

The Future of Public Employee Retirement Systems

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Chapter 11

Unifying Pension Schemes in Japan: Toward a Single Scheme for Both Civil Servants and Private Employees

Junichi Sakamoto

Countries may be classified into two groups according to whether civil servants are covered by the same social security pension scheme as the one covering private employees, or whether special schemes apply to government workers, in which case they are generally not covered by the social security pension scheme that applies to private employees. The United Kingdom and Sweden represent the former case, where all employees are included in a single social security pension. There, civil servants are also provided with occupational plans. In the latter group, we have Germany (Maurer, Mitchell, and Rogalla 2009) and France; here civil servants are not covered by the social security pension schemes as are private employees. US federal government employees are in a transitional phase, where initially they had their own plan but new entrants after 1983 are covered by the national Social Security system; for this new group, the civil service pension represents their occupational pension on the national Social Security base.

Until the middle of the 1980s, Japan used to belong to the latter group. There were special schemes for national government and local government employees, and they were not in the national system covering private employees called the Employees' Pension Insurance (EPI) system. Benefit design, benefit levels, and contribution rates were totally different from each other. This structure began to change in 1984 when the government published a Cabinet Decision to unify all the occupation-specific compulsory programs and to finish the unification by 1995. While this plan was not realized by 1995, some of the schemes were merged with the EPI scheme rendering the coverage structure somewhat simpler. Benefit design and benefit levels also converged to a considerable extent.

Nevertheless, at present there still remain three occupation-specific schemes for employees other than the EPI scheme (see Figure 11-1).¹ Contribution levels still differ from one another, though benefit provisions are considerably equalized.² In 2007, the government once again submitted a bill to unify the remaining schemes by extending coverage of the EPI

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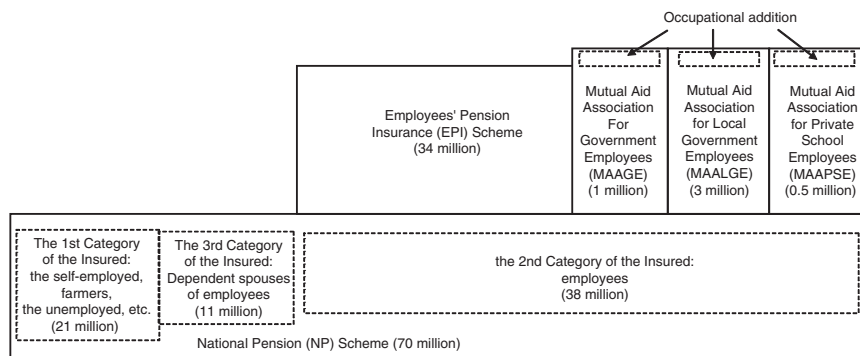


Figure 11-1 Japan's current social security pension schemes. *Note:* The figures in parentheses are the number of the insured by each scheme as of the end of March 2007. *Source:* Summary of the social security pension schemes in Japan by the Actuarial Subcommittee of the Social Security Council published on March 19, 2008 (Government of Japan 2008).

scheme to all workers including national and local government employees. At present, the ultimate shape of the fully merged system can only be outlined, as we shall show in the following text.

In what follows, we first describe how the different Japanese social security pension schemes cover the nation.³ We then analyze reasons why the move to unify social security pension schemes began in 1984, with particular reference to the Mutual Aid Association (MAA) for Japan Railway Company Employees. Next we highlight aspects of the bill submitted to the Diet in 2007, along with the forces compelling the government to submit the bill and how issues of merger are addressed. We mention the complementary retirement benefit provisions for national and local government employees after the unification. Finally we summarize the process of unification and draw some lessons from the process, as well as offer thoughts about the future path of unification.

Evolution of the Japanese government employee pension scheme

After the Meiji restoration in 1868, the government that took over the Tokugawa Shogunate regime tried to construct an industrial country. It sought to consolidate the government by establishing a personnel system that would recruit competent persons for various administrative organs and by organizing the armed forces. It was in this context that the superannuation

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systems for civil servants and members of the armed forces were introduced. The government introduced a superannuation system for the Navy in 1875 and then for the Army in 1876. It also introduced a superannuation system for civil servants in 1884. It should be noted here that government employees at that time were classified into two groups: civil servants and public employees.⁴ The superannuation system covered only the civil servants and members of the armed forces, but not for public employees more generally.

These superannuation systems were based on the concept that civil servants were people whose lives were 'bought' by the nation.⁵ In other words, they were required to work for the government for life, reflecting the German concept of lifetime commitment (Kuhlman and Röber 2004). At the same time, however, this was a concept that the general public at that time could easily accept because of the tradition under the Tokugawa Shogunate regime whereby lords required lifetime loyalty of their servants and gave them a lifetime salary in return. In this sense, the superannuation was more like a salary than a retirement plan. It was financed in principle by the general revenue with civil servants contributing 2 percent of their salary as a token of appreciation. The various superannuation systems were unified into a single system in 1923.

By contrast, public employees were covered by mutual aid associations introduced organization by organization. Once a government organization introduced its mutual aid association, its public employees were compulsorily covered and they paid contributions. The first mutual aid association was introduced in 1905 for public employees of the Yawata Iron Manufacturing Public Corporation. It began by providing compensation for workplace injuries but later added medical insurance and pension benefits for old-age, disability, and survivorship. Subsequently, the mutual aid associations for employees of other organizations like the Imperial Railway Agency were introduced.⁶ These mutual aid associations were introduced by the government organizations in charge of day-to-day operations. By contrast, public employees of government planning offices (not in charge of day-to-day operations) were without pensions until 1949.

