

November 16, 2006

Mr. Yasuhisa Shiozaki
Chief Cabinet Secretary

Masahito Tani
NPA President

Re: Results of a fact-finding survey on pension plans for public employees in major countries and corporate pension plans and retirement allowances in the private sector, and the NPA view on basic matters related to a new system for national public employees

In response to your request dated April 28, 2006, the NPA conducted a survey on pension plans for national public employees in foreign countries and a fact-finding survey on corporate pension plans and retirement allowances of private enterprises. The NPA compared the existing occupational portion of the National Public Service Mutual Aid Pension and retirement allowance with survey results and studied the system for national public employees from various viewpoints, including a study on a new system as an alternative to the occupational portion of the National Public Service Mutual Aid Pension.

The results of the surveys and NPA view are described in Exhibit.

Exhibit

I. Results of the Surveys on Retirement Benefits in the Private and Public Sectors in Japan and in Major Countries

1. Results of the Survey on Retirement Benefits of Private Enterprises

(1) Survey Method

From July to September 2007, the NPA conducted a fact-finding survey of 6,232 private enterprises selected by the stratified random sampling method based on corporate scale and industry classification from approximately 37,000 enterprises with not less than 50 employees throughout Japan (general population). The NPA surveyed retirement benefits (corporate pension plan, lump-sum retirement allowance, etc.) of these enterprises (field survey of 1,115 enterprises and correspondence survey of 5,117 enterprises). The NPA restored the survey results to the general population.

Major survey items were types and details of retirement benefit plan applied to full-time employees of administrative and technical job categories of private enterprises at the end of FY 2005 and the amount of retirement benefits paid to full-time employees of administrative and technical job categories who served for not shorter than 20 years and retired in FY 2005.

Benefits paid to retirees of private enterprises are comprised of corporate pension benefits and lump-sum retirement allowance. However, these are virtually recognized as one benefit packages because most of the corporate pension plans were shifted from a lump-sum retirement allowance and retirees can select to receive corporate pension benefits as a lump-sum retirement allowance. For this reason, the NPA refers to overall retirement allowance including corporate pension benefits and a lump-sum retirement allowance as “retirement benefits”.

(2) Outline of Survey Results

In this survey, the NPA received response from 3,850 of 6,232 surveyed enterprises with a survey completion rate of 61.8%. Regarding the amount of retirement benefits, the NPA received response from 23,680 retirees. (The number of retirees after restoring the survey results to the general population was 120,964.)

Outline of the survey results are as follows:

(See “Reference Material 1. Actual State of Corporate Pension Plans and Retirement

Allowance Systems in the Private Sector”.)

① **Outline of the Retirement Benefit Plan**

A. Penetration Rate of the Corporate Pension Plan and Lump-sum Retirement Allowance System

As shown in Appendix 1, 92.0% of enterprises have a retirement benefit plan. Of all enterprises having a retirement benefit plan, 14.5% of enterprises have only a corporate pension plan while 41.5% of enterprises have only a lump-sum retirement allowance system. As much as 44.0% of enterprises have both. Enterprises having a corporate pension plan account for 58.5% of all.

B. Reasons for Establishing the Retirement Benefit Plan

The NPA asked enterprises having a retirement benefit plan about the reason for establishing the plan (Multiple answers). The largest percentage of enterprises selected “life security in old age” (67.6%), followed by “promotion of long-term service” (64.6%), “retaining competent employees” (62.2%) and “smooth retirement management” (34.2%).

C. Designed Ratio of Corporate Pension Benefits and Lump-sum Retirement Allowance

As mentioned above, 44.0% of enterprises have both a corporate pension plan and a lump-sum retirement allowance system. As shown in Appendix 2, the design (prescribed) ratio of corporate pension benefits and lump-sum retirement allowance of these enterprises is 51.4% to 48.6% on average, a ratio of almost 50:50. However, as described later, many retirees actually receive corporate pension benefits as a lump-sum allowance.

