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Defined Contribution Country Reference

As part of its ongoing assessment of the global defined contribution (DC) savings industry, the DCIIA Global Committee conducted an initial survey of 10 key markets. This report summarizes basic information about market size, structure, contributions, distributions, investment design, recordkeeping, administration, retirement income, and taxation. We believe this information will help multinational plan sponsors who manage DC plans in foreign countries and aid other parties who service those plan sponsors. We made every attempt to provide consistent information and sources across countries to the extent made possible by reporting standards.

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FOREWORD

Reevaluation of Defined Benefit Systems

We believe that publishing this information is especially pertinent now, as some countries consider moving from defined benefit (DB) systems to defined contribution systems because of changes to labor markets, current economic conditions, and aging populations. Much of the world faces uncertain economic times with low growth, fluctuating interest rates, high levels of government indebtedness, a constrained market for the issuance of new sovereign debt, extended life expectancy, and declining support ratios (the number of workers to retirees).[1] These factors have led to a steady decline in the number of workers covered by pre-funded DB pensions, while new traditional-formula private DB plans are not being created anywhere in the world. Additionally, many countries are reevaluating their reliance on pay-as-you-go systems in light of the challenges created by stagnant economic growth or aging populations.

Large Scale, More Accessible Markets

This summary focuses on large markets where multinational plan sponsors would typically consider adding DC plans for their foreign operations. It examines countries with:

- Well-developed DC systems (Denmark, Australia)
- DB-in-transition-to-DC (the Netherlands, Canada, UK)
- Large markets with relatively low absolute levels of funded pensions – represented as a percentage of GDP – but with emerging public policies aimed at establishing new DC savings structures (Germany, France, Mexico, Japan, Hong Kong)

Given the varying maturities of these countries' DC markets, there is more robust information for some countries than others.

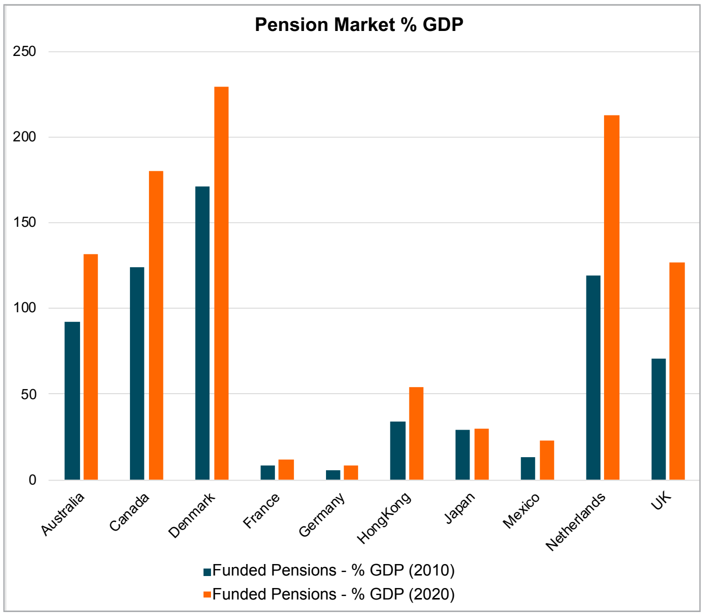
Notably absent from this survey is China, which never established wide-coverage pensions and is just beginning to create DC savings plans. There are early signs that global asset managers will play a role in this growth in partnership with local financial practitioners, which merits continued monitoring.

Statistical Overview of Markets to be Reviewed in this Paper

While total pension assets articulate the AUM/size of a retirement finance market, the assets/GDP illustrates private funding levels relative to the national economy. Low funding levels often suggest "room to grow" for emerging DC savings markets. See below for current comparative asset/GDP levels, which are a mix of DB and DC.

Exhibit 1

Comparative Levels of DB/DC Assets, 2010 vs. 2020



Source: OECD Pension Markets in Focus, 2021

By some estimates, two-thirds of new assets under management during the next generation will rise within DC savings systems.[2] And these assets will overwhelmingly rise in large economies that can generate substantial savings volumes.

The following table summarizes some key data points for the ten countries this summary considers.

Key Data Points for DB/DC Assets:

Across All Countries Covered

- Total retirement assets (DB+DC) under management for this project: These ten markets comprise some US$11.7 trillion.

Well-Funded Markets (>100% GDP)

- Well-funded markets with more than 100% of GDP comprise about US$9.47 trillion of the total.
- Of well-funded markets:
  - Denmark and Australia are primarily DC
  - Canada, UK, and the Netherlands are primarily DB, although all are undertaking policies of directing new worker/participants to DC structures.
- Because of this DB-to-DC transition, the growth of DC will be extensive.

