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## Evolving landscape of retirement plans in Asia

Allen Wu, Mercer, China

[www.mercer.com](http://www.mercer.com)

## Landscape

Big picture around the world and Asia

Move away from defined benefits (DB) to defined contributions (DC)

Cost containment driven by accounting standard changes and market conditions

Focus on cross-border retirement benefits

Increased plan governance

Consolidation of plan financing

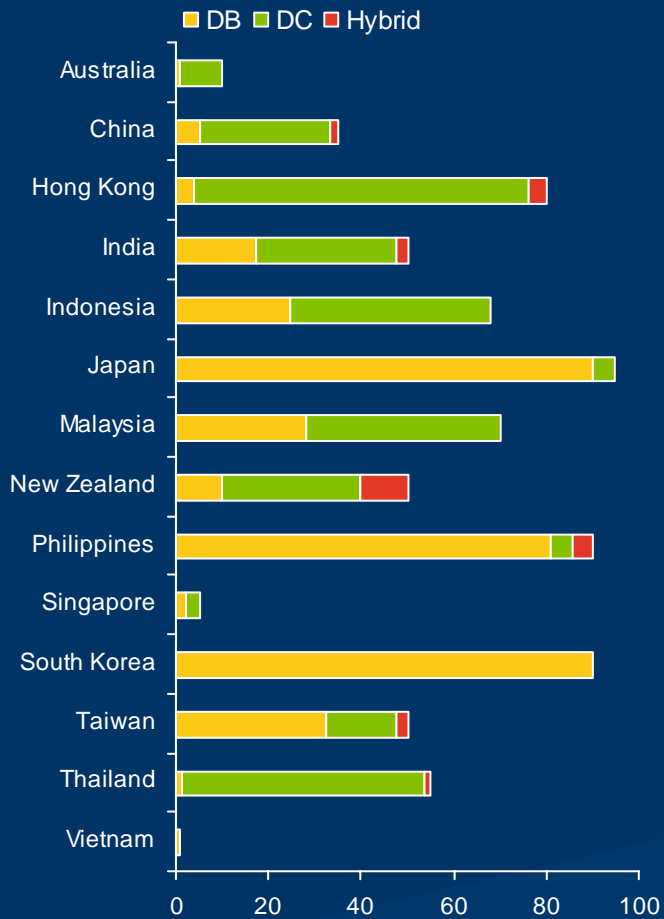
Greater involvement by corporate and finance staff

# Retirement plans in Asia Pacific

## Mercer's research – August 2007

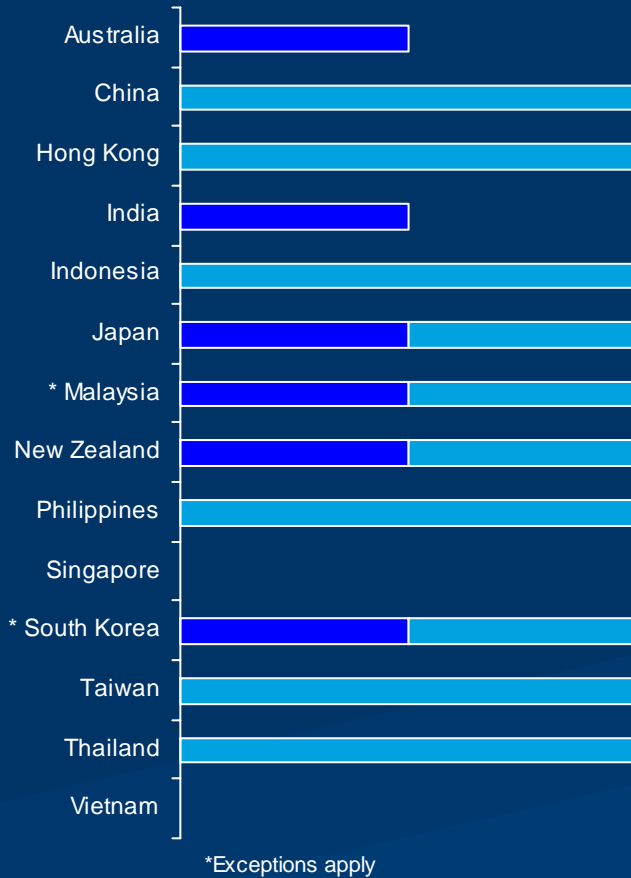
### Prevalence and types of supplementary retirement plans

