

Universal Social Protection

Universal pensions in Azerbaijan



Universal coverage for old-age, disability and survivors: one step further to achieving social protection for all

Social protection has been one of the leading priorities of the Azerbaijan Republic for the past years. The pension system is representative of the country's ability to develop and implement universal coverage taking into account a large number of self-employed worker (almost 1 million), and an important informal economy.

Historically, Azerbaijan has inherited a universal soviet pension system which was underfinanced during first years of independence. The situation was characterised by political and economic turmoil of the early 1990s, as well as and large number of Internally Displaced Persons as a consequence of armed conflicts.

In 2001 the government has started a major pension reform for three main social risks: old-age, disability and survivors. The country rapid economic achievements were partially reinvested in social protection, which helped considerably reducing poverty and vulnerability.

Indeed, social protection floors helped mitigating the impact of economic crises, due to the country's heavy reliance on oil. However, recent downturn in oil prices and rapid devaluation of national currency in 2015 had an important impact on the real pensions' level.

Main lessons learned

- Azerbaijan illustrates how a former soviet republic can progress towards universal pension coverage, integrating important coverage constrains. Strong political commitment is key to develop an efficient system and to further reform it.
- Azerbaijan has demonstrated its willingness for reinvesting economic growth in social protection and generating higher benefits rates, progressively bringing them towards minimum subsistence revenues.
- The system was built to be highly adaptable to the ever-changing socio-economic structure of the country, and to cope with possible economic

shocks. However, only partial indexation of pensions after the currency devaluation and high inflation in 2015 did not allow to cover the consequences of economic crises for the beneficiaries of pension schemes in Azerbaijan. In this regards, more efforts are necessary in order to ensure benefit adequacy.

- A multi-tier system guarantees a variety of resources and important dexterity of the system. However, the introduction of third pillar in the situation of economic turmoil on national and on regional financial markets can represent some difficulties.
- The wide coverage of the personal accounting system, based on a unique insurance-pension system, was facilitated by the introduction of a card system for payments.



1. What does the system look like?

Azerbaijan's social protection system is under the responsibility of the **Ministry of Labour and Social Protection of the Population (MLSPP)**. Since March 2016, the **State Social Protection Fund (SSPF)** was integrated in the structure of the MLSPP. Before, the SSPF had an independent structure and carried out important pension reforms in the social security branches.

The universal coverage in Azerbaijan is achieved for three major social risks:

- Old-age
- Disability
- Survivors

This universality is reached by combination of **labour pensions** (social security part) for those cleared minimum qualifying period, and **social allowances** for those who are not qualified to receive labour pension for three aforementioned risks (social assistance part).

Although since 2006 the labour pension system is based on a 3-pillars structure (basic pension + insurance part + voluntary savings), the third pillar was not really implemented.

A personal accounting system has been established in the mandatory state social insurance area, which enabled the provision of pensions and the transition to insurance principles. This was followed by the implementation of a card system in order to facilitate payments.

Coverage

At present there are 1.3 million beneficiaries of different labour pension schemes in the country (including old age, disability and survivor). It is necessary to add to this figure 0.2 million persons covered by social allowances for the same risks paid through MLSPP¹:

	labour pensions	social allowances
Old-age	781 238	13 833
Disability	374 466	139 041
Survivors	144 242	41 286
Total	1 299 946	194 160

Sources: State Statistical Committee of Azerbaijan. Data on 01/01/2016

Officially, the coverage is universal because the entitlement is automatic (either on labour pension or on social allowance). However, some problems with coverage were observed in the past, especially related with official recognition of disability and thus entitlement of disability benefits.

In 2015, 3.09 million personal accounts were registered for social insurance part. However, an important layer of economically active population is registered as self-employed people, representing around 22 % of the employed population.

Benefit packages

At least 12 years of covered employment is required to be entitled to a labour pension. Since 1 January 2010, the retirement age is 63 for men and 60 for women, with possibilities of early retirement. Those not eligible for a labour pension are entitled to social pensions at the age of 67 for men and 62 for women.

