

# Current Issues in Retirement Benefits (16th CIRB)

Hotel Sea Princess, Mumbai  
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## Introduction to Collective DC Plans

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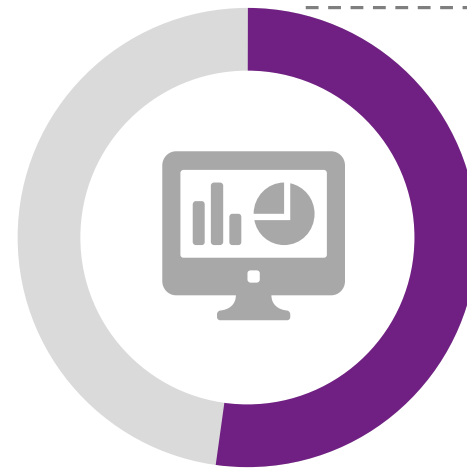
# Japan Corporate Retirement Context

A Need for a New Solution



38%

Companies providing a DB plan only



54%

DC assets invested in cash

Source: WTW BDS 2018, Japan Pension Fund Association (PFA) as at February 2019

## What is a Japanese “Risk-sharing Plan”?

Enter Collective DC in Japan

- Collectively funded pension plan under DB law (pooling investment and actuarial risks)
- Pre-defined benefits with DB formula; can be adjusted up or down depending on the financial status of the plan

$$\text{RS Benefits} = \text{Traditional DB Benefits} \times \text{Adjustment Factor}$$

Any design allowed (final-pay, cash-balance, point plan, etc.)
Function of the plan financial status

- Fixed employer contributions set at plan introduction (including risk contributions to protect the plan against adverse deviation)

## Comparison with DC and DB



Items	DC	Risk-Sharing	DB
<b>Benefits</b>	No guarantee	Targeted benefits	Guaranteed benefits
<b>Benefit adjustment</b>	Yes (indirect)	Yes (direct)	No
<b>Contributions</b>	Known in advance	Known in advance	Unknown
<b>Pooling of assets</b>	No	Yes	Yes
<b>Investment decision</b>	Employee	Employer/employee	Employer
<b>Risk bearer</b>	Employee (individually)	Employees (collectively)	Employer
<b>Risk margin / contributions</b>	No	Yes	Optional
<b>Funding valuations</b>	No	Yes (benefits)	Yes (contributions)
<b>Accounting valuations</b>	No	IFRS/JGAAP: No USGAAP: unclear	Yes

