

Actuarial Report on Social Insurance

2006

Ministry of Labour and Social Affairs
Social Insurance Department

TABLE OF CONTENTS

INTRODUCTION	11
PART A	
GENERAL INFORMATION ABOUT SOCIAL INSURANCE	13
A.1. Brief characteristics	13
A.1.1. Pension insurance	13
A.1.2. Sickness insurance	16
A.1.3. Financing	17
A.1.4. Social security organization and implementation	18
A.2. Legislative changes since the beginning of 2004	20
A.2.1. Pension insurance	20
A.2.2. Sickness Insurance	24
A.2.3. Premiums	26
PART B	
EVALUATION OF THE BASIC INDICATORS OF SOCIAL INSURANCE DEVELOPMENTS	27
B.1. Parametrs influencing the development of social insurance	27
B.1.1. Economic developments	27
B.1.2. Demographic developments	28
B.1.3. Employment developments	31
B.2. Social insurance indicators	33
B.2.1. Premiums	33
B.2.2. Pension insurance	40
B.2.2.1. Revenues and expenditure	41
B.2.2.2. Number of pensioners and pensions	43
B.2.2.3. Amount of pensions	52
B.2.2.4. Reduction of pensions due to early retirement	62

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B.2.2.5. Differentiation of pensions according to pension amount	63
B.2.3. Sickness insurance	65
B.2.4. Fulfilment of international conventions	72
B.2.4.1. Pension insurance	72
B.2.4.2. Sickness insurance	76
B.2.5. Operational expenses	77

PART C

SOCIAL INSURANCE PROJECTIONS 79

C.1 Projections of parameters influencing social insurance development	79
C.1.1. Development of basic macroeconomic indicators	79
C.1.2. Demographic development	81
C.1.3. Developments in the participation rate	82
C.2. Pension insurance	85
C.2.1. Projections of basic indicators	85
C.2.1.1. Developments in the number of contributors and pensioners	85
C.2.1.2. Developments in revenues, expenditure and the total replacement ratio	87
C.2.2. Evaluation of developments in key indicators	89
C.2.3. Sensitivity of basic indicators of the pension insurance system on certain parameters	90
C.2.3.1. Additional increases in the retirement age	90
C.2.3.2. Method of valorizing pensions	94
C.2.4. Developments in the disability rate and its impact on pension expenditure	97
C.2.5. Motivation for deferring retirement by other means than raising the retirement age	99
C.2.5.1. Implicit tax	99
C.2.5.2. Early old-age pensions	100
C.2.5.3. Deferred old-age pensions	101
C.2.6. Conclusions	103
C.3. Sickness insurance	110
C.3.1. Projections and evaluation of developments	110
C.3.2. Conclusions	116

APPENDIX

I. EXAMPLES OF BENEFIT CALCULATIONS 121

A. Example of a pension calculation	121
B.1. Examples of sickness insurance benefit calculations (year 2006)	125
B.1.1. Sickness benefit	125
B.1.2. Financial support for care of family members	127
B.1.3. Maternity benefit	127
B.1.4. Pregnancy and maternity compensation benefit	128
B.2. Examples of calculations of wage compensation and sickness insurance benefits (year 2007)	130
B.2.1. Sickness benefits and wage compensation	131
B.2.2. Financial support for care of family members	133
B.2.3. Maternity benefits	134
B.2.4. Pregnancy and maternity compensation benefit	134

II. OVERVIEW OF MAIN MEASURES ADOPTED SINCE 1990 136

A. Pension insurance	136
B. Sickness insurance	139
C. Premiums	141

III. AGREEMENT OF THE POLITICAL PARTIES ON THE CONTINUATION OF PENSION REFORMS 143

LIST OF TABLES

Table 1 Contribution rates from 2004 (% of the assessment base)	18
Table 2 GDP Development	27
Table 3 Developments in the average nominal wage in the national economy	28
Table 4 Age structure of the population	29
Table 5 Total fertility rate, life expectancy	30
Table 6 Participation rate	31
Table 7 Number and structure of insured persons	34
Table 8 Average assessment base for premiums	36
Table 9 Comparison of prescribed premiums and payments from 1999 to 2005	37

Table 10	Structure of receivables for contributors (CZK millions)	39
Table 11	Pension insurance revenues and expenditure for pensions	42
Table 12	Expenditure on pensions according to type of pension (Chapter 313 – Civil Sector)	42
Table 13	Number of pensioners according to type of pension	44
Table 14	Proportion of old-age pensioners receiving reduced old-age pensions after reaching retirement age to the number of all pensioners receiving reduced old-age pensions	45
Table 15	Increases in the number of pensioners during 2001–2005 (in %)	45
Table 16	Average age of pensioners	46
Table 17	Number of pensioners in relation to number of insured persons	46
Table 18	Number of pensions paid out	47
Table 19	Pensions paid out abroad	48
Table 20	Number of newly granted pensions and their development	50
Table 21	Average retirement age	51
Table 22	Retirement age in 2004 and 2005	51
Table 23	Year in which entitlement to pension arises for a given age	52
Table 24	Number of terminated pensions	52
Table 25	Average monthly amounts of solo paid out pensions (in CZK)	53
Table 26	Overview of increases to paid out pensions	54
Table 27	Total replacement ratio, 2001–2005)	55
Table 28	Developments in the real value of the average old-age pension	56
Table 29	Average amount of solo old-age pensions paid out according to the period they were granted (pensions paid out in 2005 in CZK)	57
Table 30	Average solo old-age pension according to year granted (in CZK)	59
Table 31	Developments in the proportion of old pensioners to the total number of pensioners	59
Table 32	Reduction limits for the calculation of pension amounts	59
Table 33	Developments in the relation of newly granted old-age pensions to wages in 40 years of being insured and at different wage levels (in %)	60
Table 34	Average amount of newly granted old-age pensions	61
Table 35	Reductions in early old-age pensions permanently reduced granted in 2005 (in %)	62

Table 36	Basic characteristics of differentiation in the amount of solo paid out old-age pensions	64
Table 37	Characteristic of the differences in the amounts of old-age pensions paid out in December according to method of reduction	64
Table 38	Basic characteristics for differentiating newly granted old-age pensions (solo) according to their amount	65
Table 39	Revenues and expenditure for sickness insurance (Chapter 313 – Civil Sector)	66
Table 40	Developments in the number of persons insured under sickness insurance (in thous.)	67
Table 41	Expenditure on social insurance benefits (Chapter 313 – Civil Sector)	68
Table 42	General indicators of sickness insurance	68
Table 43	Developments in the reduction limits, the maximum daily assessment base and daily benefits	70
Table 44	Developments in average daily sickness benefits and the average wage in the national economy	71
Table 45	Fulfilment of the ILO Conventions for old-age pensions during 2004–2006	73
Table 46	Fulfilment of the ILO Conventions for disability pensions in 2004–2006	74
Table 47	Fulfilment of ILO Conventions for survivors' benefits in 2004–2006	74
Table 48	Fulfilment of the ILO Conventions for sickness benefits in 2004–2006	76
Table 49	Fulfilment of ILO Conventions for maternity benefits in 2004–2006	76
Table 50	Operational expenses (CZK millions)	78
Table 51	List of parameters	79
Table 52	Diagram of the macroeconomic model	80
Table 53	Development of basic macroeconomic indicators	81
Table 54	Basic characteristics of future demographic developments	82
Table 55	Life expectancy	94
Table 56	Parameters for calculating wage compensation and sickness insurance benefits	111
Table 57	Financial impact on the state (CZK billions)	112

Table 58 Financial impact on employers (CZK billions)	112
Table 59 Estimate of revenues and expenditure for sickness insurance (incl. wage compensation)	116
Table 60 Examples of variants of percentage rates of sickness benefits and the amount of sickness for an equalised balance	117

LIST OF GRAPHS

Graph 1 Old-age index and economic burden index	29
Graph 2 Developments in total fertility rate	30
Graph 3 Developments in life expectancy at 65	31
Graph 4 Participation rate – in total	32
Graph 5 Participation of older persons	32
Graph 6 Developments in the assessment base of employees and the self-employed	35
Graph 7 Developments in the ratio of payments and prescribed premiums (including penalties, fines and premium surcharges)	38
Graph 8 Developments in arrears (CZK billions)	39
Graph 9 Structure of receivables for contributors as % of the total receivables (as at 31 December)	40
Graph 10 Developments in the number of newly granted old-age pensions	50
Graph 11 Total replacement ratio, 2001–2005)	55
Graph 12 Developments in the real value of the average old-age pensions as percentage of its value in 1989	56
Graph 13 Difference between the average amount of old-age pensions paid out granted in different periods and the average amount of all old-age pensions paid out (in %)	58
Graph 14 Developments in the general indicators of sickness insurance	69
Graph 15 Developments in the average daily sickness benefit, average daily wage and its share	70
Graph 16 Amount of sickness benefits for 30 days in 2006 and its ratio to the gross and net wage for various wage amounts	72
Graph 17 Development of the criteria for fulfilling the conventions for the minimum level of pensions	75
Graph 18 Developments in the criteria for fulfilling the conventions on the minimum standards of sickness benefits	77
Graph 19 Participation rate by age groups – men	82

Graph 20 Participation rate by age groups – women	83
Graph 21 Changes in the participation rate due to increases in the retirement age – men	83
Graph 22 Changes in the participation rate to increases in the retirement age – women	84
Graph 23 Total participation rate in the 15+ age group	84
Graph 24 Developments in the retirement age	86
Graph 25 Number of contributors (basic variant)	86
Graph 26 Number of pensioners (basic variant)	86
Graph 27 Dependency rate (basic variant)	86
Graph 28 Developments in revenues, expenditure and balances of the pension system (% of GDP) (basic variant)	87
Graph 29 Impact of a higher than minimum valorization carried out in 2006 on pension system expenditure (in %)	88
Graph 30 Cumulative balance (in % of GDP) (basic variant)	88
Graph 31 Total replacement ratio (%)(basic variant)	89
Graph 32 Process of increasing the retirement age to 65, 67 and 69 years	90
Graph 33 Expenditure on pensions (% of GDP) (variant: increasing the retirement age)	91
Graph 34 Expenditure on old-age pensions (% of GDP) (variant: increasing the retirement age)	92
Graph 35 Balance of the pension system (in % of GDP) (variant: increasing the retirement age)	92
Graph 36 Cumulative balance (in % of GDP) (variant: increasing the retirement age)	93
Graph 37 Total replacement ratio (in %) (variant: increasing the retirement age)	93
Graph 38 Average pension drawing time – men	94
Graph 39 Average pension drawing time – women	94
Graph 40 Expenditure on pensions (% of GDP) (variant: change in valorization)	95
Graph 41 Total replacement ratio (in %) (variant: change in valorization)	95
Graph 42 Balance of the pension system (% of GDP) (variant: change in valorization)	96
Graph 43 Cumulative balance (% of GDP) (variant: change in valorization)	96

Graph 44 Disability rate in years – men (in %)	97
Graph 45 Disability rate for generations – men (in %)	97
Graph 46 Full disability rate for the 1980 generation – men (in %)	98
Graph 47 Number of full disability pensioners (thous.)	98
Graph 48 Expenditure for disability pensions (in % GDP)	98
Graph 49 Implicit tax for 1995 generation – women (with two children)	99
Graph 50 Implicit tax for the 1980 generation – women (with two children)	99
Graph 51 System expenditure (% of GDP) (variant: canceling early retirement)	100
Graph 52 Total replacement ratio (%) (variant: canceling early retirement)	100
Graph 53 Total number of pensioners (variant: canceling early retirement)	101
Graph 54 System expenditure (% of GDP) (variant: deferring retirement)	102
Graph 55 Total replacement ratio (in %) (variant: deferring retirement)	102
Graph 56 Number of pensioners (variant: deferring retirement)	102
Graph 57 Total number of inhabitants (variant: partial dying off of the population)	105
Graph 58 Revenues, expenditure and balance of the system (variant: partial dying off of the population)	105
Graph 59 Dependency rate (variant: partial dying off of the population)	106
Graph 60 Total and implicit debt and cumulated deficits (variant: partial dying off of the population)	106
Graph 61 Comparison of the amount of sickness benefit with the amount of compensation and sickness benefits for the first 30 calendar days of sick leave in 2006	114
Graph 62 Ratio of the amount of benefits for the first 30 calendar days of sick leave to net wages for different wage levels	115
Graph 63 Comparison of the amount of maternity benefits for 28 weeks of sick leave	115
Graph 64 Impact of sickness on sickness insurance expenditure	117

INTRODUCTION

With this report the Department of Social Insurance of the Ministry of Labour and Social Affairs strives to continue in its efforts of regularly evaluating the actuarial system for social insurance. This third actuarial report summarises data for the last five years and analyses the changes that have occurred in the last 2 years while taking into account the immediately preceding 3 years. Thus the report follows up on the previous report, which summarised figures from 1999.

The report is divided into three parts. Part A summarises basic information on the system of social insurance including the legislative changes since 2004. Part B contains an evaluation of the basic indicators of social insurance for the last 5 years. Part C focuses on long-term projections whose horizons have, in contrast to previous reports, been extended by 35 years to 2100. The Annex contains several examples of calculations of the various types of social insurance benefits.

The report was drawn up by the Actuarial Unit of the Social Insurance Department of the Ministry of Labour and Social Affairs in cooperation with the Pension Insurance and Sickness Insurance Unit of this department based on statistics provided by the Czech Social Security Administration (*Česká správa sociálního zabezpečení*) and with the analyses and forecasts of experts in the demographics and economics. The aim is to provide objective information not only on current status of the system, but also on possible future developments and on recommendations ensuing there from.

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would be grateful for any comments or suggestions regarding this report.

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Part A

GENERAL INFORMATION ABOUT SOCIAL INSURANCE

A.1. BRIEF CHARACTERISTICS

The social insurance system includes basic compulsory pension insurance and sickness insurance. Apart from social security premiums, contributions for the state employment policy are also collected within the scope of the system.

A.1.1. PENSION INSURANCE¹

The **key substantive legal provision** governing entitlement under compulsory pension insurance in the event of old-age, disability or death of a provider is the **Act No. 155/1995 Coll., on pension insurance** (hereinafter the “Pension Insurance Act”), which the Chamber of Deputies passed on 30 June 1995. The Pension Insurance Act came into effect on 1 January 1996. It has been amended several times.

Participation in the basic pension insurance is compulsory provided that certain set conditions are met. The Pension Insurance Act, which contains the relevant substantive legal provisions, allows for voluntary participation to a given extent within the framework of the basic compulsory pension insurance.

¹ The present Czech system of pension insurance comprises two parts: a basic pension insurance system (used to provide old-age pensions, full disability pensions, partial disability pensions, widow pensions, widower pensions, and orphan pensions) and a supplementary system, which includes supplementary pension insurance with a state contribution (Act No 42/1994, on Supplementary Pension Insurance with a State Contribution, used to provide permanent old age and disability pensions and superannuation, temporary survivor pensions, lump-sum settlements, and severance pay) and other forms of individual security by means of products offered by commercial insurance companies. Information on supplementary pension insurance with a state contribution can be found in the Annual Report published by the Finance Ministry's Office of State Supervision in Insurance and Supplementary Pension Schemes and in the publication entitled 'Supplementary Pension Insurance with a State Contribution', published every year by the APF CR.

The various groups of participants (persons in an employment relationship, persons in a service relationship, cooperative members, the self-employed and the other groups of participants) are all subject to **the same legislation**.

Fulfilment of the conditions stipulated under the law gives rise to a **legal right to a pension**.

All **decisions** on claims for benefits under pension insurance and the amount or payment thereof are subject to **judicial review**.

The basic pension insurance is **economically guaranteed by the state** as pensioners may not be left without a source of income on which they rely for subsistence.

The principle of merit is reflected only to a limited extent due to the simultaneous application of the principle of social solidarity (the existence of reduction limits whereby a set method is applied to restrict the inclusion of higher income, which causes a decrease in the relative level of the pension with rising incomes creditable for the purposes of pension insurance).

The **dynamic nature of the basic pension insurance** is ensured by an annual update of the income levels that are used for the calculation of the percentage-based assessment of pensions and increases to the pensions paid out.

The following pensions are provided under the basic pension insurance:

- **old-age pension** (including old-age pensions granted prior to reaching retirement age – hereinafter “early old-age pension”),
- **full disability pension,**
- **partial disability pension,**
- **widow and widower pensions,**
- **orphan pension.**

Essentially, only benefits derived from the insurance period and earnings achieved are granted under the pension insurance. The only exception is if the **full disability pension** is granted provided certain conditions are met to persons who hold the status of ‘**disabled from youth**’.

An **increase to pensions for the incapacitated** is also paid out together with the pensions granted from pension insurance, even though it is paid out as a ‘pension security benefit’² (as opposed to a pension insurance benefit).³

A pension is composed of two elements (a dual component structure):

- a basic amount (flat rate) which is the same for all types of pensions regardless of the insurance period and earnings achieved,

² Article 7 and 70 of Act No. 100/1988 Coll., on social security, as amended.

- a percentage-based assessment based on the insured period and earnings achieved.

The structure of the pension calculation contains a whole series of elements; those related to earnings that are decisive for the amount of the pension are adjusted annually according to general wage developments.

The basic rules for increasing the pensions paid out are legally provided for under Article 67 of the Pension Insurance Act and, effective from 1 July 2002,⁴ are as follows:

- pensions paid out are regularly increased on an annual basis in January; this does not apply to instances of very low inflation (where the increase would be less than 2 %) and in cases of high inflation (at least 10 %),
- increases in pensions are set so that for the average old-age pension it corresponds to at least 100 % of price increases as well as to at least one third of the growth of real wages,
- the exact amount is set by the Government by decree whereby the increase could be greater than the minimum provided for under law,
- the rise in the aggregate consumer price index for households is, during regular increases from January, determined in the period of twelve months up to the July preceding the pension increase; the calendar year preceding by two years the year in which the pension was increased is decisive for determining the growth of real wages,
- pensions are increased exceptionally if the price increases for a given pe-

³ The Act No. 108/2006 Coll., on social services has been adopted and will enter into force on 1 January 2007. This Act introduces a new benefit - the contribution for care – which is granted to persons dependent on the assistance of other natural persons in order to ensure the required care and costs thereof are paid for from the state budget. In relation to this the existing ‘increases in pensions for incapacity’ were cancelled by Act No. 109/2006 Coll., amending certain acts in relation to the adoption of the Social Services Act. The last such benefit will be paid out together with the pension due in December 2006.

⁴ The following rules applied up to 30 June 2002:

- all paid out pensions are increased,
- the Government is authorised to increase pensions on the basis of decrees if the aggregate consumer price index grew by at least 5 % from the calendar month which directly preceded the calendar month in which the last increase in pensions occurred,
- the increase must correspond to at least 70 % of the aggregate consumer price index,
- at least once in the last two years the growth of real wages by at least one third was taken into account in setting the amounts of increases of the pensions.

riod reach at least 10 %; the Government shall decide on such increases within 50 days from the fulfilment of this condition,

- the factors required for setting the amount of pension increases are determined according to figures from the Czech Statistical Office (the aggregate consumer price index, average nominal wage) and the Czech Social Security Administration (the amount of the average old-age pension).

A.1.2. SICKNESS INSURANCE ⁵

The key act governing the persons insured and the entitlement of insured persons is the Act No. 54/1956 Coll., on sickness insurance, which has been frequently amended over almost the fifty years that it has been in force.

Sickness insurance is **compulsory for employees and members of the armed forces and corps**; it has been **voluntary** for the **self-employed** since 1994.

The sickness insurance system is in essence, with only a few exceptions, **uniform** for all gainfully employed persons.⁶

Sickness insurance is both financially and legally **guaranteed by the state**.

The **principle of merit** is reflected to a limited extent in sickness insurance given the simultaneous application of the **principle of social solidarity** for the same reasons as under basic pension insurance.

The dynamic nature of the system is given by the annual updating of the

⁵ Apart from the state compulsory sickness insurance, there is a gradual development of voluntary insurance with insurance companies. Greater expansion is hindered on the one side by the high tax and social security contributions burden of economically active persons, which does not leave much room for other regular voluntary payments, but also foremost by the continuing low level of knowledge of the options of commercial insurance as well as inadequate awareness of the risks associated with extended sick-leave, especially among groups of higher income employees.

⁶ Members of the armed forces are entitled to sickness benefits only as of the second month of sickness, as they receive their wages in the first month of sick leave. Certain other persons, e.g., judges and deputies, are entitled to wages for the duration of sick leave. The sickness welfare system of members of the armed forces includes an allowance for the burial of a soldier.

Some insured persons are only entitled to certain benefits under sickness insurance. For example, students and secondary school pupils are only entitled to maternity benefits and some employees are not entitled to assistance for caring for a member of the family and to pregnancy and maternity compensation benefits (e.g. employees employed under an agreement to perform work and volunteer healthcare service workers), nor are the self-employed entitled to such benefits under sickness insurance. Members of the armed forces and home workers are not entitled to benefits when caring for a family member.

reduction limits for earnings which are used for the calculation of benefits in accordance with wage developments.⁷

Following the exclusion of health care in the 1950s, of spa centre treatment in 1993 and of child allowances, birth and funeral allowances in 1995, which were transferred into the health insurance and state social welfare systems, the following benefits are provided under the system of sickness insurance:

- **sickness benefit,**
- **family member care benefit,**
- **maternity benefit,**
- **pregnancy and maternity compensation benefit.**

Sickness benefits are granted for calendar days as of the first day of illness and are calculated based on the average gross wages for the twelve calendar months preceding the claim.

A.1.3. FINANCING

The social insurance system is financed in a continuous manner (PAYGO). Therefore, expenditure on benefits for a given period are paid for from the revenues from the premiums collected in this period.

The legal provisions governing financing relations is provided for in **Act No. 589/1992 Coll.**, on social security premiums and state employment policy contributions, as amended, which came into effect on 1 January 1993. It provides in particular for:

- the **group of contributors** (including contributions to the state employment policy),
- the **method of determining the amount of the premiums**, payments of the premiums and the duties of contributors.

Social security premiums (for sickness insurance and pension insurance) and the contribution for the state employment policy are collected pursuant to this Act.

Premiums and contributions to the state employment policy form revenues of the state budget. In addition, penalties, social security premium surcharges and fines imposed according to Act No. 589/1992 Coll., as amended, also constitute revenues of the state budget. The introduction of the collection of premiums was aimed at increasing the link between the premiums paid and the level of bene-

⁷ In connection with public budget reforms it was decided to suspend the validity of the relevant provisions of the Sickness Insurance Act and not to increase the reduction limits in 2004 and 2005.

fits. Effective from 1 January 1996, a separate account for pension insurance was created as a part of the financial assets of the state. The surplus from the revenues from pension insurance premiums, including penalties and fines relating to pension insurance and the payment out of pension insurance benefits as well as expenditure related to the collection of pension insurance premiums is transferred to this account. The funds on the account may only be used for expenditure for pension insurance benefits and for transfers back into the state budget for the payment of deficits between revenues and expenditures. Such use is only possible with the consent of the Chamber of Deputies of the Parliament. The funds may not be invested.

Premiums are collected by the District Social Security Administration authorities.

Premiums are paid by employees, employers and the self-employed. Their amount is set by percentage rate (Table 1) from the assessment base determined for the period in question. Premiums are calculated based on creditable income prior to taxation. With respect to the self-employed, creditable income is decreased by the expenses incurred for achieving, determining and maintaining such income; the basis for payment of premiums as of 2006 is 50 % of the difference between income and expenses (in 2004 it amounted to 40 % and in 2005 it was 45 %).

Table 1 Contribution rates from 2004 (% of the assessment base)

	Pension insurance	Sickness insurance	State employment policy	Total
Organizations and small organizations	21.5	3.3	1.2	26
Employees	6.5	1.1	0.4	8
Self-employed	28	4.4	1.6	29.6
		voluntary		or 34
Persons voluntarily insured under pension insurance	28	-	-	28

Source: MLSA

A.1.4. SOCIAL SECURITY ORGANIZATION AND IMPLEMENTATION

The **Act No. 582/1991 Coll.**, on the organization and implementation of social security, as amended, came into effect on 1 January 1992. Pursuant to the Act:

- Social security falls under the competence of the social security authorities and organizations. Municipalities also carry out activities relating to social security.

- The social security authorities are:
 - the Ministry of Labour and Social Affairs,
 - Czech Social Security Administration [*Česká správa sociálního zabezpečení*] (hereinafter “CSSA”),
 - The District Social Security Administration,
 - the Ministry of the Interior,
 - the Ministry of Justice,
 - the Ministry of Defence.

The administrator of insurance for the “civil sphere” is the CSSA, which was established in 1990 by the merger of the administrators of pension insurance and sickness insurance. It is an independent organizational body of the state which reports to the MLSA. The main scope of activities of the CSSA as provided for under the relevant legal provisions is the carrying out of pension and sickness insurance, performing doctor appraisal services, the collection of premiums and fulfilling obligations ensuing from international conventions and EC law. Proposed changes to existing legislation, especially in the last period, had a significant impact on the activities of the CSSA. These changes are brought forth by deputies of the Chamber of Deputies of Parliament within the legislative process of deliberating government bills, which in many cases, are unrelated to the government bill in question as well as proposals for the adoption of separate acts.⁸ The CSSA must implement these adopted measures that in some cases do not even relate to the activities for which it was created, without any increases to its funding or the number of personnel. Despite problems with financing its administrative and personnel expenses, the CSSA continuously strives to generally increase its technological equipment with the aim of creating a modern institution with a high level of quality of service for insured persons. As of 2005 employers regularly submit on an annual basis to the insurance administrator the pension insurance statements of their employees. As of 1 July 2005, a register of insured persons was created whose information is regularly updated and amended. Thus the basis was formed for regularly informing insured persons of information regarding their participation in pension (and sickness) insurance. During 2006, written notification of such information began to be provided on request by an insured person (the ‘individual accounts of insured persons’).

⁸ For example, extending the range of miners who are affected by the provisions of Act No. 188/2001 Coll.; the adjustment of the amount or the release of payments of widow pensions, which were under previous legal provisions decreased or whose payment was not made as a result of “concurrent maximum amounts”; a whole number of “compensatory legislation”.

A.2. LEGISLATIVE CHANGES SINCE THE BEGINNING OF 2004

A.2.1. PENSION INSURANCE

(A) Legislative changes that have come into effect

- **Government Decree No. 337/2003 Coll.** – effective from 1 January 2004. The percentage-based assessment of pensions was increased by 2.5 %.
- **Government Decree No. 338/2003 Coll.** – effective from January 2004. The decree stipulated the general assessment base for 2002 (CZK 15,711), increased the reduction limits to CZK 7,500 and CZK 19,200. In addition, the decree set the amount of the conversion coefficient for the adjustment of the general assessment base for 2002 (1.0717).
- **Act No. 424/2003 Coll.** – effective from 1 January 2004. The Act expanded the scope of insured persons (employees in an employment relationship concluded according to foreign laws, members of the Council for Radio and Television Broadcasting [*Rada pro rozhlasové a televizní vysílání*], the financial arbitrator and the deputy financial arbitrator).
- **Act No. 425/2003 Coll.** – effective from 1 January 2004. The Act brought changes not only in the field of pension insurance, but also with respect to social security premiums and contributions to the state employment policy. It involved the most significant changes since 1995 when the existing Pension Insurance Act was adopted (which came into effect on 1 January 1996).

Changes in the pension insurance included, in particular:

- a) **increasing the age limit** for entitlement to old-age pension (hereinafter “retirement age”) at the same rate also after 2007 with the aim of gradually achieving a uniform limit of 63 years for men and childless women. The retirement age for other women will continue to be differentiated according to the number of children brought up and will range from 59–62 years,
- b) **restricting the possibility of early old-age retirement** by cancelling the ‘temporarily reduced early old-age pension’ whereby this option was temporarily maintained (up to 31 December 2006) when given conditions for the beneficiaries of partial disability pensions or the former beneficiaries of full disability pensions are met. The current legislation remains unchanged with respect to possibility of granting the later type of early retirement pension, i.e. the permanently reduced,

- c) **reducing the valuation of the period of studies** for the purposes for pension insurance in that the duration of studies in secondary school and university prior to 1 January 1996 which were acquired after the age of 18 will be valued at a maximum of 6 years whereas it will be considered to be a non-contributory period and thus for pension purposes will only be valued at 80 % (this brought it into line with the valuation of studies acquired after 31 December 1995). The period of studies preceding 1 January 1996 that were acquired before reaching the age of 18 shall continue to be valued as an insured period (i.e. “fully valued”),
- d) **cancelling the condition granting entitlement to the pay out of old-age pensions together with income from gainful activity** in the period of two years after the beginning of entitlement to such a pension only when the prescribed limit has not been reached (two times the amount of the life minimum for individuals) both for employees as well as for the self-employed. At the same time, in order for an entitlement to the payment of old-age retirement next to income from gainful activity the employment relationship must be concluded for **no longer than one year**,
- e) **classification of self-employment as either main or secondary.** Self-employed persons that carry out independent gainful activity as a main activity always (regardless of the amount of income) participate in pension insurance (and pay premiums on pension insurance and contributions to the state employment policy at a minimum from the minimum assessment base). The self-employed persons whose activity has the character of secondary activities given their income from employment or in light of the existence of certain conditions (receipt of old-age or full disability pensions, studies, etc.) participate in pension insurance based on the amount of income achieved,
- f) **extension of the scope of the self-employed to those who act as mandatories** on the basis of an agency agreement concluded pursuant to the Commercial Code, if such activity is carried out outside of a relationship that gives rise to participation in sickness insurance and the agency agreement was not concluded within the realm of another independent gainful activity.

The changes in the premiums for social security and the contribution to the state employment policy included in particular:

- a) **the “transfer” of a portion of the contributions collected for the state employment policy into the pension insurance system** by increasing

the rate of premiums for pension insurance by 2 percentage points (from 26 % to 28 % of the assessment base) and at the same time lowering the rate for premiums on the state employment policy by 2 percentage points (from 3.6 % to 1.6 % of the assessment base),

- b) **gradual increase of the minimum assessment base for determining premiums for the self-employed** for the years 2004 to 2006 from 35 % to 50 % of the difference between income obtained and the expenses incurred. At the same time, the minimum assessment base for the self-employed carrying out a main activity increased in 2004 to 2006 to a nominal amount of 20 % of the average wage in the national economy (in a monthly statement) in 2004, to the level of 22.5 % in 2005 and 25 % in 2006.
- **Act No. 359/2004 Coll.** – effective on its promulgation, i.e. 15 June 2004. The change **involved in extending the scope of insured persons** (to include members of the European Parliament elected on the territory of the Czech Republic).
 - **Government Decree No. 521/2004 Coll.** – effective from 1 January 2005. The decree **provided for the general assessment base for 2003** (CZK 16,769), **increased the reduction limits** to CZK 8,400 and CZK 20,500 respectively and **set the amount of the conversion coefficient** for adjustments to the general assessment base **for 2003** (1.0665).
 - **Government Decree No. 565/2004 Coll.** – effective from 1 January 2005. As of January 2005 **raised the basic amount for pensions to CZK 1,400** and the percentage-based assessment for paid out pensions by 5.4 %.
 - **Government Decree No. 414/2005 Coll.** – effective from 1 January 2006. The decree **set the general assessment base for 2004** (CZK 17,882), **raised the reduction limits** to CZK 9,100 and CZK 21,800 respectively, and **set the conversion coefficient** for adjusting the general assessment base **for 2004** (1.0532).
 - **Government Decree No. 415/2005 Coll.** – effective from 1 January 2006. As of January 2006, the **basic amount for the calculation of pensions was raised** to CZK 1,470 and the **percentage-based assessment of paid out pensions** accorded prior to 1 January 1996 **was increased** by 6 % of the percentage-based assessment and those for pensions granted from 1 January 1996 to 31 December 2004 by 4 %.
 - **Act No. 24/2006 Coll.** – effective from 1 February 2006. The amendment to the Pension Insurance Act related to **cancelling reduced partial disability pensions or terminating their payment** when the income limits from

gainful activity were surpassed. It also amended the legal provisions governing cases where according to a court decision, an illegal termination of a legal relation forming the basis of participation in pension insurance occurred.