Less Well-Funded Markets (<100% GDP)

- Less well-funded markets with less than 100% of GDP make up about US$2.3 trillion of the total.
- DC savings plans in France, Germany, Hong Kong, Japan, and Mexico are emerging as the funding architecture of choice.
- Less well-funded markets are expected to see the most rapid growth of DC savings.
- If these less well-funded markets achieved DC savings of 100% of GDP, this would represent US$7.3 trillion in new AUM.

Source: JM3 Projects Analysis using OECD data and World Bank data

The era of DC workplace savings is upon us. During the next generation, we expect a tsunami of growth in existing DC systems and a historic wave of new investment flows as DC systems emerge around the world.

[1] OECD Pension Markets in Focus, 2020 | GDP Data - World Bank

[2] Ibid.

EUROPE

DENMARK

What is the approximate size of the market and structure of the system?

In Denmark, the funded pension market is DKK 770 billion, based on OECD data.[1] There is a State Pension-Basic "poverty-prevention" structure, with add-on benefits dependent on work-related income. There is also a means-tested supplementary pension benefit. Public benefits are adjusted annually in line with average earnings.

The Danish Labor Market Supplementary Pension (ATP) is a statutory, fully funded DC system based on collective insurance funded by employers and employees. The system had a total of DKK 156 billion and covered 5.2 million Danish workers in 2019.

How are contributions handled?

ATP contributions are mandatory. Contributions are for a fixed amount – as opposed to a percentage of income – and vary depending on the number of hours worked. Full-time employees contributed DKK 3,408 per year in 2017. Employers put in two-thirds of total contributions and workers pay one-third. These contribution amounts are for the ATP plan only.

What does the investment structure look like for participants? What is a typical default?

Denmark's private DC ATP fund is a statutory, supplementary, fully funded collective insurance-based DC scheme, governed by collective agreements with social partners. It covers 85% of wage earners and almost all recipients of the country's social security scheme.

The ATP is nearly universal, except for self-employed workers, whose participation is voluntary. ATP is invested in a guaranteed deferred annuity. Consistent with the DC system, each generation of workers invests in its own retirement. There is no intergenerational transfer of wealth from current workers to current retirees, so there is no "intergenerational conflict." Benefits are delivered in the form of a guaranteed annuity.

What do recordkeeping, fees, and competitive market structure look like?

Because Denmark's DC system is largely a social system and nearly universal, it is difficult to assess the competitive market. "ATP covers all wage earners and almost all recipients of social security benefits."[2] The occupational pension schemes are fully funded DC schemes agreed upon between the social partners through collective agreements.

Income is becoming increasingly important to DC schemes. How does Denmark handle income?

ATP provides a lifelong pension from the normal pension age, and a survivor's lump-sum benefit for dependents when a member dies early.

Are there relevant tax considerations?

The ATP, occupational pensions and other private pension savings in Denmark have an "ETT" format – contributions are tax exempt; investment returns and distributions are taxed.

All returns to investment pension plans – lifelong pensions, annuity pensions, and lump-sum pensions – are taxed at 15.3%.[3] Recent reforms capped the annual contribution payable into fixed-term annuity contracts at DKK 50,900. Periodic pension payments are subject to personal income tax. ATP, occupational pensions, and other private pension savings are subject to an ETT tax regime. Payment under a funded pension scheme is subject to a flat tax at 40% on lump-sum withdrawals.

[1] OECD Pensions at a Glance 2019

[2] OECD Pensions at a Glance 2017: Country Profile – Denmark

[3] OECD Pensions at a Glance 2019: Country Profile – Denmark

EUROPE

FRANCE

What is the approximate size of the market and structure of the system?

France's retirement system comprises three pillars:

1. Mandatory state pension
2. Mandatory supplementary pension - DC
3. Voluntary private pension - DC

France's funded pensions represent approximately 14% of GDP. The pension system is facing a significant deficit (€14 billion as of February 2020), which is projected to grow substantially because of the pandemic.[1] Pension reform has been a key policy of President Emmanuel Macron. An initial proposal for pension reform was issued in 2019, which resulted in an extended strike in late 2019 and early 2020. The reform was ultimately delayed due to the pandemic.[2] France's new law on Business Growth and Transformation (Plan d'Action pour la Croissance et la Transformation des Entreprises – PACTE) was enacted in 2019 and reformed the voluntary pension plans. It replaced four types of plans and introduced three new ones collectively known as PER. Lack of confidence in the future of the state pension is driving interest in voluntary plans. The prevalence of voluntary retirement plans is higher among medium and larger companies.

How are contributions handled?

