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## Retirement Contributions, Russia

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### Synonyms

Insurance contributions – retirement contributions; Russia's pension fund; The pension fund of the Russian Federation – PFR

### Definitions

*Insurance contributions towards the mandatory retirement insurance (retirement contributions)* are mandatory payments made to Russia's Pension Fund (PFR – *Rossiisky pensionnyi fond*) to ensure the citizens' right to receive guaranteed pensions from the state-run pension system.

*Length of insurance period* is the total length of periods of employment and other paid activity for which retirement contributions are due and paid to the PFR, as well as other periods (paid maternity and parental leaves, military conscription service, etc.) counted towards insurance period.

## Introduction

Retirement contributions are the key element of pension systems which redistribute incomes during an individual's life cycle. Special-purpose contributions made by employees and/or employers by withholding certain amounts from wages form the income to be enjoyed after retirement from labor market. Thus, retirement contributions are a particular case of social insurance aimed at ensuring a certain standard of living after a person reaches a certain age (OECD 2013).

The importance of retirement contributions is greater in defined-contribution schemes, where the pension benefit depends on the total amount of paid contributions. By contrast, in defined-benefit schemes, popular in the twentieth century, the pension benefit usually depends on the length of residence, or work experience and, in some cases, the wage rate during a certain period in the pensioner's career, but it is not directly linked to the contributions.

In Russia, the transition to a defined-contribution system took place in 2002. Before that pension benefits were usually calculated on basis of information about the individual's wages and records in employment record books (*trudovaya knizhka*), which helped determine the length of an individual's work experience.

However, it should be pointed out that over the last 26 years of Russia's history its approaches to retirement contributions have been changing many times – not only was a defined-benefit

system replaced with a defined-contribution system, but there were also periods when the contributions were replaced with taxes; when contributions were paid jointly by employers and employees; when a portion of the contributions was paid to a pay-as-you-go (PAYG) pension system and another, paid into individual funded accounts, was invested on financial markets. And retirement contribution rates have been changing many times as well.

Presently, the contributions paid by employers do not suffice to pay pensions to present-day retirees. So, the state co-finances the pension system almost on an equal level with employers, using transfers from the federal budget to cover the difference between contributions and payments.

This entry will review the evolution of approaches to retirement contributions in Russia, compare the rates of current retirement contributions in Russia and some other countries, and describe the structure of financing of the Russian pension system.

## **Retirement Contributions Rates in Russia**

Unlike in European countries, employees in the USSR did not pay any retirement contributions. The USSR did not have a system of social insurance, although the norms set for the pension system were somewhat similar to the Bismarckian defined benefits system. Pensions of Soviet citizens were financed from the so-called funds of public consumption, which consisted of employers' contributions (between 4% and 12% of the payroll depending on the industry sector) and funds from the national budget. And by the late 1980s, the state budget already accounted for nearly half of the pension expenditures.

After the breakup of the USSR, the new law No. 340-1, adopted in 1990 and called "On State Pensions in the Russian Soviet Federative Socialist Republic," provided for the creation of a special off-budget fund, the Pension Fund of the Russian Federation (PFR), which would accumulate contributions of employees and employers

and finance pensions. That was arguably the beginning of the history of pension insurance in Russia. The rate of retirement contributions for most employers was 20.6% in 1991, 31.6% in 1992, and 28% in 1993–2000. The rate of employees' contribution was minimal: 1% of a wage (Sinyavskaya, 2011). Up until 2002, pension benefits were calculated as a percentage of the wage received during the last 2 years of employment (or during 5 years when the wage was maximal), provided the pensioner had worked for a certain period of time (20 years for women and 25 years for men) and reached a retirement age (55/60 years old for women/men correspondingly). In 1991–1997, the maximum size of pension benefit could not exceed three minimum pension benefits. In 1998–2001, a new pension formula that took into account the ratio between individual and average wage in the economy was introduced in addition to the previous one.

In the 1990s, the economic and financial crisis, as well as the absence of a clear link between retirement contributions and pension benefits, resulted in a massive retirement contribution evasion. The employers' and the state budget's contribution arrears to the PFR, in turn, triggered pension benefits arrears.