- **Act No. 264/2006 Coll.** – the amendments relating to the pension insurance came into effect on 1 July 2006. The amendment involved raising the percentage-based assessment for pensions by CZK 2,000 from the day its beneficiary reaches the age of 100.
- **Act No. 267/2006 Coll.** – the amendments relating to pension insurance came into effect on 1 July 2006. The amendment involved adjusting the amounts of widow pensions or permitting their payment if the reduction of their amounts or the non-granting of their payment occurred under legislation valid up to 1 January 1996 as a result of the existence of “concurrent maximums”.

(B) Preparation of conceptual changes

In December 2003, the MLSA submitted to the Government the document “A Proposal of the Main Principles for the Continuation of the Reform of the Pension System” whose deliberation was suspended in January 2004. On 4 February 2004, the Government adopted Resolution No. 107 whereby it approved the general and brief “Main Objectives of the Pension Reform”.

In March 2004, the chairmen of the political parties represented in the Chamber of Deputies of Parliament reached an agreement on the process of preparing the pension reform and the creation of a team of experts for the preparation of the pension reform (hereinafter the “Team of Experts”) whose members were appointed by the political parties represented in the Chamber of Deputies of Parliament. On 23 June 2004, the Government adopted Resolution No. 656 on the organizational aspects of the preparation of documentation for decisions on pension reform, the creation of the position of coordinator for the preparation of documentation for decisions on pension reforms (hereinafter “Coordinator”) and took into account the creation of the Team of Experts and the Coordinator’s Executive Team, (hereinafter “Executive Team”), which began functioning on 1 October 2004. The activities of the Executive Team terminated in June 2005 with the submission of the “Final Report” containing a comparative analysis of the various proposed variants of pension reform submitted by the political parties (further information may be obtained at: www.reformaduchodu.cz).

In July 2005, the activities of the Team of Experts was reinstigated under the leadership of the Minister of Labour and Social Affairs. A proposal for an “Agreement Between the Political Parties Represented in the Chamber of Deputies of

Parliament on the Further Continuation of Pension Reform” was prepared containing common principles of the further measures to be taken in pension reform to be carried out before elections to the Chamber of Deputies (a draft of the Agreement is attached hereto as an appendix).

These propositions contained adjustments to the basic pension insurance (with the continuing increasing of the retirement age), adjustments to life insurance and supplementary pension insurance with a state contribution (introducing a total limit of deductibles for income tax for employers and employees (including the self-employed) for “pension products” of life insurance and supplementary pension insurance with a state contribution, as well as introducing the possibility of granting a time-limited old-age pension) and the creation of “reserves for the pension reform”. The negotiations, however, did not result in a political agreement on the specific continuation of pension reform and thus this may only be expected to occur in the next election period.

A.2.2. SICKNESS INSURANCE

(A) Legislative changes that have come into effect

- **Act No. 421/2003 Coll.** – effective from 1 January 2004. The changes involved:
 - a) **extending the decisive period used for determining the daily assessment base** for setting sickness insurance benefits from a calendar year quarter to 12 calendar months,
 - b) **decreasing the daily assessment base** for the calculation of sickness benefits and financial support for care of family members for the first 14 calendar days of sick leave (quarantine) or the need for treatment from the current 100 % **to 90 % for amounts up to CZK 480** (the first reduction limit),
 - c) **decreasing the sickness benefit for the first three calendar days of sick leave from 50 % to 25 %**,
 - d) **extending the time period during which the reduction limits of the daily assessment base will not be increased** also to 2004 and 2005; this measure also applied to the system of sickness care in the armed forces.
- **Act No. 424/2003 Coll.** – effective from 1 January 2004. The act extended the scope of insured persons (employees in an employment relationship concluded under foreign laws, members of the Council for Radio and Television Broadcasting, the financial arbitrator and the deputy financial arbitrator).

- **Act No. 359/2004 Coll.** – effective from 1 September 2004. It extended the scope of employees insured under sickness insurance to include Members of the European Parliament elected on the territory of the Czech Republic.
- **Act No. 436/2004 Coll.** – effective from 1 October 2004. In connection with the adoption of the Employment Act, persons with a changed capacity for work that are preparing for employment were excluded from sickness insurance.
- **Act No. 168/2005 Coll.** – effective from 1 June 2005. It extended the scope of employees insured under sickness insurance to include foster parents, who are paid foster care remuneration in certain cases under a special legal regulation.
- **Act No. 361/2005 Coll.** – effective from 1 October 2005. Extended the scope of employees insured under sickness insurance to include members of the Council for Radio and Television Broadcasting.
- **Government Decree No. 417/2005 Coll.** – effective from 1 January 2006. This Decree adjusted the amounts for determining the daily assessment base as follows:
 - the amount of CZK 480 was increased to CZK 510, and
 - the amount of CZK 690 was increased to CZK 730.

(B) Preparation of conceptual changes

The MLSA prepared in accordance with the Government’s policy statement of August 2002 a proposal for the draft of general principles of the Sickness Insurance Act and subsequently a draft of the Sickness Insurance Act.

The basic principles of the new system of sickness insurance include:

- securing economically active citizens with short term monetary benefits in certain short-term situations,
- uniformity of the system whereby participation will be obligatory for employees and voluntary for the self-employed,
- limiting solidarity amongst persons with higher and lower incomes (reinforcement of insurance elements),
- limiting solidarity between employers by partially (gradually) privatizing the system,
- strengthening the protective elements of the system to prevent its abuse,
- revenues from premiums and expenditure on benefits will essentially be balanced,

- employers will also contribute to finally securing employees during sick leave,
- the system will respect international obligations.

The new Sickness Insurance Act (Act No. 187/2006 Coll.) together with the act amending certain acts in connection with the adoption of the Sickness Insurance Act was passed on 25 April 2006. Its effective date is set for 1 January 2007.

The new Sickness Insurance Act and the relating act provide in particular for:

- involving the employers in the development of sick leave of employees whereby the employer will pay wage compensation for the first 14 days of sick leave,
- decreasing the rate for sickness insurance premiums for employers from 3.3 % to 1.4 %,
- ensuring greater proportionality of the amount of sickness insurance benefits paid versus premiums paid by increasing the number of reduction limits for the calculation of the daily assessment base from two to three,
- transferring the carrying out of sickness insurance from large organizations to the sickness insurance authorities,
- strengthening the protective elements against abuses of the system,
- decreasing the penalty rate by half (from 0.1% to 0.05 %).

The CSSA's preparations for implementing the Act necessitated an increase in personnel and not an insignificant funds (the budget of the CSSA will be increased by approx. CZK 400 million).

A.2.3. PREMIUMS

The Act No. 264/2006 Coll. (the accompanying act to the new Labour Code) that will come into effect on 1 January 2007 will significantly change the criteria for crediting the income of employees into the assessment base for the payment of premiums on security and health insurance. The following earnings will be credited into the assessment base:

- earnings that the employer attributed to the employee, and
- are subject to income tax for natural persons, and
- are not included in the list of non-creditable income (e.g., severance pay, compensation for damages, social assistance in exceptionally difficult cases).

PART B EVALUATION OF THE BASIC INDICATORS OF SOCIAL INSURANCE DEVELOPMENTS

B.1. PARAMETRS INFLUENCING THE DEVELOPMENT OF SOCIAL INSURANCE

The development of social insurance is influenced especially by the following parameters:

- Economic (developments in the gross domestic product, prices and wages)
- Demographic (developments in the age structure of the population due to fertility, life expectancy and migration)
- Employment (developments in participation rate and unemployment)

B.1.1. ECONOMIC DEVELOPMENTS

Between 2003 and 2005, there was acceleration in economic development whereby in 2005 there was the greatest amount of real growth in GDP in the history of the independent Czech Republic amounting to 6.1 %. The Ministry of Finance is expecting a slight increase in the rate of growth for 2006 to a level of 6.2 %.⁹

Table 2 GDP Development

Year	GDP [bill. CZK]	Annual growth rate in fixed prices [%]	Rate per inhabitant (calculated using the purchase power parity)	
			[USD]	EU 12 = 100
2001	2352.2	2.5	15,800	61
2002	2464.4	1.9	16,900	63
2003	2577.1	3.6	17,400	63
2004	2781.1	4.2	18,700	66
2005	2978.2	6.1	20,500	69

Source: Ministry of Finance⁹

⁹ Macro-economical forecasts for the Czech Republic - July 2006.

For the first time since 1990, in 2003 there was an inter-year decrease in the price level. The average inflation rate thus reached 0.1 % in 2003 and as such was the lowest since 1987. In 2004 and 2005, inflation reached the level of 2.8 % and 1.9 %, respectively. It is expected that there will be an increase in the price levels in 2006 of 2.6 %.⁹

The nominal value of the average gross wages in the national economy grew year-on-year in 2003 to 2005 by 6.7 %, 6.6 % and 6.0 %. Given the above-mentioned growth in prices however, the real value of the average gross wage in the national economy grew by 6.6 % in 2003, by 3.8 % in 2004 and by 4.1 % in 2005. The growth in the real value of the average wage in the national economy was lower in 2004 and 2005 than the growth of the real GDP for these years.

Table 3 Developments in the average nominal wage in the national economy

Year	Wage [CZK/month]		Wage development Previous year = 100 %	
	Gross	Net	Gross	Net
2001	14,640	11,324	108.5	108.4
2002	15,711	12,082	107.3	106.7
2003	16,769	12,807	106.7	106.0
2004	17,882	13,601	106.6	106.2
2005	18,954	14,339	106.0	105.4

Source: CSO, MLSA

Note: Average net wage is the average gross wage decreased by the amount of income tax applicable to this wage and the respective health and social insurance premiums.

B.1.2. DEMOGRAPHIC DEVELOPMENTS

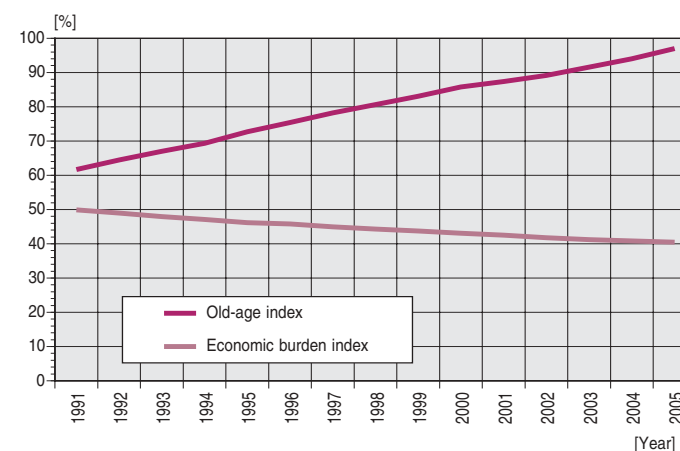
The relative proportion of the oldest generation gradually grew throughout all of the 1990s and its development contrasted with a diminishing share of the child element of the population. In 2000, the share of the population aged 65 and more was the greatest in history. After 2000, this share stagnated whereby in 2004 a small increase of 0.1 percent occurred.

Table 4 Age structure of the population

Year	0–14 years		Age group 15–64 years		65 and more years		Total [thous. pers.]
	[thous. pers.]	[% of pop.]	[thous. pers.]	[% of pop.]	[thous. pers.]	[% of pop.]	
2001	1,622	15.9	7,170	70.2	1,415	13.9	10,207
2002	1,590	15.6	7,196	70.5	1,418	13.9	10,204
2003	1,554	15.2	7,234	70.8	1,423	13.9	10,211
2004	1,527	14.9	7,259	71.0	1,435	14.0	10,221
2005	1,501	14.7	7,293	71.1	1,456	14.2	10,251

Source: CSO

Graph 1 Old-age index and economic burden index¹⁰



Source: CSO

The demographic development after 1990 was relatively positive even though the share of persons aged 65 or more increased and the population as a whole aged. However, the economic burden index¹⁰ continued to fall in this period from a value of 50 in 1991 up to 40.8 in 2004. The total demographic structure is affected especially by a low birth rate and increases in life expectancy. While the mean life span at birth for the period 2001–2004 for men grew by 0.5 year (1 year for women), upon reaching the age of 60 it was 0.3 year for men and 0.4 year for women and upon reaching the age of 65 it was 0.2 year for men and 0.4 year for women.

¹⁰ Old-age index = proportion of persons aged 65 and older for 100 persons aged 0–14. Economic burden index = proportion of persons aged 0–14 and 65 or more per 100 persons aged 15–64.

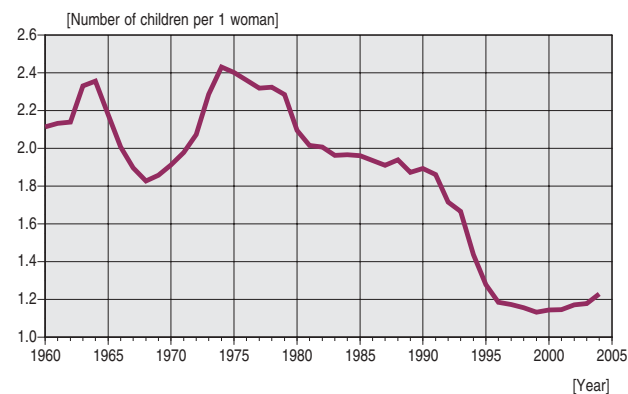
Table 5 Total fertility rate, life expectancy

Year	Total fertility rate	Life expectancy [number of years]					
		At birth		At 60 years		At 65 years	
		Men	Women	Men	Women	Men	Women
2001	1.15	72.1	78.4	17.3	21.2	14.0	17.1
2002	1.17	72.1	78.5	17.3	21.3	13.9	17.2
2003	1.18	72.0	78.5	17.2	21.3	13.8	17.1
2004	1.23	72.6	79.4	17.6	21.6	14.2	17.5
2005 ^{*)}	1.28	72.9	79.1	17.8	21.7	14.4	17.6

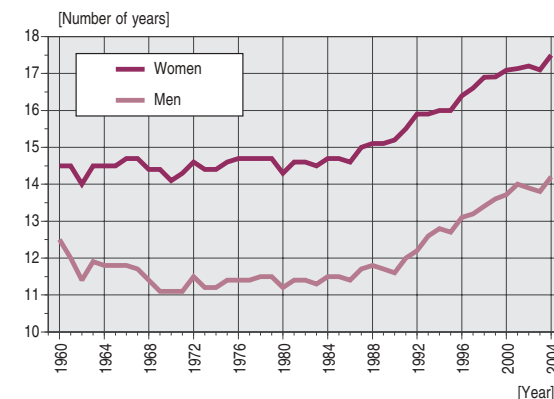
Source: CSO

* Estimated

At the turn of the 20th and 21st century, the population in the Czech Republic is the oldest that it has ever been in the history of the Czech Republic. Although the same may be said for the populations of other European countries, the prospect of further ageing of the population in Czech Republic is greater than in the majority of them.

Graph 2 Developments in total fertility rate

Source: MLSA

Graph 3 Developments in life expectancy at 65

Source: MLSA

The effect of migration abroad on the structure and size of the Czech Republic's population is marginal.

B.1.3. EMPLOYMENT DEVELOPMENTS

An important aspect of employment in the Czech Republic is the fact that the population is ageing where as this ageing process is, for the time being, reflected in the growth of the number of persons of an economic active age. However, this is significantly affected by a decreasing participation rate, which has been gradually falling since 1999 to almost 69 % for men and approximately 51 % for women. A positive shift has, however, occurred with the older age groups where the participation rate has begun to increase since 2000.

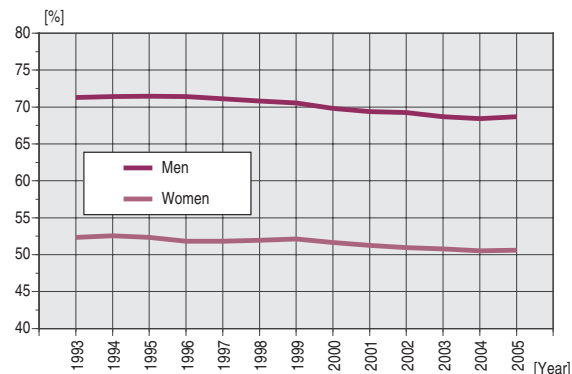
Table 6 Participation rate

Year	55–59 years	60–64 years	55–64 years	Total	Total Men	Total Women
2001	54.3	18.2	39.0	60.0	69.4	51.3
2002	57.9	20.9	42.4	59.8	69.4	51.0
2003	60.4	21.9	44.2	59.4	68.7	50.8
2004	62.8	21.4	45.1	59.2	68.4	50.5
2005	65.4	23.0	47.0	59.4	68.7	50.6

Source: CSO

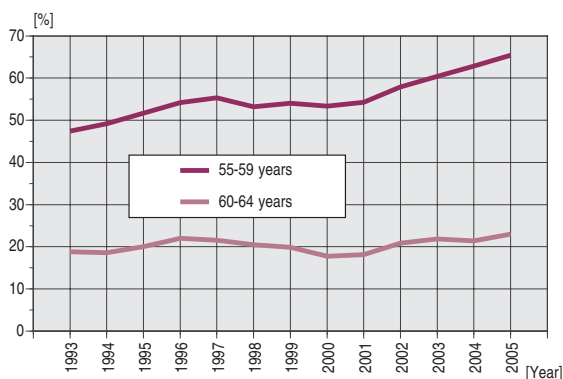
According to the Labour Force Survey, the level of unemployment gradually grew from a level of 7.3 % in 2002 to 8.3 % in 2004 and then decreased to 7.9 % in 2005.

Graph 4 Participation rate – in total



Source: CSO

Graph 5 Participation of older persons



Source: CSO

B.2. SOCIAL INSURANCE INDICATORS

B.2.1. PREMIUMS

Revenues from social security premiums and contributions to the state employment policy constitute almost 40 % of all revenues of the state budget and represent approximately 90 % of all transfers paid out from the state budget. In this respect, the MLSA is not merely a “spender” of state revenue but rather contributes substantially to state budget revenues.

Developments in social insurance revenues are affected especially by the number and structure of contributors (and thus developments in employment) as well as the average payments per insured person. Both these indicators are predetermined by demographic and social economic developments. The contribution compliance is another factor which affects the amount of the payments.

The number of contributors gradually decreased in the period 1994–2000. However, it has had a rising trend since 2000, which is due mostly to the growth in the number of the self-employed paying premium deposits on social security and the state employment policy. The increase in the number of self-employed paying social security premiums and contributions to the state employment policy was due mainly to changes in legislation. As of January 2004, a self-employed person whose activity is deemed “main” (i.e. full-time self-employed) must pay insurance even when he does not have any income. According to statistics, in 2003 there were 646,000 self-employed persons paying deposits on pension insurance as opposed to 740,000 in 2005. The aim of the provisions providing for the obligations of the self-employed carrying out main activities to pay deposits on at least the minimum basic assessment base was to draw a part of them under insurance. The proportion of self-employed to the number of insured has been slowly increasing from 13.8 % in 2003 to 15.2 % in 2005.

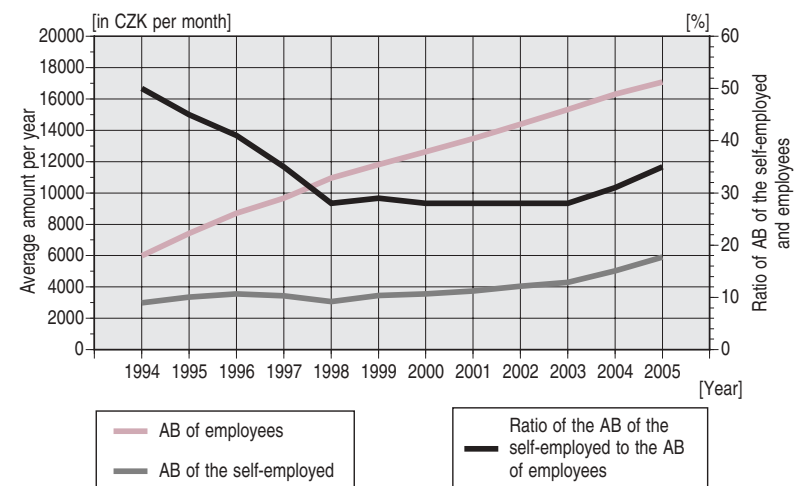
Table 7 Number and structure of insured persons

Year	Total	Employees		Self-employed	Total
		Organizations	Small org.		
Number [thous. of persons]					
1999	4,117	3,234	883	610	4,727
2000	4,016	3,169	847	619	4,635
2001	4,066	3,177	889	628	4,694
2002	4,068	3,157	911	641	4,709
2003	4,020	3,084	936	646	4,666
2004	4,041	3,093	948	727	4,768
2005	4,085	3,127	958	740	4,825
Proportion of the total number of insured persons [%]					
1999	87.1	68.4	18.7	12.9	100.0
2000	86.6	68.4	18.3	13.4	100.0
2001	86.6	67.7	18.9	13.4	100.0
2002	86.4	67.0	19.3	13.6	100.0
2003	86.2	66.1	20.1	13.8	100.0
2004	84.8	64.9	19.9	15.2	100.0
2005	84.7	64.8	19.9	15.3	100.0

Source: CSSA

The amount of the average payment per insured person is affected by developments in the income of the insured persons and whether they obtained such income as employees or as self-employed.

The assessment base for employee premiums is their total income (before tax) paid to them by the employer in relation to their employment activities which are covered under the sickness insurance, with the exception of those provided for under the law. The self-employed set their own assessment base. This amount however, may not be less than 50 % of their income from self-employed activities after deducting expenses for achieving, securing and maintaining such income and it may not be lower than the prescribed minimum. In 2006, the minimum for the self-employed carrying out main activities amounted to CZK 4,709 per month and for self-employed carrying out secondary activity (i.e. for part-time self-employed) it was CZK 1,884 per month. The maximum annual assessment base is CZK 486,000; this amount is proportionally decreased for each calendar month in which the self-employed does not carry out activities for the whole month, e.g. drew sickness benefits, etc. A comparison of developments in the above-mentioned assessment bases for the insurance of employees and the self-employed between 1994-2005 is reflected in the following graph.

Graph 6 Developments in the assessment base of employees and the self-employed

Source: CSSA

In 1994, the ratio of the assessment base for the self-employed in comparison to the assessment base of employees amounted to 50 %, then it decreased quickly and in 1998–2003 it was around 28 %. The reform of public finances which gradually increased the assessment base for self-employed premiums resulted in an increase in the ratio of the average assessment base of the self-employed to that of employees in 2005 by 35 %. The change of the premium amount is supposed to, amongst other, also raise the level of benefits so that some self-employed will not be at risk for poverty in old-age. According to the legislation in force in 2003, the amount of the future pension entitlement for the self-employed who paid premiums on the minimum assessment base is 2.5 times higher than that which they paid in premiums. Under an amendment to the legislation in 2004, the pension entitlements of employees with average income and insured periods will be approximately 13 % lower than what they will pay in premiums. In contrast, the entitlement of the self-employed with an average assessment base will be approximately 52 % higher than what they will pay in premiums.

The average assessment base for the payment of premiums (Table 8) is consistently lower than the average wage in the national economy, which is comprised of the wages of employees in organizations with more than 20 employees. In 2005, the assessment base for the payment of premiums of employees of organizations was approximately 5 % lower than the average wage in the national economy. In

addition, the year-on-year increase in the assessment base of employees has, since 2001, always been lower than the year-on-year growth of the average wage in the national economy. In contrast, the assessment base for the self-employed has since 2002 been growing faster than the average wage in the national economy. In 2005, the average assessment base of employees of organizations and small organizations from which premiums were paid amounted to CZK 17,081, which was CZK 781 (4.8 %) more than in 2004. In 2005, the self-employed paid premiums on average on an assessment base of CZK 5,914, which is 17.6 % higher than in 2004 when the assessment base amounted to CZK 5,028.

The growth of the assessment bases from which premiums are paid together with changes in the number of contributors resulted in a year-on-year increase in the amount of premiums by 7.9 % in 2004 and 6.0 % in 2005.

Table 8 Average assessment base for premiums

	2001	2002	2003	2004	2005
Average assessment base for employees [CZK/month]					
- employees of organizations	13,992	15,059	16,178	17,213	18,045
- employees of small organizations	11,616	12,051	12,553	13,321	13,936
- employees in total	13,472	14,385	15,334	16,300	17,081
- Self-employed insured under pension insurance	3,735	4,052	4,300	5,028	5,914
- Ratio of self-employed with pension insurance to employees in total [%]	27.7	28.2	28.0	30.8	34.6
Average wage in the national economy [CZK/month]	14,642	15,711	16,769	17,882	18,954
Difference in the average assessment base of employees and the average wage in the national economy [CZK/month]	-1,170	-1,326	-1 435-	-1 582	-1 873
Proportion of the average assessment base of employees and the average wage in the national economy [%]	92.0	91.6	91.4	91.2	90.1

Source: CSSA, MLSA

The maximum assessment base for social security insurance has only been set for the self-employed. As there is no maximum assessment base amount for employees, there is a large discrepancy between the premiums paid and the amounts of the benefits of those employees paying large premiums into the system. In addition, the cost of such employees to employers is very high.

Collection of premiums in relation to prescribed premiums (collection rate)

In 2005, the prescribed premiums including fines and penalties amounted to CZK 302.4 billion and total revenues including fines and penalties amounted to CZK 302.1 billion. The effectiveness of the collection of premiums, fines and penalties (contribution compliance) is set as the proportion of the total amount of

revenues to the total amount of prescribed premiums. In 2005, the collection rate amounted to 99.9 %, which is 0.7 percent less than in 2004 where the rate exceeded 100 % as a result of the recovery of outstanding claims.

In order to objectively evaluate the contribution compliance it is necessary exclude from the total contribution compliance written-off unrecoverable claims. Such write-offs decrease the total amount of prescribed premiums for a given year even though it involves old claims. The collection rate taking into account written-off claims amounted to 98 % in 2001 to 2003, 98.9 % in 2004 and approximately 98.4 % in 2005.

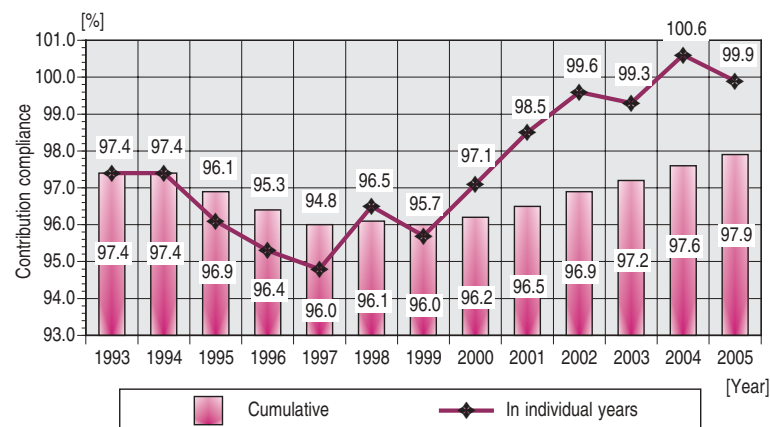
In 2005, CZK 301.4 billion was collected in premiums, not including fines, penalties and premium surcharges. Of this amount, 83 % (CZK 249.5 billion) was earmarked for pension insurance, 12 % (CZK 37.6 billion) for sickness insurance and 5 % (CZK 14.3 billion) for the state employment policy. The total prescribed amount of prescribed premiums not including fines and penalties was set at CZK 301.6 billion for all three areas of social insurance.

Table 9 Comparison of prescribed premiums and payments from 1999 to 2005

Year	Premiums including fines and penalties			Premiums without fines and penalties		
	Prescribed [mld. Kč]	Collected [mld. Kč]	Contribution compliance [%]	Prescribed [mld. Kč]	Collected [mld. Kč]	Ratio of collected/ /prescribed [%]
1999	213.8	204.6	95.7	207.5	201.6	97.1
2000	222.2	215.7	97.1	216.4	213.0	98.4
2001	238.7	234.8	98.4	233.7	232.2	99.4
2002	251.3	250.3	99.6	248.6	249.2	100.3
2003	265.9	264.2	99.4	262.2	262.1	100.0
2004	283.3	285.1	100.6	283.0	284.2	100.4
2005	302.4	302.1	99.9	301.6	301.4	100.0

Source: CSSA

Graph 7 Developments in the ratio of payments and prescribed premiums (including penalties, fines and premium surcharges)



Source: CSSA

When comparing the year-on-year growth index of prescribed premiums and collections, then up to the year 2002 the year-on-year growth index of collections was greater than the growth index of prescribed premiums as demonstrated by a contribution compliance greater than 100 %. In this respect, it is possible to state that recoverable past claims have been collected and the overall contribution compliance should in the future stabilise below 100 % (the value of the real annual collection).

The contribution compliance is impacted by the specific conditions in the regions, economic strength and the payment morality of debtors. It can be affected especially by the timely issue of statements of arrears and controlling activities. A comprehensive audit is undertaken for each contributor at least once every two years whereby it is necessary to follow the contributor's account and not permit an amount owed that is unmanageable for the contributor.

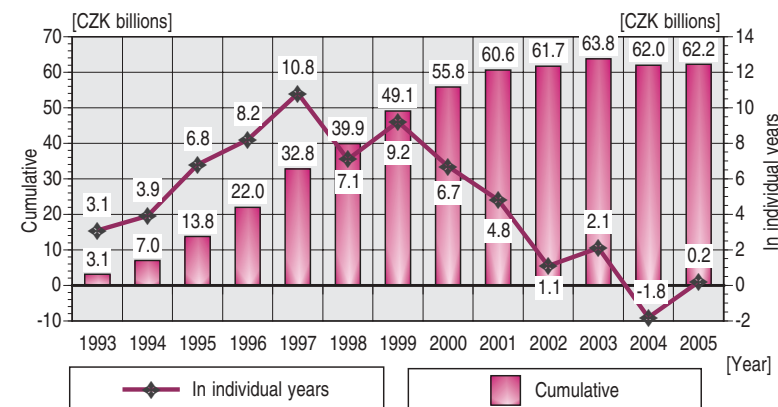
Taking into account experiences abroad, the collection of premiums may be deemed very good. The contribution compliance is comparable to that of developed European countries.

During the period from January 1993¹¹ to December 2005, a total of CZK 2,752 billion in premiums was prescribed. In the same period, the status of arre-

¹¹ On 1 January 1993, the Act No. 589/1992 Coll., on premiums for social security and contribution to the state employment policy came into effect.

ars (including fines and penalties) amounted to CZK 62.2 billion. Therefore the amount of the debt corresponded to approximately 2.3 % of the total amount of prescribed premiums and 2 % of the GDP in 2005. Claims grew by CZK 0.2 billion as compared with the previous year.

Graph 8 Developments in arrears (CZK billions)



Source: MLSA

Structure of receivables from contributors

As at 31 December 2005, receivables for deregistered entities amounted to CZK 36.8 billion (59 % of total receivables), those for current contributors CZK 24.6 billion (40 % of total receivables) and receivables in approved instalments amounted to CZK 0.8 billion (1 % of the total).

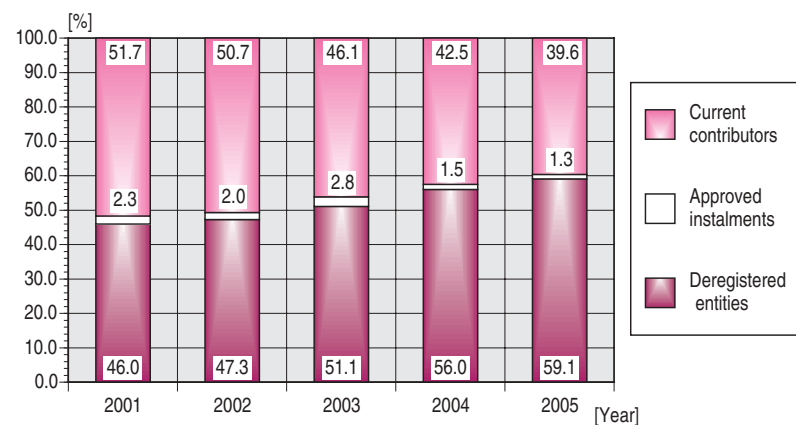
The ratio of claims against deregistered entities to the total amount of receivables continues to rise. In contrast, the ratio of claims against current payers is declining. Claims in approved instalments have been decreasing since 2003 both in absolute and relative terms.