Mandatory payroll taxes are paid into the state pension. The overall rate for state pensions is 15.45% of salary, up to €41,136 per year. The Agirc-Arrco scheme covers most workers for the mandatory supplemental pensions. As of Jan. 1, 2019, the Agirc-Arrco scheme uses a two-salary-bracket contribution basis. A separate contribution rate applies to each salary bracket and is shared between the employer (60%) and the employees (40%). For voluntary plans, market practice is 3%-5% contributions.

Pension reform was proposed in 2019 that would merge all mandatory pension schemes into a single points-based system. The legislation proposed contributions of 28.12% of renumeration, up to three times the social security cap (€123,264). This reform was delayed due to the pandemic.

What does the investment structure look like for participants? What is a typical default?

Mandatory plans (state and supplemental) are insurance-based. Voluntary retirement plans may have a fixed number of investments. Until 2019, participants in voluntary pension plans were required to purchase an annuity. Reform allows retirees to receive their pension as a lump sum and allows individuals to access their accounts early to purchase a primary residence.

What do recordkeeping, fees, and competitive market structure look like?

The state is the main guarantor of the state pension. There are 42 different programs with different rules. For private-sector employees, the mandatory supplementary pensions are administered by the Agirc-Arrco scheme. Proposed pension reform would have collapsed the 42 different programs into one.

Income is becoming increasingly important to DC schemes. How does France handle income?

An individual's state pension rates are calculated based on the best 25 years of employment. The mandatory supplementary pension scheme is a point-based system: Each year, an individual's contributions are converted to retirement pension points and added to his/her account. To calculate the retirement pension amount, the number of points is multiplied by the value of the point, which is determined each year. For the voluntary plans, income is based upon contributions and returns.

The income drawdown scheme for the mandatory state pension (pillar #1) gives two options: capped and flexible. Capped schemes (most common) allow investors to choose how much money to draw from their pension each month. If investors want to draw a lump sum, they can draw up to a certain amount (usually around 25%) of the total value of the pension fund.

The PACTE law introduced in 2019 removed the requirement that defined contribution plan participants must purchase an annuity. Participants are now eligible to receive their DC pension as a lump sum.

Are there relevant tax considerations?

With a voluntary plan, employee contributions are tax-exempt up to 8% of compensation, capped at eight times the social security ceiling (SSC), which changes annually.

[1] France24, "Why France's 'unsustainable' system may well be sustainable," Benjamin Dodman, 12/23/2019

[2] BBC News, "French reforms: Why France is resisting Macron's push on pensions," Hugh Schofield, 2/17/2020.

Sources used generally:
Center for European and International Social Security Liaisons (CLEISS.fr);
Organisation for Economic Co-operation and Development (OECD);
Thomson Reuters Practical Law's "Regulation of State and Supplementary Pension Schemes in France: Overview;"
Data received from a Morningstar coworker from Mercer Retirement Report 2017; "Worldwide Benefit & Employment Guidelines – France."

EUROPE

GERMANY

What is the approximate size of the market and structure of the system?

In Germany, the funded pension market is €308 billion.[1] It is a single-tier public pension with an earnings-related PAYGO structure. Workplace plans are DB, some hybrid, no developed DC. Fully half of funded pensions are "balance-sheet" pension plans. Individual private "Riester" savings funds are also available.

How are contributions handled?

There are three pillars of the German system:

1. State PAYGO: Obligatory pay-as-you-go system. Contribution rate 18.7%, split equally between employee and employer up to earnings cap of €72,600.[2]
2. Workplace Pensions: Employers may offer one of five supplementary voluntary pension plans: Book Reserves (offered by 52% of employers); "Pesionskasse," an insurance-based vehicle, (24%); Direct Insurance (11%); Support Fund (7%); and Pension Fund (5%). The Rürup pension is a state-subsidized pension scheme aimed primarily at contingent and part-time workers not enrolled in the main pension insurance scheme. The scheme can be funded with a workplace savings plan, but distribution is only possible as a pension payout – assets cannot be transferred or inherited.[3]
3. 3. Personal Pensions: "Riester plans" are individual pension plans composed of annuities, endowments, insurance, investment fund savings plans, and bank savings plans.

What does the investment structure look like for participants? What is a typical default?

In January 2018, Germany finalized its Betriebsrentenstärkungsgesetz (BRSG), the "law for strengthening occupational pensions." It created private pension savings plans provided by banks, insurers, and investment funds ("Riester" pensions). With BRSG, the German government is trying to expand pillar II, the workplace savings plans, particularly among smaller companies. Certain industries with collective-bargaining agreements ("Tarifverträge") will be able to set up pension vehicles with variable, non-guaranteed payouts (a first for Germany). Upon retirement, some of the accrued capital is paid from a drawdown plan. These new second- pillar plans would offer automatic enrollment with an opt-out (another first for Germany). The plans have not seen robust take-up and are hotly debated as Germany struggles to re-invent private pensions. There is limited structure regarding what investment options for participants will look like.

