

Problems of reforming of the pension system of Kazakhstan

I. V. Poryadina¹, N. V. Kabasheva², G. B. Alina³, Y. A. Statsurina⁴

¹Siberian university of consumer cooperation, Russian Federation,

²Financial Academy, Republic of Kazakhstan,

³Kazakh university of economy, finance and international trade, Republic of Kazakhstan,

⁴Eurasian Humanities Institute, Republic of Kazakhstan

Paper received 15.05.2016; Accepted for publication 02.06.2016.

Abstract. In the article the author considers the operating pension system of Kazakhstan. There was made the analysis of the modern state of the accumulative pension system in Kazakhstan and there were determined the ways of its improvement by means of increasing social significance.

Keywords: *pension funds, pension deduction, pension installments, pension accumulation.*

Setting the problem. Modern practice of the state regulation of the social-economical development of the country depends on the necessity to turn to the formation of long-term purposeful orientation of the development of the pension system. Pension provision in the Republic of Kazakhstan occupies the leading place in the system of social protection of the population and concerns the interests of more than 1.6 million of pensioners and about 8 million of the participants of the accumulation pension system of the country. Its qualitative and quantitative characteristics witness the level of social, economical, legal and cultural development of the society. The structure and functioning of the pension system in many aspects determine sustainability and dynamics of the economical and social development of the country. The effective system of the pension provision, guarantee of sufficient pensions, providing a worthy life standard of pensioners and their timely payment maintain a favorable social climate of the society. The government of the Republic of Kazakhstan sets a task to strengthen the social direction of the carried out reforms by way of fostering their activity on the reduction of unemployment and struggle against poverty, the creation of the conditions for the realization of the labor potential, timely payment of salaries, pensions, allowances and the address social aid for the poor. These measures are aimed at the improvement of the social climate in the country.

Kazakhstan was the first among the CIS countries that started reforming an old joint system of the pension provision of the citizens passing to the accumulation system. The law "About the pension security in the Republic of Kazakhstan" adopted on 20 June, 1997 was the beginning of the formation of the cumulative pension system (Law, 1997).

Initially, the reform was planned and realized to reduce the budget load and to create a just system of the pension provision. The pension accumulation allowed to implement a lot of state programs and to carry out a lot of investment projects.

According to this law a modern pension system is being formed at two levels: distributive and accumulative due to which there appeared new financial-economical institutes: accumulative pension funds, the organizations realizing the investment control of the pension assets, banks-custodies, which hadn't existed in Kazakhstan before. The main functions of these organizations are stated in the Law "About the pension provision in the Republic of Kazakhstan".

At present the optimal structure of the pension system

has been formed in Kazakhstan. Not being satisfied with achieved results, the country is still developing the system of providing pensioners and makes all efforts to assure each citizen that his/her pension will be sufficient for the worthy life. Today we face the task to use the resources of the accumulative pension funds effectively for the growth of economy and the rise of investors' income. The pension accumulation allowed realizing different state programs and investment projects. But in spite of significant and positive results of reforming the accumulative pension system, many of its problems remain unsolved.

As a result, this substantiates the urgency of the research on the problems of reforming the pension system and the search of effective financial instruments on controlling pension assets that will serve the factor of not only the growth of the amount of the population accumulation, but also a stimulating factor of the economic growth.

Analysis of the latest researches and publications.

Theoretical and practical issues on reforming the pension system of Kazakhstan are investigated in the works of K. Arstanbekova (2001), N. Alimuhambetov (2003), Ye. Nurmuhambetov (2002), N. Nurlanova (2005), A. Koryaghin (2005), V. Melnikov (2008) and others.

The subject of the research is to reveal the problems of the pension market as a whole and to suggest the ways of their solution at the present level, the development of recommendations, aimed at the further dynamic development of the country.

The aim of the research is the analysis of the modern state of the accumulative pension system in Kazakhstan and determining the ways of its improvement by way of increasing social significance.