## Pros and Cons of Risk-sharing Plans

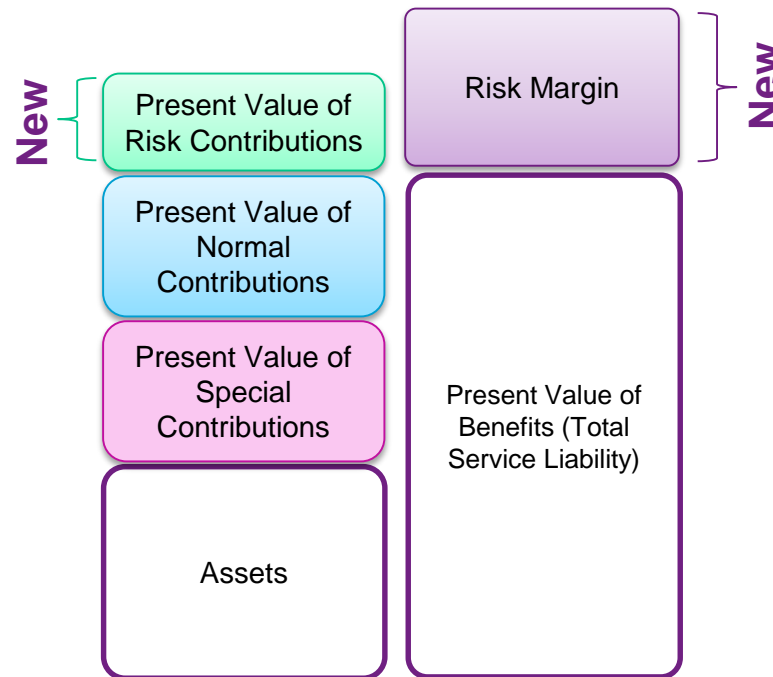


	Employer	Employee
Pros	<ul style="list-style-type: none"><li>• No investment, actuarial risks</li><li>• No accounting liabilities</li><li>• Stable and foreseeable cost</li><li>• No need for top-up plan</li><li>• Easier to transfer past benefit</li></ul>	<ul style="list-style-type: none"><li>• No need to select funds</li><li>• Risk pooling</li><li>• Risk contributions protection</li><li>• Benefits received at termination</li></ul>
Cons	<ul style="list-style-type: none"><li>• Cost of risk contributions</li><li>• Need to manage plan assets</li><li>• Communication challenging</li></ul>	<ul style="list-style-type: none"><li>• Investment, actuarial risks</li><li>• Benefits depend on assumptions</li><li>• Difficult to understand</li></ul>

# Risk Margin and Risk Contributions

## Risk Contributions

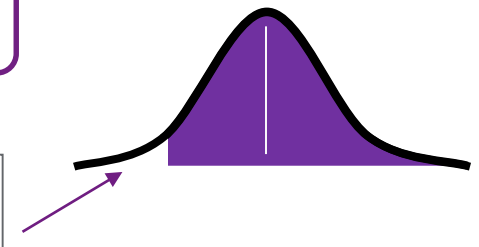
- Funding for risk margin
- Fixed at plan introduction
- Agreed between employer and employees or unions



## Risk Margin

- Protect against adverse experience
- Function of investment and actuarial risks
- Different calculation approaches

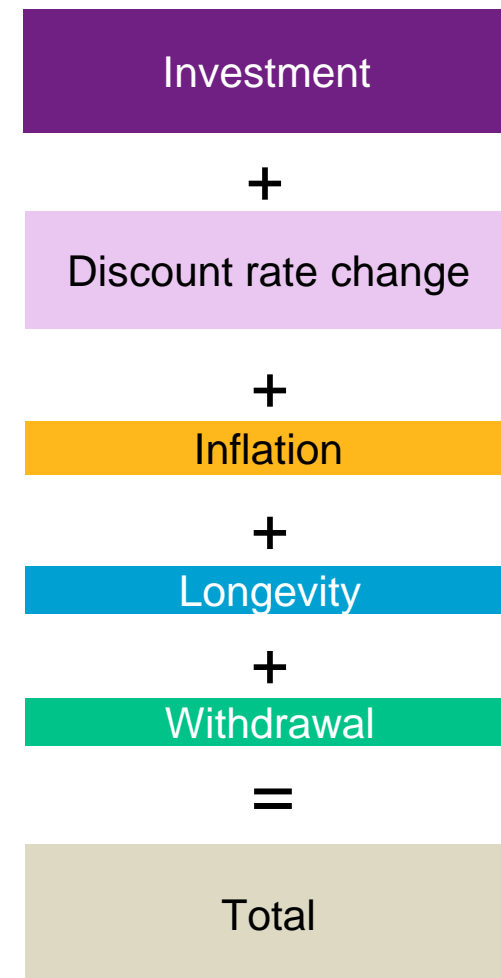
Probability of a benefit reduction



# Risk Margin Assessment

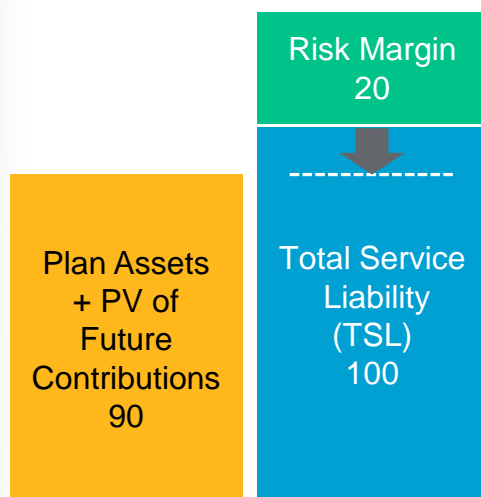


Risk	Risk Margin to cover risk that...
Investment	Less than funding discount rate
Discount rate change	Reduces
Inflation	Higher than expected in future
Longevity	Participants live longer than expected
Withdrawal	Turnover lower and more participants than expected reach full vesting