After World War II, the Japanese civil service system was reformed, and in 1947 the distinction between civil servants and public employees was abolished. Nevertheless the superannuation system for the people deemed to be civil servants in the old system was maintained, though the mutual aid association system was reformed and codified in 1949 as the Government Employees' Mutual Aid Association Act. This was done to extend the coverage to the people deemed to be public employees of the government branches for planning who were not in charge of day-to-day operations. The new mutual aid association system also equalized benefit provisions and qualifying conditions irrespective of which government organization

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or branch one belonged to.⁷ It did not, however, cover the people deemed to be civil servants in the old system.⁸

Extending coverage of the mutual aid association system to those deemed to be civil servants under the old system was spurred in 1949, when the Imperial Railway Agency was separated from the Ministry of Transportation and became a public enterprise called Japan National Railway Company (JNR). New entrants to the JNR were covered by the mutual aid association system for government employees even if they were posted in positions that civil servants used to occupy. Existing employees, who had joined the JNR before it was made a public enterprise and were deemed to be civil servants, were still covered by the old superannuation system. This provoked feelings of inequality among JNR employees and gave rise to a movement to introduce a new mutual aid association for the JNR employees. In 1956, the Public Enterprise Employees' Mutual Aid Association Act was enacted which separated this group from the mutual aid association for government employees. Their benefit provisions were more generous than that of the mutual aid association for government employees.

Two other government organizations were also made into public enterprises around the same time: the Salt and Tobacco Monopoly Enterprise (in 1949), and the Nippon Telegraph and Telecommunications Enterprise (in 1952); their employees then were covered by the Public Enterprise Employees' Mutual Aid Association Act from 1956. It should be noted, however, that contribution rates were set for each enterprise. In what follows, we denote these mutual aid associations of the JNR, the Salt and Tobacco Monopoly Enterprise, and the Nippon Telegraph and Telecommunications Enterprise by the acronyms MAA for JR Employees, the MAA for JT Employees and the MAA for NTT Employees.⁹

Stimulated by the movement in the public enterprises, demand for equal pension treatment of government employees grew until in 1959, mutual aid association coverage was extended to those deemed to be civil servants under the old system. At this point, the traditional superannuation system was abolished and Japan departed from the concept that the civil servants were those whose lives were 'bought' by the government. The government decided to unify the system in the form of mutual aid associations believing that the concept of lifetime employment was no longer acceptable to the nation. Further, mutual aid associations had been satisfactorily managed up to then so it was easy to obtain political support for these entities. It was also judged that the reserve fund to be formed under the mutual aid association system might be more conducive to government employee welfare than when the government directly managed and controlled the money. Last, the Ministry of Finance feared that rising pension costs would have to be paid from the general budget, so establishing a dedicated scheme for these employees seemed sensible at the time.

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Several insurers or financial units developed under the new system. Each of the government departments in charge of day-to-day operations (e.g., the Ministry of Post and Telecommunications, the Forestry Agency, etc.) formed its own financial unit and decided contribution rates independently. The rest of the government employees were in the financial unit administered by the Federation of National Public Service Personnel Mutual Aid Associations (FMAA). Subsequently these financial units were unified under a single unit administered by the FMAA in 1984.

The new mutual aid association system provided for retirement, disability, and survivor benefits.¹⁰ The retirement benefit formula was based on the three-year average of the basic salary prior to retirement, and 40 percent of this amount was provided for 20 years of service. One additional year of service increased the percentage by 1.5 percentage points. So after 40 years the benefit was 70 percent of the three-year average basic salary prior to retirement. The contribution rate of the financial unit administered by the FMAA was set at 8.8 percent for the part financed by contributions, with a government subsidy financing the remaining part. The contribution rate was decided based on the static level contribution method.¹¹ It should be noted that the costs of paying benefits accrued prior to October 1959, called past service costs, were to be borne solely by the government.¹² The contributions shared by the government employees and the government as employer were, therefore, for the benefits corresponding to the service period after October 1959.¹³

Although the government employee pension scheme departed from the superannuation system, the mutual aid association system itself had the nature of an occupational pension. These schemes were not only for securing income after retirement, but also for compensating the loss of opportunity to increase savings caused by the restrictions imposed on government employees.¹⁴ One consequence of this occupational nature was that benefits were indexed in line with the rise in government employees' salaries.¹⁵

Arrangements similar to the past service cost of the mutual aid association for government employees were introduced in the case of the public enterprises. The cost of paying prior service benefits (prior to 1956) is borne by the public enterprises, and contributions paid by the public enterprise employees were for benefits corresponding to service after July 1956.

The evolution of local government employee pensions

Pension schemes for local government employees followed a rather complicated process of evolution. Before the Local Government Employee Act was

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enacted in 1950, these workers also used to be classified into civil servants and public employees. At the prefectural level, civil servants were further subclassified into two groups: one was the group of civil servants deemed to be 'equal' to central government civil servants and it also included teachers of schools established by local governments and policemen. This group was covered by the superannuation system. The other group included locally recruited civil servants, and these were usually covered by schemes similar to but distinct from the superannuation system. Since such schemes were gradually introduced, their dates of inception varied from prefecture to prefecture.

Employees at the prefectural level were initially not covered by any pension scheme, until 1949 when the mutual aid association system for government employees was extended to cover them. At the same time policemen and teachers came to be covered by the mutual aid association system for government employees. This policy was based on the idea that the employees of prefectural governments were deemed to belong to the Ministry of the Interior.

At the municipal level, civil servants were covered by superannuation systems stipulated in local bylaws and their inception dates varied from municipality to municipality. Although some of them were covered by the EPI scheme, municipal public employees were not, in principle, covered by any scheme until 1955 when the Municipal Employees' Mutual Aid Association Act was enacted.

Finally in 1962, following the establishment of the new Government Employees' Mutual Aid Association Act of 1959, the Local Government Employees' Mutual Aid Association Act was enacted. This covered all the prefectural and municipal government employees by the mutual aid association for local government employees; benefits were the same as those of the mutual aid association for government employees. As was true for the mutual aid association for government employees, prior service cost for benefits prior to 1962 had to be borne by local governments.¹⁶

Evolution of the modern Japanese social security pension scheme

Private sector employees had no national pension system until 1940; while some firms provided occupational pensions, the number was very small. During the 1930s, as war loomed, the importance of maritime transportation rapidly increased. Nevertheless, seamen's jobs were strenuous and they had to retire quite young, and few wanted to be seamen. Furthermore, if a vessel carrying soldiers and arms was sunk in an attack, seamen's survivors were not compensated, while those of the members of the armed forces

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were compensated. In the face of seamen's complaints, the government in 1940 introduced Seamen's Insurance to make the occupation more attractive and retain the necessary number of seamen. At this time, the Seamen's Insurance provided not only pension benefits but also medical insurance, and the pensionable age for an old-age benefit was age 50.

