Old-Age Pension System and Its Place in the Czech Welfare State

By Marketa Vylitova,

Researcher at the Research Institute of Labour and Social Affairs, Prague, Czech Republic

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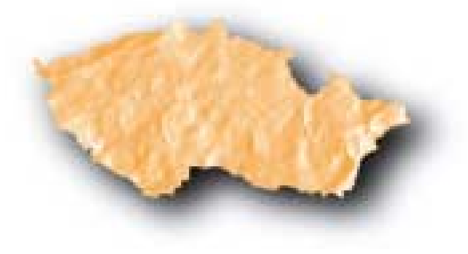
The Czech Republic: Brief Insight



The Czech Republic is a Central European country, borders with Poland, Germany, Austria and Slovakia. Republic was created in 1993 after the split of Czechoslovakia, which had a history of independent state since 1918.

Politics: Parliamentary democracy, 5 political parties in the Lower House of the Parliament today and 4 in the Senate (upper chamber); next parliamentary elections in June 2002; president elected by MPs, direct election now discussed.

Area 78,864 square kilometres. 14 self-governing regions operate since 2000, very high number of municipalities (over 6000, of which more than a quarter is smaller than 2000 inhabitants). Population density in 2000 was 130 inhabitants per square kilometre.

Population of 10.27 million. GDP per capita 14,012 US$ PPP in 2000 (source: OECD). Inflation of consumer prices 4.7 % in 2001, 3.9 % in 2000 and 2.1% in 1999 (according to the Czech Statistical Office). Unemployment rate since the end of 90's has been floating around 8-9 %, big regional differences.

I. Introduction

Basic Description of the System

The Czech PAYG scheme provides old-age, disability, and survivors' benefits. The system has 4.7 million insured (covering nearly 90 percent of the labour force) and 2.52 million pensioners. The PAYG scheme has wide coverage, self-employed and informal sector are included in the scheme; benefits are portable. Old-age pensions account for roughly three fourths of total pension expenditures. The average replacement rate for old age beneficiaries (defined as average old pension / economy-wide average wage) was 44 and 57 percent as a share of the gross and net average wages, respectively, in 2000, higher for newly awarded pensions (48 – 50 % of gross wage). Pension benefits are adequate, only 2-3 % of pensioners fall below the minimum income level.

The benefit formula for determining old-age pensions contains two components that render the system highly redistributive. The first component is a flat benefit equal to 1310 Czech crowns (40 €). The second component is related to an individual's earnings history since 1985, but includes special features that flatten the benefit.

Table below illustrates the high degree of redistribution implied by the current benefit formula. Workers with a 40-year contribution history who earn 50 percent of the average wage obtain a pension equal to 77 percent of their personal wages, while workers who earn 200 percent of the average wage receive a pension equal to 27 percent of their personal wages. The replacement ratios measured against the economy-wide average gross wage are very compressed around the 48 percent average.

OLD-AGE REPLACEMENT RATES AND REDISTRIBUTIVE PATTERN		
Personal Wage / Average Wage	Pension / Personal Wage	Pension / Average Wage
50%	77%	38%
100%	48%	48%
150%	34%	51%
200%	27%	54%

Source: Pension Reform: Approach of MOLSA. 2001. CD-ROM. Ministry of Labour and Social Affairs.

The mechanism for indexing pensions in progress is complex. Over a two-year period, the cumulative increase has to reach, at a minimum, the CPI increase plus 33 percent of real wage growth. In practice, pensions in the recent years (1993-2000) have increased at a rate equivalent to CPI inflation plus 87 percent of real wage growth.

Existing legislation passed in 1995 mandates a gradual increase in retirement ages until they reach 62 for men and 57-61 for women (depending on the number of children) in 2007. At present, the levels are 61 for men and 55-59 for women. The final retirement age will still lie below that of most OECD countries (where the 65 minimum retirement age prevails) and that of other Central European economies, such as Hungary and Poland following recent reforms. Any person with 25 years of service may retire up to three years before normal retirement age, although with a reduced pension. In addition to a lower accrual rate due to fewer years of service, the early retiree is also subject to a penalty of 3.6 percent per year.

Equity is granted to the extent that men and women are entitled to same pension if they have same working periods. Survivor's pension is available to both genders. However, lower retirement age for women will remain even after the reform period will have been finished in 2007.

The payroll tax designated for paying pension benefits and related administrative costs is 26 percent of gross wages. Total social security contributions (including unemployment and sickness benefits) amount to 34 percent of gross wages, of which 8 percent is paid by employees. These rates are significantly higher than average payroll taxes of high-income OECD countries and also surpass the average level of other transition economies in Eastern Europe and the CIS, precluding any possible increases.

Financial Performance in Recent Years

The financial performance of the PAYG scheme weakened steadily throughout the 1990's, shifting from surpluses to deficits at the end of the decade. In 1999 and 2000 the scheme recorded deficits of 1 percent of GDP. The emergence of PAYG deficits was essentially due to an increase in pension expenditures of 2 percent of GDP, driven by a rapid increase in the system dependency ratio (the ratio of pensioners to insured persons). As noted in table below, the PAYG scheme shifted from surpluses into deficits despite an increase in contribution revenues driven by an expansion of the tax base (the covered wage bill). This trend is a marked contrast with developments observed in nearly all transitional countries, which experienced a serious erosion of their tax bases during the same period.

Performance of the Pension Scheme (1993-2000)								
	1993	1994	1995	1996	1997	1998	1999	2000
Revenue (% of GDP)	7.8	8.3	8.2	8.1	8.4	8.3	8.4	8.6
Expenditure (% of GDP)	7.2	7.1	7.5	7.8	8.8	9.0	9.4	9.5
Balance (% of GDP)	0.6	1.2	0.7	0.3	-0.5	-0.7	-1.0	-0.9
Memo items:								
Covered Wage Bill (% of GDP)	28.8	30.4	30.3	31.1	32.2	32.0	32.5	32.9
System Dependency Ratio (%)	49.9	47.6	49.1	48.2	50.7	51.7	54.4	55.7
Replacement Ratio (%)	47.0	44.4	43.8	43.5	45.3	45.9	45.2	44.3

II. Old-Age Income Security

Unlike in other Central European states, pension scheme in the Czech Republic went only through parametric changes so far, no fundamental system changes occurred. Though some of the parametric changes were wide and aimed at removing old injustices, there is still a remarkable room for further reforms.

The pension scheme is well placed in the whole system of social protection in the Czech Republic. We will deal with the latter in the 2nd part of this paper. The Charter of fundamental rights and freedoms covers basic principles of social rights of Czech citizens, which is a part of the Czech constitution. Article 30 say: "Citizens have right for material security in case of old-age, incapacity for work and survivorship." We can find high level of solidarity and redistribution within the pension scheme.

A. Pension Scheme: How Does It Look Like Today?

So far, the Czech Republic has a two-pillar old-age pension system: basic (1st) and individual supplementary (3rd). Draft law on the second pillar – occupational pensions – has been prepared, however the Parliament did not accept the first version in late 2001 and the draft bill is being revised.

1. Basic Pensions

Pension insurance is mandatory for all wage earners and self-employed, people without a gainful activity in the Czech Republic may also voluntarily attend. The insurance is based on payg financing, where both employee and employer contribute. The self-employed pay the total amount of contributions with one exception: sickness insurance is optional for them. The self-employed contribute on the basis of profit with a defined minimum. This minimum is often subject to debate due to the fact, that the self-employed in average pay less then employees as they make use of various tax deductions.

