Actuarial Report on Social Insurance

2008

MLSA
Social Insurance Department

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INTRODUCTION

The actuarial report that you are examining, is already the fourth successive one and follows up on reports of 2002, 2004 and 2006. In this document the Social Insurance Department of the MLSA seeks to continue its previous efforts to provide high quality, objective and regular information to general professional and lay public on the development of social insurance in the Czech Republic. Although social insurance is basically stable and robust part of the social security system, even in this field relatively dynamic developments have been observed in the area of sickness and pension insurance. Consequently, this report includes not only statistical data for the last 5 years, but also analyses and projections of possible impact of currently discussed or proposed adjustments to the system.

The report is divided into three parts. Part A summarizes basic information on the system of social insurance including the key legislative changes since 2006. Part B contains an evaluation of the basic indicators of social insurance. The last Part C focuses on medium-term and long-term projections up to 2100, including projections of the impact of parametrical changes adopted as part of the first stage of the pension reform on the development of basic pension insurance indicators.

The report was drawn up by the Actuarial Unit of the Social Insurance Department of the Ministry of Labour and Social Affairs based on statistics provided in particular by the Czech Social Security Administration (CSSA) and its aim is to provide, as far as possible, objective information not only on current status of the system, but also on its possible future developments in the medium-term and long-term. Last, but not least, also on the basis of the described development trends suggest possible recommendations conducive to the system stability.

The MLSA and the whole team participating in the report preparation would be grateful for any suggestions or comments regarding this report.

Prague, October 2008

JUDr. Jiří Biskup
Director of the Social Insurance Department of
the Ministry of Labour and Social Affairs

PART A

GENERAL INFORMATION ON SOCIAL INSURANCE

A.1. BRIEF CHARACTERISTICS

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

A.1.1. PENSION INSURANCE[1]

The **key substantive legal provision** governing entitlement under compulsory pension insurance in the event of old-age, disability or death of a breadwinner is **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.

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 in pension insurance 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.

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[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 state contribution (Act No. 42/1994 Coll., on Supplementary Pension Insurance with 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.

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'**.

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,
- 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 Section 67 of the Pension Insurance Act and, effective from 1 July 2002,[2] 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%; effective from 28 May 2008 at least 5%),
- 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,

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[2] The following rules applied up to 30 June 2002:

- all paid out pensions are increased,
- the Government is authorized 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 amount of increases of the pensions.

- 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 period reach at least 10% and effective from 28 May 2008 at least by 5%; 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 [3]

The key act governing the scope of persons insured and the entitlement of insured persons is Act No. 54/1956 Coll., on sickness insurance, which has been frequently amended over more than 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 is basically, with only a few exceptions, **uniform** for all gainfully employed persons**.**[4]

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.

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[3] Apart from the state compulsory sickness insurance, there is a gradual development of voluntary insurance with insurance companies. Greater expansion is hindered on one hand 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.

[4] Members of the armed forces are entitled to sickness benefits only as of the second month of sickness, as they receive 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 family member care benefits 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 security corps are not entitled to family member care benefits.

The dynamic nature of the system is given by the annual updating of the reduction limits for earnings which are used for the calculation of benefits in accordance with wage developments[5].

Following the exclusion of health care in the 1950s, of spa centre treatment in 1993 and of child benefits, birth and funeral benefits 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 benefits**
- **family member care benefits,**
- **maternity benefits**
- **pregnancy and maternity compensation benefits.**

Sickness benefits are provided for calendar days. Since 1 January 2008 a three-week waiting period has been introduced, for which sickness benefits are not paid, however, it has been cancelled by the ruling of the Constitutional Court promulgated under Ref No. 166/2008 Coll. Since 1 September 2008 under Act No. 305/2008 Coll. the rate for calculation of sickness benefits for the first three calendar days of sick leave has been reduced from 60% to 25%, Sickness benefits are calculated from the average gross wages for twelve calendar months preceding the insured event. As from 1 January 2009 sickness benefits will be provided only from the 15th calendar day of temporary sick leave or the ordered quarantine.

The self-employed are not entitled to family member care benefits and to pregnancy and maternity compensation benefits.

A.1.3. PREMIUMS

The system of social insurance 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.

Legal provisions governing financing relations are provided for under **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 scope of contributors** (including contributions to the state employment policy),
- t**he 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 to the state employment policy are collected pursuant to this Act.

[5] In connection with the public budget reform 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, 2005 and 2007.

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 to generate, assure and maintain 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%).

In 2007 maximum annual assessment base for the self-employed was CZK 486,000. Effective from 1 January 2008, maximum annual assessment base for the payment of social security premiums and contribution to state employment policy for all contributors was set at 48 times the amount of the average wage in the national economy. For 2008, this maximum assessment base is CZK 1,034,880.