D. Outline of the Corporate Pension Plan

As shown in Appendix 3, the largest number of private enterprises with a corporate pension plan (some enterprises have multiple types of corporate pension plans) adopt the approved retirement annuity (60.6%), followed by the employees’ pension fund (31.4%) and the defined-benefit pension plan (14.6%), demonstrating that benefit security-type pension plans are still a mainstream option. Only 11.7% enterprises adopt the (corporate-type) defined-contribution pension plan.

Details of the corporate pension plans (eligibility, start of pension payments, payment period, and percentage of standard pension contributions paid by employers) vary from plan

to plan. The most common qualification criteria were the “length of service and age” (39.2%) and “length of service” (34.9%). The most frequently responded criteria were “not shorter than 20 years of service” and the “age of 60”. The largest number of enterprises (63.0%) responded “from a certain age” as the age for the start of pension payments and the majority of enterprises (91.2%) responded the age of 60.

With regard to the pension payment period, 34.1% of enterprises responded “whole life” while 51.4% of enterprises responded “definite term”. In the case of definite term payments, 10 years was the most frequently given response (73.3%). As much as 86.1% of enterprises pay all contributions while employees of 13.9% of enterprises pay part of the contributions.

As much as 78.1% of enterprises have a system to allow retirees to select a post-retirement lump-sum payment for corporate pension benefits.

E. Outline of the Lump-sum Retirement Allowance System

The largest number of enterprises (45.3%) calculates the lump-sum retirement allowance by multiplying the basic salary at the time of retirement by a certain rate. The largest number of enterprises (50.7%) defines the rate based on “the length of service and the reason for separation”.

As much as 15.1% of enterprises have a voluntary early retirement program in calculating the lump-sum retirement allowance. The condition to apply the program is “age” at the largest number of enterprises (90.2%).

F. Prepayment Plan

Of enterprises having a retirement benefit plan, only 2.9% have a prepayment plan to allow employees to receive benefits together with remunerations or bonuses during their tenure.

G. Outline of Other Supplementary Retirement Benefits

Of enterprises having a retirement benefit plan, 16.3% have supplementary retirement benefits such as provision of travel coupons, commemorative gift, etc. at the time of retirement.

H. Change of the Retirement Benefit Plan

The NPA asked enterprises having a retirement benefit plan whether they had changed their retirement benefit plan after 2001 when the Defined-benefit Pension Plan Law and the

Defined-contribution Pension Law were established. As a result, the NPA found that only 26.9% enterprises had changed the plan while 68.4% had not. Of the enterprises that had changed the plan, 33.6% abolished the approved retirement annuity plan and shifted to a new plan while 26.2% gave up the employees' pension fund and shifted to a new plan.

② Actual Amount of Retirement Benefits

The retirement benefits (regarding the corporate pension plan, benefits for the contributions paid by the employer) paid to full-time employees of administrative and technical job categories (university graduates or high school graduates) who served for not shorter than 20 years and retired in FY 2005 were as follows:

The average amount of corporate pension benefits converted to the present value at the time of retirement and lump-sum retirement allowance (including other supplementary retirement benefits) by reason for separation and length of service are shown in Appendix 4. In the age group with the largest number of retirees, for example, the retirement allowance for an employee who retires at the mandatory retirement age after working for 41 years was 27,068 thousand yen (pension benefits of 15,965 thousand yen (of which 5,335 thousand yen was actually paid as an alternative lump-sum payment) plus a lump-sum retirement allowance of 11,102 thousand yen). An employee who retires involuntarily after working for 32 years received 29,656 thousand yen (pension benefits of 13,251 thousand yen (of which 4,258 thousand yen was actually paid as an alternative lump-sum payment) plus a lump-sum retirement allowance of 16,405 thousand yen).

