
TWINNING PROJECT FICHE

1 Basic information

- 1.1 **Programme:** ENPI-Annual Action Programme 2012 for the Republic of Azerbaijan (CRIS number: ENPI/2012/023411)
- 1.2 **Twining number:** AZ/15/ENP/SO/38
- 1.3 **Title:** Support to the State Social Protection Fund in reforming pension system in Azerbaijan
- 1.4 **Sector:** Social Protection
- 1.5 **Beneficiary country:** Republic of Azerbaijan

2 Objectives

2.1 Overall objective:

To contribute to further reforms of the pension provision system in Azerbaijan in compliance with best European practices.

2.2 Project purpose:

To improve the capacity, tools and efficiency of the State Social Protection Fund of the Republic of Azerbaijan (SSPF) to develop and implement an automated fiscal control (e-audit) system; to strengthen the institutional and technical aspects of the budgeting as well as the strategic planning mechanisms of the mandatory and voluntary social insurance systems.

2.3 Contribution to National Development Plan / Cooperation agreement / Association agreement / Action plan

2.3.1 EU-Azerbaijan agenda

After its enlargement in May 2004, the EU faced a new geopolitical situation and adopted the **European Neighbourhood Policy (ENP)**¹, which is a new framework for the relations with its neighbours. The ENP aims to go beyond the existing Partnership and Co-operation Agreements to offer neighbouring countries the prospect of an increasingly closer relationship with the EU with the overall goal of fostering the political and economic reform processes, promoting closer economic integration as well as legal and technical approximation and sustainable development.

The central element of the ENP is a bilateral **EU-Azerbaijan Action Plan (AP)**² of 14 November 2006 which clearly sets out policy targets and benchmarks through which progress with an individual neighbouring country can be assessed over several years. With regard to reforms in the Social Protection sector, ENP Action Plan of 14 November 2006 sets out the following priorities to be pursued (priority area 6 and article 4.4.):

- “reform the social security system, notably to improve targeting and effectiveness of social protection measures and social assistance”

¹ http://eeas.europa.eu/enp/index_en.htm

² <http://pao.az/en/newsfeeds/list-all-news-feed-categories/digital-library/other-related-eu-documents/74-euazerbaijan-action-plan/file>

- “promote exchanges of experiences, dialogue and cooperation on matters of social security, notably on issues such as the reforms of the pension system and of the social insurance”.

The ENP-AP also includes co-operation tools, like Twinning, the Technical Assistance and Information Exchange Office instrument (TAIEX) and the Support for Improvement in Governance and Management initiative (SIGMA), which play an essential role in the achievement of the Action Plan priorities. In particular, the Twinning instrument, which provides for direct co-operation between EU and Azerbaijani public bodies to support institution building activities, has proved to be particularly efficient in policy areas where the expertise required by the beneficiary country exists mainly in the public sector.

2.3.2 Governmental policy and strategy

Legislation and strategic documents related to the project

The main relevant documents are:

Existing legislation:

- 18 February 1997 – Law “On Social Insurance” № 250-IQ
This Law regulates the relations in the field of social insurance, determines the legal, economic and organizational basis of the social insurance
- 27 November 2001 – Law “On Personal Accounts in the State Social Insurance System” № 221-IIQ
This Law 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
This Law regulates the creation of labour pension rights of citizens, rules for the implementation of these rights and establishes a system of labour pension provision.
- 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
This Law regulates the checks carried out by the governmental institutions at the enterprises. It determines the rights and the obligations of the inspection bodies and entrepreneurs.

Strategic documents

The reforms in the field of the proposed project are stated in:

a) DEVELOPMENT CONCEPT “AZERBAIJAN – 2020: THE VISION OF THE FUTURE”

Article 7.3 of the Concept defines the main goals in the field of pension system reform as follows:

‘In order to ensure reliable social protection for the population, consistent measures will be continued within the framework of the ongoing “State programme on the development of the insurance-pension system in the Azerbaijan Republic in 2009-2015”. In order to further deepen the pension reform, a new state programme covering 2016-2020 will be prepared. This will result in further improving the insurance-pension system, introducing voluntary social insurance and realisation of measures for activities of non-state pension funds.

The registration of insurers will be fully automated, insured persons automatically listed in the state social insurance system, electronic processing of mandatory state social insurance reports

and information about insured persons introduced, and electronic audits of insurers conducted. Besides, there will be no more need for submitting any documents, all applications will be processed electronically and pensions automatically appointed from a single centre.

A national labour and employment information system will be created, a system put in place to monitor and analyse the labour market and measures taken to prevent unofficial employment”.

b) State Programme on Development of the Insurance-Pension System in 2009-2015

Aims at ensuring sustainable and dynamic development of the system and to further improve pension provision of citizens, was approved by a Presidential Order dated 30 December 2008.

Its main directions are:

- Actuary models-based improvement of the insurance-pension system;
- Improvement of activities in the field of mandatory state social insurance;
- Improvement of labour pension provision;
- Development of personal accounting in the state social insurance system;
- Applying funded component in the insurance-pension system;
- Development of non-state pension institutions

(See details in Annex 3).

c) Concept on the Pension Provision System Reform in 2014-2020

Approved by the Order of the President of the Republic of Azerbaijan on 4 November 2014 No.827. This Concept ensures a long-term reliable social protection of the pensioners by considering international development tendencies and accommodating the pension provision to regularly updated modern requirements, benefiting from appropriate experience of the developed countries.

The main goals of the reform of the pension provision system are:

- strengthening insurance principles in pension provision system and establishing balancing mechanisms between the obtained pension rights and collected insurance funds;
- ensuring commensurate of assigned pension amounts with paid contributions in pension provision system;
- establishing mechanisms based on actuarial analyses for the long-term development of pension provision system;
- improving regulatory mechanisms for non-contributory payment, as well as differentiating state obligations;
- implementing voluntary funded component of labour pensions as well as establishing and developing non-state pension institutions.

(See details in Annex 4)

Legislation and strategic documents under development

- Amendments to the Law “On Labour Pensions” for implementation of actions stipulated in the Concept on the Pension Provision System Reform in 2014-2020
- Law "On Funded Part of the Labour Pensions "
- Law "On Private pension funds"

3 Description of the project

3.1 Background and justification

3.1.1 Current situation in the Social Protection sector

Economy overview and labour market

The Republic of Azerbaijan is a middle income country with a population of 9,593,000 people. The number of business entities is 94,563 (as of 01/01/2015) and self-employed persons are almost 1 million. The country has achieved rapid economic progress during the last decade. The annual Gross Domestic Product (GDP) was worth 74.16 billion US dollars in 2013. The revenues of the consolidated state budget were 21.986 billion Azerbaijan manat (AZN) in 2014 (28.187 billion US). The oil sector contributed for 65.6 % of the budget incomes.

The labour force significantly increased in absolute terms. While in 2000 there were 4,370,200 economically active people, in 2013 their number reached 4.7 million (1.2 Million people work for public institutions), increasing by more than 7.5%. Unemployed rate in 2013 was 5%.

The situation with Azerbaijan's labour market is similar to many other countries of the post-Soviet region. The sectors, which employ the most people, are not those which generate the largest added value per person. Many contrasts in employment level, wages and productivity may be observed among activity sectors. The oil and mining industry employs only 1.1% of all employed people while generating most of the Azerbaijan's GDP. Meanwhile, 38.3% of the labour force is employed in the agriculture sector and only generate 7.1% of the GDP. The highest salaries are also observed in the oil and mining industry: in average, they are 12 times bigger than for agriculture and almost 8 times bigger than for education. Only a small number of workers have access to the high-productive, high-wage jobs of the oil industry. The rest of the labour force works in low-productive and low-wage sectors.

The share of self-employed people within Azerbaijan's employment statistics is significant. It increased from 17.4% of the labour force in 2000 to 22.2 % in 2013. It is mostly attributed to the governmental policy that introduced simplified taxation and a "one-window" system for business registration. There is no official statistics on unofficial economy, however it believed to be significant.

Pension system overview³

At present there are 1.29 million pensioners. According to the official statistics of July 1, 2015, the number of personal accounts reached 3.09 million persons of which 59.1% (1,831,564 persons) are male and 40.9% (1,267,253 persons) are female. It makes 2.39 insured persons per pensioner.

Insured persons aged from 30 to 40 years dominate among insured persons registered in personal accounting system, 24.84% (769,030 persons). 21.59% (669,101 persons) are aged below 30 years; 20.69% (641,144 persons) from 40 to 50 years; 21.15% (655,449 persons) from 50 to 60 years; and 11.73% (363,420 persons) aged above 60 years.

In 2010, the official retirement age was 62 years for men and 57 years for women. At least 12 years of covered employment were required to be entitled to a state pension. Since 1 January 2010, the retirement age has risen by six months every year to the age of 63 for men and 60 for women. Those not eligible for a labour pension are entitled to social allowances at the age of 67 for men and 62 for women. Early retirement is possible in a number of cases, for example if a woman has had five or more children or if a person worked in difficult conditions.

³ <http://www.ssp.gov.az/view.php?lang=en&menu=76>

The labour pension is calculated as the sum of three components: 1) a basic flat-rate benefit (100 AZN as of September 2013), 2) insured part - amount of insurance part of old-age labour pension shall be 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 – not applied yet. The insured part of the labour pension is adjusted on annual basis, taking into account changes in the consumer price index. A basic flat-rate benefit is adjusted by order of the relevant executive power.

Wide application of the cutting-edge information and communication technologies has been achieved in the past period; relevant measures have been implemented concerning the automation of management. It should be noted that, registration of the insurers engaged in entrepreneurship has been totally automated. Good service by call centres has been implemented. Relevant measures are being implemented on automating the registration of other insurers. Automatically registration of the insured persons, and electronically receipt of the reports from large and medium insurers has been provided.

The insurance and pension reforms introduced a unique state pension system, incorporating functions related to social insurance, personal accounting and pension provision. It includes individual accounts for the insured persons to register their mandatory state social contributions and to determine their pension rights according to their contributions. Mechanisms allowing voluntary - state or non-state- contributions in addition to the mandatory state social insurance, are also foreseen in the 2014-2020 “Reform Concept” (details in Annex 4).

In 2014 actual revenue of SSPF budget made 2,896.9 mln. manat, and expenditures – 2,869.4 mln. manat. Surplus of the budget appeared to be in the amount of 27.5 mln. manat. 97.9% (2808.6 mln. manat) of expenditures were spent for the pensions (97.4%) and benefits (2.6%).

In 2014, 1,743,743.240 million AZN of social contributions were collected, that makes approximately 60.2% of the total budget of the SSPF. 0.4% of the total budget of the SSPF consisted of the revenues generated from other sources. The remaining 39.4% were covered by the state budget transfer carried out by the Ministry of Finance.

The collected social contributions were distributed amongst the main payers as follows:

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

According to SSPF’s 2015 budget (3,056 billion AZN) adopted by the Parliament 63,8% of revenues come from mandatory contribution (1,950 billion AZN), only 36% (1,100 billion AZN) of revenues transferred from State budget by Ministry of Finance, and other 0.2% of revenues generated from other sources.

Social contributions

The main contributors are the employees and the self-employed persons.

Employees pay 3% of their monthly gross income to the State Social Protection Fund. Employers provide an additional 22% and must transfer the total contribution to the Fund budget simultaneously with the payment of the salaries. Fifty percent of the total contribution enters into the individual account of an employee.

Self-employed persons must contribute 50 per cent of the national monthly minimum wage (currently 105 AZN) if engaged in trade or construction; different rates (from 10 to 50) apply depending on professional sector and regions.

Land owners must contribute with rates depending of the land category (it varies from category 1 to 4). The rate per capita and per hectare, is 2% to 12% of the national monthly minimum wage (currently 105 AZN).

Other categories: Civil servants, militants, prosecutors, etc. have a special social contribution payment regime stipulated in the Rules of payments of the compulsory state social contributions, which were approved by the Order № 440 on 9 August 2006, of the Chairman of the SSPF.

Contributors must submit quarterly reports (called B1 report) until the 20th of the month following the reporting quarter. In this report contributors provide information about themselves (total amount of their remuneration fund, total amount of contribution payments they have paid and so on). Also, all contributors must submit annual reports (called B3 report) until 1st of March following the reporting year. In this type of report contributors give information about their employees (number of employees have, employees' salary and so on).

Mechanisms for reporting

All categories of social contribution payers shall submit two separate reports to the SSPF (except employees whose reports are submitted by their employers): 1) a quarterly report, which is only indicating the monthly salary or revenue or royalties of the payer(s) and amount of the social contribution paid; 2) an annual report, which is analogous to the quarterly one but on an annual base. In this case, employers should include information about all their employees.