The administration is carried out by a body subordinated to the Ministry of Labour and Social Affairs, "Czech Social Security Administration", which deals with the whole social insurance – i.e. sickness incl. maternity, invalidity, survivorship. Finances (contributions) create a part of the state budget.

EFFECTIVE CONTRIBUTION RATE	Employer	Employee	Total
Social insurance:			
old-age, invalidity, survivors' pensions	**19.5%**	**6.5%**	**26.0%**
Sickness benefits	3.3%	1.1%	4.4%
Unemployment	3.2%	0.4%	3.6%

Health insurance (for health care)	9.0%	4.5%	13.5%
Total insurance contributions	35% of total wages	12.5% of gross salary	47.5%

Social security contributions are tax-deductible and benefits are basically exempt from taxation[1]. There is a minimal limit for all contributions, but no ceiling. This creates room for remarkable redistribution and income "over-solidarity". The minimum is a minimal wage.

There are a number of non-contributory, so-called substitute periods that are taken into account for calculation of entitlement for pension. The state does NOT pay social insurance contributions for "its" insured (students, unemployed, parents on parental leave etc.), but it pays health insurance contributions for these groups – health insurance companies are separate entities, mostly private, while social insurance is still managed under the heading of the state. The scale of substitute periods is enormous in international comparison.

Pensions are two-tier, consisting of a flat rate part and earning-related component. Adjustment is done according to the law in line with increase of wages and prices (combination of both factors).

2. Supplementary Pension Insurance

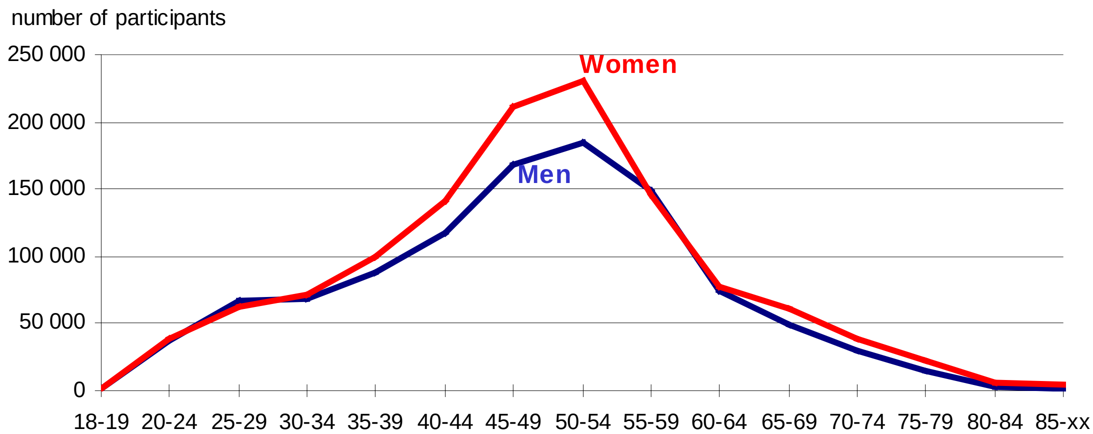
Supplementary pension insurance is voluntary in the Czech Republic and mostly individual. It shall be perceived as the "third pillar" of old-age security – when we use the EU rhetoric, where the second pillar is represented by occupational pensions. However, employers in the Czech Republic have also already started to contract pension plans for their employees. The difference is that they do not run pension funds. Supplementary insurance is possible since 1994, but tax relieves since 2000 have made it more attractive. The insurance scheme offers defined contributions plans.

DEVELOPMENT OF SUPPLEMENTARY PENSION INSURANCE INDICATORS 1994 - 2000							
Indicator	1994	1995	1996	1997	1998	1999	2000
Number of participants (in thousands)	183	1290	1546	1637	1740	2006	2281
Number of participants (as % of economically active)	3.7	25.7	30.7	33.1	35.7	42.7	49.7
Total assets of the funds (in billions)	0.1	4.4	11.5	19.6	28.4	37.7	43.2
Total assets of the funds(as % of GDP)	0	0.3	0.7	1.2	1.6	2.1	2.3
Operating costs(as % of total assets)		9.0	3.3	4.2	3.9	2.5	2.5
Average monthly contribution (amount of state contribution)	118 (43)	262 (93)	305 (103)	333 (97)	329 (93)	339 (96)	351 (97)
Average monthly contribution(as % of average wage)	1.7	3.2	3.2	3.1	2.8	2.7	2.6
Number of pension funds		44	44	38	29	22	19

[1] Pensions start to be subject of income taxation at the level of approx. 1.5 the average pension. For the purpose of taxation, pensions are not added to other taxable income.

Source: Pension Reform: Approach of MOLSA. 2001. CD-ROM. Ministry of Labour and Social Affairs.

When we look at territorial distribution of participants, more than 120 thousand participants are from the capital Prague. Most of the participants are in their late 40's and 50's. Slightly more women than men have supplementary pension



insurance.

When the supplementary system was prepared, it had moderate conditions enabling entry also to people in the pre-retirement age. However, low age for supplementary pension entitlement (50 years) and short waiting period (maximum 5 years) caused unintended effects – people perceived supplementary pensions as a kind of short term savings, not as a supplementary income in old age. It shall be on the other hand also noted that it was a completely new element and people first had to learn how to deal with it. Five years after introduction of supplementary insurance some of its conditions were made stricter on one hand (e.g. entitlement at the age of 60), while on the other the amended act has brought broader motivation items (such as higher state support, tax incentives for both the insured and for employers).

B. How Did We Get Here?

1. A Brief History of the Pension Scheme in the Czech Republic

Czech pension insurance has a longstanding tradition. It was inspired by **Bismarck**'s social insurance in Germany. Taafe's reform introduced social insurance in the Czech lands of Austrian-Hungarian Empire in 1888-1889. The 1st Czechoslovak Republic took over the imperial legal provisions in social sphere in 1918. At those times, many special schemes existed and the insurance was organized according to profession with big preferences for state officers.

Beveridgean influence: the Czech exile government in the U.K. during the 2nd World War prepared a new pension scheme based on universal coverage. The reason for such a step was that the pre-war pension funds' assets were either used during the war by the Nazis or they lost their value. The new, modern pension system was introduced in 1948. It united insurance schemes, tried to balance positions of white and blue-collar workers and for the first time it offered coverage also to the self-employed. This pension insurance had a tripartite administration.

The development until 1948 placed Czechoslovakia into a family of developed European countries. However, new provisions and changes after 1948 were influenced by the soviet pattern. The state took over care for citizens – the change might be labelled as "from social insurance to social security".

Milestones in pension scheme during the communist period:

- Reform in 1952: state administration took over the pension system; insurance contributions abolished, pensions financed from overall taxes
- 1956 categories of workers introduced; retirement age reduced
- 1960 maximum pension introduced
- 1964 pro-natal policy: differentiation of women's retirement age according to number of children raised
- 1988 link between earnings and benefits strengthened: ceiling on retirement income lowered; different indexation according to year of entitlement

Still, some features of the original insurance remained in the Czechoslovak pension scheme: pension formula still to a certain degree encompassed the length of working period and earnings. However, modified.