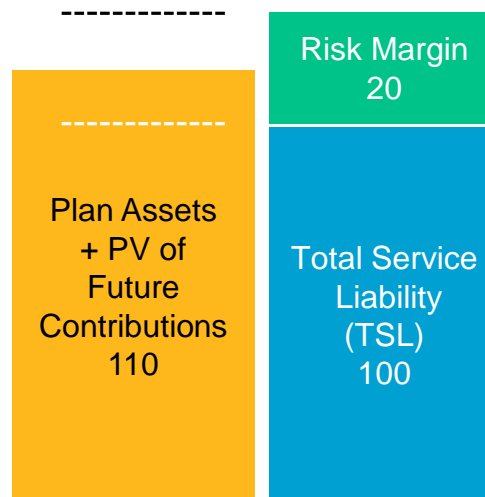
# Benefit Adjustment

Down



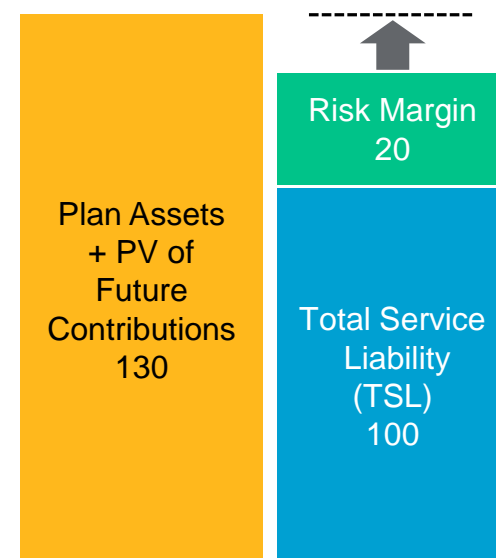
Benefit Adjustment: **90%**

None



Benefit Adjustment: **100%**

Up



Benefit Adjustment: **110%**



## Governance – Pension Committee



1. At least one employee **MUST** participate (pensioners **COULD** participate)
2. External advisors **COULD** participate
3. The investment policy and performance **SHOULD** be reviewed regularly
4. Employee committee members **SHOULD** be provided the investment policy and monitoring reports
5. Meetings **MUST** be conducted at least annually

# Key Issues and Emerging Trends



## Design

Pre-introduction simplification including removal of “risky” features

## Accounting

Still no clarity on US GAAP accounting treatment

## Funding

Risk margin calculation not yet stabilized; need to balance ee protection and er affordability

## Investment

Trend towards de-risking and traditional investments

## Communication

Target benefits not guaranteed but need buy-in from employees

## Governance

Pension committee structure and role of the company to develop

## Collective DC in Other Countries



### Netherlands (since 2006)

Can be fixed-term contract (e.g. 5 years)

Offered today by almost all large Dutch companies

### Canada (target benefit)

In some provinces (e.g. NB, AB, BC)

Contributions can vary within a predefined range

### Germany (since 2018)

Collective individual defined contribution schemes (CIDC)

Individual accounts but collective asset buffers

### UK (under review)

New legislation “as soon as Parliamentary time allows”