Reports are submitted electronically via internet using specific software developed by the SSPF. The transcription of the data into the personal accounts is automated.

Audits and inspections

Inspections are carried out in governmental institutions, private enterprises and at self-employed persons' offices.

For governmental institutions and big enterprises, the focus is the verification of the social contributions paid to the SSPF compared to the records in their respective bookkeeping. The data is manually analysed, which makes these audits time-consuming.

The inspections of the self-employed persons are focused of non-payment of the social contributions.

The regional offices of the SSPF carry out the inspections of both physical and legal entities. The central administration of the SSPF only deals with inspections of large insurance-payers and legal entities.

The control activities – audits/inspections - are divided into two parts: planned and unplanned controls. All control activities, which are planned for the following year, must be registered in a special system administered by the Ministry of Justice. Unplanned controls can only be carried in concrete justified cases.

The SSPF bases its control activities on a very basic assessment. Currently there is no department, within the SSPF, in charge for a risk assessment development or a risk assessment system. E-audit techniques are also very basic and the laws regulating the audit process do not enable implementation of different techniques and tactics.

The State Social Protection Fund conducts its audits on-site, in the offices of the insurers. 2,402 preeminent and medium scale insurers were monitored on-site in 2014.

Forecast and budget preparation in the SSPF

The Forecasting Department is responsible for forecasting and budget preparation.

Budget estimation of the SSPF is based on data and social-economic forecasts of other Ministries (Ministry of Economy and Industry, Ministry of Finance, State Statistical Committee) and on data analysis of the insurance-pension system. The SSPF budget is approved by the Parliament annually. The budget is balanced by the transfers from state budget.

(See a graphic illustration of the budgeting process in Annex 5).

Strategic planning

In order to define the prospective development priorities of the insurance-pension system, a forecast based on actuarial calculations, is carried out by the Actuarial Investigations Division under the Forecasting Department, which is a structural unit (established on 12 November 2014) of the State Social Protection Fund's Administration

The SSPF has launched a multi-functional action plan aimed at implementing measures set out in the "Concept of reforms of pension provision system in the Republic of Azerbaijan in 2014-2020". This concept concerns the long-term financial sustainability of the pension provision system and defines the development priorities of the insurance-pension system according to long-term econometric models based on multi-parametric actuarial projections. It is planned to apply the PROST model to the insurance-pension system in Azerbaijan jointly with the World Bank and to organize training courses on actuarial calculations for the SSPF staff. The PROST model identifies (i) the future pension provision to the insured persons, (ii) financial sustainability of the pension system in a long-term perspective, income and expenses of the system, (iii) the factors that may have an impact on future provision of pensions to the insured persons, and (iv) plays a major role in conduction of quantitative and qualitative analyses for the pension system. Life expectancy of the population, future macroeconomic indicators of the economy, changes in future pension amount of the insured persons by considering international trends, amount of both contributory and non-contributory pension liabilities, as well as the number of future pensioners and insured persons are projected by using the PROST model.

In order to prepare actuarial analysts and strengthen their professionalism, training courses on actuarial calculations were provided to the SSPF staff jointly with the Association of Insurance Companies. Evaluation of the ability and liabilities to pay life insurance, as well as training in statistical and practical methods of measuring loss reserves and assessing the distribution of losses in the cases of loss of ability to work were the key objectives of the training courses.

3.1.2 Problems (direct and indirect) to be addressed

Azerbaijan faces the need to adapt its social protection systems to ever-changing economic, demographic and social environments.

SSPF Budget encompasses social expenditure and income. On the expenditure side, core elements include, among others: employment-related social security expenditure on: pensions; temporary incapacity to work; maternity benefits; benefits for child care up to 3 years old; funeral benefits; unemployment benefits; and publicly financed social protection expenditure on: full or partial payment of sanatorium/recreation treatment of the insured including their travel expenses; staff running costs, medical service, food costs in sanatorium/recreation facilities. The income side accounts for all resources used to finance the above expenditure. The most important are social security contributions and public budget transfers.

The main factors that affect the financial sustainability of SSPF are (i) pension liabilities for the period of before 1992, (ii) additions to pensions and (iii) other liabilities which are not directly linked with social insurance contributions.

Existing legal framework on SSPF budget protection process and the international practice in this field should be analysed. Legal aspects of introducing new methodologies and rules for improving budgeting should be evaluated.

It is very important to study in a well-coordinated manner the changes of macroeconomic and demographic indicators and those ones defining the work of the system itself.

Within the framework of the Twinning project, the recommendations to be provided on the integration of actuarial calculations to the SSPF budget preparation process through identification of current institutional and technical aspects of the SSPF budget preparation process, in particular short- and medium-term forecast of income and expenditure, and simulations of expenditures and revenues under alternative economic, demographic and/or legislative assumptions.

SSPF has come a long way in modernizing its controls functions. However presently, inspections by SSPF fail to cover all medium and large insurers, also take much time and human labour. In this regard, the application of e-audit in the mandatory state social insurance will create real opportunities to shorten time spent on audits and immediately reveal cases of evasions, and allow to cover all medium and pre-eminent insurers and eliminate existing problems in this area.

The current legislation does not cover rules for implementing an electronic fiscal control (e-audit) of insurers; mechanisms do not exist for keeping electronically bookkeeping documents by insurers (especially for the purpose of insurance issues), for transferring this data to the e-audit software and other proceedings.

With the support of the project, the legal basis should be developed for the implementation of modern electronic audit techniques and methods to enable optimal collection of social contributions to the budget.

The SSPF lacks of implementation of modern risk management approaches such as compliance risk management within the audit, effective case selection process, evaluation and feedback to gain effectiveness and efficiency in the administration operations. Within the administration there is no department who is responsible for developing a risk management system. The project should raise skills and competence of the SSPF personnel in relevant fields, such as:

- Risk management - compliance risk management within the audit, effective case selection process, evaluation and feedback,
- Use of modern audit methods and techniques,
- E-audit methodologies, implementing e-audit tools.

The existing ratio between actors of the insurance and pension system is not sufficient (about 2.39 insured persons per pensioner). This is due to factors, which are common to many other countries: (i) abundance of undeclared jobs, which excludes many from benefiting of the social protection and reduces contribution to the system; (ii) a constant increase in life expectancy and growing share of population aged 65, which would create additional pressure for the pension system in the next two decades.

Harmonization of mandatory and voluntary social insurance systems with the country's socio-economic development, as well as building and strengthening capacity enabling to define the long-term development priorities of these systems are among the tasks of the State Social Protection Fund for the next period.

Legal aspects and practice of organization of strategic planning mechanisms of mandatory and voluntary insurance systems in accordance with the international practice should be studied and the need to improve the existing legal framework and practice evaluated.

In this regard, the project should create the ground to increase the efficiency and effectiveness of the professional capacity of SSPF for formation of conceptual framework and mechanisms for organization of strategic planning of mandatory and voluntary insurance systems process based on the European best practice, increase knowledge and skills of the staff in the relevant areas is of special importance.

Capacity strengthening needed to assess the long-term impact of various factors, in terms of interdependence of economic and social development in the country; to introduce mechanisms and tools to adjust rights and privileges available in the insurance-pension system to the demographic indicators. The Twinning project will support to develop scenarios including the cost of reform that will enable SSPF to propose political choices on how to reform the mandatory and voluntary social insurance systems.

3.2 Linked activities

The SSPF has built up a long track record on technical assistance and cooperation with international finance institutions and donors.

3.2.1 Other related EU activities

- **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"** (April 2014 – ongoing until November 2015)
This Twinning project aims at enhancing the capacity of the SSPF to establish the regulatory, legal and administrative framework for the introduction of a funded element in the insurance-pension system and the establishment of non-state pension.

The project has to achieve the following 5 results:

Component I

- Relevant pieces of legislation elaborated for establishment of the funded component in the state insurance-pension system.
- Technical description of the mechanism for accumulation and management of the funds on the individual real funded accounts provided.

Component II

- Relevant legal framework to organize the process of establishment of non-state pension funds elaborated.
 - Capacity of the relevant SSPF staff enhanced through training and coaching to ensure effective launch and implementation of the funded component in the state pension system and to play a role (which role remains to be decided) in creating a market for non-state pension funds.
 - A communication strategy elaborated to raise public awareness concerning the new funded component of the state pension system and the newly created market of private pension funds.
- **“Support to the Ministry of Taxes of the Republic of Azerbaijan in the field of Computer Assisted Audit System” (27 months, 2011-2013)**

The purpose of this Twinning project was to improve the capacity, tools, and work of the Ministry of Taxes (MOT) in the field of electronic audit (e-audit).

3.2.2 Related international initiatives

- **UNDP project “On capacity building for the State Social Protection Fund of Azerbaijan Republic” (2003-2012):**

The project elaborated the methodological, technological and legal basis for the establishment, introduction and administration of the personal accounts system, developed and conducted special training courses for SSPF’s structural units to ensure the transition to this system.

- **World Bank “Pension and Social Assistance Project” (2005- 2009):**

Within the “Capacity building for the management of social insurance system” project’s component, the pension legislation was improved, the activities for the implementation of the personal accounts system were rapidly performed, the programme-technical system for the implementation of the automated management system within the insurance-pension system was prepared, training courses and seminars on the essential principles of individual accounts were held.

- **World Bank “Social Protection Development project” (2009- 2013)**

It assisted the SSPF through its Component 3 (Pension system development), in (i) performing a comprehensive analysis of the current pension system, including actuarial analysis of its affordability and fiscal sustainability and an analysis of individual welfare consequences for different types of its participants (formal sector employees, farmers, arrangements for informal sector workers, average, high and low income earners, etc.) - *this analysis also included a thorough assessment of the economic and institutional preconditions for the diversification of the pension system* -; and (ii) formulating options for the long term development of the pension system and modelling their fiscal and welfare consequences.

3.3 Results

One prerequisite for developing a system of governance for the social sector is to know what the present overall level of expenditure is, where monies are spent, where needs are unmet, and how the overall national social expenditure and the financial burden for the different financiers of the systems (employers, workers and the government) would develop under different economic scenarios and under different reform options.

Restoration of the market economy relations in Azerbaijan and moving forward to a qualitatively new phase in social and economic development contribute to further rise of the population’s well-being based on mechanisms complying with international standards. In its turn it necessitates comprehensive development of the insurance and pension system that will interlink economy and social sphere of the country.

The project will have 3 main results:

Result 1: Automated fiscal control (e-audit) system developed and tested.

Description

The audits carried out in the SSPF do not cover all the range of methods and techniques for determining and verifying the persons who are liable to pay social contributions. Detecting and deterring non-compliance requires more than a mere examination of a business’s books and records and necessitates an analysis of the business’s financial affairs and modern tactics to collect evidence to correctly assess the social contribution liabilities. The project will help the SSPF in determination and development of an automated audit and risk management systems including the legislative issues, IT support, and software selection based on the best practices and

standards in the EU member states. The project will prepare an appropriate action plan for the implementation of an e-audit for compliance risk management within the audit, effective case selection process, evaluation and feedback. Its methodology will be developed after comparing various systems and will give a recommendation on the software most suitable. A guideline for automated audit will be produced based on the used software and on the experience built during trainings and audits carried out.

Key output indicator(s)

- Presentation of at least two examples of EU Member States modern automated audit system for social insurers
- Review of current legislation and procedures and recommendations on amendments of relative legislation for the implementation of e-audit in Azerbaijan
- Recommendations for development of an appropriate e-audit system for Azerbaijan
- Appropriate e-audit methodology implementing modern e-audit tools, methods and techniques in place
- Recommendations for standardization of e-accounting systems to meet data conversion requirements of e-audit software
- Technical specification of relevant software to meet the needs of the SSPF
- Data collection instruments to gather elements critical for operation of new e-audit system
- New database with all necessary information, including rating scores and list of high risk insurance payers for different industries, segments, regions, known schemes of evasions from closed cases, etc. in order to properly function
- Action Plan with benchmarks of quality, quantity and time prepared to monitor implementation of e-audit system
- Adapted appropriate risk management system including risk assessment measures for current controls
- Practical Guide developed on adapting automated audit methodology and techniques can be effectively used by the relevant staff of the SSPF
- 5-10 SSPF staff with good IT knowledge and skills trained as auditors using the relevant software
- SSPF trainees perform pilot computer audits under supervision by STE to ensure their capacity
- Internship organised to EU Member State for up to 5 SSPF audit trainees to work alongside auditors in EU country and encompass the study of other electronic means and in equipment that MS use in audits

Result 2: *Institutional and technical aspects of budget formulation process at SSPF improved*

Description

Special attention will be focused on learning international experience on making actuarial analysis for SSPF budget projection. For this reason it is very important to study in well-co-ordinated manner changes of macroeconomic and demographic indicators and those ones defining work of the system itself. Introducing relevant mechanisms will be ensured in order periodically to bring additional rights and privileges available in the system in line with demographic indicators. The project will help SSPF to assess current institutional and technical aspects of budget formulation process and will draw recommendations to improve the current situation. The project will provide international experience with particular focus on emerging countries or post-Soviet states where budgeting process has advanced. The project will draw recommendations how to integrate actuarial work in the budget process and these recommendations will be implemented.

