforts. First, the Post Office Life Insurance Bureau of the Ministry of Posts and Telecommunications released a new post-office pension (the word "new" is added to the recently developed pension to distinguish it from the conventional post-office pension). The new post-office pension was followed by life insurance companies who created and marketed various types of personal pension with great success. Then, other groups such as trust banks, city banks, regional banks, agricultural cooperatives, labor unions, consumer cooperatives, securities companies, credit unions, damage insurance companies and local governments began releasing a series of personal pensions, personal pension insurances and other products similar to personal pension.

Personal pension insurances are connected with tax. A certain amount of premiums paid is taken as the life insurance premium deduction and adds to the reduction of income tax. More specifically, it reduces the buyer's income taxes and local inhabitant's tax. The reduction rate in Japan, however, has been receiving criticism because it is much lower than that in other countries. Furthermore, the maximum reduction rate, 50,000 yen annually is likely to be criticized as too little, especially when it is compared with the recently developed regional type or functional type of national pensions which are being released and for which deduction from income tax of monthly premiums up to 68,000 yen (annually 816,000 yen per head or 1,632,000 yen for husband and wife together) are possible.

K–6

Life Insurance Premium Deduction from Income Tax

Category	Annual premium paid	Amount deducted
① For general life insurance premium	¥25,000 or less	Full premium amount paid
	Over ¥25,000 to 50,000 or less	(Annual premium paid × 1/2) + ¥12,500
	Over ¥50,000 to 100,000 or less	(Annual premium paid × 1/4) + ¥25,000
	Over ¥100,000	The full ¥50,000
② For personal pension premium	¥25,000 or less	Full premium amount paid
	Over ¥25,000 to 50,000 or less	(Annual premium paid × 1/2) + ¥12,500
	Over ¥50,000 to 100,000 or less	(Annual premium paid × 1/4) + ¥25,000
	Over ¥100,000	The full ¥50,000

Life Insurance Premium Deduction from Inhabitants Tax

Category	Annual premium paid	Amount deducted
① For general life insurance premium	¥15,000 or less	Full premium amount paid
	Over ¥15,000 to 40,000 or less	(Annual premium paid × 1/2) + ¥7,500
	Over ¥40,000 to 70,000 or less	(Annual premium paid × 1/4) + ¥17,500
	Over ¥70,000	The full ¥35,000
② For personal pension premium	¥15,000 or less	Full premium amount paid
	Over ¥15,000 to 40,000 or less	(Annual premium paid × 1/2) + ¥7,500
	Over ¥40,000 to 70,000 or less	(Annual premium paid × 1/4) + ¥17,500
	Over ¥70,000	The full ¥35,000

Pension benefits annually received are categorized as sundry income and are subject to income tax. In other words, if the total amount of the sundry income reaches 250,000 yen or more, it is subject to the withholding tax (10%).

It is widely accepted that the welfare pension fund pension, the eligible pension and the in-house pension, regardless of whether they are quasi-public pension (= quasi-private pension) or private pension, all derive from the retirement allowance plan and the retirement lump sum grant. As with the non-government pensions and corporate pensions, the following three views or theories have been presented from early stages regarding the retirement allowance:

(A) Livelihood security theory:

It is commonly recognized that the retirement allowance basically functions to provide financial security in retirement. This "livelihood security theory" places the greatest emphasis on that function of the retirement allowance. After World War

II, when many were finding it difficult to secure a livelihood, the theory was very popular. Therefore, the theory conceptualizes the retirement allowance from a social viewpoint. One weakness of this theory is that "the retirement allowance plan and corporate pension cannot avoid being controlled or scaled down as the government pension, public pension or social security pension is improved." Another weakness is represented by the question, "Why is it unavoidable that a company assumes a part of the public pension or social security pension? And what about those non-employees or non-salaried persons?" Such weaknesses, however, can turn into advantages of the theory; whether it is public, quasi-public, private, government pension or non-government pension, they are all intended to pursue and implement security of livelihood. This makes it possible to provide financial security in retirement through an inter-complementary system that involves mutual correlation and cooperation.

(B) Service reward theory (Service bonus theory):

In this theory, the retirement allowance and corporate pension are considered as rewards or bonuses that business owners or enterprisers award to employees, workers or salaried persons for their achievements and contributions to the companies during their terms or service. The amount of the retirement allowance and corporate pension is determined by the length of service, the type of duty, the level of responsibility and position. Such systems may largely resemble benevolent gifts presented by the management. Accordingly, the theory may be convenient and easy for the management to accept. On the other hand, from the standpoint of employees, the theory is considered dangerous in that it may be used to promote intensified labor, or used as an approach for managing labor or for intensifying productivity, which could result in "pressure in the workplace". Thus, while management accepts the retirement allowance and corporate pension as an effective approach to labor management, employees have regarded them as leading to intensified labor.

(C) Deferred payment theory:

The earnings of salaried and other employees are always less than the value of their labor during the service period. This theory, therefore, is based on the idea that the unpaid wage should be cleared in one lump sum as the retirement allowance at the time of retirement. According to the theory, it may be difficult to "shift from the retirement allowance to pension", and such a course would be somewhat logically unjustifiable. If employees or labor unions insist on this theory, then the management may insist that they should withhold their demand for immediate raise since they expect the management to make up for it later with the payment of the retirement allowance. This would produce a really strange situation. It would look as though labor unions or the labor movement had accepted or approved of such partially unpaid earnings or partially inadequate payment of earnings (even though it may be unavoidable), causing inconsistency in the labor movement. The most important aim of the labor union or labor movement should be winning a raise in earnings. Another weakness of this theory is a question which is very likely to arise from management, "How should we interpret the occurrence of bankruptcy with regard to paying retirement allowances?"

In early Japan, there was a system under which when an employee or apprentice worked for a company or shop and contributed to the business over a long period of time, and ultimately, the business owner or master supplied proper funds to the employee so that he could open his own shop ("setting up a shop in the same business"). This traditional Japanese practice, according to some, is the origin of the retirement allowance plan. The modern retirement allowance plan, however, should be considered different from that earlier practice because the modern plan has a different objective and function. It is inappropriate to consider the modern retirement plan as being derived from or having any connection with the older practice.

Basically, earnings are remuneration for labor performed. This is not entirely true with the retirement allowance. Therefore, there is a way to supply the retirement allowance in a pensionlike system. The retirement allowance heavily involves the concept of a service reward because of the typical way the amount of retirement allowance is calculated as shown below:

Amount of retirement allowance supplied
= Basic salary × Supply rate based on the number of service years

The formula obviously demonstrates a bias toward the level of contributions to a company, strongly presenting the nature of a service reward. In contrast to this, the corporate pension plan, which has been developed from the retirement allowance plan, shows less of the service reward nature. The total amount of pension supplied to an employee depends on the pension amount itself, but it also depends on the length of period that the benefits are received (the longer the person lives, the longer the benefit receiving period becomes). At any rate, it may be appropriate to consider the retirement allowance as incorporating all three factors; the characteristics of a service reward, the characteristics of welfare for protecting retirement livelihood and the characteristics of a deferred wage payment. The retirement allowance includes those characteristics or functions, which are blended differently for each case.

There are other countries having such retirement allowance plans, but the retirement allowance plan in Japan may be one of the most advanced. The Japanese retirement allowance plan has been nurtured in a special environment typically represented by the lifetime employment system that is a characteristic of Japanese society. Other nurturing factors include the hierarchical system based on the type of occupation and position, and the seniority-based earnings system. Those systems were, of course, intended to attract and maintain high quality labor (stable securing of an excellent labor force). At the same time, they were intended to enhance employees' awareness of and identification with their companies, to improve the relationship between labor and management, and to achieve greater work efficiency.

In Japan, we have witnessed changes in the work environments at companies from the end of the World War II to the present (fiscal 1991), especially in the later period.

(A) Increased income level:

It has become possible for an employee, at his own initiative, to set an amount aside

K-7

	Views from management	Views from employees
Retirement due to personal reason	Service reward + Benevolent aid	Deferred wage payment + Benevolent aid
Retirement due to company's convenience	Service reward + Unemployment allowance	Deferred wage payment + Unemployment allowance
Retirement at age limit	Service reward + Support of retirement	Deferred wage payment + Support of retirement
Retirement due to death or injury during service hours	Service reward + Support of survivor's livelihood	Deferred wage payment + Support of survivor's livelihood
Retirement due to death or injury during non-service hours	Service reward + Temporary livelihood support for survivors + Benevolent aid	Deferred wage payment + Temporary livelihood security for survivors + Benevolent aid

from his increased income in partial preparation for his retirement. Thus, the importance of the retirement allowance as a factor in livelihood security has lessened.

(B) Gradual increase and enhancement of measures for assuring retirement security:
Government pensions, public pensions and social security pensions, especially welfare pensions, are being improved, causing a change in the positioning and expected functions of the retirement allowance. In other words, the position of the retirement allowance is gradually being shifted to the corporate pension which lies midway between public social security and personal security to complement the functions of those two types of security.

(C) Less fear in losing jobs:
The high economic growth period after the war in Japan temporarily suffered from serious depression, overpopulation and serious unemployment. Those troubles were overcome and the unemployment insurance and employment insurance were started. Thus, the importance of the retirement allowance in supporting livelihood during a period of unemployment has significantly lessened (this trend has grown also due to the increased opportunities for finding new jobs). Instead, there is now stronger demand for financial security for the retirement years, which are growing longer. It appears that the aging society and economic growth have led to the need for a "shift from retirement allowance to pension".

(D) Prolonged service period:
This unavoidably leads to an increase of each retirement allowance amount, thus increasing the total retirement allowance amount. The aging society has prompted the age limit to be raised at many companies. At the same time, it has increased total amount of retirement allowance borne by a company, bringing the possibility of bankruptcy from paying retirement allowances or a hostile relationship between the young and old employees in a company in some cases. Efforts to solve such

problems have brought the implementation of a "shift from retirement allowances to pensions" in the pursuit of equal bearing of retirement allowance.

(E) **Accelerating technological innovation:**
If the speed of technological innovation had remained as slow as it was in the past, the level of contribution to a company, which is a major factor for deciding the amount of retirement allowance, would be proportional to the number of years of service. However, today's greater speed of technological innovation has dramatically decreased the labor value of "skill" (the arrival of an age of semi-skilled labor). The result is a decrease in the importance of retirement allowance. Instead, the importance of financial security after retirement has increased.

(F) **Change in employee's family structure:**
Typical changes are the collapse of the traditional family system and the prevailing of nuclear families. This trend also strengthens the demand for a pension for retired couples rather than for a one-time retirement allowance. The trend of retirement allowances being used to purchase a home or to pay off the balance of a home loan is declining. Thus, what people expect of the retirement allowance is changing.

(G) **Increasing movement of labor from company to company:**
Labor is increasingly moving around among companies. This trend makes it almost meaningless to calculate the amount of a retirement allowance in proportion to the number of service years. In this kind of trend, a corporate pension based on a portable pension, i.e., a pension add-up plan is more logical.

[External Reserve Type Retirement Allowance Plan]

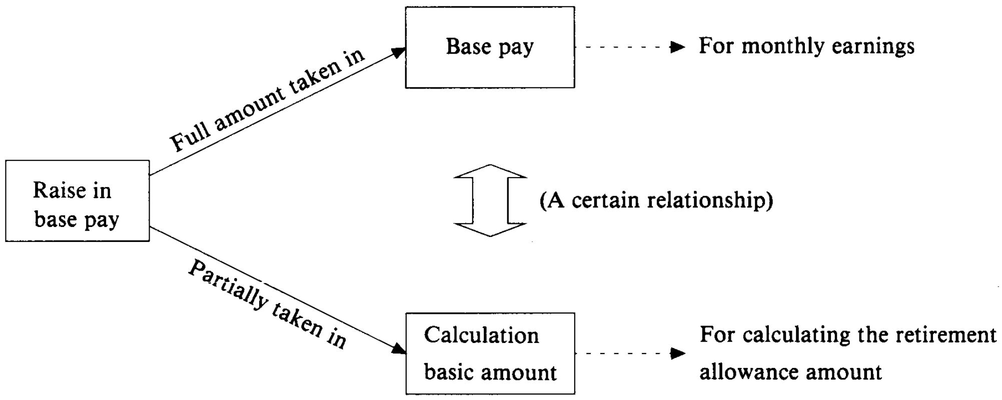
Medium and small business retirement allowance mutual aid plan
Retirement allowance mutual aid for specific lines of business
Mutual aid plan for particular retirement allowances
Retirement allowance mutual aid plan for staff at social welfare facilities
Eligible retirement pension plan
Welfare pension fund plan

A "shift from the retirement lump sum grant to a corporate pension plan" and a "shift from retirement allowance to pension" are the prevailing trend in today's Japanese society. The retirement allowance, an indirect or auxiliary benefit supplied by a company can, however, meet society's current demands if proper managerial improvement is added. For instance, instead of adding the whole amount of a raise in base pay into the base pay, a part of the raise should be withheld and set aside for something other than the base pay. This should prevent the whole amount of the raise in base pay from being reflected in the retirement allowance. Thus, significant or limitless increases in the amount of retirement allowance can be controlled by breaking the relationship between the raise in base pay and regular raise and the retirement allowance. This leads to the advent of a concept and system "the second base pay," which is not included in the calculation of the retirement allowance amount.

Another alternative is to take a strict approach in which the retirement allowance supply rate is always decreased according to a raise in base pay. In this method, the retirement allowance is deferred.

Still another alternative is to adopt a unit price rather than base pay, and use such unit price as a basis for calculating the amount of retirement allowance. This method disconnects the relationship between the retirement allowance and the raise in base pay.

K-8 Calculation Basic Amount Method



In addition to the method establishing the second base pay, other methods have also been devised. In the separate-table method, a different wage table is used for calculating a retirement allowance. This separates the retirement allowance from the wage system. Another system, the marks method, is generally based on accumulated marks multiplied by a unit price. With the marks method, each functional grade is assigned a certain number of points. Cumulative marks from the time an employee joins the company to the time he or she quits the company are determined by multiplying the marks of each grade by the number of years the employee stays at each grade. Then, the determined cumulative marks are multiplied by the unit price per point.

