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Public Pensions and Intergenerational Equity

As Japan's birthrate declines and its population ages, the financial burden of the present public pension system on younger generations is becoming increasingly disproportionate to the pension benefits that these generations will actually receive. How should we approach this problem of intergenerational inequity? The arguments presented in this issue of the NIRA Policy Review propose that, considered by generations, the discrepancy between benefits and burdens should be largely the same, and, considered at the level of the individual, benefits and burdens should be in equilibrium; at the same time, it is indicated that fairness should be ensured in the social security system as a whole.

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Comprehensive Reform of Taxation and Social Security

The social security system may be considered the ultimate key to Japan's financial problems. The amount of the finances deployed by the system is enormous, and the burden placed on citizens by taxes and social insurance premiums is high. The shape of the social security system will also have a significant effect on the design of individual lives.

Based on this understanding, the Japanese government has embarked upon comprehensive reforms of the taxation and social security systems. The LDP, DPJ and New Komeito agreed on a Comprehensive Reform of Social Security and Tax, and set in place mechanisms to ensure that a change in administration would not result in major changes to the initiative in June, 2012. As the first step in the reforms, it was decided to increase the consumption tax rate. The government established a National Council on Social Security Reform, and pushed ahead with discussions concerning the social security system.

The experts interviewed for this issue of NIRA Policy Review, while advancing a variety of arguments, all support the comprehensive reform of the taxation and social security systems. However, the National Council on Social Security Reform is a provisional organization which will complete its term in August this year. We must be aware that the actual reform of the social security system will require an enormous amount of time. In this sense, we can say that discussion of integrated reform has only just begun.

Against this background, this issue of the NIRA Policy Review focuses on intergenerational equity in the social security system. The social security system has numerous facets, including pensions, medical care, nursing care, and support for child-raising, and the question of inequity also presents a number of greatly varying aspects. We therefore considered that restricting our focus to pensions would serve to clarify the discussion. In addition, with the period of the mass assumption of pension benefits by the first baby boom generation upon us, it is the pension system which demands the most urgent response.

Nevertheless, we recognize that it is only natural that the issues involved in the pension system are also related to the rest of the social security system, and also that there is considerable merit in taking up the social security system as a whole for consideration, rather than separating off pensions. These are points that are also

raised by our interviewees.

The key phrase of these interviews is “intergenerational equity.” Against the background of a declining birthrate and an aging population, the burden of payments to the public pension system against the benefits received from the system is becoming increasingly heavy for younger generations. A system which the majority of citizens feel is unfair is one with little sustainability. Intergenerational equity is therefore an important key in considering the long-term sustainability of the system.

Unfortunately, however, insufficient attention is given to intergenerational equity in government discussions of reform of the social security system. No doubt the government is expending its greatest efforts on the resolution of immediately pressing problems, and in addition presumably has the sense that bringing the question of intergenerational inequity to the table would confuse the issue.

Nevertheless, if our social security system is not one that makes “individuals of every generation feel that society is providing support for their lives,” the necessity for which Professor Sawako Shirahase points out in this issue, it will be difficult to ensure the sustainability of the public pension system. The problem of intergenerational equity is one that cannot be avoided.

Ways of Thinking about a Sense of Fairness

The current elderly generation is receiving a high level of pension benefits in return for a low burden of payment. However, as generations become younger, the ratio of burden against benefits becomes higher. Generations yet to be born will face an even heavier burden. The inadequacies of the present system pass the buck to later generations, and the disadvantage becomes greater the younger the generation. Preventing this intergenerational inequity from remaining unaddressed is the problem at issue.