2. The 90's in Czech Pensions – Several Phases of Pension Reform

1st phase (1990 – 1992). The ultimate goal of the first phase after the "Velvet revolution" was to correct those modifications. Privileged treatment of selected groups of people was abolished, the legislators put in force regular adjustment of pensions and a new, separate administrative body to deal with pension and sickness schemes was established.

2nd phase (1993 – 1995). The second phase started with reintroduced insurance contributions, which replaced financing through taxation. In 1994, voluntary supplementary pension insurance was enacted and thus it broadened the scope of old-age income possible sources.

3rd phase (1996 – now):

- 1996 fundamental, new law on pension insurance enacted
- 1997 economic crisis in the country caused (besides demission of the government, higher unemployment and more claims for early retirement) stricter rules for pension adjustment and limitation of some substitute insurance periods (when no contributions are paid but the period is counted for pension entitlement).
- 2000 tax incentives for voluntary supplementary pension insurance
- 2001 stricter conditions for early retirement and actuarial increase in case of deferred pensions enacted

Can this development be perceived as a reform development? Let's try to define various depths and directions of reforms generally and then use this definition in relation to the Czech development in the 90's.

- Parametric reforms: change some of parameters of the pension scheme, such as retirement age, waiting period, calculating period or type of adjustment.
- Broad parametric reforms: more parameters are changed in a short period of time or the state introduced incentives for voluntary supplementary schemes.
- Partial or full privatisation of the pension scheme: private pension funds as mandatory component of old-age security.

TYPE AND MAIN FEATURES OF CZECH PENSION REFORMS

Parametric reforms	Broad parametric reforms	Partial or full privatisation
Age, calculation period, adjustment, actuarial principles for early and deferred retirement	Tax incentives and state support for voluntary supplementary scheme	Not (so far)

Reforms are however not driven only by actuarial principles or calculations proceeded at ministries or relevant bodies. Such a technical part is only one – and not the main – component of reforms. There are many other factors playing their roles as well and we will try to analyse them.

C. Factors influencing the way how reform strategies are prepared

If we try to categorize and evaluate results of pension scheme development, we shall first select basic factors that influence the type, shape and direction of reforms. The most important factors can be the following ones:

- Factor of historical development and traditional values
- Factor of socio-economic environment of pension scheme
- Factor of influence of various actors (subjects in pension scheme and reforms)

1. Factor of historical development and traditional values

Pension schemes are notwithstanding closely tight to traditional values. These values form or influence the country's social policy and within that also the old-age pensions. Typology of welfare state, no matter whether we look at Esping-Andersen's or Titmuss's or any other one, articulates among others also basic characteristics of pension schemes. Regardless of dynamic development in social protection in general and pension schemes in particular, traditional values can be characterised using several basic parameters:

- Level of solidarity and income redistribution: here we mainly look at difference between the replacement rate for average wage and for high wage. The question of redistribution often only follows the question of replacement rate itself.
- Individual versus collective responsibility: some pension schemes have mandatory pillars that only replace the wage on a very moderate (even low) rate; these schemes rely on individual's decision about further old-age income security. Other schemes offer so high replacement rate that individual do not see any incentives to take part in supplementary pension schemes.
- Way of administration of pension scheme: here we are interested in to what extent is the scheme and its administration separate from the state and the state budget and to what extent do trade unions and employers take part in administration and its decisions. We are also interested in unity of pension insurance.

FACTOR OF HISTORICAL DEVELOPMENT AND TRADITIONAL VALUES

Level of solidarity and income redistribution	Type of welfare state	Individual vs. Collective responsibility	Type of pension scheme administration
High redistribution	Transitive – corporative	Collective (state), increasing support of individuals in voluntary supplementary insurance	Central administration, budget as a part of the state budget; voluntary private funds

2. Factor of socio-economic environment of pension scheme

Dynamic changes of socio and demographic structure and economic environment visibly create pressure on the change of values and traditional approaches to the old-age security. Another key factor in influencing pension reforms emerges. There are several criteria, which we used for finding the "level of urgency" of reforms:

- Ageing of population – number of the elderly to the whole population. Meanwhile, this criterion is influenced by at least two other. The first is decreasing birth rate and the second is increasing life expectancy (among others also thanks to a better health care and thanks to healthier way of life).

- Level of economic participation – dependency index. Employment rate is decreasing. Work patterns are changing, workforce is moving from the production sector to service sector.

- The system probable financial demand towards contributors – expressed by the relation between the number of retirees and the number of economically active people[2].

- Economic severity of the pension scheme: what share on GDP is consumed on old-age pensions (public mandatory schemes)

- Replacement rate of mandatory pension schemes.

On the basis of socio-economic and demographic analysis it is possible on one hand to identify those systems that have serious difficulties and how do they solve the situation and on the other hand those comparatively balanced systems, which try to reduce future threats. Some countries face remarkable pressure on pension schemes; others do not have to implement so broad changes in old-age security. If

[2] The definitions of groups that are used in ordinary statistics are: people above 65 (potential retirees) and 15-64 (potential economically active). This is mainly because of availability of projections for these groups. The interpretation will bear in mind the fact, that current retirement age is lower than 65 in the Czech Republic (as well as in a number of other countries) and the fact, that the start of the first job has been moved to higher age than 15. Real system dependency expressed as a share of pensioners to contributors, is and will be even higher.

we look at international comparison, then for example demographic projections of Italy or Germany show very pessimistic future. Besides that, Italy already now has very low economic participation. Both countries had as a point of departure a corporative (conservative) social security system with high guaranteed benefits and their pension expenditures as a share of GDP were very high. On the other hand when we look at transition countries, we can see comparatively better starting position of Poland than of all other countries thanks to a favourable demographic development and projections.

Demographic development and projections place the Czech Republic in the family of developed countries: low birth rates, average age increasing, dependency rate rising. The following table shows difference between relation of two age cohorts (15-59 and 60+) and the relation of the insured and pensioners. The latter is much more alerting.

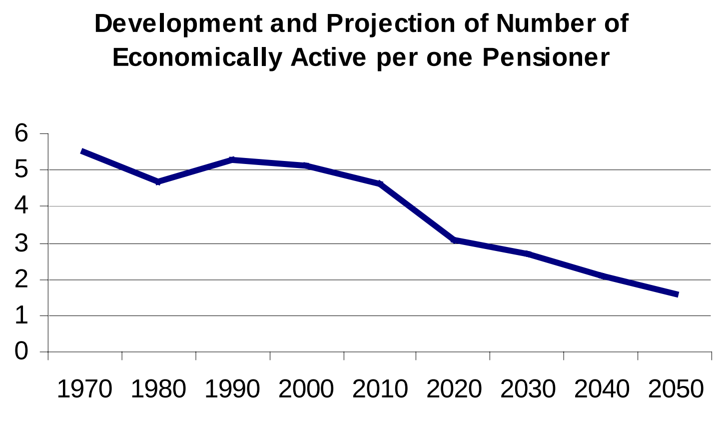
DEVELOPMENT OF DEMOGRAPHIC AND PENSION SYSTEM DEPENDENCY 1993 – 2000

	1993	1994	1995	1996	1997	1998	1999	2000
Number of inhabitants 15-59 (in thousands)	.	6526	6571	6609	6647	6674	6698	.
Number of insured persons (in thousands)	5052	5290	5134	5186	4944	4925	4728	4661
Number of inhabitants over 60 (in thousands)	.	1859	1857	1857	1857	1864	1873	.
Number of pensioners (in thousands)	2521	2519	2523	2498	2507	2545	2573	2594
System dependency ratio (pensioners as % of contributors)	49.9	47.6	49.1	48.2	50.7	51.7	54.4	55.7

Source: Pension Reform: Approach of MOLSA. 2001. CD-ROM. Ministry of Labour and Social Affairs.

