

Why is the income replacement ratio important and its role in the pension system

International organizations highlight the income replacement ratio (IRR) as one of the important indicators of pension adequacy. It reflects the ratio between pension benefits and the employee's wages before retirement, i.e. how much his pension income replaces his labor income.

It should be noted that the IRR is a target benchmark, its value is individual for each employee and depends on his labor income and length of service, regularity and completeness of pension contributions to his funded pension account.

The concept of further modernization of the pension system of the Republic of Kazakhstan until 2030 provides for maintaining the IRR with total pension benefits at a level of at least 40% of lost earnings (International Labor Organization standard) with at least 35 years of participation in the pension system and a regularity of contributions of 12 times a year.

The replacement rate for UAPF contributors who reached retirement age in 2024 and began to receive pension benefits (solidary and basic pension from the state, as well as funded pension from UAPF), in total for all types of pensions amounted to more than 41% of the average salary level.

In the future, as is happening in developed countries, the funded pension will make up an increasing part of the total pension. The Kazakhstan funded pension system has not yet completed its full cycle, which is about 40 years - the full period of a person's working life. Therefore, those who retire do not yet have sufficient savings experience. In addition, as is known, in the first years of the implementation of the funded system, low incomes, irregularity and incompleteness of contributions were characterized. Therefore, a higher share of solidarity pension is still maintained, but gradually decreases. In the future, according to actuarial estimates, the replacement rate due to the funded pension for contributors who began their working career in 2024 (at the age of 22) and will retire in 2065 will be 35% or more of their earnings. At the same time, the funded pension will be formed at the expense of compulsory pension contributions of employees (CPC) and employers (ECPC). In addition, citizens will receive a basic pension, the amount of which also depends on the length of service of CPC contributions to the UAPF. Such workers will no longer have the right to a solidarity pension.

Currently, the calculation of the average monthly income replacement rate for each contributor is carried out by the UAPF based on information from state information systems, within the limits provided by law.

How is IRR calculated for the purposes of using lump sum pension benefit payments (LSPBP) for improving housing conditions and/or medical treatment?

It should be noted that persons with pension savings in the UAPF are entitled to lump sum pension benefit payments (LSPBP) if one of the following conditions is met:

- Pension savings exceed the minimum sufficiency threshold
- Future pension (joint and basic) is not less than 40% of current income
- A pension annuity agreement has been concluded with an insurance company.

The legislation defines the algorithm for calculating the IRR as follows:

The monthly pension (basic + solidarity on the date of assignment) is divided by the average monthly income of the beneficiary (AMI) for the last 5 years (before retirement). The amount of AMI is calculated based on data on his actual compulsory pension contributions (CPC) for 5 years, adjusted for inflation, and is limited to the average monthly income in the republic.

For beneficiaries of long-service pension benefits who are assigned pension benefits in accordance with the Social Code, and retired judges who are paid a monthly lifetime allowance, the replacement rate of the AMI is taken to be 40%.

Please note that only the basic and solidarity pensions are taken into account to calculate the IRR, which should provide the pensioner with a lifetime income of at least 40%. Upon reaching this IRR level, the pensioner can use up to 50% of their savings for housing or treatment.

If a person has entered into a pension annuity agreement, that is, receives a lifetime pension benefit from an insurance company of at least 70% of the subsistence minimum established for the current financial year, they can use all savings in their pension account in the UAPF for housing or medical treatment.

Understanding the meaning of the replacement rate helps citizens plan their financial stability through pension benefits. Every year, the role of funded pensions is becoming increasingly important. It is important that public policy and the pension system develop in the direction of providing adequate pensions for all citizens.

UAPF was founded on August 22, 2013 on the basis of GNPf APF JSC. The founder and shareholder of the UAPF is the Government of the Republic of Kazakhstan represented by the State Institution Committee of State Property and Privatization of the Ministry of Finance of the Republic of Kazakhstan. Trust management of UAPF pension assets is carried out by the National Bank of the Republic of Kazakhstan. In accordance with the pension legislation, the UAPF attracts compulsory pension contributions, employer's compulsory pension contributions, compulsory occupational pension contributions, voluntary pension contributions, as well as carries out enrollment and accounting of voluntary pension contributions formed at the expense of the unclaimed amount of guaranteed compensation for the guaranteed deposit, transferred by the organization carrying out mandatory guarantee of deposits, in accordance with the Law of the Republic of Kazakhstan "On mandatory guarantee of deposits placed in second-tier banks of the Republic of Kazakhstan", ensures the implementation of pension benefits. The Fund also carries out accounting of target assets and target requirements, accounting and crediting of target savings (TS) to target savings accounts, payments of TS to their recipients in bank accounts, accounting for returns of TS in the manner determined by the Government of the Republic of Kazakhstan within the framework of the National Fund for Children program (More details at www.enpf.kz)