The main results of the research are as follows: The pension system of Kazakhstan consists of three constituents: joint, accumulative (obligatory) and voluntary. The accumulative pension system is based on accumulating means on the individual accounts of the employers. Each person involved in the cumulative pension scheme receives a personal account on which his/her pension installments are accumulated.

Pension accumulation is formed by monthly obligatory installments comprising at present 10% of the size of the employer's salary (in case with the servicemen according to article 65, point 3 of "the Law of RK of 20 June 1997 №136-I "About pension security in RK at the amount of 20 %), and also by an investment income, received by the investor after having invested pension accumulation. The sum and periodicity of allocations of voluntary pension

deposits are determined by investors. These means are accumulated and invested by accumulating pension funds and by the investors' coming into pension age the means become a source of his/her pension payments. The Kazakhstani model taking into account its own peculiarities took and adapted the experience of other countries, that's why it is considered one of the most successful in the world practice (K. Arstanbekova, 2001; N. Alimuhambetov, 2003).

The Kazakhstani model of the pension system is based on the following principles:

- giving investors and recipients the right of choice of the accumulating pension fund;
- obligatory participation in the system of all working population;
- differentiation of pensions and other forms of social security;
- personified record of pension accumulation of the investors;
- giving a social individual code to everybody, who has a right for pension provision and the further transference of pension installments according to the given social individual code of the investor;
- charging of pension installments and keeping the forming accumulation on the individual pension accounts;
- state guarantee of pension accumulation at the size of the invested obligatory pension installments taking into account the level of inflation for the moment of the investor's going on pension;
- giving the investor or the receiver obligatory information about the status of his/her pension accumulation;
- state regulation of the activity of the participants of the accumulative pension system (accumulation pension funds (APF), custody-banks and organizations implementing the investment control of pension assets (OIICPA), including: licensing and prudent regulation of APF, OIICPA, custody-banks, monitoring of their activities on the basis of financial and statistic reports; introduction of obligatory requirements on controlling and diversification of the assets;
- custody of cash and securities in the custody-bank, which cannot be affiliated either with APF or OIICPA;
- controlling of the target placing of pension assets by a custody bank;
- differentiated record of personal and pension assets in the accumulation pension fund;
- impossibility to address recovery on the pension assets on the investor's debts, APF, the custody-bank and OIICPA, including cases of liquidation or bankrupts.

During the whole transitive period to the accumulative pension system the state is responsible to the citizens having the pension service before the pension reform and also guarantees the pensioners the right to receive pensions and maintenance of the size of pensions from the State centre on pension payments taking into account the level of inflation.

The accumulative pension system obliges the involved population to carry out the responsibility for the level of their income after their retirement as far as the sources of pension payments will be the accumulation formed by them on the individual accounts. Each citizen is given the possibility to increase his/her accumulation at the expense of voluntary pension installments and by this to provide a

higher income after the completion of the labor activity.

Indices on the accumulative pension system for 1 January 2013: the number of the accumulative pension funds – 9 APF, the number of OIICPA – 2, the number of investors - more than 8 million people, the sum of pension accumulation – more than 30 billion USA dollars.

In the Kazakhstani structure of the accumulating pension system three basic elements operate: pension funds, the organization implementing investment control of pension assets (OIICPA) and custody banks (Conception, 2010).

Accumulating pension funds are included in the number of important social-economic institutes, dealing with long-term financial resources and they are the more active institutional investors in economy (V. Melnikov, 2007).

The Kazakhstani accumulative pension funds implement their activity on the basis of corresponding licenses, given by the National Bank, which guarantees that the pension fund must be specialized only on the non-state pension provision (Decree, 2005).

Custody of pension accumulation (the sums of obligatory pension installments on the account of the level of inflation) is guaranteed (Law, 1997):

- by the state on the basis of the Law of RK "About pension security in the Republic of Kazakhstan";
- by prudent normative, established by the authorized organ for the participants of the pension market;
- by separate record of the means of all participants of the accumulative pension system; the accumulative pension fund, managing company, custody bank (Decree, 1997);
- by other requirements of legislature (article 6 of the Law of RK "About pension security in the Republic of Kazakhstan").