While seamen received this special treatment, there was no general pension yet available for private employees in general. In 1922, responding to labor disputes, the government studied Bismark's German social insurance system and introduced a health insurance system. In 1942, the government then introduced the EPI scheme. At first it covered only male blue-collar workers employed by enterprises with 10 or more employees; subsequently, it extended the coverage to male and female employees including white-collar employees (in 1944). Also industrial enterprises were at first limited to those in the manufacturing and mining sectors, but in 1954 the plan was extended to all industries except for the service sector. The lower size limit of covered enterprises was also cut to 5 from 10 (in 1954) and then to one for legal entities in 1985.

After World War II ended in 1945, Japan suffered from economic turmoil: prices skyrocketed and many aspects of government were forced to change drastically. One of these changes included a reform in the civil service system, erasing the distinction between civil servants and public employees. As a natural consequence, the superannuation system and the mutual aid association system were unified into the single new mutual aid association system.

In the private sector, too, reform discussions broke out inasmuch as hyperinflation had seriously eroded benefit levels. In 1954, coverage of the EPI scheme was extended to employees of most enterprises.¹⁷ The benefit formula was also changed from the one comprising of only an earnings-related part to one that includes both a flat-rate portion and an earnings-related portion. Nevertheless, efforts to boost benefit levels were rejected by employers, whereupon three occupational groups decided to withdraw from (or not participate in) extended coverage of the EPI scheme. The first group involved private schools which established their own mutual aid association, ignoring the effort to extend EPI coverage to private educational organizations.¹⁸ The second group included public employees of municipalities, some of whom had been covered by EPI; however they decided to withdraw from it and to establish their own mutual aid association in 1955. Later, in 1962, when the new mutual aid association system for local government employees was established, this one was absorbed by the new system. The third group comprised employees of agricultural cooperatives and fishery cooperatives; they too had been covered by EPI previously. Arguing that their jobs were like those of the local government employees, they claimed independence of the EPI scheme and established

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their own system. Thus, the Mutual Aid Association for Agricultural, Fishery and Forestry Cooperative Employees was established in 1959.¹⁹

In the late 1950s, as the economy recovered, there was much discussion about how to extend the health insurance program to the whole nation, so all could receive medical services. This discussion, spurred by demands from farmers and the self-employed to be included in social security pension schemes, led the government to begin thinking about covering the whole nation with a social security pension. While there was debate over including everyone in the EPI if they were not already in a mutual aid association or EPI, it was believed impossible because of the difficulty of measuring income for the self-employed and farmers.

Eventually a new scheme called the National Pension (NP) scheme was introduced in 1961, which covered self-employed, farmers, non-employed people, and employees of small enterprises with fewer than five employees. Both the benefits and the contributions under this system were flat rate; those with little or no income were exempted from paying contributions. Though initially it covered only the self-employed, farmers, etc, it was nevertheless the largest scheme at that time, including 20 million people in 1965, while the EPI scheme covered 18.7 million people.

Pension jealousy and long-term financial problems

Altogether then, in the 1960s there were 10 separate social security pension schemes including mutual aid associations. In the 1960s, Japan experienced economic growth and the benefit level of the EPI scheme and the NP scheme were greatly improved after 1965. But in the 1970s, problems in this complex structure gradually became conspicuous.

One reason had to do with the great difference of benefit provisions between the EPI scheme and the MAA schemes. Introduction of an automatic indexation provision of the EPI scheme in 1973 caused great public expectation for the EPI scheme and interest in comparing the benefit provisions with those provided by the MAA schemes.²⁰ It eventually led to people's awareness of the fact that there were disparities between the EPI and the MAA schemes. For example, the pensionable age for the EPI system was raised to 60 after the 1954 reform, while it remained age 55 for the MAA schemes. In addition, the EPI benefit was proportionate to the worker's career indexed average salary plus a flat-rate portion, while the MAA benefit was, generally speaking, proportional to final salary. In addition, the MAA benefit was much higher than under the EPI scheme, partly due to the fact that the average length of the covered period was also much longer in the case of the MAA schemes than for the EPI scheme.

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In any case, demands grew to rectify the disparities, and pension jealousy or pension tension peaked in the mid-1970s. One reaction was to raise the MAA pensionable age to 60 with a transitional provision. It also began to be known that the financial prospects of some MAA schemes were gloomy and appeared not to be sustainable due to changes in industrial structure or employment structure. The particular ones mentioned were the NP scheme, the Seamen's Insurance, and the MAA for JR Employees.²¹

These problems were partly the result of urbanization as industrialization advanced, a process that began in Japan long before World War II but exacerbated in the 1960s and 1970s. This demographic shift resulted in a dire actuarial projection for the NP system in 1980 that indicated a decline in active participants in the near future and unsustainable contribution rates. The Seamen's Insurance system actually experienced declines in the numbers of active participants after 1970, reflecting the fact that advances in shipbuilding technology greatly reduced the number of sailors necessary to operate a ship. Further, Japan's maritime transportation industry had lost its international competitiveness because of its high cost, producing considerable redundancies. And restrictions imposed on economic activities outside the 200 sea mile zone further contributed to the pension scheme's downward spiral, requiring higher contribution rates almost every year after 1973.

Similarly the MAA for JR employees also began to experience changes in industrial structure during the 1970s. During this time, motorways came to connect many key Japanese cities, and roads were also improved for trucking; all of this produced redundancies in the JR Company. Their pension system fell into grave financial problems and after receiving help from other schemes in the 1980s, they were finally absorbed into the EPI scheme in 1997.