Key output indicator(s)

- A strategic development plan for Forecasting department of SSPF including organisational setting of the Department with a clear cut assignment of tasks and matching job descriptions
- Comparative assessment of general standards, policies and methods used for actuarial calculations, monitoring, data analysis and forecasting used in European countries and recommendations on their adaptation to the SSPF needs, underlying IT-structure
- Recommendations on improvement the institutional and technical aspects of budget formulation process at SSPF
- Recommendations on integration of actuarial calculations and forecasting in the budget formulation process at SSPF
- State-of-the-art methods for actuarial calculations, data analysis, forecasting, monitoring, evaluation, and budgeting according to European best practice, which are adapted/custom-tailored to SSPF needs
- Concept paper for IT-requirements and possible IT-architecture for budgeting purposes at SSPF and a specific actuarial software model, with technical specifications for IT-service procurement (procurement is not a part of the project)
- Training of the staff of SSPF in using the budgeting model, the selected actuarial model, monitoring and evaluation methods
- New/revised formats and templates for data collection and exchange
- At least 5 staff members of the Forecasting department of SSPF completed the Training of Trainers courses to conduct training classes for other personnel on new actuarial models and budget forecasting methodologies

Result 3: *Mechanisms for the strategic planning of the mandatory and voluntary social insurance systems strengthened based on European best practice*

Description

It is necessary to establish mechanisms that will design relevant proposals with consideration of all factors such as: turning of pensions paid before introduction of the new system, pension rights gained by the insured during functioning of the previous system, supplement payments for seniority as well as other payments not based on social insurance principles into additional financial burden for the system; amount of state budget allocations required to attain social targets set out by the state; funding demands expected in future as a result of introducing personal accounting in the mandatory state social insurance system; compliance of social insurance rates with growing financial demands; and studying other issues in well-co-ordinated manner. To this end, capacity to carry out strategic planning in the insurance-pension system should be made available and strengthened. Furthermore, the strategic planning capacity enabling to define the long-term development priorities of mandatory and voluntary insurance systems through harmonization with the country's socio-economic development should be enhanced. The conceptual framework and mechanisms should be formed in this field in accordance with the international practice taking account the modern requirements. Global processes and challenges, the analysis and study of interdependence between country's economic and social development and other factors, building and strengthening the necessary capacity to carry out investigations in order to assess the long-term impact of all this aspects on strategic planning of mandatory and voluntary insurance systems are of special importance. The project will provide technical assistance and capacity building for the strengthening of strategic planning mechanisms of the mandatory and voluntary social insurance systems for the staff of SSPF.

Key output indicator(s)

- Presentation of at least two examples of strategic planning of mandatory and voluntary social insurance systems in EU Member States
- General standards, policies and methods of strategic planning of mandatory and voluntary insurance systems based on European best practice adapted/custom-tailored to the SSPF needs
- Recommendations on organizational set up for strategic research and analyses in the area of mandatory and voluntary insurance at the SSPF
- Analysis and recommendations on introduction of global indices in the mandatory and voluntary insurance in Azerbaijan
- Recommendations on capacity building for strategic planning of mandatory and voluntary insurance systems at the SSPF
- At least 10 staff members of the SSPF completed the training and qualified to apply the strategic planning mechanisms for the mandatory and voluntary social insurance systems

3.4 Activities

In order to meet the specific mandatory results of this project, the partners may agree on alternative or complementary activities and outputs to those identified in this section.

Project kick-off event

A meeting aiming at presenting the Twinning project to the main involved stakeholders shall take place at the beginning of the project implementation.

Thematic mid-term project visibility event

A workshop aiming at communicating on the project achievements and raising awareness shall take place at the end of first year of the project implementation.

Project closing event

A conference shall present the main results achieved during the project implementation and shall be organised before the conclusion of the project.

Activities related to Result 1:

- Activity 1.1 Develop a legal basis for e-audit
- Activity 1.2 Develop an e-audit database
- Activity 1.3 Develop a risk management system
- Activity 1.4 Develop the risk assessment measures for current controls
- Activity 1.5 Identify and develop an appropriate e-audit system for SSPF meeting European best practice standards
- Activity 1.6 Implement a pilot e-audit
- Activity 1.7 Enhance knowledge transfer and skills in using the relevant software

Activities related to Result 2:

- Activity 2.1 Review existing budget formulation process as well as actuarial work with the budget process
- Activity 2.2 Workshop(s) to present best European practice of budget process drawn, actuarial calculations methods, data analysis, forecasting, social budgeting as well as the findings of the analysis of the current situation at the SSPF
- Activity 2.3 Develop the customized methods to budgeting and providing the SSPF with methods to develop actuarial models

- Activity 2.4 Prepare a strategic development plan for Forecasting department including a new organisational set-up, workflow and job descriptions
- Activity 2.5 Define the reporting obligations for Forecasting department
- Activity 2.6 Development of new/revised formats and templates for data collection and exchange
- Activity 2.7 Enhance knowledge transfer and skills

Activities related to Result 3:

- Activity 3.1 Review existing strategic planning mechanisms for mandatory and voluntary social insurance systems at the SSPF
- Activity 3.2 Capacity building to carry out strategic planning at the SSPF
- Activity 3.3 Organise Workshop(s) to present best European practice of strategic planning for the mandatory and voluntary social insurance systems as well as the findings of the analysis of the current situation in Azerbaijan
- Activity 3.4 Improve the strategic planning mechanisms for the mandatory and voluntary social insurance systems
- Activity 3.5 Investigation and analysis of the issues concerning the introduction of global indices of mandatory and voluntary insurance in Azerbaijan
- Activity 3.6 Enhance knowledge transfer and skills

Note: The various activities, benchmarks, schedules and means of verification may be subject to revision during the preparation of the contract between the Twinning Institutions.

3.5 Means/ Input from the MS Partner Administration

The MS partner administration is expected to provide the Project Leader (MS PL) and Resident Twinning Advisor (RTA) as well as a team of short term experts to support them in implementation of the project activities.

The MS PL is the key link between the partners, acting at an overall operational and strategic level. The RTA is seconded to the BC administration and resides in the BC. He co-operates day-to-day with the BC partners and coordinates the input of the MS short-term experts (STEs).

It has proved to be an advantage for the project implementation in previous Twinning projects when the MS has designated a senior STE to be responsible for each mandatory result/component of the project (i.e. a component leader) and to liaise with the respective component leader to be nominated by the BA. The BA will nominate counterparts to these key roles (see section 6.3).

The required MS experts must either be civil/public servants of the relevant MS administration or be permanent staff of authorised mandated bodies. All experts must comply with the requirements set in the Twinning Manual.

The nature of work for technical assistance abroad requests strong initiative, good analytical, interpersonal and language skills. All experts shall possess these qualities.

The RTA will be supported by a permanent RTA Assistant. In collaboration with the BA, the RTA assistant will handle administrative arrangements for conferences, training, seminars, etc. including provision of interpreters and the ensuring the translations. One assistant will be selected during the Twinning contract preparation period.

A full-time interpreter/translator will also be recruited in Azerbaijan and funded by the project. (S)he will perform most of the required interpretation/translation services. Whenever required and needed on a clear justified request, e.g. for simultaneous interpretation during seminars and workshops, additional interpretation as well as translation may be procured and funded by the project. (S)he will provide day-to-day interpretation/translation to the RTA and project experts during meetings.

3.5.1 Profile and tasks of the Project Leader (PL)

The Project Leader (PL) from the MS should be a high-ranking civil servant or an equivalent senior manager in a MS national social protection body with a work experience in the field relevant to the project.

The PL will supervise and coordinate the overall thrust of the project. (S)he will direct the project and will ensure that all the required strategic support and operational input from management and staff of the MS side are available. Together with the Beneficiary PL, he/she will organise the Project Steering Committee (PSC) meetings. **The MS PL would continue to work in her/his MS administration but should devote a minimum of three working days per month to the project in Azerbaijan with an on-site visit to Azerbaijan at least every three months to participate in the project SC meetings.**

Profile:

Qualification and skills

- University degree in law, economy, public administration or equivalent
- Familiarity with current EU-policies, existing structures and methods in the field of the project;
- Experience in project management, demonstrating good record in organisational leadership, staff motivation, and communication;
- Good command of written and spoken English

General professional experience

- Minimum 7 years of professional experience at a senior management level in her/his MS public service in the Social Protection sector
- Experience in social policy development

Specific professional experience

- Minimum 10 years of experience in the field of social protection system or 5 years of experience directly related to one of the project components;
- Experience in control of social insurers would be an asset;
- Specific experience in the management of the implementation of international instruments would be an asset;
- Experience in EU funded projects would be an asset.

Tasks:

- Liaising with the BC Administration at the political level
- Overall co-ordination, guidance and monitoring
- Ensuring the direction of the project work
- Ensuring the achievement on time of the mandatory project results
- Ensuring the availability on time of MS-Short Term Experts and other MS resources
- Executing other administrative tasks

3.5.2. Profile and tasks of the Resident Twinning Advisor (RTA)

The Resident Twinning Advisor (RTA) seconded from the EU MS should have at **least five years' work experience as a staff member in a MS Agency** working directly in the field of controlling social insurers. A network of functional contacts with related EU and Member State institutions will also be an asset. The RTA will be in charge of the day-to-day implementation of the Twinning project in Azerbaijan. (S)he should co-ordinate the implementation of activities according to a predetermined work plan and liaise with the RTA counterpart in Azerbaijan. **(S)he will reside for the entire implementation period of 24 consecutive months in Azerbaijan and work full-time for the project.** The RTA is expected to be actively involved in the implementation of all activities. (S)he should co-ordinate all components of the project.

Profile:

Qualification and skills

- A University degree in Social Protection, Economics or another relevant discipline
- Familiarity with current EU-policies, existing structures and methods in the field of the project
- Good command of written and spoken English

General Professional Experience

- Minimum 5 years' experience in the Social Protection sector
- Experience in managing teams of experts
- Experience in developing and conducting training programmes would be an asset

Specific Professional experience:

- Minimum 3 years' experience in e-audit or data analyses/actuarial calculation processes or strategic planning for mandatory and voluntary social insurance systems
- Familiarity with current EU-policies, existing structures and methods in the pension provision sector
- Knowledge of the institutional environment relating to the implementation and enforcement of EU legislation in the social protection field

Tasks:

- Day-to-day coordination and implementation of the project activities in Azerbaijan
- Managing the input of short-term experts
- Arranging study tours to MS countries for the staff of the SSPF and other involved administrations
- Substantial provision of own expertise
- Ensuring the coherence and the continuity of the inputs and the on-going progress
- Assessing continuously the Twinning-project at all stages and comparing actual progress with the specified benchmarks and time-frame
- Guaranteeing smooth implementation of the different activities;
- Liaising with the BC Project Leader and RTA Counterpart on regular basis
- Liaising with the EU Delegation and the PAO of Azerbaijan
- Preparing interim, quarterly and final reports

- Reporting to the MS-Project Leader

3.5.3 Profile and tasks of the short term experts (STEs)

All required EU institutional and technical expertise will be covered by the short-term experts. The short-term experts should have good experience in the relevant subject matter. The STEs should be civil servants or staff members of the selected MS institution(s). They should have worked in the required fields for not less than 3 years and have appropriate qualifications and necessary skills to implement the above mentioned activities.

The exact number of STEs per activity should be agreed upon during the contract negotiations. There should be a pool of short-term experts to ensure smooth implementation of the project. The STEs should be identified by the Project Leader/RTA and will be agreed with the Beneficiary Administration in the course of design and implementation of the project.