However, understanding the issue in simple terms such as these gives us an extremely restricted range of choices in seeking its resolution. We could reduce the burden on younger generations at least slightly by making further cuts in the benefits enjoyed by the elderly. But given the fact that elderly citizens represent the overwhelming majority of voters, it would be extremely difficult to implement a reform of this type. ➤

➤ The most important message to be taken away from the interviews presented here is that the problem of intergenerational equity should not be oversimplified. We must discuss equity using a more diverse range of points of focus, rather than simply focusing on generations. What could these points of focus be? In this issue, Professor Takashi Oshio emphasizes the importance of income. A significant amount of Japan's elderly have high incomes and possess a considerable amount of assets. By thus incorporating intragenerational transfers of wealth into our thinking, we ease the difficult issue of intergenerational conflict at least a little. Indicating that because “The public pension system is a reserve based on the social security framework, prepared against a long-term future [...] [a]n overemphasis on intergenerational gain and loss in the system is undesirable,” Professor Shirahase goes on to inform us of the importance of intragenerational redistribution. Redistribution within the elderly generation would make it possible to reduce the burden on younger generations.

Professor Makoto Usami suggests that we should consider equity in terms of individuals. This argument presents similarities to those mentioned above, which urge us to train our focus on income. If we are to be thorough in our consideration of equity, it will be essential to expand our frame of reference on the issue by utilizing the perspective of the individual. On the other hand, though, distribution within the family also has an important meaning in the social system. As we can see, when we dig deeper into the question of equity, we discover a wide variety of points that require discussion.

Public Pensions within the Social Security System

Focusing discussion exclusively on the monetary exchange represented by public pensions restricts our range of choices. We must give consideration to the appropriate direction for the public pension system within the social security system as a whole. Professor Shirahase and Professor Taro Miyamoto also make this point. Eschewing our exclusive focus on cash benefits and broadening our perspective to encompass, in Professor Shirahase's words, “a social security system which transcends generations and focuses on the whole of life, providing benefits-in-kind such as education and child-minding services and medical treatment based on a perspective of life security,” we are able to consider a direction for the realization of equity. And while equity is an important factor in increasing the reliability of the system, what Professor Miyamoto identifies as an “exclusive emphasis on intergenerational equity in the pension system and lack of attention to justice in society as a whole” is clearly problematic. As Professor Miyamoto further indicates, it will also be important to deploy the nation's finances “within a total social security system that takes in employment, the family, and welfare, on the provision of support for employment and for the family among the currently working generations.” Rather than

discussing equity exclusively within the framework of the public pension system, we should give greater consideration to what the currently working generations actually want. It is essential for us to discuss intergenerational equity from a comprehensive perspective, one which incorporates the “concept of [the elderly] forgoing some of their benefits to enable them to be invested in later generations,” as Professor Izuru Makihara suggests.

Focusing discussion on public pensions highlights the serious issue of intergenerational equity in a readily understandable manner. By this means, a greater number of people are able to become aware of the existence of the problem. However, once we begin to think more deeply about the problem of equity, we can no longer be content to limit our discussions to public pensions. In addition, if we expand our range of choices from public pensions to take in the social security system and the employment and education systems, we will see our way towards reforms which will be supported by a greater number of citizens.

A social security system must be one which all the nation's citizens believe in and support. It is precisely because of this that equity is so important. However, we must not restrict ourselves to considering equity simply as a matter of the individual. As Professor Usami points out, it is necessary that we should aim towards a process in which the majority of the nation's citizens take part in discussions and reach a deliberative consensus. And as Professor Miyamoto indicates, it will be essential for us to broaden our perspective, as we discuss equity in the pension system, to encompass social justice. For Professor Miyamoto, social justice means “the guarantee of the conditions for social participation no matter what the generation.” The fact that the system imposes a burden on the working generations without providing them with essential support against a social background in which, as he points out, “the stability of employment is declining, and the formation of family units is also becoming unstable,” is a serious problem.

While indicating that equity is the essential point for a public pension system, Professor Miyamoto also warns that, in the case of Japan, “If we exclusively discuss the guarantee of equity in the public pension system, it is possible that financial resources will be directed towards this problem exclusively.” Professor Miyamoto means that in order to increase the ratio of support provided to younger generations within Japan's total expenditure on social security, it will be essential for us to think in terms of the social security system as a whole, or in terms of a broader framework encompassing support for employment and other measures. This suggestion can serve as a significant reference point for the orientation of future discussion of public pensions and intergenerational equity.