Lastly, there are some measures for improvement to deal with the later retirement age limit. In one measure, the increase of the supply rate for an employee who has exceeded a certain number of service years is controlled. In another measure, no additional benefit is supplied for the number of service years after the original retirement age. Still another measure adopts a stalemate wage system in which the wage for an employee over a certain age is fixed regardless of a later retirement age limit.

[Reference Materials]

A. Advantages for management

1) Since the pension plan is long-term, it helps enhance employees' interest in their companies and establish long-lasting stable relationship between labor and management.
2) The pension helps to greatly relieve employees from worrying about their retirement, and it can lead to improved productivity.
3) Most pensions are supplied only to aged employees or to those who have worked

for a long time, therefore encouraging employees to stay with a company for a long time.

4) The pension plan provides security in retirement. This ensures smooth retirement at the retirement age, resulting in appropriate replacement of old workers by new workers.
5) The pension payment system protects a company from paying out a great amount of money at one time. Instead, it enables the company to effectively use the money as a fund for business activities.
6) In the case of a contributory plan, an increase in the benefits means an increase of the amount borne by employees, thus controlling the demand for a raise in benefits.

B. Advantages for labor unions

1) The pension, which provides a fixed amount of benefit every year over a long period following retirement, is more effective for providing livelihood security than the retirement allowance plan, which supplies a lump sum of money at the time of retirement.
2) Employees do not have to worry about how to manage or handle a lump sum of money to which they are not accustomed.
3) The pension plan is more comfortable to employees who are familiar with receiving regular paychecks.
4) Smooth retirement of older workers is ensured, thus providing younger employees with more opportunities for promotion.
5) A reserve plan allows its accumulated fund to be effectively used as the fund for welfare mutual aid.
6) By combining the pension plan with the one-time allowance, the tax amount applied to the whole retirement allowance can be decreased.

There are several approaches for shifting the retirement allowance to the retirement pension plan. The retirement pension plan, however, must be continued and operated as long as a company exists (according to the principle of everlasting pension plan or the principle of perpetual prosperity of pension plan). Therefore, once a company adopts the retirement pension plan, it is not allowed to alter or abolish the retirement pension plan as required by the company. For this reason, when shifting from retirement allowance to pension, it is necessary to carefully consider the company's present state and long-term prospects and to the balance between the benefit amount and the amount borne, so that a successful pension plan can be established. This should involve the participation of employees and labor unions, and also ensure full understanding by all employees. The table below summarizes the adjusting methods for the reserve for retirement allowance and the retirement pension:

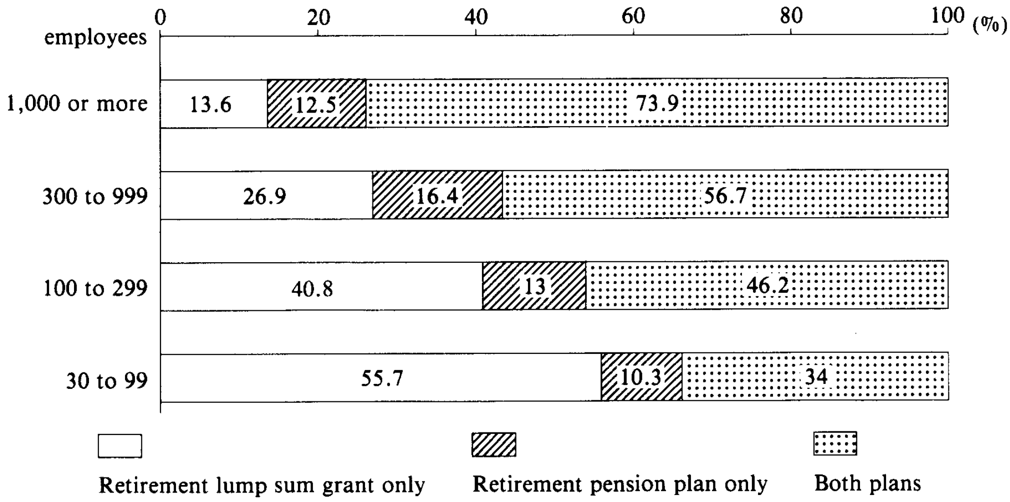
K-9 Adjustment between Retirement Pension and the Reserve for Retirement Allowance

Type of retirement pension	Tax adjustment		
	Need for adjustment	Limit amount of transfer to reserve for retirement allowance	Withdrawals from reserve for retirement allowance
Full shift[1]	Yes	Zero transfer limit amount	Full amount withdrawals required
Partial shift (within the limit)[2]	Yes	The transfer limit amount is calculated based on the retirement allowance amount to be supplied, from which the amount of a pension plan benefit is excluded.	Withdrawals is required if the accumulated limit amount prior to adjustment is exceeded.
Partial shift (beyond the limit)[3]	Yes	The transfer limit amount is calculated according to a revised regulation on retirement allowance	Withdrawals is required if the accumulated limit amount prior to adjustment is exceeded.
Partial shift (Retirement-age shift)[4]	No	Same as the previous limit amount	Not necessary. When, however, an employee retires at the age limit, settlement processing is required.
Addition[5]	No	Same as the previous limit amount	Not necessary

Notes: 1) The full shift means that the retirement lump sum grant is abolished, and the retirement pension plan is adopted.
2) The partial shift within the limit means that the regulation on retirement allowance is revised to partially adopt the retirement pension plan.
3) The partial shift beyond the limit means that the regulation on retirement allowance is revised to separately adopt the retirement pension plan.
4) The partial shift at the retirement age means that the regulation on retirement allowance is revised to adopt the retirement pension plan only for employees who retire at the retirement age.
5) The addition means that the retirement pension plan is added without changing the regulation on retirement allowance.

[Reference Statistical Tables]

K-10 Retirement Allowance Plans Calssified by Company Scale
(as of November 1990)



K-11 Retirement Allowances Supplied to Average Male Employee Classified by the Type of Benefit Supply (as of November 1990)

(unit: ¥10,000)

Academic career, Type of employee, Company scale		Retirement lump sum grant only	Retirement pension plan only	Both plans
College graduates (Managerial/administrative/ technical jobs)	Company scale	1,219	1,400	2,009
	(No. of employees)			
	1,000 or more	1,956	2,068	2,590
	100 to 999	1,360	1,510	2,124
	30 to 99	1,134	706	1,778
Junior-high & high school graduates (Managerial/administrative/ technical jobs)	Company scale	1,107	1,249	1,920
	(No. of employees)			
	1,000 or more	1,731	1,780	2,348
	100 to 999	1,291	1,480	2,023
	30 to 99	1,011	612	1,727
Junior-high & high school graduates (Work-site operations)	Company scale	927	1,178	1,815
	(No. of employees)			
	1,000 or more	1,705	1,729	2,016
	100 to 999	1,078	1,378	1,961
	30 to 99	833	643	1,662

K-12 Distribution of Model Total Retirement Allowance Amount

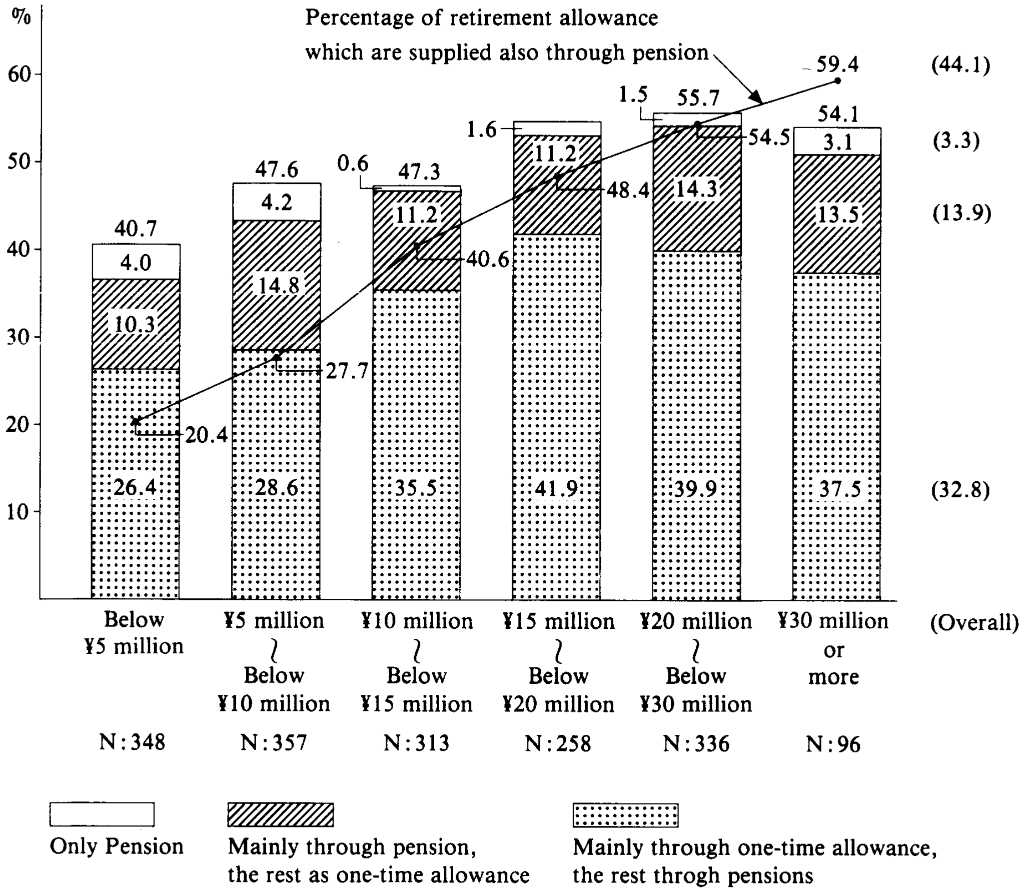
(Male employees with 30 years of service, classified by size of workfore)

(in 1989; unit: %)

		Below ¥5 million	¥5 million ~ Below ¥10 million	¥10 million ~ Below ¥15 million	¥15 million or more	Unknown	Average (unit: ¥10,000)
Size of workforce	99 or less	13.5	27.7	20.9	8.8	29.1	889
	100 to 299	6.5	23.2	28.4	11.2	30.8	1,060
	300 to 999	2.0	11.2	25.0	27.3	34.5	1,359
	1,000 or more	1.0	5.0	23.3	34.8	35.7	1,621

K-13 Percentages of Employees Who Wish to Receive Their Retirment Allowance Also in the Form of Pension (classified by the amount of retirement allowance)

(May and June 1990)



K-14 Reasons Why Employees Wish to Receive Their Retirement Allowance throough Pension

(multiple-answer method; unit: %)

		N	Easier to live on	Tend to spend one-time allowance	Advanta-geous tax wise	Cannot effectively apply one-time allowance	Too much money to receive at one-time	Cannot think of effective use of one-time allowance
Overall		345	84.1	33.6	23.2	20.3	18.6	16.8
Age	Twenties	126	81.7	40.5	19.8	19.8	12.7	7.9
	Thirties	103	90.3	25.2	22.3	21.4	23.3	22.3
	Forties	56	85.7	28.6	26.8	16.1	16.1	23.2
	Fifties	60	76.7	38.3	28.3	23.3	25.0	20.0
Desired method	Full amount received through pension	66	78.8	34.8	25.8	16.7	21.2	30.3
	Mainly through pension with the rest as one-time allowance	279	85.3	33.3	22.6	21.1	17.9	13.6

K-15 Requests on the Retirement Allowance Plan

Employees selected as many requests as they wanted from those listed below regarding the retirement allowance and corporate pension:

1. The period of receiving corporate pension should be lifetime → "Lifetime supply of corporate pension"
2. The age when an employee starts receiving corporate pension and the receiving period should be made optional → "Optional age for beginning receipt of corporate pension"
3. Materials and explanation on the corporate pension plan and the retirement one-time allowance should be supplied → "Provision of materials and explanation"
4. Employees should also contribute installments to increase the amount of corporate pension → "Corporate pension installment borne by employees"
5. The corporate pension of a previous employer should be added when an employee moves to another company → "Add-up system for corporate pension"
6. The amount of corporate pension should slide up with prices → "Slide-up of corporate pension with prices"
7. Rather than providing retirement one-time allowance or corporate pension, a service such as assuring a right to move into an old people's home should be provided → "Right to move into an old people's home
8. Rather than providing retirement one-time allowance or corporate pension, a corporate house or company-owned land should be sold at lower price → "Selling corporate house or company-owned land
9. A certain portion of retirement one-time allowance, which is not needed immediately should be held by the company at a certain interest → "Deferment of retirement one-time allowance"
10. Information on operating retirement one-time allowance and corporate pension reserve should be supplied → "Supply of information on application"

IV. Functions and Growth of Corporate Pensions

In Japan, various private, non-governmental pensions which are not accepted as social security pensions are called corporate pensions. These are, however, established to complement the areas that cannot be satisfied by public pensions. Some corporate pensions can be practically regarded as semi-public, semi-private pensions or quasi-public pensions because they take the place of some functions of public pensions, governmental pensions or social security pensions. They are at least not purely personal pensions or private pensions. Such corporate pensions come in a non-contributory plan pension whose premium is entirely borne by the companies, and a contributory plan pension whose premium is partly borne by the employees or salaried men. In either type, its major function is the same; to fulfill employees' economic security in their retirement days.