General requirements on STEs are the following:

- University degree in a relevant discipline or at least 5 years of equivalent work experience;
- Good interpersonal and communication skills;
- Computer literacy;
- Excellent command of written and spoken English;

Indicative fields of experience for the short-term experts:

- Insurance-pension system laws and regulations
- Insurance-pension system policies and strategies
- Expertise in development of risk analysis system and risk criteria
- Expertise in drafting legislation
- Expertise in developing software for e-audit
- Expertise in conducting e-audit
- Expertise in forecast and budgeting processes
- Expertise in the field of actuarial calculations
- Expertise in the field of the strategic planning mechanisms for the mandatory and voluntary social insurance systems
- Others (to be defined in the proposal and/or during the contracting phase)

STEs' main tasks:

- Provision of their specific expertise
- Know-how transfer according to the ToR prepared by the RTA and BA
- Reporting on their missions
- In addition to their missions in Azerbaijan, the STEs are expected to contribute actively in developing programmes for the study visits proposed in the project.

3.6 Reporting and monitoring

The MS Project Leader must draw up Interim Quarterly Reports and a Final Report. (S)he will be responsible for submitting them to the relevant authority.

For templates and requirements to reporting and monitoring, see the Twinning Manual.

Project Steering Committee (PSC)

The PSC will be convened at least every three months. The PSC will be chaired jointly by the MS PL and the BC PL. The PSC composition will be defined in the Working Plan according to requirements set in the Common Twinning Manual. Representatives from the PAO of the Republic of Azerbaijan and the EU Delegation, the RTA counterpart and BC PL as well as the RTA, MS PL and BC component leaders will participate in the PSC meetings. Observers from other institutions may be involved from time to time in cross-cutting issues. Representatives from other administrations or short term experts, may also be invited if necessary. The PSC will follow the achievement of the project results and the timely implementation of the project activities in order to identify and rectify any problems that may arise in the course of the implementation of the project.

The secretarial support of the PSC will be provided by the RTA and RTA Assistant, who will prepare the agenda of the meetings, the documents to be discussed as well as the minutes of the meetings.

The working language of the Project implementation will be English. Translation and interpretation will be provided where necessary and where permitted in the provisions of the Twinning Manual.

4 Institutional framework

4.1 Main Azerbaijani stakeholder

The State Social Protection Fund (SSPF) is state agency with responsibility for mandatory state social insurance and labour pensions in the Republic of Azerbaijan. SSPF collects social insurance contributions (social security taxes on wages) and administers payments of pensions and allowances within the framework of the state social insurance system.

4.2 Indirect Azerbaijani stakeholders

The Ministry of Labour and Social Protection of Population (MLSPP) is the executive state body carrying out the state policy on labour relations, occupational safety and health issues, using of labour resources, social protection of population, employment, the rehabilitation of peoples with disabilities. In regards to the proposed project, the Labour inspectorate under the MLSPP is in charge of registration and control of the labour contracts of all employees.

The Ministry of Taxes is the central executive body responsible for the implementation of national tax policies, timely and complete collecting tax payments and other returns and related government control. In regards to the proposed project, the Ministry of Taxes is in charge of registration of the economic entities (both legal and physical persons).

The Ministry of Finance is the central executive authority body carrying out the state finance policy and organizing the management of state financing. In regards to the proposed project, the Ministry of Finance balances the SSPF budget by transfers from the state budget.

4.3 Organisation of the Beneficiary Administration (BA)

Functions, Departments and Staff

The SSPF provides social protection types of benefits: old age pensions, survivor's benefits, disability benefits and benefits paid due to the mandatory state social insurance contributions.

The main functions of the SSPF are as follows:

- to develop proposals on the state policy directions in the sphere of social insurance and labour pension and participate in the implementation of this policy;
- to prepare the draft budget of SSPF and ensure the performance of the approved budget;
- to ensure collection of mandatory state social insurance contributions in the amount set under the legislation from entities, organizations, institutions, their branches and representatives

irrespective of their form of incorporation and ownership with a status of a legal person established in accordance with the legislation of Azerbaijan Republic or foreign state, and individuals (insurers) engaged in private enterprise as well as from the insured;

- within its powers to exercise control over fulfilment of legislative requirements in the area of mandatory state social insurance, labour pensions as well as the duly utilization of these funds;
- to implement the financing of all labour pensions in the country out of the mandatory state social insurance funds and state budget funds;
- to ensure financing of the following expenses out of the mandatory state social insurance funds:
 - in accordance with the Law of Azerbaijan Republic “On labour pensions” - the labour pensions;
 - on the basis of voluntary (supplementary) social insurance – supplements to the state pensions;
 - temporary disability pensions (for the periods established under the legislation);
 - pregnancy and child-delivery benefits;
 - lump-sum child-birth grants;
 - child-care allowances up to the age limit provided under the legislation;
 - full or partial payment of spa treatment of the insured;
 - unemployment benefits;
 - death grants;
- within the limits of legislation to implement activities promoting SSPF's regular financial solvency;
- to ensure timely calculation and payment of mandatory state social insurance contributions;
- to ensure the introduction of the personal accounts in the system of state social insurance;
- to ensure timely and accurate input in the personal accounts of the data submitted by the employer and the insured, its safe storage and security;
- upon the request of the insured to clarify the rules of disclosure of information on his personal account;
- to disclose the data on the personal account of the insured applying for pension assignment;
- to provide explanations with regard to the introduction of the personal accounts in the social insurance system and to pass the respective normative acts within its delegated powers;
- to implement other duties provided for under the legislation.

The Central Administration of the SSPF consists of 13 departments (see Annex 2). The Department of Current Control over the Insurance Incomes, Audit units of the Department for work with preeminent insurers and Baku Department for work with legal entities, Income units of the Department for work with military personnel and persons with special ranks and income units of local offices implement the functions of audit in the insurers.

Number of employees (excluding support staff) is as follows:

SSPF total – 3,045 persons, of which Central Office - 284 persons

The direct beneficiary/s will be the Forecasting Department which is in charge for budget preparation and actuarial modelling, IT department in charge for IT support and IT infrastructure management process at SSPF, Finance department in charge of revenue consolidation and financial

planning and Personal Accounting Department which is in charge of registration of personal accounts.

5 Budget

The maximum budget allocated to this Twinning project is €1,200,000

The Azerbaijan beneficiary administration will provide the RTA and other MS experts with office space in its main building in Baku, equipment and other provisions as stated in the Common Twinning Manual.

6 Implementing arrangements

6.1 Implementing Agency responsible for tendering, contracting and accounting

The Implementing Agency responsible for tendering, contracting and accounting is the European Commission represented by the **Delegation of the European Union to the Republic of Azerbaijan**. Its contact details are:

Delegation of the European Union to the Republic of Azerbaijan

Landmark III, 11th Floor, 90A, Nizami str.

AZ 1010 Baku, Republic of Azerbaijan

Tel. +994 12 497 20 63

Fax +994 12 497 20 69

E-mail: DELEGATIONAZERBAIJAN-FINANCE@eeas.europa.eu

Website: <http://eeas.europa.eu/delegations/azerbaijan>

6.2 Main counterparts in the Beneficiary country

Programme Administration Office in Azerbaijan (PAO) will support the twinning project implementation process. The person in charge of this project at the PAO is:

Mr. Ruslan RUSTAMLI, Director of PAO

Head of the Department on Cooperation with International organizations

Ministry of Economy and Industry of the Republic of Azerbaijan

6th floor, Government House,

84 Uzeyir Hajibayli str.

Baku, AZ 1000

Republic of Azerbaijan

Tel.: (+994 12) 493 88 67 (ext. 2115)

Fax: (+994 12) 598 85 19

E-mail: ruslan.rustamli@economy.gov.az

Website: <http://pao.az>

Ms Narmin ALASGAROVA, PAO Manager

Department on Cooperation with International organizations
Ministry of Economy and Industry of the Republic of Azerbaijan
6th floor, Government House,
84 Uzeyir Hajibayli str.
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Tel.: (+994 12) 493 88 67 (ext. 2304)
Fax: (+994 12) 598 85 19
E-mail: narmin.alasgarova@economy.gov.az
Website: <http://pao.az>

Beneficiary Administration – State Social Protection Fund

The Beneficiary Administration has nominated its main counterparts to the MS PL and RTA:

Project Leader – Mr Rufat Oruclu, Deputy Head

Forecasting Department
80 H. Zardabi avenue,
Baku, AZ 1122
Republic of Azerbaijan
Tel.: (+994 12) 4345786
E-mail: rufat.orucli@sspf.gov.az

RTA counterpart –Ms Taliya Shikhlinskaya, acting Leading advisor

Finance Department
80 H. Zardabi avenue,
Baku, AZ 1122
Republic of Azerbaijan
Tel.: (+994 12) 4345794
E-mail: taleya_s@mail.ru

During the contracting phase of the project, the beneficiary administration will nominate leaders for each result.

6.3 Contracts

One Twinning contract is foreseen for this project.

A new Financial Regulation applicable to the general budget of the European Union entered into force on 1st January 2013⁴. This implies several changes to the Twinning contract templates. An updated version of the Twinning Manual and of its Annexes, incorporating these changes, is in preparation and shall be published soon on EuropeAid website⁵. The Twinning contract, which shall be signed as a result of the present procedure shall follow the templates of the updated Twinning Manual and Annexes.

7 Implementation schedule (indicative)

7.1 Launching of the call for proposals: October 2015

7.2 Start of project activities: September 2016

7.3 Workplan duration: 24 months

8 Sustainability

The Twinning project will have to seek sustainable solutions and approaches based on the adoption of best practices and thus prepare the grounds for Azerbaijani enhanced compliance with the selected EU Acquis and specifically best European practices in the field of Social Protection.

Sustainability issues will be further elaborated in the course of the preparation of the project contract as a joint responsibility of the MS partner and the Beneficiary Administration. Besides, in the final report, twinning partners will include specific recommendations and strategies for consolidating and safeguarding the achievement of mandatory results in the beneficiary administration.

To ensure sustainability, Beneficiary Administrations should be provided with the training materials (all handovers) in both languages, English and Azerbaijani. That means that a budget for the translation of Guidelines, Handbooks, Glossaries, Methodology Manuals, etc. developed within the project should be foreseen.

9 Cross-cutting issues

9.1 Equal opportunity

The proposed project will comply with EU equal opportunity policies. Equal treatment of women and men in project implementation at all levels will be one of the most important principles in the project management and implementation. The beneficiaries are already equal opportunity employers. In particular, great attention will be given to the equality principle in the training of personnel and the recruitment of the STEs. Of course, appropriate professional qualifications and experience will be the main decisive factors in personnel recruitment and evaluation but, subject to that, both women and men will have identical prospects.

9.2 Environment

The principle of implementation of this Twinning project is based on a paperless work environment. This means, in particular, minimising paper use during project implementation by the maximum

⁴ Financial Regulation: Regulation (EC, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002.

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:298:0001:0096:EN:PDF>

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:362:FULL:EN:PDF>

⁵ Rules of Application: Commission Delegated Regulation (EU) No 1268/2012 of 29 October 2012 on the rules of application of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union.

http://ec.europa.eu/europeaid/where/neighbourhood/overview/twinning_en.htm

feasible use of e-mails and, if available, project web-site and/or project electronic data base for co-operation between partners. Documents are automatically saved in electronic format.

10 Conditionality and sequencing

An open and constructive cooperation by the SSPF staff members involved in the project will be critical to make the Twinning project a success. Furthermore, support from the SSPF leadership as some elements of the project are sensitive in nature.