Approximate % of multinationals and leading local companies



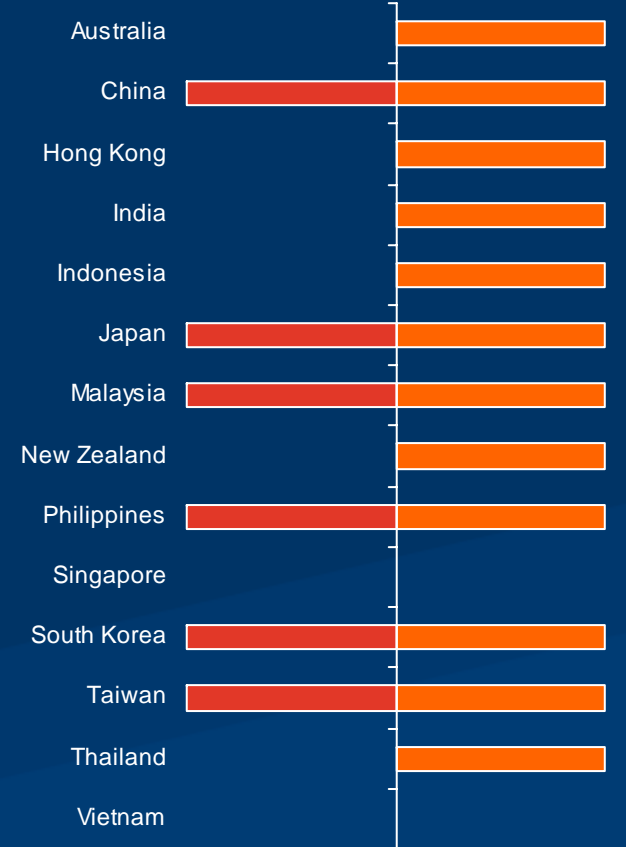
### Plan eligibility in a typical supplementary plan

Management or higher earners only  
All employees
















### Plan financing in a typical supplementary plan

Unfunded  
Funded and/or Insured



# Retirement plans

Design – type of corporate program

	Mandatory	Discretionary
DB widespread	 Taiwan  South Korea	 Japan  Philippines
Mix	 Hong Kong  India	 Indonesia  New Zealand
DC widespread	 Australia	 Malaysia  PRC  Singapore  Thailand

## Move away from defined benefits

- **Hong Kong:** Increased sophistication of DC investment choices and member services
- **Indonesia:** Move from un-funded DB book reserve to a DC plan to fund mandatory termination benefits
  - Driven by Labor Law #13 – termination due to attainment of retirement age
- **Japan:** Low contribution limits mean DC only is not viable; ~ 8,000 companies implemented DC-type plan
- **Malaysia:** Move towards DC in the form of additional contributions to Employee's Provident Fund
- **Taiwan:** New portable DC-type mandatory retirement system – Labor Pension Act – effective 1 July 2005
- **Thailand:** Increased usage of voluntary Provident Fund (DC)

## Increased plan governance

- **China:** All local labor and social security bureaus are to transfer existing supplementary pension funds to appointed licensed Enterprise Annuity provider in 2008
  - Driven by Shanghai Pension Bureau issue
- **India:** From 1 April 2006, Indian Accounting Standard (AS 15) for DB was revised; more detailed disclosures required
- **Indonesia:** All pension funds to comply with new pension fund governance law by 1 January 2008
- **South Korea:** Compliance with International Financial Report Standards (IFRS) will commence from 2011

## Changes to benefits financing

- **China:** Proposed new law, if approved:
  - Will permit insurers to expand their business into superannuation trustee management and third-party benefits administration
  - May impact or create competition for brokers currently in the same business
- **Hong Kong:** MPF Authority proposes to raise the cap of the monthly salary to which MPF contributions apply
  - From HK\$20,000 to HK\$30,000

## Changes to benefits financing (cont'd)

- **Japan:** TQPP plans must be converted into new plans (qualified DC or qualified DB) by March 2012
- **Singapore:** Effective from 1 July 2007, the government will raise the employer's Central Provident Fund contribution rate by 1.5%
- **South Korea:** Existing book reserves will lose their tax qualified status by December 2010
- **Thailand:** The Thai government is planning to make the Provident Fund a mandatory vehicle in 2008

