Consider public pension system (22)

This newsletter explains the pension reform plans outlined in the draft for the comprehensive reform of social security and tax systems, decided by the headquarters of the government and ruling parties for social security reform on January 6, 2012. The draft was compiled based on the final draft issued on June 2011, but there was no significant progress on the pension reforms.

1. Establish a new public pension system

The government aims to establish a new public pension system, comprised of earnings-related pension and minimum guaranteed pension, in order to cover everyone residing in Japan.

(1) Earnings-related pension (social insurance system)

- Premium rate: around 15%
- Benefit: cash balance plan in which the accumulated amounts of premiums paid by individuals as well as notional interests are credited to individual account. (The accumulated amounts are converted to an annuity, based on life expectancy and interest rates.)

(2) Minimum guaranteed pension (tax financing)

- Guarantee payments of 70,000 yen a month in full (at present value)
- Benefits are reduced as earnings-related pension benefits become greater, and are cut off when the earnings-related pension benefits exceed at a certain level.

【The government continues discussions to reach a national consensus on a new public pension system and plans to submit a bill to the ordinary session of the Diet in fiscal 2013.】

2. Improve the current public pension system

It will take significant time (probably around 40 years) to establish a new public pension system and complete the transfer to the new system after the establishment. Hence, the government plans to improve the current public pension system this time in line with the designated goal of the comprehensive reform.

(1) The government's share of contributions to the basic pension remains unchanged at 1/2

After the consumption tax is raised, the government's share remains at 1/2 permanently. For fiscal 2012, basic pension will be financed by the bonds issued solely for the purpose of pension payments. For fiscal 2013 onwards, the government will continue discussions to secure the financing source of basic pension.

【The government plans to submit a bill to the ordinary session of the Diet in fiscal 2012.】

(2) Strengthen the role of minimum guarantee of social security system and revise pension benefits for high income earners.

(i) Relax eligibility requirements to receive pension benefits

The number of qualifying years, currently set at 25, is shortened to 10.

(ii) Provide supplemental benefits to basic pension benefits for low income earners and for disabled persons.

The focus is placed on protecting low income earners, and a certain amount of supplemental benefits are provided to basic pension benefits for them. In setting up a minimum standard of social security system, the government must create a structure that does not disincentivize people to pay pension premiums.

(iii) Reduce basic pension benefits for high income earners

Introduce a system where basic pension for high income earners are reduced by the amount equivalent to the government's share of contributions to the basic pension.

【The government plans to implement this from the year in which the consumption tax rate is raised, and submit a bill to the ordinary session of the Diet in fiscal 2012.】

(3) Eliminate overpayments created when a special rule for macro-economic indexation is applied.

The benefits for current pensioners are 2.5% higher than what they should have been, and the overpayments are eliminated for the period of three years starting from fiscal 2012.

【The government plans to implement this from October 2012, and submit a bill to the ordinary session of the Diet in fiscal 2012.】

(4) Exemption from the payment of employees' pension insurance premiums during the child-care leave and maternity leave.

【The government aims an early implementation and plans to submit a bill to the ordinary session of the Diet in fiscal 2012.】

(5) Expand the coverage of employees' health insurance and employees' pension insurance systems to part-time employees

Currently, employees who work more than 30 hours per week (three quarters of regular working hours) are covered by the employees' health insurance and employees' pension insurance systems, and this coverage is expanded to part time employees.

【The government discusses the scope of coverage and the timing of implementation, and submit a bill to the ordinary session of the Diet in fiscal 2012.】

(6) Unify employees' pension.

Pension premiums and benefits of the mutual aid association of public servants and private school personnel, currently set separately from the employees' pension insurance system, are unified into those of employees' pension insurance system. The government discusses a treatment after the abolition of the occupational pension.

【The government plans to submit a bill to the ordinary session of the Diet in fiscal 2012, based on the bill submitted in fiscal 2007.】

(7) Others

(i) Revise pension system for category III insured persons

The government continues a discussion to resolve the issue of inequality arose from the category III insured persons who are not required to pay pension premium.

(ii) Revise old age pension for active employees

The government carries out an analysis of how the old age pension for active employees in their early 60's may take away the will to work and continues discussions on a structure of the old age pension for active workers, including an amendment of the structure to make it identical to the structure for active workers in their late 60's.

(iii) Revise macro-economic slide

The government plans to revise the automatic benefits adjustment method (known as macro-economic slide), which currently does not work under deflation, in order to achieve intergenerational equality and stability of pension financing.

(iv) Revise the upper limit of standard monthly remuneration

The upper limit of standard monthly remuneration, a basis for calculating employees' pension insurance premium, is currently set at 620,000 yen. The government plans to revise this upper limit, referring to employees' health insurance system and a trend of average standard monthly remuneration.

(v) Plans to raise pensionable age

Currently, the pensionable age is on the rise to age 65. The government discusses a rise in pensionable age over the mid-long term period, paying close attention to employment situation of the elderly.

3. Summary

The drastic pension reform plans required to sustain the public pension system such as revision of macro-economic slide and a rise in the pensionable age etc are postponed. The only reform plan remained effective is to raise the consumption tax rate (raised to 8% by fiscal 2014 and 10% by October 2015). Raising the consumption tax rate is strongly desired in order to sustain the rapidly expanding social security system.

Written by Hideki Kuroda (President of JP Actuary Consulting Co., Ltd., F.I.A.J.）