Number of pensioners

Similarly to number of contributors – the insured – also the number of pensioners is determined by a demographic development. It can however be remarkably modified by conditions inside the pension scheme – conditions such as length of insurance, age limit etc. The Czech retirement age is comparatively low and it won't change even after the process of increasing the retirement age will have been finished by 2007.



Note: this graph shows relation of number of people aged 15-64 to one person older than 65, which is not exactly economically active to one pensioner.

Source for the graph: United Nations Population Division, World Population Prospects: the 1998 Revision. In: OECD Statistical and Analytical Information on Ageing, NBER-Kiel Institute Conference, Berlin, 20-21 March 2000.

As a consequence of very advantageous conditions of early retirement, this option was used quite often in the 90's and thus the expected positive consequences of increased retirement age were not fully met.

NUMBER OF NEWLY AWARDED OLD-AGE PENSIONS AT RETIREMENT AGE AND NUMBER OF EARLY RETIREES					
Year	Old-Age Pension awarded at the retirement age or later	Early retirement (reduced)			
		Absolute numbers		As a % of all old-age pensions	
		Temporarily reduced	Permanently reduced	Temporarily reduced	Permanently reduced
1996	48,846	3610	7258	6	12
1997	56,514	7958	16,360	10	20
1998	59,299	12,330	43,205	11	38
1999	51,609	12,075	45,853	11	42
2000	39,297	10,085	46,966	10	49
2001	36,940	6576	44,744	7	51

Source: The Czech Social Security Administration

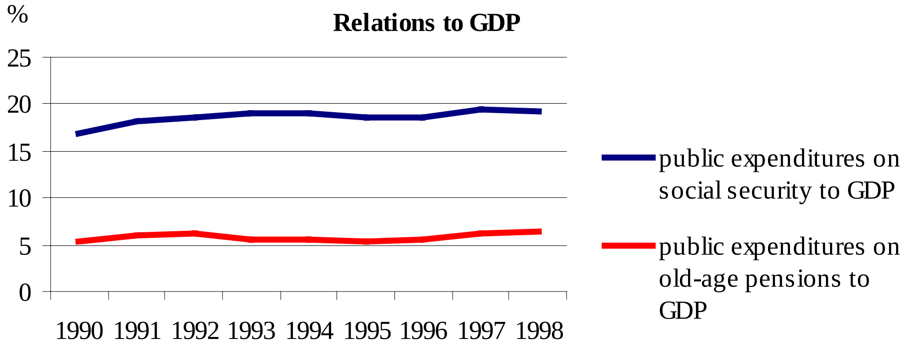
Real age of retirement thus rose more slowly than the legal retirement age. It led to the already mentioned stricter conditions of early retirement that came into force in the mid of 2001. However, the original proposal of actuarial reductions of early retirement on one hand and of actuarial increase in case of deferred retirement were smoothened during the political debates over the draft law.

Economic development

Relatively favourable activity rate of employed population means fairly sound starting position for Czech pension reforms. The administration costs of the basic mandatory scheme are considerably low – on the level of about 1.5% of income from contributions. Expenditures on mandatory old-age pensions oscillate around 7% of GDP, while expenditures on the whole social security show a slight increase over the 90's.

DEVELOPMENT OF VARIOUS PENSION SYSTEM INDICATORS								
	1993	1994	1995	1996	1997	1998	1999	2000
Administration costs (bil. CZK)	1.8	2.4	2.7	3.2	3.0	3.1	3.3	3.3
Unemployment rate	3.0	3.3	3.0	3.1	4.4	6.0	8.5	9.0

Source: Pension Reform: Approach of MOLSA. 2001. CD-ROM. Ministry of Labour and Social Affairs. Bulletin No.16, RILSA. 2001



International comparison[3] - can we learn from that?

When we apply cluster analysis on socio-economic indicators ageing of population, dependency ration, demographic dependency, economic participation and a share of pensions on GDP in 80's and at the end of 90's, the Czech republic is placed as follows. The closest, when measuring the distance from the centre of the cluster, is Switzerland followed by Hungary and Great Britain, the U.S.A., Italy and Sweden. If we look only at clusters as such, our partners in same clusters are (in order according to number of times in same cluster) Poland and Hungary, Slovenia, Switzerland, the U.S.A. and the U.K., Sweden and only once it is Germany and Italy.

If we look at reforms that led to a current stage in various countries, we can say that the Czech Republic is close to Slovenia. Both countries have defined benefit payg basic pension schemes, which guarantee two-tier benefits composed of a flat rate part and earnings-related part and both countries have further pension "pillar" with voluntary participation, which is supported by state. Though past developments of some socio-economic indicators were different, economic participation of inhabitants is similar and particularly their demographic projections are almost identical. Number of children is continuously decreasing due to lower fertility rate; number of pensioners is increasing due to higher life expectancy. Both countries are of similar size, they have to solve similar problems that stem from demographic development and at the same time, both go under an important and demanding transition from centrally directed economies towards democratic market economies. Both used to be parts of the same Austrian-Hungarian Empire at the beginning of the 20th century and thus have similar traditional values. We can say that proposals of pension reforms stem from very similar conditions in these two countries and have very similar consequences.

We can say (also on the basis of international comparison not mentioned expressly in this paper) that **an ideal approach to pension reform does not exist**. Reforms of pension schemes are very up-to-date theme in most of developed and transitional countries. The chosen reform strategies differ; however, we can identify several common features. Reason for the fact that ideal strategies are often subject to discussions but scarcely subject to agreement lies in the reality, that inhabitants of different countries have different expectations towards their respective national systems. These expectations stem from traditional perception of the role of state as well as of individual responsibility. The expectation can, in times of reforms and mainly in times of their preparation, come through remarkable mutations. It is up those who prepare reforms to submit the proposals to the public well in advance and well prepared and to try to gain the biggest possible consensus. There are many factors playing role during those "public discussion periods". The expectations of the public may be influenced by immediate feelings, which stem

[3] Comparison of nine European countries and the U.S. in Vylitova, Macha, Vyhnakova [2001].

from both objective circumstances, such as economic and demographic projections, outlook on the EU integration, foreign debt or international conventions) and from subjective ability of different groups of actors (experts, reformers) to put through their respective arguments.

The most often questions regarding pension reforms deal with the matter of partial or overall reforms. Is it possible to maintain high protection of the post-productive population, which carries a burden of ageing and a burden of smaller group of active (productive) population in developed countries? Is it possible to cope with future problems with financing of pensions only by changes of technical parameters of the current pension schemes or is it necessary to adopt radical reforms and to individualize and privatise old-age income security? Any clear answer does not exist. The only recommendation is **diversification of old-age income sources**. International organizations, mainly the World Bank, but also the ILO do not only support this recommendation; it is also being introduced in many countries. A natural consequence is unification of various special pension schemes[4] or increase of retirement age. There is no need to retire before 60 and to receive old-age pension for twenty years if the life expectancy has risen by 4 years over the last twenty years and if the employment shifted from industry to service sector.