Pension reform in the 1980s

To cope with pension system financial problems caused by changes in industrial and employment structure, and to respond to the pension jealousy discussion, a massive reform in pensions was carried out in 1985. A first element of the reform involved the extension of NP system coverage to the whole nation; further, the NP scheme was restructured to provide flat-rate basic pensions, while schemes for employees including the EPI scheme and the MAA schemes were rearranged to provide only an earnings-related benefit. In the process, the government devised a 'Basic Pension Sub-account' in the National Pension Special Account, and the financing framework for basic pension benefits was established (see Figure 11-2).²² As a result, the current NP scheme was born in the 1985 reform. This framework

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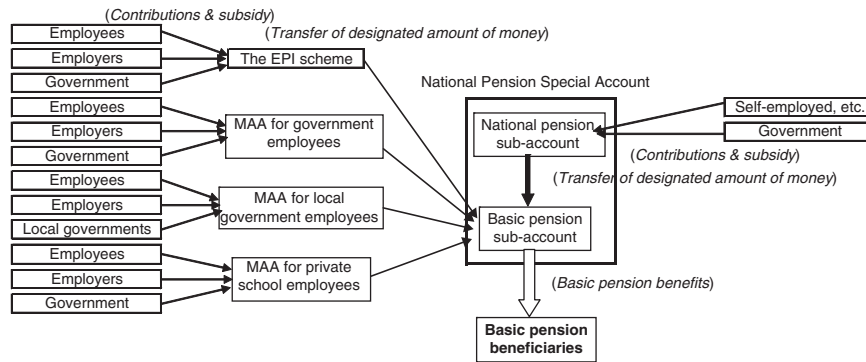


Figure 11-2 Financing basic pension benefits in Japan. *Source:* 2004 Actuarial Report of the EPI scheme and the NP scheme by the Ministry of Health, Labour and Welfare (Government of Japan 2005).

is no longer affected by changes in industrial structure because even if farmers do become employees, they will continue to support basic pension beneficiaries as contributors to the Basic Pension Sub-account of the NP Special Account.

The second major element of the 1985 reform was a change in MAA benefit formulas, where the approach moved away from a final salary formula toward a career average salary formula. It should be noted, however, that an amount equal to 20 percent²³ of the amount calculated by the new formula was added to the basic part of the MAA benefit; this was called the 'occupational addition.' This was added to MAA benefits because national government and local government employees were, from time to time, prohibited from saving on their own due to the code of conduct imposed upon them as public servants. The occupational addition was to compensate for such loss of opportunities. In any event, the occupational addition has been one of the main sources of pension jealousy, and proposed legislation has stipulated that the occupational addition be abolished.

A third element of the 1985 reform required the merger of the Seamen's Insurance and the EPI scheme.²⁴ As we have seen, the Seamen's Insurance scheme had suffered from a decline in active participants and faced worsening conditions. Fortunately, benefit provisions under the Seamen's Insurance plan were the same as those for mineworkers in the EPI scheme, so it was rather easy to merge it with the EPI scheme. A reserve fund corresponding to an amount that would have been accumulated to the same degree as the mine workers would have accumulated in the EPI scheme was transferred to the EPI scheme.

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As a result, the 1985 reform partially solved many problems facing the NP and Seamen's Insurance schemes. The financial problems faced by the MAA for JR Employees were, however, left unsolved though the financial conditions were relieved to a certain extent by the introduction of the basic pension benefits. The problems with the MAA for JR Employees were grave because of the steep decrease of active participants. The 1985 reform also addressed the pension jealousy discussion, so by and large, the disparities were minimized. Nevertheless, differences including the occupational addition and other benefit provisions or contribution rates remain; these are the subject of current reform bills.

In the mid-1980s, with the Cabinet Decision of 1984, the Japanese government declared that the unification of social security pension schemes should be completed by 1995. Although full unification has not yet been completed, the process has been pursued and legislation was submitted to the Diet in 2007 to unify all social security pension schemes for employees. In the meantime, several schemes have been absorbed by the EPI. Several driving forces have been in play. One is pension jealousy, but another is the fact that some schemes actually faced insolvency. After this Cabinet Decision of 1984, all benefit reforms made in the EPI scheme were also reflected in the MAAs: for example, in 1994, the benefit indexation basis was changed from gross salary to disposable income, and this change was reflected in both the EPI and the MAAs. In 2000, the EPI old-age pensionable age was raised to 65 from 60, and so too in the MAAs. In 2004, the EPI introduced a modified indexation, and the MAAs also adopted the same index. This situation thus seems similar to that in Germany after 1992, where civil servant pensions have followed the reforms of the social security pension scheme (Börsch-Supan and Wilke 2003).

The MAA for JR Employees. As we have seen earlier, the MAA for JR Employees faced a steep decrease in active participants in the 1980s due to the shift of transportation on land from railway to lorry. This had a great impact on the financial basis of the MAA scheme and forced it to raise its contribution rates every year, from 10.24 percent in 1980 to 16.99 percent in 1984. Yet further contribution rates increases were in the offing, leading the government to require financial help from the MAA schemes for Government Employees, JT Employees, and NTT Employees beginning in 1984. Nevertheless this financial help did not solve the problems, so in 1990 the government required all employee schemes including the EPI scheme to help out the MAA for JR Employees. As this measure would stabilize the financial problem for the time being, the government set up in 1994²⁵ a group consisting of scholars and representatives from the social security pension schemes to work out measures to merge the MAA for JR Employees with the EPI scheme with the ultimate goal being the unification of the social security pension schemes for employees.

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As of 1990, when the financial transfers began from all the schemes to the MAA for JR Employees, it turned out that the MAA for JT Employees was also in financial difficulties. Here the number of active participants fell from 38,000 in 1980 to 25,000 in 1990, mainly due to the invention of automatic tobacco-rolling machines which led to labor redundancies. As a consequence, the MAA for JT Employees was also provided with financial help by the 1990 framework.

In its 1995 report the working group suggested that the three MAA schemes for JR, JT, and NTT Employees should be merged with the EPI scheme as of 1997, and the remaining schemes for employees should also be gradually unified as they matured in the early years of the twenty-first century. One might ask why the MAA for NTT Employees was asked to merge with the EPI scheme, as this system was not in financial difficulty at that time. Nevertheless, the NTT Company had been privatized in 1985 and so the working group suggested that it should also be merged with the EPI scheme. (Incidentally, the JR Company was privatized in 1987 and the JT Company in 1985.) Following this report, a bill was passed in 1996 to merge the three MAA schemes with the EPI scheme and the merger took place in 1997. Thus the financial problems faced by the MAA for JR Employees were solved,²⁶ lagging behind the NP scheme and the Seamen's Insurance for more than a decade.