Table 10 Structure of receivables for contributors (CZK millions)

State of receivables as at 31 st December	2001	2002	2003	2004	2005
Total	60,638	61,749	63,754	61,977	62,180
Deregistered contributors	27,897	29,147	32,609	34,720	36,777
Approved instalments	1,417	1,243	1,780	942	781
Current contributors	31,324	31,359	29,365	26,314	24,622

Source: CSSA

Graph 9 Structure of receivables for contributors as % of the total receivables (as at 31 December)



Source: CSSA

B.2.2. PENSION INSURANCE¹²

The basic compulsory pension insurance is based on the PAYGO method, i.e. benefits are directly paid out from the premiums collected. Financial funds are not accumulated with the aim of investing them.

Balanced financial results in a continuously financed system may be obtained if revenues are the same as expenditure, i.e. the following equation applies:

$$NC \times W \times (AB/W) \times CR \times CC \times (1 - AC) = NP \times P \quad [1]$$

where NC represents the number of contributors, W the average wage in the national economy, AB the average assessment base for the collection of premiums, CR the contribution rate, CC the contribution compliance, AC administrative costs expressed as a percentage of total revenue, NP the number of pensioners, P the average pension amount. By adjusting the equation no. 1 as follows, the relationship for the main parameters of balanced accounts may be obtained: the contribution rate, the total replacement ratio (the relation between the average pension and the average wage in the national economy) and the relation between the number of insured persons and the number of pensioners

$$CR \times (AB/W) \times CC \times (1 - AC) = P/W \times NP/NC \quad [2]$$

¹² More detailed data may be found in the Statistical Yearbook in the field of pension insurance published by the CSSA.

Developments in the number of contributors (including the problems associated with the development of their structure taking into account the amount of the premiums), the development of the average assessment base for the collection of premiums and its relation to the average wage in the national economy and the contribution compliance are dealt with in greater detail in Chapter B.2.1. which relates to both pension and sickness insurance. This section evaluates in particular expenditure for pension insurance and its causes. It focuses on the relationship between revenues and expenditure, developments in the number of pensioners and pensions, pension amounts and their differentiation.

B.2.2.1. Revenues and expenditure

In 1997-2003, expenditure on pensions surpassed revenues from pension insurance. A change in this trend occurred in 2004 as a result of an increase in the contribution rates for pension insurance from 26 % to 28 %. This development confirms that the decrease in the contribution rate to 26 % which occurred as of 1 January 1996 was inadequate given the needs of the pension system.

The surplus between revenues and expenditure in the pension system are amassed for the benefit of the pension insurance system, pursuant to Act No. 60/1995 Coll., amending and changing certain acts in relation to the adoption of the Pension Insurance Act, on a 'special account for pension insurance', which forms a part of the state financial assets. Under the Budgetary Rules Act, the surplus between premium revenues for pension insurance (including revenues from penalties and fines relating to pension insurance) and expenditure for pension insurance benefits (including costs associated with the collection of pension insurance premiums and the payment of pension insurance benefits) is transferred to this account.

As of the creation of the special pension insurance account by law in 1995, there was a surplus of CZK 4.4 billion for premiums for pension insurance versus expenditure in 1996. The surplus was used to cover a portion of the deficit of the pension insurance system in 2001. In 1997 to 2003, only a deficit was obtained, which forms a part of the aggregate deficit of the state budget and therefore no transfers to the special pension insurance account occurred. In 2004, **the surplus of the pension insurance system amounted to CZK 8.3 billion and CZK 6.6 billion in 2005**, respectively (data for all insurance administrators and including administrative costs).

In Chapter 313 – Civil Sector, **the surplus of revenues from premiums and on pension expenditure amounted to CZK 10.6 billion in 2004 and CZK 8.9 billion in 2005**.

Table 11 Pension insurance revenues and expenditure for pensions (Chapter 313 – Civil Sector)

Years	Revenues ¹ [CZK billions]	Expenditure ² [CZK billions]	Revenues - - Expenditures [CZK billions]
2001	180.2	196.1	-15.9
2002	192.2	208.3	-16.1
2003	202.8	220.3	-17.6
2004	235.8	225.2	10.6
2005	250.1	241.2	8.9

Source: National final accounts

Notes: ¹ Including fines, penalties and voluntary supplementary insurance.

² Not including deposits provided in the previous year but including deposits for the following year, without administrative costs.

The highest share of expenditure¹³ on pension insurance are those for old-age pensions. This is because old-age pensioners number the most from the total number of pensioners and the level of their pensions is the highest amongst all types of pensions.

Table 12 Expenditure¹ on pensions according to type of pension (Chapter 313 – Civil Sector)

Year	Type of pension						Total
	Old-age	Full disability	Partial disability	Widow	Widower	Orphan	
Expenditure [CZK billion]							
2001	140.7	28.0	7.7	15.9	1.2	2.4	195.8
2002	150.8	30.2	8.5	17.1	1.4	2.5	210.4
2003	156.3	31.5	9.1	17.3	1.5	2.5	218.3
2004	163.0	32.7	9.6	17.4	1.5	2.6	226.9
2005	175.7	35.0	10.6	18.0	1.7	2.7	243.6
Expenditure [% of total]							
2001	71.8	14.3	3.9	8.1	0.6	1.2	100.0
2002	71.6	14.4	4.0	8.1	0.7	1.2	100.0
2003	71.6	14.4	4.2	7.9	0.7	1.1	100.0
2004	71.9	14.4	4.2	7.7	0.7	1.1	100.0
2005	72.1	14.4	4.3	7.4	0.7	1.1	100.0

Source: CSSA

Note: ¹ Net expenditure not including deposits to post offices for the payment of pensions.

The basic parameters that influence expenditure on pension insurance are the number of pensioners or pensions and the amount of the pensions.

B.2.2.2. Number of pensioners and pensions

The total number of pensioners significantly increased in 2004 mostly due to an increase in the number of old-age pensioners, especially those to whom permanently reduced early old-age pensions are paid out. However, a change in this trend also occurred with respect to the number of pensioners drawing full (non-reduced) old-age pensions (granted once the retirement age is reached). Where as up to 2003 their number decreased, they have been increasing since 2004. The year 2003 was key for the development of the number of pensioners drawing temporarily reduced early old-age pensions. In that year, their number also doubled, however in subsequent years it has decreased. Developments in the number of old-age pensioners from 2003 to 2005 were significantly influenced by the response of pensioners to the legal provisions governing the conditions for entitlement to pensions (limiting the possibility of taking early retirement and the cancellation of the condition permitting entitlement to old-age pensions concurrently with performing gainful activity) as well as by the method of calculating pensions (the reduction of the crediting of the duration of studies). In 2004 and 2005, the number of women drawing only widower's pension decreased and the number of pensioners drawing disability pensions increased. The increase in the number of pensioners drawing partial disability pension was, however, smaller than in preceding years.

¹³ The annual expenditure on pensions are tracked statistically in two ways. For budgetary purposes they are stated including the balance from deposits provided to post offices for the payment of pensions at the beginning of the year (Table 11). The figures do not include such deposits for the purposes of comparing developments in real expenditure for the payment of pensions in a given year (Table 12).

Table 13 Number of pensioners¹ according to type of pension

Year	Total	Type of pension				Disability full	Disability partial	Widower and widow ⁶	Orphan ⁶	TOTAL
		Old-age Not reduced ²	Old-age Reduced permanently ³	Old-age Reduced temporarily ⁴	Proportionate old-age ⁵					
TOTAL										
2001	1,896,496	1,681,223	199,529	15,744	26,277	376,455	157,832	72,996	53,958	2,584,014
2002	1,883,314	1,659,163	210,960	13,191	24,516	378,433	166,405	70,729	54,401	2,577,798
2003	1,891,577	1,639,500	225,933	26,144	22,642	380,416	173,569	67,438	55,202	2,590,844
2004	1,923,728	1,648,673	250,683	24,372	21,187	384,203	179,173	63,374	54,020	2,625,685
2005	1,942,079	1,656,890	270,892	14,297	19,791	385,149	184,906	60,632	52,543	2,645,100
MEN										
2001	664,092	579,347	77,807	6,938	957	187,258	88,696	6,708	25,409	973,120
2002	656,217	568,327	82,034	5,856	1,057	188,680	92,891	7,255	25,339	971,439
2003	657,771	559,274	87,433	11,064	1,146	190,456	96,562	7,532	25,453	978,920
2004	669,969	563,112	96,641	10,216	1,251	192,961	99,197	7,535	24,773	995,686
2005	679,071	568,237	104,780	6,054	1,327	193,836	101,710	7,701	23,871	1,007,516
WOMEN										
2001	1,232,404	1,101,876	121,722	8,806	25,320	189,197	69,136	66,288	28,549	1,610,894
2002	1,227,097	1,090,836	128,926	7,335	23,459	189,753	73,514	63,474	29,062	1,606,359
2003	1,233,806	1,080,226	138,500	15,080	21,496	189,960	77,007	59,906	29,749	1,611,924
2004	1,253,759	1,085,561	154,042	14,156	19,936	191,242	79,976	55,839	29,247	1,629,999
2005	1,263,008	1,088,653	166,112	8,243	18,464	191,313	83,196	52,931	28,672	1,637,584

Source: CSSA

Notes: ¹ Number of pensioners to whom a pension was paid out in December; does not include pensions paid abroad.

² Only pensions paid out independently (not simultaneously with old-age, disability or partial disability pension).

³ Not reduced = old-age pension upon reaching retirement age.

⁴ Permanently reduced = up to 3 years before reaching the retirement age pursuant to Article 31 of Act No. 155/1995 Coll.

⁵ Temporarily reduced = up to 2 years before reaching the retirement age pursuant to Article 30 of Act No. 155/1995 Coll.

⁶ Proportionate old-age pension = old-age pensions granted under Article 26 of Act No. 100/1988 Coll. and pursuant to Article 29 (b) of Act No. 155/1995 Coll. (a short period of insurance).

The number of pensioners to whom a reduced old-age pension is paid out as a result of retirement before reaching retirement age also includes pensioners who have already reached retirement age. The ratio of these pensioners to the total number of pensioners drawing reduced old-age pensions is gradually increasing.

Table 14 Proportion of old-age pensioners receiving reduced old-age pensions after reaching retirement age to the number of all pensioners receiving reduced old-age pensions

Year	2001	2002	2003	2004	2005
Share in %	54.0	66.9	75.9	77.2	80.2

Source: MLSA

In 2001 to 2005, the total number of pensioners increased by 2.4 % whereas the greatest increase occurred in the number of pensioners with permanently reduced early old-age pensions. This is due to the specific structure of this group of pensioners. In their relatively small number increases in new pensioners are more evident. The smaller decrease in their number is caused by the lower age of these pensioners.

Table 15 Increases in the number of pensioners during 2001–2005 (in %)

	Type of pension									
	Total	Old-age Not reduced ²	Old-age Reduced permanently ³	Old-age Reduced temporarily ⁴	Proportionate old-age ⁵	Disability full	Disability partial	Widower and widow ⁶	Orphan ⁶	TOTAL
Total	2.4	-1.4	35.8	-9.2	-24.7	2.3	17.2	-16.9	-2.6	2.4
Men	2.3	-1.9	34.7	-12.7	38.7	3.5	14.7	14.8	-6.1	3.5
Women	2.5	-1.2	36.5	-6.4	-27.1	1.1	20.3	-20.1	0.4	1.7

Source: MLSA

Notes: viz Table no. 13.

The average age of pensioners did not change significantly from 2001 to 2005. The increase in the average age of recipients of reduced old-age pensions is reflected in the fact that the reduction of pensions continues even after reaching the retirement age. Thus, an increase in the proportion of older pensioners is reflected in these groups of pensioners. The average age of recipients of solo widow's pension is falling slightly as women are making use of the option of taking early retirement which is paid out concurrently with the widow's pension. The payment of only a widow's pension occurs with younger women who are not yet entitled to retire.

Table 16 Average age of pensioners¹

Year	Type of pension									TOTAL
	Total	Old-age Not reduced ²	Old-age Reduced permanently ³	Old-age Reduced temporarily ⁴	Proportionate old-age ⁵	Disability full	Disability partial	Widower and widow ⁶	Orphan ⁶	
MEN										
2001	70	71	60	59	72	56	48	49	15	63
2002	70	71	61	60	72	56	48	50	15	63
2003	70	71	62	60	72	56	49	50	15	63
2004	70	71	62	60	72	56	49	51	16	63
2005	70	71	63	61	72	56	49	51	16	63
WOMEN										
2001	68	69	56	55	78	58	47	61	16	65
2002	68	70	57	56	79	58	47	60	16	65
2003	68	70	58	56	79	58	47	60	16	65
2004	68	70	58	56	79	58	48	59	17	65
2005	69	70	59	57	79	58	47	59	17	65

Source: CSSA

Note: ¹ Age reached by pensioners whose pensions were paid out in December; does not include pensions paid abroad.

See notes ²⁻⁶ for Table No. 13.

In 2004 and 2005, the **ratio of pensioners to the number of contributors** – one of the basic indicators that is decisive for the balanced financial accounts of pension insurance – reflected a positive development. The number of contributors in the system increased faster in these years than the number of pensioners. As a result, the proportion of pensioners and the number of contributors decreased in 2004 to 54.8 % (in 1996 it was however 47.6 %).

Table 17 Number of pensioners in relation to number of insured persons

Year	Number of insured [thous.]	Number of pensioners [thous.]	Ratio of the number of pensioners to number of insured persons [%]
2001	4,694	2,584	55.0
2002	4,709	2,578	54.7
2003	4,666	2,591	55.5
2004	4,767	2,626	55.1
2005	4,826	2,645	54.8

Source: CSSA

Under the Act, pensioners may draw more than one type of pension. It is possible to concurrently receive a direct pension (i.e. old-age, full or partial disability) and a survivor's pension (i.e. widow, widower or orphan). The number of pensions paid out thus exceeds the number of pensioners. The following equation applies:

$$NP = NPs - WP_{\text{concurrency}} - OP_{\text{concurrency}} \quad [3]$$

where NP is the number of pensioners, NPs is the number of pensions, $WP_{\text{concurrency}}$ is the number of widow or widower pensions paid out together with a direct pension and $OP_{\text{concurrency}}$ is the number of orphan pensions paid out together with a direct pension.

The number of pensions paid out, after decreasing in 2002, continued to rise in the following years whereby the highest year-on-year increase (1.2 %) occurred in 2004. This development and its causes were the same as those for the development in the number of pensioners. The ratios of the various types of pensions did not significantly change in these years. The most significant increases occurred in partial disability pensions whereas, in contrast, the number of widower pensions has been decreasing.

Table 18 Number of pensions paid out¹

Year	Type of pension							TOTAL
	Old-age	Proportionate old-age	Full disability	Partial disability	Widow	Widower	Orphan	
2001	1,896,496	26,277	376,455	157,831	610,483	81,716	53,961	3,203,219
2002	1,883,314	24,516	378,433	166,405	608,003	84,677	54,401	3,199,749
2003	1,891,577	22,642	380,416	173,569	602,861	86,219	55,202	3,212,486
2004	1,923,728	21,187	384,203	179,173	599,530	87,865	54,020	3,249,706
2005	1,942,079	19,791	385,149	184,906	595,072	89,133	52,543	3,268,673
As a % of total								
2001	59.2	0.8	11.8	4.9	19.1	2.6	1.7	100.0
2002	58.9	0.8	11.8	5.2	19.0	2.6	1.7	100.0
2003	58.9	0.7	11.8	5.4	18.8	2.7	1.7	100.0
2004	59.2	0.7	11.8	5.5	18.4	2.7	1.7	100.0
2005	59.4	0.6	11.8	5.7	18.2	2.7	1.6	100.0

Source: CSSA

Notes: ¹ The number of pensioners to whom a pension was paid out in December; does not include pensions paid abroad.

A marginal amount of pensions are paid out abroad. Their proportion to all pensions paid out is increasing slightly.

Table 19 Pensions paid out abroad

Year	2001	2002	2003	2004	2005
Pensions paid out abroad	25,703	26,153	32,520	33,935	37,788
Share of all pensions (in %)	0.80	0.81	1.00	1.03	1.14

Source: CSSA

The total number of pensions paid out up to the end of the year T (NPs(T)) is composed of the total of number pensions paid out up to the end of the year T-1 (NPs(T-1)) after deducting the number of pensions that terminated in year T (NPsT(T)) and the aggregate number of newly granted pensions in the year T (NNPs(T)). Therefore, the following equation applies to the number of paid out pensions:

$$\text{NPs(T)} = \text{NPs(T-1)} - \text{NPsT(T)} + \text{NNPs (T)}. \quad [4]$$

The development of paid out pensions is affected by the **number of newly granted pensions**.¹⁴ In 2003, there was a substantial increase in the number of newly granted pensions (17 %) of which a large portion represented an increase in the number of newly granted old-age pensions (a total of 34 %). To a certain degree, this trend is caused by demographic developments, i.e. an increase in the number of persons who are of a possible retirement age. The following may be considered as the main factors influencing the increase in the number of newly granted old-age pensions:

- the reaction of citizens to the Act adopted in 2003 under which as of 1 January 2004 the possibility of taking a temporarily reduced early old-age pension was kept only for those who are long-term disabled and not as a solution for those citizens who are unemployed. These citizens attempted to make use of this option while the previous Act was in force especially in light of rising unemployment. This led to a significant inc-

¹⁴ The statistical following of data for newly granted pensions is carried out as of 2002 according to a new methodology. Data is now categorised according to the date when the pension was granted as opposed to the old method under which it was from the date from which the pension began to be paid out (these dates may differ even by a few months, where such difference depends on the length of the proceeds for granting pension and the administrative technological measures of processing the application for pension). The new methodology corresponds exactly with the granting of the pension and thus provides a more objective data, e.g. the amount of the pension influenced by reduction limits whose amounts change as of 1 January of each year. The said change in the statistic methodology had an impact on the comparability of the time aspects from previous years and therefore the data is listed only from 2002.

rease in the number of newly granted temporarily reduced early old-age pensions, which compared to 2002 more than doubled (an increase of 127 %).

- rising unemployment and changes in the calculation of old-age pensions from 1 January 2004 (reduction of the valuation of studies) may have caused an increase of 35 % in the number of newly accorded permanently reduced early old-age pensions as opposed to 2002 despite the measures adopted in 2001 which limit the advantageousness of this type of pension. The ratio of newly granted early old-age pensions (temporarily and permanently reduced) to the total amount of old-age pensions granted thus reached 45 %.

In 2004, the number of newly granted pensions grew about by one third compared with 2003. The number of newly granted temporarily reduced early old-age pensions decreased by about 1/5, but the number of newly granted permanently reduced early old-age pensions increased by 55 %. The number of old-age pensions granted upon reaching retirement age increased by about one third and the number of old-age pensions granted after deferring retirement by 2/5, thereby reaching a ratio of 24 % of all old-age pensions accorded. This increase was apparently influenced the cancelling of the condition limiting the payment of old-age pensions concurrently with gainful activity during the first two years after entitlement to such pension occurs.

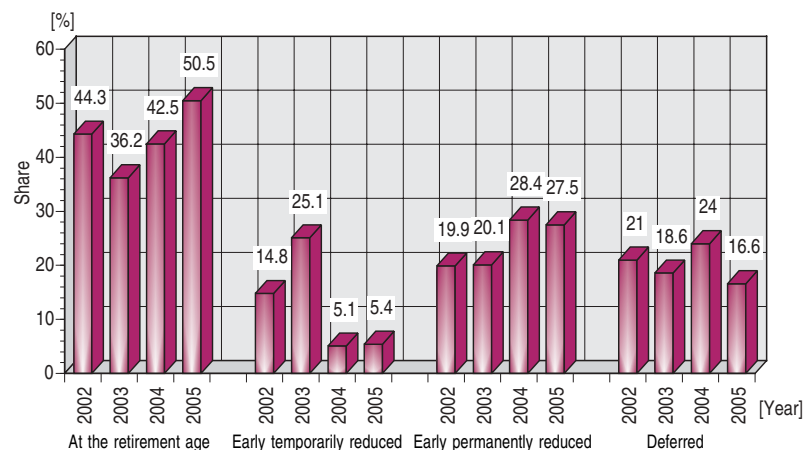
In 2005, the number of newly granted pensions decreased by 13,019, i.e. by 7 %, as compared to 2004. This occurred with all types of the pensions. The most significant (by 10 %) occurred with the permanently reduced early old-age pensions and with full disability pensions. The decrease in the share of old-age pensions granted after reaching retirement age fell from 24 % to 17 % and the proportion of old-age pensions granted to the date of reaching retirement age increased from 43 % to 51 %. This is apparently caused by less interest in deferring retirement as a result of cancelling the condition limiting the entitlement to the payment of old-age pension concurrently with income from gainful activity in the first two years following entitlement to such pensions.

Table 20 Number of newly granted pensions and their development

Type of pension	Number of pensions granted				Change from previous year		
	2002	2003	2004	2005	2003	2004	2005
Total old-age	63,560	85,331	93,855	86,631	134	110	92
Total after the retirement age	41,487	46,807	62,439	58,142	113	133	93
At the retirement age	28,171	30,906	39,895	43,764	110	129	110
Deferred	13,316	15,901	22,544	14,378	119	142	64
Total early	22,073	38,524	31,416	28,489	175	82	91
Temporarily reduced	9,429	21,415	4,795	4,645	227	22	97
Permanently reduced	12,644	17,109	26,621	23,844	135	156	90
Proportionate old-age	292	273	265	282	93	97	106
Total full disability	24,438	25,544	26,353	23,613	105	103	90
From youth	590	579	587	594	98	101	101
Other	23,848	24,965	25,766	23,019	105	103	89
Partial disability	21,711	23,010	24,088	22,571	106	105	94
Widow and widower	38,495	40,741	39,840	38,708	106	98	97
Orphan	5,580	5,726	5,666	5,243	103	99	93
TOTAL	154,076	180,625	190,067	177,048	117	105	93

Source: CSSA

Graph 10 Developments in the share of newly granted old-age pensions



Source: CSSA

The average retirement age has not changed significantly since 1996; its small growth relates to increases in the retirement age.

Table 21 Average retirement age

Year	Type of pension							
	Total	Old-age Not reduced	Reduced permanently	Reduced temporarily	Proportionate old-age	Disability full	Disability partial	Widower and widow
MEN								
2002	60	61	58	59	65	48	47	68
2003	60	61	59	59	65	49	48	69
2004	61	61	59	59	65	49	48	69
2005	61	61	59	59	65	49	49	69
WOMEN								
2002	56	57	54	55	65	45	45	65
2003	56	57	55	55	65	46	46	65
2004	57	57	55	55	65	46	46	65
2005	57	57	56	56	65	46	46	66

Source: CSSA

Notes: Not reduced = old-age pension upon reaching retirement age.

Permanently reduced = up to 3 years before reaching the retirement age pursuant to Article 31 of Act No. 155/1995 Coll.

Temporarily reduced = up to 2 years before reaching the retirement age pursuant to Article 30 of Act No. 155/1995 Coll.

In 2004 and 2005, the average retirement age was 61 for men and 57 for women. The age for retiring thus did not significantly differ from the prescribed retirement age in these years.

Table 22 Retirement age in 2004 and 2005

	Men	Women with number of children				
		0	1	2	3 or 4	5 or more
For those born in the year	1943	1945	1946	1947	1948	1949
Retirement age	61y+4m	59y+4m	58y+4m	57y+4m	56y+4m	55y+4m
For those born in the period	I 1944	I 1946	I 1947	I 1948	I 1949	I 1950
Retirement age	VI 1944	IV 1946	IV 1947	IV 1948	IV 1949	IV 1950
Retirement age	61y+6m	59y+8m	58y+8m	57y+8m	56y+8m	55y+8m

Source: MLSA

The retirement age has been continuing to increase since 1996. Under the Act currently in force, the retirement age will continue to increase gradually up to 63 for men and 59 to 63 for women according to the number of children brought up. This retirement age will be reached by men in 2016 and by women in 2019.

Table 23 Year in which entitlement to pension arises for a given age

Retirement age	Men	Women with number of children				
		0	1	2	3 or 4	5 or more
54						1999
55						1999 2003
56				1999	2003	2007
57			1999	2003	2007	2011
58		1999	2003	2007	2011	2015
59		2003	2007	2011	2015	2019
60		2007	2011	2015	2019	
61	2002	2011	2015	2019		
62	2009	2015	2019			
63	2016	2019				

Source: MLSA

In 2005, approximately 162,224 pensions **terminated** for various reasons, i.e. about 14,000 less than the number of pensions newly granted. Of the terminated pensions, 74 % occurred due to the death of the pensioner and 17 % due to the granting of a different type of pension. In comparison with previous years, there was a significant increase in the number of temporarily reduced early old-age pensions, which ended due to the granting of a different type of pension (from 44 in 2004 to 9, 695 in 2005). This increase is due to a change in the method of recording changes.

Table 24 Number of terminated pensions

Year	2002	2003	2004	2005
Total of terminated pensions	144,656	170,024	148,009	162,224
of which: old-age	64,648	77,526	65,449	76,601
full disability	22,300	25,179	22,626	23,925
partial disability	13,526	16,783	16,112	17,239
Reason for termination				
due to granting of another pension	12,919	15,783	15,764	27,351
death	115,955	139,651	117,798	120,338

Source: CSSA

B.2.2.3. Amount of pensions

The **average amount of the pensions paid out** is affected foremost by the adjustment (valorization) of the pensions paid out. Its growth is, however, also influenced by generational changes which cause the average amount of pensions

paid out to increase even if the pensions are not adjusted due to the termination of the pensions of older pensioners, which are lower than the pensions that are newly granted.¹⁵ Given that in 2002 no adjustment of pensions occurred, the total average monthly amount of solo pensions only increased by 0.1 % and old-age pensions by 0.4 % (the amount in December 2001 and the amount in December 2002). With the uniform increase in the percentage-based assessment of paid out pensions by 2.5 % from January 2004, the aggregate average amount of solo pensions increased by 2.7 % from December 2003 to December 2004 and by 2.8 % for old-age pensions. In 2005, the said average pension amounts increased by 6.5 %.

Table 25 Average monthly amounts¹ of solo paid out pensions (in CZK)

Year	Total	Type of pension						TOTAL		
		Old-age Not reduced ²	Reduced permanently ³	Propor- -tionate temporarily ⁴	old-age ⁵	Disability full	Disability partial		Widower and Orphan ⁶ widow ⁶	
TOTAL										
2001	6,814	6,908	6,303	6,011	3,808	6,638	4,147	4,783	3,289	6,389
2002	6,841	6,949	6,272	5,896	3,705	6,666	4,132	4,739	3,327	6,398
2003	7,083	7,226	6,432	6,122	3,699	6,911	4,243	4,830	3,440	6,616
2004	7,280	7,454	6,537	6,191	3,666	7,088	4,315	4,889	3,529	6,797
2005	7,755	7,953	6,914	6,536	3,775	7,537	4,584	5,143	3,780	7,238
MEN										
2001	7,594	7,682	7,074	6,743	3,609	7,172	4,399	3,620	3,274	7,040
2002	7,627	7,731	7,044	6,625	3,437	7,192	4,382	3,651	3,313	7,045
2003	7,909	8,044	7,241	6,934	3,376	7,449	4,501	3,770	3,426	7,285
2004	8,141	8,306	7,379	7,020	3,313	7,628	4,579	3,862	3,512	7,487
2005	8,671	8,860	7,802	7,406	3,413	8,096	4,861	4,123	3,761	7,969
WOMEN										
2001	6,195	6,278	5,778	5,372	3,829	5,977	3,809	4,901	3,303	5,841
2002	6,221	6,319	5,744	5,255	3,739	6,015	3,803	4,863	3,340	5,854
2003	6,438	6,571	5,879	5,479	3,748	6,243	3,905	4,963	3,452	6,053
2004	6,610	6,774	5,963	5,545	3,730	6,415	3,975	5,028	3,544	6,216
2005	7,042	7,227	6,302	5,839	3,848	6,840	4,235	5,291	3,796	6,621

Source: CSSA

Notes: ¹ The average amount of pensions paid out in December; does not include pensions paid abroad.

Solo = only pensions paid out independently (not concurrently with survivor's pensions)

³⁻⁶ see notes to Table No. 13.

¹⁵ The average amount of terminated pensions has for several years no longer been recorded by CSSA.

Under the Act, paid out pensions are as of 2003 adjusted regularly in January of each year whereas the minimum prescribed increase provided for under law reflects a 100 % growth in prices and a 1/3 growth in real wages. This stipulated minimum was exceeded by the adjustments carried out in 2003 and 2005 by 0.1 % and by 0.2 % in 2004 respectively.

Table 26 Overview of increases to paid out pensions

Month and year the increase came into effect	December 2001 January 2003 January 2004 January 2005 January 2006				
	Increase of the basic amount of pension				90 Kč
Increase of the pension percentage-based assessment					
- old-system pensioners	11%	4.0%	2.5%	5.4%	6.0%
- new-system pensioners	8%	3.8%			4.0%
Basic amount of pension	1,310 CZK	1,310 CZK	1,310 CZK	1,400 CZK	1,470 CZK

Source: MLSA

Notes: Old-system pensioners = pensions granted before 1 January 1996; new-system pensioners = pensions granted after 31 December 1995.

Pensioners to whom a pension was paid out in June 2004 were also paid out a one-time payment of CZK 1,000 as assistance for changes made in the amount of the value added tax. This benefit does not constitute a pension insurance benefit, nor is the expenditure for its payment included in the pension insurance expenditure.

The growth of the average amount of paid out pensions was, for the most part, slower than the growth of the average wage in the national economy. Therefore, the total replacement ratio (the second parameter that affects the balancing of pension insurance accounts) kept falling until 2004. In 2005, it increased by 0.2 % to 40.8 % of the gross wage and to 53.9 % of the net wage.

Table 27 Total replacement ratio, 2001-2005¹

Year	Average pension ² [CZK]	Average wage		Total replacement ratio	
		Gross ³ [CZK]	Net ⁴ [CZK]	Gross [%]	Net [%]
2001	6,352	14,640	11,324	43.4	56.1
2002	6,830	15,711	12,082	43.5	56.5
2003	7,071	16,769	12,807	42.2	55.2
2004	7,256	17,882	13,601	40.6	53.3
2005	7,728	18,954	14,339	40.8	53.9

Source: MLSA

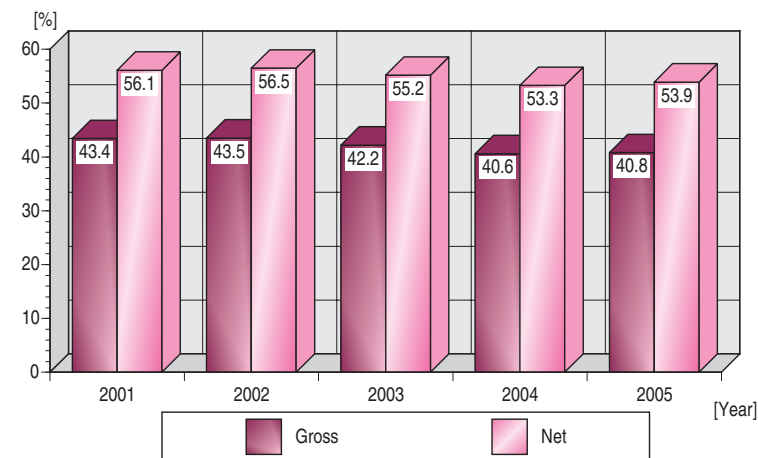
Notes: ¹ Total replacement ratio = relation of the average old-age pension to the average wage.

² The average pension is the average monthly solo old-age pension paid out in a given year.

³ The general assessment base (Article 17 (2) of Act No. 155/1995 Coll.) is published by Government Decree and equates to the amount of the average monthly wage as determined by the Czech Statistical Office.

⁴ The average net wage is the average gross wage decreased by the corresponding amount of income tax, health insurance and social security premiums.

Graph 11 Total replacement ratio, 2001-2005¹



Source: MLSA

Note: ¹ Total replacement ratio = relation of the average old-age pension to the average wage.