Reforms in various countries differ in their speed, extent, in sequence of their steps due to different historical, political, economic and social context of hitherto development. We can generally say that pension schemes tend to converge. Governments and social partners have to focus on securing the broadest possible income basis for the public (general) pension scheme and also to focus on introducing a viable mix of pillars of old-age income security, which would support each other. Whatever are the case, a **successful system as well as successful and acceptable reform shall guarantee stable rules and transparency**.

The EU member countries highlight a need of “European approach” to European social security – although nothing like that actually exists. When it comes to reforms, European countries have so far mostly introduced parametric reforms only, which were accompanied by diversification of income sources from voluntary fully funded schemes, where participation is often supported by state.

Lets apply statistical methods (mainly cluster analysis and box plots in one-dimension analysis) to individual factors of socio-economic circumstances of pension schemes and of influences of their development in recent years. On the basis of that we can confirm a fundamental difference between Central and Eastern European countries in transition and the EU member states. Although this statement seems to be a trivial certification of clearly visible facts, distances

[4] Such as special scheme for farmers or for civil servants or for the self-employed etc.

between clusters show importance of further influences that step into the reform processes in pension schemes. We can find several examples. Czechs and Slovenians has chosen different path from Poland and Hungary although their socio-demographic indicators would have predetermined another development. We can also identify different reform goals in similar environment in strong market economies of Western Europe.

We shall mention here a proximity of Czech conditions to those countries that have chosen partial privatisation of their pension systems, be it either Hungary, Poland, Sweden, Italy or in some indicators even the U.S.A. or Switzerland. The first four represent to a certain extent traditional schemes, where the mandatory part covers most of retirement income. It is questionable whether the Czech Republic belongs to that tradition. The first two countries are just as the C.R. transitional. Let's also notice the two last mentioned countries, which meet with the C.R. in cluster analysis of socio-demographic indicators: those are countries typical by their liberal and individualised approach to social protection.

D. Political Economy of Pension Reform - Factor of influence of various actors (subjects in pension scheme and reforms)

Our team have characterised basic approaches towards pension reforms among individual international organizations, which often play crucial role in pension reform decision-making in various countries. What international institutions can be taken into consideration? It's mainly the EU and the World Bank, followed by the ILO and OECD. E.g. the World Bank is remarkably strong actor in pension reforms in some CEE[5] countries. In the case of the Czech Republic, the World Bank did not, contrary to Poland or Hungary, play a big role in the outline of pension system in the of 90's, when it strongly supported privatisation of pensions. It showed its preferences, but thanks to the given economic results the Czech government was not forced to adopt those preferences. The Bank shows its very clear preference for pension privatisation, however in some cases it recommends a step-by-step reform: to start with NDC and possibly continue with fully funded scheme only after the high acquired rights of current pensioners will have been met.

However, also further subjects (actors) take part in processes of pension reforms. They influence the direction and overall character of reforms either directly or indirectly. Among these important actors we can find the ones mentioned in the table at the end of this chapter.

Exact roles of these actors are different in different countries, just as their powers and influences in pushing forward the preferred approach are. They also make use

[5] CEE stands for Central and Eastern Europe

of different methods of carrying their interests and recommendations. We cannot omit political factors in analysing pension reforms. It's particularly important for countries in transition – but not just for them. For example the trade unions were in the Czech Republic opponents of any reforms and wanted to keep status quo – no increase of retirement age, no lengthening of required working years etc. although they knew all the conditions and consequences of such an approach.

FACTOR OF INFLUENCE OF VARIOUS PENSION ACTORS
1 no influence – 5 important influence

Experts	European Commission	Ministry of social affairs	Ministry of finance	Politicians	Pension scheme administrators	Trade Unions	Employers	ILO	World Bank
3	3	5	3	4	1	4	2	2	2

E. The Future of the PAYG Scheme in the Absence of Reforms and Reform Options

The World Bank carried out a mission of technical assistance in the Czech Republic in 2001. The WB's actuary has developed a simulation model, which may be used for illustration and simulation of various reform paths. A model was introduced to the Czech partners in 2001 and supplemented thus a row of models tested by the Czech Ministry of Labour and Social Affairs. The WB's simulations indicate the need to implement a strong reform package, in order to prepare the pension system for the two adverse demographic shocks projected for the coming decades. In the absence of reform, the pension system would generate large and increasing deficits, reaching more than 8 percent of GDP in 2050. In addition to the prospect of large financial imbalances, the Czech authorities are also concerned that the high degree of redistribution in the pension system may eventually weaken the incentives for the self-employed and higher income workers to contribute, and lead to an erosion of the tax base (though tax evasion).

As regards the possible reforms, the WB analysed various options and came to a conclusion that NDC system with parametric reforms would have some advantages over a pure package of DB parametric reforms. The NDC system would be able to adapt itself more easily to unforeseen demographic shocks. Both the strong package of DB parametric reforms and the combination of NDC with parametric reforms would tighten the link between contributions and revenues, which may be one of the objectives of the reform. According to the World Bank and in line with its primary objective of alleviation of poverty, the simulations however indicate the need to introduce a minimum, top-up pension guarantee amounting to around 25 percent of the average wage, in order to avoid that low-income workers fall under the poverty line.

The WB's projections show that as other countries in the region, the Czech Republic will also experience rapid population aging over the next few decades due to low fertility rates and increased life expectancy. Baseline demographic projections that approximate recent estimates by the Department of Demography and Geodemography of the Charles University indicate that the old age dependency ratio will jump from 30 to 45 percent over the next 15 years, and will reach 56 percent by 2030. Thereafter, the old age dependency ratio will suffer an even more accelerated rise until the mid-2050's at which time it will improve slightly (due to a moderate increase in the fertility rate projected for the next decades).

The negative demographic developments will put an enormous strain on the PAYG scheme, particularly the second demographic shock that will generate explosive deficits. Using the already mentioned WB's "C-PRISM" model developed for the Czech pension system, it is projected that the deficit will widen to an unsustainable 2.3 percent of GDP by 2015 and continue to increase to staggering levels, reaching a peak deficit of more than 8 percent in 2050. To balance the system, the contribution rate would need to jump from the current rate of 26 percent to 53 percent in 2050.

SIMULATION OF THE PAYG SCHEME IN THE ABSENCE OF REFORMS (AS PERCENT OF GDP)

	2000	2005	2010	2015	2020	2030	2040	2050	2060	2070
Old-age dependency ratio	30	33	39	45	49	56	73	82	79	77
Balance (% of GDP)	-1.1	-0.9	-1.3	-2.3	-3.0	-4.7	-7.6	-8.7	-7.8	-7.0
Expenditures (% of GDP)	9.7	9.6	9.9	10.9	11.6	13.3	16.1	17.1	16.3	15.5
Contribution rate to balance the system	29	29	30	33	35	40	50	53	50	47

Note: Forecasts assume the flat rate remains constant as a percent of the average wage.

Reform is unavoidable and needs to be addressed soon to avert the fast rising deficits. Given that total social security contributions are already high, amounting to 34 percent, there is clearly no room for any payroll tax increase that could induce negative labour market effects. Financial viability will have to focus on constraining the explosive rise of expenditures and linking them more closely to resource availability. The elimination of the actuarial imbalances can be achieved by implementing "parametric reforms" to the existing Defined Benefit (DB) system, or by moving towards a Notional Defined Contribution (NDC) system. These reforms will invariably involve a decline in replacement ratios, particularly for young workers. To avoid an excessive decline in the replacement ratios of young generations, the authorities may need to combine these alternative PAYG reforms with the introduction of a mandatory and funded pillar capable of offering higher returns. The following sections analyse the impact of different reform options on the total balance of the system and the replacement ratios of different cohorts and income classes.

