Universal Social Protection

Universal old-age, disability and survivors pensions in

Ukraine

Region: Europe & Central Asia
Income level: Lower middle income

Population (2016):
42.59 million
Annual population growth (2016):
↘ - 0.4
Population above 65 years old (2016):
15. 9 %
Life expectancy for ♀/♂ (2015):
76/66 years old
HDI (2014):
0.74 [81/188]
Economically active population (2015):
18.1 million
GDP (WB/WDI, 2014):
131.8 billion US$
GDP growth (WB/WDI, 2014):
↘ - 6.8%
Real GDP per employed person (in 1990 US$)
10,757.00 (2013)
Average level of old age pensions in relation to GDP per capita (excl. mean-tested) (2007):
21.5 %
GNI per capita, PPP:
8 560 current int $
Minimum wage / substance minimum per month: 1074 hryvnia (2016)
Public social protection expenditure as a % of GDP: 24.6 **(2013)**
Public social protection expenditure on old age, disability and survivors as a % of GDP: 16 **(2013)**
Share of population above statutory pensionable age receiving an old age pension:
95%
Share of economically active population contributing to a pension scheme:
60.6 %
Share of unemployment population receiving regular periodic unemployment benefits:
73.7%
Average monthly earnings of employees (local currency): 2013
3,265.00
Employment-population ratio (%):2014
56.58
Urban population (WB/WDI, 2012):
69%

Sources:
World Bank/ World Development Indicator (WB/WDI)
United-Nations Development Programme/
Human Development Indicator (UNDP/HDI)
State Statistics Service of Ukraine

The pension coverage in Ukraine is universal, based on a mandatory/contributory system for employed and self-employed that includes old-age pensions, disability pensions, survivor's pensions, long service pensions and burial benefit. These social insurance mechanisms supplemented with social assistance are intended to cover all Ukrainian citizens.

As many of the former republics, Ukraine inherited from the USSR a social security system and has undergone enormous changes since its independence. Consecutive waves of reforms in 2003, 2010 and in 2014-2015 brought significant changes to the pension system, among which gradual increasing of retirement age, reduction of preferential pensions for special groups, introduction, then revision, of single social contribution and reduction of burden on employees and employers.

Social security system, including pension system is facing regular deficit. Undeclared and informal employment, wage arrears have notably been a regular problems that resulted in a lack in social security contribution based on wages. Since the independence and especially during last three years, poverty represents a crucial issue specifically due to low income level of population. The minimum wage and the subsistence minimum as a key policy parameters linked to pension level were frozen since 2014 thus reducing the pensions in real terms in the period of high inflation and economic downturn.

Moreover Ukraine is facing a very problematic pattern depopulation due to decreasing birth rate when 15.9% of the population is above the age of 65, 21% above the age of 60.

Main lessons learned

- Although Ukraine demonstrate the quasi-universal coverage of population based on its legal framework, the replacement rate is relatively low and small benefits are distributed to large part of population covering for pensions around 30 % of population. However, the effective coverage is lower due to the prevalence of the informal employment and undeclared work.
- The discussion is ongoing aiming to transform universal or categorical social benefits to means-tested benefits targeted to low-income families. However, more detailed analysis of the impact of these benefits on poverty reduction is necessary. The positive outcomes of introduction of targeted social assistance systems could be counterbalanced by negative features such as high administrative costs which can undermine the positive effect of more effective resources reallocation.
- The recent reforms in reduction of single social contribution was applied in order to reduce the informal employment and evasion of social security contributions. However the additional fiscal pressure on the State budget to cover the widening financial deficit could lead to additional cuts in benefit entitlements.
- Before considering the introduction of a mandatory funded pension tier, the Government and the social partners should examine the experiences of failure of similar reforms in countries in Central and Eastern Europe and in Latin America.
- In 2015, the Ukrainian Government initiated the process for ratifying the ILO Social Security (Minimum Standards) Convention, 1952 (No. 102), which was concluded on 16 March 2016, and initiated the process for signing the European Code of Social Security.

