



Japan Update

Proposed Amendments to the Defined Contribution Pension Sub-Limits

October 29, 2021

Outline of the proposal

The newly proposed changes aim to change contribution sub-limits when employees participate in multiple pension arrangements, either employer sponsored (such as Corporate Pension Plan or Fund, or Defined Contribution Pension Plan) or individual (personal DC – iDeCo). While total contribution limit is unchanged, this amendment could significantly affect companies offering both a Defined Contribution plan and a funded DB plan.

The main proposed changes are the following:

- Changing the fix DC contribution limit when employees participate both in a funded DB plan and a DC plan
- Changing maximum contribution to iDeCo when employees participate in other funded arrangements
- Introduce an “equivalent DB contribution” (“EDBC”) to allow for comparison of DB accrual to DC-type contributions

Current Legislation

Under the current legislation, total contribution to Defined Contribution plans is limited to ¥55,000 per month. This contribution is applied against the sum of plan sponsor and participant contributions, with plan sponsor

contribution considered first. In other words, if the plan sponsor’s contribution is ¥55,000 per month or more, participants cannot contribute.

This limit is reduced to ¥27,500 per month if a funded Defined Benefit is offered to employees together with the DC plan and this limit is irrespective of the DB benefit level.

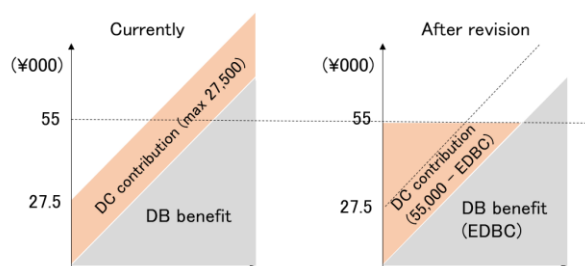
Finally, employees can contribute up to ¥12,000 or ¥20,000 to iDeCo depending on what other plans they participate in, but there are certain strong criteria, some of which will be relaxed in 2022 (for details, please refer to our earlier Japan Update on the subject¹). If corporate DC participants are allowed to contribute to iDeCo, contribution limit to corporate DC must be reduced to ¥35,000 per month, irrespective of iDeCo participation and contribution level.

Changes to DC contribution limits when a funded DB plan is offered

If the proposed changes are enacted, starting from December 2024, corporate DC contribution limits will not reduce by a fixed amount (currently ¥27,500). Instead, contribution limit will be defined as ¥55,000 minus EDBC. From the plan sponsor’s perspective, this means that if the benefit offered through the DB plan is lower, more contribution can be directed toward the DC plan, practically increasing participants’ benefit. On the contrary, if the benefits from

¹ <https://aon.io/2YE5BBq>

the DB plan (and therefore the EDBC) is higher, maximum contribution to DC can reduce compared to the current legislation. With sufficiently high benefit from the funded DB plan, employers may even face a situation where they cannot contribute to their corporate DC plan.



To provide two examples, under the currently proposed changes, a plan sponsor with EDBC of ¥15,000 per month would have an effective DC contribution limit of ¥40,000 per month (up from the current ¥27,500). On the other hand, with an EDBC of ¥55,000, the sponsor would no longer be able to contribute to the DC at all (while under current legislation, it can contribute up to ¥27,500).

There will be a transitional measure in place to ensure that for schemes where this new limit calculation method would lead to the reduction of DC contributions, the current DC contribution limit (¥27,500) will be maintained. However, this transitional measure will stop applying if any plan changes are made to either the DB or the DC plan after December 1, 2024.

iDeCo contribution changes

As mentioned earlier, from October 2022, there will be some changes to iDeCo contribution limits if employees participate in a corporate DC, or corporate DC and funded DB.

For employees who participate in corporate DC and iDeCo, the current iDeCo contribution

limit is ¥20,000 per month and plan sponsor contribution to corporate DC is capped at ¥35,000. After the 2022 changes, iDeCo contribution will be limited to ¥55,000 minus corporate DC contribution or ¥20,000 whichever is lower. There are no further changes under the new proposal.