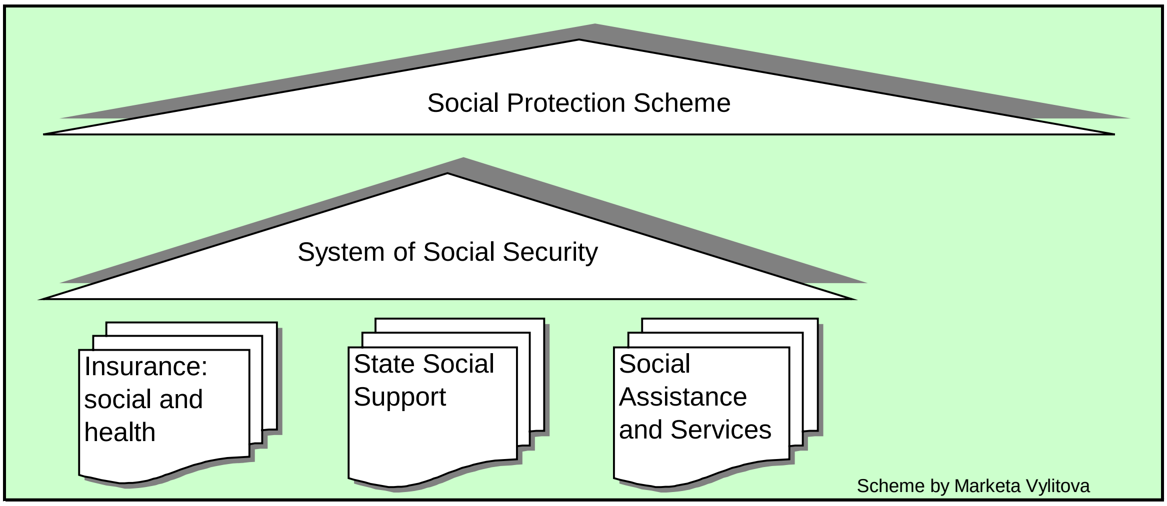
III. Pensions as an Integral Part of Social Protection System in the CR

Welfare state typology created for and applied to the developed countries used to recognize three basic types: liberal (focus on individual), conservative (focus on work effort with maintenance of status differences) and social-democratic (where all contribute and all benefit). No matter how much have the ideal types converged and how criticised the typologies have been, we can use it as a basic tool for setting the Czech welfare state to a certain “family”. If we try to characterize the Czech welfare state according to that typology, we may say that it tends to follow the corporative paths. It has its pension entitlements based on working periods. But it has universal scheme, including the self-employed.

A. Social Security System in the Czech Republic

Since 1989 there have been attempts to reform the system of social security, the conception of which is based on three fundamental tiers, already mentioned above: social insurance, state social subsidy and social assistance.

Besides the three outlined schemes there are also other policies, which aim at protecting and development of inhabitants. One of them is housing policy, where the state supports people who invest in their housing. Education free of charge can



act as another example. However, we will deal with social security system only.

Besides pensions, health, unemployment and sickness schemes, the major role in protecting families is played by the so-called State Social Support scheme. Though drafted as a scheme with income-tested benefits, entitlement conditions are set in remarkably wide brackets and thus almost all families are entitled to the most frequent benefit from this set, child allowance. In February 2002 the Lower Chamber passed the governmental proposal of universal child allowances thanks to the left-wing parties' MPs, however it is believed that it won't be adopted by the Upper Chamber as the political composition there is more right-wing.

The following table shows the composition of state social support expenditures from the year of enactment, 1996, until 2000. It also indicates public expenditures on social support as a share of GDP, which flows around 2 %. The only exception to a stable development in expenditures is a significant increase in expenditures on housing benefit over the five indicated years. Rents are still subject to state-given ceilings and thus further increase in housing benefit might be expected.

STRUCTURE OF STATE SOCIAL SUPPORT BENEFITS 1996 - 2000

In %	1996	1997	1998	1999	2000
Child allowance	43.06	42.74	38.78	39.82	40.02
Social allowance[6]	22.05	21.29	21.17	19.95	19.46
Parental allowance[7]	25.98	26.04	26.25	24.64	24.14
Birth grant (one-off benefit)	1.71	1.80	1.90	1.81	1.82
Maintenance allowance	0.12	0.09	0.08	0.06	0.05
Housing allowance	2.39	2.78	4.61	6.65	7.90
Foster care benefit	0.51	0.53	0.79	1.01	1.06
Transport allowance	2.96	3.21	3.19	3.17	3.28
Funeral grant	1.23	1.13	1.75	1.73	1.70
Energy prices compensatory allowance		0.23	0.93	0.75	0.33
Rent prices compensatory allowance		0.17	0.55	0.41	0.23
State social support benefits total	100.00%	100.00%	100.00%	100.00%	100.00%
GDP accounted for by state social support	1.96%	2.04%	2.11%	2.25%	2.22%

Source: Labour and Social Affairs Statistical Yearbook 1996, 1997, 1998, 1999, 2000, 2001. Prague; RILSA Bulletin No. 16, Prague 2001

Then, there is an issue of poverty. Does it exist in the Czech Republic? And if, in what scale? What are the circumstances of benefiting from social assistance benefits? A scale of benefits aimed at combating poverty might be found under the state social support scheme and under the social care (assistance) scheme. Entitlements to these benefits and their levels are derived from the subsistence minimum.

Specific mechanisms forming a **social safety net** were prepared and introduced at the very beginning of the transition period. The social safety net is designed to safeguard people who unwillingly find themselves in poverty and for whom there are no other sufficient social protection devices. These mechanisms mainly include the set of minimum income quantities such as the minimum wage and the subsistence minimum as the minimum guaranteed income. Until 1995 also a minimum pension (when the sole source of income) existed, now the minimum possible income of the pensioner equals his or her subsistence minimum. The

[6] paid to low-income families with children
[7] paid until 4 years of age of the child in case of full-time care by one of parents (i.e. no kindergarten or nursery school)

safety net needed to be introduced before the economic transition begun to assist those affected by the changes in economy and by occurrence of new phenomena such as unemployment.

The official **subsistence minimum** (SM) takes centre position in the system. It expresses the socially recognised lowest level of household's income and expenditure, that is sufficient to cover the sum of possessions and services necessary to satisfy basic needs. The subsistence minimum only provides protection from material need temporarily, expenditures on articles of long-term consumption are excluded and in case that income stays insufficient for longer than 12 to 18 months, other social protection measures shall be used (such as one-off social assistance benefits to renew articles of long-term consumption, services etc.). Hand in hand with the subsistence minimum goes the mechanism of the **minimum wage** (MW). It was introduced in the beginning of 1991, as part of the legal definition of wage and pay-fixing mechanisms in private and public sectors. The level of the minimum wage and conditions of its application are laid down by law and government ordinance. The existing **relationship** between the subsistence minimum and wage levels acts however as a disincentive to work. Reason for this can be found in the philosophy of both measures: while subsistence minimum aims at securing households, minimum wage protects an individual worker (employee). Minimum wage and even wage below the average does not "pay off" for more-member households as social benefits are based on subsistence minimum, which is in such a case higher then wage of the breadwinner. We can, in fact, talk about social parasitism that is supported by the SM-MW relationship. It shall be noted that the system of **Social Assistance** represents also a system, which is designed to protect by benefits and services also citizens whose personal situations are complicated by health or further social handicaps. The system has been under a reform process since the first half of the 90's, however a new law has not yet been passed.

