# Retirement Pension Plan Reform

In the two years since fiscal year 2001, ITOCHU's consolidated net cost of retirement and severance benefits increased from ¥12.4 billion to ¥22.7 billion, heavily impacting ITOCHU's consolidated financial performance. As ITOCHU Corporation (non-consolidated basis) accounts for most of this, we decided to revise the retirement and severance plan for ITOCHU Corporation employees as follows.

ITOCHU Corporation's retirement and severance plan consists of two pension plans: an employee pension fund and a tax-qualified pension fund. As of the end of fiscal year 2003, projected benefit obligations (PBO) totaled approximately ¥290 billion, assets under management totaled approximately ¥160 billion, and pension trusts totaled approximately ¥130 billion. (Non-consolidated Japan Accounting Standard: Hereinafter all figures are based on non-consolidated Japan Accounting Standard.)

In order to cope with the deterioration in the fund operating environment and with changes such as the introduction of retirement benefit accounting, ITOCHU took steps to ensure the health of pension finances. These steps included the reduction of PBO by, in October 1999, lowering the defined interest rate for the future benefit payment (from 5.5% to 3.5%) and extending the guarantee period (from 15 to 20 years); in September 2000, the establishment of a pension trust in order to make a one-time amortization of the underfunding resulting from the introduction of retirement benefit accounting (¥45.8 billion of net projected benefit obligation (actuarial difference) caused by a change in accounting standard), and the additional contribution to pension trust.

Subsequently, however, due to the prolonged slump in the asset management environment, operated pension asset resulted in negative returns for three years in a row. Also, because of the lowered interest rate, ITOCHU changed the discount rate. In addition, the prices of the stocks in the trust fell. Thus, from fiscal year 2001 through fiscal year 2003, these factors resulted in a total unrecognized actuarial loss (unamortized obligation) of more than ¥200 billion. Judging that there should be limits to how long the retirement and severance plan could last in its existing scheme, given the harshness of the environment, we decided to make a fundamental review of the system.

In fiscal year 2000, we introduced a new human resources management system with remuneration packages based on job responsibility and performance. The retirement and severance plan, however, continued to be based on "years of employment" and "age." It remained a major issue to revise the plan into a more flexible system based on the principles of the new human resources management system.

From fiscal year 2002, in response to the increased number of options for retirement and severance plans by the expected enactment of a series of bills related to retirement and pension systems, ITOCHU began a full-fledged study for a revision of the plan.

The aim of this revision is to minimize the impact of the retirement and severance plan on our management by reducing PBO or lowering PBO risk. In terms of specific changes to the plan, we aim to develop a structure that incorporates the principles of the new human resources management system and respond to the diversification of employees' values.

Negotiations with the labor union on revision of the retirement and severance plan began in August 2002 and culminated in an agreement in March 2003. The agreement seeks to reduce the risk that has hitherto been entirely on the Company's shoulders by dividing it; a portion of the risk will return to the government, a portion will be carried by each employee, and the concept of "market linkage" will be introduced to the portion that the Company continues to bear. Specifics are as follows.

1. ***Returning the public pension portion held by the employee pension fund to the government:*** Returning the future portion has already been authorized and relevant records are being prepared for returning the current and past portions. Returning the public pension portion to the government will eliminate risk for approximately ¥37 billion worth of PBO (as of end of fiscal year 2003).
2. ***Revising the supplementary portion of the employee pension fund:*** When the past public benefit portion is returned to the government, we will introduce a "cash balance plan" that links benefit amounts to market interest rates. This will lower interest rate sensitivity and enable the lowering of asset management hurdles for about ¥190 billion worth of PBO (as of end of fiscal year 2003) for the supplementary portion of the employee pension fund, and thus will minimize the risk for the maintenance and operation of the plan. In addition, although benefits are currently paid entirely as perpetual annuities, we plan to make some portion terminable, expecting to reduce PBO and lower asset management risk.
3. ***Revising tax-qualified pension:*** After reducing the future portion of the tax-qualified pension, in July 2003 we will introduce an "optional defined contribution pension plan." This gives employees the option of receiving the Company's contribution through the "defined contribution pension" that employees manage on their own or as an addition to their monthly salary. The introduction of this new system will not bear PBO.

*Summary of ITOCHU Corporation's Retirement Pension Plan Revision*

| | Old Plan | New Plan |
|---|---|---|
| 1. Employee Pension Fund (Public Pension Portion) | Perpetual | Returned to government |
| 2. Employee Pension Fund (Supplementary Portion) | Perpetual annuity guaranteed for 20 years<br>Defined interest rate: 3.5% | Introduction of Cash Balance Plan<br>Some portion changed to be terminable |
| 3. Tax-Qualified Pension | Terminable annuity guaranteed for 20 years<br>Defined interest rate: 3.5% | Some portion changed to defined contribution pension |