The tax reform in 2000 abolished employees' retirement contributions, and employees' payments to the PFR and other social insurance funds were replaced with the unified social tax (UST) with regressive rates. Initially, the UST was designed to relieve the tax burden of employees and employers, but as employees' contributions were abolished, employers came to see the UST as yet another kind of tax. The Russian Tax Code as amended on December 29, 2000, set the UST rate at 35.6%, including 28% of the portion of an employee's wage not exceeding 100,000 per annum payable to the PFR (Part II of the Russian Tax Code No. 117-FZ, as amended on December 29, 2000a). Incomes of higher-paid employees were taxed at a lower rate. Beginning from 2002, tax payments to the PFR were replaced with payments to Russia's federal budget. Despite the growth of wages, the thresholds for the UST contributions were not indexed,

which resulted in a decline of the amount of possible contributions per pensioner. From May 1, 2005, onwards the maximal rate of UST was reduced to 26%, and the thresholds for contributions were raised. The purpose of this move was to entice businesses out of the shadow economy but this did not happen. The decrease of the UST rates was not compensated with an expansion of the tax base, so the stream of tax payments to the PFR shrank further, which was one of the causes of the deficit at the PFR (Sinyavskaya 2011).

Since 2002, Russia has had a new, multi-pillar pension system, consisting of the universal basic component; the so-called insurance, or PAYG, component organized on defined-contribution principles (which was very similar to the notional defined-contribution accounts existed, for instance, in Sweden or Poland); and the mandatory funded component. Calculated on basis of defined contributions, the sizes of insurance and funded parts of pension benefits depended on the amount of paid contributions and indexation of notional pension capital (in the insurance component), or investment income (for the funded component). (For more information, see “► [Pension Reform](#).”) Changes in the pension formula enhanced the importance of retirement contributions.

Furthermore, in the 2002, pension formula the indexation of both pension benefits and notional pension capital were linked to the growth of the total amount of UST paid for insurance part of pension per one pensioner. Therefore, the indexation rate depended on the ratio between contributors and pensioners as well as on the effective UST rate, which determined the total amount of taxes paid to the PFR. Decreases in the UST's effective rate used to bring down the indexation levels of insurance pensions and of the notional pension capital. Which, in turn, caused pensions to grow more slowly than wages. (For more information, see “► [Retirement Incomes](#).”)

From 2010 onwards, the UST was again replaced with retirement contributions. The rate of insurance contributions in the mandatory pension scheme amounted to 20%, payable from all annual incomes not exceeding 415,000 rubles (Sinyavskaya 2010). It was resolved to regularly

index the “ceiling” of the portion of the wage from which the contributions were due. In 2011, the retirement contribution rate was raised to 26%, but already next year (2012) it was down to 22%, to relieve businesses' tax burden. The rate of retirement contributions payable by employers – 22% from the capped basic portion and 10% from the amount exceeding the base – is still valid and will be until 2019 (Federal Law No. 167-FZ Dated December 15, 2001). In 2017, the cut-off “ceiling” for insurance contributions towards the mandatory pension insurance was 876,000 rubles per annum (Russian government's Directive No.1255 Dated November 29, 2016).

Since 2002, Russia has had mandatory funded pension component. This component of the pension system was applied, in 2002–2004, to men born in 1953 or later and women born in 1957 and later. Since 2005, only individuals born in 1967 or later remained participants of the individual funded pension accounts. The rate of employers' contribution for this group of employees was gradually growing from 1% to 6% of a wage. For this category of employees, the contribution rate towards the PAYG component – the insurance part of pension – was lower than the total contribution rate to the rate paid to the funded component.

In 2014–2015, persons born in or after 1967 could choose a future pension plan: either the insurance scheme alone or the insurance and mandatory funded schemes simultaneously. Those who, submitting relevant applications, opted for a private pension fund or chose an investment portfolio of their private asset manager pay 6% out of 22% of retirement contributions towards the funded component, and the remaining 16% towards the insurance component. Insurance-only pension plans were the option set by default for the other categories of contributors.