The Financial Framework for the Merger. When the working group decided to merge the three MAA schemes for JR, JT, and NTT Employees with the EPI scheme, they proposed a financial framework that would avoid imposing a new burden solely on the EPI scheme and distribute it among the remaining schemes for employees. Without such a framework, all of the financial imbalance would have gone for compensation solely by the EPI scheme. The working group suggested that it should be compensated for by all the remaining schemes for employees. Three principles formed the basis of the proposal:

- (i) Benefits corresponding to the period after the merger would be supported by all active participants of the EPI scheme.
- (ii) The three MAA schemes would transfer the bulk of the reserve fund to the EPI scheme. The amount is so calculated as to secure benefits promised when contributions were paid. In other words, it is roughly the reserve based on the unit credit method without revaluing pensionable remunerations.
- (iii) Benefits corresponding to the period before the merger would be financed by the reserve fund transferred from each of the three MAA schemes, the national subsidy, and contributions paid by the active participants of JR, JT, and NTT Companies.²⁷ If these

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financial resources prove insufficient to finance the benefits, then the difference would be spread to all the schemes for employees.

A conceptual chart for the financial framework mentioned earlier appears in Figure 11-3. In the case of the MAA for JR Employees, the transferred reserve fund, the national subsidy, and the contributions were not enough

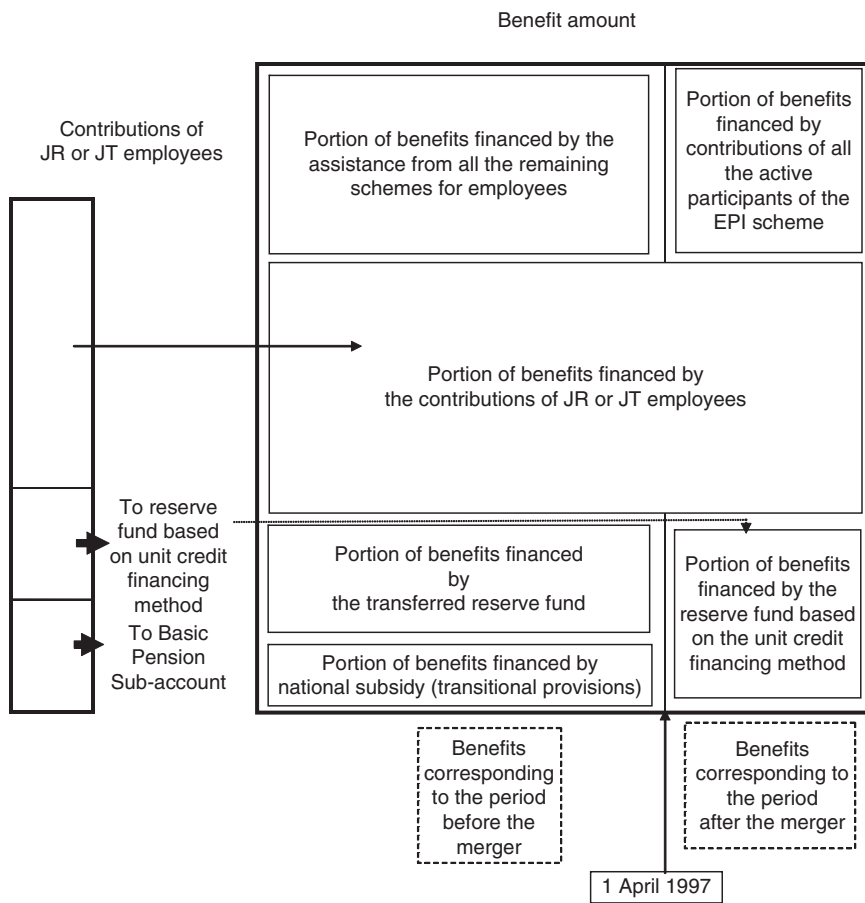


Figure 11-3 Merging the Mutual Aid Associations (MAAs) for Japan Railway Company (JR), Salt and Tobacco Monopoly Enterprise (JT), and Nippon Telegraph and Telecommunications Enterprise (NTT) employees with the Employees' Pension Insurance (EPI) scheme. *Source:* 2004 Actuarial Report of the EPI scheme and the NP scheme by the Ministry of Health, Labour and Welfare (Government of Japan 2005).

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to pay the benefits, so the difference has been supported by the remaining schemes for employees. In the case of the MAA for JT Employees, the situation was the same and the shortfall of the benefit expenditure was covered by the other schemes. In the case of the MAA for NTT Employees, these financial resources were enough to pay the benefits so there have been no further transfers from the remaining schemes for employees.

Substantial reserves were transferred to the EPI scheme from each of the three MAA schemes on the merger. The actual reserve fund that the MAA for JR Employees held at the time of the merger was only JPY 0.3 trillion while the amount to be transferred was JPY 1.2 trillion; the clearing house corporation set up by the government to handle long-term debts when the JR Company was privatized is paying the difference over a 20-year installment period. The shortfall created by the merger of MAA schemes for JR and JT Employees has been compensated for by the remaining schemes for employees. The amount is based on financial projections, with the leveled annual shortfall totalling about JPY 0.13 trillion (in terms of the FY 2005 value); this is indexed to the rate of increase of yearly pensionable remunerations including pensionable bonuses for active participants of the schemes for employees. It is shared by the remaining schemes for employees.²⁸

The Scheme for Agricultural, Fishery, and Forestry Cooperative Employees. In late 1990s, the Agricultural Cooperatives were forced to restructure their businesses due to globalization and deregulation. The number of active participants in the MAA for Agricultural, Fishery, and Forestry Cooperative Employees decreased from 511,000 in FY 1994 to 475,000 in FY 1999. Ultimately the MAA was merged with the EPI scheme in 2002, with a financial framework for the merger similar to that stipulated for the JR, JT, and NTT Employees schemes. The MAA for Agricultural, Fishery and Forestry Cooperative Employees transferred the reserve fund of JPY 1.6 trillion to the EPI scheme. The transferred reserve fund, the national subsidy, and contributions from active employees of the cooperatives were enough to finance the benefits corresponding to the period before the merger, so there was no need for support from the remaining schemes for employees.