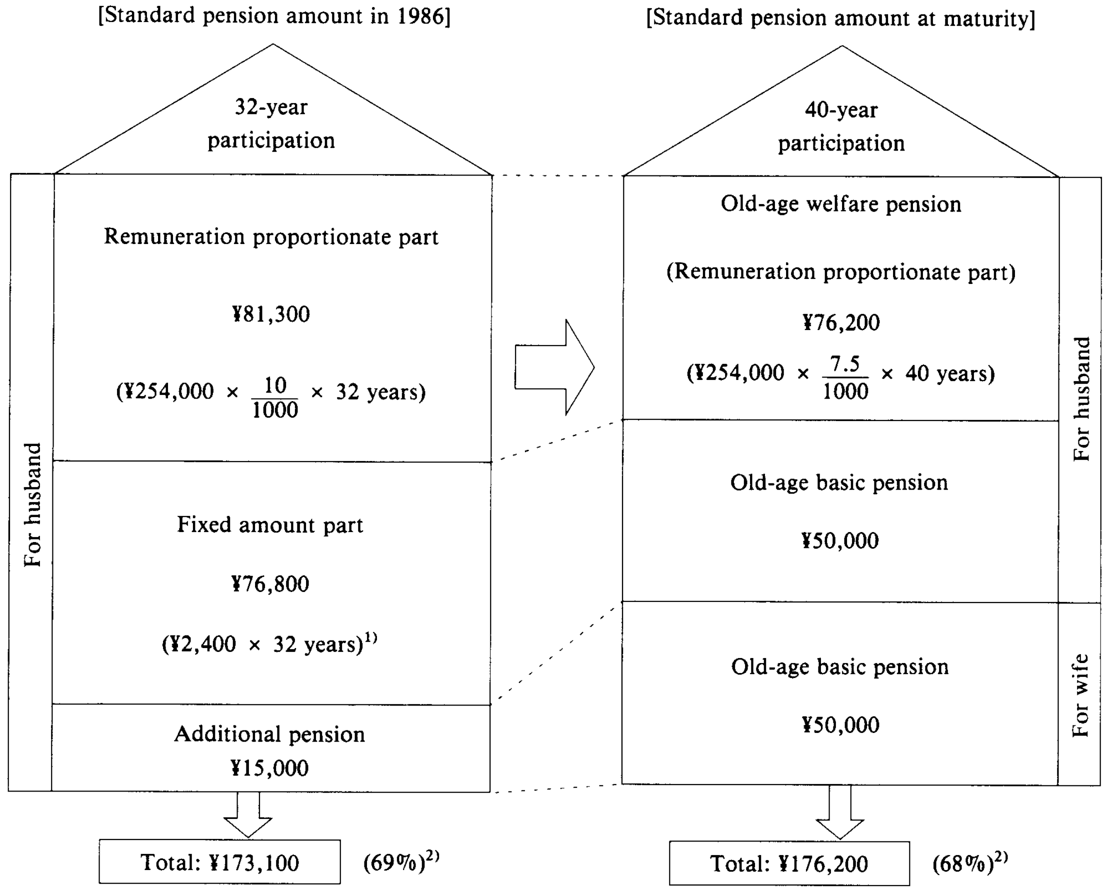
In Japan, the public pension system was twice significantly amended, in 1985 and 1989. The amendment carried out in 1985 was particularly highly rated in Japan and abroad as a radical amendment and reorganization of the Japanese public pension system. The amendment introduced the basic pension in the national pension. There is a noteworthy aspect of the amendment in connection with the direction of the future corporate pension. As a result of the basic pension being introduced, the portion of the old-age basic pension (incorporated in the national pension in the same amount for husband under the husband's name and wife under the wife's name) in the welfare pension insurance system was increased, causing a reduction in the portion of the remuneration proportionate pension (the portion of the old-age welfare pension).

In 1985, there began a worldwide trend and opportunity to demand reconstruction of the free world through activation of economy and restructuring of the system through re-evaluation of the spirit of competition in a capitalistic economy in a true sense. This led to the belief that those who work harder and contribute more are paid higher wages; that those who are paid higher wages will receive better pension benefits as a result; and that those receiving better pension benefits will live better in their old age.

In Japan, however, the pension reform attached even more importance to the fixed amount portion of the pension benefits. Conversely, the portion of the benefits proportional to remuneration, in which the wage level is reflected in the pension amount, was constricted within the pension benefit structure. This pension reform gave rise to the claim that "under these circumstances, corporate pension must take a new path and function effectively to compensate and reward employees who worked hard and contributed more to the company". This is a marked departure from the past words and actions of the labor unions and their activists, who claimed that they "absolutely opposed the implementation of corporate pension, because such a plan would be used as a tool for labor management and intensification of labor". Such a drastic change in the position, evaluation and expectations concerning corporate pension was brought about by the seriousness of the rapid progress of the aging of Japanese society. In other words, the trend of the times is about to change the ways of corporate pension.

The ultimate role of corporate pension is to complement the government/public/

K–16



* The amounts are based on the prices in fiscal 1984.

Notes: 1) Converted to the prices in fiscal 1984 according to the unit price ¥2,050 amended in 1980.

2) The rates in percentage (%) are based on the average standard monthly remuneration ¥254,000 for males in active service.

social security pensions. Since the recent pension reform has resulted in a suppressed level of welfare pension benefits (for the present and future), this complementary role of corporate pension is absolutely essential, and its importance can only increase in the future. At the same time, corporate pension is expected to play a substitute role for personal pension. As in the rest of the world, the burden of income taxes here is heavy, and the progressive tax rates are unusually high. Under these circumstances, employees at many successful or large corporations are starting to show an appreciation for better corporate pension plans more than for higher wages. Rather than receiving higher wages and paying a lot of taxes, while spending part of those wages to purchase personal pension plans, it is considered more efficient and profitable to accept a somewhat smaller wage increase, but receive the difference in the form of pension insurance contribution, which will result in better pension benefits.

<Functions of Corporate Pension in Japan>

1. Complement social security pension Substitute for personal pension

2. Labor management functions

1) Introduction of young, high quality work force (Attracting such workers).
2) Voluntary resignation of old work force (Encouraging retirement).
3) Improvement of labor relations in the company by fostering the workers' loyalty toward the company through a long term guarantee of a living standard throughout employment (wages) and retirement (corporate pension benefits).
4) Enrichment of corporate welfare. Management of corporate pension fund to promote employee welfare and various welfare activities, including health, cultural and educational programs.
5) Management of pension fund to establish and expand disaster relief fund, congratulations and condolences fund, maintenance and educational fund, surviving child pension, survivors pension, and disability fund systems.

3. Financial management functions

1) Retirement fund maintained outside the company
The corporation hires an ouside source (life insurance company, trust bank or other financial institution) to manage the corporate pension in order to ensure payment of corporate pension benefits for employee's old age, regardless of the state of the company's business, and even in the event of possible bankruptcy. Here, the function of corporate pension is defined as "retirement fund maintained outside the company", based on the fact that corporate pension is a variation of retirement fund.
2) Leveling of retirement allowance expenditure by adopting pension installment system
To avoid the problems caused by the fluctuation of the number of retirees each year and the subsequent fluctuation of the total amount of retirement allowance, retirement allowance expenditure is restructured into fixed expenditure in the form of installments or premiums, enabling consistent management of corporate finances. Each corporation develops an efficient way to bear thc cost of retirement allowance.
3) Profitable, high-return management of corporate pension fund
The corporation expects and promotes the most profitable fund management and the highest interest rate possible, whether the fund is managed by the corporation itself or by an outside financial institution. By achieving such goals, the corporation is able to increase pension benefits, control the rise of pension premium, and increase employee welfare activities.
4) Establishing a good reputation in the society and achieving higher business goals through better labor management and successful financial management enabled by the introduction of a corporate pension program.
In the end, these functions will contribute to the modernization of the management of the corporation and, ultimately, the industry, and to the improvement of their image.

<Types of Corporate Pension in Japan>

1. Classification by the Method of Accumulation and Management of Corporate Pension Fund

A. Non-Reserve Financing Plan (Pay-as-you-go plan)

B. Reserve financing Plan: Paying installments toward the pension fund, starting before becoming eligible for benefits.

(1) Company Pension/Internal Pension: Accumulation of pension reserve fund within the company. Company or internal reserve.

(2) Eligible Retirement Pension: Accumulation of pension fund or reserve fund at an outside financial institution (outside or external reserve). The fund must be managed according to the eligible retirement fund contract which meets the tax requirements, e.g., management for the sole purpose of providing retirement pension (including lump sum payment), payment of installment or premium to a trust bank or a life insurance company, and management according to appropriate pension mathematical principles.

(3) Welfare Pension Fund Pension: This is also a type of pension in which the pension fund or reserve fund is accumulated at an outside special financial institution (outside or external reserve). The purpose of this pension, however, is to provide the old age welfare pension of the welfare pension insurance plan (a type of government pension and major part of public pension) in place of the government and to further increase the benefits. It is provided with the approval of the Minister of Public Welfare. This pension was created in response to strong demand by corporations and business owners for adjustment of public welfare pension and retirement allowance for more reasonable cost responsibilities, based on the fact that these two plans share the function of guaranteeing a standard of living in one's old age. Because of this adjustment function, this pension plan was called "adjustment pension" when it was established in 1966. The issue of adjustment of lump sum retirement allowance or corporate pension as corporate welfare and welfare pension played a significant role in the establishment of this plan. Traditionally, Japanese corporations have promoted the "group management system" and the "business family concept", which resulted in highly developed corporate or non-legal welfare facilities and systems. These characteristics are still prevalent in today's Japanese corporations, and the retirement allowance plan is a very important part of such systems. It is understandable that the adjustment of retirement allowance and newly established corporate pension, or the adjustment of welfare pension itself and corporate pension, became an important issue. To address this issue, the welfare pension fund system and the pension derived from that system (also called adjustment pension) were established.

K-17 Comparison of the Welfare Pension Fund Plan and the Tax Eligible Pension Plan

Category		Welfare pension fund	Tax eligible pension plan
Corporate scale		700 or more employees May be jointly established by a parent company and its subsidiary, or by companies of the same trade.	15 or more employees 100 or more employees in the case of a trust agreement
Type of pension		Shall be a perpetual annuity. The benefit amount may be increased or decreased during the benefit payment period.	It may be either terminable pension or perpetual pension.
Selective one-time allowance		Can elect to take all or a part of the benefit as one-time allowance, the upper limit being the amount covered by the guaranteed period or 90% of the current price of the pension, whichever is smaller.	Can elect to take all or a part of the current price of the pension as one-time allowance.
Calculation of premium		Both standard and special premiums may be paid in a fixed rate or fixed amount. The depreciation term of PSL (past service liability) is between 7 or more years and 20 or fewer years.	A longer PSL depreciation term is acceptable.
Handling in tax system	Corporate premium	Full amount is loss of money	Full amount is loss of money
	Premium of the principal	Social insurance premium deduction	Life insurance premium deduction
	Accumulated fund	The special corporate tax of 1% applies to a portion exceeding the level of the national public service personel mutual-aid union.	The special corporate tax of 1% applied to the full amount of the accumulated fund.
	Benefit	The full amount of benefit is taxable as an income. (The pension benefit is defined as a salary income. The one-time allowance is defined as a retirement income.)	The amount determined by deducting the principal's premium amount is taxable as an income. (The pension benefit is defined as a salary income. The one-time allowance is defined as a retirement income.)
Management method		A fund (special corporation) is established to handle all necessary jobs for the fund, including the determination and collection of premiums, the management of records, and decision and payment of benefits.	A corporation concludes contracts with trust banks or life insurance companies to take care of the necessary jobs.
Partial substitution of welfare pension		Essential condition	None

* The table is based on the data opened to the public by the Federation of Welfare Pension Fund in April 1986. The figures have been updated according to the changes in society and the economy. (A problem involved in the updating is discussed later.)

The company pension plan offers the advantage of increased freedom in benefits and design. A company pension may be set up according to the company's circumstances, and is advantageous in that it is a hedge against inflation through increased income from internal corporate investment and increased ability to contribute due to the growth of the company. In other words, this is private insurance (although it is questionable if it can be defined as personal pension. It certainly is private pension, and cannot be defined as semi-public, semi-private pension or quasi-public pension) that also plays the role of self-financing. Therefore, this plan is susceptible to the danger of loss of pension benefits if the company goes bankrupt or performs poorly. In other words, there is no guarantee of pension rights.

The eligible retirement pension or tax eligible pension receives approval of the National Tax Administration Agency by meeting certain requirements of the Corporate Tax Law, and is given tax incentives. It has the advantages of relatively simple application and management procedures. Corporations have utilized this plan extensively as a means of leveling the burden of retirement allowance expenses (a part of financial management). This plan can be classified as semi-public, semi-private pension or quasi-public pension.

The systems related to financial security in retirement comprise two groups; one includes government pension, public pension and social security pension, and the second group includes non-government pension, quasi-public pension and corporate pension. These are considered the two major props (although it is common to add personal pensions to make it three major props). Regarding the corporate pension, the two major props are considered to be the eligible retirement pension and the welfare pension fund pension. (In-house pension is added to form three corporate pension plans). Employees or salaried persons in private companies are expecting much from corporate pensions. Measures provided by companies to ensure employees' retirement security include profit sharing plan, wage-economy savings plan and employee stock ownership in addition to the corporate pension. Furthermore, in Japan, there are several retirement allowance mutual aid plans such as the medium and small business retirement allowance mutual aid plan, the retirement allowance mutual aid for specific lines of business, and the mutual aid plan for particular retirement allowances. Those plans are also contributing greatly to the security of retirement. It is roughly estimated that the public pensions pay 50% to 60% of the necessary living expenses in retirement, the corporate pension pays 15% to 20% and the individual efforts, particularly, personal pensions pay the remaining 20% to 35%.

There are several different types of in-house pension; one type is designed to reserve the source fund in a company by utilizing the reserve for retirement allowance plan. Another type is designed to reserve the pension source fund at financial institutions by utilizing group pension and the like. Still another type does not have any special reserve, but it supplies pension benefits as required every year from the management fund. The in-house pension does not have tax incentives, and the pension income tends to be unstable because of its close relationship with business results or management conditions in the company. For this reason, the in-house pension can be carried out only by a company which is confident of maintaining healthy management. Because of this, public characteristics have not been approved for in-house pensions. In contrast, the welfare pension fund pension, which partially substitutes for the welfare pension, is naturally regarded as a quasi-public pension. Likewise, the eligible retirement pension is also regarded as a quasi-public pension, since it gets tax incentives. It requires government or government agency permission for establishment, and it is subject to governmental control. Thus, the eligible retirement pension is subject to certain restrictions and requirements.