List of the abbreviations

AP	Action Plan
AZN	Azerbaijani manat, (currency code for the currency of Azerbaijan)
BA	Beneficiary Administration
BC	Beneficiary Country
ECD	European Commission Delegation
ENP	European Neighbourhood Policy
ENP AP	European Neighbourhood Policy Action Plan
ENPI	European Neighbourhood and Partnership Instrument
EU	European Union
GDP	Gross Domestic Product
HR	Human Resources
IT	Information Technologies
MS	Member State
MS PL	Member State Project Leader
NIP	National Indicative Programme
PAO	Programme Administration Office
PCA	Partnership and Cooperation Agreement
PSC	Project Steering Committee
RTA	Resident Twinning Adviser
SIGMA	Support for Improvement in Governance and Management
SSPF	State Social Protection Fund of the Republic of Azerbaijan
STE	Short Term Expert
TAIEX	Technical Assistance and Information Exchange Instrument
ToR	Terms of Reference
UNDP	United Nations Development Programme

ANNEXES

1. Logical framework matrix in standard format
2. SSPF Organigramme
3. State Programme on Development of the Insurance-Pension system in 2009-2015
4. Concept on Reforms of the Pension Provision system in 2014-2020
5. Graphic illustration of the budgeting process

ANNEX 1: Logical Framework Matrix*

Support to the State Social Protection Fund in reforming pension system in Azerbaijan.		Programme name and number: AZ/15/ENP/SO/38 ENPI AAP 2012	
State Social Protection Fund of the Republic of Azerbaijan		Contracting period expires:	Disbursement period expires:
		Total budget: 1.2 million EUR	
	Objectively Verifiable Indicators	Sources of Verification	Assumptions
Overall objective:			
To contribute to further reforms of the pension provision system in Azerbaijan in compliance with best European practices	<ul style="list-style-type: none"> • Positive assessment of the pension reform by local and international organisations • Policy making of the SSPF is based on precise actuarial information and budget forecasting • Due to exact budget forecasting the deviation between planned/collected social contributions is reduced 	<ul style="list-style-type: none"> • EU ENP Progress Report • World Bank reports on country's progress • Annual reports of the State Social Protection Fund • Statistical Yearbook 	
Project purpose:			
To improve the capacity, tools and efficiency of the State Social Protection Fund of the Republic of Azerbaijan (SSPF) to develop and implement an automated fiscal control (e-audit) system; to strengthen the institutional and technical aspects of the budgeting as well as the strategic planning mechanisms of the mandatory and voluntary social insurance systems	<ul style="list-style-type: none"> • A new automated fiscal control (e-audit) system is in place • The SSPF applies state-of-the-art methods for actuarial calculations, data analysis and budget forecasting • The SSPF is able to implement the new strategic planning mechanisms of the mandatory and voluntary social insurance systems 	<ul style="list-style-type: none"> • EU ENP Progress Report • Annual reports of the SSPF • Decisions by the Government of the Republic of Azerbaijan • Decisions of the SSPF Chairman • Project Interim Reports • Project Final report 	<ul style="list-style-type: none"> • The Government of Azerbaijan supports the proposal of the SSPF for the pension reform • Possible institutional changes do not affect the existing roles and responsibilities of related institutions and departments • Adequate financial resources are allocated to ensure solid backing of the pension reform • SSPF retains its key staff who possess relevant knowledge, competences and skills to continue working on the pension reform • Strong commitment and support of SSPF management to the Project implementation

Mandatory Results:			
<p>1. Automated fiscal control (e-audit) system developed and tested</p>	<ul style="list-style-type: none"> • At least 2 examples of EU Member States modern automated audit system for social insurers presented • Report with recommendations on amendments of relative legislation for the implementation of e-audit in Azerbaijan prepared and accepted by beneficiary • Report with recommendation made for development of an appropriate e-audit system for Azerbaijan prepared and accepted by beneficiary • Appropriate e-audit methodology implementing modern e-audit tools, methods and techniques in place • Report with recommendations made for standardization of e-accounting systems which meet data conversion requirements of e-audit software prepared and accepted by beneficiary • Technical specification of relevant software to meet the needs of the SSPF developed and accepted by beneficiary • Data collection instruments to gather elements critical for operation of new e-audit system prepared • New database with all necessary information, including rating scores and list of high risk insurance payers for different industries, segments, regions, known schemes of evasions from closed cases, etc. in order to properly function developed • Action Plan with benchmarks of quality, quantity and time prepared to monitor implementation of e-audit system prepared and accepted by beneficiary • Adapted appropriate risk management system including risk assessment measures for 	<ul style="list-style-type: none"> • Assessment report with recommendations on how to improve a legal framework for the implementation of e-audit in Azerbaijan • Report with recommendations on how to develop an appropriate e-audit system for Azerbaijan • List of needed revisions of the legal & normative framework; • Recommended texts of revised laws, decrees & bylaws • e-audit methodology • Assessment report with recommendations on standardization of e-accounting systems • Technical specification documents for relevant software • List of data collection instruments • New database • Action Plan • Approved by the SSPF top manager(s) document on Risk Management system • Documents on a new risk management system • Practical Guide for 	<ul style="list-style-type: none"> • The SSPF has a good knowledge of best practises EU countries and different type of e-audit tools • Capacity of beneficiary is sufficient to absorb the projects results • SSPF establishes appropriate cooperation and information exchange links with other relevant institutions in the administration (e.g. Ministry of Finance, Ministry of Taxes, MLSP, etc.) • Collaboration and cooperation among the stakeholders are good • Strong involvement and commitment of SSPF staff at all levels • Sufficient staff at SSPF in terms of qualification, quantity and availability • Coordination between departments and institutions connected with the Project is ensured • Access to indispensable information and documents is ensured • Required data are available

	<p>current controls developed and accepted by beneficiary</p> <ul style="list-style-type: none"> • Practical Guide on how the adopted automated audit methodology and techniques can be effectively used by the relevant staff of the SSPF developed • 5-10 SSPF staff with good IT knowledge and skills trained as auditors using the relevant software • SSPF trainees perform pilot computer audits under supervision by STE to ensure their capacity • Internship to EU Member State for up to 5 SSPF audit trainees to work alongside auditors in EU country and encompass the study of other electronic means and in equipment that MS use in audits implemented 	<p>automated audit methodology and techniques</p> <ul style="list-style-type: none"> • Training modules on e-auditing • Reports on the delivered trainings • List of risk assessment measures • Scoping documents for the pilot project • Quality Report on the results of the pilot project • Pilot documentations • Reports on the internship with involvement of relevant SSPF staff • Quarterly progress reports 	
2. Institutional and technical aspects of budget formulation process at SSPF improved	<ul style="list-style-type: none"> • A strategic development plan for Forecasting department of SSPF including organisational setting of the Department with a clear cut assignment of tasks and matching job descriptions developed and accepted by beneficiary • Comparative assessment of general standards, policies and methods used for actuarial calculations, monitoring, data analysis and forecasting used in European countries, underlying IT-structure carried out • Report with recommendations on how to improve the institutional and technical aspects of budget formulation process at SSPF prepared and accepted by beneficiary • Report with recommendations on how to integrate actuarial calculations and forecasting 	<ul style="list-style-type: none"> • A strategic development plan • Comparative assessment report • Assessment reports with recommendations on how to improve the institutional and technical aspects of budget formulation process at SSPF • Assessment report with recommendations on how to integrate actuarial calculations and forecasting in the budget formulation 	<ul style="list-style-type: none"> • SSPF establishes appropriate cooperation and information exchange links with other relevant institutions in the administration (e.g. Ministry of Finance, Ministry of Taxes, MLSP, etc.) • Capacity of beneficiary is sufficient to absorb the projects results • Collaboration and cooperation among the stakeholders are good • Strong involvement and commitment of SSPF staff at all levels • Sufficient staff at SSPF in terms of qualification, quantity and availability • Coordination between departments and institutions connected with the Project is ensured

	<p>in the budget formulation process prepared and accepted by beneficiary</p> <ul style="list-style-type: none"> • State-of-the-art methods for actuarial calculations, data analysis, forecasting, monitoring, evaluation, and budgeting developed according to European best practice, which are adapted/custom-tailored to SSPF needs • Concept paper for IT-requirements and possible IT-architecture for budgeting purposes at SSPF and a specific actuarial software model, with technical specifications for IT-service procurement (procurement is not a part of the project) developed and accepted by beneficiary • At least 5 staff members of the Forecasting department of SSPF completed the Training of Trainers (ToT) courses on new actuarial models and budget forecasting methodologies • New/revised formats and templates for data collection and exchange are developed and accepted by beneficiary 	<p>process</p> <ul style="list-style-type: none"> • Documents on state-of-the art methods • Concept paper • Training modules on ToT courses on new actuarial models and budget forecasting methodologies • Reports on the delivered trainings • New/revised formats and templates for data collection and exchange • Quarterly progress reports 	<ul style="list-style-type: none"> • Access to indispensable information and documents is ensured • Required data are available
3. Mechanisms for the strategic planning of the mandatory and voluntary social insurance systems strengthened based on European best practice	<ul style="list-style-type: none"> • At least 2 examples of the leading EU Member States' strategic planning mechanisms for the mandatory and voluntary social insurance systems presented • General standards, policies and methods of strategic planning of mandatory and voluntary insurance systems developed based on European best practice adapted/custom-tailored to the SSPF needs • Report with recommendations on organizational set up for strategic research and analyses in the area of mandatory and voluntary insurance • Report with recommendations on introduction of global indices of mandatory and voluntary insurance in Azerbaijan 	<ul style="list-style-type: none"> • Documents on general standards, policies and methods of strategic planning of mandatory and voluntary insurance systems • Assessment report with recommendations on how to set up the strategic research and analyses in the area of mandatory and voluntary insurance • Assessment report with recommendations on how to introduce global 	<ul style="list-style-type: none"> • There is political will at the top management of the SSPF to promote introduction of the voluntary funded elements in the pension system and overall political support to the SSPF for the pension reform • SSPF establishes appropriate cooperation and information exchange links with other relevant institutions in the administration (e.g. Ministry of Finance, Ministry of Taxes, MLSP, etc.) • Collaboration and cooperation among the stakeholders are good • Strong involvement and commitment of SSPF staff at all levels

	<ul style="list-style-type: none"> Report with recommendations on capacity building for strategic planning of mandatory and voluntary insurance systems at the SSPF At least 10 staff members of the SSPF completed the training and qualified to apply the strategic planning mechanisms for the mandatory and voluntary social insurance systems 	<ul style="list-style-type: none"> indices of mandatory and voluntary insurance in Azerbaijan Assessment report with recommendations on how to increase capacity building for strategic planning of mandatory and voluntary insurance systems at the SSPF Training programme in applying the strategic planning mechanisms for the mandatory and voluntary social insurance systems Reports on the delivered trainings Quarterly progress reports 	<ul style="list-style-type: none"> Sufficient staff at SSPF in terms of qualification, quantity and availability Coordination between departments and institutions connected with the Project is ensured Access to indispensable information and documents is ensured Required data are available
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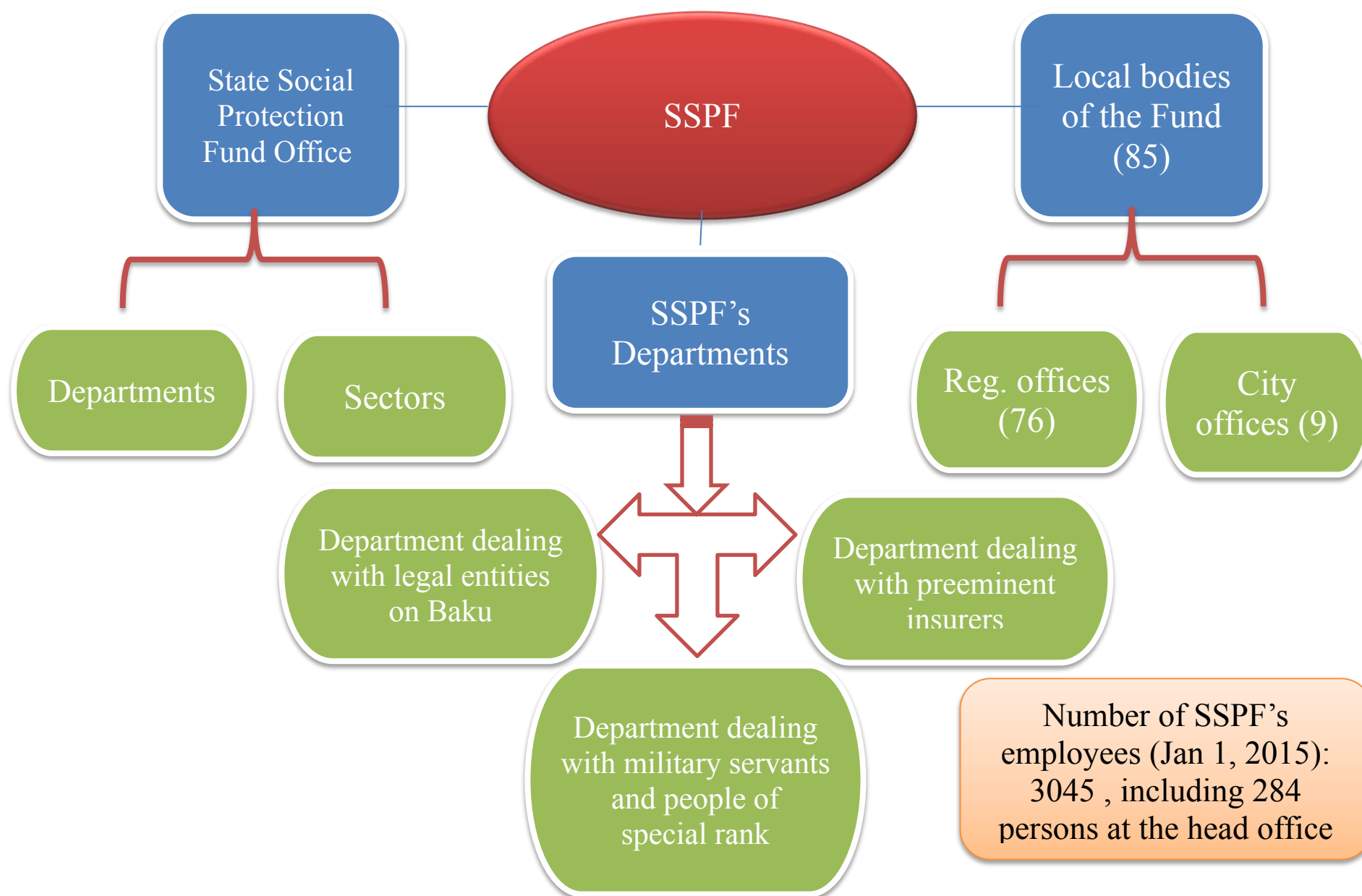
	Means	Costs	
Mandatory Result 0: Visibility actions			
0.1. Kick-off meeting			
0.2. Quarterly meetings of the Steering Committee			
0.3. Thematic mid-term project visibility event			
0.4. Final conference			
Mandatory Result 1: Automated fiscal control (e-audit) system developed			
1.1. Develop a legal basis for e-audit	RTA, STEs		
1.2. Develop an e-audit database	RTA, STEs		
1.3. Develop a risk management system	RTA, STEs		
1.4. Develop the risk assessment measures for current controls	RTA, STEs		