1. What does the system look like?

The reform of pension system is under way in Ukraine as part of its austerity measures under the influence of IMF. The main characteristics of this system, although rapidly changing today, are as follow:

The main risks covered by contributory pension system include old-age, disability, survivors. These risks are supplemented by long service pensions and burial benefit. ***Social insurance mechanism*** is mandatory for all residents, and stateless persons employed under labour agreements or under civil law agreements, including those who work abroad and self-employed persons. It covers the ***labour pensions*** for those cleared minimum qualifying period. Those who are not qualified to receive labour pension are receiving ***social pension (social assistance)***.

Some privilege-based pension schemes were widespread in Ukraine for specific categories of employees such as civil servants, legislators, judges, National Bank employees, diplomats, journalists, scientists, local governors, and victims of the Chernobyl disaster. However, since 2014 the reforms are under way in order to reduce the favorable provisions for these special groups and render their pension benefits in line with regular workers.

In addition, some other benefits can be taken into consideration such as the caregiver's allowance paid to an unpaid caregiver of a person older than age 80 in need of constant attendance; social services for lonely elderly persons etc. Furthermore, like all the citizens of Ukraine, the elderly can benefit from targeted mean-tested social assistance for low-income families. Furthermore, non-contributory social benefits, such as maternity benefit, child benefits to single mothers play a major role in poverty reduction in Ukraine.

Coverage

The legal coverage of the Ukrainian social security system is almost universal (up to 95% of population above statutory pensionable age receiving an old age pension). However, the effective coverage is lower due to the prevalence of the informal employment and undeclared work.

Old-age pension covers 60 years old men with at least 35 years of contribution history and 55 and six months years old women (women, gradually rising to age 60 up to 2021) with at least 30 years of contribution history. The period of contribution includes years spent in higher education, the armed services, caring for persons with disabilities or children younger than age 3, or being unemployed and seeking a job, if contributions are paid for these periods.

It is possible to get a ***partial pension*** for people who contributed during 15 to 34/29 years of coverage (for men/women).The pension is

paid to unemployed older workers from ages 58/54 and 6 months to 60/55 and 6 months (men/women) (depending on the date of birth, gradually rising to age 60 in 2021). The pension ceases if the beneficiary is reemployed.

All pensions are paid monthly through bank and post offices. The pensions are payable abroad for six months in advance, beginning the month the pensioner leaves the country; thereafter, only if there is a reciprocal agreement.

Table 1 shows that between 2013 and 2016 the number of beneficiaries of pension schemes is reducing, but still remains around 29 % of overall population of the country. At the same time, the share of pensioners receiving the benefit equal or below minimum pension is increasing from 2.4 % in 2013 up to 7.7% in 2016. This is worsened by the high inflation and frozen indexation of pension benefits since 2014.

Table 1: Distribution of pensions, 2013-2016 (As of 1 January of each year)
Sources: ILO (2016)

	2013		2014		2015		2016	
	Share	Average pension (UAH)	Share	Average pension (UAH)	Share	Average pension (UAH)	Share	Average pension (UAH)
Below the minimum pension	1.0%	583	0.9%	587	0.8%	582	5.3%	932
Equal to the minimum pension	1.4%	894	3.1%	949	4.6%	949	2.4%	1,074
Above the minimum pension	97.6%	1,488	96.0%	1,554	94.6%	1,621	92.3%	1,761
Minimum pension (UAH/month)	894		949		949		1,074	
Total number of pensioners (persons)	13,639,739		13,533,308		12,147,189		12,312,459	

Benefits

The ***labour pension*** in Ukraine is calculated using following formula:

Monthly Pension (in UAH) = AS x cW x cQ

AS - Average salary in the Ukrainian economy during three years before retirement
cW – coefficient of wage of retiring person compared to average salary in the Ukrainian economy
cQ – coefficient of qualifying period (every working year can bring 1,35% of replacement income, with maximum of 75 %)

> Due to the high inflation during 2014 and 2015 and the freeze of the subsistence minimum levels during 2014, the average subsistence minimum has lost nearly 40 percent of its value in real terms up to 2016. Indexation of pensions was also frozen. The approved 2016 State budget takes into account the planned increases in the subsistence minimum level for May and December 2016.