The eligible retirement pension was approved as an extra-corporate contributory pension plan and granted tax incentives under the corporation tax law (Act No. 34, 1965) revised in April 1962, and the income tax law (Act No. 33, 1965). Incidentally, the eligible retirement pension is occasionally referred to as the tax eligible pension or frequently abbreviated as the eligible pension). The eligible pension, to qualify for eligibility, must satisfy the following conditions, which are specified under Art. 159 of the corporation tax law enforcement act (Government ordinance No. 97, 1965):

1. The plan's sole aim is to supply retirement pension, including retirement one-time allowance.
2. The plan is a trust agreement with employees specified as the beneficiaries, or an insurance contract which specifies employees as the beneficiaries of insurance money.
3. No corporate executives or sole proprietors can join the plan.
4. The installment and benefit amount are calculated according to an appropriate pension calculation method.
5. The regular installment is based on the fixed-amount method, salary-proportionate method or other similar method.
6. Regarding the repayment of the past service debt, the annual repayment amount is 20% or less of the total past service debt amount, and it is based on the fixed-amount method or the salary-proportional method. Further, repayment at a fixed rate within 30% of the unpaid past service debt is also acceptable.
7. For surplus, at certain intervals (each interval should be less than 5 years), the amount exceeding the liability reserve is applied to installments or to other similar objective.
8. In principle, no required reserve amount is returned to a business owner.
9. When a contract or agreement is discontinued, the required reserve amount reverts to an employee.
10. No employee is subjected to undue discriminatory treatment.
11. No business owner gets advantages such as privileged loans. Also, no business owner may give personal instructions on application for a trust agreement.
12. The contract or agreement is expected to continue for a significant period of time.

After the eligible retirement pension is established and implemented, it is handled taxwise as follows:

1) The full amount of installment contributed by the company is allowed to add up as a financial loss. The life insurance premium deduction applies to the installment contributed by employees.
2) The pension is taxed as salary income, while the one-time allowance is taxed as retirement income (the amount borne by employees is excluded).
3) The special corporate tax at a 1% tax rate applies to the reserve (excluding the amount

borne by employees).

4) When a company shifts from the retirement allowance plan to the eligible retirement pension plan, withdrawal from the reserve for retirement allowance must be implemented according to a specified procedure.

The characteristics of the eligible retirement pension are better understood when it is compared with the welfare pension fund:

(1) The eligible retirement pension is more flexible than the welfare pension fund in designing the plan.
(2) It permits easier absorption of a corporate welfare plan.
(3) Its characteristics are nearer private pension than is the welfare pension fund.
(4) Regarding the procedures for initiating the plan, the welfare pension fund requires a permit by the Minister of Health and Welfare, which takes a few months, while the eligible retirement pension takes no time because its application may be submitted afterward.
(5) The welfare pension fund is to supply the remuneration-proportionate portion of the welfare pension in place of the government. Thus, it is based on that substitutional portion, and therefore, even the additional portion decided by each company is subjected to restrictions when it is actually designed. It is truly the tax eligible pension or eligible retirement pension from the standpoint of tax eligibility, but it has design restrictions based on the self-reviewing procedures. Nevertheless, it permits more flexible design than in the welfare pension fund.
(6) The installment (exemption rate) applied to the substitutional supply of the remuneration-proportionate portion of the welfare pension in the welfare pension fund is to be paid to the fund. (The premium which is exempt from being paid to the government is called the exempt premium.) Each company calculates its own installment amount; therefore, the benefits can generally be paid under the exemption rate if the average age of company employees is lower (a company with many young or female employees). A company with many mature or aged employees cannot cover the benefits with the exemption rate, and it may encounter difficulties in establishing a fund. A difference large enough to cover the benefits under the exemption rate is called a substitutional advantage. A company which produces such substitutional advantage goes ahead and establishes the welfare pension fund, while a company whose benefits significantly exceed the exemption rate will select the eligible retirement pension plan.
(7) It is possible to shift from the eligible retirement pension to the welfare pension fund, while there is no way to shift the welfare pension fund to the eligible retirement pension.
(8) The welfare pension fund is more advantageous taxwise than the eligible retirement pension, especially in terms of the tax on reserve.
(9) While the welfare pension fund is taken as a quasi-public pension, the eligible retirement pension is one level lower than that, i.e., it is taken as a quasi-"quasi-public pension". The welfare pension fund, however, may be said to have slightly reduced its nature as a public pension after its in-house operation based on expanded operation

methods has been accepted.

The following major considerations exist for designing the eligible retirement pension plan:

(1) Scope of participants,
(2) Qualification for participation,
(3) Date of participation,
(4) Qualification for receiving benefits,
(5) Time to start the supply of pension,
(6) Period over which the pension is supplied,
(7) Selective one-time allowance,
(8) How to decide benefits,
(9) Benefit standard,
(10) Contribution method, and
(11) Handling of related companies.

[Functional Comparison Between Eligible Retirement Pension and Welfare Pension Fund Pension]

A. Function of financial security in retirement
   Eligible retirement pension — Not very satisfactory because the benefit period is 10 years or less in most cases.
   Welfare pension fund — Almost wholly satisfactory.

B. Preparatory function
   Eligible retirement pension — Satisfactory.
   Welfare pension fund — Satisfactory.

C. Labor management function
   Eligible retirement pension — Functions satisfactorily especially because of its flexibility.
   Welfare pension fund — Functions satisfactorily. In particular, its benefits are highly appreciated. It can also be effective in labor management through welfare project activities.

D. Return financing function
   Eligible retirement pension — None
   Welfare pension fund — Provides return financing to participants with an upper limit of 25% of the pension assets to promote the welfare of participants.

Initially, although eligible retirement pensions had been established, many employees tended to select the one-time allowance, This is considered a result of the following reasons peculiar to japan. Firstly, the previous benefit standard made the pension look really insufficient, which is now being slightly improved. Secondly, many employees, when they retire, still have home loans to repay, and they frequently tended to pay them off with the retirement one-time allowance. Recently, however, many companies, especially large ones, are beginning to introduce a plan for encouraging employees to own their homes, so that employees can obtain loans at low interest from their companies at an earlier stage of their careers. The companies may even mediate the acquisition of homes for employees. Thus, the second problem has been improved. Thirdly, employees were afraid that receiving long-tierm pension benefits would incur a larger decrease in value due to inflation than receiving retirement one-time allowances. This problem, however, is being solved because inflation is cooling. Some have tried to apply their retirement one-time allowances to high-interest operations, but they frequently ended in bitter experiences due to recent upheavals in the financial environment, violent fluctuation of interests and financial changes in Japan. This has also helped encourage employees to select the pension.

After the country's defeat in World War II, many Japanese developed a mistruct of government and of companies. That mistrust largely faded as the economic reconstruction went smoothly, bringing amazingly rapid economic growth, thus more employees came to select the eligible retirement pension, which retains strong ties to their companies even after they retire. This trend toward the eligible retirement pension is expected to grow further even if receiving the retirement one-time allowance becomes more advantageous taxwise. Behind this trend are continuing extensions of the average life span and life expectancy, and the further aging of society.

As the first step, it is necessary to shift from the retirement allowance plan to the eligible retirement pension plan. At this time, the shifting rate becomes a necessary consideration. The percentage of those selecting the pension is another consideration. Just seeing the arrival or a pension age is meaningless. The eligible retirement pension plan should be a breakthrough for shifting from the retirement allowance plan to the pension plan.

Establishing or introducing the eligible retirement pension or the welfare pension fund pension would be meaningless if employees select the retirement one-time allowance. Here are several possible measures for increasing the percentage of the eligible retirement pension being selected.

a. It is necessary to publicize and explain to employees that receiving the pension rather than the retirement one-time allowance is more dependable in the aging society and more advantageous in most cases. At this time, it should be emphasized that the pension is the right choice in light of the average life span and remaining days are very likely to continue extending. It is true that receiving the retirement one-time allowance is more advantageous taxwise than receiving the pension. Selecting the retirement one-time allowance, however, is not entirely advantageous because the pension benefits also offer the benefit of having no tax charged up to a certain amount. More specifically, for people under 65 years, a received annual amount of up to 700,000 yen is non-taxable, and for people of 65 years or more, a received annual amount up to 1,400,000 yen is non-taxable.
b. Receiving a part of the retirement one-time allowance should be made possible. More specifically, a flexible method should be developed so that an employee can select to receive his or her source fund partly through the retirement one-time allowance with the remaining source fund received through the pension, or vice versa.
c. It should be made possible to select the age at which benefits begin. There is no need to start supplying the pension to every participant when he or she reaches 60 or 65

years. The standard age to begin receiving the pension should be made flexible so that it can be advanced or delayed according to the situation of each participant.

d. The benefit amount should also be made flexible so that it can be increased or decreased as necessary. For example, the benefit amount may be increased for a certain period as a "bridging pension", then the amount may be adjusted according to the "additional pension" approach after the participant reaches the age that qualifies for receiving the welfare pension benefit.

e. The yield during the pension supply period should be set higher than the current estimated interest of 5.5%, to provide a higher pension amount for the present. This should make the pension more attractive, helping to encourage more employees to select the eligible retirement pension rather than the retirement one-time allowance. As an alternative, the estimated interest may be set adequately lower than the actual interest to assure stable pension financial state and stable income and outgo of the pension in the future. Or the surplus resulting from setting such a low interest may be returned to the participants through dividend. The best way to attract more employees, however, is to use the actual interest for the estimated interest from the beginning to set the estimated pension amount higher rather than taking such alternatives.

We also need to discuss measures for improving the eligible retirement pension plan in Japan for the future.

Firstly, we must improve the pension benefit itself. Conventionally, the majority of the eligible retirement pensions were of the 10-year terminable annuity, term annuity or definite annuity which uses the retirement allowance source fund. The increasing average life span and remaining days are giving rise to the strong demand for extending the supply period. Accordingly, the adoption of a life annuity, perpetual annuity or lifetime annuity would add greatly to the attraction of the pension, leading to better financial security of employees' retirement days. It would naturally add to the load from the pension on business owners or companies, however, such increased load should be nearly repaid by increased productivity because of the improved welfare that would effectively motivate the employees.

Secondly, the application of the fund produced by accumulated pension installment money should be more active. It should be applied at high interest to produce a profit which can be used for improving the pension benefit.

Thirdly, the contribution by employees should be raised to raise the pension benefit amount. The fact that increasing the pension benefit amount is more advantageous taxwise than raising salaries is very persuasive. Labor unions should carefully compare and discuss the advantages of the "fight for higher earnings" and the "fight for improved pension" when they develop their labor strategies.

The fourth consideration is to make flexible the contribution and the repayment rate of past service liability. Every category of business and every company experiences variations in business cycles, so they can contribute or repay a greater amount during prosperity and vice versa. Accordingly, more flexibility should be introduced for improvement.

The fifth consideration is to provide the eligible retirement pension with measures for protecting employees from a decreased value of security because of inflation. An inflation sliding-scale pension would be even harder to establish than the welfare pension fund. This is because the inflation sliding-scale portion in the welfare pension fund is assumed by the government while there is no such system available for the eligible retirement pension. A possible solution is a gradual-increase pension. Although this type of pension adds to the load on companies, it is well worth trying.

The sixth consideration is to provide the eligible retirement pension also with the tax incentives equal to those of the welfare pension fund. At the same time, constant efforts should be made to request tax incentives that encourage more people to select the pension rather than to receive the retirement one-time allowance. In general, it has become essential to provide measures for reducing tax on the eligible retirement pension to make it more appealing.

The seventh consideration is to strive to achieve a life pension also in the eligible retirement pension just as in the welfare pension fund. Basically, the life pension is regarded as the ideal form of pension, and therefore, offering the life pension should be considered logical in light of the welfare pension fund pension.

The welfare pension fund system and the pension derived from that fund are characterized by their function of adjusting the welfare pension (government pension / public pension / social security pension) and the corporate retirement allowances, and the newly established corporate pension and the retirement allowances. It also provides the old age welfare pension portion of the welfare pension in place of the government. This "substitute function" gives this type of plan a unique position, but in general, the plan can be classified as semi-public, semi-private pension, quasi-public pension, or something close to government pension.

2. Classification by Form of Welfare Pension Fund Establishment

A. Single Fund:
A corporation establishes a fund by itself. As a general rule, one fund is established for a pension plan that includes all applicable offices belonging to that corporation.

B. Combined Fund:
When two or more corporations have a substantial cooperative relationship such as exchange of officers and other capital or personnel interaction centering around a main corporation, the main corporation establishes a joint fund together with the other corporations. Cooperative joint fund by a parent company and subsidiaries.

C. Comprehensive Fund:
When most of the small businesses in the same or similar industries are unified by a trade association, a health association, or a similar organization with strong influence, a number of businesses in the organization establish a joint pension fund. The economic structure of Japan still has a dual structure, although not as clearly as in the past; in this dual structure, large corporations and small companies play separate but complementary roles. It is a distinctly Japanese characteristic that small companies (and there are many of them, playing essential roles in certain industries) establish their own comprehensive pension fund.

3. Classification by Method of Providing Welfare Pension Fund Benefits

A. Substitute Method:

Benefits are designed in the same manner as the substitute portion. The benefit amount is calculated as follows:

Average standard salary during participation period × Prescribed rate ($10+\alpha/1000$ to $7.5+\alpha/1000$, according to date of birth) × participation period

Since this calculation method is the same as that of the proportional remuneration portion of the welfare pension, the method is standard and easy to understand. It is, however, not necessarily suitable for achieving the goal of smooth transition of corporate retirement allowance system.

