



ANNEX 12

Twinning Project AZ/13/ENP/SO/24

**Support to the State Social Protection Fund on the
introduction of funded element within the insurance-
pension system, establishment of non-state pension funds
and development of legal framework for regulating their
activity**

Closing Conference

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**MINISTRY OF WELFARE
OF THE REPUBLIC OF LATVIA**



Gesellschaft für
Versicherungswissenschaft
und -gestaltung e.V.





“Framework of pension system including Republic of Azerbaijan”

von

Prof. Dr. Heinz-Dietrich
Steinmeyer





Introduction

- Multi-level pension systems
 - Different approaches
 - Different legal requirements
- Overview about existing approaches
- Aims and requirements



Existing Approaches

- Depending on the size / replacement rate of the basic scheme
- ➡ Means:
 - the lower the replacement rate of the basic scheme
 - ✓ the more important are second and third level
 - ✓ the more the state is eager to promote it
 - ✓ May lead to mandatory second tier
- Example: United Kingdom (Great Britain)
- Example: To a certain extent the Netherlands



Existing Approaches

- In case of high replacement rates of the basic system
 - ✓ Second and third level is often underdeveloped
- Examples are Southern European countries



Existing Approaches

- A country might have to limit the scope of its basic system
 - ✓ Supplementing (in part replacing) it by a mandatory or voluntary supplementary system
- Examples: Germany (Riester) and Sweden

- A country might want to diversify the financing of its system
 - ✓ From PAYG to a combination of funding and PAYG



Existing Approaches

- The different tiers / layers
- Traditionally three tiers / layers
- ➡ May Mean
 - ✓ Public system
 - ✓ Occupational pension
 - ✓ Individual Savings / Life Insurance
- Example: Germany

- ➡ May also mean
 - ✓ Basic public system (not earnings-related)
 - ✓ Earnings-related second – public-system
 - ✓ Individual savings / Life Insurance
- Examples: Canada, Switzerland



Existing Approaches

- Additional second tier
- Based primarily on employer
 - ✓ Defined contribution (DC)
 - ✓ Defined benefit (DB)
- Core questions:
 - ✓ Who should bear what risk?
 - DC plans and investment risk
 - in DB plans less likely
 - ✓ Lump sum or annuity?
 - Longevity Risk?



Existing Approaches

- ➡ Own initiative
 - Incentives?
 - ✓ tax deductibility
 - ✓ subsidies
- Example: Germany (Riester)
 - Risks?
 - ✓ Choice of product
 - Requirements
 - ✓ Limited to use in old age?



Existing Approaches

- Mandatory vs. voluntary
 - Advantages and Disadvantages
 - ✓ mandatory only good for limited amount
 - ✓ mandatory full coverage
 - ✓ Voluntary needs incentives (costs for budget)
 - ✓ Mandatory – how to enforce?
- Examples:
 - Netherlands quasi-mandatory by collective agreements
 - Canada / Switzerland – mandatory according to the law
 - Germany voluntary – limited coverage



Existing Approaches

■ Public vs. Private Solution

- In case of public solution – state is in charge and may have to give guarantess
- In case of private solution – control on investment – protection against insolvency
- In both cases: Institutions to manage the system
- ✓ In case of private solution
 - via for-profit insurance companies
 - via non-profit institutions



Existing Approaches

■ Contributions /Financing

➤ Only employer



Example:

Germany on occupational pension
(changing)

➤ Only employees

➤ Combination of both



Azerbaijan Solution

- ❖ Will now be a three-tier system
 - With the second pillar consisting of two elements
 - ✓ social insurance
 - ✓ voluntary funded component
 - With the third pillar consisting of a voluntary funded system in addition



Azerbaijan Solution

- ❖ funded component in the state system is to be found in a number of countries
 - Constructed in different ways
 - Mandatory as well as voluntary
 - ✓ In the latter case issue of incentives
 - Usually not state run – but for transition
- ❖ Voluntary Third Pillar more or less linked to employment
 - also here issue of incentives



Azerbaijan Solution

- The new system which is proposed is based on international experiences and follows those models
- ✓ But with a special Azerbaijan component and solution
- ❖ It is important not to take one system as blueprint but find a tailored solution



THANK FOR YOUR ATTENTION!

Twinning Project contacts:

- +994 51 310 76 90
Agrita Groza Resident Twinning Adviser
- Email: twinning.baku@gmail.com
- Address: 80 H.Zardabi avenue, 8th floor, AZ1122, Baku, Azerbaijan



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