What do recordkeeping, fees, and competitive market structure look like?

Several German companies, particularly large ones, maintain a voluntary pension plan fully or partially sponsored by the company. Approximately 40% of all employees in Germany benefit from company pension plans. As the DC market is in its infancy, the recordkeeping market is not yet robust.

Income is becoming increasingly important to DC schemes. How does Germany handle income?

Most of Germany's benefits are fixed. In general, the German Social Security and other state benefits provide 52% of retirement income, individual plans provide 31%, and employers provide 15%.[4] Individual and employer income comes from guaranteed income investment products such as annuities.

Are there relevant tax considerations?

The taxation of retirement is shifting from a tax-tax-exempt (TTE) system (contributions are post-tax, investment returns are taxed, and withdrawals are exempt) to an exempt-exempt-tax (EET) treatment (contributions and returns are exempt from taxes, and withdrawals are taxed).[5]

[1] OECD Pensions at a Glance 2019

[2] Ernst & Young Global Pension Study, 2015

[3] https://www.bvi.de/en/about-funds/savings-and-provision-for-retirement/ruerup-pension/

[4] Aegon Global Retirement Readiness Report

[5] OECD Pensions at a Glance 2019: Country Profile – Germany

EUROPE

THE NETHERLANDS

What is the approximate size of the market and structure of the system?

The Dutch pension market is significant at €1.9 trillion as of the end of 2020 and comprises most of the pension system in the Netherlands. The current split between DB and DC assets is at 94%/6% of the total market.[1]

The Dutch pension system is undergoing significant change. The current pension system is scheduled to convert in 2026 to a hybrid DC pension scheme, known as the Collective Defined Contribution (CDC) pension schemes. The pension amount is based on salary and service years, similar to a DB scheme. However, the contribution is fixed for a large number of years. If it turns out that contributions were not sufficient to pay the promised pension, the pension benefit will be lower than originally intended. CDC schemes combine a limited risk of fluctuating pension liabilities for the employer with the advantages of a collective pension system. There will be two kinds of contracts introduced, one of them is called a contract of solidarity. This means that people are divided into age cohorts and their investments made collectively. There is some risk sharing per cohort, as a maximum of 10% of contributions go to a rainy-day fund to compensate cohorts with “too low” returns. This change ultimately will create a meaningful shift in the composition of assets invested in both the DB and DC landscape.

How are contributions handled?

DC plans have a contribution rate that escalates over time. However, it is expected to change to a flat-rate system. The benefits are almost always paid from employee and employer contributions. The percentages depend on what is agreed to by the unions or employer/employee, and are expected to vary.

It is still to be determined whether contributions will be mandatory or voluntary going forward.

What does the investment structure look like for participants? What is a typical default?

There is much work to be done on the future investment structure of defined contribution plans. The Netherlands has a very mature DB market with a significant allocation to long-duration fixed income strategies and other liability-driven investing (LDI) exposures. As plans move from DB to DC, the primary investment will likely be a lifecycle-like strategy with a diversified toolkit for investment. But a default investment has not yet been identified.

What do recordkeeping, fees, and competitive market structure look like?

As the market shifts from DB to DC, a significant evolution will occur in terms of the values of participant balances, which will convert from an actuarial value to a DC balance.

Work remains to determine what the recordkeeping and competitive market structure will look like by 2026.

Income is becoming increasingly important to DC schemes. How does the Netherlands handle income?

The retirement structure of the Netherlands is currently set up across three pillars:

1. General Old Age or Algemene Ouderdomswet (AOW): This is a basic state pension system. The state pension age is 65, increasing to 67 by 2025.
2. Occupational pension plans (often CDC schemes): Industrywide pension schemes (e.g., PGGM), company schemes, and insurance contracts. There is no national statutory obligation to offer a pension scheme, generally because of industry cohort agreements. Approximately 91% of employees are covered by this type of plan.
3. Individual savings schemes

Pension schemes in the Netherlands have gained international interest as a way of sharing risks among members of the plan. However, like most countries, the Dutch system has experienced increasing pressures since the financial crisis. The government, in conjunction with unions and industry groups, agreed on a new “Pension Accord,” which will see a conversion to CDC by 2026. As the plans begin to transition from the DB to DC system, the level of benefits paid to a participant would no longer be fixed but would vary based on market conditions and demographics. It remains to be seen what type of investment strategies will evolve for decumulation.

Are there relevant tax considerations?

Pension funds in the Netherlands are subject to the “Exempt Exempt Taxed” (EET) regime, where a beneficiary’s contributions and a fund’s return on the investments (including income and capital gains) are exempt while withdrawals are subject to taxation (or partial exemption), based on OECD data.