B. Additional Method:

In addition to the basic portion, in which the substitute benefits are provided in the same method as the substitute portion, a portion calculated by a different method is added according to the situation of the corporation. By incorporating individual corporate goals and methods in the additional portion, the corporation can achieve a design with diversification of benefits and establish a pension that matches the needs of the company. This is a prime example of the labor management function of a pension plan. The plan is also easily adaptable for transition of corporate retirement allowance system into a pension fund system.

C. Mutual-Aid Type:

Also called "Merger Type", since it merges the substitute portion and the additional portion by using the final salary or the average salary of a most recent period according to the company's plan, as the basis of calculating benefits. The calculation formula is as follows:

Standard salary × Prescribed rate (or multiplying factor by participation period)

This type of plan may be classified as a government-related agency pension.

Probably the most important of the corporate pension plans is the welfare pension fund, for the following reasons:

(1) It sets an example for other corporate pension plans by being somewhat more democratic in nature; it is operated by an organization with management and labor participation;

(2) It is a national cooperative system based on the Welfare Pension Fund Federation; and

(3) It matches the trend of the time, i.e., more frequent movement of employees (labor) between corporations, by providing aggregate pension and/or portable pension in the form of the Federation Aggregate Retirement Pension Plan. Under this plan, if a person drops a welfare pension fund plan and acquires another plan, he/she may be eligible for the Federation Aggregate Retirement Pension at the age of 60, provided through the Welfare Pension Fund Federation, which acts as the aggregate center. This aspect of the plan is certain to become a significant advantage of the fund pension in future years.

As described above, welfare pension fund and its pension have significant advantages over the other types of corporate pension. Therefore, the future goal of the corporate pension plans in Japan should be to encourage all corporations, large and small, to establish corporate pension plans, and to steer such corporate pension plans, especially eligible retirement pension plans, toward welfare pension fund, at the earliest opportunity. The methods of establishing combined or comprehensive fund will be very useful for this purpose. It is also necessary to ease the standards for fund establishment. As a result, a recent reform allowed establishment of a fund with at least 500 participants for a single fund, at least 1,000 participants for a combined fund, and at least 3,000 participants for a comprehensive fund.

The minimum number of employees for independently establishing a welfare pension fund was reduced from 1,000 to 700. The minimum requirement has now been further reduced to 500. This should cause Japanese corporate pensions to be the fund pensions of the future.

In fiscal 1989, 100 new funds were born. The number of funds reached 1,358 with 9,030,000 participants. This is more than 30% of the number of persons insured by welfare pensions, which equaled 29,830,000 at the end of September 1989. In April, an additional 48 funds were established. It is expected that extremely smooth growth of the funds will continue for another few years. The fund plan was begun in 1966, and at the end of that year, 142 funds were established; the number of funds has steadily increased year by year. After 1971, however, the number of new funds suddenly decreased, with only 9 funds being established all year (compare this with fiscal year 1967 when 163 funds were established). The same situation arose again during the period from 1975 to 1980, with the sluggish climate continuing until 1984. In 1985, the public pensions were reorganized, and new pension plans were introduced, leading to a rapid increase of new funds. The number of new funds had already begun a gradual increase toward 1984. Welfare pension forms the other support of public pension and is a governmental pension and also social security pension. It was decided that the welfare pension should cover slightly less than 70% of the average wage of workers in active service, which is slightly more than 50% in terms of annual income (in Japan, the annual income is actually much more than 12 times the monthly wage or salary after adding in the twice-yearly bonuses) as the retirement benefit. In Japan, however, food expenses are high, and housing expenses are even more expensive (especially in big cities). Therefore, the pension's living security of 70% or 50% mentioned above does not ensure stable financial support in retirement. For this reason, the demand for the corporate pensions has rapidly increased, and thus more new corporate pensions and welfare pension fund pensions were established.

V. Recent Considerations on Corporate Pensions in Japan

The welfare pension funds and the various corporate pensions based on such funds are presently undergoing a dramatic change due to the influences exerted by the amendments of the government pensions, public pensions and social security pensions in Japan. They are also being influenced by the growth of non-government pensions, private pensions and personal pensions in Japan. Essentially, the change should be regarded as progress, and through this stage of improvement, their nature and the way they function as semi-public, semi-private pension and the quasi-public pensions will be significantly enhanced in Japan. Corporate pensions are intended to replace personal pensions, while at the same time complementing public pensions. Based on this understanding, the Japanese Government is approving and promoting them. Typical of these efforts, are the special tax considerations given to corporate pensions. Thus, the Japanese Government supports and is expecting further growth or corporate pensions, especially the welfare pension fund pension. In this setting, corporate pensions are presently in the midst of improvement and amendment.

A. Benefit Level and Contents of Corporate Pensions and Welfare Pension Fund

Twice recently the welfare pension for employees and salaried men and the pensions for workers and employees of Japanese private enterprises have been amended. As a result, it was decided to maintain the benefit standard for the full pension or model pension with 40-year participation at 69% of income. Any raise exceeding that level is prohibited. Although the 69% rate drops to 50% or 55% when bonuses are taken into account, the rate is considered too high as a benefit standard for employees' pensions when compared with the wages, and especially the disposable income, of workers in active service. On the other hand, from the psychological point of view, people can hardly accept a living standard that is significantly lower than the living standard they maintained before their retirement. This is why corporate pensions were required; they provide something extra to help maintain the insured living standard at as high a level as possible. Accordingly, several formulas were devised as shown below. After all, the expectation of workers regarding their corporate pensions has risen sharply.

(1) Welfare pension benefit + Welfare pension fund benefit = Income before retirement
The objective of this formula is to combine the welfare pension benefit amount (69% of the average standard monthly remuneration amount) to the welfare pension fund benefit amount, making it equivalent to the amount of disposable income before retirement of a person who has welfare pension insurance. It is not designed to ensure an income equivalent to the disposable income before retirement. Rather, it is designed to ensure the full amount of the income before retirement. This shows that the concept is shifting from the ensuring of nominal wage to the ensuring of real wage.

(2) (Public pension benefit + Welfare pension fund benefit) × 12 = Annual average standard remuneration amount = Monthly average standard remuneration amount × 12 + Monthly average standard remuneration amount × (5 to 6)
This calculation formula is not based on the monthly salary or annual income immediately before retirement. Instead, it is based on the monthly average standard remuneration amount* and the annual average standard remuneration amount (which should be possible as a concept). The formula is distinctive in

* The monthly average standard remuneration amount is determined by totaling the re-evaluated monthly standard remuneration amount of each term during the participation period of the welfare pension insurance, then the result is divided by the number of months of participation by the insured person. Replacing "month" with "year" in the description leads to the concept of the annual average standard remuneration as introduced by the writer, Niwata.

that it is based on an annual income amount. Because of the bonuses which are peculiar to Japanese companies, discussing the income of an employee according to his or her monthly income would not lead to accurate analysis. Any discussion should be based on the annual income which includes the bonuses. ("5 to 6" in the formula is the number of months' salaries corresponding to the amount of the bonuses supplied annually.)

(3) The mutual-aid pension for national public service personnel is actually better than the welfare pensions for salaried persons at private companies, i.e., the government pensions, public pensions or social security pensions. Therefore, people expect corporate pensions to at least make up for that difference to compete successfully with the mutual-aid pension. And now it is desibrable that the benefits of corporate pensions or welfare pension fund pensions be better, if possible.

(4) Welfare pension benefit + Welfare pension fundbenefit + Personal pension benefit = Income before retirement
The income before retirement means the income amount corresponding to the disposable income before retirement. According to the calculation, the insured persons will be able to enjoy retirement without reducing the level of their living standard from the level they enjoyed before retirement.

(5) Welfare pension benefit + Welfare pension fund benefit = Income immediately before retirement × 70%
A nominal wage is adopted as the basis of this formula. Seventy percent of that nominal wage is supplied. the formula is based on an assumption that the amount equivalent to 70% of the wage immediately before retirement should be enough to lead adequately comfortable life after retiring from a company at an advanced age.
The following formulas show the simplest comparison between the basic pension of the old-age welfare pension and the welfare pension fund:
Old-age welfare pension = Monthly average standard remuneration amount × 10 to 7.5/1000 × No. of participating months
Basic pension of fund = Monthly average standard remuneration amount × (10 to 7.5) + α/1000 × No. of participating months

Note: The first step of the calculation is to determine the average monthly salary of an employee over his or her lifetime, and to determine the percentage of that amount that the public pension benefit amounts to. The second step is to determine the percentage of the lifetime average annual income, which includes the bonuses (typically supplied twice a year totaling to an amount equaling 5 or 6 months' worth of salary in Japan), that the 12-month pension benefit amount corresponds to. The third step is to determine the percentage of the monthly salary immediately before retirement that the pension benefit amounts to. The last step is to determine the percentage of the annual income, including bonuses immediately before retirement, that the 12-month pension benefit amounts to. a simplified example is given below:
Lifetime average monthly salary × 69% = Model benefit amount of welfare pension
Lifetime average monthly salary × (12 + 5) × x% = Lifetime average monthly salary × 69% × 12

$x = 48.7 \fallingdotseq 50 \longrightarrow$ Annual pension income corresponding to 50% of lifetime average annual income

The annual income immediately before retirement is taken as approximately 1.5 times the lifetime average annual income.

Lifetime average monthly salary $\times$ $(12+5)$ $\times$ 1.5 $\times$ $y\%$ $=$ Lifetime average monthly salary $\times$ 69% $\times$ 12

$y = 32.47 \fallingdotseq 32.5 \longrightarrow$ The annual pension income corresponds to 32.5% of the annual income immediately before retirement.

The disposable income, disposable monthly salary and disposable annual income correspond to approximately 60% of nominal income, of nominal monthly saraly, and of nominal annual income. (This is typical in japan.)

When the pension annual income is 32.5% for 100%, then what percentage will it be when the basis reduces to 60?

$60 \times z\% = 100 \times 32.5\%$

$z\% = 54.16\% \longrightarrow$ Approx. 54% of the disposable income (disposable annual income) immediately before retirement

When a person retires under the age limit and lives only on the welfare pension, his or her actual living standard will be slightly higher than half that immediately before retirement.

Note: Concepts used here

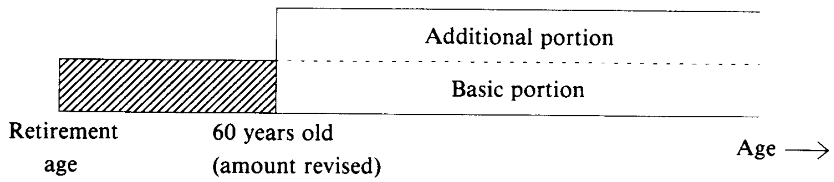
1. Monthly average standard remuneration amount and annual average standard remuneration amount
2. Monthly salary immediately before retirement and annual income immediately before retirement
3. Disposable monthly salary of lifetime average monthly salary and disposable annual income of lifetime average annual income
4. Disposable part of the monthly salary immediately before retirement and disposable part of the annual income immediately before retirement

The efforts to improve the corporate pensions and welfare pension fund pension should be focused not only on the standard of benefits but also on the contents of the benefit. The first of these efforts is the consideration given to the sliding system that takes inflation into account. Inflation in Japan is progressing at an extremely low rate compared with that in other countries. Japanese measures taken to control prices and the value of money seem to be exceptionally successful so far. Inflation, however, is the biggest enemy threatening those living on pensions, and there is a constant need for corporate pensions to adopt the inflation-based sliding system. In the case of the welfare pension fund, the substitute portion itself (which occupies a majority of the basic portion) slides with inflation, thus keeping in step with its major part, i.e., the welfare pension. Further, the welfare pension itself has been amended to slide automatically with prices. Thus, establishing a sliding system that is keyed to inflation may no longer be as difficult as was once generally believed. However, there is still the possibility that wildly soaring prices could occur, and virtually no corporate pension incorporates an inflation-based sliding system. At best, advanced corporate pensions adopt a gradually increasing type of pension. Other companies may put extra effort into reviewing their benefit amounts as necessary in accordance with changing situations, or into supplying a one-time allowance to compensate for reduced security. Basically, the expenses for adjusting pension benefits to inflation are usually borne by future generations, and they ultimately depend on the company's capacity for growth and investment profits. On the other hand, more companies in Japan are losing confidence in continuing growth rates that would be adequate to support such expenses. The impossibility of maintaining stable fund operation at a high rate of return has also become widely accepted. This is primarily because of the violent fluctuations in interest rates and the inherent instability of the financial market. Thus, it has become more difficult for corporate pensions to incorporate such inflation-based sliding systems.

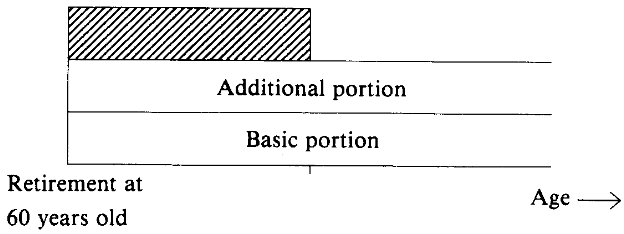
In addition, survivor pensions and disability pensions are not welcomed by insurance carriers or corporate mangers. There are, however, some cases where such pensions are implemented, though not really adequately, in the form of an allowance (not as pension benefit) as a part of welfare activities. There are some cases where a surviving-child pension is supplied; if an employee or insured person dies, his or her surviving child or children are supplied with educational expenses under a term annuity. The amount is being increased not only for the pension but even for one-time allowances.

