Social Security

International Update:

Recent Developments in Foreign Public and Private Pensions

September 2016

Europe

Turkey Introduces Automatic Enrollment for Private Pensions

On August 10, the Turkish government approved an amendment to the Private Pension Savings and Investment System Law (implemented in 2003) that requires the automatic enrollment of all wage-earning citizens younger than age 45 (in both the public and private sectors) into private defined-contribution pension plans. The amendment is effective on January 1, 2017. According to the government, the reform will expand participation in private pension plans and increase retirement savings in the country. At present, only around 8 percent of the population (6.4 million people out of a total estimated population of 79 million people) contributes to a private pension plan.

Under the new rules, employees will automatically contribute 3 percent of their gross income to private pension plans chosen by their employers. (The Council of Ministers has the authority to increase the automatic contribution rate up to 6 percent or to decrease it to 1 percent in the future.) Employees may choose to opt out of the system within the first two months following their automatic enrollment and have their paid contributions plus any investment returns refunded. The government will match 25 percent of an employee's contributions and will make an additional one-time contribution of 1,000 liras (US$337.73) for those who do not opt out within the first two months. (Government contributions are subject to certain vesting requirements.) There is no contribution requirement for employers.

Other key provisions of the amendment include:

- A participating employee who changes jobs will have his or her account balance transferred to the new employer's private pension plan. If the new employer does not have a private pension plan, the employee may choose to remain covered under his or her previous employer's plan or terminate participation altogether.
- Upon retirement, employees may choose to withdraw their savings as a lump sum or purchase an annuity. As an incentive to annuitize, the government will contribute an extra 5 percent of the account balance for those who purchase an annuity paid over a period exceeding 10 years.

Under the rules currently in place, enrollment in the private pension system is strictly voluntary and available to all individuals aged 18 or older. (There are no employment relationship requirements.) Participants may open an account with a pension company, and the contribution varies according to the contract with the company. (Details are not yet available on the impact of the new amendment on these current rules for voluntary participants.) As with the new rules, the government provides a match (since 2013) of 25 percent of an employee's contributions to encourage participation. There are currently 19 private pension companies with around 56 billion lira (US$18.9 billion) in assets under management.

Private pensions supplement the public pay-as-you-go (PAYG) pension program that covers all employees, including civil servants, self-employed persons, and full-time household workers. Employees contribute 9 percent of their monthly earnings to the PAYG program; employers contribute an additional 11 percent. In general, public old-age pensions are paid at age 60 for men (age 58 for women) with at least 7,200 days of paid contributions, or at age 63 for men (age 61 for women) with at least 5,400 days of paid contributions.

Sources: *OECD Private Pensions Outlook 2008*, Organisation for Economic Co-operation and Development, 2008; *Social Security Programs Throughout the World: Europe, 2014*, U.S. Social Security Administration, September 2014; "Turkey Approves New Auto-Enrollment Law for Private Pensions," International Adviser, August 15, 2016; "Turkish Employees to be Automatically Enrolled to the Private Pension System," Baker & McKenzie International, August 25, 2016; "A New Era for the Private Pension System in Turkey," CMS Law-Now, August 25, 2016; "Turkey Lawmakers Approve New Mandatory Private Pension Law," *Middle East Insurance Review*, September 1, 2016.

Asia and the Pacific

India Lowers Minimum Annual Contribution and Balance Requirements for Individual Account Program

On August 9, India's Pension Fund Regulatory and Development Authority (PFRDA) announced that it would immediately lower the minimum annual contribution and balance requirements for the country's National Pension System (NPS), an individual account program. As a result, the minimum annual contributions required to keep an NPS account active were reduced from 6,000 rupees (US$89.72) to 1,000 rupees (US$14.95) for the Tier I (retirement) account and from 250 rupees [US$3.74] to 0 rupees for the Tier II (savings) account. Likewise, the minimum annual balance to keep a Tier II account active, which had been 2,000 rupees (US$29.90), was abolished. (There is no balance requirement for Tier I accounts.) In conjunction with these policy changes, the PFRDA took the one-time action of reactivating all existing NPS accounts that had been frozen for not meeting the prior contribution and balance requirements.

By lowering the account minimums and restoring frozen accounts, the PFRDA is seeking to boost active participation in the NPS. As of January 2, the NPS had nearly 9.5 million registered participants (out of a 2016 estimated population of 846 million people aged 18 or older), but only about half of those participants (53 percent, or 5 million) were potentially eligible to contribute to their NPS accounts (the remaining portion were NPS pensioners). Moreover, within this group of potential contributors, the overwhelming majority of participants (89 percent, or 4.5 million) were government employees. The concentration of NPS participants in the public sector has only decreased slightly (by approximately 11 percent) since the program was opened in 2009 to all Indian citizens (aged 18 to 60) on a voluntary basis. Participation in the NPS has been mandatory for all new central government employees and some new state government employees since the government established the program in 2004.

Although the NPS has undergone several reforms in recent years, the basic design of the program has not changed. Every participant in the NPS receives access to two types of accounts: (1) a compulsory Tier I account for retirement savings and (2) an optional Tier II account for personal savings. Similar investment options exist for both types of accounts, but participant access to account funds is much more restricted for Tier I accounts than it is for Tier II accounts. Funds in Tier I accounts cannot be accessed unless they are primarily used to purchase an annuity (the exact share that must be annuitized varies from 40 percent to 100 percent depending on the age of the participant and the size of the Tier I balance). NPS rules require participants to annuitize their Tier I accounts by age 60. By comparison, funds in Tier II accounts can be withdrawn at any time and used for any purpose.