However, in 2014, Russia froze the funded component because of a deficit of resources in the pension system. Instead of the funded part, all retirement contributions of all employees were channeled into the PAYG part to pay pension benefits to current pensioners. Later, the freeze was extended to 2015–2019 and its possible abolishment still remains a matter open to debate

(Federal Law No. 447-FZ Dated December 19, 2016).

Unlike the retirement contributions paid by employers for their employees depending on the latter's wage amounts, self-employed, individual entrepreneurs, defense lawyers, mediators, notaries, and some other Russians in private practice have to pay mandatory pension insurance contributions irrespective of the presence and amount of their business revenue in a given year. If an individual entrepreneur during a year earns less than 300,000 rubles, the fixed contribution amount (s)he has to pay would be 26% of the annual minimum wage (MROT – *minimalnyi razmer oplaty truda*) as of the beginning of the year. Considering that on July 1, 2016, the MROT was raised to 7,500 rubles, the individual entrepreneurs' fixed retirement contribution for 2017 will be 23,400 rubles. If an individual entrepreneur's annual income exceeds 300,000 rubles, the fixed insurance contribution into the mandatory pension insurance plan includes 1% of the amount exceeding this threshold. The maximal amount of retirement contributions set for individual entrepreneurs, defense lawyers, mediators, and other relevant categories of tax payers may not exceed the MROT x 8 (Part II of the Russian Tax Code No. 117-FZ Dated August 5, 2000b, as amended on April 3, 2017).

Retirement contributions should be paid by employers or self-employed persons during periods of their employment or other activity in the Russian Federation, and in some cases – outside the country. The insurance period of an employee/self-employed person is equal to the length of period when the contributions were paid to the PFR. The insurance period can also include socially important periods when retirement contributions were not paid: military service by conscription; being a spouse of a serviceman on a mission where employment options are unavailable; taking care of an infant younger than 1.5 years (this rule applies to four children in a family); taking care of a first-category disabled person, a disabled child or a person older than 80; being in receipt of a benefit on account of short-term disability; being in receipt of an unemployment benefit; compulsory community

service; imprisonment on account of unwarranted sentence; other (Federal Law No. 400-FZ Dated December 28, 2013).

## Sources of Retirement Contributions: Russian in the International Context

A pension system can have three main sources of financing: employees' contributions, employers' contributions, funds from the state budget. Practically, all pension systems in the world are financed by employees and/or employers (Table 1). Financing pensions, a state usually draws on the general taxes or, less often, the special taxes (for instance, excise duties). Unlike retirement contributions paid by employers or employees as a percentage of the latter's wages towards future pensions, the state's payments can be used to cover administrative costs and/or to cover a deficit in the pension system. Some nations abolished retirement contributions for low-paid employees, replacing them with payments from the state.

Rates of retirement contributions can be uniform for the entire employed population or differentiated depending on the wage amount. Usually retirement contribution rates are higher for the self-employed, "compensating" the contributions paid jointly by employees and employers. The contribution rates can vary depending on the type of pension systems. Some nations apply a single rate of insurance contributions not only for pension plans but also for family benefits, employment benefits, or disability benefits (Social Security Programs Throughout the World: Europe 2014).

The total rates of retirement contributions paid by employers and/or employees significantly differ from one country to another: from 1.94% in Israel to 36% in Singapore. Russia, with its 22% (since 2012) or 26% (in 2011), is located approximately in the middle of the ranking, an equal to such countries as Estonia (22%), Norway (22.3%), Sweden (22.73%), Austria (22.8%), Finland (23.3%), Switzerland (23.8%), The Netherlands (24.2%), Slovenia (24.35%), France (24.75%), Lithuania (26.3%).