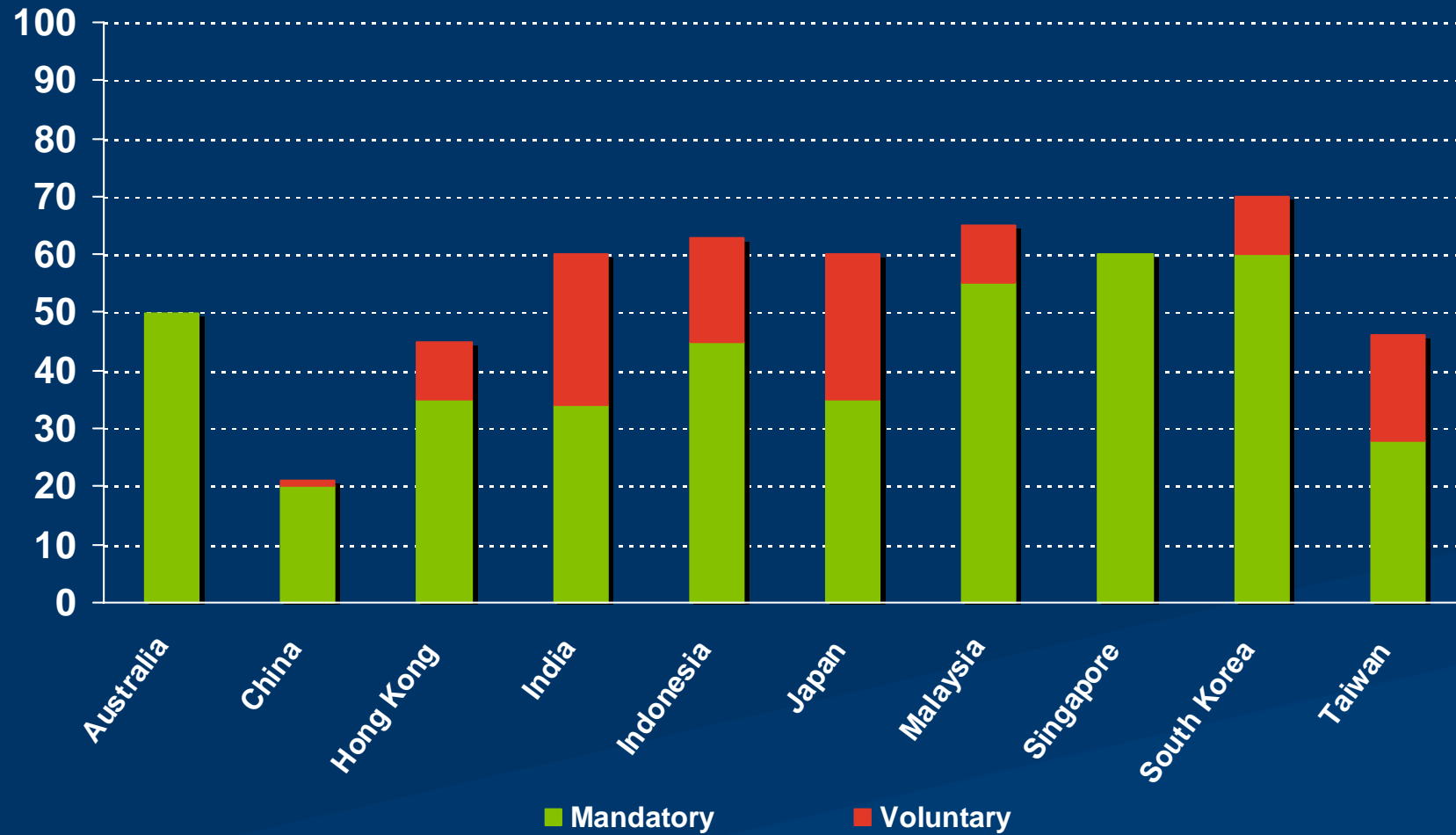
## Growth of new plans

- **China:** More than 60% of multinationals surveyed plan to implement an Enterprise Annuity plan between 2006 and 2008
- **Singapore:** As of October 2007, the government will abolish hospital subsidies for all foreigners and replace with a compulsory employer-paid medical insurance scheme
- **South Korea:** Over 40% of Foreign Affiliate companies surveyed plan to adopt ERSA within the next two years. 14,235 new ERSA plans in existence (as at December 2006)

## Complexity of managing retirement issues in Asia

Diverse retirement benefit arrangement

Retirement benefit expressed as a % of average salary at retirement



# Managing retirement/savings issues

How are companies are coping?