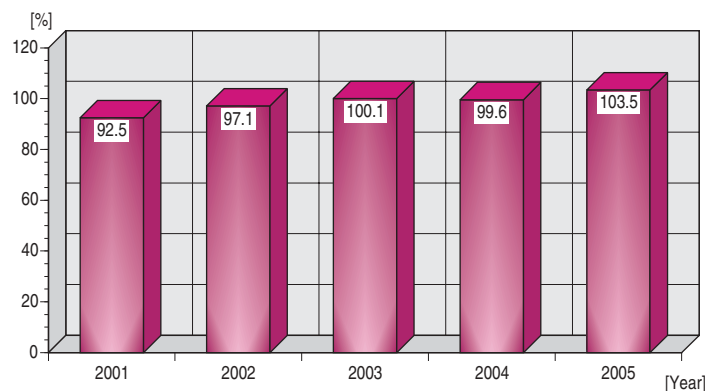
The developments of the relation between the average old-age pension to the wage may be deemed “positive” in terms of its effect on the balance of revenues and expenditure on pensions, however not with respect to the development of the standard of living of pensions, particularly in comparison with developments in the standard of living of economically active persons. **The development of the real value of pensions lags behind the development of the real value of wages.** Whereas the real value of wages grew year-on-year by 3.7 % in 2004 and by 4.1 % in 2005 (Chapter B.1.1.), the real value of the average old-age pension paid out increased by 4.0 % in 2005 but decreased by 0.6 % in 2004 (the one-time payment paid out in June 2004 was not included in the calculation as not all pensioners were entitled to it).

Table 28 Developments in the real value of the average old-age pension

Year	100 % in the year			
	2001	2002	2003	2004
2001	100.0			
2002	105.0	100.0		
2003	108.3	103.1	100.0	
2004	107.7	102.5	99.4	100.0
2005	111.9	106.6	103.4	104.0

Source: MLSA

Graph 12 Developments in the real value of the average old-age pensions as percentage of its value in 1989



Source: MLSA

The average amount of old-age pensions also depends on the year that they were granted: the longer the pensions are paid out, the lower they are. Such differences are caused by wage developments and changes in the method of calculating newly granted pensions.

Table 29 Average amount of solo old-age pensions paid out according to the period they were granted (pensions paid out in 2005 in CZK/month)

Year granted	Total	Not reduced	Early reduced	
			permanently	temporarily
-1975	7 233	7,233		
1976-80	7,253	7,253		
1981-88	7,443	7,443		
1989-95	7,666	7,666		
1996-98	7,795	8,116	6,847	7,016
1999	7,681	8,121	6,512	7,137
2000	7,575	8,372	6,238	6,974
2001	7,833	8,488	5,814	6,846
2002	8,101	8,594	5,907	6,405
2003	8,044	8,606	6,166	6,584
2004	8,172	8,773	6,521	6,666
2005	8,394	8,957	6,795	6,986
Total	7,756	7,953	6,536	6,914
Old-system pensioners	7,558	7,558		
New-system pensioners	7,920	8,453	6,536	6,914

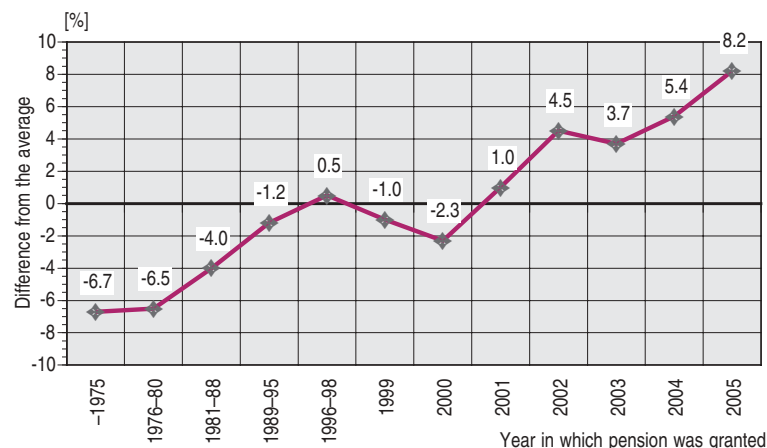
Source: CSSA

Notes: Not reduced = an old-age pension upon reaching retirement age.

Permanently reduced = up to 3 years before reaching the retirement age pursuant to Article 31 of Act No. 155/1995 Coll.

Temporarily reduced = up to 2 years before reaching the retirement age pursuant to Article 31 of Act No. 155/1995 Coll.

Graph 13 Difference between the average amount of old-age pensions paid out granted in different periods and the average amount of all old-age pensions paid out (in %)



Source: MLSA

The changes under the Pension Insurance Act (Act No. 155/1995 Coll.) caused the pensions of old-system pensioners (i.e. pensions granted before 1 January 1996) to be continuously lower than those of the new-system pensioners (i.e. pensions granted after 31 December 1995) even though the pensions of the old-system pensioners were adjusted five times between 1998 and 2003 more advantageously than those of the new-system pensioners. Given that the adjustments in 2004 and 2005 were not differentiated in such a way, the difference between the average amount of the old-age pensions of the old-system pensioners and that of the new-system pensioners increased to CZK 362 (4.8 %) in December 2005. With respect to new-system pensioners, the average amount of all old-age pensions is affected (decreased) by a specific factor which is the increasing share of reduced early old-age pensions. As concerns non-reduced old-age pensions, the difference between the average amount of the old-age pensions of old-system pensioners and those of the new-system pensioners is higher – in December 2005 it amounted to CZK 895, i.e. 11.8 %.

At present, increases in the earnings from which pensions are assessed have a greater impact on differences in the amounts of the pensions of old-system pensioners and those of the new-system pensioners rather than the changes in their calculation brought on by Act No 155/1995 Coll. Such growth in earnings and its corresponding increase in the amounts of the newly granted pensions permanently raises the average amount of the pensions of new-system pensioners. This

is seen in comparing the average amount of the pensions of the groups of pensioners granted both before and after Act No. 155/1995 Coll. came into effect.

Table 30 Average solo old-age pension according to year granted (in CZK)

	Period of granting the pension			
	Before 1989	1989–1995	1996–2000	2001–2005
All old-age pensions	7,405	7,666	7,717	8,130
Non-reduced old-age pensions	7,405	7,666	8,160	8,714

Source: MLSA

Note: Non-reduced = old-age pension on reaching the retirement age.

The number of old-system pensioners is gradually decreasing; their share of the total number of pensioners fell in the period 2001–2005 by almost 17 percentage points.

Table 31 Developments in the proportion of old pensioners to the total number of pensioners

Year	2001	2002	2003	2004	2005
Share in %	69,5	65,9	61,5	56,5	52,7

Source: MLSA

The average amount of newly granted pensions is higher than the average amount of paid out pensions and their relation to the average wage in the national economy is more advantageous. This is caused by the fact that these pensions are derived from higher earnings as a result of growth in wages and the dynamic pension structure in which the assessment bases (earnings of the insured) are indexed to wage growth in the national economy and the regular increases of the reduction limits limiting the inclusion of earnings decisive for the calculation of the pensions.

Table 32 Reduction limits for the calculation of pension amounts

	2001	2002	2003	2004	2005	2006
First reduction limit [CZK]	6,600	7,100	7,400	7,500	8,400	9,100
as a % of the average wage ¹	45.1	45.2	44.1	41.9	44.3	x
Second reduction limit [CZK]	15,300	16,800	17,900	19,200	20,500	21,800
as a % of the average wage ¹	104.5	106.9	106.7	107.4	108.2	x

Source: MLSA

Note: ¹ Average wage = the general assessment base (Article 17 (2) of Act No. 155/1995 Coll.).

With higher earnings there is a decrease in the relation of the pension amount to such earnings due to the reduction limits decisive for the calculation of pensions. Until 2004, the first reduction limit increased slower than the average wage in the national economy so the band of earnings that are fully credited in the amount of pensions was becoming smaller (in relation to the average wage). The second reduction limit grew in these years somewhat faster than the average wage in the national economy except for in 2003. As a result, the band of earnings that are credited by 30 % for the pension amount was extended (both absolutely and relatively as a % of the first reduction limit) and did so, for the most part, to the detriment of the categories in which earning are fully credited for the pension amount and which affect the amounts of all pensions. These trends were reflected in the decreasing level of newly granted pensions (their relation to wages in the national economy) up to 2004 and in their slight increase in 2005.

Table 33 Developments in the relation of newly granted old-age pensions to wages in 40 years of being insured and at different wage levels (in %)

Multiple of the average wage ¹	Year in which old-age pension was granted				
	2001	2002	2003	2004	2005
0.7	57.8	57.0	55.6	53.6	55.1
1.0	45.9	45.3	44.3	42.9	44.0
1.5	33.0	32.8	32.1	31.2	32.0
2.0	26.2	26.1	25.6	24.9	25.5
2.5	22.2	22.1	21.7	21.1	21.6
3.0	19.5	19.4	19.1	18.6	19.0

Source: MLSA

Note: ¹ Average wage = general assessment base (Article 17 (2) of Act No. 155/1995 Coll.).

Table 34 Average amount¹ of newly granted old-age pensions

Type of pension	CZK				As a % of the average gross wage ²			
	2002	2003	2004	2005	2002	2003	2004	2005
Total old-age	7,117	7,248	7,760	8,391	45.3	43.2	43.4	44.3
Total after the retirement age	7,781	8,096	8,489	9,092	49.5	48.3	47.5	48.0
At the retirement age	7,362	7,537	7,968	8,693	46.9	44.9	44.6	45.9
Deferred	8,665	9,179	9,410	10,306	55.2	54.7	52.6	54.4
Total early	5,863	6,217	6,308	6,960	37.3	37.1	35.3	36.7
Temporarily reduced	5,994	6,319	6,404	6,836	38.2	37.7	35.8	36.1
Permanently reduced	5,765	6,088	6,291	6,984	36.7	36.3	35.2	36.8
Proportionate old-age	2,301	2,372	2,366	2,489	14.6	14.1	13.2	13.1
Total full disability	7,164	7,413	7,740	8,396	45.6	44.2	43.3	44.3
From youth	5,567	5,766	5,979	6,483	35.4	34.4	33.4	34.2
Other	7,203	7,451	7,780	8,446	45.8	44.4	43.5	44.6
Partial disability	4,163	4,289	4,451	4,809	26.5	25.6	24.9	25.4
Widow and widower	4,386	4,513	4,659	4,961	27.9	26.9	26.1	26.2
Orphan	3,574	3,637	3,778	4,050	22.7	21.7	21.1	21.4
TOTAL	6,231	6,488	6,916	7,458	39.7	38.7	38.7	39.3

Source: CSSA

Notes: Does not include pensions paid out abroad.

Deferred = old-age pensions increased by additional activities after reaching retirement age without drawing a pension.

Early temporary = up to 2 years before reaching the retirement age for granting old-age pensions pursuant to Article 30 of Act No. 155/1995 Coll.

Early permanent = up to 3 years before reaching the retirement age pursuant to Article 31 of Act No. 155/1995 Coll.

Proportionate old-age = old-age pensions granted pursuant to Article 29 (b) of Act No. 155/1995 Coll. (short period of being insured).

Disability in youth = disability pensions pursuant to Article 42 of Act No. 155/1995 Coll.

¹ Amount of pensions not decreased for concurrence with another pension.

² Average gross wage - general assessment base (Article 17 (2) of Act No. 155/1995 Coll.).

B.2.2.4. Reduction of pensions due to early retirement

In early old-age retirement, the amount of the percentage-based assessment of the old-age pension is decreased as seen in Table 35. Given the different importance accorded to the basic amount of pensions for those pensioners with varying periods of insurance and amounts of assessment bases, this decrease has a different impact on the total amount of the old-age pension. In increasing the basic amount, a smaller decrease in the early old-age retirement occurs due to the increase in its weight in relation to the total pension, whereas this is most evident for those persons with a low assessment base and a short insured period. The increase in the basic amount of pensions from CZK 1,310 in 2004 to CZK 1,470 in 2006 has an impact on the cases set forth in the Table by 0.1–0.4 percentage points.

The greatest decrease in pensions (proportion of the monthly amount of reduced pensions to the monthly amounts of non-reduced pensions) occurs for those insured persons who have a short insured period and a high assessment base, which is caused by the great impact of the reduced percentage-based assessment and the relative large weight of the assessment in relation to the total pension. In contrast, such a reduction has the lowest impact on persons with low assessment bases and long insured periods.

Table 35 Reductions in early old-age pensions permanently reduced¹ granted in 2005 (in %)

Personal assessment base [CZK]	Number of years being insured				
	25	30	35	40	45
5 000	-5,5	-4,9	-4,5	-4,1	-3,8
10 000	-6,7	-5,9	-5,3	-4,7	-4,3
15 000	-7,0	-6,1	-5,4	-4,9	-4,4
20 000	-7,3	-6,3	-5,6	-5,0	-4,5
25 000	-7,4	-6,4	-5,6	-5,1	-4,6
30 000	-7,5	-6,4	-5,7	-5,1	-4,6

Source: MPSV

Note: ¹360 days before reaching retirement age (i.e. 4 x 90 days).

B.2.2.5. Differentiation of pensions according to pension amount¹⁶

The differentiation of old-age pensions according to their amount is affected by a number of factors. Their level and development is influenced especially by the following:

- developments in the differentiation of newly granted pensions in individual years, which clearly has an increasing trend as a result of dynamic elements in the equation for calculating the amount of pensions,
- varying differentiation of the pension amounts taking into account the period when they were granted and the decreasing share of pensions granted in the past (with a smaller differentiation),
- developments in the ratio of the basic amount of a pension to the total pension amount,
- valorization of pensions and the differentiation of their amounts for old-system and new-system pensioners,
- structural differences in the groups where the differentiation is measured from the perspective of the influence of factors not relating to the pension system.

The differentiation of pensions decreases with a shift from the group of all old-age pensions to groups for men and women. In 2002–2005, the differentiation continued to grow slowly foremost as a result of a slightly faster growth in the higher pensions of women.

¹⁶ Quantiles and the characteristics derived from them will be used for the measurement of the differentiation of old-age pensions according to pension amount. A quantile is the amount of earning (e.g. pension) which a certain group of pensioners reaches. For example, 10% quantile is the amount of earning stating that 10 % of the people have earnings up to this amount. A 50% quantile is referred to as the median and, in cases of normal division, amounts to the average. The basic characteristic will be the width of the interval in earnings around the median expressed in percentage of the median, in which are found:

- 20 % pensioners: the respective characteristic is marked as $M(20) = 100 \times (k_{60} - k_{40}) / \text{median}$,
- 50 % pensioners: the respective characteristics is marked as $M(50) = 100 \times (k_{75} - k_{25}) / \text{median}$,
- 80 % pensioners: the respective characteristic is marked as $M(80) = 100 \times (k_{90} - k_{10}) / \text{median}$,

where k_x marks the x % quantile.

The more the numbers $M(XX)$ are greater, i.e. the interval in which the respective share of pensioners is greater, the larger is the difference.

Calculated according to data on solo old-age pensions.

Table 36 Basic characteristics of differentiation in the amount of solo paid out old-age pensions

Year	2001	2002	2003	2004	2005	Change 2001-2005
M(20) Men	6.5	6.6	6.8	7.0	7.2	0.7
Women	5.5	5.7	6.0	6.3	6.7	1.1
Total	8.5	8.7	9.0	9.4	9.5	1.0
M(50) Men	16.3	16.6	17.1	17.9	19.8	3.5
Women	15.8	16.4	17.3	18.3	19.2	3.4
Total	22.4	22.9	23.7	24.7	25.3	2.9
M(80) Men	33.7	34.3	36.3	37.5	38.4	4.7
Women	35.4	36.6	38.3	40.3	41.5	6.1
Total	42.2	43.0	44.5	46.6	48.8	6.5

Source: MLSA

The developments in the differentiation of paid out old-age pensions according to their amounts are also influenced by the growing importance of the number of early old-age pensions whose differentiation is different than that of non-reduced old-age pensions granted upon a given retirement age.

Table 37 Characteristic of the differences in the amounts of old-age pensions paid out in December according to method of reduction

	Total	Not reduced	Reduced	
			permanently	temporarily
M(20) Men	7.2	7.0	5.3	6.2
Women	6.7	6.7	7.7	7.0
Total	9.5	9.7	10.3	11.5
M(50) Men	19.8	20.0	15.1	17.9
Women	19.2	18.9	20.6	19.5
Total	25.3	25.3	26.0	29.2
M(80) Men	38.4	38.4	31.4	36.9
Women	41.5	39.4	41.9	40.8
Total	48.8	46.5	46.7	51.6

Source: MLSA

The differentiation is clearly higher for the early old-age pensions of women than for the old-age pensions of women granted at the retirement age; however, for men it is clearly lower. Apparently, it is mostly men with lower incomes that go into early old-age retirement, whereas the group of women going into early

old-age retirement is not so homogenous as that of men. Another differentiating factor for women which causes a greater variation in the insured period relates to the number of children raised.

The increase in the basic amount of pensions as of 1 January 2005 which led to significant decreases in all these differentiation characteristics clearly had an impact on the **development of the differentiation of newly granted old-age pensions.**

Table 38 Basic characteristics for differentiating newly granted old-age pensions (solo) according to their amount

Year	2002	2003	2004	2005
M(20) Men	7.5	9.4	8.0	7.0
Women	11.7	11.5	12.1	10.4
Total	12.3	11.9	12.4	11.8
M(50) Men	20.0	22.1	22.5	21.3
Women	31.4	30.5	31.9	28.4
Total	31.1	32.3	31.9	30.0
M(80) Men	42.2	45.0	44.7	42.3
Women	57.4	58.6	59.5	55.8
Total	54.8	59.6	58.0	56.6

Source: MLSA

B.2.3. SICKNESS INSURANCE

Sickness insurance, like pension insurance, is based on the method of PAY-GO under which the financial balance is balanced out each year if the revenues from premiums less administrative costs are, in a given year, the same as expenditure on sickness insurance benefits. Therefore, the following equation should apply:

$$NC \times NDCY \times AA \times CR \times CC \times (1 - AC) = DB \times NDS + EOB \quad [5]$$

whereby NC marks the number of contributors, NDCY the number of days in a calendar year, AA the average daily assessment base for the payment of premiums, CR is the contribution rate, CC the contribution compliance, AC the administrative costs stated as a share of the total revenues, DB as the average daily sickness benefit, NDS the number of calendar days of sickness and EOB the expenditure for other sickness insurance benefits. The EOB is not outlined in greater detail given that the sickness insurance has the greatest share of expenditure

res for sickness benefits and this share 'p' does not differ greatly in the various years. Thus, equation no. 5 may be replaced by the following relationship:

$$NC \times NDCY \times AA \times CR \times CC (1 - AC) \times p = DB \times NDS \quad [6]$$

By adjusting equation no. 6, an equation for the basic indicators of sickness insurance may be obtained:

$$CR \times CC \times (1 - AC) \times p = DB/AA \times NDS/ (NDCY \times NC), \quad [7]$$

whereby DB/AA is the relation of sickness benefits to earnings to date (replacement ratio) and characterises the level of sickness benefits, and NDS/(NDCY x NC) is the sick leave rate. It ensues from equation no. 7 that the balancing of the financial balance does not depend directly on the number of insured persons, but rather of the contribution rate (modified by the contribution compliance and by administrative costs), the level of benefits and the sick leave rate.

Developments in the number of contributors (including the problems connected with their structure given the amount of the premiums), the development of the average assessment base for the collection of premiums and its relation to the development of the average wage in the national economy and the contribution compliance are discussed in Chapter B.2.1., which covers both pension and sickness insurance. Operational costs are assessed in Chapter B.2.5., which also covers both pension and sickness insurance.

In 2004 and 2005, revenues from sickness insurance were approximately CZK 6 billion higher than the expenditure for sickness benefits. In 2002 -2003, however, the revenues did not cover the expenditure and, as a result, the level of sickness benefits was reduced within the framework of public finance reform. This measure then had a positive impact on the balance of sickness insurance.

Table 39 Revenues and expenditure for sickness insurance
(Chapter 313 – Civil Sector)

Year	Revenues ¹ [CZK billions]	Expenditure [CZK billions]	Revenues - Expenditure [CZK billions]	Expenditure [% GDP]
1999	25.8	19.3	6.5	1.01
2000	27.3	27.2	0.1	1.37
2001	29.7	29.6	0.1	1.36
2002	31.6	32.6	-1.0	1.43
2003	33.3	34.3	-1.0	1.34
2004	35.7	29.6	6.1	1.07
2005	37.7	31.7	6.0	1.08

Source: MLSA

Note: ¹ Including fines, penalties and premium surcharges.

The number of employees insured under sickness insurance also has an impact on the growth of revenues from premiums. As of 2000, this number is gradually increasing and the number of voluntarily insured self-employed persons is decreasing.

Table 40 Developments in the number of persons insured under sickness insurance¹ (in thous.)

Year	Sickness insurance			Pension insurance
	Employees	Self-employed	Total	Self-employed
1999	4,117	322	4,439	610
2000	4,016	313	4,329	619
2001	4,066	304	4,370	628
2002	4,068	298	4,366	641
2003	4,020	295	4,315	646
2004	4,040	279	4,319	727
2005	4,085	252	4,337	740

Source: CSSA

Note: ¹ Average number in a year.

Expenditure on sickness insurance benefits in 2004 significantly fell (by 14 % in comparison to 2003) as a result of the lowering of both the benefits and the sick leave rate. The average daily amount of sickness benefits (expenditure on sickness benefits / the number of calendar days of sick leave) fell in 2004 in comparison to 2003 by CZK 5 and it increased by CZK 1 in 2005 in comparison to 2004. The sick leave rate fell in 2004 as compared to 2003 by almost one percentage point. Therefore, for every 100 employees there was one less employee missing from the work place due to sick leave. In 2005, the sick leave rate increased again in comparison to the previous year by 0.23 percentage point.

The greatest portion of expenditure on sickness insurance benefits is sickness benefits which in 2005 amounted to 83 % of all expenditures. The expenditure for maternity benefits comprised 14 % of the total expenditure and expenditure on financial support in caring for a family member amounted to 3 %. It may be stated that the ratio of sickness benefits to all benefits is gradually decreasing and, in contrast, the share of maternity benefits to all benefits has had a growing trend since 2000 due to increases in the birth rate.

The self-employed are not entitled to financial support in caring for a family member and to pregnancy and maternity compensation benefits.

Tabulka 41. Expenditure on social insurance benefits
(Chapter 313 – Civil Sector)

Year	Sickness benefits	Financial support for care of family members	Pregnancy and maternity compensation	Maternity benefits	Total
In absolute terms [CZK billions]					
1999	16.434	0.696	0.006	2.151	19.287
2000	23.653	0.785	0.008	2.760	27.205
2001	25.574	0.957	0.007	3.047	29.585
2002	28.222	0.893	0.007	3.487	32.609
2003	29.523	1.004	0.006	3.774	34.307
2004	24.704	0.730	0.005	4.123	29.562
2005	26.258	0.819	0.004	4.579	31.660
Relative [% of total]					
1999	85.21	3.61	0.03	11.15	100.00
2000	86.94	2.88	0.03	10.14	100.00
2001	86.44	3.23	0.02	10.30	100.00
2002	86.55	2.74	0.02	10.69	100.00
2003	86.06	2.93	0.02	11.00	100.00
2004	83.57	2.47	0.02	13.95	100.00
2005	82.94	2.59	0.01	14.46	100.00

Source: CSSA

Development in sickness is characterised by sick leave rate, by the average duration of a case of sick leave and the number of cases of sick leave per 100 persons insured under sickness insurance. The following equation applies to these indicators:

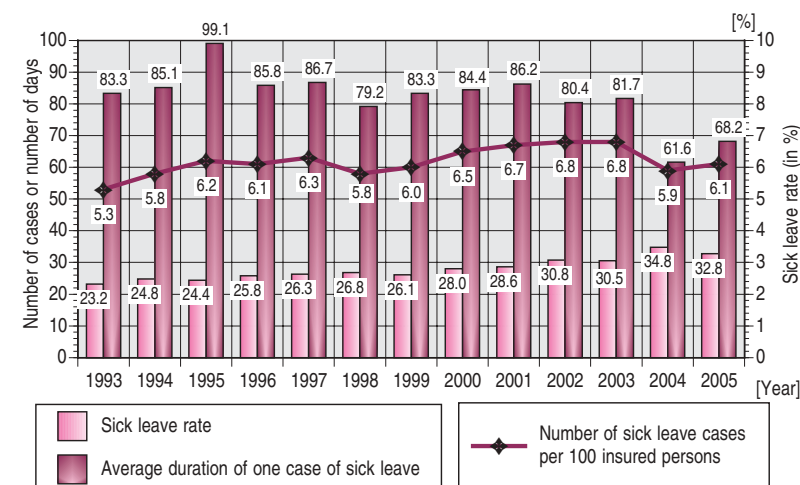
$$\text{Sick leave rate} = \frac{\text{Average duration of 1 case of sick leave} \times \text{number of cases of sick leave per 100 persons insured under sickness insurance}}{\text{number of days in the calendar year}} \quad [8]$$

Table 42 General indicators of sickness insurance

Year	Sick leave rate [%]	Average duration of one case of sick leave [days]	Number of cases of sick leave per 100 persons insured under sickness insurance
1999	5.95	26.1	83.3
2000	6.46	28.0	84.4
2001	6.75	28.6	86.2
2002	6.77	30.8	80.4
2003	6.81	30.5	81.7
2004	5.86	34.8	61.6
2005	6.13	32.8	68.2

Source: CSO

Graph 14 Developments in the general indicators of sickness insurance



Source: CSO

The lower sick leave rate in 2004–2005 as compared to the preceding period of 2001–2003 is a result of a lower number of respiratory diseases as well as the response of insured persons to the decrease in benefit amounts.

The amount of the sickness benefits depends on the earnings achieved and on the prescribed reduction limits of the daily assessment base for calculating sickness benefits, which from 2000 to 2002 were adjusted annually to the 1 January in accordance with developments in wages. With respect to the cost savings measures taken due to the floods in 2003 and in 2004 and 2005 within the framework of public finance reforms, the adjusting of the reduction limits was not undertaken. In 2006, the reduction limits were raised to CZK 510 and CZK 730 respectively.

As of 1 January 2004 the:

- decisive period for determining the assessment base for the amount of sickness benefits is the period of twelve calendar months preceding the calendar month in which the sick leave arose,
- from the first to fourteenth calendar day of sick leave the daily assessment base includes only 90 % of the amount up to the first reduction level. The daily assessment base is calculated fully up to the first reduction limit from the first day of maternity benefits and from the fifteenth day of sick leave for illness and injury. The daily assessment base is calculated only at 60 % of the amounts between the first and second reduction limit and the amounts above the second reduction limit are not taken into account,

- for the first three calendar days of sick leave, sickness benefits amount to 25 % of the daily assessment base and from the fourth day of sick leave they amount to 69 % of the daily assessment base.

Table 43 Developments in the reduction limits, the maximum daily assessment base and daily benefits

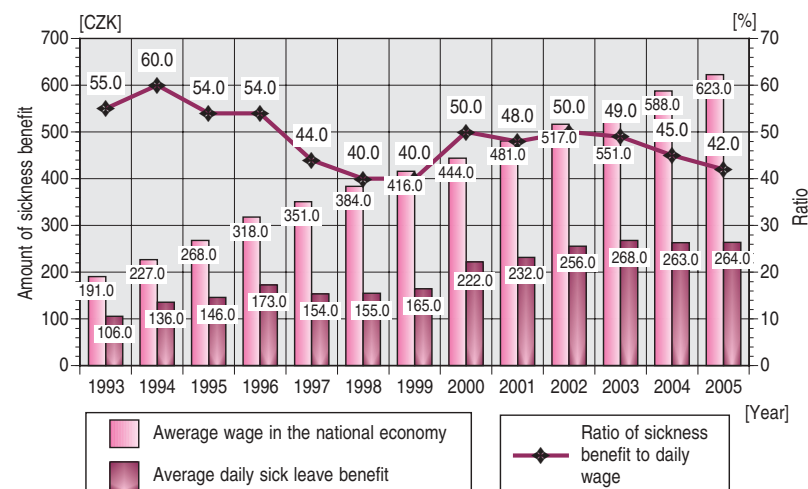
Year	Reduction limit		Maximum			
	First [CZK]	Second [CZK]	Assessment base [CZK]		Benefit ¹ [CZK]	
			1 st -14 th day SL	From 15 th day	4 th -14 th day SL	From 15 th day
Before 1. 10. 1999	270		270	270	186	186
1999	360	540	468	468	323	323
2000	400	590	514	514	355	355
2001	430	630	550	550	380	380
2002	480	690	606	606	419	419
2003	480	690	606	606	419	419
2004–2005	480 ²⁾	690	558	386	386	419
2006	510 ²⁾	730	591	624	418	443

Source: MLSA

Notes: ¹ The maximum daily benefit is determined by a rate of 69 %.

² For the 1st to the 14th day of sick leave (SL) only 90 % of the daily assessment base is calculated in the reduction limit.

Graph 15 Developments in the average daily sickness benefit, average daily wage and their ratio



Source: MLSA

The gradual growth in the average amounts of the benefits was due to the adjusting of reduction limits in 2002 and growth in wages. In 2003, adjusting was not carried out and thus the increase in benefits was influenced only by the growth in wages. The consequences of not raising the reduction limits also resulted in a decrease in the relation of the average daily sickness benefit to the average gross wage in the national economy (in 2002 it reached 50 % and then gradually fell to 42 % in 2005). The average daily benefit during the period 2003–2005 fell by CZK 4.

Table 44 Developments in average daily sickness benefits and the average wage in the national economy

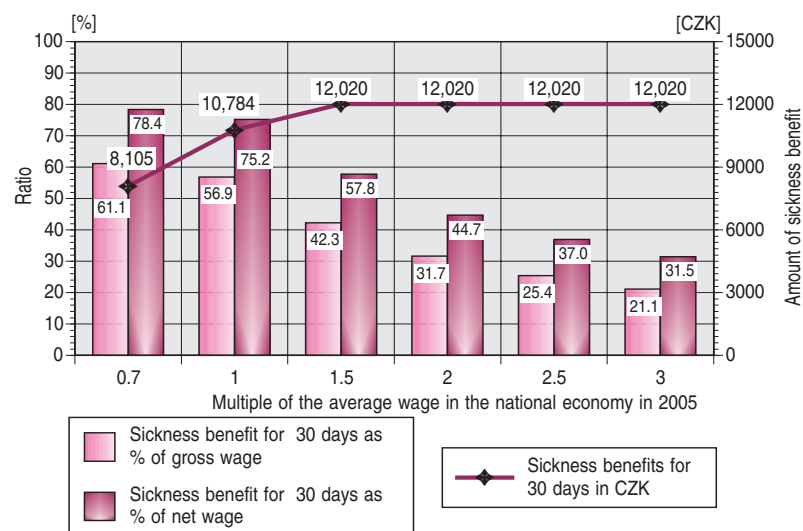
Year	Average gross wage in the national economy		Average daily sickness benefit	
	Monthly [CZK]	Daily [CZK]	[CZK]	[% of the average daily wage in the national economy]
1999	12,655	416	165	40
2000	13,490	444	222	50
2001	14,640	482	232	48
2002	15,711	517	256	50
2003	16,769	551	268	49
2004	17,882	588	263	45
2005	18,954	623	264	42

Source: MLSA

Note: The average daily wage is calculated as a ratio of the average monthly wage and the average number of days in a month.

A consequence of the effect of the reduction limits is that the replacement ratio decreases when wages increase (Graph 16). Therefore, there is a relatively large solidarity in the sickness insurance system between insured persons with high earnings and those with low earnings.

Graph 16 Amount of sickness benefit for 30 days in 2006 and its ratio to the gross and net wage for various wage amounts



Source: MLSA

B.2.4. FULFILMENT OF INTERNATIONAL CONVENTIONS

B.2.4.1. Pension insurance

In the field of social security, the Czech Republic is bound by both bilateral and multilateral conventions. Multilateral conventions include the International Labour Organization (ILO) Convention No. 102 on Social Security (Minimum Standards) of 1952, the ILO Convention No. 128 on Invalidity, Old-age and Survivors' Benefits of 1967 (both conventions came into effect for the Czech Republic in 1993) and the Council of Europe's European Code of Social Security (the "Code"). The ILO Convention No. 102 and the Code have less stringent provisions for the required level of benefits and were ratified by the Czech Republic for all types of pensions under pension insurance. The Czech Republic only ratified the provisions of the more stringent ILO Convention No. 128 that relate to old-age pensions.

The method of setting the level of benefits depends on the scope of persons protected. With respect to pension insurance, the Czech Republic acts in accordance with Article 16(b) of the Convention No. 128 as it fulfils the requirement that the scope of persons protected, which includes the prescribed classes of the population provided for under the Convention, represents at least 75 % of the whole economically active population.