In all, then, the 10 schemes that existed in the 1960s have been merged down to five with the NP scheme extending its coverage to the whole nation.

Ongoing merger efforts

In early 2001, the Cabinet published a decision stating that measures should be adopted to enhance the financial basis of employees' schemes

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and urged unification discussions should continue after the MAA for Agricultural, Fishery and Forestry Cooperative Employees was merged with the EPI scheme.²⁹ This Cabinet Decision also urged the MAA for Government Employees and the MAA for Local Government Employees to unify their financial bases which actually occurred in 2004; contribution rates are equalized as of 2009.³⁰ National pension reform occurred in 2004 with the introduction of an automatic balancing mechanism through modified indexation (Sakamoto 2005). The indexation is to be applied to all the schemes.

The political debate over pension mergers continued throughout 2004, in which the largest opposition party, the Democratic Party, campaigned on the pledge of a single social security pension scheme.³¹ Shortly after the landslide victory of the ruling Liberal Democratic Party in the Lower House election in September 2005,³² the government set up a formal meeting of the ministries³³ charged with the schemes to resolve problems of unification. The group's 2005 report referred to differences in contribution rates and benefit provisions, as well as questions about how to manage the pooled MAA reserve funds. They also noted the question of what to do with the occupational addition, how to treat benefits of national or local government employees corresponding to the period before the merger of the superannuation system with the mutual aid associations, etc. Around the same time, the government parties' Pension Reform Council issued a report recommending the equalization of contribution rate, abolishing different benefit provisions, abolishing the occupational addition, etc. Following this, a Cabinet Decision of 2006 was issued and a bill submitted to the Diet in April 2007, with these ideas. The bill went further to stipulate that the EPI scheme should be extended to national and local government employees as well as private school employees, and it also proposed all MAA schemes be restructured as branches of the EPI scheme.

Twenty-first century unification efforts

In early 2007, the government submitted to the Diet a new reform bill to unify the schemes for employees into a single scheme. It had several elements, first and foremost among them the extension of EPI coverage to national and local government employees and private school employees. Benefit provisions for future accruals are to be made uniform, including no further accrual of occupational additions after 2010.³⁴ Past benefits corresponding to the period before October 1959 must be cut by 27 percent to reduce the tax burden by reducing past service cost.³⁵ (There are alleviating provisions that the total benefit cut should not exceed 10 percent and that the annual benefit amount after the reduction should not

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TABLE 11-1 Contribution programs for each scheme for employees

<i>FY</i>	<i>MAA for Government Employees</i>	<i>MAA for Local Government Employees</i>	<i>MAA for Private School Employees</i>	<i>(%) EPI Scheme</i>
Just before the 2004 actuarial valuation	14.38	13.03	10.46	13.58
2004	14.509	13.384	10.46(*)	13.934
2005	14.638	13.738	10.814	14.288
2006	14.767	14.092	11.168	14.642
2007	14.896	14.446	11.522	14.996
2008	15.025	14.800	11.876	15.350
2009		15.154	12.230	15.704
2010		15.508	12.584	16.058
↓		↓	↓	↓
2017				18.3
2018		18.3		
↓				
2027			18.3	

Note: *The initial date of the latest actuarial valuation of the MAA for Private School Employees was April 1, 2005.

Source: Ministry of Health, Labour and Welfare (Government of Japan 2005).

go below JPY 2.5 million.) Contribution rates are also to be made equal to those of the EPI scheme (with a transitional period) and future MAA contribution rates will be raised in step with EPI (namely by 0.354% every year); see Table 11-1.

Under the new structure, the MAAs are to become administrative branches of the EPI scheme, keeping records, collecting contributions, awarding benefits, paying benefits with partial financial interchange among the EPI sub-account and the MAA branches, managing and investing the reserve funds, etc. Active participants in the new scheme will be classified into four groups: active participants whose contributions will be collected by the Pension Sub-account of the Social Insurance Special Account; active participants whose contributions are to be collected by the MAA for Government Employees; active participants whose contributions are to be collected by the MAA for Local Government Employees; and active participants whose contributions are to be collected by the MAA for Private School Employees.

The MAA schemes will manage and invest the portion of their reserve funds; it is unclear whether the segregation will be notional or actual.³⁶ Given the current size of the reserve funds of the MAA schemes, there

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will certainly remain some reserve funds though the bill does not clarify how these remaining reserve funds will be utilized.³⁷ Investment principles for these funds will be determined by the Minister of Health, Labour and Welfare in consultation with other ministries, and every year the funds' investment performance will be published.

Assuming that the bill is adopted, what can be forecast for future government employee benefits? They will have the old-age basic pension benefit and the old-age EPI benefit, as well as new retirement benefits from newly-established occupational pension schemes that have yet to be established. They may also have retirement lump-sum benefits and personal savings including personal annuities. As yet, all the provisions of the to-be-established occupational pension scheme are not known, but it appears that its payment combined with employer-provided lump-sum benefits must not exceed the average retirement benefits of private companies with at least 50 employees. A 2006 survey found that the private benefit amount expressed as a lump-sum was JPY 29.8 million, while that which had been paid to government employees was JPY 29.6 million including the occupational addition of the MAA for Government Employees. If the portion paid by employees themselves was included, the private sector average was JPY 30.4 million while that of government employees was JPY 31.8 million. Overall the new occupational pension scheme will likely pay lower benefits than before.³⁸ It should also be noted that the new occupational pension scheme will be defined benefit; the fact that some government employees access to insider information precludes a defined contribution plan.

In 2007, political turmoil stymied the prospects for pension unification since the government party lost its majority in the Upper House. In addition, the Democratic Party has said it will not agree to the bill's passage³⁹ unless the whole nation is covered, including the self-employed. Adding to the debate was the recent revelation of the existence of 50 million unidentified records of the NP and the EPI schemes kept by the Social Insurance Agency, giving rise to massive public anxiety. Hence the reform agenda will continue to be debated for some time.