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[1] https://www.bnymellon.com/content/dam/bnymellon/documents/pdf/aerial-view/the-changing-face-of-dutch-pensions.pdf.coredownload.pdf

Source used generally: https://www.wtwco.com/en-US/Insights/2020/06/netherlands-sweeping-pension-reforms-further-details-released

EUROPE

UNITED KINGDOM

What is the approximate size of the market and structure of the system?

The UK DC market is approximately £500 billion. The National Employment Savings Trust (NEST) program, which began in 2012, totaled £9.5 billion as of March 31, 2020.[1] The NEST program's Master Trust is the plan structure growing most rapidly. The market is growing at about 10% per year, as the vast majority of the UK working population now pays into DC schemes.

How are contributions handled?

Regulations mandate auto enrollment for anyone over age 20, employed, and making more than £10,000 per year. Workers can opt out, but few do. The minimum mandatory contribution into DC pension schemes was increased in phases. Mandatory contribution rates beginning in 2019 are 8% (3% individual, 5% company).

What does the investment structure look like for participants? What is a typical default?

Defaults are mostly passive (for cost and scalability). For active managers, the Diversified Growth Funds are the primary vehicle to position products. A critical aspect of UK plans is that DC default schemes cannot charge more than 75 bps (basis points), including investment, administrative, and platform costs. This cap does not apply to members who "self-select" funds to invest in. Legislation is being considered to include transaction costs within the charge cap, which would make the market even more difficult for active management solutions. Assets in NEST, as of March 31, 2020, were allocated 49% to equities, 23% to investment grade bonds, 13% to non-investment grade bonds, 9% to property, 3% to short-term reserves, and 3% to commodities.[2]

What do recordkeeping, fees, and competitive market structure look like?

Recordkeepers are largely insurance companies. L&G, Aegon, Scottish Widows, Aviva, and Phoenix Group are among the major players. Schemes must have fees no greater than 75 bps, including administrative, investment, and platform costs.

Income is becoming increasingly important to DC schemes. How does the UK handle income?

In the past, all retirement assets were annuities. Following the Pension Schemes Act in 2015, annuities are no longer mandated post retirement. Life companies have broadened their retirement offerings, which range from annuities (for those wanting a guaranteed income) to fund propositions (where the risk is with the policy holder). Some schemes are looking to offer "through-retirement" products that cater to members post-retirement. Post-retirement costs are not covered by the charge cap (75 bps) and are therefore high relative to company default schemes. Most post-retirement solutions also carry high advisor fees (calculated as a percentage of total assets).

Are there relevant tax considerations?

The UK tax rules regarding pension contributions changed on April 6, 2020. The annual allowance of £40,000 (the most a member can save in their pension pots in a tax year) will now apply to individuals with an adjusted income of up to £240,000. Therefore, the amount of pension contributions that higher earners can receive tax relief on was reduced from £10,000 to £4,000 per annum. Those who exceed their annual allowance are taxed at the point of contribution and when the pension is drawn.

The lifetime allowance (allowable accumulated balance) for an individual was £1,073,100 in the tax year 2020-21. Amounts above that are subject to tax. It applies to all pensions a person has, including pensions promised through any defined benefit schemes but excluding state pensions.[3]

[1,2] https://www.nestinsight.org.uk/wp-content/uploads/2021/02/Retirement-saving-in-the-UK-2020.pdf

[3] https://www.nestpensions.org.uk/schemeweb/nest.html

Source used generally: UK background on the defined contribution market provided by industry experts in the London office of Wellington Management Company.

ASIA PACIFIC

AUSTRALIA

What is the approximate size of the market and structure of the system?

There was AU$3.3 trillion in the Superannuation system as of September 2022.[1]

Australia has a three-pillar structure:

1. 95% of assets are in the DC superannuation system.
2. The Age Pension is the Australian equivalent of Social Security. It is means tested, and the benefits are relatively small.
3. DB plans make up the third pillar, and they are small and mostly frozen.

There are about 500 superannuation funds ("supers") but the top 10 hold more than 25% of the system's assets.[2] Participants can choose their own super, but each employer must select a default because contributions are compulsory. Participants can have accounts in more than one super at a time.

How are contributions handled?

Contributions have been compulsory since 1992. Employers currently must pay at least 10.5% of a worker's gross salary into a super account. Mandatory contributions escalate over time as increases are approved by the government. Elective contributions are allowed but not common. Before tax contributions are capped at AU$27,500. After-tax contributions are capped at AU$110,000.

What does the investment structure look like for participants? What is a typical default?