1.5 Identify and develop an appropriate e-audit system for SSPF meeting European best practice standards	RTA, STEs		
1.6 Implement a pilot e-audit process	RTA, STEs		
1.7 Enhance knowledge transfer and skills in using the relevant software	RTA, STEs		
<i>Mandatory Result II: Institutional and technical aspects of budget formulation process at SSPF improved</i>			
2.1. Review existing budget formulation process as well as actuarial work with the budget process	RTA, STEs		
2.2 Organise Workshop(s) to present best European practice of budget process drawn, actuarial calculations methods, data analysis, forecasting, social budgeting and strategic planning as well as the findings of the of analysis of the current situation at the SSPF	RTA, STEs		
2.3. Develop the customized methods to budgeting and providing the SSPF with methods to develop actuarial models	RTA, STEs		
2.4. Prepare a strategic development plan for Forecasting department including a new organisational set-up, workflow and job descriptions	RTA, STEs		
2.5. Define the reporting obligations for Forecasting department	RTA, STEs		
2.6. Development of new/revised formats and templates for data collection and exchange	RTA, STEs		
2.7. Enhance knowledge transfer and skills	RTA, STEs		
<i>Mandatory Result III: Mechanisms for the strategic planning of the mandatory and voluntary social insurance systems strengthened</i>			
3.1. Review existing strategic planning mechanisms for mandatory and voluntary social insurance systems at the SSPF	RTA, STEs		
3.2 Capacity building to carry out strategic planning at the SSPF	RTA, STEs		
3.3. Organise Workshop(s) to present best	RTA, STEs		

European practice of strategic planning for the mandatory and voluntary social insurance systems as well as the findings of the of analysis of the current situation in Azerbaijan			
3.4. Improve the strategic planning mechanisms for the mandatory and voluntary social insurance systems	RTA, STEs		
3.5. Investigation and analysis of the issues concerning the introduction of global indices of mandatory and voluntary insurance in Azerbaijan			
3.5. Enhance knowledge transfer and skills	RTA, STEs		

** - This Logical Framework Matrix is tentative. The Twinning partners shall revise the content of the Logical Framework Matrix, mainly measurable indicators / benchmarks basis of commonly agreed activities and outputs during the drafting of the work plan for this project*

ANNEX 2: Organigramme of the SSPF



ANNEX 3:

State Programme on the Insurance and Pension System Development for 2009-2015

1. General Provisions

1.1. Current Situation

Reconstruction of citizens' pension provision in our country on the basis of developed international practice is one of the socio-economical directions to be implemented.

Reconstruction of the pension system inherited from Soviet times and absolutely inadequate to the present-day demands has started with implementation of the Pension Reform Concept of Azerbaijan for 2001-2005. During that period important steps have been made to bring insurance and pension system in line with contemporary standards and activities have been implemented to introduce insurance principles in the pension system. The core of those activities included separation of the insurance and pension system from the system of social assistance benefits and coordination of social insurance contributions with the quoted pension amounts.

Since 2006 a new labour pension system based on internationally well-taken 3-staged structure (basic, insurance and savings parts) has been functioning in the country. Gained experience indicates on high social efficiency of the new system. During functioning of new system both minimum (basic) part and average monthly pension have been significantly increased. Running of the pensions' growth mechanism in line with market economy requirements allowed distributing current funds among pensioners in more equitable way. Personal accounting system has been established in mandatory state social insurance area, provision of pensions for beneficiaries has been based on data from personal accounting and transition to insurance principles in pension provision has been arranged.

Additionally in this period the management in the mandatory state social insurance area, the introduction of personal accounting for the insured and the pension payment issues have been handled by a single pension agency and the advanced technologies-based activities have been implemented to improve and restore these areas. A card system has been successfully introduced to facilitate the payment of pensions.

In addition to all these achievements it is important to ensure sustainable and autonomous development of the insurance and pension system and to identify from this prospective main goals and duties as well as activities to be implemented.

Though present labour pension system has been established mainly in line with the insurance principles, one of the current pressing problems is substantially big financial burden of non-insurance payments made from this system. Funding of incentive payments on labour pensions to those who are pensioned off before retire age (eligible for labour pensions on preferential terms), supplements to the labour pension (supplements to the basic part of labour pension and supplements to the labour pension for seniority) as well as other non-insurance payments from the collected mandatory state social insurance contributions as it is stipulated by current legislation should be considered as a factor weakening insurance principles in the present insurance and pension system.

Another important issue in the context of financial sustainability of the insurance and pension system is full clarification of purpose and share of the state budget funds in provision of pensions. It is also very important to adhere to compliance of social insurance rates with ever-

growing funding needs in reaching social targets set out for provision of pensions and to improve a work on collection social insurance contributions.

It necessitates developing actuarial analysis-based mechanisms and designing relevant outcomes, as well as implementation of the comprehensive action plan required for long-term development of the insurance and pension system. Together with this a special attention will be given to appropriate evaluation of the beneficiaries' pension rights gained till January 1, 2006 (prior to introduction of the new pension system), gradual elimination of difference in pensions of beneficiaries who have retired before and after introduction of the new system and implementation of these activities without imposing additional financial burden to this system.

Though basic and insurance parts of the labour pension system are already being introduced successfully, it is now required to make efforts to activate the saving function, 3rd element of the labour pension stipulated by legislation. In addition implementation of reforms which include such elements of pension relations as voluntary pension insurance and provision of non-state pensions will play a key role in perspective social and economic development of the country.

Though legislative framework as well as technical and physical resources consistent with present requirements have been provided for functioning new insurance and pension system, other goal consists of full automation of the system's work, capacity building of the staff who will run this system, development of the personal accounting system and awareness raising of the insured.

The State Program on the Insurance and Pension System Development in the Republic of Azerbaijan for 2009-2015 (hereinafter referred to as the State Program) is aimed at comprehensive solution of the above mentioned problems and specifies next phase of reforms to be implemented in the insurance and pensions system of the country with consideration strategic objectives, targets and indicators reflected in the State Program on Poverty Reduction and Sustainable Development in the Republic of Azerbaijan for 2008-2015 approved by Decree #3043 of the President of the Republic of Azerbaijan dated September 15, 2008.

1.2. Goals and Tasks

Restoration of the market economy relations in Azerbaijan and moving forward to the qualitatively new phase in social and economic development contribute to further rise of the population's well-being based on mechanisms complying with international standards. In its turn it necessitates comprehensive development of the insurance and pension system that will interlink economy and social sphere of the country.

While bearing in mind strengthening of the insurance principle in provision of pensions and gradual introducing saving component, main goal of the State Program includes further deepening of the pension reforms, ensuring sustainable and dynamic development of the new insurance and pension system established as a result of reforms implemented and further improving in provision of pensions to beneficiaries.

Main tasks stipulated by the State Programme are as follows:

- strengthening of the insurance principles in the insurance and pension system and improving regulatory mechanisms of non-insurance payments;
- ensuring closer incorporation of the pension rights gained by the beneficiaries prior to January 1, 2006 into new labour pension system;
- improving mandatory state social insurance and developing voluntary pension insurance;

- activating saving component of the labour pensions as well as establishing and developing non-state pension institutions;
- ensuring current paying capacity as well as mid- and long-term financial sustainability of overall insurance and pension system;
- ensuring wide introduction of modern ICTs in work of the insurance and pension system, full automation of management as well as wide coverage of personal accounting system.

3. Main Directions of the State Programme

In line with the goal and tasks set out for 2009-2015 the State Programme shall be developed in following main directions:

Actuarial models-based improvement of the insurance and pension system

Identification of the prospective development directions in the insurance and pension system depends directly on proper arrangements of actuarial calculation-based forecasts.

For this reason it is very important to study in well-coordinated manner changes of macroeconomic and demographic indicators and those ones defining work of the system itself. In order to bring additional periodically rights and privileges available in the system in line with demographic indicators introducing relevant mechanisms will be ensured.

It is necessary to establish mechanisms that will design relevant proposals with consideration of all factors such as: turning of pensions paid before introduction of the new system, pension rights gained by the insured during functioning of the previous system, supplement payments for seniority as well as other payments not based on social insurance into additional financial burden for the system; amount of state budget allocations required to attain social targets set out by the state; funding demands expected in future as a result of introducing personal accounting in the mandatory state social insurance system; compliance of social insurance rates with growing financial demands; and studying other issues in well coordinated manner.

Special attention will be focused on learning international experience on making actuarial analysis; involving skilled international experts and consultants to study various subjects; more intensive introducing advanced experience of developed countries on making actuarial calculations in Azerbaijan.

Improvement activities in the area of mandatory state social insurance

Establishment of the insurance relations-based insurance and pension system in Azerbaijan enhanced the role of mandatory state social insurance in social protection of the population. Sustainable development of the current insurance and pension system depends directly on straight interlinking of mandatory state social insurance contributions with social insurance payments. Meantime one of the main tasks is to adhere to compliance between growing financial demand and social insurance rates.

On the other hand, as current problems in documenting relations between employer and employee as well as in quoting salaries affect this area, undertaking some mitigation measures should be ensured in this direction.

One of the main directions for improving activities and enhancing transparency in the area of mandatory state social insurance includes automation of quoting and recording of the benefits to be paid from mandatory state social insurance contributions

Improvement of labour pension provision

The labour pension system established in line with international standards is currently functioning in Azerbaijan. The main indicators affecting amounts of pensions in this system are funds available on personal accounts of beneficiaries and expected term of the pension payment. In the context of the system improvement it is also very important to develop alternative mechanisms regulating, based on these indicators, a number of rights and privileges within the system.

Additionally improving evaluation of the pension rights gained before introducing of the new pension system; automated quoting of pensions; preparing agreements with relevant countries on further provision of pensions for citizens of Azerbaijan working abroad as labor migrants; and implementing activities in other directions will be ensured. At the same time implementation of activities aimed at gradual eliminating differences in pensions of beneficiaries who have retired before and after introducing the new system will be continued.

Moreover another issue of great importance is further expansion of the advanced methods-based system of paying pensions. For this purpose regular improvement of the card system for the pension's payment will be continued, payment by ATMs and post-terminals enhanced, using of multifunctional chip-cards ensured, experience of various countries on advanced methods-based payments in the remote areas studied and applied.

Development of personal accounting in the state social insurance system

In order to develop and introduce personal accounting in the state social insurance system important activities have been implemented. Establishment of regulatory and legislative framework, establishment of required infrastructure, registering personal accounts for all beneficiaries and delivering insurance certificates issued for them were provided for.

Another important prospective task includes receiving annual reports on the insured, reflecting relevant data on personal accounts and providing this data to the insured. For this reason, mechanisms on protection individual data of the insured will be identified, and responsibilities of the employers on providing data about every insured will be further increased.

Indicators on labour pension rights gained by the insured until introducing new insurance and pension system in the country will be included in the personal accounts. Identification of the earlier gained pension rights of the insured in conformity with new pension system will allow speeding up the work in the given direction.

Establishment of the State Social Protection Fund (SSPF) Regional Centre on personal accounting of the insured and automation of the SSPF activities will be completed.