The accumulative pension funds operate so that the pension deductions should work for the economy of the country and bring their investors the so called investment income. And the activity of the pension funds is strictly regulated by the state that allows reducing to minimum the investment hazards. If the pension fund has definite losses then it must compensate its investors these losses. Managers of companies who work out the strategy of investing the means manage the pension funds. As a result of such system the investor without any efforts not only accumulates for his/her own old age, but also has a possibility to receive the investment income from his deduction, this money works for the country economy and the budget has minimum losses for the social security of pensioners. At the same time if the investor of the fund is not satisfied with the results of the fund work, for example, the amount of the income, he has a right to change the fund and to transfer his/her pension capital to another fund, where there are more optimal possibilities for the rise of the investment income capital (A. Koryaghin, 2005).

The investment control of pension assets is implemented by the organizations, which control the pension assets or pension funds independently if they have corresponding licenses. The organization which controls the pension assets of the accumulative pension funds is a legal entity, a professional participant of the market of securities and is created in the form of a joint stock company in the order established by the legislature of the Republic of Kazakhstan. In their activity the

accumulative pension funds, organizations implementing the investment control of pension assets and the custody bank in relation to each other are guided by the regulations of a three-sided custody agreement, in which all the rights and obligations of each of the sides and all legal relations are settled in detail. The interaction among these three legal entities of pension service takes place in the following way: in accordance with the agreement about the pension security between the pension fund and the investor the installments of the investor-receiver go to the custody bank with which the fund has concluded the custody agreement, but it is specially open for the investment pension account of the fund.

OIICPA as follows from their name control pension assets, investing them in different instrument, allowed by the legislature. The pension fund concludes an agreement with the managing company and that company taking into account its own experience and strategy makes the pension accumulation work at the expense of purchasing and selling of financial instruments.

These market players have two main tasks: to invest the pension assets and to evaluate them regularly (Ye. Nurmuhantbetov, 2002; N. Nurlanova, 2005). Besides, OIICPA must regularly report about its activity to the National Bank and APF and also through mass media - before the investors of the funds. OIICPA are significantly distinguished from other investment companies. Firstly, they are limited in the choice of directions for investment. These are more reliable instruments with low incomes, but with the minimum degree of risk. Secondly, if a client of an ordinary investment company shares investment risks together with this company then in case with OIICPA the pension fund has the right to demand from it compensation of the losses caused by the inappropriate management of the pension assets. OIICPA is responsible for its commitments to the accumulative pension funds and to the investors by all its property. Thirdly, the legislature makes a number of demands and limitations to the OIICPA it self and also to the

auctioneers and managers except for other investment companies.

The third element of the system is the custody bank which cannot be affiliated either with APF or OIICPA and keeps the pension money and controls its target placement. It informs the APF monthly about the condition of his/her accounts and about the activity of OIICPA. The accumulation pension fund must have one custody bank. But the bank cannot serve some funds simultaneously. The custody bank is the bank implementing the activity on fixing and recording the rights on securities, keeping documentary securities and recording the client's money. The custody bank controls the target placement of pension assets of APF and is obliged to block (not to fulfill) the instructions of OIICPA or APF in case of their unconformity to the legislature of RK. More over, the law envisages that the custodian in this case must immediately inform the commissioner and APF about this. This system of independent elements allows maintaining a high level of reliability of the operation of the pension capital. Besides the three main elements of the market the National Bank and the Kazakhstani fund exchange (KFE) play an important role in the operation of the pension system (Conception, 2010).

A great significance is paid to the investment of pension accumulation in the country. The fund/managing company buys securities on the coming pension installments every day in order to get the investment income. The investment income is charged to the investor every day it may be either positive or negative. In any case the investor must know the strategy of his/her fund's investment and be able to analyze the investment portfolio of the fund take a timely decision about transferring his/her accumulation if the accumulation decreases because of the losses during a long period. The investment income is an important constituent of the investor's pension, because on the completion of a long period of time – about 30 years as is shown in the scheme (figure 1) – the share of the investment income ca comprise more than a half of pension accumulation.