TRENDS IN AVERAGE MONTHLY SIZE OF CHILD ALLOWANCE, SOCIAL ALLOWANCE, PARENTAL ALLOWANCE AND BIRTH GRANT IN 1992, 1996 AND 2000; COMPARISON WITH TRENDS IN WAGES – IN CZK

Year	Parental allowance	Child allowance	Social allowance	Birth grant	Average wage	Minimum wage
1992	1200	200 - 1720[1)]	average per child 243[3)]	3000	4644	2200
1996	2112	198 – 650[2)] average per child: 475	177 - 762[4)] average per child: 984	5240	9676	2500
2000	2409	224 – 740[2)] average per child: 502	200 - 867[4)] average per child: 1054	6400	13,289	5000

Note: Where a range is given, law sets the values; the average values are calculated from the actually paid-out allowances

[1)] paid out according to the number of children: 200 CZK for one child, 1720 CZK for 4 or more children

[2)] if the right has been incurred; paid out according to the age of the child and in dependence on the family income (not paid out to families with incomes over 3 times the subsistence minimum)

[3)] according to the statistics of family budgets (in: Hirsl, 2001)

[4] if the right has been incurred; paid out according to the age of the child and in dependence on the family income (not paid out to families with incomes over 1.6 times the subsistence minimum)

Sources: Data from the Ministry of Labour and Social Affairs; Statistics on family budgets of the Czech Statistical Office; Trends in economic and social indicators in CR 1990 - 2000, No. 16, Prague, RILSA 2001

The third pillar of social security system in the Czech Republic is the (partly) already mentioned system of **insurance**. Besides the pension scheme the **social** insurance scheme protects against the risk of loss of income due to loss of employment, illness, invalidity or death. Old-age pensioners, who are not able to take care after themselves, can be granted a pension increase on behalf of this incapacity. The system of **health** care is administratively and financially separated from the system of social insurance. The former ensures medical care and provides material health care benefits, while the latter provides monetary benefits in the case of illness and childbirth.

We can see that old-age pensioners mainly benefit from two schemes. Those are social insurance (be it invalidity or old-age) and social services (be it in kind or in cash). We shall not obviously forget about health insurance scheme, but that's in the Czech context a different issue.

B. Financing of Social Security

In describing the means of financing it is necessary to distinguish individual schemes within the framework: social insurance, health insurance, state social subsidy and social assistance.

Contributions for social insurance schemes are set as a percentage of wages. Employee pays One quarter and the employer pays three quarters. Under insurance scheme these are financed:

1. Sickness and maternity benefits
2. Old-age, invalidity and survivors pensions
3. State employment policy (unemployment benefits, active employment policy programmes and measures).

State social support (subsidy) benefits are granted as mandatory and paid from the state budget through district offices.

Benefits paid under the scheme of social assistance do not follow same pattern of financing. Part of that is mandatory, granted by legal provisions and paid basically from the state budget, again through district offices. However, some of these benefits, both in cash and kind, are under discretion of either district or municipal offices and then paid by the mentioned as well.

C. General policy context

With the aim of economic transition development, it is desirable to maintain social peace and stability. None of Czech political parties has cast doubts upon the importance of social dimension of transition. The public itself puts social assurance on the second place among its basic needs. Although liberal rhetoric has been widespread, it might be said that social assurance was given a serious respect during the previous twelve years.

However, it shall be mentioned that economic transition was the first to fulfil, which was not followed by any clear strategy of social policy. On one hand the right wing parties highlighted the need of strengthening individual responsibility and goal–oriented social assistance. On the other hand the left wing parties pointed out risks of social exclusion as a consequence of inflation and unemployment. Christian Democrats tried to mix market principles and social solidarity. All these mentioned approaches stayed however at the level of general formulations.

The development of the main concepts of reform can, from the pension reform point of view, be used to differentiate three important phases, which has been the basis for further decision making and implementation procedures.

Social policy was not listed among the most serious tasks of the first period of transition. During that time low unemployment rate played an important role, and thus social problems were not so emerging. The first stage can be labelled as a „Federal concept“. Predictably, it can be dated from the year 1989 to the division of the Czech and Slovak Federation. Its characteristics are as follows:

- An inclination to a „Bismarckian Model“ - the reform concept has mostly been inspired by the classical system of legal public (social) insurance or its combination with other approaches,
- Tendency to accept elements of corporation,
- Willingness to create a pension security fund (and/or other social funds) within the privatisation of state enterprises.

Second period. More comprehensive idea of the reform of social security was introduced no earlier than after 1992 elections, after the “divorce” of the Federation. Liberal principles became the highlighting ones:

- An attempt to transfer the wage component of pensions to other systems.
- The consistent maintenance of the citizen principle and citizen equality.
- Attempts to enforce radical reforms of the pension system.
- Attempts to enforce radical changes of health care system.
- System corresponding to the needs of the market economy.
- Stimulate individuals and social groups towards assuming greater responsibility for their own social situations and achieving social independence with a view of reducing reliance on state benefits.
- Comply with international conventions and with the need to harmonize the legislation with European social insurance systems.

Third stage started in 1997 when social democrats started to be a strong opposition in the Parliament, deepened by their governance that started in 1998.

- Several increases of minimum wage with aim to remove incentives to social parasitism.
- Proposals of universal child benefits (so far means-tested, but almost everyone is entitled).
- Incentives to take part in voluntary supplementary pension insurance.
- More actuarial principles in basic pensions applied.

During the transition period, Czech social policy has played two basic roles - an instrumental and a conceptual one. The instrumental role was to create tools to compensate for the social impact created by the economic transition and to ensure the necessary political support for that transition. The conceptual role encompassed efforts to design a social reform package representing a new concept of social protection of the population.

Economic transition in the Czech Republic has progressed without serious social conflicts and upheavals, in spite of the fact that numerous parts of the population have been adversely affected. This favourable result can surely be credited, to a considerable extent, to a well-designed social policy.

IV. Conclusions and outlook for the future

The **pension insurance** act in the Czech Republic represents the first CEE pension reform, though it remained payg financed, one-pillar. That act introduced dynamics of the system that was needed in new economic environment. Newly awarded pensions retain their value thanks to more accurate system of pensions adjustment. Process of increasing retirement age has started as well as process of lengthening of calculating period, some items of flexibility were introduced in the system and so were widower's pensions. Even though the administration body is not independent, there is at least a separate account within the state budget, which enables to clearly define balance of the pension scheme.

In the **supplementary pension scheme** with a state subsidy still remain some imperfections, which are planned to be removed by an already prepared amendatory act. So far, supplementary scheme operates mostly with low contributions and has older insured persons who have joined the supplementary pension insurance plans. The state offers in this respect tax incentives that might be interesting also for younger generations.