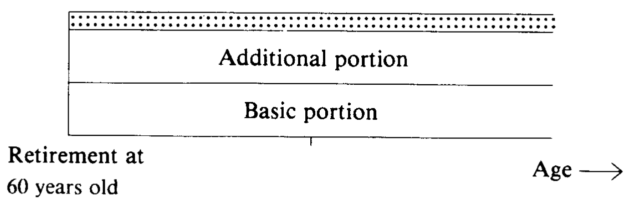
There is a plan to raise the age to begin receiving welfare pension to 65 in the near future (although there is no indication whether it is really possible to implement this in Japan). Based on the assumption that such a plan will really be carried out, some ideas for corporate pensions have been suggested:

1. **Stopgap type:**
   Adopts a special pension benefit that applies to the period from retirement under the age limit (from the end of receiving wages) to the time that benefits begin.



2. **Additional type:**
   Provides the basic portion and the additional portion with a fixed amount of life pension to which a terminable annuity is added. In other words, there is no stopgap

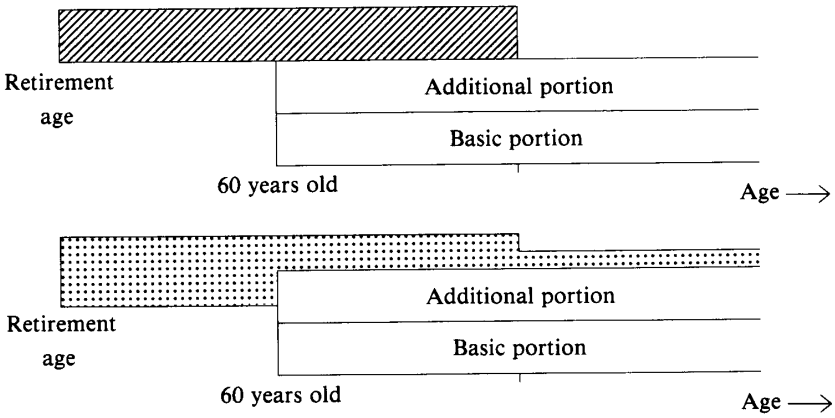




pension. There can be some cases where the additional pension is combined with life pension.

3. Mixture of stopgap and additional types:

This is commonly called a "pistol" type pension,



Note: The basic portion is paid in the same way as that for the substitute portion. The additional portion is provided in a different way from that for the basic portion according to the actual situation of each company.

B. Installment of Welfare Pension Fund

Many employees or salaried persons (the terms are interpreted almost identically as "workers" or "wage earners") participate both in the welfare pension which is the government pension, public pension or social security pension, and the welfare pension fund pension which is the semi-public, semi-private pension or quasi-public pension. Accordingly, they pay two different premiums. Strictly speaking, the payment for the welfare pension is called a premium, while the payment for the fund is called an installment (however, this is strictly a custom; there is no theoretical reason). The fund's purpose is not only to partially substitute for the welfare pension but also to supply benefits of at least 30%, in many cases, plus extra which brings it to more than 30%. Therefore, the installment amount of the fund as a whole should be higher than the premium amount for the welfare pension, but all such extra amount is borne by the companies. As a result, the amount an employee pays for the fund is identical to the premium of an employee who does not participate in the fund, i.e., identical to the premium for the welfare pension.

Premium: To be paid to the government. Expressed by <Standard monthly remuneration amount × Premium rate>

Regular installment: To be applied to the substitute portion of the old-age welfare pension and to the source fund for the additional pension peculiar to the fund. Expressed by <Standard monthly salary amount × Regular installment rate>

Installment for administrative expenses: To be applied to the expenses required for running the fund, and the full amount to be borne by companies. Expressed by <Standard monthly salary amount × Administrative expense installment rate>

As previously mentioned, the installment for the welfare pension fund is applied to pension benefits and a one-time allowance, and also to the expenses for running the project. For each month (the basis of calculating the pension benefit amount), the installment amount is collected according to the amount of the participant's standard monthly salary. Or, in another method, the installment amount is determined by multiplying the standard salary of each participant by a fixed rate, then a certain amount is added to that calculated amount as necessary. There are many possible factors that influence the installment rate and amount, and the installment amount is eventually determined by an appropriate pension mathematical principle formula. The formula should be established so that it will ensure a fairly level amount in the future. The financial system of the welfare pension fund is of exact fully reserve financing. This financial calculation requires extreme strictness. The basic rate is one of the factors for calculating the installment rate, and at least every five years, it is reviewed according to the actual situation of the time to establish a new installment rate which is used for financial re-calculation. The installment rate is influenced also by the responsibility level of past service and the length of its redemption period.

There is "exemptible premium rate" in Japan. The exemptible premium rate of the welfare pension fund is defined as a premium rate established as a level premium rate applied to the substitute portion when it is assumed that all insured members of the welfare pension establish a fund at a certain point. Among the premiums collected from the participants of the fund, the premium which is exempt from payment to the government applied to the source fund for the benefits substituted by the welfare pension fund. Because of such exemption, the premium rate is referred to as the exemptible premium rate.

The Premium that a participant of the welfare pension fund pays to the government as the premium of the welfare pension insurance is fixed at a smaller amount than that paid by the insured of a general welfare pension. The difference between the premium rate for the general insured and that for the fund participant may be referred to as the exemptible premium rate. Whether or not the welfare pension insurance benefits which the welfare pension fund substitutes can be paid within the range of the exemptible premium rate depends on the condition of the participants of the welfare pension fund;

1. A company with many female or younger employees is advantageous with respect to the exemptible premium rate.
2. If the age distribution becomes higher than it was when the fund was established, then the fund will eventually be insufficient with respect to the exemptible premium rate.
3. A company with a higher age distribution may have difficulty in establishing a fund with respect to the exemptible premium rate in the future.
4. An improved death rate (a financially threatening factor to the pension plan), an increased number of members receiving benefits with increasing average age, and raising the upper or lower limit of the standard monthly remuneration amount are all common phenomena observed with the current Japanese pension plan. These factors are expected to lead to increased benefit expenses, which, in turn, will result in an increased exemptible premium rate of the welfare pension fund.
5. The exemptible premium rate is determined based on the age distribution of persons

when the plan was first initiated and is based on the assumption that the age distribution will remain unchanged in the future. Therefore, as the average age increases, a figure based on that assumption unavoidably become unmatched to the actual situation. In a country like Japan, where the society is rapidly aging, the exemptible premium rate must be revised.

The following suggestions are for improving how the exemptible premium rate is calculated:

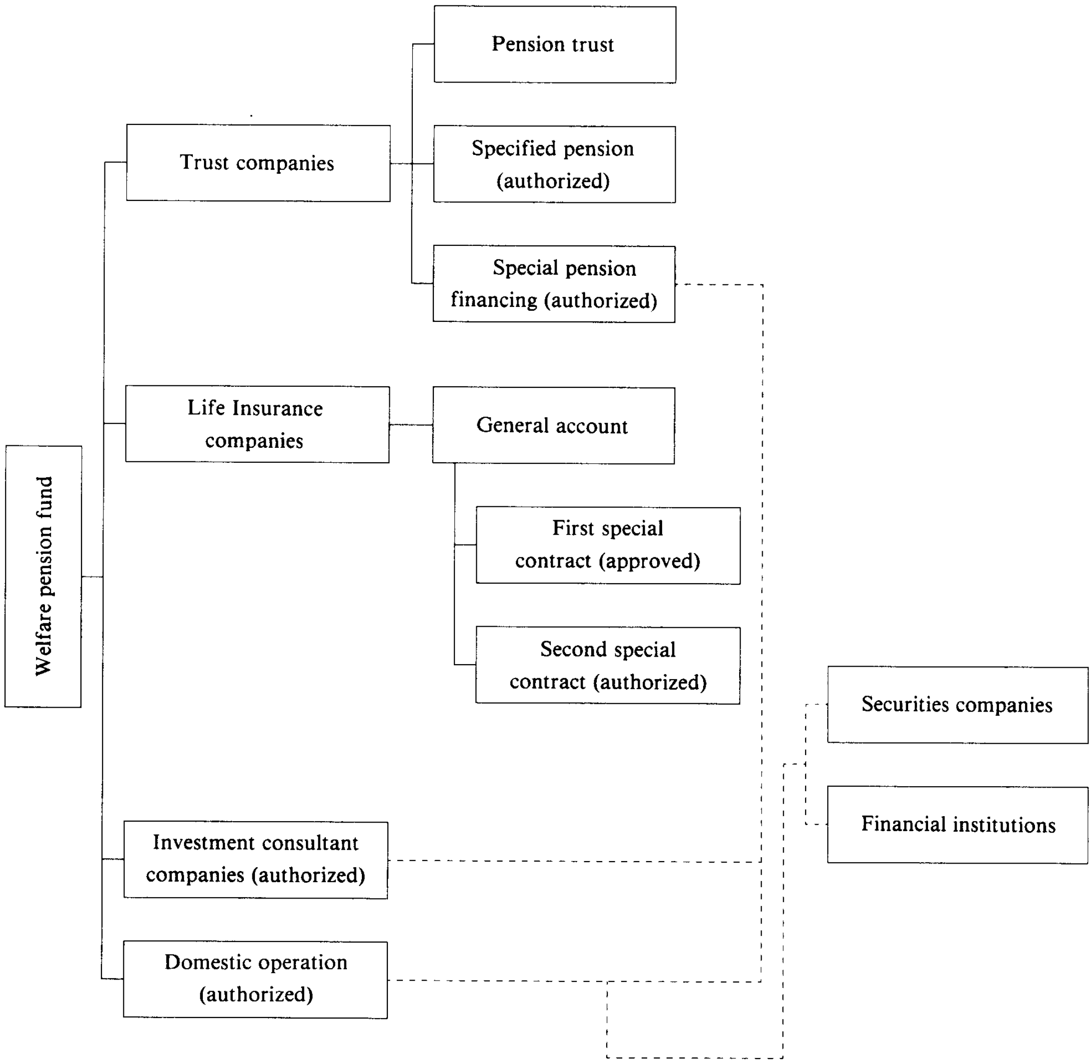
a. To establish an exemptible premium rate suited for each fund.
b. To pool an exemptible premium rate for the whole fund to adjust overs and shorts.
c. To allow a special exemptible premium rate for a deficient fund.
d. To review and modify the current Japanese fund pension, which starts supplying benefits unconditionally to participants when they reach 60 years old, so as to avoid raising the premium rate. (If participants aged 60 years or older still work and receive wage incomes, it may not be necessary to unconditionally supply fund pension benefits to them.)

C. Increasing Welfare Pension Fund Consignee Agencies

Management of corporate pension funds calls for efforts to activate or streamline just as other activities do. Recently, there is an increasing demand for establishing independent management as an independent or special corporation. This is because it is becoming necessary to clarify the responsibilities as well as to establish the independence. Efforts for improvement are being made in various aspects. Currently in Japan, "operation of assets" and "administration" are consigned to consignee agencies under a single contract. There is a trend to approve separating the two responsibilities to conclude a contract separately on each of them. Also, switching the conventional "obligatory consignment" to "optional consignment" is under discussion. Presently in Japan, it is obligatory to consign the management and operation of fund reserve funds to trust banks and life insurance companies. Some organizations who own a fund are capable of running the fund; therefore, making such consignments optional is being discussed. The number of agencies handling the actuarial job is increasing, and as the optional consignment is allowed in the future, the agencies operating fund capitals are likely to add investment advisors, city banks, securities companies and voluntary or self operation to the conventional trust banks and life insurance companies.

According to the Welfare Pension Act, as revised in December 1989, the number of authorized methods for operating pension assets was increased in April 1990. Life insurance companies have been consigned to handle premiums of the welfare pension funds and operate the pension fund for over 20 years since 1966. During that time, they have been implementing extensive operation of such pension funds to ensure long-term stability. Some examples are combining the pension fund with other insurance assets under general account to provide them for loans in Japan and abroad, stocks and bonds, real estate, etc. They have reportedly been providing special dividends for long-term contracts and also stable dividends supported mainly by interest dividend income under a guaranteed interest of 5.5%, thus endeavoring to respond to funds' expectations by operating

K–18 Agencies Managing and Operating Reserve Funds for Pension Benefit, etc.



highly safe and stable pension assets.

However, with the increasing financial liberalization and interest preference in the upheaval of the recent financial revolution, two special types of contracts were developed under the same operation rules (30% or less stocks, 20% or less assets in foreign currency, etc.) as those for general accounts. The first special contract accepts participation of any funds, while the second special contract accepts only funds that satisfy certain requirements under the new operating rules (50% or more highly safe assets, the upper limits set on the operating percentage of stocks and assets in foreign currency, etc.) provided by the revised Welfare Pension Insurance Act; one of the requirements is that the funds must have been in existence 8 years or more. However, the basic policy for operating the pension fund at life insurance companies remained unchanged; only the form of the plan was changed. The basic policy is to build up "off-the-book profit" by maintaining stable operation over a long period of time, thereby ensuring reasonable earned revenue.

Avoiding risks by carrying out diversified investment and long-term stability (in operating the pension fund) is another part of the basic policy. As the operating revenue goals, the first special contract is based on the greatest common divisor of multiple funds, while the second special contract is based on the operating policy of each fund. In either case, the actual operating results are directly reflected, helping achieve accurate prediction of risks and returns with a resultant improved operating revenue rate.

Life insurance companies are facing a new operating age. The Japanese life insurance companies and industry are world leading investors. They ought to fully utilize their accumulated financial knowhow to successfully operate the pension funds of the first and second special contracts. Thus, a financial scuffle among life insurance companies, trust banks and investment consultant companies is expected to be seen in the near future.

D. Problems Involved in Operating Pension Funds

Until very recently, the designation of "asset" operation was common in the insurance and pension industries. However, it is becoming more common to call them "fund" operations these days. This is because the pension system is implemented in the form of the flow of a series of money <Pension premium • Pension installment − Pension fund = Fund operation − Pension benefits>. Therefore, the pension system should logically be analyzed from the aspect of the manipulation of money, thus it should be identified in terms of fund operation rather than asset operation. In that sense, the pension incorporates fund operation, i.e., a financial function in its structure. When we consider a pension, its function of providing security for retirement days must not be considered separately from its financial function. In other words, both security and financial functions should be considered integral parts of the pension system. The financial management function of the pension system includes outside preservation of a retirement allowance source fund, leveling the retirement allowance expenditure by utilizing pension installment, and high-interest operation of pension funds.