**Retirement Contributions, Russia, Table 1** Rates of retirement contributions paid by employees and employers (%)

Country	Employee	Employer	Total
<i>Russia</i>	<i>0.00</i>	<i>22.00</i>	<i>22.00</i>
Singapore	20.00	16.00	36.00
Hungary	8.50	27.00	35.50
Portugal	11.00	23.75	34.75
Latvia	10.50	23.59	34.09
Italy	9.19	23.81	33.00
Romania	10.50	20.80	31.30
Belarus	1.00	28.00	29.00
Moldova	6.00	23.00	29.00
India	12.00	16.50	28.50
Spain	4.70	23.60	28.30
Czech Republic	6.50	21.50	28.00
China	8.00	20.00	28.00
Brazil	8.00	20.00	28.00
Poland	11.26	16.26	27.52
Slovakia	7.00	20.00	27.00
Lithuania	3.00	23.30	26.30
France	10.05	14.70	24.75
Slovenia	15.50	8.85	24.35
The Netherlands	18.50	5.70	24.20
Switzerland	11.90	11.90	23.80
Finland	5.55	17.75	23.30
Austria	10.25	12.55	22.80
Sweden	7.00	15.73	22.73
Norway	8.20	14.10	22.30
Estonia	2.00	20.00	22.00
Great Britain	9.05	11.90	20.95
Croatia	20.00	0.00	20.00
Greece	6.67	13.33	20.00
Malta	10.00	10.00	20.00
Turkey	9.00	11.00	20.00
Iceland	4.00	15.79	19.79
Germany	9.45	9.45	18.90
Bulgaria	7.90	9.90	17.80
Japan	8.737	8.737	17.474
Belgium	7.50	8.86	16.36
Luxemburg	8.00	8.00	16.00
Cyprus	7.80	7.80	15.60
USA	6.20	6.20	12.40
Canada	4.95	4.95	9.90
Australia	0.00	9.50	9.50
South Korea	4.50	4.50	9.00
Mexico	1.75	6.90	8.65
Ireland	4.00	4.25	8.25
Israel	0.34	1.60	1.94

Source: Collected by authors based on Social Security Programs Throughout the World: Europe (2014), Asia and the Pacific (2014), and The Americas (2015)

Russia is distinctive because employees in this country do not pay the contributions. Among the countries mentioned above only Australia has a similar scheme, with all retirement contributions paid by employers. There are also a number of countries (for instance, Belarus, Estonia, Mexico) where employees pay retirements contributions at a much smaller rate (1–2%) than employers. Overall, in most countries the rates of retirement contributions payable by employers are higher than those payable by employees. Equal rates for the employer and the employee are set in Switzerland, Malta, Germany, Japan, Canada, South Korea, and some other countries. The countries with the highest retirement contribution rates payable by employees are Singapore and Croatia (20%), The Netherlands (18.5%), Slovenia (15.5%). In Croatia, all contributions are paid by employees.

Retirement contribution rates for the self-employed vary even more (Table 2). As has been noted earlier, in Russia contributions from the self-employed practically do not correlate with the presence and amount of their revenues, and the fixed contribution amount is calculated on basis of the MROT. Similar schemes for retirement contributions of the self-employed, dependent on a minimal or median wage, are applied in China or Mexico. In most countries, the basic taxable income for the purposes of calculating retirement contributions is an individual entrepreneur's revenue, often with a cap. The rate of retirement contributions is differentiated depending on the pension type (old-age pension, disability pension, survivor's pension) or on the pillar of the pension scheme (main/subsidiary/occupational, PAYG pension insurance or mandatory funded individual pension account). Romania and Chile have a special rate for covering administrative overhead. Overall, it can be said that in most countries rates of retirement contributions of the self-employed are higher than those paid by employees or their employers.

## Structure of Financing of Russian Pension System

Retirement contributions are a major source of the revenues of the Russian pension system. Prior to 2005, retirement contributions sufficed for paying the insurance part of pensions and the federal budget financed only uninsured periods and pensions not related to the retirement contributions (social pensions, state-provided pensions) (Fig. 1).

From 2005 onwards, when the UST's effective rate was significantly reduced, the need in state financing has been growing. An additional factor accounting for the PFR's deficit and, accordingly, the demand for transfers from the federal budget was the indexation of pensions in 2008–2010, which was greater than the limits set by law. In 2009, the amount of federal budget transfers became equal to the amount of retirement contributions paid towards the pension's insurance component. In 2010, after the so-called valorization of the pension rights accrued for the periods before 2002, and especially before 1991, had raised the amounts of pensions paid to most senior pensioners, the situation became even worse and the size of federal budget transfers exceeded the total amount of retirement contributions (to both the insurance and funded components) by 1.4. In 2011–2013, the size of federal budget transfer was comparable to the amount of retirement contributions towards the insurance component. In 2014–2015, due to the abolishment of contributions towards the funded part, the authorities managed to diminish the size of federal budget transfers. However, it still remains significant.