The labour pension is calculated as the sum of three components: 1) a basic flat-rate benefit (110 AZN since February 2016) fixed directly by order the government, 2) insured part revised each year, based on the consumer price index and fixed by the formula $SH=PSK/T$ where, SH-amount of insured part, PSK- pension capital recorded in the insurance part of the personal account of the insured from 1 January 2006 on the date of granting old-age labour pension plus pension capital for the mandatory social contribution years of insured person for the period of prior 2006, T- number of months (144 months according to legislation) of the expected pension payment period and 3) voluntary funded element.

The basic flat-rate pension as well as minimum pension are fixed in relation minimum wage in Azerbaijan which is 105 AZN since February 2016. The amount of these minimum standards have progressed during last years in order to reach progressively the subsistence minimum for the persons who are incapable of work, which is 115 AZN in 2016. This subsistence minimum for different categories of population is reconsidered every year based on basket of selected commodities and services.

The average labour pension amount per month is 177.6 AZN in the beginning of 2016 (whereas average old-age pension of 197.6 AZN). The social

¹ The MLSPP is paying other social allowances, but they are not making part of this note because they don't illustrate the universal approach.

allowances are fixed as follows: 66 AZN for old-age and disability, 61 AZN for survivors).

The pension adequacy represent an issue because the average replacement rate represents between 38% and 45 % compared to official salary. At the same time, the studies show the positive impact of universal pensions on the absolute poverty rate.

Financing

In 2014, 1,743,743.240 million AZN of social contributions were collected by SSPF. They were distributed as follows:

- Public entities (employers and employees): 36%
- Self-employed: 2%
- Other employers: 62%

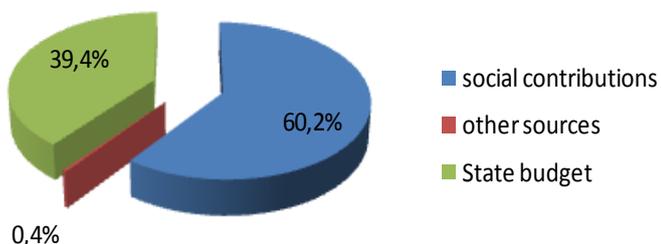
Employees pay 3% of their monthly gross income to the MLSPP, **employers** 22%. They are in charge of transferring the entire contribution to the MLSPP at the same time than the salary. In the end, half of the contribution will go on the employee’s personal account.

Self-employed persons: 10 to 50% of the national monthly minimum wage (105 AZN in 2016). Different rates apply depending on the sectors and regions.

Land owners must contribute with rates depending of the land category. The rate per capita and per hectare, is 2% to 12% of the minimum wage.

Other categories: Civil servants, military, prosecutors, etc. have a special compulsory contribution.

The sources of financing of insurance part of pension system are following:



State budget is covering the liabilities related to labour pensions acquired before 1992. Furthermore, the social allowances are paid by state budget through the MLSPP.

Legal aspects

18 February 1997 – **Law “On Social Insurance” № 250-IQ**, which determines the legal, economic and organisational aspects of the social insurance.

27 November 2001 – **Law “On Personal Accounts in the State Social Insurance System” № 221-IIQ**, which regulates the data collection in the personal individual accounts for the provision of social security rights in the future.

7 February 2006 – **Law “On Labour Pensions” № 54-IIIQ**, which introduced the labour pension rights of citizens, rules for the implementation and establishes a pension provision system.

2 July 2013 – **Law “On regulation of the checks which are carried out to areas of entrepreneurship, and protection of the rights of entrepreneurs”, № 714-IVQ**, which regulates the firms audit by the government. It determines the rights and the obligations of the inspection bodies and entrepreneurs.

2. How was this achieved?

Historically, Azerbaijan has inherited universal soviet pension system which was critically underfinanced during first years of independence. Although the State Social Protection Fund was established in 1991, the basic information for management of pension system was missing: employment records and employment periods, income levels for workers who used to live in other Soviet republics. Furthermore, the situation was worsened by socio-political and economical cataclysms of the early 1990s and large number of Internally Displaced Persons.

Starting from the beginning of 2000s, the country’s economic positive results set conditions for improvement in the socially oriented policy of the State. The social protection become a development priority of the government and the provisions are made in order to bring extremely low but universal social benefits close to subsistence minimums.

In 2001, with support of international organisations, the government adopted a 3-tier pension system reform concept, including a reinforcement of basic pay-as-you-go component, an additional mandatory insurance part, and a third voluntary scheme.