Besides the NPS, the other major pension programs in India are the Employees' Provident Fund (EPY), Employees' Pension Scheme (EPS), and Atal Pension Yojna (APY) Universal Pension. The EPY offers lower income workers employed at larger firms (those with 20 or more employees) a provident-fund pension that can be claimed at age 55. The EPS covers the same group of workers as the EPY, but a worker must be aged 58 or older and have at least 10 years of coverage to qualify for a full benefit from this supplemental defined-benefit program. The APY is a voluntary defined-benefit program targeted at informal-sector workers aged 18 to 40.

Sources: "India," *International Update*, U.S. Social Security Administration, August 2012; *Social Security Programs Throughout the World: Asia and the Pacific, 2014*, U.S. Social Security Administration, March 2014; "1.15 Crore Subscribers for National Pension System (NPS) as on 23.1.2016," Indian Ministry of Finance press release, February 2, 2016; "Circular No. PFRDA/2016/19/CORP/4," Pension Fund Regulatory and Development Fund, August 9, 2016; "NPS: PFRDA Lowers Minimum Contribution to Rs 1,000 per Year," The Economic Times, August 15, 2016; *International Data Base*, U.S. Census Bureau, September 15, 2016.

Japan Will Implement Changes to Defined Contribution Plans

The Japanese government recently passed amendments to the Defined Contribution (DC) Law, which will produce significant changes to Japan's system of voluntary defined contribution (DC) pension plans beginning January 2017. Those changes will affect plan eligibility, fiduciary responsibilities of plan sponsors, and investment rules. With the amended law expanding plan coverage to groups currently unable to participate, the government expects that the resulting increase in DC plan participation will improve the

retirement income security of Japan's aging population. According to the Organisation for Economic Co-operation and Development, Japan's population is one of the oldest in the world, with nearly one-third aged 60 or older, and retirement savings relative to population size and age remain relatively low. Only 10 percent of the working-age population of 65 million currently participates in a DC plan.

The affected voluntary DC plans, first implemented in 2001, fall into two categories: (1) corporate DC plans provided by private-sector companies for employees and (2) individual plans for employees and self-employed persons without access to a corporate DC plan. In the case of corporate DC plans, only employers were initially allowed to contribute, but this changed in 2012 when employees were also permitted to contribute. Contributions for both categories of DC plans are tax deductible, while investment gains are untaxed. Because of the tax-advantaged nature of the accumulated funds, withdrawals are generally only allowed once a participant reaches age 60. Participants choose investment options from a pre-selected menu of financial products offered by a financial services provider or a plan administrator (hired by the company in the case of corporate DC plans). Employers must provide investment education through the plan administrator. When employees change jobs, their account funds roll over into another (corporate or individual) DC plan.

The amended rules will apply to both categories of DC plans and will be phased in as follows:

- Beginning on January 1, 2017—
  - — Restrictions on DC plan participation will be removed to allow contributions from non-working spouses of employees, public-sector employees, and individuals currently covered only by private defined benefit (DB) plans (current restrictions prohibit participation where entitlement to a private defined benefit plan already exists);
  - — The "exception rule" that currently allows DC plan participants with modest balances of up to 500,000 yen (US$821.35) to cash out if they stop working (and thus become ineligible to participate) will be eliminated.
- Beginning on January 1, 2018—
  - — Contribution limits will be redefined from an annual to a monthly basis to allow for more flexible contribution arrangements.

Additional changes to corporate DC plans are expected—effective date(s) yet to be determined—including new restrictions on the number and type of investments offered; a reduction in employee control over the investments offered; and a requirement that plan sponsors review the service quality of DC plan administrators every five years. Other changes will also allow smaller employers to contribute on behalf of their employees to individual DC plans and permit state-sponsored retirement plans for small employers to transfer employee assets to DC plans.

At the end of 2014, there were 5.2 million members in both corporate and individual DC plans with total assets exceeding 7.5 trillion yen (US$72.3 billion). In addition to DC plans and employer-sponsored DB plans, Japan has a two-tiered public pension system that includes a flat-rate plan for all residents under the National Pension program and an earnings-related plan under the Employees' Pension Insurance program.

Sources: "Taking Japan's Defined Contribution Pension Plans to the Next Level," *Nomura Journal of Capital Markets*, Winter 2013; "Japan: Eligibility for DC Plans Could Be Expanded," *Global News Briefs*, Willis Towers Watson, January 8, 2015; "Japan: Defined Contribution Act to Be Amended," *Global News Briefs*, Willis Towers Watson, April 7, 2015; "Japan: New Legislation a Game Changer for the Defined Contribution Market," *Global News Briefs*, Willis Towers Watson, June 9, 2016.

International Update is a monthly publication of the Social Security Administration's (SSA's) Office of Retirement and Disability Policy. It reports on the latest developments in public and private pensions worldwide. The news summaries presented do not necessarily reflect the views of SSA.

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SSA Publication No. 13-11712
Produced and published at U.S. taxpayer expense