(Note) Retirement benefits are comprised of corporate pension benefits and a lump-sum allowance. The lump-sum allowance (including part or all of pension payments paid as an alternative lump-sum payment) is defined at the time of retirement but corporate pension benefits are not defined because the age for the start of pension payments and payment period vary among enterprises and individuals. Therefore, comparing only actual annuity is inappropriate. For this reason, the NPA converted the accumulated corporate pension benefits to be paid in the future to the present value at the time of retirement and regarded the total of this amount and the lump-sum allowance (including pension payments paid as an alternative lump-sum payment) as the total retirement benefits.

In converting the pension benefits to the present value at the time of retirement, the NPA applied the same rate for both the public and private sectors and used the assumed return rate (2.20% for FY 2005) specified in an announcement of the Minister of Health, Labour and

Welfare for calculating the minimum funding standard for pensions, as the conversion rate. The amounts converted using the assumed return rates and deferred rates set for each corporate pension plan are shown in Table 20 in Reference Material 1.

As mentioned above, it is necessary to note that the accumulated pension benefits to be paid in the future were converted to the present value at the time of retirement and added to the lump-sum retirement allowance for the purpose of comparison.

2. Results of the Survey on the Mutual Aid Pension (Occupational Portion) and Retirement Allowance of National Public Employees

(1) Outline of the Retirement Benefit Plan

The Mutual Aid Pension for national public employees is composed of the portion equivalent to the employees' pension and the occupational portion which is unique to public employees.

The lump-sum retirement allowance which corresponds to the retirement allowance in the private sector is specified to balance with the private sector, based on fact-finding surveys on retirement allowances in the private sector conducted every 5 or 6 years. The lump-sum retirement allowance paid to public employees has the nature of a bonus for continued service, life security and deferred salary in an indivisible manner, but it is recognized that the largest element of the allowance is a bonus for continued service over a long period of time.

In August 2007, the NPA conducted a survey on payments of the occupational portion of the Mutual Aid Pension (hereinafter referred to as "occupational portion") to compare the retirement benefits for national public employees with the retirement benefits of private enterprise employees. The NPA also used results of a fact-finding survey on the retirement allowance of national public employees conducted by the Ministry of Internal Affairs and Communications in April and May this year.

The occupational portion and retirement allowance paid to national public employees to whom the Salary Schedule for Administrative Service (I) was applied and who retired in 2005, based on these surveys, are described in (2) below.

(See "Reference Material 2. Facts about the Occupational Portion and Retirement Allowance System for Public Employees".)

The government (employer) and employees pay 50% Mutual Aid Pension contributions, including the contributions for the occupational portion, respectively. In order to compare the amount paid by employers, as is done with the retirement allowance, the NPA included only

the portion of which contributions were paid by the employer and excluded the portion paid by employees.

(2) Outline of the Retirement Benefit Amount

① Total Amount of Retirement Benefits

In the case of retirees (university or high school graduates) who served not shorter than 20 years and retired in FY 2005, the average amount of occupational portion converted to the present value at the time of retirement was 2,214 thousand yen. In this calculation, the NPA used the same rate (2.20%) as was used as the conversion rate for calculation of corporate pension benefits in the private sector. (See “Note” in 1.(2) ②.)

The amount paid as the occupational portion is determined in proportion to the standard remuneration, so there is almost no difference among individuals.

The average retirement allowance of all retirees was 19,103 thousand yen while the average retirement allowance of mandatory or encouraged retirees (university or high school graduates) who served not shorter than 20 years was 27,386 thousand yen.

Appendix 5 shows the average of total retirement benefits by reason for separation and length of service, summing up the present value of the occupational portion and retirement allowance, of retirees who served for not shorter than 20 years. In the age group with the largest number of retirees, for example, the retirement benefits of mandatory retirees with 42 years of service is 28,466 thousand yen (present value of the occupational portion of 2,415 thousand yen the plus retirement allowance of 26,051 thousand yen) and the retirement benefits of encouraged retirees with 41 years of service is 29,549 thousand yen (present value of the occupational pension 2,357 thousand yen plus retirement allowance 27,193 thousand yen).