The second pillar was actually implemented in 2006 with introduction of individual accounts. The works on implementation of third pillar were under way during last years, however present economic situation represent a serious obstacle for such development.

Furthermore, up to 2006 Azerbaijan had universal child benefits coverage. However, these allowances (extremely low at that period) were transformed into Targeted Social Assistance (safety net mechanism).

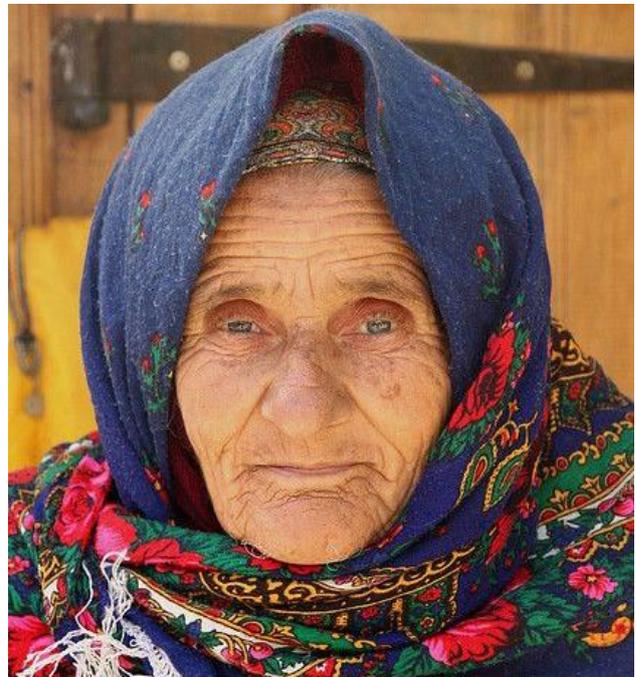
Last reform has brought the State Social Protection Fund (SSPF) under the responsibility of the Ministry of Labour and Social Protection of the Population (MLSPP) in March 2016. This reform is intended to render more comprehensive the pensions system through better coordination between labour pensions and social allowances for the same categories of peoples. Furthermore, the government expects a reduction of administrative costs for the management of social protection system in the period of deficit of budgetary resources.

The insurance and pension reforms led to the creation of a system including functions related to social insurance, personal accounting and pension provision. The following documents contain guidelines for future reform and improvements:

a) Development Concept “Azerbaijan – 2020: The vision of the future” Article 7.3 sets the main goals of pension system, including voluntary social insurance and non-state pension funds.

b) State Programme on Development of the Insurance-Pension System in 2009-2015, was approved by a Presidential Order in 2008. It aims at developing a viable system and ensuring its continuous improvement, and to guarantee a proper pension provision.

c) Concept on the Pension Provision System Reform in 2014-2020 was approved by the Order of the President of the Republic of Azerbaijan on 4 November 2014 No.827. It offers recommendations based on international best practices and experiences, in order to establish a robust pension system and provision in the long run.



Overcoming constraints

The benefits adequacy in the social protection system in Azerbaijan represents an important issue. Although the government has demonstrated important efforts to bring the social protection benefits closer to the level of minimum subsistence standards of population between 2000 and 2015, the last developments in the economy of Azerbaijan have seriously undermined these policies.

The economic crisis and high inflation rates IN 2015 can represent an important threat, to the State capacity to deliver on the long-run pensions indexed on prices. Thus, the subsistence minimums themselves where only partially indexed after the devaluation of 2015. Scarce resources will be accompanied by a larger demand in terms of beneficiaries impacted by the crisis but also in terms of pension amount.

Indeed, annual level of consumer price index defined by corresponding executive body is taken into consideration in case of re-establishing basic part of old-age labour pension. The insurance part of a labour pension and pension capital accumulated in the insurance part of a personal account are indexed at least once a year to the level of the consumer prices index established by the appropriate executive body.