If the employee participates in a funded DB, corporate DC and iDeCo, under current regulation, iDeCo contribution limit is ¥12,000 per month. From October 2022, this will change to ¥27,500 minus plan sponsor DC contribution or ¥12,000, whichever is lower. From December 2024, this will further change to ¥55,000 reduced by plan sponsor DC contribution and EDBC but not exceeding ¥20,000.

Finally, for employees who participate in a funded DB and iDeCo, the current iDeCo contribution limit is ¥12,000 per month and this is not changing in 2022. However, from December 2024, under this scenario, iDeCo contribution limit will be ¥55,000 minus EDBC or ¥20,000, whichever is lower.

As a result of these proposed changes, especially combined with the iDeCo related other relaxations in 2022, employees will have more flexibility and may be able to contribute to iDeCo more under certain circumstances.

Plans		Current contribution limits
DC and DB	Without iDeCo	DC: ¥27,500
	With iDeCo	DC: ¥15,500 iDeCo: ¥12,000
DC only	Without iDeCo	DC: ¥55,000
	With iDeCo	DC: ¥35,000 iDeCo: ¥20,000

Plans		From October 2022
DC and DB	Without iDeCo	DC: ¥27,500
	With iDeCo	DC: ¥27,500 iDeCo: ¥27,500 minus DC contribution (up to ¥12,000)
DC only	Without iDeCo	DC: ¥55,000
	With iDeCo	DC: ¥55,000 iDeCo: ¥55,000 minus DC contribution (up to ¥20,000)

Plans		From December 2024
DC and DB	Without iDeCo	DC: ¥55,000 minus DB contribution
	With iDeCo	DC: ¥55,000 minus DB contribution iDeCo: ¥55,000 minus DC and DB contribution (up to ¥12,000)
DC only	Without iDeCo	DC: ¥55,000
	With iDeCo	DC: ¥55,000 iDeCo: ¥55,000 minus DC contribution (up to ¥20,000)

Equivalent DB Contribution (EDBC)

Equivalent DB Contribution (EDBC) is being introduced to allow the comparison and integration of funded defined benefit programs with defined contribution type benefits.

The EDBC will be calculated by the funding actuary, using the same assumed rate of return that is used for the most recent

standard contribution calculation. Similar to funding valuations, the EDBC will need to be recalculated at least once every 5 years.

There are multiple approaches to calculate the EDBC, but under all approaches, the result should be a monthly figure that can be compared against DC-type plans to determine contribution sub-limits to those plans.

It's important to note that EDBC is simply a technical figure to allow integration on DB and DC-type benefits; and not a different or additional contribution the plan sponsor needs to pay into DB systems.

Impact of DC sponsors

Employers who offer both funded DB and corporate DC plan to their employees should be paying close attention to these changes.

While the above-mentioned transitional measure will make sure DC contributions can be maintained at least at the current level for existing plans, if any changes are made to these plans after December 2024, the transitional measure will not apply anymore new limits will be enforced. Especially for schemes where a funded DB benefit is considerably high, this may lead to sponsors not being able to contribute to their DC plan anymore. Under this circumstance, they will need to consider their options, including, but not limited to

- Close the DC plan and accrue the entire retirement benefit under the funded DB
- Freeze or dissolve the funded DB plan, making DC the main source of accrual

Therefore, sponsors offering a strong DB benefit and are thinking about making changes to their pension plans should take action in the near future to avoid this.

Sponsors who offer a lower benefit from funded DB, contribution to DC and therefore participant benefit level may be increased.

Finally, employers should review their DC plan rules and consider changes if they set fixed contribution limits as opposed to referencing relevant legislation.

Aon's services

In connection with the above revisions, Aon can provide the following support:

- Review retirement benefit design, including DB or DC systems and their combinations
- Advise on the best approach to take, tailored to each plan sponsors' needs
- Support with closing or dissolving funded DB plans and transition of past accrual to DC

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About Aon

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