## Governance/financial management

- Coping with financial reporting requirement and managing financial volatility
- Evaluation on proper funding and financing
- Asset liability modelling

4

## Governance/financial management

- Setting new plans, plan conversions
- Employee communications
- Trustee and provider selections

1

## Complexity of retirement issues

3

## Adequacy/aging workforce

- Replacement ratios evaluation
- Employee education
- Post-retirement phase

2

## Delivery for talent

- Benchmarking
- Workforce segmentation
- Attractive plan features
- Mobile employee solutions

## Key takeaways

Active management of regulatory changes (China, Korea, Japan, Singapore, Vietnam, Thailand)

High-performance plan design for benefit delivery (China, India, Korea)

Greater emphasis on managing benefit adequacy and aging workforce (Singapore, Malaysia, Hong Kong)

Regional governance framework and risk management – DB & DC (China, India, Indonesia, Philippines)



**Questions?**



**Appendix**

# **Asia Pacific country updates**

## Asia Pacific country updates

- [China](#)
- [Hong Kong](#)
- [India](#)
- [Indonesia](#)
- [Japan](#)
- [Malaysia](#)
- [Philippines](#)
- [Singapore](#)
- [South Korea](#)
- [Taiwan](#)
- [Thailand](#)
- [Vietnam](#)

## China

### Regulatory environment

#### **Social security retirement benefit is insufficient**

- A national social pension system now applies throughout China
- Low-income replacement ratios are expected among employees from multinational companies
- From 1 January 2006, benefits to employees were reduced as their Individual Account contribution rate lowered from 11% to 8%
  - Employer contribution goes to Public Account

#### **Mandatory practice**

##### **Old Age Pension Insurance (DB and DC)**

- Contributions:
  - Employer: 20-22% (varies by city)
  - Employee: 8%
- Goes towards pension, medical, unemployment, work injury, housing

### Supplementary DC plans available and becoming popular

- China has set in motion a 401(k) type of pension market (Enterprise Annuity or EA)
- Over 60% of surveyed multinationals in China plan to convert / implement an EA in the next five years\*
- No nation-wide tax relief policy on SPP contributions
- EA contributions are tax deductible up to certain limits

### Typical practice

- Approximately 20-35% of multinationals provide supplementary plan:
  - DB – 15%
  - DC – 80%
  - Hybrid – 5%
- Employer contribution: 5-10% of salary (SRP). EA: Max 1/12 of payroll.
- Typical DC plan design: All employees eligible. SRP: Insurance policy, book reserve. EA: Trust.
- Executive-only plan: Not prevalent

\*Source: Mercer 2007 Retirement Survey

## Hong Kong Regulatory environment

- From 18 January 2008:
  - Housing allowances and benefits and included in definition of relevant income
  - All remuneration items to be taken into account for mandatory contributions

### Proposals under review:

- Raise cap of monthly salary (relevant income) to which MPF contributions apply from HK\$20,000 to HK\$30,000
- Allowing employees to decide MPF service provider for their own contributions
- Tax deduction up to 10% voluntary employee contributions but will need to be preserved until retirement

## Mandatory practice

### Mandatory Provident Fund (MPF) (DC)

- MPF mandatory contributions towards retirement
  - Employer: 5% (salary capped)
  - Employee: 5% (salary capped)
- Plus social security system, financed entirely by government
  - provides a safety net for people with low income

### Increased sophistication of DC plan member services and investment choices

- Companies starting to review their service provider's performance
  - MPF attracting more employee attention as balances grow
- Some larger employers still operate voluntary (ORSO) schemes due to greater flexibility
- Some employers using retirement schemes to increase tax efficiency for members

### Typical practice

- Approximately 80% of multinationals provide supplementary plan (including MPF top-up):
  - DB – 3%
  - DC – 95%
  - Hybrid – 2%
- Employer contribution: 5-10% of salary (uncapped) inclusive of mandatory contributions
- Typical DC plan design: Permanent full-time employees eligible for supplementary benefits. MPF top-up plan: Majority are master trust.
- Executive-only plan: Not prevalent