Conclusion

Looking back on efforts to unify the Japanese social security pension schemes, several factors enabled the process to proceed as far as it has. First, some schemes encountered financial difficulties due to changes in industrial structure. Second, the 1985 reform made benefit formulas the same which facilitated the later mergers. Third, strong political leadership helped drive the bill to unify the schemes.⁴⁰ Fourth, pension jealousy

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justified the claim that social security pension benefits should be equalized without exceptions.

There remain some outstanding matters to clarify in future years. For instance in some cases, the former insurers remain as administrative branches of the EPI scheme. Also the financial interchange is only partial. Nevertheless, progress has been made to strengthen the financial basis of the social security pension benefits and make the benefits and contributions equitable.

Notes

- ¹ The current Japanese social security pension provisions include two layers. The first layer is the National Pension (NP) scheme which covers the whole nation with a flat-rate basic pension benefit. Active participants in the NP scheme are classified into three categories: (a) the self-employed, farmers, the unemployed, etc; (b) the active employees below age 70; and (c) non-working dependent spouses. The second layer is for employees, and there are four schemes in this second layer: (a) the Employees' Pension Insurance (EPI) scheme for private employees, (b) the Mutual Aid Association (MAA) for government employees, (c) the MAA for local government employees, and (d) the MAA for private school employees. Both the EPI and the MAA schemes provide earnings-related benefits.
- ² Contribution rates as of April 2008 are 14.996 percent for the EPI scheme, 14.896 percent for the MAA for government employees, 14.446 percent for the MAA for local government employees, and 11.876 percent for the MAA for private school employees.
- ³ For an outline of the current framework of Japanese social security pensions see Sakamoto (2007). Additional information is available from Government of Japan (1957, 1984, 1994, 1996, 2001, 2003, 2006a, 2006b, 2006c) and Yoshiwara (1987, 2004).
- ⁴ Government employees were ranked. Their ranks were raised when they got promotions. Civil servants were those whose ranks were above or equal to a certain rank.
- ⁵ A man named Toshinaga Kawaji studied the French police system in Paris and contributed to constructing the modern police system in Japan in 1870s. He concluded that civil servants can be thought of as commodities bought by taxes paid for by the general public.
- ⁶ In 1907, the mutual aid association for employees of the Imperial Railway Agency was introduced.
- ⁷ Some people deemed to be public employees were promoted to be civil servants. However, if both of their periods of service as public employees and as civil servants did not satisfy the qualifying period for the mutual aid association and for the superannuation system, they could receive only lump-sum payments and not pensions from either of them. There was no portability permitted between the superannuation and the mutual aid association system.

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- ⁸ Around this time, in 1950, Robert Myers, former Deputy-Commissioner of the Social Security Administration of the US government, came to Japan at the invitation of the General Headquarters and gave advice to the Japanese government about the reconstruction of the civil service pension schemes.
- ⁹ The Japanese national railway was privatized in 1987 and became the Japan Railway Company. The Salt and Tobacco Monopoly Enterprise was privatized in 1985 and became the Japan Tobacco Company. The Nippon Telegraph and Telecommunications Enterprise was privatized in 1985 and became the Nippon Telegraph and Telecommunication Company. The names of the three public enterprise employees' mutual aid associations are derived from those companies' names after privatization.
- ¹⁰ The mutual aid associations provided health insurance as well.
- ¹¹ The level contribution method is the financing method in which the contribution rates are set to be level throughout the period of equilibrium. By static we mean that we do not take account of the salary increase nor price increase in the future when we calculate the level contribution rate.
- ¹² Government employees from the period prior to October 1959 are very old and form a closed group, so the past service cost is decreasing. It was JPY 0.47 trillion out of the total expenditure of JPY 2.2 trillion in FY 2005.
- ¹³ Ten percent of the contribution amount was subsidized by the government and the rest was shared equally by the employees and the employer (the government). This was changed later; currently the national subsidy is given by a fixed percentage of particular expenditure and the contributions themselves are shared equally by employees and the employer (the government).
- ¹⁴ In Japan, government employees are forbidden to strike and are prohibited to hold stock.
- ¹⁵ In 1973, benefit indexation was introduced in the EPI scheme.
- ¹⁶ Past service costs of the local government employee plan amounted to JPY 1.2 trillion out of the total expenditure of 5.6 trillion in FY 2005.
- ¹⁷ The exception was the service sector in the secondary classification of industry.
- ¹⁸ Some universities decided not to participate in the MAA for Private School Employees but were covered by the EPI scheme, because they judged that their health insurance contributions would be larger if they had joined the MAA for Private School Employees. Most of the MAA schemes provided health insurance benefits for the participants as well.
- ¹⁹ Unlike other MAA schemes, the MAA for Agricultural, Fishery, and Forestry Cooperative Employees did not provide participants with health insurance benefits. Instead, these employees were covered by a health insurance society that was a contracted-out insurer of the Health Insurance scheme provided by the government.
- ²⁰ The 1973 oil crisis caused daily goods prices to soar by 11.7 percent in 1973, 23.2 percent in 1974, and 11.7 percent in 1975. These inflation rates were reflected in the benefit amount according to the automatic indexation provision.
- ²¹ In the 1970s, the company was still the Japan National Railway Company so it would be more accurate to denote it by the MAA for JNR Employees. However we denote it here by the MAA for JR Employees since later in 1987 the

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JNR Company was privatized and became the Japan Railway Company as noted previously.