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Expert Opinions

How Do We Define Intergenerational Equity in the Public Pension System?

Intergenerational inequity in Japan's public pension system is increasing with the decline in the nation's birthrate and the aging of its population. The situation is the subject of discussion, but fundamental changes remain to be made. What would intergenerational equity in the public pension system mean? And how can we break through the present deadlock? We asked leading figures in the fields of economics, philosophy of law, political science and sociology for their opinions.

Interviewer: Manabu Shimasawa, NIRA Senior Researcher
Period of interviews: October-December, 2012

Promoting reform with “Generations” and “Income” as twin focal points

Takashi Oshio

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Ideally, in a public pension system, the difference between the total amount of the pension which one will receive and the total burden represented by insurance contributions and taxation payments over the course of one's lifetime should be roughly the same, no matter when one is born. In reality, however, there is inequity between generations, and there are significant differences in the discrepancy between benefits and burdens depending on one's generation. In the early phase of development of a system, a certain degree of inequity is unavoidable, but a system that one-sidedly places the yet-to-be-born members of future generations into a position of disadvantage is unacceptable. For a public pension system, intergenerational equity, unaffected by when one was born or one's degree of involvement in the political decision-making process, should be a fundamental principle of operation.

In order to correct intergenerational disparities, we need a mechanism by means of which the amount of pension benefits as a whole is automatically reduced in response to the level of pension premiums being paid by younger generations. It will be objected that this would increase the number of elderly low-income households; how do we guarantee their livelihoods? This will necessitate a mechanism which assists people who are experiencing income difficulties, no matter what their age, and which positions people who are not experiencing such difficulties on the side providing assistance, even if they are elderly. We must consider systemic reform with “generations” and “income” as twin focal points. ■

Fairness should be considered at the level of the individual

Makoto Usami

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I understand the key concept of a social system as being to ensure “fairness.” A specific social system is fair when the benefits and the burdens of that system in relation to each individual citizen are in a state of balance. It is important that we should consider this balance at the level of the individual. Because generations are an agglomeration of individuals, if we can ensure fairness at the level of the individual, we will also guarantee fairness between generations. Some believe that because the current elderly generation supported their parents and families and contributed to the era of high economic growth, the current state of intergenerational inequity does not represent an issue. However, given that not all individuals within the present elderly generation supported their parents and families, and that they also differed in the degree of their contribution to the economy, an argument which claims that they should be considered as a homogeneous group is rather unconvincing.

Today, as Japan's birthrate declines and its population ages, under our present pay-as-you-go system the burden on future generations is increasing, and intergenerational equity is increasingly declining. In this situation, fundamental reforms that take in the funded system or the tax-financed system are essential. It is difficult for the Japanese public to actively discuss this subject and promptly reach a rational consensus on the basis of adequate data and information, but expanding intergenerational inequity makes it a problem that cannot wait. Given this, the government should proceed, on its own initiative, with systemic reforms that it might assume would be supported by the type of consensus resulting from careful deliberation of the facts which would have been reached by public debate based on adequate information (“deliberative consensus”), and present the public with data enabling it to judge the necessity for those reforms. ■

Consideration that transcends generations

Izuru Makihara

Professor, School of Public Policy, Tohoku University

Political science understands the term “generation” in three ways. The first is as a group that shares a specific period (i.e., a cohort). Examples would be the interwar generation, or the baby boom generation. The second is in terms of family lineages: Grandparents, parents, children, grandchildren. The third is in terms of age group: young or elderly.

