Key theme
Corporate (private) post employment benefits

Title
Consideration of the structures and techniques of risk sharing in cash balance pension plans

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Abstract[2]
When the Defined Benefit Corporate Pension Act was enacted in June 2001, Employees' Pension Funds and newly born Defined Benefit Corporate Pension Plans were permitted to design their benefits by Cash Balance Pension Plans (CBPs). The CBP defines the promised employee benefit by reference to a notional account balance (NAC). An employee's NAC is increased with periodic notional principal credits and notional fixed and/or variable interest credits. Upon resignation, usually with more than 3 years of service, the employee is entitled to the lump-sum amount of his/her NAC.

The interest credits are calculated based on the revaluation rate that has been chosen by the plan sponsor. In many cases, the interest rate of the government bond is used for the revaluation rate.

The reasons of this selection are considered as follows:
① The correlation between the interest rate of the government bond and the discount rate used in the calculation of the projected benefit obligation is high. Which results in the mitigation of the volatility of the projected benefit obligation.
② When the interest rate falls the benefits by CBPs will become small in comparison with the conventional defined benefit pension plans.

Although the benefits by CBPs change according to the yield curve, plan sponsors bear investment risks, which means they will bear additional burden when a significant drops in funding levels occur. In the current financial crisis, a decline in funding levels of pension plans is spreading, and CBPs are no exception.

In this paper, I review the structure of risk sharing by employers and employees in CBPs in my country, based on the current environment, and I also consider the sharing of the investment risks in order to maintain pension plans in good shape.