Klimentova, a Czech ministerial pension expert, says (2002): "**Reform process** in area of social insurance may be evaluated and perceived as very positive, compared to other countries in transition. The Czech Republic became in 1996 one of the first CEE countries where substantial pension reform was realized. This fact is often forgotten in international assessment in light of recent reforms carried out in Hungary and Poland, which led to a certain extent to mandatory fully funded pension schemes. Those countries, however, not earlier than in relation to the essential concept changes realize such measures like increase of retirement age, unification of the system, abolishment of privileged groups, change of benefit formula etc. All these changes were in the Czech Republic introduced already in the 1st half of 90's. So was the Czech Republic the 1st CEE country to establish a scheme of voluntary supplementary pensions. That basic architecture of the pension scheme made the Czech Republic different from most of EU member states, where a three-pillar system is perceived as a standard one[8]. Occupational pension scheme still lacks in the full range. Supplementary pension insurance with a state subsidy is more perceived as an individual form of old-age income security."

Here are some key conclusions that has emerged from the WB's technical exercise:

- The aging demographics will put ever-growing pressure on the finances of the PAYG scheme with deficits rapidly accelerating. The deficits will become

[8] By 3-pillar system we understand: basic mandatory scheme, occupational pensions (often fully funded) and individual schemes.

even more explosive after 2040 when the system undergoes a second demographic shock.

- A combination of strong parametric reforms to the DB scheme (retirement age increase to 63 years of age, adoption of price indexation, freezing of the flat benefit, and elimination of non-contributory years for students) can bring stability to the system, but would reduce significantly the replacement rate. Maintaining the replacement rate would require further increases in the retirement age that might be difficult to introduce.

- The gradual transformation of the DB PAYG system into an NDC system with automatic financial stabilizers would eliminate the imbalances in the long run and produce a pension system that is more resilient to adverse demographics and uncertainties in labour market trends. However, a reform restricted to the introduction of an NDC scheme would take a long time to eliminate the PAYG imbalances. Therefore, it would be essential to combine the NDC with parametric reforms.

- To maintain a balanced PAYG and prevent a decline in the long-term replacement rate, the authorities could consider a combination of PAYG reforms (involving the NDC and parametric reforms) with a funded scheme (the second pillar). The NDC cum parametric reforms would produce a long-term replacement rate equivalent to 35 percent for the average-income worker, while the two-pillar system could secure a replacement rate closer to 45 percent. However, it would be essential to start the PAYG reforms without delays, in order to create a cushion for the introduction of the second pillar.

An alternative scenario would involve not introducing the second pillar, but making efforts to increase coverage in the third pillar, primarily of younger workers, who will suffer the largest cuts in the replacement rate. The introduction of DC occupational funds may contribute to an increase in the coverage of young workers and an increase in contribution rates, as noted below. However, the increase in coverage and in the average contribution may still prove insufficient to ensure an adequate replacement ratio for young and unborn generations. For this reason, the Government will have to follow closely developments in this area and maintain open the option to introduce a mandatory funded pillar in the future.

Despite some positive features, the Czech third pillar will still need to be substantially strengthened, in order to become a significant and reliable source of supplementary retirement income. Coverage of the labour force is not as high at it seems, as nearly 20 percent of participants are above 60 years of age and retired. The significant participation of older workers has raised the average age of participants to nearly 49 years of age. Particularly workers under 35 years of age are not well covered by the third pillar. The inadequate coverage of younger workers is a source of concern, as these are precisely the generations that will be more affected by the inevitable reforms to the PAYG scheme, and that will be more dependent on supplementary sources of retirement income.

In addition to the narrow coverage of young workers, the Czech third pillar has other weaknesses that will prevent it from playing its expected role in the provision of retirement income. Average contributions to the system have remained small – below 3 percent of average wages. Largely because of the low level of contributions, total assets have grown at only 0.3 percent of GDP per year in the recent years, and amounted to only 2.3 percent of GDP at end-2000. Recent withdrawals of accumulated balances by older workers (allowed by the short minimum periods of accumulation) have also contributed to the slow growth of assets.

The World Bank's expert's conclusion was that despite the successful effort of regulators to eliminate the weakest institutions and to improve regulatory standards, the performance of the Czech third pillar in the first seven years of operation has been rather disappointing. The Czech private pension system seems to share the weak aspects of the open systems operating in Latin America (e.g., large marketing expenses and high costs, relatively short time horizons) and the occupational systems operating in the OECD (e.g., insufficient disclosure and transparency) without sharing the strong aspects of either one (e.g., greater transparency of systems based on open funds, long time horizons and lower costs of systems based on occupational funds). While some of these deficiencies may be corrected by further improvements in regulation and supervision, structural changes will be required to ensure that Czech workers have access to a reliable private pension system, capable of operating with lower costs and of generating higher returns.

Currently, **discussions** about several issues are held in the Czech Republic:

- Mandatory 2nd pillar in old-age security; draft law on occupational pensions did not pass the Parliament late in 2001

- Long discussions about separation of administration of basic pensions from the state budget; draft law on Social Insurance Company was not adopted either in 2001

- A relatively new issue: discussions about transferring the current payg-financed basic pensions into NDC; that would allow closer link between contributions and benefits

The Czech Republic now has a unique chance to learn from reform developments and outcomes in countries, which had similar starting point. Feedback regarding European reforms is available already now and so are their first outcomes. That fact can largely ease the situation of other countries, which are now in preparatory phases for reforms. It is visible already now that it is necessary for introduction of fully funded mandatory schemes to take many indicators into account, namely those indicators that influence a successful transition. However, even if reformators take all the necessary indicators into account, a mandatory fully funded scheme does not have to solve all problems connected with demographic, social and economic development of the new millennium.

Our analyses also confirm that preparation of pension reform, finding consensual solutions and in future also communication of the adopted concepts cannot be narrowed to technical argumentation of effectiveness and financial stability of the system only. As was mentioned already, incoming factors are so manifold and have to underpin historical, social, economic and last, but not least also political circumstances.

A consensus among society as well as among important actors is essential for smooth adoption and for reform process as such. Besides individual responsibility, so highlighted in private pension schemes, we shall not forget redistributive role and solidarity in sharing risks of ageing. Basic schemes shall retain these roles.

The only possible way of future development of the Czech pension scheme will probably be a closer link between contributions and benefits in basic mandatory scheme, higher retirement age and high support of “pension market”, as referred to by the WB’s experts - either to introduce occupational scheme or attract more younger people into the current supplementary scheme. Taking international experiences and politico-economic analyses of Czech development into account, it seems that the Czech Republic is facing a clear, start-up decision on the level, to which attendance in privatised funded schemes will be voluntary or mandatory. That choice is sensitive not only to socio-economic factors, but also – and often – to factors of traditional values, of influence and respect that individual actors possess in society. Maximal rationalization of such a decision shall further be encompassed by detailed analyses of situation in present and future preferences and expectations of Czech society. Strong economic growth and steady reduction in unemployment, combined with sustaining high levels of employment for both men and women would make a considerable contribution to tackling the demographic challenge facing the pensions.

The Czech republic is facing elections, which will take place in June 2002. There are substantial variations among political parties regarding a desirable system of old-age income security and regarding the scope of Czech welfare state as such. The upcoming elections shall besides other things also answer questions such as “Will separate Social Insurance Office be established to manage basic mandatory pensions?”, “Will occupational pension scheme be introduced as mandatory? And if so, what shall be the relation (share) of basic and occupational part in individual’s pension?”

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