## India

### Regulatory environment

#### **New accounting standard introduces greater plan governance**

- Effective 7 December 2006, Indian Accounting Standard (AS15) for DB schemes is revised to be in line with IAS 19 – more detailed disclosures
- Some multinationals operate gratuity schemes which provide for amounts higher than the statutory minimum
- Most employers extend Employee's provident fund (EPF) participation to all employees

#### **Mandatory practice**

##### **Gratuity Scheme (DB) compulsory for companies with 10 or more employees + Employees' Provident Fund (EPF) (DC if government managed)**

- Contributions\*: EPF: Employer: 12%; Employee: 12%
- Salary cap is INR6,500 per month

\* Applies to companies with 20+ employees and only for employees with salary of INR6,500 or less

### Growing interest in DC investment options and employee choice

- Insurance companies offering DC investment options in voluntary superannuation schemes since 2002
- Employee investment choice not typical but growing interest
  - Only under a scheme with life insurance company
- Employer contributions to superannuation scheme do not incur Fringe Benefits Tax for many plan participants except high earners

### Typical practice

- Approximately 50% of multinationals provide supplementary plan:
  - DB – 35%
  - DC – 60%
  - Hybrid – 5%
- Employer contribution: 15% of wages (salary + dearness allowance)
- Typical DC plan design: Only management staff eligible  
Superannuation scheme:  
Insurance policy or private fund
- Executive-only plan: Common

## Indonesia

### Regulatory environment

- New law on pension fund governance
  - Pension funds need to comply by 1 January 2008
- New government regulation requiring employer funding of the Labor Law termination indemnity
  - Contribution = 3% of basic salary (capped) + additional contributions in relation to past service – expected to come into effect in 2008
- 2004 Social Security regulation needs further guidelines for implementation
  - Planned within five years from signing of law, at the latest

### Mandatory practice

#### Labor Law #13 Year 2003 (DB) + JAMSOSTEK (DC)

- Labor Law #13: Payable to all employees who have been terminated from the company due to the attainment of retirement age
- JAMSOSTEK: Compulsory for companies with more than 10 employees or with a monthly payroll of at least IDR1 million

## Indonesia

### Market practice

[Return](#)

- Nowadays DC plans are more popular than DB plans, namely DC plans secured through a FIPF
- Trend among companies to:
  - Move from an unfunded DB book reserve
  - Use a DC plan to fund the mandatory termination benefits under Labor Law #13

### Typical practice

- Approximately 68% of multinationals provide supplementary plan:
  - DB – 36%
  - DC – 64%
  - Hybrid – 0%
- Employer contribution: 6% of base salary
- Typical DC plan design: All employees eligible. EPF (larger schemes) or FIPF (small- to medium-sized companies)
- Executive-only plan: Not prevalent

## Japan

### Regulatory environment

#### Companies with TQPP plans to convert to new qualified DC or DB or other replacement plan by March 2012

- Normal retirement age (NRA) is gradually changing from 62 to 65 between 2006 and 2013
- 2001 new DB law introduced funded cash balance plans and minimum funding requirement; 2001 new DC Law

#### Mandatory practice

##### National Pension (NP) (DB) + Employees' Pension Insurance (EPI) (DB)

- Employer and employee contribute 14.642% (shared equally and covers EPI + NP) of standard monthly remuneration and standard bonus amounts
- Rate is increasing each year to reach 18.3% in 2017

## Japan Market practice

Return

### Traditionally DB, but recently DC-type plans introduced

- Some 8,000 companies have implemented DC-type arrangement
  - Contribution limits low so DC only is not a viable option
  - Although the number of DC plans are still relatively low, since many ‘big’ companies have them, a large portion of the workforce already has some form of DC accrual
- Applying a point system has been popular (approach unique to Japan)
- Trend to reduce or at least change directors’ pension arrangements

### Typical practice

- Approximately 95% of multinationals provide supplementary plan:
  - DB – 95% (55% funded, 40% unfunded)
  - DC – 5%
  - Hybrid – 0%
- Employer contribution: Full cost of plan
- Typical DC plan design: All regular employees eligible. Book reserve, TQPP/New DB, EDF, or combination
- Executive-only plan: Executive only plans are not common. Directors’ plans are fairly common

## Malaysia

### Regulatory environment

**From 2 January 2007, EPF member accounts are consolidated from three to two accounts**

- **Previously:** Account 1 (60% of members' savings), Account 2 (30%) and Account 3 (10%)
- **New structure:** Account 1 (70%) and Account 2 (30%)
  - Account 1 can be withdrawn only after age 55
  - Aims to increase funds for retirement and provide more flexibility
    - (a portion of Account 1 can be managed by approved external fund managers)