• Old-age pension

The ILO Convention No. 102 requires that the **ratio of the newly granted old-age pension to wages** in the year before retirement amounts to 40 %. The ILO Convention No. 128 requires a ratio of 45 % for old-age pensions. The Conventions are fulfilled if the required "replacement ratio" (the benefit compensating for the previous earnings prior to an insured event) is obtained for newly granted pensions **for at least one given typical recipient**. A typical recipient is considered to be an insured person with thirty years of insurance and whose wages correspond to 1.25 times the average wage in the national economy or to the wage of a **skilled labourer** (a turner). The ILO accepts for the Czech Republic the setting of **the ratio to the net wage** as pensions in the Czech Republic are taxed from amounts exceeding CZK 198,000 annually (the 2006 tax period) and the state pays for the pensioner's health insurance.

Table 45 Fulfilment of the ILO Conventions for old-age pensions during 2004–2006

Year	Wage of a skilled labourer [CZK/month]		Old-age pensions		
	Gross	Net	Amount [CZK/month]	As % of wage of a skilled labourer Gross	Net
2004	17,682	13,826	6,060	34.3	43.8
2005	18,717	14,551	6,574	35.1	45.2
2006	19,507	15,103	6,971	35.7	46.2

Source: MLSA

The replacement ratio for newly granted old-age pensions amounted to 46.2 % in 2006, whereby the Czech Republic fulfils the requirements of the ILO Convention No. 128 and the Code.

Whereas up to 1999, the Czech Republic fulfilled the ILO Convention No. 128 even by setting the replacement ratio from 125 % of the average wage in the national economy, in following years the Convention was fulfilled only when using the average wage of the skilled labourer (which is lower) and in 2004 it was no longer possible to find any permissible criteria according to which the Czech Republic would fulfil the ratified Convention No. 128.

The increase of the first reduction limit for setting the calculable base to CZK 8,400 in 2005 was a sufficient measure for fulfilling the Convention No. 128. Subsequent increases of the first reduction limit in 2006 to CZK 9,100 meant a further increase in the replacement ratio of 1 percentage point above the required minimum level of the ratio of the pension to the previous wage.

- **Full disability pension and survivors' benefits**

The ILO Convention No. 102 and the Code require replacement ratio of **40 %** for these benefits. For newly granted full disability pensions and survivors' benefits the typical recipient is an employee with a wage corresponding to 1.25 times the average wage in the national economy or with the wage of a skilled labourer with two children. Therefore, child benefit payments for two children are also included in the calculations of the earnings of the employee and the pensioner. Like with old-age pensions, the ratio of the benefit to the net wage is decisive for evaluating the fulfilment of the convention.

Table 46 Fulfilment of the ILO Conventions for disability pensions in 2004-2006

Year	Wage of a skilled labourer [CZK/month]		Benefits for 2 children [CZK/month]	Disability pension [CZK/month]	Disability pension with benefits Amount [CZK/month]	As % of wage of a skilled labourer	
	Gross	Net				Gross	Net
	2004	17,682				14,481	1,319
2005	18,717	15,551	1,342	6,574	7,916	39.5	46.9
2006	19,507	15,883	1,193	6,971	8,164	39.4	47.8

Source: MLSA

Note: With benefits = including child benefits for two children (aged 7 and 12).

Table 47 Fulfilment of ILO Conventions for survivors' benefits in 2004-2006

Year	Wage of a skilled labourer [CZK/month]		Benefits for 2 children [CZK/month]	Widower and 2 orphan pensions [CZK/month]	Widower and 2 orphan pensions with benefits Amount [CZK/month]	As % of wage of a skilled labourer	
	Gross	Net				Gross	Net
	2004	17,682				14,481	1,319
2005	18,717	15,551	1,342	10,927	12,269	61.2	72.6
2006	19,507	15,883	1,193	11,563	12,756	61.6	74.7

Source: MLSA

Note: With benefits = including child benefits for two children (aged 7 and 12).

During the period of 2004-2006, the Czech Republic fulfilled the requirements of the ratified Convention with respect to full disability pensions and survivors' pensions. The required minimum level (40%) of newly granted full disability pensions in 2004-2006 was met in the case of net wages of a skilled labourer and surpassed the required level by approximately 7.8 percentage points. The Conventi-

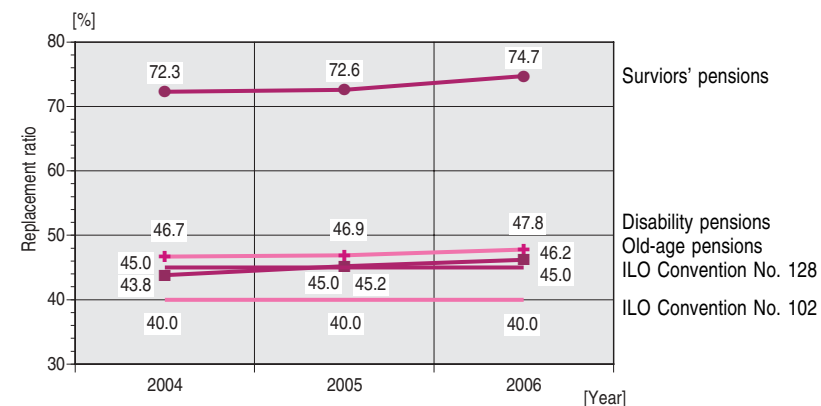
on requires a replacement ratio of 40 % for survivors' pensions. The level of the survivors' pensions granted greatly exceeds the required level both in terms of gross wages and of net wages; the replacement ratio reaches 60–74.7 %.

- **Conclusions**

In conclusion, it may be stated that the replacement ratio, which is the criteria for the fulfilment of the conventions on minimum level of the benefits was the lowest in 2004 when the Czech Republic stopped fulfilling the criteria of the ILO Convention No. 128 for old-age pensions. The increase of the first reduction limit and of the basic amount of pensions in 2005 and 2006 enabled the replacement ratio to be increased in order for the Czech Republic to fulfil the given criteria.

The Czech Republic fulfils the criteria of ILO Convention No. 102 and the Code, which are less stringent. The reduction limits for the calculation of pensions should not be increased by an amount lesser than that which corresponds to the growth in wages as otherwise the Czech Republic could stop fulfilling the Conventions with respect to old-age pensions.

Graph 17 Development of the criteria for fulfilling the conventions for the minimum level of pensions



Source: MLSA

The replacement ratio for old-age and disability pensions is slightly above the level required by the ILO Conventions No. 102 and 128, whereas the replacement ratio for survivors' pensions and for sickness insurance benefits (Graph 18) greatly exceeds the amount required under the ILO Convention Nos. 102 and 130.

B.2.4.2. Sickness insurance

Sickness benefits are provided for under the ILO Conventions No. 102 and No. 130 as well as the Code. The ILO Convention No. 102 and the Code require that the ratio of sickness benefits to previous earnings of a typical recipient reaches the value of 45 %. The ILO Convention No. 130 requires a replacement ratio of 60 % to previous earnings. Table 48 demonstrates that the Czech Republic fulfils these requirements with a great reserve.

The method of setting the levels of the benefits depends on the scope of persons protected. With respect to sickness insurance, the Czech Republic acts in accordance with Article 19(b) of the Convention No. 130 as it fulfils the requirement that the scope of persons protected include at least 75 % of the whole economically active population.

Table 48 Fulfilment of the ILO Conventions for sickness benefits in 2004-2006

Year	Wage of a skilled labourer [CZK/month]		Benefits for 2 children [CZK/month]	Sickness benefits [CZK/month]	Sickness with benefits		
	Gross	Net			Amount [CZK/month]	As % of wage of a skilled labourer ¹	
						Gross	Net
2004	17,682	14,526	1,319	10,191	11,510	60.6	72.6
2005	18,717	15,551	1,342	10,489	11,831	59.0	70.0
2006	19,507	15,883	1,193	11,025	12,218	59.0	71.6

Source: MLSA

Note: With benefits = including child benefits for two children (aged 7 and 12).

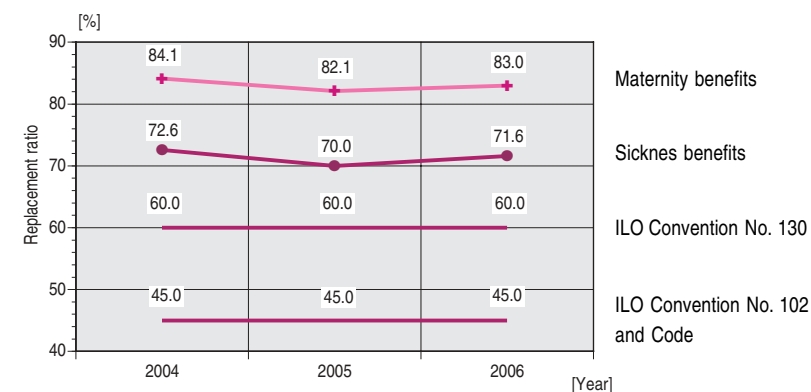
The ILO Convention No. 102 and the Code require that the ratio of the amount of maternity benefits and previous earnings of a typical recipient amount to 45 %, which the Czech Republic greatly exceeds.

Table 49. Fulfilment of ILO Conventions for maternity benefits in 2004-2006

Year	Wage of a skilled labourer [CZK/month]		Maternity benefits Amount [CZK/month]	As % of wage of a skilled labourer	
	Gross	Net		Gross	Net
2005	18,717	14,171	11,640	62.2	82.1
2006	19,507	14,743	12,240	62.7	83.0

Source: MLSA

Graph 18 Developments in the criteria for fulfilling the conventions on the minimum standards of sickness benefits



Source: MLSA

The decrease in the replacement ratio of sickness benefits was caused for the most part by no increases to the reduction limits for setting the daily assessment base for the calculation of benefits during 2003–2005.

B.2.5. OPERATIONAL EXPENSES

Operational expenses are included in the overall balance of the social security system. The operational expenses of CSSA are very low in comparison with other similar institutions. The budgetary resources for operational expenses greatly complicate fulfilling the current needs for the basic operation of the authority.

Table 50 Operational expenses (CZK millions)

	2000	2001	2002	2003	2004	2005
Total operational expenses	3,402	3,878	4,286	4,700	5,290	5,580
Total investments	442	339	337	544	924	828
Of which: building and machinery	280	213	265	500	634	442
computer technology	162	126	72	44	290	386
Total administrative costs	2,960	3,539	3,949	4,156	4,366	4,752
Of which: wages and other	1,153	1,290	1,466	1,601	1,689	1,875
personnel expenses						
premiums and the Cultural	424	477	538	592	625	694
and Social Needs Fund						
postage	530	523	489	578	582	562
net material expenditure	853	1249	1,456	1,385	1,470	1,621
Operating costs ¹ [in %]	1.58	1.65	1.71	1.78	1.85	1.85
Performance indicator ² [in %]	0.80	0.84	0.87	0.90	0.97	0.97

Source: CSSA

Notes: ¹ Ratio of the total operating expenditure (including investment) to total revenues (in %).

² Ratio of the total operating expenditure (including investment) to the sum of total income and benefit expenditure.

In the year-on-year comparison of 2005 to 2004, operational expenditure increased by 5.5 % (of which investment decreased by 10 %). In addition, in contrast to 2003, operational expenditure grew by 12.6 % (of which investment increased by 70 %) in 2004. Expenditure on wages, premiums, the Cultural and Social Needs Fund and postage are prescribed to the CSSA as binding budget indicators. Therefore, the indicator of net material expenditure reflects the possibilities of financing the common operating needs of the CSSA for ensuring the carrying out of social security. Its amount was inadequate at a time of when there are greater demands being placed on the CSSA due to accession to the EU and the need to improve the administration of the pensions and sickness insurance systems as well as the creation of a modern, efficient and effective information system.

The CSSA performs extensive tasks both in the field of state income (representing approximately 38 % of revenues of the state budget) and in the field of expenditure (approximately 31 % of state budget expenditures). In 2005, its performance indicator amounted to 0.97 %. Such a low ratio of operating expenditure to tasks performed has no equivalent amongst similar authorities in the Czech Republic. The share of total operating expenditure (including investments) to total income in the last two years reached 1.85 %. This indicator was higher in 1996 (1.88 %) and in 1999 (1.91 %).

PART C SOCIAL INSURANCE PROJECTIONS

C.1 PROJECTIONS OF PARAMETERS INFLUENCING SOCIAL INSURANCE DEVELOPMENT

C.1.1. DEVELOPMENT OF BASIC MACROECONOMIC INDICATORS¹⁷

For determining the macroeconomic scenario the method selected is one which is commonly used both in OECD projections as well as by the European Union's Economic Policy Committee's working group on ageing population. It involves the expert estimate of several basic parameters (Table 51) that are used to predict macroeconomic events based on theoretically justified relations. The macroeconomic model uses the four parameters outlined in the left side of the table.

Table 51 List of parameters

Participation rate	Real rate of return for 10-year government bonds in the EU-12
Unemployment rate	Real rate of return for capital markets in the EU-12
Productivity growth rate in the EU-12	Inflation rate in the EU-12
Speed of convergence of the CR	Inflation rate in the CR
	Administrative costs of pension funds

Source: Final Report of the Executive Team

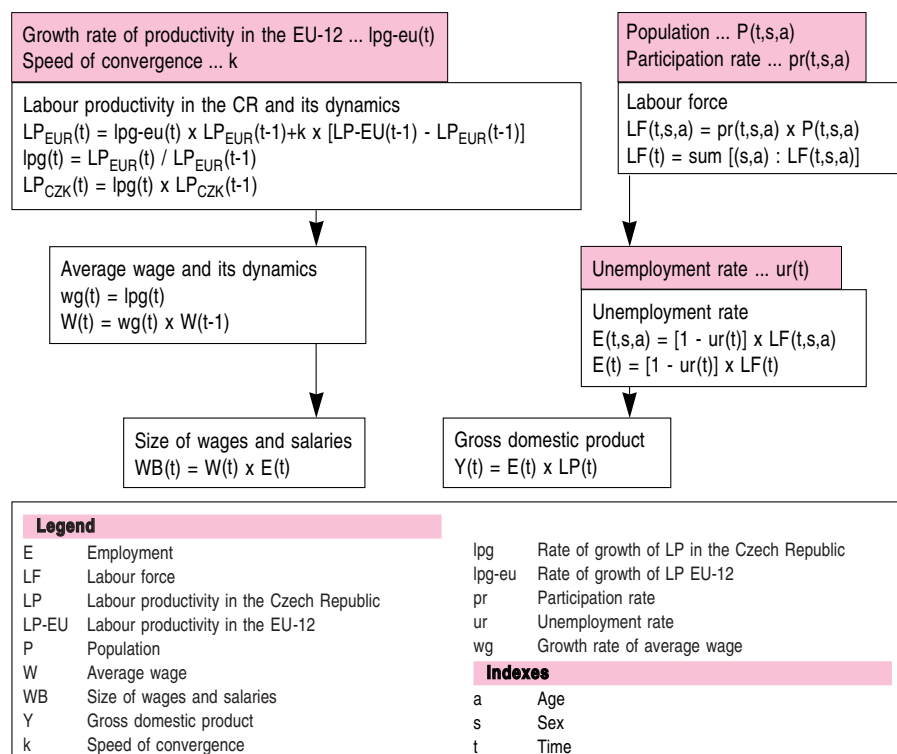
The diagram explaining the logical relationships between the individual macroeconomic events is outlined in the next Table (Table 52). The basic indicators are labour productivity in the Czech Republic (i.e. the gross domestic product per employee) and the size of the labour force (i.e. the number of persons who are working or who are actively looking for employment). In determining the labour productivity in the Czech Republic it is expected that a gradual convergence with the level of productivity in developed countries will occur. The average of the countries within today's Euro zone (EU-12) can serve as a basis for comparison basis (i.e. level where convergence is reached).

¹⁷ The method used is the same as that which was used for the work of the Executive Team.

The growth in the labour productivity rate was derived based on the assumption of a convergence with the level of labour productivity in the EU-12. The basis for the labour productivity in the Czech Republic is, in relation to the EU-12, set after recalculating the data from Czech crowns into euros using the purchase power parity.

The number of employed persons that participate in the creation of value added, i.e. the gross domestic product, was derived from assumptions on the unemployment rate and the size of the labour force (the method of projecting the work force is further described below). The gross domestic product was obtained by summing the number of employed persons and the labour productivity per employee. Such a method implies a constant proportion of the manufacturing factor of labour on value added from which also ensues that the growth rate of the average wage must correspond to the growth rate of labour productivity.

Table 52 Diagram of the macroeconomic model



Source: Final Report of the Executive Team

Table 53 demonstrates that the average growth rate of real GDP for the whole projected period amounts to 1.9 %. The growth of the real GDP is limited after 2020 by the decrease in the employment. With the retirement age fixed at 63, after 2020 there is a rapid decrease in the number of people who are of an economically active age as a result of negative demographic developments. An absolute decrease of the number of employed persons (on average by 0.3 % per year) is in this period accompanied by a decrease in the population as a result of which the employment rate falls slower than the number of employed and the growth of GDP per capita thus exceeds the growth of GDP by 0.1 % during the whole projected period.

Table 53 Development of basic macroeconomic indicators

		2005- -2010	2010- -2020	2020- -2030	2030- -2040	2040- -2050	2050- -2060	2060- -2070	2070- -2080	2080- -2090	2090- -2100
Economic level											
GDP, constant prices	growth in %	3.6	2.8	2.2	1.6	1.4	1.6	1.7	1.6	1.7	1.8
GDP per capita	growth in %	3.5	2.7	2.2	1.7	1.6	1.8	2.0	1.8	1.8	1.7
Labour productivity	growth in %	3.2	2.8	2.5	2.3	2.1	2.0	1.9	1.9	1.9	1.8
Labour productivity	EU-12 = 100	66.1	73.2	80.2	85.3	89.3	91.9	94.0	95.6	96.7	97.6
Labour market											
Employment	growth in %	0.5	0.0	-0.3	-0.7	-0.7	-0.4	-0.2	-0.2	-0.1	-0.1
Participation rate (15-64)	%	76.7	78.5	78.7	77.3	77.1	77.1	77.3	77.2	77.1	77.2
Unemployment rate	%	7.9	7.2	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
Average real wage	growth in %	2.9	2.8	2.5	2.3	2.1	2.0	1.9	1.9	1.9	1.8
Prices											
Inflation rate	%	2.8	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Other assumptions											
Real rate of return - obligations	% p.a.	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Real rate of return - shares	% p.a.	5.5	5.5	5.5	5.5	5.5	5.5	5.5	5.5	5.5	5.5
Administrative costs	% aktiv	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0

Source: Final Report of the Executive Team

C.1.2. DEMOGRAPHIC DEVELOPMENT

All projections of the social insurance system are founded on the demographic forecasts drawn up by the Faculty of Natural Sciences of Charles University¹⁸ that have a horizon of 2065, which was extended by a demographic projection for

¹⁸ The projections of the Faculty of Natural Sciences were completed in 2003 and are based on the results of the population census carried out in 2001. They were selected as they have the longest horizon, which is extremely important for pension system projections.

the period 2066–2100. In contrast to the preceding report, the horizons of all projections was extended by an additional 35 years, which enables the demonstration of developments after overcoming the peak of the demographic shock.

Table 54 Basic characteristics of future demographic developments

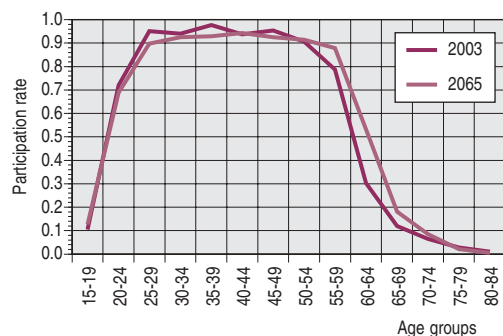
		2010	2020	2030	2040	2050	2060	2070	2080	2090	2100
Total fertility rate		1.34	1.51	1.57	1.61	1.64	1.67	1.68	1.7	1.72	1.73
Life expectancy at birth											
Men	years	74.1	76.5	78.7	80.4	82	83.4	84.6	85.8	86.9	88.0
Women	years	80.3	82.4	84	85.4	86.7	87.6	88.8	89.7	90.6	91.4
Migration	thous. of persons	20.0	24.9	25.9	25.7	25.4	24.6	25.2	25.4	25.5	25.3

Source: B. Burcin and T. Kučera, *Prognóza populačního vývoje České republiky na období 2003–2065, Projekce vývoje obyvatelstva České republiky na období 2066–2150.*

C.1.3. DEVELOPMENTS IN THE PARTICIPATION RATE

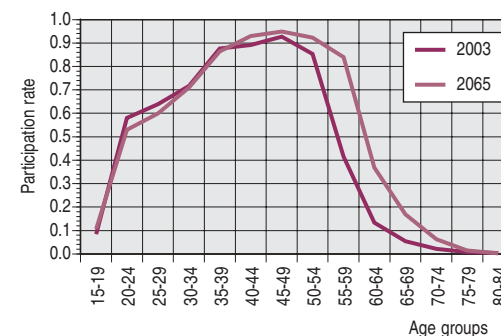
The dynamic method was used for estimating the future rate of participation, which reflects the different behaviours of the various generations as reflected in the decreasing participation of lower age groups and the growing participation of higher age groups. The decrease in the rate of participation of the lower age groups is due to greater participation of the younger generations in the educational process, especially university. In contrast, the positive cohort effect is reflected in the higher age groups (women older than 40 and men older than 50) where the younger generations of men and women participate more intensely in the labour force in contrast with the older generations due to amongst other their higher level of education.

Graph 19 Participation rate by age groups – men



Source: Final report of the Executive Team

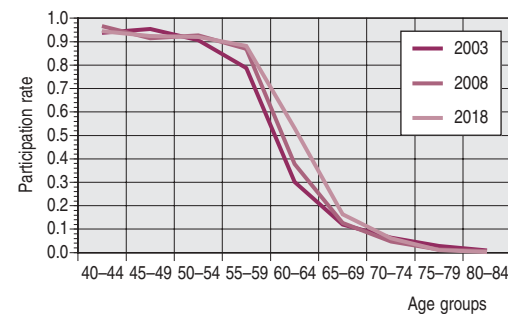
Graph 20 Participation rate by age groups – women



Source: Final Report of the Executive Team

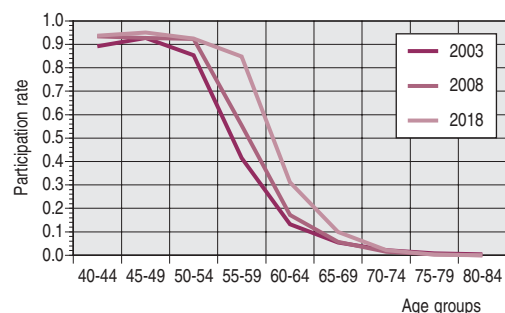
A separate question is the method of reflecting the increases of the retirement age into the participation rate of persons close to retirement age. Generally, shifts in retirement ages have a significant impact on the rate of participation. The method of reflecting the increases in the retirement age involves adjustments to the projections of probable entries into the labour force. The shift in the retirement age corresponds here to the decision to leave the labour market later.

Graph 21 Changes in the participation rate due to increases in the retirement age – men



Source: Final Report of the Executive Team

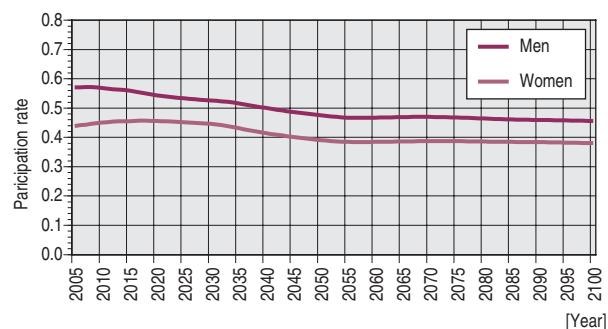
Graph 22 Changes in the participation rate to increases in the retirement age – women



Source: Final Report of the Executive Team

The total participation rate in the 15+ age group decreases for men about until the middle of this century and thereafter it stays relatively stable. With respect to women, it appears to increase up to 2020 and then declines until about the middle of this century, which is then, similar to men, followed by a period where the rate remains relatively stable. The development of the rate over time is significantly impacted by changes to the retirement age and this situation also applies to the retirement age prescribed by current legislation (Graph 24).

Graph 23 Total participation rate in the 15+ age group



Source: Final Report of the Executive Team

C.2. PENSION INSURANCE¹⁹

C.2.1. PROJECTIONS OF BASIC INDICATORS

The following number amongst the basic indicators of the pension insurance system:

- developments in the number of contributors and pensioners,
- developments in the relation of the average pension and the average wage,
- developments in income, expenditure, balances and cumulative balances.

In contrast to the last published report, no measures were taken in the pension system that would have a significant impact on the projections. At the same time, no revisions or updates were made of the demographic prognoses. Given the above, no circumstances occurred that would impact the trends stated in the projections published in the last report. At the same time, within the framework of the Executive Team, detailed analyses were made in 2005 of the current system including the effects of certain parametrical changes.²⁰ As such, the following text is only a brief summary of the already mentioned projections and the conclusions ensuing therefrom.

C.2.1.1. Developments in the number of contributors and pensioners

The number of contributors in a given year is determined by the demographic structure of the population, the participation rates in the individual age groups (or the average participation rate of the population) and, of course, the unemployment rate in a given year. The unemployment rate is more important from a short-term perspective as the effects of the demographic development have a greater impact over the long term.

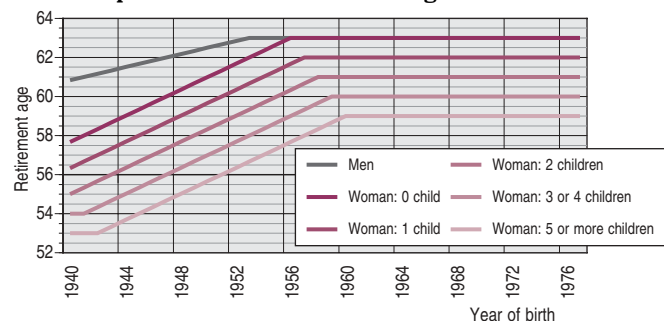
The number of pensioners is given foremost by, depending on the demographic structure, the retirement age (Graph 24), which determines the potential number of old-age pensioners. Other factors, such as the rate of disability (see Chapter C.2.4. for details) do not have such a significant impact when there is a relatively slow growth of the retirement age.²¹

¹⁹ All calculations are based on the status as at the end of 2003 and reflect adjustments of the reduction levels and the valorizations of pensions in 2004, 2005 and 2006.

²⁰ All of the analyses may be found at: www.reformaduchodu.cz and www.mpsv.cz.

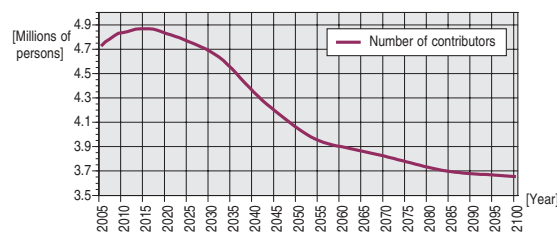
²¹ In the event of a more marked growth in the retirement age, the models show a greater impact also on the number pensions other than old-age.

Graph 24 Developments in the retirement age



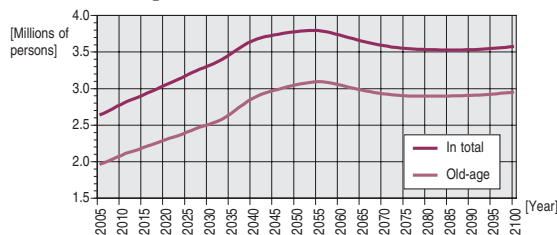
Source: MLSA

Graph 25 Number of contributors



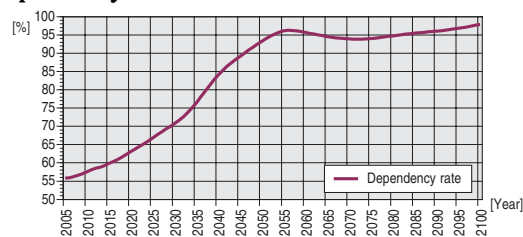
Source: MLSA

Graph 26 Number of pensioners



Source: MLSA

Graph 27 Dependency rate



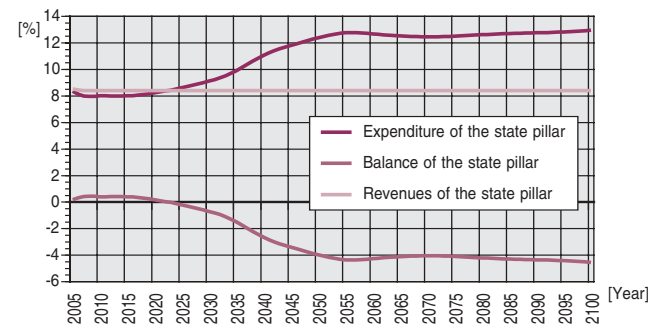
Source: MLSA

Decisive for the future balancing of the pension insurance system (PAYGO financing) is not the actual development of the number of contributors or pensioners, but rather the development of the 'dependency rate,' which is the proportion of the number of pensioners to the number of contributors.

C.2.1.2. Developments in revenues, expenditure and the total replacement ratio²²

The expected change in the demographic situation is reflected in the developments of the expenditure and balances of the pension system to which, under the current setting of the various parameters, the pension system essentially does not react. The system is getting into permanent deficits which will gradually exceed 4 % of the GDP. After 2020, following great growth, expenditure will stabilise at a level just below 13 % of GDP. Even though this system is not financially sustainable in the long-run (Graph 30), it is to a great extent dependent on the valorization of pensions only at a minimum level provided for under the law. Failure to fulfil this condition will result in a significant growth in total expenditure.

Graph 28 Developments in revenues, expenditure and balances of the pension system (% of GDP)²³

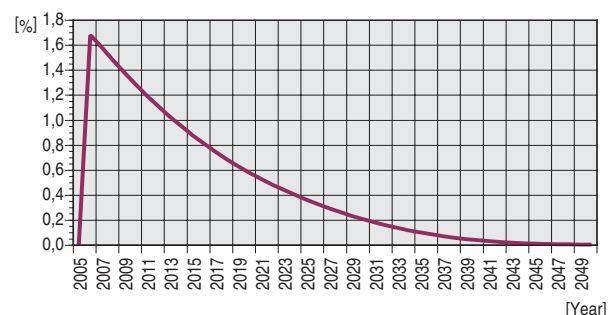


Source: MLSA

²² The total replacement ratio is a ratio of the average old-age pension to the average wage.

²³ Under the assumption that the valorization of paid out pensions is carried out only at the minimum level provided for under law.

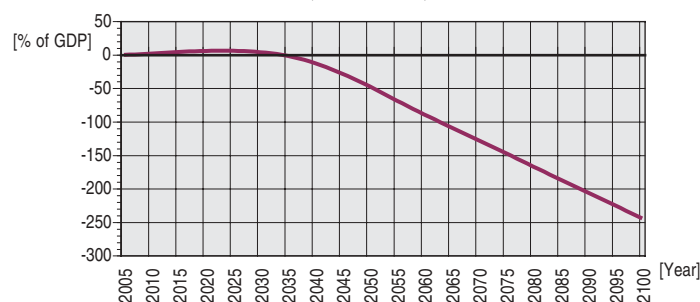
Graph 29 Impact of a higher than minimum valorization carried out in 2006 on pension system expenditure (in %) ²⁴



Source: MLSA

In this respect, it does not have to involve a valorization that is in the long-term higher than minimum, but rather an increase in the valorization in one year suffices (as was carried out e.g. in 2006). A higher valorization not only affects the expenditure in the given year in which it is carried out, but it also affects subsequent periods as it creates a higher base for subsequent valorizations. Therefore, the valorization carried out in 2006 not only increased the expenditure for 2006 by approximately CZK 4.3 billion, but it will also be reflected in the pension system for several more years (Graph 29) and will result in additional expenses amounting to approximately CZK 93 billion. Graph 29 thus clearly illustrates the substantial staying power of changes made to the pension system.