Investment menus tend to be broad and typically include lifestyle funds, balanced or target-risk options, and single-asset-class funds. A balanced or lifestyle fund is a common default investment. These options tend to be managed by the superannuation fund and are broadly diversified. They tend to have sophisticated managers and include alternatives such as private real estate, infrastructure, hedge funds, and private equity.

Income is becoming increasingly important to DC schemes. How does Australia handle income?

As Australia does not have an IRA equivalent, participant assets stay in the account until withdrawn. Retirement income options are similar to systematic withdrawal accounts. Some are innovative, such as Australian Super's "account-based pension" option, which simplifies the setup of periodic withdrawals from specially designed investment funds.

Annuity-based options are offered by some supers but are not popular. A unique feature allowed in Australia is the ability to contribute while taking income payments (starting at age 55).

Are there relevant tax considerations?

In Australia, the term "before tax" is used, but it has a different meaning than in the United States. Contributions are taxed at a reduced rate of 15% (or 30% for annual income greater than $250,000 AUD).

Investment earnings during working years are taxed "in-plan" at a rate of 15%. If a retiree is receiving periodic withdrawals, taxes on the investment earnings are waived. Withdrawals are tax-free over age 60. Between ages 55 and 60, a member generally can withdraw up to AU$230,000 tax-free. Special COVID withdrawal rules in 2020 let participants take out AU$20,000 in two payments tax free to ease financial hardship (with self-assessment). The program was under scrutiny as withdrawal applications exceeded estimates and was closed on Dec. 31, 2020.[3]

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[1] ASFA, Association of Superannuation Funds of Australia

[2] Ibid.

[3] ARPA.gov.au

Sources used generally:
AustralianSuper: australiansuper.com;
Q Super: qsuper.qld.gov.au;
SunSuper: sunsuper.com.au;
University of Sydney

ASIA PACIFIC

HONG KONG

What is the approximate size of the market and structure of the system?

Hong Kong's Mandatory Provident Fund assets were HK$1.138 trillion (about US$145.8 billion) at the end of December 2020.[1]

How are contributions handled?

Almost all employees and employers must make contributions to the Mandatory Provident Fund (MPF) schemes. The mandatory contributions from employees and employers are 5% of compensation (HK$1,500 per month) each for those that make over HK$30,000/month. Mandatory employee contributions are considered tax-deductible up to HK$18,000 per year. Contributions above 5% are considered voluntary contributions. Under an amendment introduced in 2019, employees can receive tax deductions for voluntary contributions and qualified deferred annuity premiums up to HK$60,000 per year.

What does the investment structure look like for participants? What is a typical default?

Employees may allocate their contributions. There are up to 29 funds in the MPF schemes. The MPF Conservative Fund and Default Investment Strategy Fund (including the Core Accumulation Fund and the Age 65-Plus Fund) are required in each MPF. The Core Accumulation Fund and the Age 65-Plus Fund are the default for those who have not made an investment election.

What do recordkeeping, fees, and competitive market structure look like?

There are over 30 MPF schemes managed by 16 trustees. These providers have backgrounds in banking, insurance, and asset management and include companies such as HSBC, AIA, Principal, Sun Life, etc. According to Willis Towers Watson,[2] as of 12/31/2020, over 50% of the market is managed by three trustees: Manulife (25.65%), HSBC (18.81%), and Sun Life (10.85%). Fund fees vary, but the average across 487 funds was 1.45% as of Feb. 28, 2021.

Income is becoming increasingly important to DC schemes. How does Hong Kong handle income?

Before the Public Annuity Scheme was adopted in 2017, MPF members would receive a lump sum. The Public Annuity Scheme allowed members over the age of 65 to receive guaranteed monthly payments for life. The Inland Revenue and MPF Schemes Legislation Bill adopted in 2019 allowed tax deductions for qualified deferred annuity premiums and was designed to encourage voluntary savings. This bill resulted in many new annuity products being introduced.

Are there relevant tax considerations?

MPF mandatory contributions are tax-deductible. Contributions over 5% of salary are considered voluntary contributions. Voluntary contributions and qualified deferred annuity premiums are tax-deductible up to HD$60,000. Withdrawals are generally not allowed before retirement.

[1] https://www.mpfa.org.hk/en/info-centre/press-releases/202103003

[2] Willis Towers Watson: https://www.wtwco.com/en-HK/Insights/2021/01/mpf-market-share-as-at-december-31-2020

Sources used generally:
Mandatory Provident Fund Schemes Authority: mpfa.org.hk;
Colleague in Morningstar's Hong Kong office.

ASIA PACIFIC

JAPAN

What is the approximate size of the market and structure of the system?