### Mandatory practice

#### SOSCO (DB) + Employees' Provident Fund (EDF) (DC)

- Contributions to SOSCO:
  - Employer: 1.75%
  - Employee: 0.5%
- Contributions to EPF:
  - Employer: 12%
  - Employee: 11%
- Retirement benefits are provided by the EPF

## Discretionary voluntary additional contributions to EPF

- Move to DC in form of additional contributions to EPF
  - Increasingly companies are making voluntary contributions to EPF and closing existing voluntary gratuity schemes
- Most common for management employees only but have now been extended to non-management
- Cheaper than a self-administered retirement plan – EPF administers plan at zero cost to employer

## Typical practice

- Approximately 70% of multinationals provide supplementary plan:
  - DB – 40%
  - DC – 60%
  - Hybrid – 0%
- Employer contribution: 3-5%; some bigger companies contribute 7%
- Typical DC plan design: Only management staff eligible. Voluntary additional contributions to EPF
- Executive-only plan: Fairly common

## Philippines

### Regulatory environment

- Pending bill to provide tax incentives to voluntary personal retirement accounts managed by accredited financial service providers
- Pag-IBIG coverage is mandatory for employees earning in excess of PHP4,000 per month
  - Both employers and employees are required to contribute
  - Private sector compliance has been low
  - Authorities indicate a determination to enforce the requirements with penalties and prison sentences

### Mandatory practice

#### Social Security (DB) + Labor Code (DB) + Pag-IBIG Fund (DC)

- Social Security Program has 29 contribution classifications based on employee earnings
- Under Labor Code, in the absence of a retirement plan, an employee is entitled to retirement pay equivalent to at least half a month's salary for every year of service
- Pag-IBIG provides housing and other loans to members, lump sum benefits per length of membership

## Philippines

### Market practice

Return

### New plans are still predominantly DB

- DC plans must still consider legal minimum (which is a defined benefit) so effectively become hybrid plans
- Underfunding of DB plans common
- Tax laws still favor plans operated as trusts (as opposed to insured plans)
- Pre-need (select financial services companies) and insurance companies offer pension plans which are attractive to small companies

### Typical practice

- Approximately 90% of multinationals provide supplementary plan:
  - DB – 90%
  - DC – 5%
  - Hybrid – 5%
- Employer contribution: Full cost of plan
- Typical DC plan design: All full-time employees eligible. Trust fund.
- Executive-only plan: Not prevalent

## Singapore

### Regulatory environment

**From 2008, employers may contribute to individual savings plans on a tax efficient basis**

**From 1 July 2007, employer's CPF contribution rate increases by 1.5%**

- For most workers aged 50 and below, this means employer contribution will increase from 13% to 14.5%:
  - 1% will go into employees' Ordinary Account, and
  - 0.5% will go into Medisave Account

**From 2006, the CPF salary ceiling was lowered to SGD4,500/month**

- A larger proportion of salary is not subject to CPF contribution for mid managers and above

### Mandatory practice

#### Central Provident Fund – CPF (DC)

- Contributions to CPF are divided into three accounts:
  - Ordinary account
  - Medisave account
  - Special account – for old age, contingency purposes and investment in retirement-related financial products

## Singapore Market practice

Return

- Supplementary pension plan is not prevalent but a few tax approved plans exist separate from CPF
- Employees without Singaporean citizenship or permanent residency are ineligible to participate in CPF
  - Most common response by companies when this restriction was introduced in 2003 was to pay cash in lieu of benefits for existing employees
- Increased interest in supplementary plan to provide benefits for non residents and employees earning above the CPF salary ceiling

### Typical practice

- Less than 5% of multinationals provide supplementary plan:
  - DB – 40%
  - DC – 60%
  - Hybrid – 5%
- Executive-only plan: Not prevalent

## South Korea

### Regulatory environment

#### **ERSA effective 1 December 2005**

- Existing book reserves will lose tax qualified status by December 2010
- Companies can meet both the statutory requirement (termination indemnity) and any supplementary benefits under single ERSA plan
- Employers with less than 10 employees can offer Individual Retirement Account (IRA) as alternative to ERSA plan