Graph 30 Cumulative balance (% of GDP) ²⁵



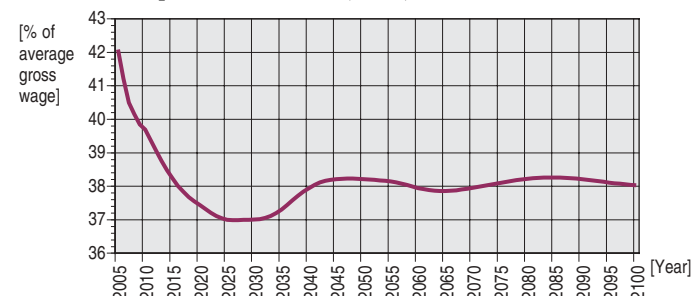
Source: MLSA

²⁴ Under minimum valorization, pensions would have been increased by 3.1 %. However, the actual amount of valorization was 4.9 %.

²⁵ It is expected that the accumulation of surpluses will be placed on the capital market in a portfolio of 50 % shares and 50 % bonds, i.e. with respective returns, and that the cre-

The total replacement ratio for about the next 20 years will reflect a growth in the old-age pensions to the total number of old-age pensions paid out. The increase in the share of early old-age (i.e. lower) pensions will lead to a decrease in the total replacement ratio.

Graph 31 Total replacement ratio (in %) ²⁶



Source: MLSA

C.2.2. EVALUATION OF DEVELOPMENTS IN KEY INDICATORS

The expected ageing of the Czech population characterised by a falling mortality rate and supported by a low birth rate will create mounting pressure on the pension system. In the projected period, two large generations (the post-war and the 1970s generation) will go into retirement. The post war-generation, followed by the large 1970s generation, does not appear to be such a problem for the pension system as the large 1970s generation for which it will be necessary to create financial reserves in order to finance their pensions or where necessarily an increase in expenditure on pensions in relation to the GDP will occur. The shift of this generation from being economically active to retirement will lead to a significant rise in expenditure for pensions in relation to GDP, which may be seen between the years of 2030 to 2050.

After 2060, it will become stabilized whereby there a deficit of approximately 4.5 % of the GDP will occur in the system each year. Changes to the system should therefore aim to eliminate such expected deficits.

The average level of old-age pensions in relation to the average wage should in the closest period decrease, whereas it should reach the lowest level around 2030. This decrease is seen despite an expected stable relative level for newly granted pensions. The main reason for such a decrease is the increasing share of reduced ear-

-ated debt will be covered by government bonds, i.e. with respective interests. It is necessary to note the fact that this is a projection which does not reflect secondary effects, e.g. the impact of a debt of approx. one hundred percent GDP on interest rates for government bonds. The estimated values of the rates of return are listed in Table 53.

ly (i.e. lower) pensions to the total number of old-age pensions. To a limited extent, the expected valorizations at the minimum level provided for under the law (i.e. 100 % growth in prices and 1/3 growth of real wages) also has a limited impact. After 2030, a slight increase in this relation should occur and should stabilize at a level around 38 %. Given that the expected decrease of the above-mentioned relation is primarily caused by the conduct of individuals (preference for early retirements), any future changes should not aim to eliminate it.

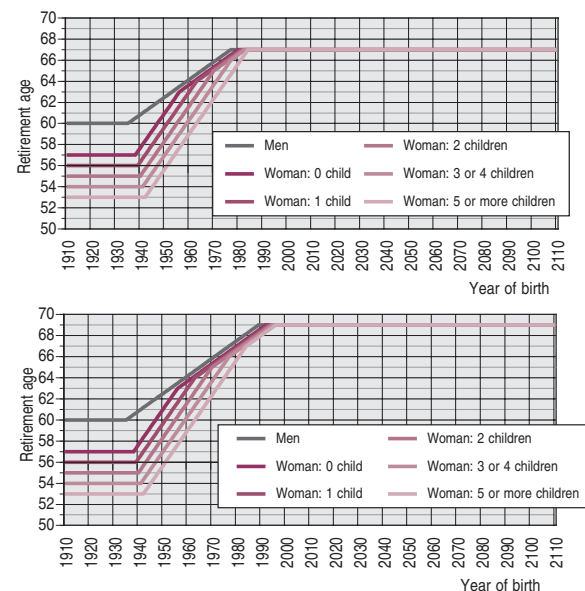
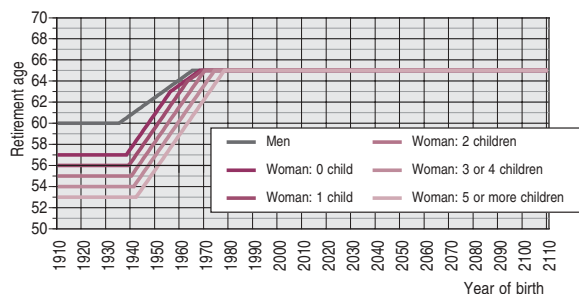
C.2.3. SENSITIVITY OF BASIC INDICATORS OF THE PENSION INSURANCE SYSTEM ON CERTAIN PARAMETERS

Within the framework of the Executive Team, relatively extensive analysis of the effects of various parametrical changes on the development of the pension system was carried out. These analyses related to adjustments to the retirement age, the method of valorizing paid out pensions and, last but not least, also possible changes to the actual formula for the calculation of pensions. The analyses carried out related both to effects on financial stability (basic indicators) as well as the possible effects on the various income individuals. The complete texts of the above-mentioned analyses may be found at: www.reformaduchodu.cz. The following text will essentially focus on the impact on certain basic indicators and will be based on the conclusions of the analysis.

C.2.3.1. Additional increases in the retirement age

In order to demonstrate its sensitivity, apart from the scenario of maintaining the current status (the basic variant), three scenarios of further increases to the retirement age above those provided for under exiting legislation in force were selected. These include increases at the current rate to 65, 67 and 69 years. The development of the retirement age in these scenarios may be seen in the following graphs.

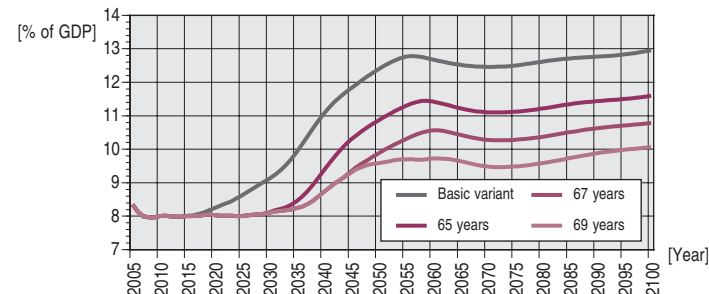
Graph 32 Process of increasing the retirement age to 65, 67 and 69 years



Source: MLSA

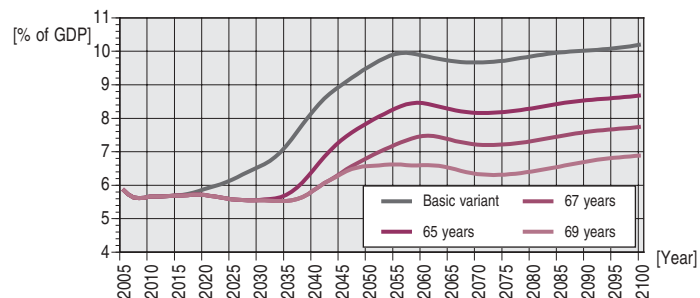
Of the basic indicators, expenditure on pensions (as a proportion of the GDP) is the most sensitive to the retirement age. In the basic scenario, the expenditure grows in the long-term to 13 % of GDP. Increasing the retirement age to 65 (from 63 in the basic scenario) reduces expenditure in the pension system in the long-term to 11.5% of GDP. Additional increases up to the age of 67 would result in a long-term stabilisation of expenditure on pensions at a level of about 10.5 % of GDP. If such increases were to continue up to an age of 69, then expenditure on pensions would, in the long-term, be lower than 10 % of GDP.

Graph 33 Expenditure on pensions (% of GDP)



Source: MLSA

Graph 34 Expenditure on old-age pensions (% of GDP)

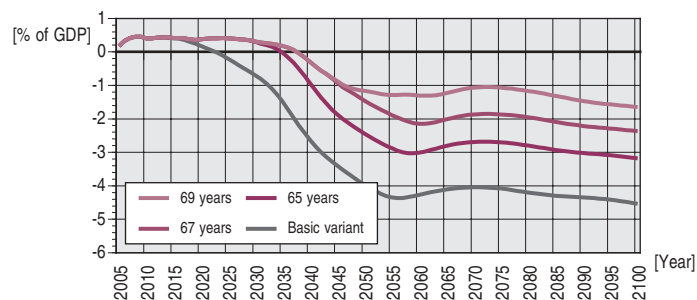


Source: MLSA

In the scenarios with higher retirement ages, the growth of expenditure other than old-age pensions is also seen (especially in disability pensions). These effects are described in Chapter C.2.4.

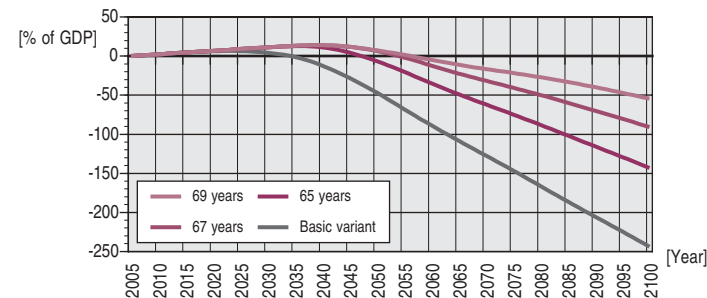
Taking into account the projected stability of revenues of the pension system in relation to the GDP (which ensues from the structure of the macroeconomic scenario), the development of the expenditure is key for balancing the system. In comparison with the basic scenario, all scenarios with an increase in the retirement age lead to better results in the balance. Increasing the retirement age delays the moment when the surpluses of the system turn into deficits.

Graph 35 Balance of the pension system (% of GDP)



Source: MLSA

Graph 36 Cumulative balance (% of GDP)

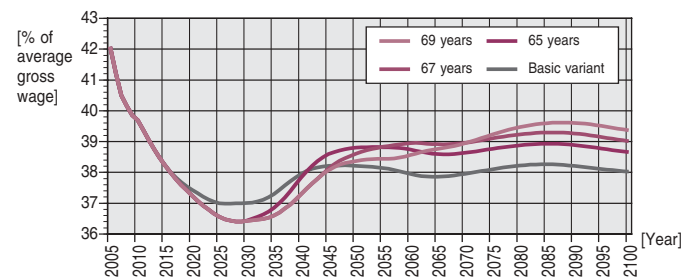


Source: MLSA

The positive effect of increasing the retirement age is most clearly seen in the cumulative balance of the system, where with a gradual increase of up to 69 years, the cumulative debt is almost 200 % of GDP lower than in the basic scenario, it that reaches a still significant 50 % of GDP.

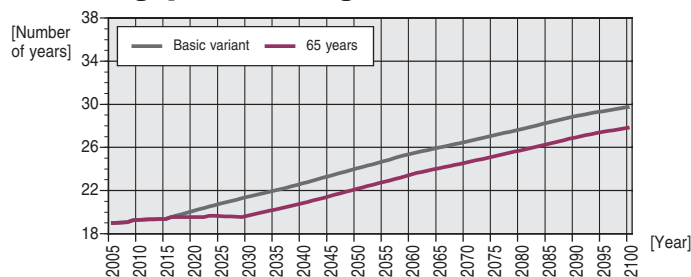
The scenarios working with the different retirement ages do not vary greatly in terms of the total replacement ratio. Partial variations reflect the various growth rates of the natural replenishing of pensions which, in contrast to the basic scenario, are affected by the process of gradual increases in the retirement age. A higher retirement age defers the entry of new pensioners into the system which, with their higher pensions granted, raises the total replacement ratio. In the long-term, after the end of increases to the retirement age, the replacement ratio will be slightly higher than in the basic scenario as pensions are paid out for a shorter period of time, i.e. relatively in relation to the average wage their level decreases less by valorization (lower than wages).

Graph 37 Total replacement ratio (in %)



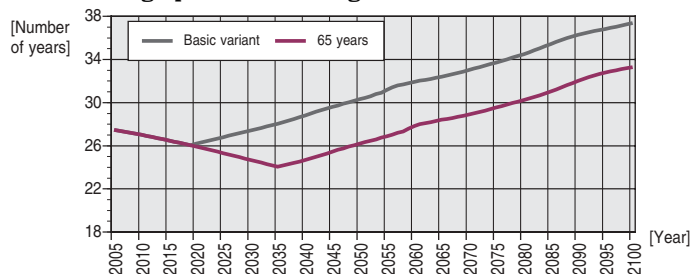
Source: MLSA

Graph 38 Average pension drawing time – men



Source: MLSA

Graph 39 Average pension drawing time – women



Source: MLSA

Table 55 Life expectancy

		2005	2010	2020	2030	2040	2050	2060	2070	2080	2090	2100
Life expectancy – men												
at 60 years	years	20.2	21.1	22.7	24.1	25.5	27.0	28.3	29.5	30.7	31.8	32.7
at 65 years	years	17.0	17.7	19.1	20.2	21.5	22.8	24.1	25.2	26.3	27.4	28.3
Life expectancy – women												
at 60 years	years	25.0	25.8	27.2	28.4	29.9	31.4	32.9	34.1	35.6	37.3	38.4
at 65 years	years	20.9	21.6	22.9	24.1	25.5	26.9	28.4	29.5	31.0	32.8	33.9

Source: MLSA

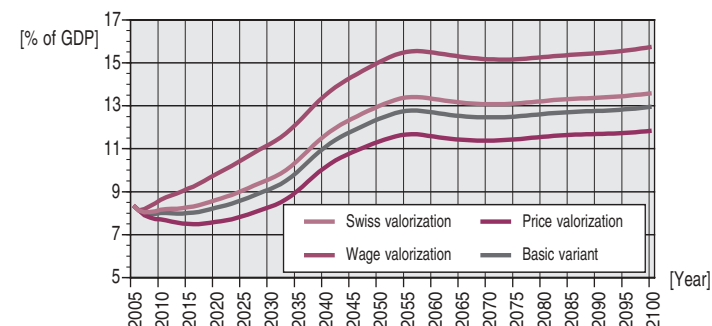
C.2.3.2. Method of valorizing pensions

In order to demonstrate the sensitivity 4 scenarios were chosen: valorization only according to growth in price (CPI), according to the growth in prices and 1/3 of the growth in real wages (the minimal valorization according to the law – i.e. the basic variant), ‘Swiss valorization’ (i.e. 1/2 the growth in prices and 1/2 the growth in nominal wages) and full wage valorization.

Changes in the valorization scheme affect the expenditure of the pension sys-

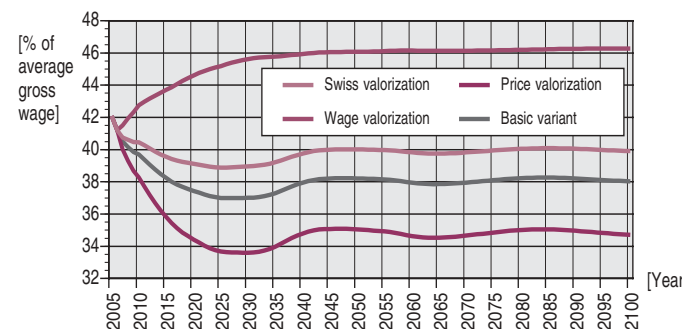
tem only through its effects on the relative amounts of the pensions paid out. No changes occur to the number of pensions granted or paid out, nor to the amount and replacement ratio of newly granted pensions. Differences in the amounts of expenditures in the individual valorization scenarios may be fully explained by comparing them with the total replacement ratio.

Graph 40 Expenditure on pensions (% of GDP)



Source: MLSA

Graph 41 Total replacement ratio (in %)



Source: MLSA

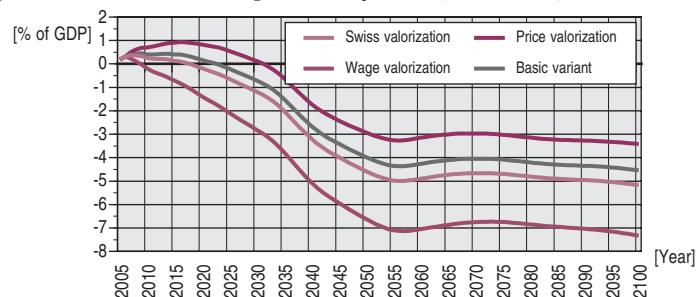
Expenditure for the pension system is the lowest in the least generous valorization variant, which is the price valorization. In contrast, wage valorization and Swiss valorization (in the given rates of price and wage growth) ensure a greater growth of pensions paid out than the basic scenario.

With the wage valorization the balance of the pension system shifts to a deficit already in 2009 and from thereon the debt of the system cumulates, which at the end of the projected period may be at almost 450 % GDP. The high debt of the system is a direct result of high long-term deficits which amount to about

7 % of GDP annually. Similarly, under the Swiss valorization the temporary cushion created from the restructuralisation of the insurance rate in 2004 is drawn out sooner than in the basic scenario. From 2017, the pension system will have permanent deficits and in the long-run their amounts will settle at a rate of around 5 % of GDP. Surpluses of the pension system will under this scenario be used up in 2026, when the cumulative balance of the system will go into red numbers. At the end of 2100, the debt of the pension system will reach 290 % of GDP.

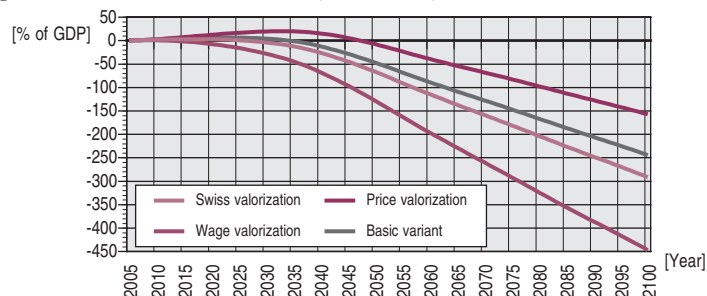
Price valorization defers up to 2031 the moment when the pension system will go into deficit. Up to this year, the pension system will have surpluses of up to 1 % of GDP. However, even this scenario has, in the long-term, large deficits which exceed 3 % of GDP. Not even limiting the growth of pensions in applying price valorization is capable of preventing the rapid growth of expenditures after 2030. Up to 2030 the cumulated surpluses would amount to 20 % of GDP, which would permit the financing of the deficits of the pension system up to 2047. However, at the end of the horizon of the projected period there would be a projected debt reaching almost 160 % of GDP.

Graph 42 Balance of the pension system (% of GDP)



Source: MLSA

Graph 43 Cumulative balance (% of GDP)



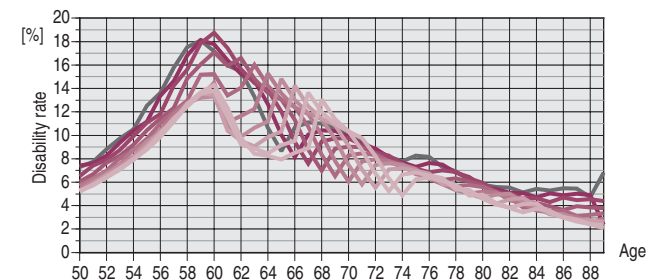
Source: MLSA

C.2.4. DEVELOPMENTS IN THE DISABILITY RATE AND ITS IMPACT ON PENSION EXPENDITURE

The disability rate together with the demographic structure of the population are the basic determinants for the development of the number of disabled pensioners. Estimating the future development of the disability rate is quite difficult as it depends on the development of the general health of the population and on any legislative changes to the method of evaluating entitlement to disability pensions.

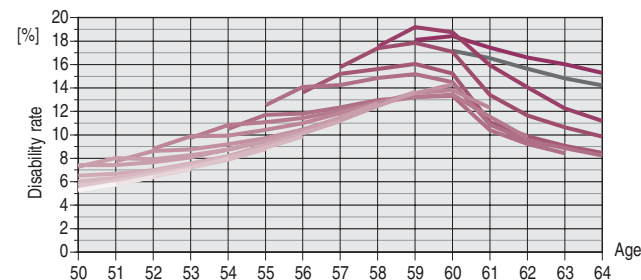
The generational approach was used for setting the future rate of disability (similarly as with the rate of participation), which reflects the specific rate of disability of cohorts on the basis of existing disability rates and changes thereto. This approach was selected on the basis of data analysis where, in following the various generations (Graph 45), it is possible to ascertain certain trends (as opposed to the data seen for the individual calendar years).

Graph 44 Disability rate in years – men (in %)



Source: MLSA

Graph 45 Disability rate for generations – men (in %)

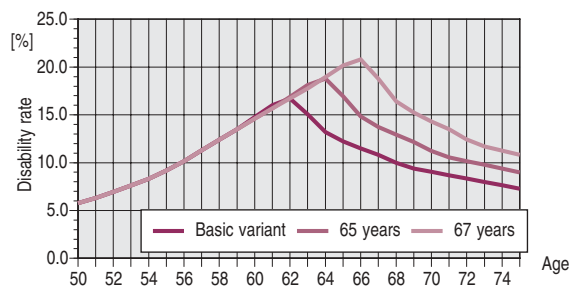


Source: MLSA

An important factor for estimating the disability rate is assessing the effects of increases to the retirement age. Under existing legislation, a disability pension may not be granted after reaching the retirement age (only old-age pensions), which

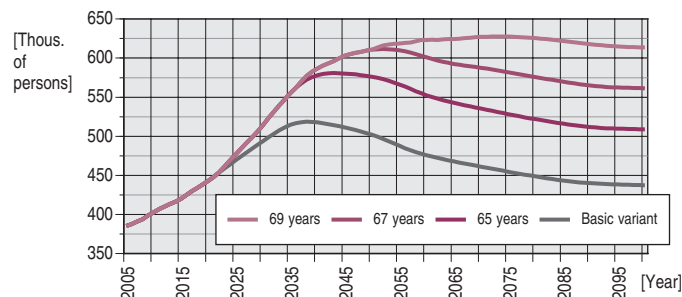
explains the change in the trend of the disability rate in the graphs above. Any increases of the retirement age are reflected in the disability rate by a higher rate of disability for those persons who, as a result of an increase in the retirement age, may not retire (Graf 46). A higher disability rate leads to a larger number of persons with disability pensions and consequently to greater expenditure for this type of pension.

Graph 46 Full disability rate for the 1980 generation – men (in %)



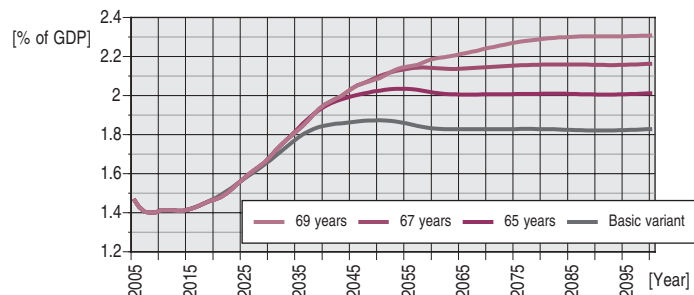
Source: MLSA

Graph 47 Number of full disability pensioners (thous.)



Source: MLSA

Graph 48 Expenditure for disability pensions (% of GDP)



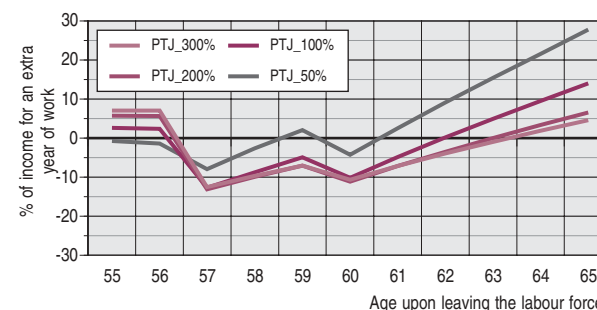
Source: MLSA

C.2.5. MOTIVATION FOR DEFERRING RETIREMENT BY OTHER MEANS THAN RAISING THE RETIREMENT AGE

C.2.5.1. Implicit tax

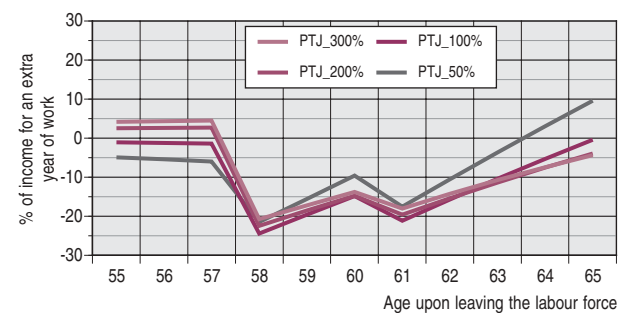
The criterion of the implicit tax was used for evaluating the financial motivation for deferring old-age retirement. It compares the situation of retiring in a given age to the situation where this retirement is delayed by one year. In the event that the implicit tax becomes negative, then there is a motivation in the system to delay retirement. On the other hand, with positive values the individual is motivated to retire. The structure of the implicit tax that was used is based on the work of the Executive Team and may in some details differ from the approach used by others.

Graph 49 Implicit tax for 1995 generation – women (with two children)



Source: MLSA

Graph 50 Implicit tax for the 1980 generation – women (with two children)



Source: MLSA

Certain conclusions may be made from the direction of the curves (some may also be seen in Graph 49 and Graph 50 above):

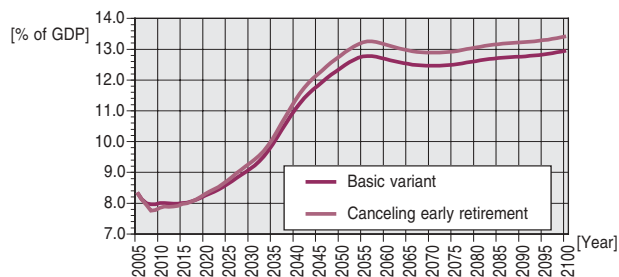
- implicit tax is lower for women than men, which relates to the longer life span for women. Women are thus more motivated to delay retirement,
- implicit tax falls with time (with increases in the life span) and the curve shifts to the right (depending on increases in the retirement age),
- implicit tax varies according to previous earnings, but not significantly.

Additional calculations demonstrate that the greatest motivation is with individuals with high earnings and short insured periods. In contrast, it is the lowest for those persons with low earnings and a long insured period.

C.2.5.2. Early old-age pensions

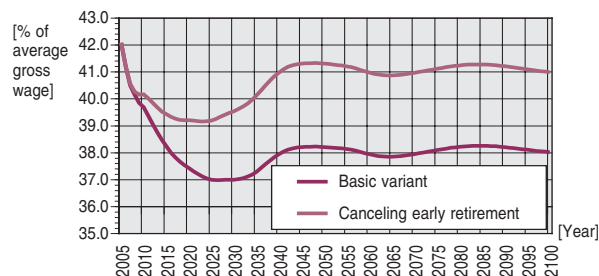
The direction of the curves of the implicit tax demonstrate that in the period of possible early retirement there are certain motivations for not making use of this option. As reflected in the following projection that foresees the cancellation of early retirement, the possibility of going into early retirement does not pose a financial risk to the system.

Graph 51 System expenditure (% of GDP)



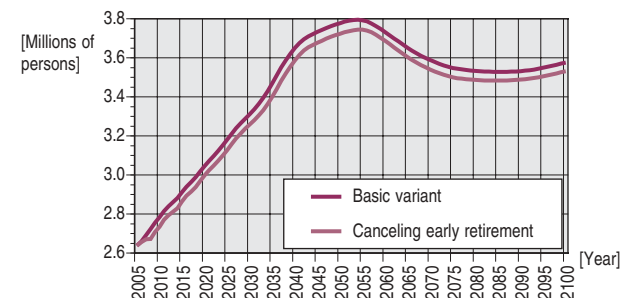
Source: MLSA

Graph 52 Total replacement ratio (%)



Source: MLSA

Graph 53 Total number of pensioners



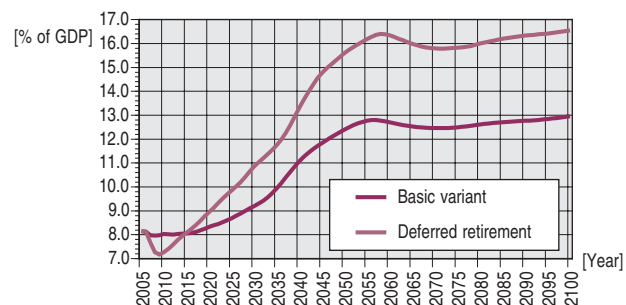
Source: MLSA

The graph of the total replacement ratio (Graph 52) also demonstrates that a significant part of the decrease of this ratio and thus the relation of the level of pensions to wages is actually caused by the existence of early (lower) retirements. In the event of their cancellation, the decrease in the total replacement ratio would, in the long term, be only marginal (even with the expected valorization to the minimum required under law).

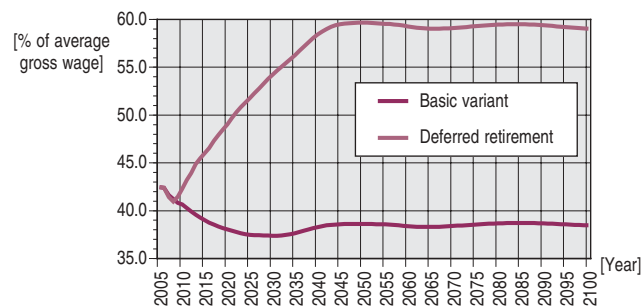
C.2.5.3. Deferred old-age pensions

A different approach was used for deferred pensions that would also emphasize the effects of financial motivations on the stability of the pension system. In the projection, it is expected that the coefficient for deferred pensions will be doubled (which will result in a decrease in the implicit tax) and such increase will lead to the deferring of retirement for those persons retiring after 2006 by two years after reaching the retirement age.

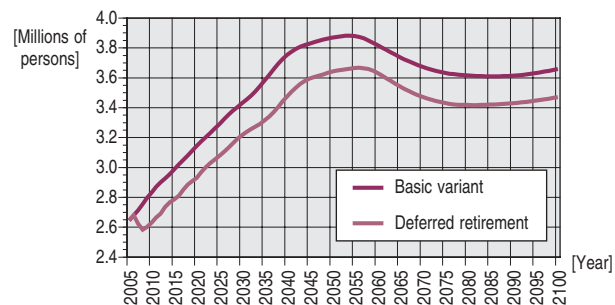
The risk involved in the existence of stimuli for deferring retirement after reaching retirement age is reflected in the projection below. In the short-term, a positive effect in the field of expenditure may be seen (as with the cancellation of early retirement) where as a result of delaying of retirement a decrease in the number of pensioners occurs (Graph 56 – where the lower number of pensioners is reflected in the remaining projection). Subsequently however, an increase occurs in expenditure above current levels as a result of the financial advantage-ousness of delaying retirement. This is reflected in the growth of the average pension. Therefore, in the long-term the effects of these measures on the financial un-sustainability of the system are significantly negative.

Graph 54 System expenditure (% of GDP)

Source: MLSA

Graph 55 Total replacement ratio (in %)

Source: MLSA

Graph 56 Number of pensioners

Source: MLSA

C.2.6. CONCLUSIONS**It will be necessary to increase the retirement age**

The existing pension system is, in maintaining the existing parameters, financially unsustainable (Graph 28 and Graf 30). The financial unsustainability is caused by the expected developments in the basic demographic parameters. The most important is the prolonged average life span and, ensuing therefrom, the **prolongation of the duration of drawing pensions** (Graph 38 and Graf 39 – according to the projections carried out this parameter represents up to **3/4 of the total imbalance**).

Extending the period for receiving pensions necessarily leads (with no decreases in the accumulated total pension rights)²⁶ to a decrease in the average pension level²⁷ even when preserving the total pension paid out.²⁸ In order to maintain a relatively stable level of pensions that would be able to secure an adequate level of income in old-age, it is not necessary to keep constant the period for drawing pensions. An important parameter is also the period of paying premiums²⁹ and the pensions rights ensuing therefrom.³⁰ In this respect, the employment rate is important and its increase may, to a certain extent, limit the need of reducing the growing period of drawing pensions. It is necessary to maintain a stable ratio between the above-mentioned periods, in order to maintain a stable relative level of pensions that do not disturb the inter-generational fairness.

This may be achieved in the pension system foremost by adjusting the retirement age which, as the only parameter, may serve as the corrector of demographic trends in the long-term. Subsequent increases of the retirement age above the framework of the above-mentioned ratios would enable the increase of the average pension level and thus better ensure an adequate income in old-age or a decrease in the burden on work in the form of premiums and increasing the freedom in deciding to retire.