The issue of fund operation in a corporate pension is rapidly increasing in importance. Here is the reason; it is said that if the operating yield is, for example, increased by about 1%, then the pension cost is reduced greatly (e.g. 15% to 19% in a welfare pension fund of the average fund scale in Japan now), and furthermore, a progressive pension with approximately 2% increase will be possible (this, however, is strictly an example). The increase of about 2% will reduce the cost by 30% to 35% (this is also strictly an example). The reduced cost may be interpreted as a reduction of premium rate or installment rate. This means that increasing the operating efficiency will lead to 10-fold premium or installment savings.

The welfare pension fund is a long-term project, and the reserve fund such as pension benefits must be safely and efficiently managed and operated as a source fund for providing benefits (and one-time allowance). For applying the fund to the expenses for pension benefits (and one-time allowances), trust or insurance contracts must be concluded with trust companies, trust banks or life insurance companies. And the number of types of agencies entrusted with pension assets (entrusted with administration and operation of pension assets) have been increased to include investment consultant companies in addition to the conventional trust banks and life insurance companies. As a result, competition among them in service and fund operation has heated up as previously described.

Note: 1) Principles of fund operation —— 1. Pursuit of safety 2. Pursuit of advantages and high profits 3. Pursuit of restoration-oriented operation 4. Pursuit of welfare-oriented operation 5. Pursuit of public characteristics 6. Pursuit of cashability 7. Pursuit of independent, domestic operation

2) To entrust an investment consulting company with fund operation, the fund must have been in existence at least 8 years, and the upper limit is one third of the total assets.

The revision of the Welfare Pension Act was passed in December 1989, when the number of methods was increased for operating pension assets by the welfare pension funds and the fund federation. In March 1990, the Welfare Pension Fund Law and the Welfare Pension Fund Regulations were modified, and the revised law and regulations became effective on April 1, 1990. The most noteworthy feature of the revision was the issue of the independent operation and domestic operation of pension funds.

The independent operation of a welfare pension fund is called "free zone," and requirements for authorization include:

1. At least 8 years have passed since establishment of the fund was approved.
2. Applicable only to the installments received after the day when the independent operation was allowed (the existing reserve fund is excluded) and limited to one third of the total assets (total reserve fund amount).
3. There is a director (a director in charge of operation who also serves as a managing director) for implementing the management and operation duties.
4. Financially sound operation is expected to continue in the future.

It is possible to upgrade from independent operation to domestic operation (operation by a welfare pension fund itself). Domestic operation is referred to also as in house operation, and requirements for the domestic operation include:

1. The fund or federation has been approved for independent operation.
2. The balance of assets, i.e., the total amount of the pension reserve fund is 50,000 million yen or more (the operation is implemented on a basis of 1,000 million yen).
3. There is an established basic policy for management and operational jobs.
4. There is a fund manager, or a contract for investment counsel.
5. The assets for domestic operation are limited to the assets (corresponding to installment) obtained after the day when the domestic operation was approved by the Ministry of Public Welfare, and limited to one third of the total assets.
6. Purchase of certain negotiable securities which are considered safe, conclusion of contracts on cash in trust (specific cash in trust) which specifies the operating method, and operation based on deposits and savings.

The assets and funds for such independent operation or domestic operation are the portion obtained by deducting the expenditures (a part of benefits, etc.) accruing after the day it was approved from the revenue (installment, etc.) accruing after the day it was approved. Such portion is called "new money".

The domestic operation was an innovative proposal for the fund operation of welfare pension funds. And councils, investigation committee and task forces involved with corporate pension and/or welfare pension funds represented in their replies and reports their wish for active promotion of domestic operation. On the other hand, the reports presented by other agencies (e.g. "Survey on corporate pensions in fiscal 1988" in Nikkei Finance Newspaper issued in December 1989 and "Survey and investigation of corporate pensions" by Mitsubishi Research Institute, Inc. issued in January 1986) showed that the people related to funds were not very eager to promote the domestic operation. This is another example of the discrepancy between principle and real intention, which may be peculiar to the Japanese society.

Presently, regarding independent and domestic operations, the agencies entrusted with these operations are expected to promote them with intention of each fund fully reflected.

In the past, those consignee agencies were only required to give detailed reports or frequent disclosures, or at the most, finance welfare activities or welfare facilities. However, in these days of increasingly unpredictable financial situations, sluggish fund operation and lowering operating yield, the demand for operating the welfare pension funds with highest possible profits and interest rates is increasing. To respond to these requests, the category of consignee agencies was expanded, and requests for activating the independent or domestic operation as part of such efforts were presented.

Basically, highly efficient operation with high profits and high interest rates requires that the fund be large enough to recover if operation should fail. Also, the accumulated fund amount which corresponds to the portion of private pension must be increased to exceed the portion of public pension. It is this increase, i.e. the fund portion that is to be operated with a high interest rate. If, however, only high-profit, high-interest operation is pursued, consignee agencies tend to concentrate on increasing immediate income gain at the cost of capital gain to be acquired in the future. This may not necessarily be profitable to funds as a whole nor in the long term. Also, disclosure should not be requested too often because otherwise it would easily lead to focusing efforts on short-term operating tactics, making it difficult to establish successful medium- or long-term operating strategies. The disclosure items are expected to include details on assets possessed, transactions and revenues.

Life insurance companies, which act as operating consignee agencies, combine pension funds with various of their other insurance funds into a large "lump" fund, and they operate this as one giant fund. This is called joint operation (or aggregate operation in some cases) which is intended to take advantage of the giant fund. Recently, however, a new method has appeared in which the pension fund of a welfare fund is independently operated under a separate account. In contrast to this, trust banks use a method in which they operate each pension fund individually (although there are some exceptional cases where some funds called a joint operation group are combined and operated as if they were a joint operation). This method is advantageous in that each fund can immediately check the operating results of its fund. Naturally, if the fund amount is small, it is difficult to successfully apply the method in which a pension fund is independently operated under a separate account. In this aspect, both life insurance companies and trust banks have funds which are large enough, enabling them to implement the individual operation. The results of high-profit, high-interest operation with high efficiency not only improve pension benefits and control the rise in installment amount but also provide a fund for running welfare facilities in preparation for losses from mortality (as opposed to the savings from mortality in a mortality insurance) which is expected to continue in the future. It is also necessary to accumulate pension source funds for women; this change is expected to appear in Japanese corporate pensions in the future (more women are staying in service until retirement age, thus acqauiring corporate pensions rather than quitting companies early. This is why such accumulation of source funds is necessary). Most importantly, however, the profits from efficient operation described above need to be used to ensure and increase something extra to the additional portion.

The operation of most Japanese corporate pensions focuses first on guaranteeing the principal. The second consideration is the investment and/or financing based on systematic or collective ideas supported by the relationship between companies in terms of materials, human resources, financial and technological resources. Two types of investment and financing are becoming popular; one is the diversified type in which companies in different industries are involved, and the other is a balanced type. These types of investment and financing are a little different from the professional type investment and financing seen in the United States (in that type of investment and financing, a fund chooses an operating agency who is expert in a particular industry that seems brisk and promising at a particular time).

Recently in Japan, the operating yield is trending downward because of the financial recession. Life insurance companies have maintained much better results (or we should say they have a smaller drop in results) than trust banks. This is because life insurance companies average the interest rate in each financial year over a long period of time so that the yield is given with a stable interest rate. Therefore, a yield obtained during a period in which the business climate is favorable is used to make up for the yield during an unfavorable period. This results in a leveled yield over a long period of time. Thus they are able to maintain a fairly good figure even in the period of recession such as we see today. In contrast to life insurance companies, trust banks cannot avoid good figures when the business situation is brisk and bad figures when business is sluggish. As a result, they are behind life insurance companies in terms of yield, and are facing the possibility of losing their share as operating agencies. One point should be mentioned: to switch from a trust bank to a life insurance company, the pension fund to which the operation will be consigned must also be transferred. This naturally requires the cashing of all sorts of assets. At this time, "latent loss" turns into "realized loss" which will be announced. If it is kept as latent loss, however, it will be hidden in an account-book, although it is theoretically calculated as "resulting loss". It would be a great shock for it to turn into a "visual loss" or "actual loss" with a specific figure. If it remains a latent loss, then it may be offset by a latent profit in the future.

Another factor is also helping to place life insurance companies in an advantageous position over trust banks in Japan; all life insurance companies are now releasing their "latent profit" or "latent property" accumulated in the past and adding it to their yield. (Trust banks are also doing the same thing, but they cannot compete with life insurance companies because of their smaller accumulations.) This tactic of life insurance companies, however, is now reaching the limit because their latent profit and latent property are rapidly being used up and disappearing.

Here are several considerations for improving the fund operation for the welfare pension fund pension which is basically non-government/private pension but also semi-public/semi-private, quasi-public pension:

1. It is necessary to alleviate the administrative regulations on the operation to achieve profitable operation with high interest rate and efficiency.
2. The financial investment/financing cooperation shall be withdrawn.
3. Full-scale operating consultants should be nurtured to make full use of their functions.
4. Foreign investment activities should be built up along with promotion of a system for including international pensions.
5. The fields for investing and/or financing should be expanded to cover venture businesses, leading-edge technology companies, particularly the high-tech and information industries, and the tertiary industries.
6. Representatives of employees should be encouraged to be more aware of and participate in fund operation.
7. A new relationship between corporate capital and pension funds should be considered. In other words, a new concept or principle of capital (in pursuit of smooth fusion between the two objectives, the pursuit of profits and the pursuit of welfare — something like "welfare capitalism") should be sought for.
8. To achieve good balance; the fund operation should not work to profit its mother corporation but at the same time it should not harm the profit of its mother corporation, either.
9. It is necessary to find an agency to monitor the actual condition and results of operation, since we want free and open operation. There are suggestions to establish an asset management section or asset management committee to ensure full use of such a monitoring function. That type of section or committee would be intended to provide guidelines for fund operation, define the activity responsibility of consignee agencies (or the defending responsibility from the standpoint of the funds who entrust them with their fund operation), and enhance the checking and supervising aspect of the fund operation.
10. Efforts should be made to thoroughly eliminate Japanese-like customs or trends such as "consignment based on personal connections or personal considerations". These frequently arise from "orders from executives" who are frequently superiors or managerial authorities in a company or its fund.
11. Having too many consignee agencies causes much loss from expenses, but on the other hand, the investment and financing risk can be distributed. The opposite is also true when there are too few agencies. Careful attention must be given to the selection of managing companies to whom fund operation is entrusted, the combination of consignee agencies and the allotment of a fund amount.
12. It may become necessary to purchase the bonds of a mother corporation or finance a participant at a low interest rate. In such cases, strict supervision or management

must be provided to avoid any possible risk, and it is especially important to set a limit to such investment or financing.

E. Implementation of Welfare Projects and Welfare Facilities

In addition to its primary objective of assuring a stable retirement life for participants, welfare pension funds are also considered capable of providing welfare facilities to promote the welfare of participants (who are employees of the companies) or ex-participants. The welfare facilities here are not limited to the buildings; they should rather be regarded as welfare projects. The installment of the welfare pension fund pension includes a portion called "welfare facility installment", the full amount of which is borne by users or business owners.

The welfare projects and welfare facilities primarily include:

a. Loans for buying houses
b. Facilities for recreation and promoting and preserving health
c. Facilities such as homes for benefit recipients, life consulting centers, etc. for retirement days
d. Providing and subsidizing pension consultation, pension proliferation and enlightening activities, life planning lectures, various circles and various classes for enhancing education and cultural activities.
e. Working facilities such as farms and orchards.
f. Congratulation and condolence money for ceremonial occasions, gift money in token of sympathy in the case of disasters, financial aid for diseases, injuries, disabilities, etc., scholarship for orphaned children, and loans for general living fund.
g. Promotion of information exchange by issuing pamphlets and printed matters.
h. Congratulatory money and/or memorials for celebrating long life.

In Japan, there is a traditional philosophy which is represented by the theory that "a company is a family". More specifically, a company functions as if it were a family, with the business owner a parent and the employees the children. All those members form a managing community together and help each other; the company is never just an aggregate or group of individuals. Based on this philosophy, welfare projects are developed, and management activities based on such group-ism are enhanced, and they succeed, through efforts to promote welfare projects. This is partly true with the welfare projects in funds.

F. Establishment of Payment Guarantee System

In April 1989, the Welfare Pension Fund Federation started the payment guarantee project to assure participants eligibility for receiving benefits if their fund is disbanded due to unpredictable situations such as bankruptcy of the mother company. Three major factors led to the advent of the payment guarantee project: the first was the relaxed requirements for establishing a welfare pension fund; the second was the introduction of the tax eligible pension (eligible retirement pension) into a fund; and the third, and most influential, factor was the considerable fluctuation of the socio-economic situation during recent years in Japan. The project requires that each fund checks the reserve fund level every fiscal year as a part of the self-reliance efforts of the fund, and that each fund bears subscription money and secures a certain percentage of the additional pension of a participant of a disbanded fund, i.e., 30% of the substitute pension.

Practically speaking, large companies with excellent profits or that are growing seldom go bankrupt, and therefore, the project is aimed primarily toward preparing for the bankruptcy of medium to small companies and for securing a part of the fund pensions. In other words, the project is said to provide financial adjustment or a flow of money from large companies to medium and small companies, from companies with excellent business results to companies with poor business results or from successfully growing companies to regressing companies. In Japan, there is a traditional social custom that the strong helps the weak, the large helps the small, the successful helps the unsuccessful. This social custom helps to smoothly establish and run the payment guarantee project. Incidentally, the project or system can hardly be regarded as so-called reinsurance.

G. Add-Up System

Japan, since olden times, has had a world-famous "lifetime employment system", and employees' moving from one company to another were quite uncommon. In recent years, however, many more employees are changing from one company to another. This trend has led to the demand for a pension add-up system, and the system was greatly improved by the legal revision made in 1988.