The fact that the amount of the federal budget transfer continues to be large is partially explained by the reduction of the retirement contribution rate to 22% in 2012 from the rate of 26% set for the previous year – 2011. The Federal Law No. 167-FZ Dated December 15, 2001, provides that the difference of 4 percentage points is temporary and should be compensated by the state. Besides, the law sets lower retirement contribution rates for certain categories of the employers or employees: agricultural producers meeting certain criteria; organizations and individual



**Retirement Contributions, Russia, Table 2** Rates of retirement contributions of the self-employed (%)

Country	Self-employed
Russia	26.00% of the MROT x 12 if an entrepreneur's annual income less than 300,000 rubles 26.00% of the MROT x 12 + 1.00% of the amount above 300,000 rubles if an entrepreneur's annual income exceeds 300,000 rubles
Belarus	29.00%
Bulgaria	Social insurance: 17.80% for persons born before January 1, 1960 12.80% for persons born after December 31, 1959 Mandatory individual account: 5.00%
Cyprus	14.60%
Czech Republic	28.00%
Denmark	Contributions are paid quarterly up to 3,240 kroner a year
Estonia	Social insurance: 16.00% Mandatory individual account: 4.00%
Greece	20.00%
Hungary	7.00 and 27.00% in the form of a social contribution tax
Iceland	Universal pension: 7.79% of presumptive income (the employment income one would receive if similarly employed by an unrelated person) Mandatory occupational pension: 12.00%
Ireland	4.00% of annual income above €5,000
Italy	22.20%
Lithuania	Basic pension: 26.30–50% Supplementary pension: 15.00–100%
Luxemburg	16.00%
Malta	€28.38–€61.82 a week depending on net income
The Netherlands	17.90% (old-age pension) + 0.60% (survivors' pension)
Norway	11.40%
Poland	19.52% (old-age pension) + 1.50% (disability pension and survivors' pension)
Romania	Social insurance: 31.3% Mandatory individual account: 4.50% + administrative fees
Serbia	24.00%
Slovakia	24.00%
Slovenia	24.35% 15.50% for certain farmers

(continued)

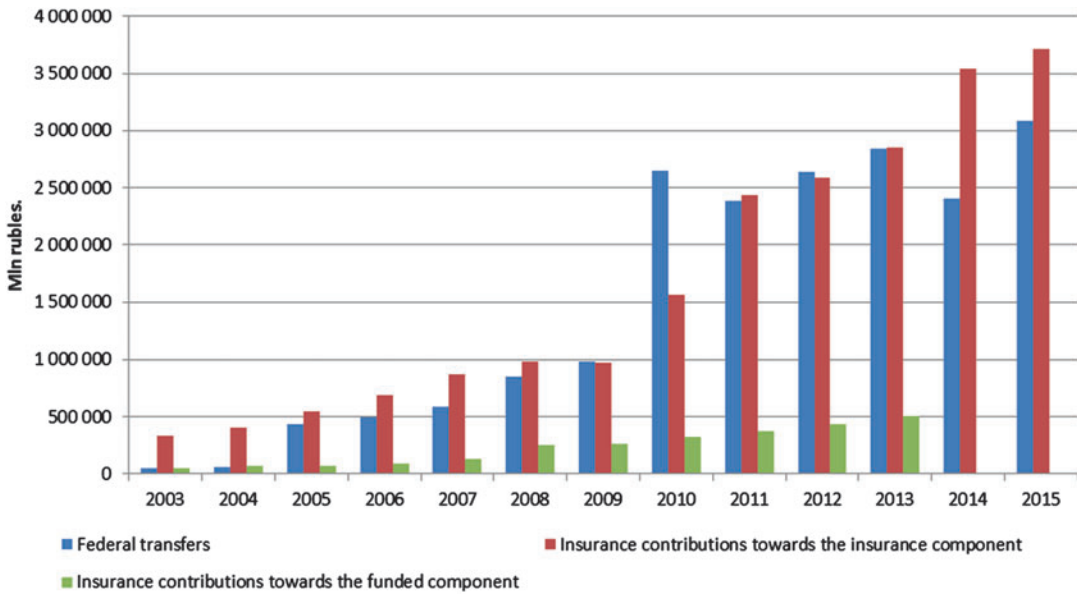
**Retirement Contributions, Russia, Table 2** (continued)