Adjustment of the retirement age may not be considered to be a reform of the system, but rather a necessary and natural reaction to changes in the demographic situation. In contrast, its necessity may not be eliminated by carrying out a reform.

²⁶ Arising from premiums paid and not the pension sample.

²⁷ The end shift depends also on the equability of the original state.

²⁸ The sum paid out for the whole duration of receiving a pension.

²⁹ The actual period during which premiums were paid does not have to correspond with the insured period.

³⁰ Pension rights may be increased also by increases in premiums which, however, may have a negative impact outside the pension system and, in its consequences, may result not only in no increases but even in a decrease of such rights.

An increase in pension expenditure will occur

The second demographic parameter which will affect the stability of especially PAYGO systems is the **low birth rate**, which does not secure the basic reproduction of the population and which **leads** to its gradual dying out. This gradual process leads in the PAYGO system to a transformation of the implicit debt³¹ **to an explicit debt** (whereby the sum of the debt remains unchanged) and **creates an imbalance between revenues and expenditures**. The financing of a deficit thus created will have to be divided amongst the generations so that it does not create significant inter-generational inequality.

The following simulation³² demonstrates the effects of partial dying out³³ on the status of the pension system. Graph 57 demonstrates the gradual decreases in the number of inhabitants which is caused by a lower number of children that are born. Given that this involves a decrease in absolute numbers, after a certain period of time a new balance is created in the new total number.³⁴ At the same time, the lower number of children being born is also negatively reflected in the demographic dependency rate (Graph 59), where there is an increase in the number of older persons. Given its temporary nature, the dependency rate then returns to the original point when the targeted status of the population is achieved. The decrease in revenues due to the decrease in the number of persons that pay premiums (an absolute decrease which is given by the assumption on the fixed wages) may be seen in the graph showing revenues and expenditure (Graph 58). The decrease occurs gradually over time when the smaller less-numbered generations enter into retirement, which is followed by a decrease in expenditure and, following the elapse of a transitional period, revenues and expenditures are once again balanced.

The temporary imbalance between revenues and expenditures results in the creation of debt which, as seen in Graph 60, is not a newly created debt but rather a transformation of a part of the existing implicit debt into an explicit debt whereby the total debt remains unchanged. From these graphs it may be seen that, as a result of the low birth rate in the continuous system, additional debt is

³¹ This is debt ensues from the obligations towards future pensioners, which are not covered by reserves. It forms a natural component of PAYGO systems and arises in the beginning when obligations were created for which premiums were not paid.

³² This is a simplified simulation which does not have any direct relation to the situation in the Czech Republic. It is expected that wages and prices are fixed in time.

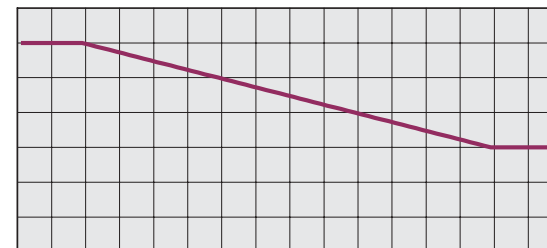
³³ The absolute number of children born will decrease by half, i.e. in the long-term, the population will decrease by half.

³⁴ This process is permanent when there are decreases in the birth rate and, in the long-term, will lead to the dying out of a population.

not created whose “creators” would be childless persons or persons with an “insufficient” number of children.

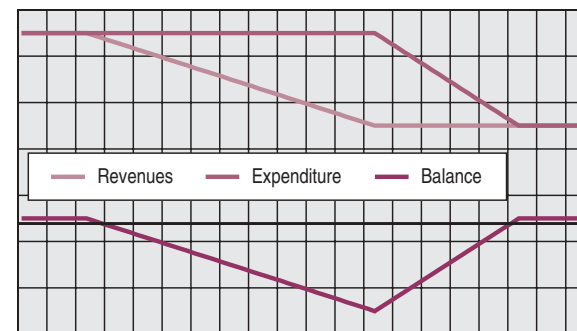
Another reason for the **growth in expenditure** is the field of **disability pensions**, where (provided there is an increase in the retirement age) an increase in the number of recipient of these pensions may be expected (Graph 47). This area is however very difficult to project as it depends also on the general development of the health and disability conditions.

Graph 57 Total number of inhabitants



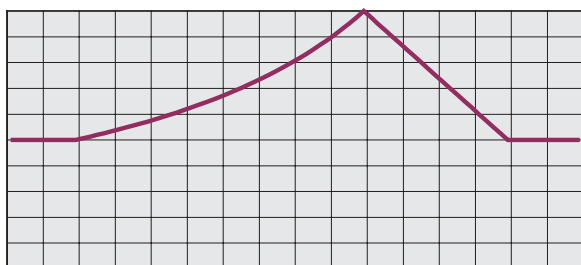
Source: MLSA

Graph 58 Revenues, expenditure and balance of the system



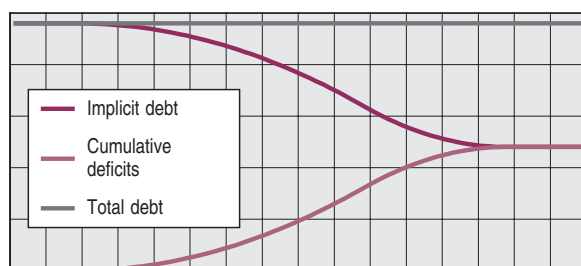
Source: MLSA

Graph 59 Dependency rate



Source: MLSA

Graph 60 Total and implicit debt and cumulated deficits



Source: MLSA

It is not suitable to create financial incentives for deciding to retire

The pension system should be as actuarially neutral as possible and should not create any incentives to remain on the labour market or to retire. Such neutrality should be reached for the most part in the period after reaching retirement age. **Prior to reaching retirement age, there may be demotivation** for entering into retirement, which **however should not be excessive** so that it does **not increase the risk of inadequate pensions**. The creation of a motivation may threaten the financial stability of the pension system and the pressure to defer retirement should therefore rather be made by increasing the retirement age.

On the basis of current demographic forecasts regular revision of the coefficients governing the shortening or increases of early and deferred pensions should be carried out.

It will be necessary to undertake a reform leading to the diversification of the system

Even though it was stated above that increases to the retirement age and its adjustment to changes in the demographic parameters may not be considered to be a reform, this does not mean that the current pension system does not require any reforms. Such a reform should be targeted at diversification of both the revenues and the expenditure of the system, which should result in strengthening the security of adequate pensions in old-age. Therefore, the reform should lead to:

- **strengthening the differentiation of pensions in the middle and higher income groups and introducing a limit for premiums**

Possible strengthening of the equivalence of pensions is due to the possibility of lowering the pension levels for lower income groups. The room for differentiation of pensions is given by the differences in the minimum pension granted and the average pensions. The possibility of differentiating pensions depends also on the level of premium limits which determines to what extent should differentiation in the system of basic pension insurance should be dealt with. In cases of relative low limits of premiums, the differentiation will be the task of rate supplementary schemes. In contrast, with a high level of premium limit or its non-existence such differentiation must be dealt within the system of basic pension insurance.

Increasing the equivalence should be achieved for the middle and higher income groups at the cost of strengthening the levelling for lower earning groups. This may be achieved by, e.g. **combining the equivalent system with a minimum pension** where a portion of the premiums is geared at covering a minimum pension and the remainder is for equivalency (ideally DC) plan. Another possibility would be the **combination of certain form of flat rate pension with the equivalent scheme** where rights in the equivalent scheme are obtained only after reaching a certain level of earnings. Up to a certain level of earnings premiums are paid only into the flat rate pension scheme and above this level a portion goes into the equivalent (ideally DC) scheme. Both of the above-mentioned options would enable the introduction of funding elements of financing. In the event of introducing funding elements of financing in the basic pension system, the transition to this system should be, on the basis of stipulated rules, compulsory, which in contrast to discretionary system (a system with an opt out), would not lead to increasing the potential risk of pover-

ty or inadequate income in old-age. The compulsory transition with set rules does not prevent any further necessary changes or adjustments.³⁵

- **Introducing payments of premiums for all insured periods and decreasing the contribution rates**

The setting of the assessment base and the payments of premiums even for non-contributory periods of insurance whereby the insurance rate would be decreased for pension insurance with a positive impact on the labour market in such a manner that the effect on revenues in the system would be neutral. It would be the most suitable to set the assessment base for this period at the level of the minimum wage in such a way so that it would not be possible to acquire higher entitlements within the non-contributory period of insurance than within the realm of economic gainful activity or in certain types of non-contributory periods of insurance (e.g. the care of a child) to set the assessment base higher, e.g. as a percentage of the average wage in the national economy. Such a measure would lead to increasing the motivation to actively participate in the labour market. In connection with this measure, it would be necessary to **extend the decisive period** from which earnings are determined for the calculation of pensions **for the whole duration of participation in insurance**. The category of 'excluded periods' would have to be cancelled.

In relation with introducing payments and lowering premiums it will be necessary to limit the risk of shifting the tax burden to individuals and thereby lowering their disposable income. For example, in situations where a decrease in the contribution rate for employers (and thereby lowering the total cost of employment) would be compensated by increasing VAT.

- **It will be necessary to create a reserve pension insurance fund**

The reserve fund should be created so that it will enable to carry out the reform measures and would not create inter-generational inequality in the pension insurance system. In relation to the expected reform measures, it will then be necessary to create a reserve fund both in terms of the size and the structure of revenues and expenditure.

³⁵ In enabling options, the conditions valid at the time when the selection was made should be preserved for individuals as any subsequent changes to the parameters in the system of basic pension insurance which would be made later could impact the decision-making.

- **The reserve serves to achieve inter-generational equality**

This reserve is created as a result of short-term surpluses (differences in premiums and expenditure) which are caused by the given structure of the population (larger and smaller generations). The reserve (e.g. Graph 30) covers the deficits that are incurred for the same reasons. This type of reserve is created or should be created autonomously³⁶ in the system even if the system is set for inter-generational equality and through its investment a certain diversification of revenues may be achieved.

- **The reserve serves to finance entitlements in the event of decreases in premiums**

This reserve will enable the financing of existing entitlements in the event that a decrease in revenues occurs in the system of basic pension insurance either as a result of a transfer of part of the premiums into a newly created funded scheme or in the decrease in the contribution rate as a result of reforms that limit the size of the pension system (e.g. as a result of a proposal for flat rate pensions). This type of reserve would be created from resources outside the pension system and its size depends on the size of the transformation debt thus created, which the reserve will cover.

The actual creation of a reserve fund only makes sense when revenues and expenditure of the pension system are separated from the state budget. The separation of revenues and expenditures must necessarily be associated with the transfer to the insurance provider of the responsibility for the financial stability of the system and the decision-making powers that will enable such stability to be reached. In practice, this would mean that, e.g. decisions on the valorization of pensions or adjustments to the reduction limits would no longer be accorded to the government but would be in the competence of the insurance administrator, whereby each such decision would have to be taken while taking into consideration the financial sustainability of the system and the adequacy of pensions.

³⁶ The described scenarios were demonstrated in the previous actuarial report whose text may be found at: www.mpsv.cz/cs/1353.

C.3. SICKNESS INSURANCE

C.3.1. PROJECTIONS AND EVALUATION OF DEVELOPMENTS

The balance of the sickness insurance depends on the amount of the assessment bases for premiums and for benefits, the insurance rate, the contribution compliance, the sick leave rate and parameters for calculation of benefits. The projections of the number of payers and beneficiaries of benefits are not a basic indicator for projections of the sickness insurance as, unlike pension insurance, the group of contributors and beneficiaries is approximately the same.

Developments in the number of contributors and beneficiaries of sickness insurance are determined by the demographic structure of the population and the participation rates of various age groups. Another important indicator is the development of unemployment. As the self-employed may choose whether to participate in sickness insurance and given the different method for determining premiums from employees and the self-employed, two groups of insured persons exist: employees and the self-employed. The number of voluntarily insured self-employed versus the total number of self-employed uninsured under pension insurance has gradually decreased from 51 % in 2000 to 34 % in 2005. Increases in the premiums for the voluntarily insured self-employed led to a decrease in their ratio to the total number of those who paid deposits on pension insurance. However, it is now expected that under the new Sickness Insurance Act this ratio will no longer decrease. The developments in the number of contributors as well as the number of beneficiaries will in the future copy developments in the number of contributors of pension insurance. However, the absolute total number of persons uninsured under sickness insurance will be lower by the number of self-employed who choose not to be insured under sickness insurance (at the moment they number approximately 500,000).

Revenues from sickness insurance premiums depend on the number of contributors, the amount of the assessment base, the insurance rate and the contribution compliance. In the long-term projections, the revenues in the system of sickness insurance will, as with pension insurance, be constant in comparison to the GDP (Chapter C.2., Graph 28), however their absolute amount will vary according to the prescribed amount of the contribution rate.

New measures will impact **expenditure** on sickness insurance for the most part in the near future; therefore, long-term projections are not as important as in the pension insurance system. **As a result, short-term forecasts are preferred.**

In 2006, the new Sickness Insurance Act (Act No. 187/2006 Coll.) and the accompanying Act No. 189/2006 Coll. were adopted and will come into effect on

1 January 2007 (see Chapter A). Employers will also play a role in the financial securing of employees during sick leave and quarantine as they will for the first two weeks off sick leave (quarantine) provide employees with compensation of wages for the days when they do not receive any income. This method of increasing social oversight against abuse is currently being used in 20 EU Member States. The need of such a change was recommended by experts of international organizations already in the beginning of the 1990s as it is a necessary measure to prevent the growth of sick leave in market economies. The change in the calculation of the amounts of sickness benefits is outlined in the following table:

Table 56 Parameters for calculating wage compensation and sickness insurance benefits

Measure	Current legal status as at 1 January 2006	New Act as at 1 January 2007
Decisive period	12 months	12 months
Reduction in the DAB (daily assessment base):		
Reduction limit (RL)	CZK 510 and CZK 730	For sickness benefits: one third of the amount 1.0-1.5-3.0 times GAB*; for wage compensation: 1.4 times RL of sickness benefits
Reduction rate		
Wage compensation		1 st -14 th day 90 %-60 %-30 %
Sickness benefit	1 st -14 th day 90 %-60 %-0 % From the 15 th day 100 %-60 %-0 %	From the 15 th day 100 %-60 %-30 %
Financial support for care of family members	1 st -14 th day 90 %-60 %-0 % From the 15 th day 100 %-60 %-0 %	From the 1 st day 100 %-60 %-30 % From the 1 st day 100 %-60 %-30 %
Maternity benefit	From the 1 st day 100 %-60 %-0 %	From the 1 st day 100 %-60 %-30 %
Rate for the daily benefit		
Wage compensation		Per work day 1 st -3 rd day 30 % AE* From 4 th day 69 % AE
Sickness benefit	Per calendar day 1 st -3 rd day 25 % From the 4 th day 69 %	Per calendar day From the 15 th day 69 % DAB*
Maternity benefit	69 %	From the 1 st day 70 % DAB
Financial support for care of family members	69 %	From the 1 st day 65 % DAB
Concurrent employment	Benefit from each	Just 1 benefit

* GAB = general assessment base; AE = average earnings; DAB = daily assessment base.

Economic effects of the new Act

Financial impact on the state

Table 57 Financial impact on the state (CZK billions)

Year	Revenues from premiums	Expenditure for sickness benefits	Revenues - expenditure
2007	24.1	-27.9	-3.8
2008	25.4	-29.5	-4.1
2009	26.8	-31.1	-4.3

Source: MLSA

It is expected that during the period 2007-2009 the balance of the sickness insurance benefits will be a deficit of around CZK 3.8 - 4.3 billion provided that the sick leave rate remains the same as in 2005 (6.1 %). If the participation of employers in the sickness insurance system helps decrease the sick leave rate (as occurred e.g. in Slovakia), then the balance of the state budget will be much better.

Financial impact on employers

Table 58 Financial impact on employers (CZK billions)

Year	Decrease in premiums	Wage compensation	Decrease in expenditures
2007	-18.3	9.7	-8.6
2008	-19.3	10.2	-9.1
2009	-20.3	10.8	-9.3

Source: MLSA

The effects of the new Act on employers' expenditure are influenced by savings on the premiums paid (decreasing the contribution rate from 3.3 % to 1.4 % and increasing the expenditure for wage compensation paid out). The savings from the decrease in premiums should be sufficient for employers to pay out wage compensation in the first 14 calendar days of sickness for those employers whose employees have an above-average sick leave rate. Given the same sick leave rate as in 2005 (6.1 %), employers would have in 2007 in total about CZK 8.6 billion more than if the current legal status is maintained.

Savings on premiums are higher the greater the amount of the assessment base for premiums. Therefore they increase:

- the more employee wages are higher,
- the more total period of sickness of employees is shorter.

Therefore, any sickness decreases savings on premiums (it is irrelevant if the sickness is shorter than 14 days, nor is the number of illnesses important).

Expenditure on wage compensation increases:

- the higher employee wages are,
Above-average wages impact less the growth of paid out compensation as a result of the effects of the reduction limits. Given that savings on premiums remain the same percent of the assessment base (1.9 %) regardless of the amount of the wages, while the portion of the amount of compensation for previous earning decreases with rising wages (for above-average wages), the financial effects of the new Act on employers will at the same sick leave rate be more positive for those employers whose employees reach higher earnings.
- the higher the number of days of sickness up to the first 14 days, whereby the equation for the calculation of the amount of the compensation causes the number of work days after the 3rd calendar day of sickness to have the greatest importance.

Sickness longer than 14 calendar days does not impact the employer's expenditures on compensation, but does affect the amount of premiums as it lowers the amount of the assessment bases for the calculation of premiums. Sickness longer than 14 days thus does not increase but rather decreases the employer's expenditures on premiums. Compared to the current legal situation however, smaller savings on premiums will occur (savings on premiums = amount of the assessment bases x 0.019) as a result of the smaller amount of the assessment bases. In comparing the expenditures of employers to the current legal situation and to the new Act, sickness longer than 14 days also has a negative impact on employers.

For those employers who achieve profits and pay income tax for legal entities it is necessary, in comparing employers' expenditure, to take in account also this fact. Expenditure for the payment of wage compensation and changes to the amounts of premiums will be reflected in the amount of the tax base, which will lead to an increase or decrease in the amount of the tax payable and thus will affect the total financial impact of the new Act on employers.

Employers with 'supplementary' insurance and employers employing persons with an altered work capacity form a special group for which other circumstances must also be taken into account. Half of the expenditure on the payment of wage compensation will be refunded to such employers.

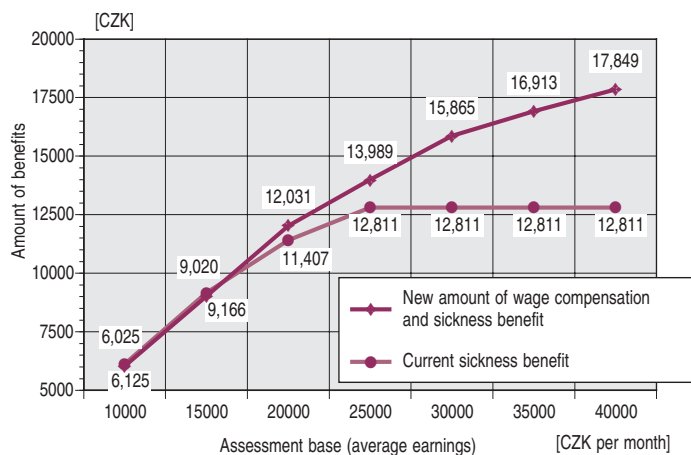
Factors that affect the difference between the employers' expenditure under the current legal situation and that under the new Act are sick leave (i.e. sickness up to 14 calendar days, the average duration of sick leave, and the number of cases of sick leave per 100 insured persons) and the amount of wages.

Financial impact on insured persons

Sickness benefits

The new method of calculation sickness benefits will, as a result of changes to the reduction limits in 2007, lead to increases in income for contributors with average and above-average wages and the replacement ratio for these persons will also increase (the ratio of the benefits amount to net wages). Graph 61 demonstrates the differences between the amount of the sickness benefits according to the legal situation as at 2006 and the amount of the wage compensation and sickness benefits for the first 30 calendar days of sickness under the new Act. Graph 62 reflects the comparison of the compensation ratio.

Graph 61 Comparison of the amount of sickness benefit with the amount of compensation and sickness benefits for the first 30 calendar days of sick leave in 2006

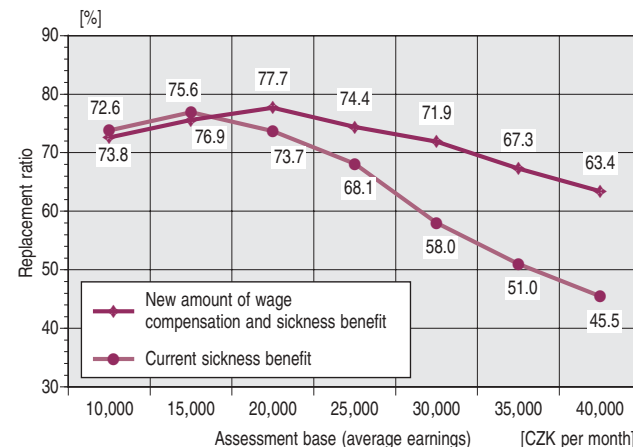


Source: MLSA

Maternity benefits

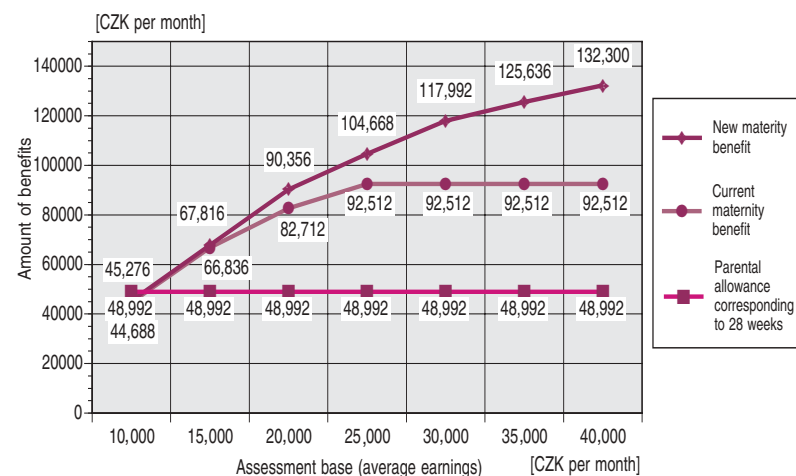
The same changes in the reduction limits and reductions as with sickness benefits will occur in determining the daily assessment base. The percentage rate of the daily amount of the benefits will increase from 69 % to 70 % of the daily assessment base. This percentage rate for the daily maternity benefit will mean higher benefits and ratio of the benefits versus previous earnings (the replacement ratio) for all those insured and a greater increase will occur for those who paid premiums on higher earnings (Graph 63).

Graph 62 Ratio of the amount of benefits for the first 30 calendar days of sick leave to net wages for different wage levels



Source: MLSA

Graph 63 Comparison of the amount of maternity benefits for 28 weeks of sick leave



Source: MLSA

C.3.2. CONCLUSIONS

The financial overview of the effects of the new measures brought by the Sickness Insurance Act is summarised in the following table.

Table 59. Estimate of revenues and expenditure for sickness insurance (incl. wage compensation)

Balance of revenues and expenditure in 2007					
		Current situation	New Act	Change	
Insurance rate	in %	Employee	1.1	1.1	0.0
		Employer	3.3	1.4	-1.9
		Total	4.4	2.5	-1.9
Revenues from premiums	billions CZK	Employee	10.6	10.6	0.0
		Employer	31.8	13.5	-18.3
		Total	42.4	24.1	-18.3
Expenditure for benefits	billions CZK	Employer		9.7	9.7
		State	35.5	27.9	-7.6
		Total	35.5	37.6	2.1
Revenues - expenditure	billions CZK	Employer	-31.8	-23.2	8.6
		State	6.9	-3.8	-10.7
		Total			-2.1

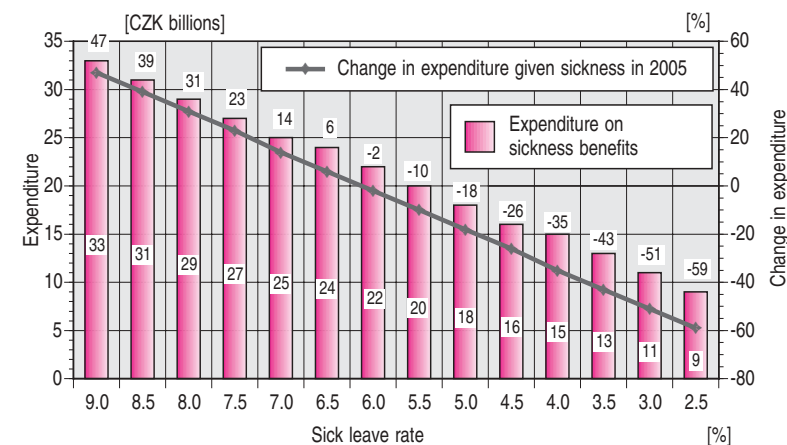
Source: MLSA

Revenues from premiums are impacted also by the amount of the sick leave rate (Chapter B.2.3). If the sick leave rate falls by half a percentage point, then the revenues from premiums will increase by 0.2–0.5% of the previous value, i.e. by CZK 50–120 million.

Likewise, expenditure for sickness benefits is significantly influenced by sick leave for sickness and injury. A decrease or increase in the value of the sick leave rate by half a percentage point results in a decrease or increase in expenditure on sickness benefits by about 8 % of the previous expenditure on sickness benefits.

Given a sick leave rate of 6.1 % (the same as in 2005), it is expected that expenditure on sickness insurance will surpass the revenues from premiums in 2007–2009 by CZK 3.8–4.3 billion. In order to achieve a balanced level of revenue and expenditure in sickness insurance the sick leave rate would have to be 1.1 percentage points³⁷ lower, i.e. that it amounts to 5.0 %.

Graph 64 Impact of sickness on sickness insurance expenditure



Source: MLSA

Balanced accounts may also be achieved by changing the structural parameters either by changing the amount of the reduction limits or the rate for the daily amounts of the benefits.

- For example, with a sick leave rate of 6.1 % (as in 2005) a balance would have been achieved by lowering the daily rate from 69 % to 56 % while lowering the daily rate by 9 percentage points, i.e. from 69 % to 60 % of the daily assessment base a balance would be achieved with a sick leave rate of 5.7 %.

Table 60 Examples of variants of percentage rates of sickness benefits and the sick leave rate for an equalised balance

	Amount of sickness benefits rate	Sick leave rate
1	69 %	5.0 %
2	65 %	5.3 %
3	60 %	5.7 %
4	56 %	6.1 %

Source: MLSA

³⁷ At present, in the Czech Republic 6 employees out of every 100 are on sick leave. In Slovakia, there were 5 employees missing every day for every 100 employees, however after involving the employers in the sickness insurance system this rate fell by 2 employees which means that daily there are only 3 employees on sick leave for every 100 employees.

The statistics demonstrate that after decreasing the relative level of benefits there is always also a decrease in the sick leave rate. Decreasing benefits and thereby also the sick leave rate may however affect about three quarters of the expenditure for sickness insurance. Expenditure for maternity benefits, which constitute about one-fifth of expenditure, and partially also the financial support for care of family members are not affected by the sick leave rate as they depend on other factors.

- The impact of the difference between the second and third reduction limit has a relatively insignificant impact on the amount of expenditure. For example, the total cancellation of the crediting of income between the second and third reduction limit would in 2007 decrease expenditure on sickness insurance only by CZK 300 million.
- The introduction of a quarantine period for the first 3 days of sick leave would not directly affect expenditure for sickness insurance benefits as benefits from sickness insurance are only accorded after the 15th day of sick leave; employers would save about CZK 1.3 billion on wage compensation.

The **contribution rate also affects the balance**. Under the new system, the contribution rate for employers is decreased by 1.9 % (from 3.3 % to 1.4 %). The lowering of the contribution rate or stipulating a higher rate of premiums would have a positive effect on the system's balance.

- Setting the **contribution rate for employers at 2.3 % would retain the aggregate expenditure for sickness benefits for employers** (premiums and wage compensation) at about the same level, i.e. CZK 32 billion. Employers' savings on premiums would thus correspond to their expenses for the payment of wage compensation. The balance of revenues and expenditure in sickness insurance in the state budget would be positive and would amount to CZK 5 billion (there would be about CZK 2 billion less than under the situation before the new Act).
- Setting the contribution rate for employers at **1.8 %** would result in that **the balance of revenues and expenditure for sickness insurance in the state budget would be balanced** (under the legal situation before the new Act there would be approx. CZK 7 billion less in the state budget). **The expenditure of employers would be in total CZK 5 billion lower** than under the legal situation prior to the new Act.
- Setting the contribution rate for employers at **2.5 %** would result that **the balancing of revenue and expenditure on sickness insurance in the state budget would be approximately the same as under the legal conditions prior to the new Act** (revenues from sickness insurance premiums

would exceed expenditure on benefits by CZK 7 billion). **Employers' expenditure would in total be CZK 2 billion higher** than under the legal situation before the new Act.

APPENDIX

I. EXAMPLES OF BENEFIT CALCULATIONS

A. EXAMPLE OF A PENSION CALCULATION

Case example

A man born on 1 April 1944, after completing the compulsory nine years of schooling in 1959, studied at high school and university until 30 June 1967. After completing his studies, he was continuously employed up until 31 December 2005. In 1993, he was sick 10 days, in 1994 he was sick 20 days and in 1996 he was sick 15 days. As of 1 January 2006, he was granted an old-age pension under Article 29 of Act No. 155/1995 Coll. (a “normal” old-age pension).

Calculation

1. Determining retirement age

The retirement age was reached on 1 October 2005.

The age limit of 60 was reached on 1 April 2004, i.e. in the ninth calendar year after 1995, therefore the retirement age amounts to $60 + 9 \times 2$ months (Article 32 of Act No. 155/1995 Coll.).

2. Determining the insured period acquired up until becoming entitled to old-age pensions

The acquired insured period amounts to 45 full years.

Included in the insured period is in the full period from the beginning of studies at high school up to 18 years (1 September 1959–31 March 1962), i.e. 943 days and the duration of employment (1 July 1967–30 September 2005), i.e. 13,972 days. The duration of studies after the age of 18 (1 April 1962–30 June 1967) is included at a rate of 80 %, i.e. 1,534 days (1917×0.8). The total insured period thus amounts to 16,449 days, i.e. 45 full years and 24 days ($16449 / 365$).

3. Determining the decisive period

The decisive period for determining the personal assessment base will in this case be 18 years and will include the years from 1986 to 2005 (2005 being the last year before the granting of the pension).

4. Furthermore it is necessary

- to determine for each of the calendar years of the decisive period the amount of the assessment base and the number of days of the excluded period (hereinafter “EP”) – in this case this involves the days of sickness referred to in the facts of the case,
- for each of the calendar year “t” of the decisive period (with the exception of the calendar year preceding the year in which the pension is granted) determine from the relevant government decree the amount of the general assessment bases (hereinafter “GAB”) and the amount of the respective recalculation coefficient (hereinafter “RC”), whereas for the calculation of the pension accorded in 2006 $RC_{2004} = 1.0532$ is set by Government Decree No. 414/2005 Coll.,
- for the individual calendar years of the decisive period set the coefficient of the growth of the general assessment base (hereinafter “CGGAB”, whereby the following applies:

$$CGGAB_t = \frac{GAB_{2004} \times RC_{2004}}{CAB_t}),$$

- to set the annual assessment bases for each calendar year of the decisive period (hereinafter “AAB” whereby the following applies: $AAB_t = AB_t \times CGDAB_t$).