These labour pensions covering old-age, disability and survivor social risks are subject to minimum and maximum amounts. The Constitution of Ukraine (Article 46) and the Law on State Social Standards and Social Guarantees stipulate that the minimum wage and pensions and other social benefits must not be lower than the subsistence minimum established by law. Thus, ***minimum pension*** is related to minimum subsistence level for the persons who are incapable of work (elderly, peoples with disabilities). This minimum subsistence level (together with other minimum subsistence levels for children and able-bodied population) should be reconsidered every year based on basket of selected commodities and services. The ***maximum pension*** is 10 times the minimum pension.

Social pensions are paid to different vulnerable groups of population aged 63/59 (men/women, gradually rising to age 63 in 2021) who are not working and ineligible for an old-age pension. The amount of these social pensions is related to minimum subsistence level for the persons who are incapable of work. Social pension for old age varies from 30% to 100% of this minimum subsistence level. If the social pension is less than the minimum subsistence level for the persons who are incapable of work (1074 UAH /month in the beginning of 2016), old people can get a social pension supplement to fill the gap.

To encourage older workers to remain in the workforce, the old-age pension is increased for workers by 0.5% for every additional month of coverage if the pension is deferred up to 60 months after normal retirement age; 0.75% for every additional month of coverage for more than 60 months.

According to current rules, the replacement rate is set at 45-50 % of the average individual wage for the best five or last two years for men and women (having accomplished the required length of service), with 1 percent increase for each year of additional work up to a maximum of 75 percent of the average individual wage.

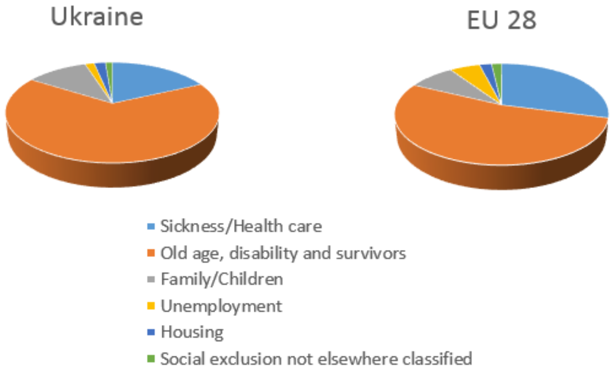
Financing

According to ESSPROS methodology[1], the total social security expenditure of Ukraine in 2013 was estimated at 24.6 % of GDP which is higher than in any of the new EU countries neighbouring Ukraine. However, this indicator

[1] European Integrated System of Social Protection Statistics developed by EUROSTAT and applied by the State Statistics Service of Ukraine

is close to the average in EU 28 (28.6% of GDP). Expenditure on old-age, disability and survivors' benefits dominate the Ukrainian social security expenditure with 16 % of GDP, or nearly two-thirds of the total. This rate is seriously higher than in EU 28.

Chart 1: Social security expenditure by type, Ukraine and EU 28 (2013)



Drastic changes were introduced in 2016 in social protection financing mechanisms. ***Single social contribution*** which represents a consolidated contribution rate to finance all social insurance schemes in Ukraine was significantly reduced. After its introduction in 2011, employers' contribution rate was between 36.76 % and 49.7 %, depending on the assessed risk of occupational accident and disease, while employees' contribution rate was 3.6 %. In 2016, the single social contribution rate for employers was reduced to 22 %, and the contribution from workers was abolished (see Table 2).

Table 2: Changes in single social contribution rates in 2016

Categories	2011-2015	2016
Employers	36.76% to 49.7%,	22%
Entrepreneurs working on civil contracts and self-employed persons	34.7%	22%
Budgetary institutions	36.3%	22%
Employees	3.6%	0%
Physical persons working under civil contracts	2.6%	0%
Civil servants	6.1%	0%

Sources: ILO (2016)

This measure was introduced based on the hypothesis that the reduced contribution rate would reduce the incentive of social security contribution evasion, widen the tax base and results in positive fiscal effects. However, preliminary observations show that the total contribution revenue will decrease, specifically affecting the pension system through the significantly reduced allocation rate.