There was JP¥12 trillion in corporate DC assets as of March 2019.[1] As a comparison, DB and DC total system assets were about JP¥200 trillion.[2]

Japan has a three-pillar system:

1. All citizens are covered by the National Pension (or basic pension), which is similar to Social Security.
2. Corporate and public-sector employees are also covered by mandatory Employees' Pension Insurance.
3. 3. The third layer consists of a mosaic of private DB and DC plans, plus a National Pension Fund (NPF) for self-employed individuals and non-working spouses.[3]

DC plans are positioned as supplemental to public pensions and employees' pension insurance.

DC plan administration is unbundled with a plan administrator (recordkeeper) and asset administrator serving as a custodian who acts independently but is bound by fiduciary laws.

How are contributions handled?

Contribution maximums are stated in yen per month and scaled according to whether the participant is eligible for a supplemental DB plan and/or an individual DC plan (similar to an IRA with higher limits). The maximum combined participant and employer contribution is JP¥660,000 per year (about US$6,250). The low limit restrains the value of DC plans as a benefit for higher-paid employees.

What does the investment structure look like for participants? What is a typical default?

DC assets in Japan are heavily weighted toward low-risk investments, with about 50% invested in bank deposits and general account insurance products.[3] The default investment option is at the sponsor's discretion, but bank deposit funds are almost universal since an employer is liable for default fund losses.

Income is becoming increasingly important to DC schemes. How does Japan handle income?

Eligibility for withdrawals works on a sliding scale (age 60-65) based on age and years of service. It is common to have three withdrawal options: 1) lump-sum payout, 2) periodic payments, or 3) a hybrid. If a participant does not make an election by age 70, a lump-sum withdrawal is processed as the default. More advanced retirement income options are yet to evolve.

Are there relevant tax considerations?

Participant and employer contributions are excluded from taxable income. Withdrawals are not allowed until after age 60. No taxes are imposed on investment gains. Lump-sum withdrawals and periodic payments have different tax treatments. For a lump sum, the longer a participant worked, the less they pay in taxes. Periodic payments are treated as regular income.

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[1] Pensions & Investments, September 2020

[2] OECD 2021

[3] Nomura Institute of Capital Markets Research

Sources used generally: Trust Companies Association of Japan;
Anshin Immigration & Social Security;
ICI Global

AMERICAS

CANADA

What is the approximate size of the market and structure of the system?

As of Dec. 31, 2020, DC plans account for approximately CA$114 billion in assets, representing about 5.7% of Canadian occupational pension assets.[1]

The retirement income system in Canada is a blend of mandatory and voluntary arrangements involving the government and unions, employers, and individuals. Ultimately, there are three pillars supporting retirement in Canada:

1. Government-sponsored retirement benefit plans
2. Employer-sponsored retirement plans
3. Individual savings plans

An employer may sponsor a retirement plan, such as a group Registered Retirement Savings Plan (RRSP) or a Registered Pension Plan (RPP). Under both of these plans, both the employee and employer or just the employer contribute money to the plan, depending on how it is set-up. At retirement, employees may be eligible to receive either a regular income from the plan or a lump sum of money that can be converted into an income.

How are contributions handled?

An RRSP is a government-assisted retirement savings vehicle offered by banks and insurance companies, where contributions, capital gains, and interest accrued inside the plan are tax-exempt until withdrawn. Workers can make annual contributions to an RRSP equal to 18% of their earned income, up to a stated limit and up to age 71, at which time the accumulated funds must be converted to an annuity or disbursed yearly according to a minimal withdrawal schedule. Contributions are handled similarly for an RRP.

What does the investment structure look like for participants? What is a typical default?

Target date funds have been increasingly included among the investment choices for member-directed defined contribution plans and have received some support from governments and regulators. "The federal Pension Benefits Standards Act of 1985 requires administrators of DC plans and defined benefit plans with additional voluntary contribution options to offer investment choices – including default investments – with varying degrees of risk and rates of return that would allow a reasonable and prudent person to create a portfolio of investments that is broadly suited to his/her needs. Where this standard is satisfied, the administrator will be viewed as fulfilling the statutory duty of prudence regarding the investment of plan assets."[2]

What do recordkeeping, fees and competitive market structure look like?

The large insurance-owned platforms dominate the recordkeeping business in Canada, with Manulife, Sunlife, and Canada Life representing the top three. These services generally are bundled with administration, communication, education, etc.

Income is becoming increasingly important to DC schemes. How does Canada handle income?

For employer-sponsored DC plans, the employee usually receives a payout of their account balance at retirement. The amount depends on how the plan is managed and how the investments perform. At retirement, the employee usually must choose where to put the money. The options include an annuity within a locked-in registered retirement savings plan or a locked-in registered retirement income fund.

Are there relevant tax considerations?