- ²² In order to finance the cost of paying the basic pension benefits, the Basic Pension Sub-account of the National Pension Special Account collects the designated amount of money from all the schemes, namely the EPI scheme, the MAA for Government Employees, the MAA for Local Government Employees, the MAA for Private School Employees, and the National Pension Sub-account of the National Pension Special Account. The self-employed, farmers, and such pay contributions to the National Pension Sub-account of the National Pension Scheme. The cost of paying the basic pension benefits is shared by these schemes in proportion to the number of active participants age 20–59 plus the number of dependent spouses age 20–59.
- ²³ If the number of covered years was fewer than 20, then it was 10 percent, and if it was less than 1, then there was no occupational addition.
- ²⁴ Strictly speaking, the pension provisions of the Seamen’s Insurance were merged with the EPI scheme, and the rest of the provisions like health insurance and work injury provisions were left in the Seamen’s Insurance.
- ²⁵ The establishment of the 1994 working group was also based on the Cabinet Decision of February 1984.
- ²⁶ It goes without saying that, every time they obtained financial help from other schemes, the MAA schemes for JR and JT Employees sought to reduce benefit costs including abolishing the occupational addition of the newly awarded and paying higher contributions than other active participants even after the merger.
- ²⁷ Strictly speaking, they are the contributions left after the amount to be transferred to the Basic Pension Sub-account and the amount corresponding to the increased accrued liabilities during the year measured in the unit credit cost method are deducted. The contributions left are split into two parts to finance the benefits corresponding to the period before and after the merger in proportion to the benefit amount of each part.
- ²⁸ Setting each scheme’s share is rather complicated. To briefly outline the process, half of the level amount is shared in proportion to the total amount of the yearly pensionable remunerations including pensionable bonuses of each scheme. The remaining half is shared taking account of the cost rate of each scheme. The share is only on the schemes whose cost rates are not more than the cost rate of the EPI scheme. It of course includes the EPI scheme. The share is then decided in proportion both to the total amount of yearly pensionable remunerations including pensionable bonuses and to the difference of the cost rate of the scheme and that of the EPI scheme with some relief for the EPI scheme.
- ²⁹ This was a continuation of the Cabinet Decision of February 1984. In fact, in March 1996, just before the bill to merge the three MAAs for former Public Enterprise (JR, JT, and NTT) Employees was submitted to the Diet, the Cabinet had also announced a decision to continue the effort to unify the framework of social security pension schemes for employees before system maturity in the twenty-first century. Both Cabinet Decisions, in this way, confirmed the direction of the Cabinet Decision of February 1984 and urged future governments to complete the policy implementation.

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- ³⁰ Each of the two MAAs still remains as an independent insurer while the unification of the financial bases is carried out through financial interchange. The basic idea of this financial interchange is that the insurer with the lower cost rate (excluding the expenditure for basic pensions) gives cash to the insurer with the higher cost rate. Since this neglects the investment return, if one of the insurer becomes short of cash to pay benefits (including the expenditure for basic pensions), the other gives cash to the one from its surplus.
- ³¹ During the 2004 Diet deliberations, the Democratic Party, which is the largest opposition party, tried to prevent the bill from passing the Diet by disclosing bribes by high-ranking officials of the Social Insurance Agency and by attacking several ministers who they said had not paid NP contributions for certain periods. The information was apparently provided by those supportive of the Democratic Party within the Social Insurance Agency. In the 2004 Upper House Election, the government parties lost only one seat which was sufficient to arouse anger against Social Insurance Agency staff. Ultimately the government decided to abolish the Social Insurance Agency and split it into two parts, the National Health Insurance Federation in charge of health insurance (mainly for small companies), and the Japan Pension Organization which is slated to take over the EPI and NP schemes. Interestingly, the new staffs will not be government employees. During this restructuring process, in 2007 it was revealed there were as many as 50 million unidentified records from both the EPI and NP schemes stored in the Social Insurance Agency, a revelation that apparently contributed to eventual fall of Prime Minister Shinzo Abe.
- ³² This time the Prime Minister dissolved the Lower House when the bill to privatize Japan Post was rejected in the Upper House.
- ³³ They are the Cabinet Secretariat; the Ministry of Internal Affairs and Communications; the Ministry of Finance; the Ministry of Education, Culture, Sports, Science and Technology; and the Ministry of Health, Labour and Welfare.
- ³⁴ There are other small differences. For example, under the MAA schemes, survivors' benefits can be taken over by the parents of the deceased if they are alive when the children of the deceased reach the age of 18. Under the EPI scheme, it cannot be taken over. This case is to be treated in the same way as the EPI provisions. Another example is the income testing for the old-age beneficiaries actively covered by other schemes. If an old-age EPI beneficiary is actively covered by an MAA scheme, his/her old-age EPI benefit is not subject to income-testing while, if a retirement MAA beneficiary is actively covered by the EPI or another MAA scheme, his/her retirement MAA benefit is subject to income-testing. This case is, roughly speaking, to be treated in the same way as the MAA provisions. This sort of equalization is to be introduced.
- ³⁵ When the new MAA for Government Employees was introduced in October 1959, the contribution rate was 8.8 shared equally between employer and employees, so the government employees' share was 4.4 percent. For the superannuation system, on the other hand, the civil servants had paid 2 percent of their salary as a token of gratitude to the country. This was interpreted as having been short of the full contribution rate by 2.4 percent during the time of the superannuation system. Consequently it was decided to cut the benefits by 2.4/8.8 or roughly 27 percent.

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- ³⁶ The reform bill only states the segregation and leaves the details to regulations that will be published when the bill passes the Diet.
- ³⁷ There are several options as to how to share the reserve fund. One approach would be to follow the path selected when the MAA for JR Employees was merged with the EPI scheme, but this was not adopted in this case since the JR scheme was on the verge of financial collapse while the MAAs for Government Employees, Local Government Employees, and Private School Employees are not.
- ³⁸ Government employees are not to be allowed to register in the DC scheme, probably because the new occupational pension scheme is to be introduced.
- ³⁹ The government parties control over two-thirds of the Lower House, so they can utilize the provision that the bill passes the Diet as long as it gains approval of more than two thirds of the whole seats in the Lower House even after the Upper House denies the bill. This provision was utilized to force passage of a bill providing fuel by the Self Defence Forces in the Indian Ocean to war vessels of allied nations engaged in the Afghanistan war. It is believed that too-frequent utilization of this provision will give the government parties a bad image causing them to lose elections, so they are understandably cautious when implementing the provision.
- ⁴⁰ It is not clear why the then-Prime Minister Junichiro Koizumi ordered the Chief Cabinet Secretary to come up with the bill to unify the social security pension schemes for employees. One apparent motivation might have been that in 2004, the Democratic Party refused to deliberate the bill, insisting that the true reform was the unification of all schemes and the coverage of both employees and the self-employed under a single scheme. Yet the Party's insistence seemed unrealistic relating especially to the treatment of the self-employed. Mr. Koizumi might have thought that he could win the next election by unifying employee schemes and curtailing government employee prestige.

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