② Composition Ratio

The ratio of the present value of the occupational portion and the retirement allowance in the retirement benefits is 7.5% to 92.5%. The retirement allowance occupies a larger portion than the private sector.

3. Outline of Pension Plans for Public Employees in Major Countries

The NPA surveyed the history, details and benefit levels of national public employee

pension systems in major developed countries (U.S., U.K., Germany and France). Outline of the survey is as follows:

(See “Reference Material 3. Outline of the National Public Employee Pension Plans in the U.S., U.K., Germany and France)

(1) Outline of the Pension Plans

Pension plans are widely used for retirement benefits in both the public and private sectors of the four countries. Germany and France have a completely separate plan for national public employees and do not apply the public pension plan as social security. On the other hand, the U.S. and the U.K. apply the social security pension plan and add a occupational portion for national public employees. In either case, the total pension benefits paid to national public employees are larger than the benefits based only on the social security pension plan.

The public employee pension plans in these countries developed to ensure an old-age security for public employees who served for many years and prevent misconducts of public employees. Later, such systems were introduced to all citizens or employees from the perspective of social security.

① U.S.

Only a defined-benefit pension plan is established for public employees recruited before 1983. Regarding public employees recruited after 1984, an earnings-related social security pension plan (common in the public and private sectors) is applied and a defined-benefit pension plan and a defined-contribution installment saving system have been established as additions.

② U.K.

A fixed-amount basic pension plan (public pension plan) is applied to public employees. Public employees select a defined-benefit pension plan or defined-contribution pension plan as an addition.

③ Germany (Government officials)

Germany does not apply the social security pension plan to government officials. It applies a government pension plan for government officials. In this system, government officials do not pay the contributions and the government pays the pension in fulfillment of the obligation to support retired government officials.

④ France (Government officials)

France does not apply the social security pension plan to government officials. It has a defined-benefit pension plan for government officials. A defined-contribution pension plan has also been established as an addition.

(2) Pension Benefit Level and Contributions Paid by Employees

The defined-benefit pension plans and the government pension plans for public employees of the four countries are life annuity plans. Basically, pension benefits are calculated by multiplying the highest remuneration or the last remuneration by a coefficient corresponding to the length of service.

Specifically, for example, the amount of annual pension payments (converted into yen using the purchasing power parity in 2002) for a Director-General of a Central Office or Ministry who served for 38 years is somewhere between 7.75 million yen (France) and 16.18 million yen (U.K.) and the ratio of the pension amount to the last remuneration is between 57% (U.K.) and 73% (France) (See Appendix 6.). These are much higher than the total annual amount (pension benefits plus retirement allowance converted to pension payments) of 6.22 million yen (with the ratio of 34%) for a Director-General of a Central Office or Ministry in Japan.

With regard to contributions paid by employees, German government officials do not pay contributions and the percentages of contribution paid by government employees in the U.S., U.K. and France are 7%, approximately 11–13% and 7.85%, respectively (including contributions for the basic pension portion, if any). The percentage of contribution paid by Japanese national public employees is 7.3835% (including contributions for the basic pension portion).

(3) Attitude on the Public Employee Pension Plan

In the four countries, pension payments are calculated based on the remuneration at the time of retirement (the highest remuneration) from the perspective of life security. On the other hand, public pension payments in the private sector are calculated based on the average remuneration throughout the period of service and only limited private enterprise employees receive corporate pension benefits as an addition. Therefore, the pension benefit level in the public sector is generally recognized as higher than in the private sector. One of the reasons for the higher benefit level in the public sector is an attitude on the public employee pension

plan that the pension benefits should be determined in deference to the history of respective pension plans and the public employee pension levels have thus been established over a long period of time.