Region: [Europe & Central Asia](#)
Income level: Lower middle income
Population (2015): 9 593 000
Annual population growth (2014):
 ↗ 1.2%
Population above 65 years old (2016):
 5.6% of total population
Life expectancy at birth for ♂/♀ (2014):
 71.6 / 76.8
HDI (2014):
 0.751 [78/188]
GDP (in billion current US\$, 2015):
 53,047
GDP growth (2015):
 ↘ 1.1 %
GDP per capita (current US\$, 2015):
 5 496,34
GNI per capita, Atlas method (current US\$, 2015):
 6560 \$
General government final consumption expenditure (% of GDP)
 12,51%
Minimum wage:
 105 AZN
Average salary in 2015
 466,9 AZN
Labour force participation rate (% ages 15 and older, 2015):
 66.1%
Employment to population ratio, ages 15-24, total (%) (modelled ILO estimate)
 30.4%
Number of economically active population – thsd. Persons - 4915,3
Unemployed persons, thsd. Persons
 243,7
People benefiting from unemployment benefits:
 1543
Number of pensioners
 1 494 106 (87 % through labour pensions and others through social allowances)
People benefiting from an old age labour pension
 785 068
Amount of old-age social allowance
 66 Azn
Amount of survivor social allowance
 61 Azn
Amount of basic-flat rate benefit for old-age labour pension
 110 Azn
Amount of the minimum pensions allocated
 110 Azn
Poverty rate (2015):
 5%
Urban population (2015):
 54,62 %
Sources:
[World Development Indicator \(WB/WDI\)](#)
[Human Development Indicator \(UNDP/HDI\)](#)
[The State Statistical Committee of the Republic of Azerbaijan](#)

The social insurance pensions financing represent several concerns. According to pension reform concept, the public budget was responsible for the financing of pension liabilities for the period of rights acquired before 1992. However, in reality the public budget covers only the difference between benefits which should be paid as labour pensions and the contributions collected through pensions system. In this regards, the effective introduction of third pillar of the pension system is difficult.

During last years the country has made a range of important efforts in coverage of population by social insurance mechanisms. If in 1990s the most of population was unaware of existence of pension system and was reluctant to pay any contributions. At present, most of employed persons in Azerbaijan are covered by social protections system. However, the informal economy and self-employed persons represent an important impediment in further extension of social security coverage. The actuarial forecasts show that if the present trend will continue, the number of beneficiaries of social allowances will raise because important part of population will not have any rights to labour pension².

² See Durin & Tretyak (2012)

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

Economic results demonstrated by Azerbaijan since 2000s due to positive dynamics of energy prices have enabled the Government to achieve an improvement of citizen's well-being, through reinforcing the qualitative aspects of the social protection system and economic development, based on international best practices. However, it is necessary to further develop a comprehensive insurance and pension system that reflect the country's economic and social situation.

During the recent years a number of important measures were taken in the area of improving the standards of living of the population, serious steps were made in the direction of improving the pension provision of the citizens.

According to the studies made in 2009, the social protection system had a very positive impact on the absolute poverty reduction. Thus, the universal social protection system had reduced the absolute poverty rate from 30.9% to 10.9 %, with special positive impact of old-age and disability pensions³. Although the more recent figures were not found, the positive impact of universal social protection system on poverty elevation remains strong.

4. What's next?

Now that the first two tiers of the system (fixed allowance and insurance) are well established, Government plans to develop a third pillar, based on savings, as stipulated in the pension provision reform concept and in the development concept Azerbaijan 2020. This would diversify the financial sources of the pension system and thus its sustainability, while allowing higher pension rates. This pillar should nonetheless be developed taking carefully into account the inflation rates, economic situation and stability of financial markets.

Even if MLSPP has made great progresses in the modernisation of its controls functions, the system still fails to cover all medium and large insurers, and control are highly time-consuming. In this regard, the MLSPP (and SSPF as part of its structure) is planning

to develop an automated fiscal control (e-audit) system crossing the various public database, in order to reduce the time spent on audits and develop automatic alert mechanisms, for all types of insurers.

Finally, a sustainable pension system requires sound analysis mechanisms based on actuarial calculations and statistical data, with the corresponding action plan. Harmonization of pension schemes with the country's socio-economic development, as well as building and strengthening capacity should enable Azerbaijan to define the long-term development priorities of these systems.

This Universal Social Protection brief was produced by Olivia de Vendeuvre of Expertise France. It was reviewed by Andrei Tretyak of Expertise France, and Isabel Ortiz, Mariko Ouchi and Loveleen De of the ILO.

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³ Studer (2012)