Tax treatment for accumulation phases is tax-exempt through deductions and tax credits. For the RRSP plans, individuals get a deduction on their income tax, depending on their income and the amount contributed. There is no tax on the money earned if it stays in the RRSP. The income-tax deduction for RRSP contributions is up to the RRSP deduction limit, which is typically 18% of earned income for the previous year (up to a maximum amount set by the Government of Canada).

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[1] https://www.oecd.org/daf/fin/private-pensions/Pension-Markets-in-Focus-2021.pdf

[2] https://www.osler.com/en/blogs/pensions/november-2019/target-date-funds- don-t-let-your-guard-down

Sources used generally:
2017 International Bank for Reconstruction and Development / The World Bank, "The Evolution of the Canadian Pension Model: Practical Lessons for Building World-class Pension Organizations";
OECD Private Pensions Outlook 2008: Pension Country Profile: Canada;
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OECD and G20 Indicators: Pensions at a Glance, 2019

AMERICAS

MEXICO

What is the approximate size of the market and structure of the system?

The mandatory defined contribution Retirement Savings System (SAR) is the main component of the Mexican pension system and is a fully funded system with individual accounts. All private-sector employees who entered the labor force on or after July 1, 1997, and most public-sector employees who entered the labor force on or after April 1, 2007, have an individual account in the SAR. The current size of the market is over MX$200 billion.

Mandatory contributions from employees, employers, and the government are deposited in the SAR individual accounts that are invested in pension funds known as the Specialized Retirement Fund Investment Companies (SIEFOREs) and managed by specialized private managers known as Retirement Fund Administrators (AFOREs).

For private employees, the total employee, employer, and government contributions to the retirement subaccount are 6.5% of salary, of which 1.125% is paid by the employee, 5.15% by the employer and 0.225% by the government. Contributions are based on the employee's basic salary, up to a ceiling of 25 times the minimum wage.

Public-sector employees must have an individual retirement account, which is funded by contributions from the employee and the employer (state departments and related bodies), plus the social quota paid by the federal government. The total employee and employer contribution to the retirement sub-account is 11.3% of salary, of which 6.125% is paid by the employee and 5.175% by the employer (state departments and related bodies).

There are also various types of voluntary contributions that can be made, including:

- Short-term voluntary contributions
- Additional contributions to individual retirement accounts
- Long-term voluntary contributions
- Contributions to special "savings for retirement" accounts

What does the investment structure look like for participants? What is a typical default?

AFOREs must have four basic SIEFOREs for investing the compulsory savings, and they may have additional SIEFOREs for voluntary contributions and occupational pension plans. Each basic SIEFORE has a specific investment regime that depends on the worker's age. This multi-fund system creates a lifecycle scheme. As beneficiaries age, their assets are invested in a more conservative investment structure, similar to a glide path on a target date fund. All workers may invest their resources in a more conservative fund than the default option.

Workers still have minimal choices in the multi-fund system. Despite increased diversification, Mexico's pension funds are still significantly concentrated in debt relative to other countries.

What do recordkeeping, fees, and competitive market structure look like?

AFOREs manage workers' retirement accounts. Workers can choose their AFORE and are free to switch between them once a year. More recently, fees charged by AFOREs in Mexico have declined materially. Current regulations require max total expense ratio (TER) of equity mutual funds to be 65 bps and fixed-income mutual funds to be 35 bps.

Income is becoming increasingly important to DC schemes. How does Mexico handle income?

When a worker fulfills the age and contribution weeks requirements, retirement benefits are determined based on the accumulated balances in individual retirement accounts managed by the AFOREs, plus any remaining balance in a separate sub-account.

Should the accumulated balances in a worker's retirement account be sufficient to finance a minimum pension level, the worker can choose between two pension modalities:

- Life annuity: The worker signs an irrevocable contract with the insurance company of his/her choice to buy an annuity. A life annuity only can be bought by workers with enough funds to obtain a pension equal to or higher than the guaranteed pension in effect.
- Programmed withdrawals: The worker's balance in the individual retirement account is still managed by the AFORE and therefore continues to obtain the returns of the corresponding SIEFORE. The AFORE pays the pension through monthly withdrawals from the individual account until its balance is depleted. The amount of the monthly payment is adjusted annually considering the life expectancy of the pensioner at the time of the recalculation and the balance in the individual account.

Are there relevant tax considerations?

In general, investment income is tax-exempt if it is invested. Members' contributions are taxed, while employers' contributions may be deducted from profits for tax purposes. Benefits are tax-exempt up to a ceiling set at nine times the annual minimum salary.

Sources used generally:
OECD Private Pensions Outlook 2008: Pension Country Profile: Mexico;
OECD Reviews of Pension Systems 2015: Mexico;
OECD and G20 Indicators: Pensions at a Glance, 2017