Applying saving component on the insurance and pension system

National legislation on labour pension stipulates 3-tier pension system consisting of basic, insurance and saving parts. Within the new insurance and pension system established in the country quoting and paying mechanisms of basic and insurance parts of the labour pension have been successfully introduced. One of the upcoming main challenges is to introduce saving part, i.e. 3rd tier of labour pension envisaged by legislation.

Introducing of the most complicated, i.e. saving component of the insurance and pension system depends very much on investment environment, financial and securities market development in the country and other factors beyond the insurance and pension system.

For this purpose at first mechanisms of directing social insurance contributions to the saving part of personal accounts (personal saving accounts) and guidelines for management of these funds should be properly defined by learning international practice, after it, accumulating of the social insurance contributions at personal saving accounts will be started.

Legislative and regulatory framework will be developed and include using funds accumulated at personal saving accounts, requirements to managing companies as well as will offer opportunities for the insured to choose relevant investment portfolio of the managing companies. Then it is provided to introduce a number of additional mechanisms in order to start accumulating social insurance contributions at personal saving accounts and personal recording of income gained from use of these funds as well as to encourage accumulating social insurance contributions at personal saving accounts.

Development of non-state pension institutions

Establishment of non-state pension institutions and development of their activities in Azerbaijan is very important for social protection of beneficiaries as well as for development of the financial market in the country.

For this purpose it is important to develop legislative framework that will regulate establishment and activities of non-state pension funds dealing with additional provision of pensions to beneficiaries. At the same time guidelines will be developed to allocate and oversight allocation of the reserve pension funds of the non-state pension institutions as well as mechanisms on fixing, funding and paying of non-state pensions will be established.

In order to encourage activities of the non-state pension institutions, in addition to various methods they may be involved in management of funds accumulated at the personal saving accounts of the insured.

4. The State Programme Funding Sources

No	Policy Measures	Duration (by years)	Implementing Agency
2.1	Arranging mid- and long-term actuarial analysis based studies of the insurance and pension system	2009-2011	SSPF
2.2	Actuarial modelling based forecasting of prospective development of the insurance and pension system	2011-2015	SSPF, Ministry of Economic Development (MED), Ministry of Finance (MF), Ministry of Labor and Social Protection of the Population (MLSPP), State Statistics Committee
2.3	Designing proposals for strengthening link	2009-2010	SSPF

	between social insurance contributions pensions and benefits for all the insured.		
2.4	Designing relevant proposals for making changes in legislation to officialise illegal labour relations and to prevent cases of deliberately low quoting of salaries in order to ensure social protection and rights of the employed on future provision of pensions	2009-2010	Cabinet of Ministers (CM), SSPF, MED, MF, MLSPF, Ministry of Justice (MJ)
2.5	Designing proposals for introducing insurance principles in calculation and payment of benefits from mandatory state social insurance contributions	2009	CM, SSPF, MLSPF, MJ
2.6	Quoting benefits paid from mandatory state social insurance contributions and automating its records	2009-2010	SSPF
2.7	Designing relevant proposals for making changes in legislation in order to improve mechanisms regulating non-insurance payments in the pension system	2010-2011	SSPF, MLSPF
2.8	Designing proposals for identifying in line with the new pension system the pension rights of the insured gained till January 1, 2006	2009	CM, SSPF, MLSPF, MJ
2.9	Preparing proposals for eliminating differences made by previous pension system and existent in pensions of beneficiaries retired before and after introducing of the new insurance and pension system	2009	CM, SSPF
2.10	Designing proposals for establishing special financial reserve in the SSPF budget for stable and sustainable funding of pensions	2009-2010	SSPF, MF
2.11	Implementing activities aimed at ensuring transition to automated system of pension quoting	2010-2015	SSPF
2.12	Undertaking measures for signing agreements with countries where citizens of Azerbaijan work as labour migrants in order to ensure recognizing their future pension and other social insurance rights	2009-2015	CM, Ministry of Foreign Affairs, SSPF

2.13	Studying international experience on forming and managing funds at personal saving accounts	On regular basis	SSPF
2.14	Establishing mechanisms on sending certain part of mandatory state social insurance contribution to the saving accounts	2010-2012	CM, SSPF
2.15	Developing regulatory and legislative framework specifying management mechanisms of funds accumulated in saving part of personal account of the insured and requirements to the managing companies and specialized depositories	2013-2014	CM, SSPF, MED, National Bank (NB), MF, other related state agencies
2.16	Establishing guidelines on procedures of selection the managing company that will manage funds accumulated in saving part of personal account of the insured and introduction of the relevant managing companies to the insured for their choice	2013-2014	CM, SSPF, MED, NB, MF, other related state agencies
2.17	Developing regulatory and legislative framework specifying administrative and technical oversight mechanisms over investing funds accumulated in saving part of personal account of the insured	2014	CM, SSPF, MED, MF, other related state agencies
2.18	Starting accumulation of the social insurance contributions at the personal saving accounts	2015	SSPF
2.19	Designing proposals for forming and developing voluntary pension insurance	2012-2014	CM, SSPF, MJ
2.20	Studying international experience on establishment and functioning of the non-state pension institutions	2009-2012	SSPF, MED, MF, MLSPP
2.21	Developing regulatory and legislative framework regulating establishment and activities of the non-state pension institutions	2012-2013	CM, SSPF, MED, MF, NB, other related state agencies
2.22	Preparing guidelines on allocation of funds from the non-state pension institutions and oversight such allocation	2013	CM, SSPF, MED, MF, NB, other related state agencies
2.23	Designing proposals on mechanisms of quoting, funding and paying of non-state	2013	CM, SSPF, MED, MF, other related

	pensions by the non-state pension institutions		state agencies
2.24	Undertaking measures to involve non-state pension institutions in managing funds accumulated in saving part of personal accounts of the insured	2015	CM, SSPF, MED, MF, MLSPP
2.25	Improving a card system of the pension payment by ATMs and introducing multifunctional chip-cards for payments	2009-2015	SSPF
2.26	Studying experience of various countries to expand the advanced methods based payment of pension to the rural areas especially to the remote villages	2009-2015	SSPF
2.27	Ensuring transition to running of operations by single centre through full automation of quoting pension	2013	SSPF
2.28	Strengthening mechanisms of protection personal data of the insured in the state social insurance system	2011-2012	SSPF, Ministry of Communication and Information Technologies (MCIT), other related state agencies
2.29	Establishing modern reporting system about social insurance contributions accumulated at personal accounts of the insured	2013-2015	SSPF
2.30	Establishing client's service centre replying efficiently on requests of the insured about their personal accounts	2013-2015	SSPF
2.31	Establishing corporative network facilitating e-data exchange between the SSPF Headquarters and its local offices, carrying out works for automation SSPF activities	2009-2013	SSPF
2.32	Undertaking relevant measures to provide safety of the SSPF automated operation centre	2011-2012	SSPF, MCIT
2.33	Implementing activities to arrange effective mutual data exchange with social insurance and pension authorities of other countries	2009-2015	SSPF

2.34	Developing training manuals and introducing continued skills upgrading system to provide insurance and pension system with high skilled staff	2009-2015	SSPF
2.35	Establishment of the SSPF Training Centre	2010	CM, SSPF
2.36	Implementing relevant activities with involvement of the Mass Media to raise awareness of population about insurance and pension issues	2009-2015	SSPF

ANNEX 4:

CONCEPT of the reforms of pension system in the Republic of Azerbaijan in 2014-2020

Approved by the Executive Order
of the President of Republic of Azerbaijan
Dated November 4, 2014

1. Introduction

Pension provision system is one of important and main directions of social protection policy implemented by the government.

Within the first years of independence, because of poor development of the country's economy, and insufficiency of financial resources, there occurred difficulties in pension provision system. In addition, strict inconformity of pension provision system with market economy inherited from soviet period that is not based on social insurance was an important and general problem for the Republic of Azerbaijan.

Sustainable development achieved by political stability in the Republic of Azerbaijan from 1993, became the main factor of strengthening social protection of population. During this period, reconstruction of country's pension provision system in line with international practices was determined as one of the strategic directions of social policy.

Within the past years, it was achieved to establish a modern and socially efficient pension provision system in Azerbaijan due to reforms conducted. As a result, the social welfare conditions of section of population in pension age improved significantly and poverty was almost eliminated in this section. Reasonable activities aimed at social protection of population allowed increasing the average monthly amount of labour pensions by 5.7 times within 2006-2013, so the country occupied leading places according to this indicator in the post-soviet geographical space. However, the necessity to bring pension provision system in line with regularly updated modern requirements is a precondition to continue reforms that meet the new challenges in this field today. The necessity for improving the existing pension provision model in Azerbaijan taking account of international best practices, relates first of all, to creation of a system that allows ensuring pension provision of citizens through more improved mechanisms under the circumstances of the end of our country's transition to market economy and new realities. The targets set in Development Concept "Azerbaijan 2020 – Vision To Future" provides favourable conditions for outlining new perspectives in citizens pension provision and for implementing changes strategy in conformity with international best practices, based on achievements attained by our country.

Concept of reforms of pension provision system in the Republic of Azerbaijan in 2014-2020 specifies the basis of government policy in pension provision within the period of its coverage.

2 International practices in pension provision

2.1 The relevant conventions and recommendations of International Labour Organization, as well as Council of Europe in social security providing for security against aging, disability and loss of breadwinner, refer to mechanisms of realization of these payments through

mandatory state social insurance. At the same time, in a number of countries, voluntary pension insurance is developed along with mandatory social insurance system which plays an important role in additional pension provision of population.

2.2 In international practices, financing of pensions is carried out based on pension systems comprised of PAY GO, funded models, as well as of a combination of these models. PAY GO system provides for financing of pensions of aged generation at the expenses of social contributions paid primarily by the currently-employed people. Unlike this, social contributions paid mandatorily or voluntarily by the currently-employed people, in the funded system, are not spend for current pension expenditures, and are managed as directed to different investment programs for the purpose of generating additional incomes.

2.3 In leading countries, it is more common to have a pension system based on combination of such financing models in different ratios and forms. In most cases, there are used pension provisions systems operating based on funded financing model in addition to state pension provision systems financed primarily under the principle of PAY GO and applied mandatorily.

2.4 Currently, development trends of pension provision are defined by measures taken in provision of financial sustainability of this field as a whole, as influenced by global economic and demographic factors in the world.

2.5 Under the circumstances of global financial crisis, the serious problems encountered concerning depreciation of funds strengthened the trends to enhance PAYGO models on one hand, and to prefer to ensure citizens participation in funded pension provision schemes based on voluntary principle rather than mandatory.

2.6 Practically, in a number of leading countries, improvement of state pension provision systems established under PAYGO principle is ensured primarily through spreading the application of insurance principles. Strengthening the insurance principles in state pension provision, is linked to reform activities that foresee the provision of balance between accrued pension liabilities and accrued financial resources, as well as the observation of actuarial justice with respect to participants of these systems (the fact that the contributions paid by each participant is proportionate to the amount of pension to be granted).

2.7 International practices show that it is extremely difficult to achieve a higher pension amount through application of a system only based on mandatory state social insurance. In addition to mandatory state social insurance, introduction of voluntary insurance allows to have a worthy pension amount. Introduction of voluntary insurance necessitates establishment of private pension funds which is a precondition to ensure the mutual relation between pension systems and financial markets.

3. Current status of pension provision system in the Republic of Azerbaijan

3.1 As a result of reforms conducted in pension provision in the Republic of Azerbaijan, there was formed a uniform state pension provision system where functions of social insurance, personal accounting and pension provision complement to each-other. This system operates to the modern requirements, by opening individual accounts for the insured, there was established the mechanism for personal accounting of paid mandatory state social contributions in these accounts, and for determination of citizens pension rights denominated as value based on the data of this personal accounting.

3.2 due to reforms conducted, there were eliminated a number of problems caused by the inconformity of the previous pension provision system with market economy first of all, and completed the integration of the persons not covered by that system into the new conditions without any restrictions.

3.3 In whole, it was ensured to conform the pension increase mechanism to requirements of market economy and to protect pension amounts against inflation by way of indexation.

3.4 In addition, for the purpose of achieving reliable social protection of pensioners in the long run, it is very important to continue reforms activities aimed at strengthening the financial sustainability of pension provision system and further deepening the insurance principles. There several issues to be settled in pension provision system.