Pensions and benefits were tax exempt in Ukraine up to 2015. Since then, pensions above certain thresholds are taxed. Income from old-age pensions between three and ten times the minimum wage is subject to a 15 percent personal income tax and a 1.5 percent military duties tax.

Institutional arrangements

Ministry of Social Policy (http://www.mlsp.gov.ua) is responsible for policy and provides general coordination. Regional and local social protection departments administer the program.

The Pension Fund manages/administers autonomously the pension scheme/pensions. (http://www.pfu.gov.ua/pfu/control/uk/index).

2. How was this achieved?

During the soviet era the full employment and pay-as-you go system guaranteed a quasi-full coverage of population for three main risks: old-age, disability and survivors. After the transition to market economy the important challenge was to integrate the population of informal sector and self-employed persons as well as combating informal employment.

The Constitution of 1996 as well as specific laws on social security benefits have established the right to social security in Ukraine. Three major waves of reforms were implemented in 2003 (tentative for introduction of multi-pillar system), in 2011 (gradual increasing of retirement age) and in 2014-2015 (reduction of single social contribution rate and reduction of preferential pensions for special groups).

A reform conducted in ***2003*** with the adoption of the Law of Ukraine "On mandatory State Pension Insurance" was intended to rebuild the Ukrainian pension system. This law created a ***legal framework for multi-pillar system***, including:

- a modified pay-as-you-go (PAYG) program;
- a mandatory state pension insurance (or mandatory individual accounts) = second-pillar with a contribution of employees;
- voluntary individual accounts = third-pillar ('Non-State Pension Provision') based on a tax relief (15 % of the gross yearly wage).

However, the ***real implementation of that new system has been postponed indefinitely*** due to lake of support from population and social partners.

The second wave of reforms started in ***2011*** by ***increase of the retirement age for women from 55 to 60 years by 2021***. This measure equalised the retirement age for men and women. The reform also increased the contribution period required for the partial pension from 10 to 15 years for both sexes and increased the number of contribution years required to receive a full pension (to 35 years for men and 30 years for women). A ***maximum pension*** equaling ten times the minimum pension has been introduced for newly-granted pensions. Furthermore, since 2011, **single social contribution** (a consolidated contribution rate) has been collected to finance all social insurance benefits in Ukraine.

The reform measures implemented in 2014 and 2015 were axed on the reduction of favourable provisions for special groups. Furthermore, the reduction of pension benefit was introduced for all the other groups of working pensioners who receive pensions higher than 150 percent of the subsistence minimum for pensioners. In 2016, the single social contribution rate for employers was reduced to 22 percent, and the contribution from workers was abolished.

In 2015, the Ukrainian Government initiated the process for ratifying the ***ILO Social Security (Minimum Standards) Convention, 1952 (No. 102)***, which was concluded on 16 March 2016, and initiated the process for signing the European Code of Social Security.

3. What are the main results in terms of impact on people's lives?

Although the majority of population is covered by the pension schemes, the level of replacement payment remains rather low. This low level of pensions can be explained by the widespread declaration of workers on minimum wage in order to reduce the social protection contributions and taxes. This situation is resulted in the replacement only for officially declared wage and the low level of pensions.

The numerous pension reforms were unpopular because the Government has failed to organize a genuine dialogue with population involving social partners. However the level of deficit of the Pension Fund was important and the efforts for gaining an equilibrium were necessary.

Another problem represents the direct energy subsidies. The households, and especially those composed of the elderly peoples were granted with subsidized prices for these commodities. The government has carried out the reform of energy subsidies under the pressure of IMF because these subsidies have concerned not only vulnerable layers of population, but the industry as well. The reform of 2016 has unified household and commercial natural gas tariffs. Although there is no evidence based research yet, the impact of this reform on the wealth of elderly population seems to be important.

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