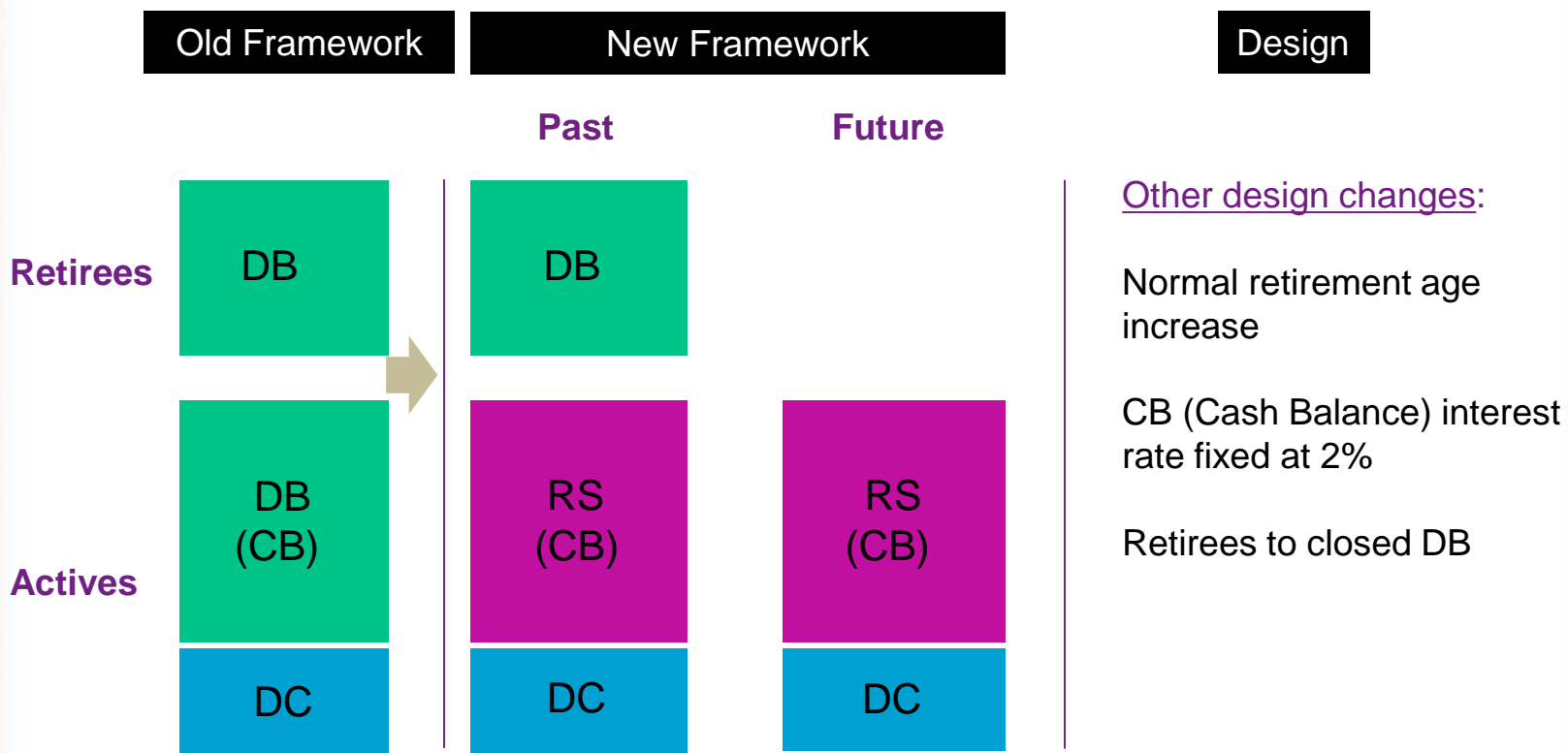
No explicit risk margin/capital (current proposal)

