

New Pension System in Ukraine



By Evgenia N. DERBAL

On 1 January 2004 the *Compulsory State Pension Insurance Act* and *Non-State Pension Insurance Act* came into effect. The aim of these Acts is to establish a new pension system in Ukraine, which envisages providing pensioners with an adequate pension and ensuring a more equitable procedure for the definition of the size of pensions. From now on the amount of a pension depends on the size of the salary received and on the length of time, which a person and his employer spent making payments into a pension fund.

Structure of new pension system

From 1 January 2004 the pension system of Ukraine has three levels. This analysis will cover all these levels.

1. The joint system will function with the assistance of the Pension Fund of Ukraine. This system calls upon a state pension to be provided to insured persons, among which the *Compulsory State Pension Insurance Act* places: employees, those working under civil legal agreements, private entrepreneurs, attorneys, notaries and others.

In order to receive a state pension the persons mentioned have to pay compulsory contributions into the Pension Fund of Ukraine. Such payments are to be made from a person's income. In addition, all employers should pay a part of their profit as pension contributions. Uninsured persons (for example, Ukrainians living or working abroad) have the right to pay pension contributions voluntarily. To enjoy this an agreement has to be concluded between the person and the Pension Fund of Ukraine.

The joint system retains the validity of the system of pension insurance which was used before 2004. It is important that as a result of adoption of Acts pension contributions are no longer referred to as taxes and are not regulated by tax legislation.

Simplified taxation

The *Compulsory State Pension Insurance Act* enlarged the circle of payers into the Pension Fund of Ukraine. Legal entities and private entrepreneurs who enjoy simplified taxation were included in that circle. Therefore, payers of the single tax and fixed tax are obliged to pay pension contributions for their employees. The rate of payment is 32 % from the wage fund. Moreover, private entrepreneurs who use simplified taxation are to pay pension contributions for themselves. The Cabinet of Ministers of Ukraine should stipulate the value of payments in a fixed amount.

2. The accumulation system is included in the State Pension Insurance system and aims to increase the size of the pension due to a person through investment income. A special Accumulation Fund will be established for this. In that Fund every insured person will have an individual pension account to which

a part of pension contributions will be paid.

Special management companies are entitled to manage accumulated pension assets and are responsible for investing these assets effectively. According to the requirements of the *Compulsory State Pension Insurance Act*, the work of management companies is subject to licensing.

Pension assets have to be deposited in a bank chosen according to the tender. A person can receive a pension from the Accumulation Fund only after reaching pension age in part-payments or a one-time payment (for example, if a person goes abroad to live there permanently or in the event of the onset of disability). The accumulation system brings insured persons some advantages. For example, a rise in their future pension and the possibility of handing down pension assets.

It should be mentioned that the *Compulsory State Pension Insurance Act* doesn't set out precise data for implementing the accumulation system. The Accumulation Fund will be established only after some conditions have been fulfilled, among which is economic growth in Ukraine for two years. Consequently, all the pension contributions of insured persons and their employers will be paid into the joint system till a special Act is adopted.

3. Non-state pension insurance, unlike *Compulsory State Pension Insurance*, is voluntary. In order to enjoy it persons should make extra pension contributions besides payments to the joint system and accumulation system. The basic unit of non-state pension insurance is a non-state pension fund. A person who wants to receive an additional pension should conclude an agreement with a chosen pension fund and pay his contributions into it.

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Types of non-state pension funds

Non-state pension funds are considered as non-profit organizations and the following types can be established:

- Open pension funds (any person regardless of his place of work can be a participant of this fund);
- Corporate funds (only employees of a company that is a founder of the corporate fund can be participants);
- Professional funds (only professionally related persons can be participants of the professional fund).

A legal entity is allowed to be a founder of only one corporate or professional fund, but it can establish more than one open pension fund.

Every non-state pension fund will have a board in order to supervise day-to-day operation of the fund and to conduct its principal affairs. Furthermore, each pension fund is obliged to conclude a treaty with an administrator, management company and bank to keep pension assets. According to the *Non-State Pension Insurance Act* the work of all the organizations mentioned is subject to licensing.

Pension contributions

Non-state pension insurance is formed on the basis of voluntary payments of persons which accumulate on their individual accounts. Conse-

quently, every person can by request conclude an agreement with a non-state pension fund regardless of the fact that he is already insured in the State Pension System (joint and accumulation system). His employer, parents, children or spouse can make a pension contribution for him. The amount and procedure for making payments are set out in the pension agreement in accordance with the pension scheme chosen.

The work of non-state pension funds

A non-state pension fund is entitled to invest pension assets in order to receive a profit for the benefit of its participants. The investment policy of the fund is set out in an investment declaration and is carried out by an asset management company. Such a company can invest pension assets in certain securities and bank deposits. The profit from the mentioned activity is shared out between participants of the fund *pro rata* to the sums in their individual accounts.

The investment activity of a fund can be either profitable or unprofitable. If it is unprofitable, how can a person protect himself from losing his money?

To avoid such consequences it is necessary to include a clause in the agreement with the asset management company on its obligation to ensure a minimal yield at the level of the official rate of inflation. If this obligation is

breached the asset management company shall indemnify any losses from its reserve fund or other assets.

Receipt of pension

According to the *Compulsory State Pension Insurance Act*, in order to receive a state pension a person has to reach pension age, which is 60 years for men and 55 for women. If a person is insured in a non-state pension insurance system he can define his pension age himself. This age can be more or less than the age for receipt of a state pension within the range of 10 years. The amount of a non-state pension depends on the sum in a person's individual account and the period of time the pension will be paid. But the period during which a person was paying contributions to a non-state pension fund isn't taken into account.

Non-state pension funds have to make the following payments:

- A pension for a fixed period (at least 10 years);
- One time payment (in the event of going abroad to live on a permanent basis or onset of a disability).

Through non-state pension insurance every person can increase his pension and choose an acceptable way for receiving this pension. Nevertheless, it will take time for pension funds to find profitable investments and to gain the trust of potential participants. ■

Have You Missed Any of These?

- *Ukrainian Judicial System Act* (UJBL No.1, Vol.1)
- *Ukrainian Television and Radio Broadcasting Act* (UJBL No.2, Vol.1)
- *Ukrainian Companies Act* (UJBL No.3, Vol.1)
- *Ukrainian Profit Taxation of Enterprises Act* (UJBL No.4, Vol.1)
- *Ukrainian Protection of Rights to Trademarks for Goods and Services Act* (UJBL No.5, Vol.1)
- *Ukrainian Restoration of the Debtor's Solvency or Declaring It Bankrupt Act* (UJBL No.6, Vol.1)
- *Ukrainian Printed Mass Media (Press) in Ukraine Act* (UJBL No.7, Vol.1)
- *Ukrainian Planning and Development of Territories Act* (UJBL No.8, Vol.1)
- *Ukrainian Securities and the Stock Market Act* (UJBL No.9, Vol.1)
- *Protection of Economic Competition Act* (UJBL No.11, Vol.1)
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