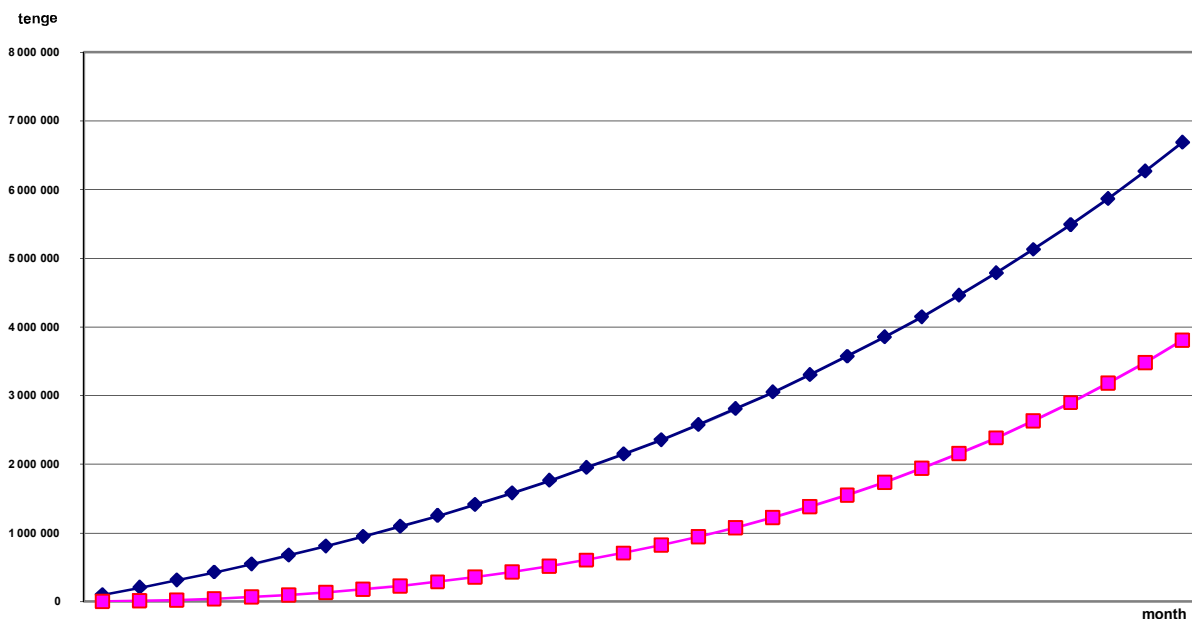


Figure 1. Changes of pension accumulation and investment income. Compiled by the author

From figure 1 we see that the pension accumulation rises and the investment income falls.
In Kazakhstan for 1 January 2012 the pension funds

must create multi-portfolios (figure 2), the aim of which is a more effective management of pension assets, the control of the level of risk and income projection.

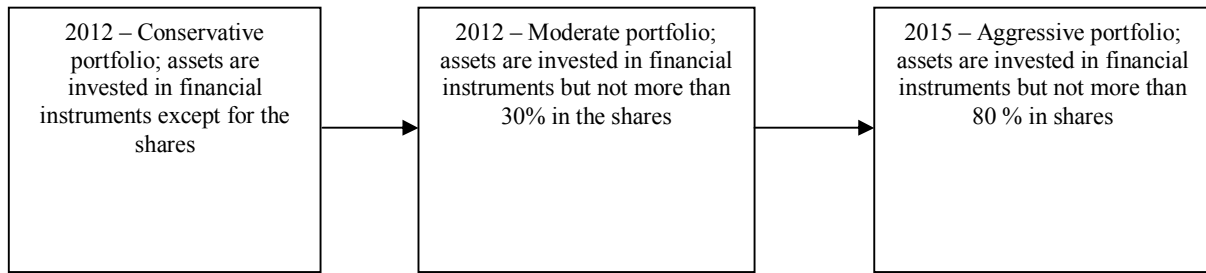


Figure 2. Types of multi-portfolios of pension funds. Compiled by the author

For the investors of the funds there is always a choice of the strategy and portfolio according to his/her investment requirements and expectations, participation in the process of managing his/her pension assets.