Until around the 1980s, when Japan's high economic growth was to some extent entering its decline, the Japanese tended to share a sense of compassion towards the generation which had suffered during the war period. Thus, we understood “generations” in terms of cohorts and family lineages, and the view that we should distribute the benefits of growth between generations was a compelling one. Today, however, as Japan's population ages and younger generations are exposed to changes in the economic status of the nation such as low growth, deflation and economic crisis, it is important for us to consider “generations” from the perspective of age. It is essential for the elderly to turn their thinking towards the concept of forgoing some of their benefits to enable them to be invested in later generations. Even if one was affluent in one's prime, it is necessary to have consideration for later generations given the change in the social situation since one's retirement.

In relation to this consideration that transcends generations, it will not be enough to simply increase the transparency of the system and appeal to reason. What we will need in order to take the final step are stories with which people can empathize. Communicating the empathetic message that the elderly are called upon to make a return to coming generations will be, of course, the role of those in the political arena. ■

Realizing justice in the social security system as a whole

Taro Miyamoto

Professor, Graduate School of Law, Hokkaido University

The essential point for a public pension system is that the amount that is contributed is returned to the contributor; the system is equitable when the mechanism that makes this happen is operated with a high degree of transparency.

I am perplexed, however, by recent discussions concerning pension reform, with their exclusive emphasis on intergenerational equity in the pension system and lack of attention to justice in society as a whole. I believe that not merely the realization of a balance between burden and benefits, but also the guarantee of the conditions for social participation no matter what the generation, is important as the very substance of justice. We should be focusing more carefully on the present situation, in which the stability of employment is declining, and the formation

of family units is also becoming unstable. What is most important for Japanese society at present is to achieve social justice by focusing finances, within a total social security system that takes in employment, the family, and welfare, on the provision of support for employment and for the family among the currently working generations. This would mean that Japanese society was preparing the conditions enabling the working generations to work, form families, and raise children.

If we exclusively discuss the guarantee of equity in the public pension system, it is possible that financial resources will be directed towards this problem exclusively, and will not be used to provide support for the working generations. I hope, therefore, that in addition to equity in the pension system, we will give consideration to the achievement of justice in the social security system as a whole. ■

Intragenerational redistribution should also be on the agenda

Sawako Shirahase

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When we discuss subjects such as inequity and unfairness, it is not only the situation in the present that is important, but also the outlook for the future. For example, the sense of unfairness in relation to public pensions is rooted in the individual's feeling of uncertainty in relation to their own benefit when they become elderly.

The public pension system is a reserve based on the social security framework, prepared against a long-term future containing a significant degree of uncertainty. An overemphasis on intergenerational gain and loss in the system is undesirable. It is therefore essential to ensure that individuals of every generation feel that society is providing support for their lives. The path that we may consider in order to do so is to reconsider the present system, which has been designed with a focus on age, and to appeal to the advantages of a social security system which transcends generations and focuses on the whole of life, providing benefits-in-kind such as education and child-minding services and medical treatment based on a perspective of life security.

The social and historical background differs depending on when one is born, and the nature and degree of risks also differs. We may therefore say that a certain degree of intergenerational inequity is built into the public pension system. Nevertheless, we should also be aware of the merits of mutual support throughout society as a whole. Why not, then, actively consider redistributive measures which enable us to respond not merely to intergenerational inequity between the young and the old, but also to inequity within the same generation? For example, we could attempt to correct our trajectory towards the realization of an intergenerational balance in which the burden is not placed exclusively on the young productive generations by actively incorporating wealthy elderly people in the system as providers of funding. ■

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Utilizing a network of scholars, researchers, and specialists in a wide range of subjects, NIRA works for the public benefit from a fair and neutral perspective, attempting to reinvigorate policy debate and contribute to the process of policy formation in Japan. The institute focuses on domestic social and economic policy, international relations, and regional issues in Japan as its principal areas of research.

Established in 1974 as a government-authorized independent research institution, NIRA became an incorporated foundation in 2007, and since February 2011 has been recognized as a Public Interest Incorporated Foundation.

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