Public employees in the four countries are required to maintain rectitude. Their employment at private enterprises are regulated (the U.S. has a regulation on contact with private enterprises) and dual employment is basically prohibited. Furthermore, strict penalties are applied to public employees such as depriving pension rights if they leak confidential matters after retirement. It is believed that pension levels are determined to secure competent personnel with advanced expertise under strict discipline, guarantee post-retirement income to public employees who have served for many years maintaining neutrality, and allow retired public employees to live without reemployment.

(4) Trends of the Public Employee Pension Plan

Recently, social security pension funds in the four countries are facing financial difficulties due to progressively declining birthrates and the aging populations combined with an increase in life expectancy. These countries revised their social security pension systems to establish sustainable pension systems. The public employee pension plans were also revised as part of the revisions. However, the revisions aimed to reduce financial burden remained within the framework of traditional institutions.

For example, recent revisions of public employee pension systems include raising of the age for the start of pension payments (U.S.), extension of the payment period of the full pension (France), and introduction of a defined-contribution personal pension plan as a supplement (U.K. and Germany). Regarding the benefit levels, Germany reduced the government pension level slightly while the U.K. increased both contributions paid by employees and benefit payments.

The countries did not apply revisions retroactively, set a sufficient transitional period, and paid attention to reduce impacts on public employees to protect pension rights.

II. Comparison of Retirement Benefits between the Public and Private Sectors

1. Attitude on the Comparison

As described in I. 1, corporate pension plans are offered by private enterprises developed from lump-sum retirement allowance systems and many enterprises manage both in an integrated manner. On the other hand, in the public sector, as described in I. 2, the

occupational portion managed integrally with the public pension plan has been recognized as different from the retirement allowance which has the nature of a bonus for continued service.

Both the occupational portion and the retirement allowance in the public sector obviously are for the purpose of post-retirement life security. Therefore, it is appropriate to compare the total amount of retirement benefits in the public and private sectors, namely, compare the sum of pension benefits for which contributions are paid by employers and retirement allowances, to consider the ideal public employee retirement benefit level in comparison with the private sector. It is probably necessary to additionally consider public employee management needs described below in setting the retirement benefit level for public employees.

(1) Strict Discipline

Unlike employees of private enterprises, public employees are subject to legal constraints which extend to off-duty hours and post-retirement periods. Public employees are required to maintain self-discipline including their lifestyles and attitudes. In particular, violation of the prohibition of dispute actions (goading and other actions) (Article 98 of the National Public Service Law), confidentiality (Article 100 of the said law), prohibition of political actions (Article 102 of the said law) and regulation on employment at profit-making enterprises after leaving the public service (Article 103 of the said law) are exposed to criminal liability.

Furthermore, public employees are basically prohibited to have a spare-time occupation and are requested to refrain from stock trading, although stock trading itself is not illegal as a free economic activity of individuals, from the perspective of ensuring fairness. Public employees are thus subject to restrictions on asset formation for old age, so it is necessary to give consideration to the financial conditions of public employees.

Currently, the occupational Mutual Aid Pension benefits, including pension benefits of which the contributions were paid by the employees, are not paid during the term of penalty to retired public employees who were sentenced to imprisonment or a heavier penalty after retirement. The benefits of which contributions were paid by the employer are not paid for a certain period even after completion of the term of penalty. In the U.S., U.K. and Germany, penalties such as deprivation of pension rights are imposed to retired public employees if they leak confidential information. Public employee pension systems in these countries appear to require life-long loyalty to the nation in return for more generous benefit levels than the private sector.

(2) Necessity of Ensuring Long-term Service

It is necessary to further promote exchange between the public and private sectors to activate public administration. Meanwhile, public employees supporting the respective field operations of public administration are required to enhance expertise, maintain strong morale and rectitude over a long period of time, and exercise diligence in duties to ensure the continuity, stability and fairness of public administration. Long-term service of public employees is observed in the four major countries where fluidity of labor is much higher than Japan.

Private enterprises are also utilizing a preferential retirement benefit plan for certain employee groups to ensure their long-term service when enterprises encourage these employee groups to serve over a long period of time.