Previously, for a person whose fund participation period was less than 10 years and who retired before reaching age 60 or 55 (early retiree), the control of his or her pension source fund was transferred to the Welfare Pension Fund Federation so that he or she could receive benefits as an add-up pension from the federation in the future. This, however, applied only to the substitute portion (basic pension), and the portion of the additional pension of the additional type fund was supplied as a seceder's (job changer or early retiree) one-time allowance. Thanks to the revision, it was decided to supply that portion in the pension manner. More specifically, control of the source fund which covers the portion of the additional pension is also transferred to the federation to supply the pension. Thus the federation adds up and supplies a liberal pension even to employees that repeatedly joined and seceded from several different funds. Behind this system lies the idea that receiving a pension rather than a one-time allowance ensures better welfare for employees when economic security in retirement is considered.

H. Problem with Taxation of on Corporate Pensions that are Non-Government, Semi-Public/Semi-Private and Quasi-Public

The concept is theoretically accepted of dividing the function of the social security system into medical security and income security. It is also publicly approved that medical security is implemented through disease insurance and health insurance, while income security is implemented mainly through the pension system called security for retirement days. Since the pension system belongs to income security, the pension benefits received under the system are regarded as a kind of income. This naturally means that tax is imposed on the pension because "where there is income, there is always taxation" in modern nations.

Regarding the taxation on the pension, it is necessary to select either < tax on contribution but tax exemption on benefits > or < tax exemption on contribution but tax on benefits >. In most cases, there are tax incentives for pensions that serve to secure income after retirement. Accordingly, selecting the tax exemption on contribution but tax on benefits would be advantageous in terms of the total amount of tax imposed. Some people, however, wish to select the other way, tax on contribution but tax exemption on benefits because it makes them feel easier about their retirement days. Under the Japanese tax system, the tax for the aged and their spouses drops after all deductions are made, or the deductions amount to such a large amount that the disposable income may exceed that of an employee in actual service. Despite that, there is a strong demand for even further tax incentive < tax exemption on contribution as well as on benefits >, which may be hard to get accepted. In any case, there is a strong feeling of "we do not want to pay the tax now", which led to the voice for tax exemption on contribution, and the wish for a comfortable life in retirement led to the voice for tax exemption on benefits. We cannot conclude, however, that their wish for < tax exemption both on contribution and on benefits > is greedy or selfish when we consider the social environment that is unlikely to promise a comfortable life for the aged. The expenses of housing and food that are so basic to living are very high, and the rapidly disappearing Japanese traditional relationship in which parents and children support each other. All those indicate increasing bitterness of life for the aged.

When we discuss the issue of taxation on the corporate pension, the most important point is taxation of the contribution and installment paid by a business owner. On the

K-19 Outline of Proposed Revesion of Taxation on Public Pension Benefits (Income tax)

	Current	Proposed revision (After Jan. 1988)
Income category	Salary income	Sundry income
Deductions	○ Special deduction for old-age pension ¥780,000 (65 years or more) ○ Salary income deduction [Min. ¥570,000] up to ¥1,650,000 40% up to ¥3,300,000 30% up to ¥6,000,000 20%	○ Deduction for public pension, etc. ① + ② [Min ¥1,200,000 (¥600,000 for people under 65)] ① Fixed-amount deduction ¥800,000 (¥400,000 for people under 65) ② Fixed-rate deduction (After deduction of ①) up to ¥3,600,000 25% up to ¥7,200,000 15% over ¥7,200,000 5%
	○ Deduction for the aged ¥250,000 (65 years or more) ○ Deduction for spouse ¥330,000 ○ Basic deduction ¥330,000	○ Deduction for the aged ¥500,000 (65 years or more) ○ Deduction for spouse ¥330,000 ○ Special deduction for spouse ¥165,000 ○ Basic deduction ¥330,000

subject of corporate pensions, take eligible retirement pensions (tax eligible pension) in this case, as an example. Theoretically, if a business owner pays an installment for an employee, at that point it should automatically become the employee's salary income, and therefore, income tax would be imposed on it. However, in the case of the eligible retirement pension, at the stage of paying the installment, each employee's benefit amount is not yet determined, therefore, the tax payment will be deferred until the employee begins receiving benefits, rather than having the tax imposed immediately on the income of the employee. In Japan, as the delay interest or overdue interest for such deferred taxation, a corporate tax or special corporate tax which corresponds to 1.0% of the retirement pension reserve fund is imposed on trust banks or life insurance companies who are the consignees of pension funds. Technically speaking, those consignee agencies merely assume the legal obligation to pay the tax in place of the pension funds themselves, on whom the tax should immediately be imposed. Accordingly, the taxes are actually paid from the pension funds. In addition, the special corporate resident tax of 0.173% annually is imposed on the reserve fund.

Since the welfare pension fund system is designed to complement and partially substitute for the government pension, public pension and social security pension provided by the government, it is given better taxation incentives than that given to the eligible retirement pension. More specifically, there is tax exemption for the retirement pension reserve fund that the welfare pension funds and the fund federation save at the trust banks or life insurance companies, up to the amount of the reserve fund that is equal to the standard amount of the pension of the Government Officials Mutual Benefit Association. When the amount exceeds that standard, only the excess is subject to the special corporate tax that is applied to the eligible retirement pension. This is based on the idea that the social security pension should be up to the standard of the pension of the Government Officials Mutual Benefit Association.

Here are the specific, actual process details of the welfare pension fund based on the view discussed above. In a welfare pension fund contract, the special corporate tax is imposed on a reserve fund (taxable reserve fund) for retirement pension, etc. only if the regular installment amount of the fund exceeds the standard pension installment amount (corresponding to 2.7 times the exemptible premium rate) of the Government Officials Mutual Benefit Association. And the special corporate tax applies only to the portion that exceeds the standard. In other words, the level of the pension of the Government Officials Mutual Benefit Association is regarded as nearly equal to the welfare pension (the major part of the welfare pension) plus 2.7 times the substitute portion, and the special corporate tax is imposed on the portion that exceeds that level. This means that the standard installment amount of the pension of the Government Officials Mutual Benefit Association is 2.7 times the amount obtained by multiplying the standard monthly salary amount of the welfare pension fund by the exemptible premium rate. It is clear, therefore, that the reserve fund taxation is based on the idea of how much reserve fund is required to provide pension benefits that are to be taxed. The benefits are taxed from the reserve fund.

The special corporate tax is imposed at a rate of 1% on the reserve fund for retirement pension in the welfare pension fund. Just as with the eligible retirement pension, the installment paid by a business owner is regarded as a part of the salary it pays to its employees. Accordingly, the payment of the income tax and resident's tax on that part of the salary is deferred until payment of the pension benefits begins. Interest for the deferred taxation is collected. The special corporate tax equivalent to 1% of the reserve fund for retirement pension applies as the interest on the deferred taxation. Thus the special corporate tax is charged on the reserve, in contrast to taxation on the contribution or benefits. Although the discussion so far is theoretically true, the reserve fund of a corporate pension is originally intended for income security in retirement. Also, withdrawal from the corporate pension is limited up to a certain time. Because of this special nature, measures that are different from those for other types of savings should be applied. Even if it is impossible to discontinue the special corporate tax, every effort must be made to prevent the current tax level from being increased.

K-20 Comparison of Tax Amount Paid per Capita
(as of the end of fiscal 1989)

	Eligible pension system	Welfare pension fund system
Number of participants	9,040,000	9,000,000
No. of participants per system	109	6,647
Reserve fund amount per capita	¥1,310,000	¥2,500,000
Tax amount paid per capita	¥13,355	¥96

K-21 Payment of Special Corporate Tax

	① Number of taxable welfare pension funds	② Tax amount	
		Welfare pension fund	Eligible retirement pension
1982	11 funds	¥40 million	¥37,399 million
1983	12 funds	¥73 million	¥44,901 million
1984	16 funds	¥119 million	¥59,219 million
1985	15 funds	¥174 million	¥67,937 million
1986	11 funds	¥186 million	¥81,911 million
1987	12 funds	¥283 million	¥88,998 million
1988	20 funds	¥512 million	¥101,515 million
1989	24 funds	¥764 million	¥54,061 million

Note : The tax amount of the eligible retirement pension in 1989 is the amount as of the end of May 1989.

VI. Assignments of Corporate Pension for the Future

As previously mentioned, the corporate pension is not entirely a non-government/public pension, but it is a semi-public, semi-private, quasi-public pension. What direction should the corporate pension take? Here are some suggestions for improvement:

K–22 Taxation Balance between Pension (Sundry Income) and One-Time Allowance

	Pension	One-time allowance
Condition	Corporate pension ¥210,000 monthly Public pension ¥180,000 monthly	Retirement money ¥19,600,000 Public pension ¥180,000 monthly
Tax amount (Income tax and inhabitant tax)	¥4 million	¥ 1.44 million
Ratio of tax amount to total income amount (10 years)	8.5%	3.5%

Notes: 1) Both corporate pension and public pension start supplying benefits to participants when they reach the age of 60. The benefit will be paid for 10 years, and the tax amount will be the sum paid over the 10 years.
2) Employee eligible for retirement money ······ White-collar college graduates with 32 years of service (based on the survey by the Japan Federation of Employers' Association)
< Equivalent to the amount of corporate pension benefits paid for 10 years. >
3) Public pension ······ Representative pension of the Ministry of Public Welfare, which is the primary pension in 1987, old-age basic pension and old-age welfare pension (with wife but no other dependent)
4) Income deductions include basic deduction, spouse deduction, old-age deduction, spouse special deduction and deduction for public pension, etc.

1. Switch from retirement one-time allowance to corporate pension: There are still many employees who retire from companies, electing the retirement one-time allowance rather than making use of their corporate pensions. One of the reasons is that they apply the retirement money to pay off the remaining loans on their mortgaged homes. More importantly, it is because the tax imposed on pension benefits is heavier than that imposed on the retirement one-time allowance. This tax imbalance urgently needs correcting.
2. Increasing the "something extra" portion: The employees' and workers' expectations in pension was reduced due to the revision for controlling the benefit level by decreasing the multiplying rate of the welfare pension. To compensate for it, the "something extra" portion of the corporate pension should be increased.
3. Flexible benefit plan: The benefit plan needs to be made more flexible through the use of computers. The pension should also be diversified. For instance, free combinations of one-time allowance and pension.
4. Activation of fund operation.
5. Measures for enhancing labor management and for improving productivity.
6. Activation by increasing the types of consignee agencies and the competition among them.
7. Incorporating eligible retirement pension in welfare pension fund.
8. Promotion of switching from company pension to welfare pension fund.

9. Expansion and enhancement of welfare projects and welfare facilities: The pension may be regarded as ''future welfare'' while a welfare project may be referred to as ''present welfare''. The pension makes the aged who will soon retire very soon happy, while the welfare project makes the young and middle-aged happy. Since it is the young and the middle-aged generations that are forced to support the pension, it is essential to develop energetic welfare projects for them. And the variety of such welfare projects needs to be gradually increased. At the same time, they must contribute to improving the productivity of both companies and their employees. Typical examples of these projects include

K–23 Present State of Welfare Pension Fund

Present State of Welfare Pension Fund as of October 1, 1990

1. Number of funds	1,456
	(The highest fund No. is 1498)
2. Number of participants	9,033,924
	(As of the end of March 1990)
3. Number of offices with funds	119,755
	(As of the end of March 1990)
4. Number of recipients	1,334,844
	(The recipients of the federation are not included. As of the end of March 1990)
5. Average pension amount	¥301,761
	(The figures of the federation are not included. As of the end of March 1990)
6. New funds established this month	27
	(The total in fiscal 1990 is 99.)
7. Mergers this month	0
	(No funds has been merged in fiscal 1990.)
8. Disbanded funds this month	1
	(The total in fiscal 1990 is 1.)
9. Assets	¥22,487,800 million
	(As of the end of March 1990)
	¥18,316,500 million
	(Financial results of fiscal 1988; Source: NEWS RELEASE)
10. Number of funds with authorized independent operation	171
	(As of September 29, 1990)
11. Small-scale fund	11

≪ Form of Establishments ≫	
Single	472
Combined	534
Comprehensive	450
Total	1,456

≪ Type of Benefit ≫	
Substitute fund	327
Adding fund	1,116
Mutual aid fund	13
Total	1,456

The data given under the from of establishment is based on the business report or other document of the 4th quarter in fiscal 1989.

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companies and their employees. Typical examples of these projects include information centers, education and training centers and activities for redeveloping ability.

10. Improvement of the pension by having employees bear the contribution.

[Reference Materials]

a. As of January 1990
   Premium rate of welfare pension insurance
     Male: 143/1000
     Female: 138/1000
   Exemptible premium rate of welfare pension fund
     Male: 32/1000
     Female: 30/1000
b. Proposed revision of the special corporate tax (Reduced multiplying rate by revised pension: From 10/1000 to 7.5/1000)

Proposal 1: When the public pension benefit is added to the welfare pension fund pension benefit, the special corporate tax applies to a portion of the reserve fund, which exceeds the fund reserve fund required to secure the benefit level equivalent to the disposable income amount of a retiree in the welfare pension insurance.

Proposal 2: When the public pension benefit is added to the welfare pension fund benefit, the special corporate tax applies to a portion of the reserve fund, which exceeds the fund reserve required to maintain the amount equivalent to the average standard remuneration amount of the welfare pension. (The additional pension benefit amount of the fund nearly equals the amount which corresponds to the remuneration proportionate portion of the welfare pension.)

Proposal 3: To change the multiplier 2.7 to 3.0, which is the multiplier for the amount determined by multiplying the standard monthly salary amount of the welfare pension fund by the exemptible premium rate. In other words, the multiplier 2.7 is to be changed to 3.0, which is used as the multiplier of the premium (exemptible premium) and corresponds to the portion where the regular installment amount substitutes for the welfare pension insurance.