#### **Mandatory practice**

##### **National Pension Scheme (DB) + termination indemnity under SPS (DB) or funded ERSA plan (can be DB or DC)**

- National Pension Scheme has 45 contribution classifications based on employee earnings
- Termination indemnity = one month salary per year of service

## South Korea Market practice

Return

### Over 40% of foreign affiliate companies in Korea plan to adopt ERSA between 2006-2008

- As at December 2006, over 14,000 new ERSA plans are in existence
  - Local companies prefer DB
  - Foreign affiliates prefer DC
- Majority (50%) employee/union consent is required to establish a funded ERSA DB or DC plan

### Typical practice

- Approximately 90% of multinationals provide supplementary plan:
  - DB – 100%
  - DC – 0%
  - Hybrid – 0%
- Employer contribution: Full cost of plan
- Typical DC plan design: All full-time employees eligible but executive employees may have higher benefits. Book reserve (most plans), insurance or trust
- Executive-only plan: Not prevalent

## Taiwan

### Regulatory environment

#### **New Labor Pension Act (LPA) effective from 1 July 2005**

- LPA is a portable DC-type system. Old DB TLISA system is not portable
- From June 2006, first annuity insurance policy for LPA financing
  - Alternative to contributions to the Bureau of Labor Insurance
  - Only available for businesses employing 200+ employees

#### **Mandatory practice**

##### **New system: Labor Pension Act (LPA) (DC)**

##### **Old system: Taiwan Labor Standards Act (TLISA) (DB)**

- TLISA retirement benefit: Full cost of plan is borne by employer
- LPA contributions
  - Employer: Minimum 6%
  - Employee: 0% voluntary contributions, but possible up to 6%

### Discretionary leaving service benefit (DB) or voluntary additional contributions to LPA (DC)

- Due to LPA, many companies restructured their supplementary benefit to integrate it with new LPA
- If employees stay with one company until retirement age, they will receive TLSA benefit but not leaving service benefit
  - Cannot receive both benefits
- Underfunding is common
- Increasing interest/need for executive retirement arrangements

### Typical practice

- Approximately 50% of multinationals provide supplementary plan:
  - DB – 65%
  - DC – 30%
  - Hybrid – 5%
- Employer contribution: Full cost of plan
- Typical DC plan design: All full-time employees eligible. Book reserve
- Executive-only plan: Not prevalent

## Thailand

### Regulatory environment

#### Government proposes to make the Thai Provident Fund a mandatory vehicle in 2008

- Key features of the proposal:
  - Employers and employees mandatory contributions starting at 3% of salary but increasing to 6% (to be confirmed)
  - Contributions paid into a newly set up National Pension Fund (NPF)
  - Employee choice of investment funds from a set of approved fund managers

### Mandatory practice

#### Social Security (DB and DC)

- Contributions
  - Employer: 3% for retirement
  - Employee: 3% for retirement
  - 0% based on earnings, subject to minimum of THB1,650 and maximum of THB15,000 annually

## Thailand

### Market practice

Return

### Most supplementary plans are voluntary Provident Funds

- Increasing trend among companies to offer a voluntary Provident Fund
- Increasing trend among companies to consider offering choice of investment instead of a one-size-fits-all approach

### Typical practice

- Approximately 55% of multinationals provide supplementary plan:
  - DB – <5%
  - DC – 95%
  - Hybrid – <5%
- Employer contribution: Varies. Starts at 5%, then increasing based on service. Must equal or exceed EE contribution
- Typical DC plan design: All employees eligible. Voluntary Provident Fund
- Executive-only plan: Not prevalent

## Vietnam

### Regulatory environment

#### **New Social Insurance Law effective 1 January 2007**

- Reduces contributions to Social Insurance system for employees with salaries above a certain ceiling (currently VND9 million per month)
- Employer to decide whether or not to compensate employees for the reduction in mandatory contributions

### Mandatory practice

#### **Social Insurance Law (DB)**

- Contributions
  - Employer: 15% of contracted gross base salary
  - Employee: 5% of contracted gross base salary

**Retirement plans not prevalent and legislation is almost non-existent**

- Provision of retirement benefits is tax neutral compared to cash compensation
- Several companies are inquiring about possible options
- At least two large multinationals have chosen an unfunded cash balance arrangement (DB in IAS 19 sense)

**Typical practice**

- Less than 1% of multinationals provide supplementary plan:
  - DB – 100%
  - DC – 0%
  - Hybrid – 0%
- Executive-only plan: Not prevalent

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