(3) Public Employee Pension Levels in Major Countries

As described in I. 3, pension plans for public employees in major countries are institutionally and practically more advantageous than the private sector. This is probably because public employees are required to exercise diligence over a long period of time with the principles of professionalism and neutrality. The countries probably offer post-retirement life security to public employees as a state responsibility so that public employees can devote themselves to public services without anxiety.

2. Comparison of Retirement Benefit Levels in the Public and Private Sectors

It is necessary to compare retirement benefits of similar job categories under similar conditions as much as possible in comparison with benefits between the public and private sectors. Therefore, it is appropriate to compare retirement benefits of public employees and private enterprise employees who engage in similar duties, together with comparison of reasons for separation and length of service.

The NPA compared retirement benefits of public employees and employees of all selected private enterprises (with not less than 50 employees) to consider appropriate retirement benefit levels of public employees.

Specifically, the NPA conducted a Laspeyres comparison of the total amount of retirement benefits (for the portion of which contributions are paid by employers) of public employees to whom the Salary Schedule for Administrative Service (I) is applied and private enterprises employees who engage in duties similar to those of the above mentioned public employees (university and high school graduates, respectively) by the reasons for separation (mandatory retirement age in both sectors, encouraged retirement in the public sector and involuntary

retirement in the private sector) and by the length of service.

As shown in Appendix 7, the total amount of retirement benefits paid to public employees was 29,601 thousand yen while the total amount paid to private enterprise employees was 29,802 thousand yen, showing that the amount is higher in the private sector than the public sector by 201 thousand yen (0.68%). The occupational Mutual Aid portion of retirement benefits for public employees stood at 2,214 thousand yen, so the total amount in the private sector will be higher than the public sector by 2,416 thousand yen (8.82%) when the occupational portion is abolished.

III. Basic Attitude on the National Public Employee Pension

Over 90% of private enterprises have retirement benefit plans comprised of a corporate pension plan and a lump-sum retirement allowance for employees as post-retirement life security to supplement the public pension benefits. It is appropriate for the public sector to continue to retain the retirement benefit plan to balance the public and private sectors.

As described in II. 2, the average retirement benefits in the private sector will exceed the public sector average by 2,416 thousand yen (8.82%) when the occupational Mutual Aid pension (the so-called third-floor portion) is abolished in 2010 based on the decision made at the Cabinet meeting held in April this year. Therefore, it is necessary to take measures at least to eliminate the difference in order to balance the two sectors.

It will be appropriate to establish a new pension system, separately from the public pension system, based on public employee management needs in order to eliminate the difference because (1) each public employee has a long-term life plan based on the two benefits of pension and retirement allowance, (2) retirement benefits in the form of corporate pension benefits are common among private enterprises, and (3) life annuity is the basis of the retirement benefit plans in foreign countries.

IV. Perspectives Required to Consider Retirement Benefits for Public Employees

In considering the retirement benefits for public employees, it is necessary to give sufficient consideration to retirement benefits of private enterprises managing employees in a similar way to the public sector and enterprises which compete with the public sector in terms of recruitment, based on human resources and work pattern needs in the public sector, in addition to a comparison with the average retirement benefit level in the private sector. It is also necessary to give sufficient consideration to the necessity of improving the retirement benefit system in view of the particular necessity of strict discipline and long-term service in

public employee management.

In regard to this, it is also necessary to note that there is no revision of the functions of public employee pension systems as post-retirement life security in major countries with an established public employee pension system and that sufficient benefits are guaranteed for public employees.

In designing the pension system, it is probably necessary to give further consideration to the ratio of pension benefits and the lump-sum allowance, which currently occupies the major part of retirement benefits for public employees, the increase of the percentage of retirement benefits to the last remuneration in reference to examples of major countries, and the relationship between pension benefits and the restriction on employment at profit-making enterprises after leaving the public service or the re-employment system of national public employees.