3.4.1. Lack of financial sustainability in the long run within the present conditions in the pension provision system. Currently, one part of pension amounts constitutes the amounts formed for the period prior to January 1, 1992 when social insurance legislation was applied in the independent Republic of Azerbaijan. Since the government liabilities created for that period, as well as supplements to pensions of the persons of some categories were not based on insurance principles, there appeared uncovered financial liabilities in the pension provision system. Furthermore, the fact that liabilities created as a result of a number of reforms conducted by the government for the purpose of strengthening the social protection of pensioners, (regular increases in the basic part of old-age labour pensions, higher pension provision that is not adequate to the paid social insurance contributions etc) has created an increase in the amount of these liabilities that is not consistent with the pension capital recorded in the notional savings system. Currently, liabilities not related to social insurance in the pension provision system in our country, increasing the financial load significantly, became a precondition to increase expenditures, as well as allocations (transfers) from state budget. Consequently, in 2014, the expenditures in the approved budget of State Social Protection Fund was 2,928.5 mln manat, which has increased by 5 times as compared to 589.5 mln manat in 2006. Within that period, allocations (transfers) from state budget increased by 6.8 times from 167 mln manat to 1,142 mln manats and the specific weight of total expenditures increased from 28.3 percent to 39 percent. In addition to the aforementioned, for the purpose of further strengthening the financial sustainability for the long-term development of pension provision system, there should be developed relevant measures, regulated the impact of government liabilities not based on social insurance principles, on the system, strengthened the relationship between social contributions and social insurance payments.

3.4.2. Inconformity of application of basic part of labour pensions with reform requirements in the next stage. Unlike the previous stage (bringing the average monthly amount of pensions to a certain limit with government support), the basic part of labour pensions has a negative impact on deepening of insurance principles in pension provision system. That is, the fact that a part of paid total contributions are applied for financing of basic part, weakens the relationship between contributions and pensions. And this allows the employees paying long-term and higher amount of social contributions to indirectly subsidize the future pensions of persons paying short-term and lower – amount of contributions. Eventually, there is reduced interest in paying social contributions from higher wages.

3.4.3. Necessity for improvement of structure of social contributions normative. The existing structure of social contributions normative, that is the fact that employer undertakes the main part of the burden, to pay social contributions, causes reduction in the activities of insured. Strengthening of insurance principles in pension system, necessitates the gradual increase in the responsibility of the insured in structure of social contributions normative.

3.4.4. Factors weakening the saving potential of the pension provision system. There are a number of factors having a negative impact on the solvency of pension provision system in the Republic of Azerbaijan. First of all, there is an unsatisfactory current level of the ratio between participants of pension provision system, i.e., the between the number of the insured and pensioners. Such a situation concerns factors outside the pension provision system,

especially the problems existing in arrangement of employer-employee relations and in organization of labour payment.

Currently, the number of pensions 1.28 mln persons, and the number of insured is 2.7 mln persons. There are approximately 2.1 insured per pensioner. Approx. 1.4 mln persons out of the insured are hired employees and their mandatory state social insurance contributions are paid in amount of 25 percent of wage bill. Others are those paying social contributions with a lower social insurance normative (in amount of 2-50 percent of minimum monthly salary). This mainly includes persons using agricultural lands in their possession and physical persons performing entrepreneurial and labour activities individually. Such conditions cause significant difficulties for pension provision system based on PAYGO principle and the fact that insurance principles are not fully observed, allows increasing the specific weight of expenditures not related to paid social contributions.

3.4.5. Problems existing in regulation of a number of indicators of pension provision systems. Existing pension granting conditions (the existing level of social contributions normative and the requirement over insurance record) does not allow efficient replacement rate and its increase proportionate to the increase in the wages amount. The requirement over shorter insurance record and the application of the same expected pension payment period to the persons retiring at various ages, causes inadequacy in the pension amounts. Consequently, long-term execution of payments while contributions are paid for a short term to the pension provision system, increases the financial burden of the system. The inconformity between paid contributions (especially for persons use agricultural lands in their possession and persons performing entrepreneurial and labour activities individually) creates liabilities which have no financial basis. Furthermore, the cases of entitlement to pension earlier than general pension age and the existence of age differences in entitlement to pension are factors weakening the insurance principles. The existence of special pension conditions, allowing supplements to granted pensions under difference conditions, causes different provisions. The right of the persons who have certain service years to retire earlier than the general pension age, also creates additional financial liability in the pension provision system.

3.5 It is necessary to define the directions of pension provision system based on long-term econometric models based on multi-parametric actuary projections. Within the past period, there was organized actuary analysis of individual topics by involving competent international experts and advisors in this field. This process should be continued, and there should be applied mechanism for observance of proportionality between incomes and expenditures of pension provision system and for interconnected study of other problems.

4. Main objectives and duties of pension provision system.

4.1. There are new strategic objectives in the field of reforms of pension provision system in line with the established new socio-economic conditions.

4.2. The following are main objectives of reforms of pension provision system:

4.2.1. achievement of financial sustainability of pension provision system for current period, mid-term and long-term.

4.2.2. pension provision ensures citizens social protection and worthy standard of living.

4.3. The following are main duties of reforms of pension provision system:

4.3.1. strengthen the insurance principles in the operation of pension provision system and form balancing mechanisms between attained pension rights and accrued insurance funds;

4.3.2. ensure that the amount of pension granted in pension provision system is proportionate to paid contributions;

4.3.3. Form mechanisms based on actuary analyses for long – term development of pension provision system;

4.3.4. improve the mechanisms for regulating payments not inline with insurance principles, including differentiation of a number of liabilities as government liabilities;

4.3.5. application of voluntary funded component of labour pensions in real practice and establish and develop non-state pension institutes.

5. Main directions of implementation of the concept

5.1. Achievement of financial sustainability of pension provision system for long-term. Reforms conducted in pension provision system should be directed at achievement financial sustainability of this system, and at it protection against liabilities not based on social insurance at the same time. For this purpose, it is intended to specify the liabilities of pension provision system, to direct mandatory state social insurance contributions only to the expenses resulting from social insurance, to optimize the sources of financing of expenses not based on insurance principles by minimizing them. To this end, it is intended to differentiate as government liabilities, the amounts formed for the period prior to January 1, 1992 when social insurance legislation was applied which are a part of pension amounts, as well as expenditures directed at payments of supplements to labour pension granted according to age to persons served in a number of positions. At the same time, it is indented to define pension amount in conformity with the contributions paid by each person. It is offered to change the practice of directing contributions paid by persons with higher salaries towards pensions of persons with low salaries. Employees paying higher amount of contributions during labour activities will have adequate replacement rate. Accordingly, pension system will not allow pension provision with attractive replacement rate for the persons paying contributions in short-period of activities and from low salary.

5.2. Restructuring the basic part of labour pension. Restructuring the basic part of labour pension will allow increasing the funds of employees accounted in the notional saving system, and the funds considered in the personal accounts of the employees will ensure that the paid contribution is considered in full, not in half. This will allow considering the full amount of contribution in pension granted, and to strengthen the insurance principles. With regard to restructuring the basic part of labour pension, minimum pension indicator will be applied. In case amount of pension granted is less than minimum pension amount, a requirement will be imposed in pension right and it will be brought to that amount. In case amount of pension granted is more than minimum pension amount, no requirement will be imposed ion insurance record. Increase of minimum pension amount will be carried out in the manner of indexation together with the total pension amount, but not individually.

5.3 Improvement of structure of social contributions normative. It is intended to gradually transfer certain part of social contributions normative from employer to employee for the purpose of encouraging participation in pension provision system.

5.4. Strengthening the pension system's ability to pay. Increase of attraction of pension provision system, optimization of the ratio between the number of contributors and number of pensions through elimination on problems existing in arrangement of employer-employee relations and organization of labour payment are assessed as an important source increasing the financial receipts of pension provision system.

5.5. Provision of proportion between pension amount and paid contributions in case of retirement under preferential and special conditions, that is conditions not conforming to insurance principles, as well as in case of earlier retirement. For the purpose of provision of proportion between pension amount and paid contributions in case of retirement under

preferential and special conditions, that is conditions not conforming to insurance principles, as well as in case of earlier retirement, it is intended to determine optimum age limit of pension, to reconsider the conditions of pension granting and insurance contribution normative for those working in harmful and dangerous workplaces, those using agricultural lands in possession, those performing entrepreneurial activities and other categories.

5.6. Formation of mechanisms based on actuary analyses for long term development of pension provision system. Provision of projections based on actuary modelling of perspective development of pension provision system, will allow foreseeing the processes to occur in the system and taking preventive acting to control them.

5.7. Activation of voluntary funded component of labour pensions and development of non-state pension institutes. In order to achieve a reliable pension provision of people, it is intended to form mechanisms that allow provision additional to the mandatory state social insurance. It is considered reasonable to introduce voluntary social insurance on order to establish funded component in state pension provision system, as well as non-state pension institutions. To this end, it is intended to use a number of promotional means.

6. Expected results of the implementation of the concept.

6.1. Implementation of activities provided for in this Concept will allow achieving the following results in pension provision system:

6.1.1. the amount of pension granted and paid contribution amount will be consistent;

6.1.2. savings potential of pension provision system strengthened;

6.1.3. principles on insurance in legislation related to pension provision system improved;

6.1.4. structure of social contribution normative improved;

6.1.5. number of deviations from payment of mandatory state social contributions reduced;

6.1.6. actuary mechanisms based on actuary analyses for long term development of pension provision system formed;

6.1.7. long-term financial sustainability of pension provision system achieved.

7. ACTION PLAN

for implementation of the Concept

No.	Activity	Period of execution (years)	Responsible body
1	2	3	4
7.1.	Improvement of legislative pieces for the purpose of strengthening social insurance principles in pension provision system		
7.1.1.	Preparation and submission to President of Republic of Azerbaijan of proposals to ensure improvement of law of Republic of Azerbaijan "On labour pensions" in the following		

	directions		
7.1.1.1.	optimize the sources of financing of expenses not based on insurance principles by minimizing them	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.1.2.	conform pension granting conditions, to amount of social contribution paid for each person	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.1.3.	Restricting the basic part of labour pension and application of minimum pension amount	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.1.4.	Application of mechanism encouraging later retirement, and reducing interest in earlier retirement	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.1.5.	restriction of cases of earlier pension	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.1.6.	differentiation of government liabilities and insurance pension system liabilities in pension provision	2014-2015	State Social Protection Fund of Republic of Azerbaijan, Ministry of Finance
1	2	3	4
7.1.1.7.	conforming the minimum insurance record years required for those entitled to retirement under preferential conditions, to the insurance principles	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.1.8.	conform pension age for men and women to demographic indicators	Starting from 2018	State Social Protection Fund of Republic of Azerbaijan, Ministry of Labour and Social Protection of Population
7.1.2.	Preparation and submission to President of Republic of Azerbaijan of proposals to ensure improvement of law of Republic of Azerbaijan "On social insurance" in the following directions		
7.1.2.1.	Improvement of mandatory state social insurance contribution	2014-2015	State Social Protection Fund of Republic of

	normative		Azerbaijan
7.1.2.2.	Improvement of insurance normative of payers of mandatory state social insurance contribution in relation to minimum salary (persons using agricultural lands in their possession and persons performing entrepreneurial and labour activities individually	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.2.3.	To impose a certain limit on salary subject to mandatory state social insurance, and to allow citizens to choose usage of social insurance contributions exceeding this limit	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.1.2.4.	determination of conditions for payment of voluntary social insurance contributions	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.2.	improvement of system of notification of insured about the amount of social insurance contributions accrued in their personal accounts	2014-2015	State Social Protection Fund of Republic of Azerbaijan
7.3.	preparation of proposals regarding Activation of voluntary funded component of labour pensions and development of non-state pension institutions	2015	Cabinet, Ministry of Finance, Ministry of Economy and Industry, Ministry of Labour and Social Protection of Population, State Social Protection Fund of Republic of Azerbaijan
7.4.	Establishment of non-state pension funds and creation of legal framework for regulating their activities	2015-2017	Cabinet of Ministers, Ministry of Finance, Ministry of Economy and Industry, Central Bank, State Social Protection Fund of Republic of Azerbaijan, relevant state authorities
7.5.	Increase of attraction of pension provision system, optimization of the ratio between the number of contributors and number of	2014-2020	State Social Protection Fund of Republic of Azerbaijan

	pensions through elimination on problems existing in arrangement of employer-employee relations and organization of labour payment		
7.6.	Provision of projections based on actuary modelling of perspective development of pension provision system	2014-2020	State Social Protection Fund of Republic of Azerbaijan
7.7.	Improvement of labour pensions payment system,	regularly	State Social Protection Fund of Republic of Azerbaijan
7.8.	Strengthening the mechanisms for protection of individual data of the insured in state social insurance system	regularly	State Social Protection Fund of Republic of Azerbaijan, Ministry of Communications and High Technologies and relevant state authorities

ANNEX 5: Graphic illustration of the budgeting process