# Case Study

## European Multinational

# Case Study

## New Plan Framework and Design



## Case Study

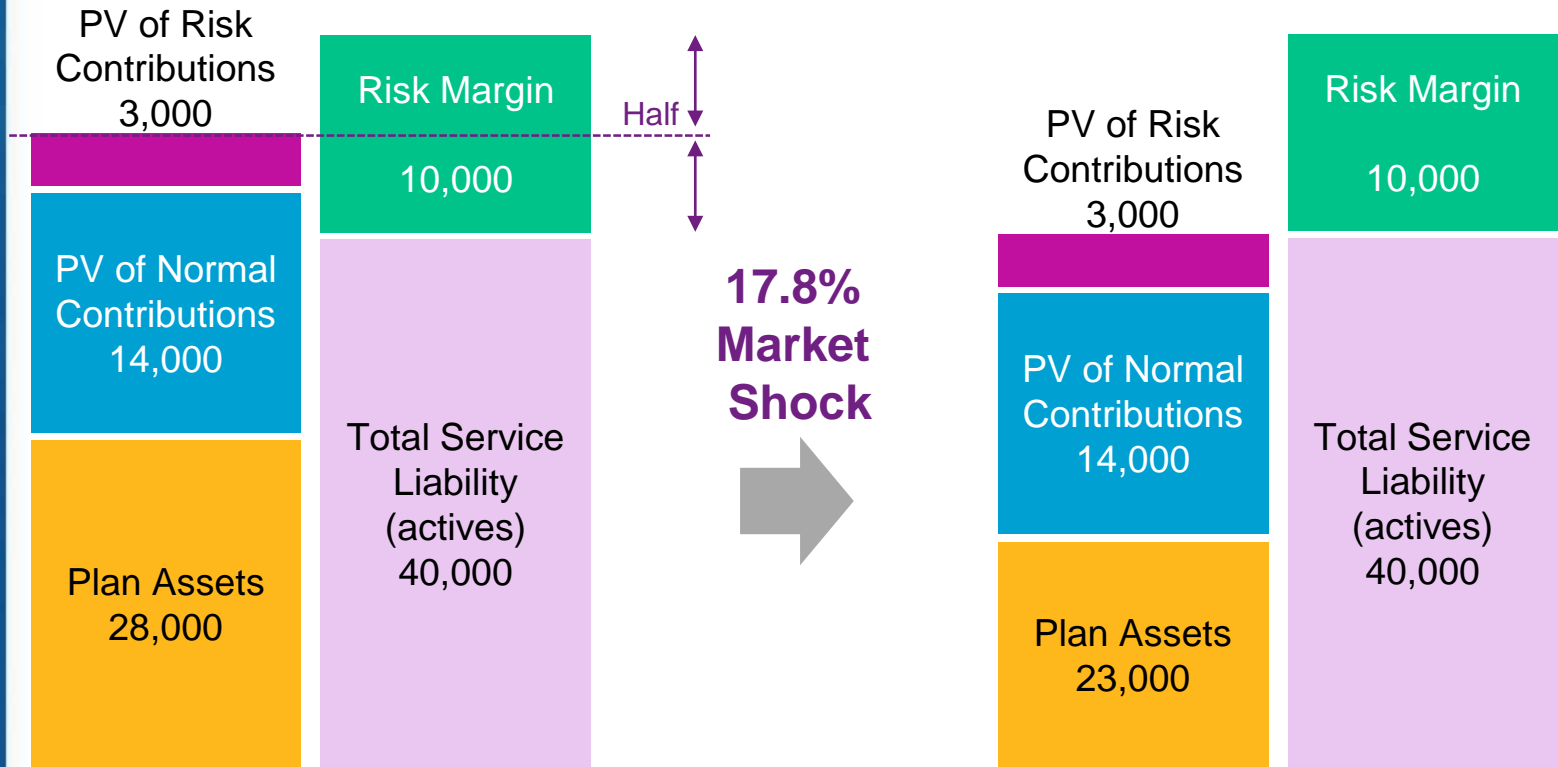
### New Strategic Asset Allocation

Asset classes	Old (DB)	New (RS)
Cash	3%	
Japanese Bonds		15%
Foreign Bonds (hedged)		65%
Global Bonds	46%	
Global Equities (unhedged)	27%	20%
Private Equity	4%	
Global Real Estate Investment Trust	7%	
Fund of Hedge Fund	13%	
Bonds / Equities / Alternatives allocation	49 / 27 / 24	80 / 20 / 0
Net foreign currency exposure	25%	20%

De-risked and removed alternatives to simplify

## Case Study

### Risk Margin and Risk Contribution Level



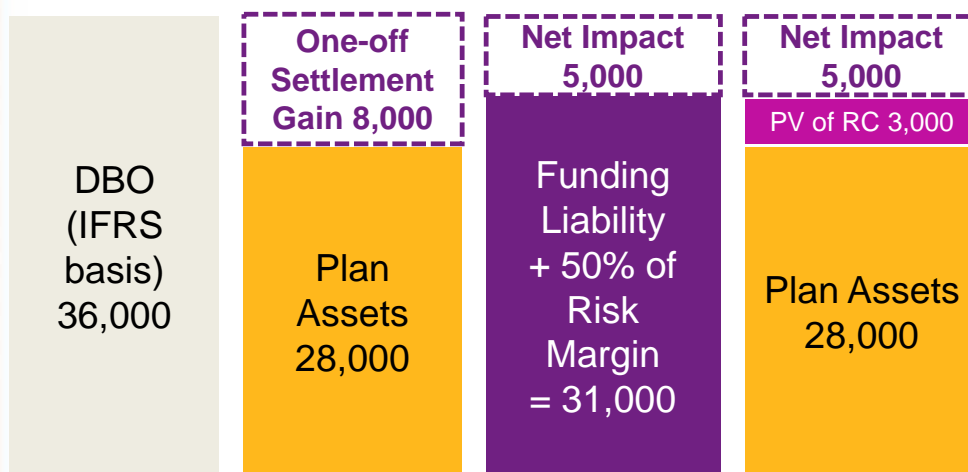
JPY millions

# Case Study

## Financial Impact



### One-off Settlement Gain and Net Impact



### Change in On-going Cost



JPY millions



# Case Study

## Benefit Adjustment Simulations



### Surplus to Risk Margin Ratio

**Risk Margin: JPY 10 billion**

Risk margin funding level: 50%

PV of Risk Contributions: JPY 3 billion