Country	Self-employed
Switzerland	Base pension: 7.80% (old-age and survivors' pensions) + 0.7% (disability pension) Mandatory occupational pension depends on the insured's pension fund
Turkey	20.00%
China	Basic pension insurance: 12.00% of the local average wage Mandatory individual account: 8.00% of the local average wage
Israel	3.09% of earnings up to and 5.21% of earnings above 60% of the national average wage
Japan	15,250 yen a month till March 2015 gradually rising to 16,900 yen a month by September 2017
South Korea	9.00%
Argentina	27.00%
Chile	10.00% (old-age pension) + 1.15% (disability and survivors' pensions) + 1.39% (administrative fees)
Mexico	6.275% of the legal daily minimum wage (old-age pension) + 2.375% (disability and survivors' pensions)
Peru	13.00%
USA	12.40%
Venezuela	13.00%

Source: Collected by authors based on Social Security Programs Throughout the World: Europe (2014), Asia and the Pacific (2014), and The Americas (2015)

entrepreneurs applying the unified agricultural tax; the disabled of I, II, and III categories in organizations meeting certain criteria; organizations and individual entrepreneurs working in special economic zones, and many others (Federal Law No. 167-FZ Dated December 15, 2001).

The deficit in the PFR and the growing need for federal budget transfers also stems from the increasing informal employment in Russia since the early 2000s. According to the most modest estimates of informal employment suggested by the data of the Rosstat's Labor Force Survey, the share of people employed in the informal sector grew from 13% in 1999 to 17–18% in 2009



**Retirement Contributions, Russia, Fig. 1** Dynamics of the amounts of retirement contributions paid to the PFR towards the insurance and funded components of the

pension system and federal budget transfers to the PFR, 2003–2015 (Source: Calculated by authors on basis of the official information on the PFR budgets.)

(Gimpelson 2011). This means that the gap between the numbers of the employed (formally and informally) and the numbers of retirement contributors continues to grow.

Increases in the numbers of people formally employed would push up the numbers of the contributors and the amount of collected retirement contributions paid to the PFR, while keeping the numbers of pensioners at the same level. According to the prognostic estimates of Grishina and her colleagues (Grishina et al. 2014), if all wages become fully transparent (i.e., formal), the amount of retirement contributions will grow by 14.3–14.8%, which corresponds to 0.6–0.7 percentage points of the GDP. Such an increase in the amount of the insurance-component contributions to the PFR, with the replacement rate unchanged, would reduce the federal budget transfers by 18–24%.

## Conclusion

Russia has a defined-contribution system whereby the pension's benefit depends on the amount of

contributions paid over the course of the working life. The retirement contribution rate is 22% of payroll now, which is on average level by the international standards.

One of the distinctive features of Russia's pension system is a lack of employees' contributions. Hence, pension benefits are financed by the employers' contributions and federal budget transfers. Only Australia as Russia has no employees' contributions; in most other developed countries, retirement contributions are paid both by employers and employees. The self-employed and individual entrepreneurs in Russia pay retirement contributions themselves. However, compared to some developed countries, the self-employed taxpayers' retirement contributions are fairly low because they are calculated on the basis of the MROT instead of the entrepreneurial revenues like in most countries.

The state's inconsistent steps in setting retirement contribution rates and amounts for pension indexation, together with the absence of a source of financing for the transition to funded pensions, are the causes of the deficit in the PFR. As a result, a large part of the pension payments is financed



through federal budget transfers. The dynamics of the amounts of the federal budget transfers to the PFR and retirement contributions reveal a serious deficit in Russia's pension system.

## Cross-References

- Retirement Contributions, Russia
- Active Ageing Policies and Globalization, Russia
- Human Resource Management in Russia
- Family Policy, Russia

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