The method of calculation is seen in the following table:

Year	CB _t [CZK]	EP [days]	GAB _t [CZK]	CGGAB _t	AAB _t [CZK]
1986	28,000		2,964	6.3540	177,912
1987	30,000		3,026	6.2238	186,714
1988	31,000		3,095	6.0851	188,639
1989	33,000		3,170	5.9411	196,057
1990	35,000		3,286	5.7314	200,599
1991	41,000		3,792	4.9666	203,631
1992	51,000		4,644	4.0554	206,826
1993	66,000	10	5,817	3.2376	213,682
1994	79,000	20	6,896	2.7311	215,757
1995	96,000		8,172	2.3046	221,242
1996	115,000	15	9,676	1.9464	223,836
1997	128,000		10,696	1.7608	225,383
1998	142,000		11,693	1.6106	228,706
1999	155,000		12,655	1.4882	230,671
2000	167,000		13,490	1.3961	233,149
2001	181,000		14,640	1.2864	232,839
2002	194,000		15,711	1.1987	232,548
2003	207,000		16,769	1.1231	232,482
2004	221,000		17,882	1.0532	232,758
2005	220,000			1.0000	220,000

Note: The coefficient of growth of the general assessment base is stipulated precisely to four decimal points (the numbers on the fourth decimal place are rounded up according to general rules). The annual assessment base is rounded up to full Czech crowns.

5. Setting the personal assessment base (hereinafter “PAB”)

PAB = the monthly average of the sum of AAB for the years 1986 to 2005 =

$$= \frac{\text{Sum of AAB}_{1986 \text{ to } 2005}}{\text{No. of days 1986 to 2005} - EP} \times 30.4167 = \frac{4,303,431}{7,305 - 45} \times 30.4167 = \text{CZK } 18,030$$

Given that there were days when sickness benefits were received (i.e. excluded periods), the total number of days of the decisive period must be decreased by the number of such days (in this given case 45 days) when setting the personal assessment base.

Note: The personal assessment base is rounded up to full Czech crowns.

6. Setting the calculation base (hereinafter “CB”)

Reduction: into the 1st reduction limit 100 % of the PAB is included, from the first reduction limit to the 2nd reduction limit 30 % of the PAB

is included and from the 2 reduction base 10 % of the PAB is included. For pensions granted in 2006 the reduction limits are provided for in Government Decree No. 414/2005 Coll. in the amounts of CZK 9,100 and CZK 21,800.

$$CB = 9,100 + (18,030 - 9,100) \times 30 \% = \text{CZK } 11,779$$

7. Setting the percentage-based assessment (hereinafter “PA”). The amount of the PA for each entire insured year acquired until entitlement to old-age retirement in 1.5 % of the AB, i.e. $45 \times 1.5 \% AB = 67.5 \% AB$, therefore $67.5 \% \text{ CZK } 11,779 = \text{CZK } 7,951$ per month;

Note: the minimum amount of the percentage – based assessment is CZK 770 per month.

8. Setting the basic amount (hereinafter “BA”)

BA = CZK 1,470 per month (last amended by Government Decree No. 415/2005 Coll.).

9. Increased by the period of gainful activity carried out after entitlement to old-age pension

From 1 October 2005 to 31 December 2005, i.e. for 92 calendar days, there is an entitlement to an increased percentage-based assessment of the pensions by 1.5 % of the AB, i.e. $11,779 \times 1.5 \% = \text{CZK } 177$, therefore

$$\text{total PA} = 7,951 + 177 = \text{CZK } 8,128 \text{ per month.}$$

Note: The increase is for every complete 90 calendar days (not including periods of sickness) and amounts to 1.5 % for the period obtained after 30 June 2001 and 1 % for the period prior to 1 July 2001.

10. Valorization increase pursuant to Government Decree No. 415/2005 Coll. does not apply.

11. Total amount of old-age pension

$$P = BA + PA = \text{CZK } 1,470 + \text{CZK } 8,128 = \text{CZK } 9,598 \text{ per month}$$

Note: The amount of the old-age pension is rounded up to the next Czech crown; the amount of the old-age pension calculated to the date of entitlement to pension is rounded up separately as well as any increases of old-age pension for the period of employment performed after the entitlement.

Other examples of sample calculations of pensions and information about some terms may be found on the Internet pages of the MLSA:

<http://www.mpsv.cz> in the section Pension Insurance – Calculators.

B.1. EXAMPLES OF SICKNESS INSURANCE BENEFIT CALCULATIONS³⁸

legal status as of January 2006

The following **four benefits** are paid out of sickness insurance: sickness benefit, financial support for care of family members, maternity benefit and the pregnancy and maternity benefit compensation.

B.1.1. SICKNESS BENEFIT

Case example

An employee became incapable of work on 4 January 2006 and sick leave lasted until 30 January 2006 (i.e. 27 calendar days). His creditable income in the months January – December 2005 amounted to:

- A) 0.7 times the average wage in the national economy for 2005, i.e. approx. CZK 13,268 per month.
- B) 1.5 times the average wage in the national economy in 2005, i.e. approx. CZK 28,431 per month.

³⁸ GENERAL NOTE – Definition of terms:

- **‘Decisive period’** is as a rule the 12 calendar months preceding the calendar month in which the work incapacity occurs (quarantine, need to care for a family member or maternity leave).
- **‘Daily assessment base’** (DAB) the creditable income (all income subject to the payment of premiums for social security and contributions for the state employment policy assessed to an employee in the decisive period) divided by the number of calendar days in the decisive period (some days are however not included in this number in order to prevent the unjustified reduction of the daily assessment base – e.g. days for which sickness benefits are provided).
- **‘Reduction of the daily assessment base’** (DABr) two limits are set for the reduction. In 2006, the first reduction limit is CZK 510 and the second reduction limit is CZK 730. For sickness benefits and the family member care benefit the first 14 calendar days of sick leave 90 % of CZK 510 is included, 60 % from the amount above CZK 510 to CZK 730 and any amount above this is not taken into account. From the 1st day of maternity benefits and from the 15th calendar day of sick leave for sickness benefits and family member care benefits amounts up to CZK 510 are included in the full amount, 60 % from amounts exceeding CZK 510 up to CZK 730; amounts exceeding CZK 730 are not taken into account.
- **‘Daily benefit set by a percentage rate’** the sickness benefits for the first three days of sick leave amount to 25 % of the DABr, for the fourth and subsequent days of sick leave they amount to 69 % of the DABr; maternity benefits amount to 69 % of the DABr; the family member care benefit amounts to 69 % of the DABr.

Calculation

1. Decisive period	<i>January – December 2005</i>	
	<i>365 calendar days</i>	
2. Daily assessment base		
A) Creditable income	CZK 159,216	12 x 13,268
Daily assessment base	CZK 436.21	159,216 / 365
B) Creditable income	CZK 341,172	12 x 28,431
Daily assessment base	CZK 934.72	341,172 / 365
3. Reduction of the daily assessment base³⁹		
Day 1–14 of sick leave		
A) CZK 393		436.21 x 90 %
B) CZK 591		510 x 90 % + (730 - 510) x 60 %
From the 15th day of sick leave		
A) CZK 437		436.21 x 100 %
B) CZK 642		510 x 100 % + (730 - 510) x 60 %
4. Daily sickness benefit³⁹		
A) 1 st to 3 rd day of sick leave	CZK 99	393 x 25 %
4 th to 14 th day of sick leave	CZK 272	393 x 69 %
from the 15 th day of sick leave	CZK 302	437 x 69 %
B) 1 st to 3 rd day of sick leave	CZK 148	591 x 25 %
4 th to 14 th day of sick leave	CZK 408	591 x 69 %
from the 15 th day of sick leave	CZK 443	642 x 69 %
5. Amount of the sickness benefit for a sickness of 27 calendar days³⁹		
A) CZK 7,215		3 x 99 + 11 x 272 + 13 x 302
B) CZK 10,691		3 x 148 + 11 x 408 + 13 x 443

³⁹ The calculation is rounded up the next whole Czech crown.

B.1.2. FINANCIAL SUPPORT FOR CARE OF FAMILY MEMBERS**Case example**

A worker cares for a sick child and the financial support for care of family members lasted from 4 January 2006 to 12 January 2006 (9 days, i.e. the maximum period for one case for a non-single spouse). Her creditable income in the months January–December 2005 amounted to CZK 18,954 a month (the estimated amount of the average wage in the national economy in 2005).

Calculation

1. Decisive period	<i>January–December 2005</i>	
	<i>365 calendar days</i>	
2. Daily assessment base		
Creditable income	CZK 227,448	12 x 18,954
Daily assessment base	CZK 623.15	227,448 / 365
3. Reduction of the daily assessment base³⁹		
CZK 527		510 x 90 % + (623.15 - 510) x 60 %
4. Daily benefit³⁹		
For each day of receiving the FSCFM	CZK 364	527 x 69 %
5. Amount of the financial support for care of family members for the 9 calendar days³⁹		
CZK 3,276		9 x 364

B.1.3. MATERNITY BENEFIT**Case example**

A women went on maternity leave which lasted from 4 January 2006 to 18 July 2006 (196 calendar days). The maternity benefit entitlement lasts for 28 weeks. Her creditable income from January to December 2005 amounted to CZK 18,954 per month (the estimated amount of the average wage in the national economy in 2005).

³⁹ The calculation is rounded up the next whole Czech crown.

Calculation

1. Decisive period	January–December 2005	
	365 calendar days	
2. Daily assessment base		
Creditable income	CZK 227,448	12 x 18,954
Daily assessment base	CZK 623.15	227,448 / 365
3. Reduction of the daily assessment base³⁹		
CZK 578	510 x 100 % + (623.15 - 510) x 60 %	
4. Daily maternity benefit³⁹		
Per day of maternity benefit	CZK 399	578 x 69 %
5. Amount of maternity benefit for 196 calendar days		
<u>CZK 78,204</u>	399 x 196	

B.1.4. PREGNANCY AND MATERNITY COMPENSATION BENEFIT**Case example**

A worker is assigned to different work due to pregnancy on 1 February 2006 and she goes on maternity leave on 1 May 2006. Prior to the transfer, her creditable income from February 2005 to January 2006 amounted to CZK 18,954 per month and CZK 13,268 after the transfer (0.7 times the estimated average wage in the national economy in 2005).

Calculation

1. Decisive period	February 2005–January 2006	
	365 calendar days	
2. Daily assessment base before the transfer		
Creditable income	CZK 227,448	12 x 18,954
Daily assessment base	CZK 623.15	227,448 / 365

³⁹ The calculation is rounded up the next whole Czech crown.

3. Reduction of the daily assessment base³⁹

CZK 578 510 x 100 % + (623.15 - 510) x 60 %

4. Average daily amount per calendar day after the transfer³⁹

i.e. the average creditable income for one calendar day in the calendar months after the transfer

February	CZK 473.86	13,268 / 28
March	CZK 428.00	13,268 / 31
April	CZK 442.27	13,268 / 30

5. Daily pregnancy and maternity compensation benefit³⁹

i.e. the difference between the daily assessment base determined to the date of the transfer and the average creditable income for one calendar day after the transfer

February	CZK 105	578 - 473.86
March	CZK 150	578 - 428.00
April	CZK 136	578 - 442.27

6. Pregnancy and maternity compensation benefit for the period from the transfer to the beginning of the maternity

CZK 11,670 105 x 28 + 150 x 31 + 136 x 30

Note: The pregnancy and maternity compensation benefit is granted only up to the beginning of maternity leave and only up to the ninth month after giving birth after the end of the maternity leave.

Additional examples of the calculation of benefit of sickness insurance benefits under the legal situation as at 2006 can be made with the calculator on the web pages of the Ministry of Labour and Social Affairs at: www.mpsv.cz /sekcce nemocenské pojištění / kalkulačka pro výpočet nemocenských dávek v roce 2006.

³⁹ The calculation is rounded up the next whole Czech crown.

B.2. EXAMPLES OF CALCULATIONS OF WAGE COMPENSATION AND SICKNESS INSURANCE BENEFITS⁴⁰

legal status as of january 2006

Pursuant to Act No. 187/2006 Coll., on sickness insurance and Act No. 189/2006 Coll., its accompanying act, four benefits are provided under sickness insurance: sickness benefits, financial support for care of family members, maternity benefit and the pregnancy and maternity compensation benefit. Wage compensation for work days is provided for the first 14 calendar days of sick leave due to sickness (quarantine). Entitlement to sickness benefits begins only from the 15th calendar day of sick leave.

⁴⁰ GENERAL NOTE: The reduction limit for the calculation of wage compensation and sickness benefits will be determined according to the data of the Czech Statistical Office on developments in the average wage by a notice of the MLSA in the Collection of Laws probably in September 2006. The amounts used in the examples are based on estimates. Definition of terms for **WAGE COMPENSATION**.

Entitlement to wage compensation occurs in the first 14 calendar days of sick leave and is only provided for work days.

- **'Decisive period'** always the previous calendar annual quarter.
- **'Average daily earnings'** are determined from the gross wages attributed to an employee's pay in the decisive period and the number of days worked in the decisive period. If an employee did not work at least 22 days in the decisive period, then likely earnings will be used instead of the average earnings. These are determined from the gross wages, which the employee obtained from the beginning of the decisive period or from the gross wages which he would likely have received.
- **'Reduction of the daily average earnings'** (DAEr) three limits are set for the reduction which amount to 1.4 times the reduction limits of sickness benefits. It is expected that in 2007 the first reduction limit will be CZK 936, the second approx. CZK 1,403 and the third approx. CZK 2,806. Ninety percent is included for wage compensation from amounts up to the first reduction limit, 60 % from amounts more than the first reduction limit up to the second, 30 % from amounts more than the second reduction limit up to the third and amounts more the third are not taken into account.
- **'Daily amount of compensation'** are set by the following percentage rate: the wage compensation for the 1st to 3rd work days of sick leave amounts to 30 % of the DAEr; from the 4th work day it amounts to 69 % from DEAr. The calculation is rounded up to the next whole Czech crown.

Definition of terms for **SICKNESS INSURANCE BENEFITS**

- **'Decisive period'** is generally the 12 calendar months preceding the calendar month in which sick leave occurs (quarantine, need to care for a family member or maternity leave). *next*

B.2.1. SICKNESS BENEFITS AND WAGE COMPENSATION

Case example

A worker became incapable of work on 4 January 2007 and the sick leave (SL) lasted until 30 January 2007, i.e. 27 calendar days. His creditable income in the months from January to December 2006 amounted to:

- A) 0.7 times the estimated average wage in the national economy in 2006, i.e. CZK 14,050 per month.
- B) 1.5 times the estimated average wage in the national economy in 2006, i.e. CZK 30,108 per month.

Calculation

WAGE COMPENSATION

In the first 14 calendar days of sick leave an employee is entitled to wage compensation for work days (i.e. 10 days).

1. Decisive period for average earnings **October–December 2006**
65 shifts worked

2. Average daily earnings

- | | | | |
|---|---------------------|-------------|--|
| A) Gross wage calculated in the decisive period | CZK 42,150 | 3 x 14,050 | |
| Average daily earning | CZK 648.46 | 42,150 / 65 | |
| B) Gross wages calculated in decisive period | CZK 90,324 | 3 x 30,108 | |
| Average daily earnings | CZK 1,389.60 | 90,324 / 65 | |

next

- **'Daily assessment base'** (DAB) is creditable income (all income subject to social security premiums and contributions to the state employment policy assessed to the employee in the decisive period) divided by the number of calendar days in the decisive period (certain days, however, are not included in this amount in order to prevent the decrease of the amount of the daily assessment base – e.g. days when sickness benefits are provided).
- **'Reduction of the daily assessment base'** (DABr) three limits are set for the reduction. In 2007, the first reduction limit is expected to be approx. CZK 668, the second approx. CZK 1,002 and the third approx. CZK 2,004. For sickness benefits, amounts up to the first reduction limit are included 100 %, amounts above the first but below the second reduction limit are included 60 %, amounts greater than the second but lower than the third reduction limit are included 30 % and amounts exceeding the third reduction limit are not taken into account.
- **'Daily benefit set by percentage rate'** Sickness benefits from the 15th day of sick leave amount to **69 %** of the DABr; maternity benefits amount to **70 %** of the DABr and financial support for care of family members amount to **65 %** of DABr.

3. Reduction of the average daily earnings³⁹

- A) **CZK 584** 648.46 x 90 %
 B) **CZK 1,115** 936 x 90 % + (1,389.60 - 936) x 60 %

4. Daily wage compensation⁴²

- A) For the 1st to 3rd day of sick leave **CZK176** 584 x 30 %
 4th to 14th day of sick leave **CZK 403** 584 x 69 %
 B) For the 1st to 3rd day of sick leave **CZK 335** 1,115 x 30 %
 4th to 14th day of sick leave **CZK 770** 1,115 x 69 %

5. Wage compensation for 10 calendar days³⁹

- A) **CZK 3,349** 3 x 176 + 7 x 403
 B) **CZK 6,395** 3 x 355 + 7 x 770

SICKNESS BENEFITS

Sickness benefits for calendar days are provided from the 15th calendar day of sick leave.

1. Decisive period

January–December 2006
365 calendar days

2. Daily assessment base

- A) Creditable income CZK 168,600 12 x 14,050
 Daily assessment base **CZK 461.92** 168,600 / 365
 B) Creditable income CZK 361,296 12 x 30,108
 Daily assessment base **CZK 989.85** 361,296 / 365

3. Reduction of the daily assessment base³⁹

- A) **CZK 462** 461.92 x 100 %
 B) **CZK 862** 668 x 100 % + (989.85 - 668) x 60 %

4. Daily sickness benefit³⁹

- A) **CZK 319** 462 x 69 %
 B) **CZK 595** 862 x 69 %

5. Sickness benefit for 13 calendar days³⁹

- A) **CZK 4,147** 13 x 319
 B) **CZK 7, 735** 13 x 595

³⁹ The calculation is rounded up the next whole Czech crown.

Total amount of the wage compensation and sickness benefits for 27 calendar days of sick leave

- A) **CZK 7, 496** 3,349 + 4,147
 B) **CZK 14,130** 6,395 + 7,735

B.2.2. FINANCIAL SUPPORT FOR CARE OF FAMILY MEMBERS**Case example**

A worker cared for a sick child which lasted from 4 January to 12 January 2007 (9 days, i.e. the maximum period for 1 case if the parent is not a single parent). Her creditable income from January to December 2006 amounted to CZK 20,072 per month (estimated amount of the average wage in the national economy in 2006).

Calculation**1. Decisive period**

January–December 2006
365 calendar days

2. Daily assessment base

- Creditable income CZK 240,864 12 x 20,072
 Daily assessment base **CZK 659.90** 240,864 / 365

3. Reduction of the daily assessment base³⁹

- CZK 660** 659.90 x 100 %

4. Daily benefit³⁹

- For each day of FMCB **CZK 429** 660 x 65 %

5. Benefits for 9 calendar days³⁹

- CZK 3,861** 9 x 429

³⁹ The calculation is rounded up the next whole Czech crown.

B.2.3. MATERNITY BENEFITS

Case example

A women went on maternity leave, which lasted from 4 January 2007 to 18 July 2007 (196 calendar days). Maternity benefits entitlement is for 28 weeks. Her creditable income from January to December 2006 amounted to 20,072 per month (the amount of the estimated average wage in the national economy in 2006).

Calculation

1. Decisive period	<i>January–December 2006</i>	
	<i>365 calendar days</i>	
2. Daily assessment base		
Creditable income	CZK 240,864	12 x 20,072
Daily assessment base	CZK 659.90	240,864 / 365
3. Reduction of the daily assessment base³⁹		
CZK 660		660 x 100 %
4. Daily maternity benefit³⁹		
For each day	CZK 462	660 x 70 %
5. Maternity benefits for 196 calendar days		
<u>CZK 90,552</u>		462 x 196

B.2.4. PREGNANCY AND MATERNITY COMPENSATION BENEFIT

Case example

A worker was transferred to other work due to pregnancy on 1 February 2007 and began maternity leave on 1 May 2007. Prior to being transferred her creditable income in February 2006 to January 2007 amounted to CZK 20,072 per month and after the transfer it amounted to CZK 14,050 per month (0.7 times the estimated average wage in the national economy in 2006).

Calculation

1. Decisive period	<i>February 2006–January 2007</i>	
	<i>365 calendar days</i>	
2. Daily assessment base prior to transfer		
Creditable income	CZK 240,864	12 x 20,072
Daily assessment base	CZK 659.90	240,864 / 365
3. Reduction of the daily assessment base³⁹		
CZK 600		659.90 x 100 %
4. Average daily amount per calendar day after the transfer		
i.e. the average of the creditable income for per calendar day in each month after the transfer		
February	CZK 501.79	14,050 / 28
March	CZK 453.23	14,050 / 31
April	CZK 468.33	14,050 / 30
5. Daily pregnancy and maternity compensation benefit³⁹		
i.e. the difference between the daily assessment base ascertained to the date of the transfer and the average creditable income per calendar day after the transfer		
February	CZK 159	660 - 501.79
March	CZK 207	660 - 453.23
April	CZK 192	660 - 468.33
6. The pregnancy and maternity compensation benefit for the period from the transfer to the maternity leave		
<u>CZK 16,629</u>		159 x 28 + 207 x 31 + 192 x 30

Note: The pregnancy and maternity compensation benefit is provided until a women goes on maternity leave and following the maternity leave up to the end of the ninth month after birth.

Additional examples for comparing the benefit amounts according to the legal situation in 2006 and the new Act are possible with the use of tables on the web pages of the Ministry of Labour and Social Affairs: www.mpsv.cz / nemocenské pojištění / nový zákon o nemocenském pojištění a změny v doprovodných zákonech / příklady vlivu nového zákona. Under the title 'Employers' it is possible to set the expenses of employers associated with sickness insurance (three options are possible).

³⁹ The calculation is rounded up the next whole Czech crown.

II. OVERVIEW OF MAIN MEASURES ADOPTED SINCE 1990

A. PENSION INSURANCE

● 1990 to 1992

- ✓ Discrimination of the self-employed persons was eliminated (in particular the social security of the self-employed was placed on the same level of social security of other gainfully employed persons) and preferences in the pension system were cancelled (the work categories and personal pensions were cancelled). These measures meant that nearly all of the persons economically active receive entitlement to pensions under uniform conditions and suitable conditions were thus created for further reform measures.
- ✓ The implementation of pension insurance and sickness insurance (sickness insurance was transferred from the capacity of trade unions, the Czech Union of Manufacturing Cooperatives [*Českého svazu výrobních družstev*] and regional national committees and was organizationally unified with pension insurance under one state authority – the Czech Social Security Administration, which was created by the Ministry of Labour and Social Affairs.).
- ✓ The rules for the valorization of pensions were implemented – the first systematic valorization measures were adopted which provided for the conditions and method of regularly increasing pensions.

● 1994

- ✓ Adoption of the Act on Supplementary Pension Insurance with a State Contribution. The Czech pension system is thus formed of two pillars – the basic compulsory pillar defined benefit and PAYGO and a second supplementary pillar defined contribution and funded by capital with state subsidised contributions, which also includes private life insurance.

● 1995

- ✓ Adoption of the Pension Insurance Act. The new legal provisions include such fundamental measures as the gradual raising of the retirement ages, the unification of the system, changes to the structure of

the calculation of pensions that, to a certain degree, react to developments in external factors. In addition, full (and partial) disability was newly defined in relation to the percentage-based reduction of the ability to continuously carry out gainful activities as a result of a long-term poor health, which does not enable the previous ‘professional’ and ‘estate’ disability. Moreover, in addition to the existing option of taking temporarily reduced old-age pension for up to two years earlier before reaching the retirement age (which was taken over from the current legislation) it is now possible to take a permanently reduced early old-age retirement up to three years before reaching the retirement age. The Pension Insurance Act presented a significant shift to practices common in the EU Member States (e.g. the entitlement to pensions is not subject to residency on the territory of the CR) and complies with EC law.

● 1996

- ✓ A special account was created for pension insurance as a part of the state financial assets. It enables the defining of the balance of the basic pension insurance albeit within the framework of the state budget. The funds on this account may only be used for increasing benefits or to cover deficit balances of premiums for pension insurance.

● 1997

- ✓ Under cost-saving measures, the crediting of all forms of non-contributory periods was limited and the conditions for the valorization of pensions were made more stringent.

● 1999

- ✓ An amendment to the State Subsidized Supplementary Pension Act was adopted which increased the security of deposits of participants and extended the possibilities of this form of supplementary insurance (increasing the contribution by the state, introduction of tax breaks for participants – employees and for the contributing employers, the setting of more strict conditions for supplementary pension insurance.

● 2001

- ✓ The actuarial rules (an increase of the reduction of the percentage-based assessment for early old-age retirement and delaying retirement

was made more advantageous) were taken more into account in setting the pension amounts.

- **2002**

- ✓ The regular increasing of pensions as of January of every year (in 2003 for the first time) was introduced and the conditions for increasing pensions were clarified so that the decisions on such increases could be made on the basis of final statistical data and not just on estimates of these indicators with the possibility raising pensions in exceptional circumstances when greater price increases occur.

- **2003**

- ✓ Effective 1 January 2004:
 - increases in the retirement age after 2007 up to reaching a uniform age level of 63 for men and childless women, whereby the retirement age for other women will remain differentiated based on the number of children brought up (59 to 62 years),
 - limiting the possibility of retiring before reaching the retirement age by cancelling temporarily reduced early old-age pensions (one of the two forms of early retirement),
 - reducing the crediting of studies for the purposes of pension insurance,
 - cancelling the condition enabling entitlement to the payment of old-age pensions concurrently with income from gainful activities during two years following entitlement to such a pension only when it does not exceed the prescribed level of income and introducing a condition of concluding a employment relation for no longer than one year (to date no such requirement existed),
 - the classification of, for the purposes of pension insurance, self-employed activities as 'main' and 'secondary'.
- ✓ An amendment to the Act on Supplementary Pension Insurance with a State Contribution was approved whose aim was primarily to achieve harmonisation with EU law.

- **2006**

- ✓ The system of reducing partial disability pensions or the suspension of their payment due to exceeding the set income levels from gainful activity was cancelled.

- ✓ The percentage-based assessment of pensions was increased by CZK 200 as of the day when its beneficiary reaches the age of 100.
- ✓ The adjustment of widower pensions or permitting their payment if the reduction of the amounts of these pensions or their non-granting occurred under legislation in effect prior to 1 January 1996 due to "concurrent maximums".

B. SICKNESS INSURANCE

- **1993**

- ✓ Spa care was transferred into the health insurance system.

- **1993 to 1994**

- ✓ Sickness benefits began to be granted for calendar days and were calculated from the average gross wages for the calendar year quarter preceding the insured event.
- ✓ The income decisive for participation in sickness insurance was increased from CZK 120 to CZK 400 per calendar month.

- **1995 to 1996**

- ✓ The transfer of child allowances, birth grant and death grant into the system of state social support; apart from sickness benefits, three other benefits continue to be provided under the sickness insurance system, which include the financial support for care of family members, maternity benefit and the pregnancy and maternity compensation benefit.
- ✓ Compulsory sickness insurance of the self-employed was changed to voluntary.

- **1999**

- ✓ The introduction of reduction limits for stipulating the amount of sickness benefits and their regular valorization (annually as of 1 January).

- **2002**

- ✓ The decision was made not to increase the reduction limit for setting the earnings decisive for the calculation of sickness insurance benefits in 2003 (in connection with the financial impact of the floods of 2002).

- **2003**

- ✓ Effective from 1 January 2004:
 - the decisive period used for determining the daily assessment base for setting sickness insurance benefits was extended from a calendar quarter to 12 calendar months,
 - the daily assessment base for the calculation of sickness benefits and financial support for care of family members for the first 14 calendar days of sick leave (quarantine) or for the purposes of financial support for care of family members was decreased from the current 100 % to 90 % for amounts up to CZK 480 (the first reduction limit),
 - sickness benefits for the first three calendar days of sick leave were reduced from 50 % to 25 %,
 - the period during which the reduction limits of the daily assessment base will not be increased to also include 2004 and 2005; these measures will also apply to the sickness welfare system in the armed forces.

- **2005**

- ✓ Effective from 1 January 2006, the reduction limits for determining the daily assessment base were increased as follows:
 - the amount CZK 480 was increased to CZK 510, and,
 - the amount CZK 690 was raised to CZK 730.

- **2006**

- ✓ A new Sickness Insurance Act was adopted, which will come into effect on 1 January 2007. The new Sickness Insurance Act and relating Act:
 - involves employers in the development of employee sick leave in that employers will pay wage compensation for the first 14 days of the sick leave,

- decreases the contribution rate for sickness insurance for employers from 3.3 % to 1.4 %,
- ensures greater equality of the amounts of sickness insurance benefits paid to insured persons for sickness insurance by increasing the number of reduction limits for the calculation of the daily assessment base from two to three,
- transfers the carrying out of sickness insurance from 'large organizations' to the sickness insurance authorities,
- strengthens protective elements against abuse of the system,
- decreased the penalty for outstanding amounts by half (from 0.1% to 0.05%).

C. PREMIUMS

- **1993**

- ✓ Social security premiums (pension insurance and sickness insurance) and contributions to the state employment policy were introduced in connection with tax reforms as special payments outside the tax system which form revenue of the state budget at a rate of 36 % of the assessment base (4.8 % for sickness insurance, 27.2 % for pension insurance and 3 % for the state employment policy).

- ✓ Effective from 1 January 1994, the total contribution rates for social security and contributions to the state employment policy were decreased from 36 % to 35 % of the assessment base (4.8 % for sickness insurance, 27.2 % for pension insurance and 3 % for the state employment policy).

- **1995**

- ✓ Effective from 1 January 1996, the total contribution rate for social security and contributions to the state employment policy were decreased from 35 % to 34 % of the assessment base (4.4 % for sickness insurance, 26 % for pension insurance and 3.6 % for the state employment policy).

- **2003**

- ✓ Effective from 1 January 2004:
 - the contribution rate for pension insurance increased by two per-

centage points (from 26 % to 28 % of the assessment base) and at the same time the contribution rate for state employment policy decreased by two percentage points (from 3.6 % to 1.6 % of the assessment base),

- there was a gradual increase in the minimum assessment base for setting premiums for the self-employed in 2004 to 2006 from 35 % to 50 % of the difference between income obtained and expenses incurred (40 % in 2004, 45 % in 2005),
- the categorization of the self-employed according to those persons carrying out 'main' and 'secondary' independent gainful employment; those carrying out 'main' independent gainful employment always participate in the pension system and thus must pay deposits on premiums regardless of the amount of their income and also have a higher assessment base than those carrying out 'secondary' independent gainful activity.

● 2006

- ✓ A new Sickness Insurance Act and accompanying act was adopted which amends certain acts relating to the adoption of the Sickness Insurance Act. Effective from 1 January 2007:
 - the contribution rate for sickness insurance is decreased from 3.3 % to 1.4 %, employers employing less than 26 employees insured under sickness insurance have the option of selecting a higher contribution rate for sickness insurance (3.3 % in 2007); in the event they make such a selection, the employer will be entitled to deduct from premiums half the amount of wage compensation for temporary sick leave of all his employees which he accounted for.

Additional information on pensions and sickness insurance benefits may be obtained on the Internet pages of the Ministry of Labour and Social Affairs and the Czech Social Security Administration at

www.mpsv.cz

www.cssz.cz

III. AGREEMENT OF THE POLITICAL PARTIES ON THE CONTINUATION OF PENSION REFORMS

(draft from DECEMBER 2005)

AGREEMENT

of the political parties represented in the Chamber of Deputies of Parliament on the continuation of pension reform

The political parties represented in the Chamber of Deputies of the Parliament of the Czech Republic (hereinafter "political parties"), knowing the long-term unsustainability of the pension system, have agreed on the adoption of these common principles on further measures for pension reform:

- Solidarity, continuous and state guaranteed basic pension insurance will continue to play a key role in ensuring the pension income of citizens.
- The existing gradual raising of the retirement age provided for under law will continue even after 2012 until it reaches 65 years. This should be achieved at the latest by 2036.
- A reserve will be created from the surpluses of the premiums on pension insurance and partially from the funds from privatization, which will be separate from the state budget.
- In order to maintain or increase the total replacement ratio, further development of supplementary pension systems will be supported by increasing the tax benefits for employees and employers or through state contributions. At the same time, participants in supplementary pensions will be able to request, after reaching the age of 60, the payment of the funds from 'supplementary pensions' in the form of a pension paid for an agreed time period (which will not be shorter than 5 years). The regular payment of the participant's funds will be more advantageous than the payment of a lump sum compensation.
- In order to increase transparency, the trustworthiness and security of the third pillar of pension system while preserving the maximum amount of equality of the relevant products, clients' access to sufficient information for their decisions on the selection of products should be provided for under law.

The political parties undertake to prepare on the basis of the above-mentioned common principles proposals for laws containing the relevant provisions of legislation in such a manner so that they may still be adopted prior to the elections to the Chamber of Deputies in 2006.

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