From 1 January, 2012 the law about the division of the investment portfolio of the accumulation pension funds into the conservative and moderate came into force. Today about 230 thousand pensioners make investments in the conservative portfolio. The conservative strategy of investing – no shares, voluntary – low, profitability – minimum, risks – minimum. The moderate strategy of investing – till 30%, voluntary – medium, profitability – medium, risks – medium. The aggressive strategy of investing: shares – till 80%, voluntary – high, profitability – high, risks – high.

Before 1 January 2013 the accumulation pension funds had to pass the procedure of listing at the Kazakhstani Fund Exchange for the realization of gradual initiatives of KFE of RK in order to regulate the activity of auctioneers (at present 3 funds have passed through such procedure).

Conclusion and perspectives. As far as in Kazakhstan the pension system is being formed with the participation of a lot of professional participants of the financial market, the APF refers to the participants of the financial market as far as they are big institutional investors at the fund market of Kazakhstan.

At present the National Bank of RK raises the question about the creation of a single pension fund. Now in Kazakhstan there are 9 accumulative pension funds,

which jointly manage a large sum of money (almost 30 billion USA dollars) of future pensioners of the country. Until present time the main activity of these funds was investing in securities (which could be state securities, bonds of local companies, the shares of local companies and in less degree - foreign securities). Today the private accumulation pension funds are the most active group of investors at the market of securities of Kazakhstan. They provide either the activity (liquidity) or competition at the market. Uniting of all private accumulative pension funds into one single pension fund will practically exclude competition and also will strongly influence the liquidity of the market of securities in Kazakhstan. Liquidity and competition at the market will provide just evaluation of securities. The monopolist position of a single pension fund will cause great doubts to the justice of evaluating securities, which will be placed at the initial market. And also the monopolist position of a single pension fund will create the situation in which potential producers of securities will strongly depend on a single investor at the market and such situation will lead to the ineffectiveness and, probably, to corruption at the initial placement of securities. In these conditions potential producers will prefer to get financing from the banks (which are in a very competitive environment), than through the market of securities. As a result, the Kazakhstani companies will lose the access to a cheaper funding and that's why they will not be able to invest in new projects the amount they have planned that undoubtedly is waning for the economy of Kazakhstan.

REFERENCES

1. Arstanbekova K. What a sudden change from scarcity to plenty // AlPari. – 2001. - № 3. - P.41-43.
2. Alimuhambeto N. New methods of calculating pension assets // The market of securities of Kazakhstan. - 2003. - № 9. - P. 8.
3. The concept of development of the financial sector of the Republic of Kazakhstan in the post-crisis period, approved by the Decree of the President of the Republic of Kazakhstan № 923 dated February 1, 2010. // nationalbank.kz
4. Decree of the Government of the Republic of Kazakhstan of 16 September, 1997 N 1342 "About the establishment of the order of giving the individual code to the citizens of the Republic of Kazakhstan in the State centre on pension payments".
5. Koryaghin A. Pension accumulation: questions and answers // Finance of Kazakhstan. – 2005. - № 4. - P.64-66.
6. Melnikov V. Basics of Finance: textbook. - Almaty: LEM. - 2007. - 568 p.
7. Nurmuhambetov Ye. Analysis of pension services of Kazakhstan // The market of securities of Kazakhstan. - 2002. - № 7. - P.40-49.
8. Nurlanova N. Problems of management of pension fund assets in the conditions of a new legal field // Banks of Kazakhstan. – 2005. - №6. - P.56-6
9. Resolution of the Management of the National Bank of RK of 29 May, 2005 № 177 "About the approval of license regulations on investment management of pension assets".
10. The Law of the Republic of Kazakhstan of 29 June, 1997 № 136-I "About pension provision in the Republic of Kazakhstan" (with amendments on 1 January, 2013).