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 voluntary	1.6	29.6 or 34
Persons voluntarily insured under pension insurance	28	-	-	28

Source: MLSA

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

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 premiums for pension insurance, including penalties and fines relating to pension insurance and expenditure on pension insurance benefits, including expenditure related to the collection of premiums for pension insurance and payment of pension insurance benefits is transferred to this account[6] under chapter 313 of the Ministry of Labour and Social Affairs, chapter 307 of the Ministry of Defence, chapter

[6] The manner of calculation of the difference between revenues from premiums for pension insurance and expenditure on pension insurance and the method of calculation of expenditure associated with the collection of premiums for pension insurance and the payment of pension insurance benefits is stipulated by the Regulation of the Ministry of Finance. Administrative expenses in the budgetary chapter of the MLSA shall be calculated on the basis of the coefficient of administrative expenses of the CSSA as provided for by the Regulation. Administrative expenses of other social security authorities shall be calculated as the product of expenditure on pensions in the relevant budgetary chapter and the quotient of administrative expenses included in the budgetary chapter of the MLSA to expenditure on pensions in the budgetary chapter of the MLSA.

314 of the Ministry of the Interior, chapter 336 of the Ministry of Justice and chapter 312 of the Ministry of Finance. The funds collected in this account could be used only for expenditure on pension insurance benefits and transfers to the state budget to offset deficits arising from the difference between the above revenues and expenditure. Such use was possible only with consent from the Chamber of Deputies of the Czech Parliament. The funds could not be invested. Effective from 1 March 2008, the special pension insurance account was transformed to a special pension reform reserve account as a part of state financial assets. The Ministry of Finance every year, in which revenues from premiums for pension insurance, including penalties and fines relating to pension insurance are higher than expenditure on pension insurance benefits, including expenditure related to the collection of premiums for pension insurance and payment of pension insurance benefits, transfers to this account from the state budget the amount equal to the difference between the above income and expenditure. Revenues in this account are also comprised of funds credited to this account under special legal regulations. Also funds in the account of state financial assets, in which since 2004 resources from dividends obtained by the Ministry of Labour and Social Affairs, as the administrator of state ownership interests, are accumulated, are credited to this account. It is envisaged that the funds in the special pension reform account will be used for a pension reform, under the resolution of the Chamber of Deputies at the suggestion of the Government. The Ministry of Finance is entitled to invest temporarily available funds kept in this account into government bonds and bonds of the Czech National Bank, as well as into bonds issued by member states of the Organization for Economic Cooperation and Development, and bonds issued by central banks of these states or the European Central Bank. Revenues from investing activities constitute revenues of this account. Reports on management of funds in the account form part of the state final account.[7]

A.1.4. SOCIAL SECURITY ORGANIZATION AND IMPLEMENTATION

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 within the remits of social security authorities and organizations. Municipalities also carry out activities relating to social security.
- Social security authorities are:
  - Ministry of Labour and Social Affairs
  - Czech Social Security Administration (hereinafter CSSA),
  - District Social Security Administrations,
  - Ministry of the Interior
  - Ministry of Justice
  - Ministry of Defence

[7] Under Act No. 26/2008 Coll., amending Act No.218/2000 Colll. on budgetary rules and on amendment to certain related Acts (budgetary rules),as amended, and other related Acts, inter alia, Section 36 of budgetary rules was amended.

The administrator of insurance for the "civilian 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 implementation of pension and sickness insurance, performing doctor appraisal services, the collection of premiums and fulfilling obligations ensuing from international conventions and EC law. 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. Thereby the basis was established for regularly informing insured persons of data 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'). CSSA has put in place electronic filing options via the Internet by means of the Public Administration Portal or memory media. CSSA clients may make use of several types of electronic filings. They may file electronically pension insurance statements, pension insurance registrations and deregistrations of employees and the Statement of Income and Expenditure of self-employed persons.

A.2. LEGISLATIVE CHANGES SINCE THE BEGINNING OF 2006

A.2.1. PENSION INSURANCE

(A) Legislative changes that have come into effect

- **Act No. 267/2006 Coll.** - effective from 1 July 2006. The Act regulates the amount of widow pension for widows who became entitled to this pension before 1 January 1996 and due to fixed maximum limits applicable to concurrent pensions under previous regulations its amount was limited, or its payment permitted if the widow pension had not been paid.
- **Government Decree No. 461/2006 Coll.** - effective from 1 January 2007. As of January 2007, the basic amount of pensions was increased to CZK 1,570 and the percentage-based assessment of paid out pensions granted prior to 1 January 1996 was increased by 6.6% of the percentage-based assessment and the percentage-based assessment of pensions granted from 1 January 1996 to 31 December 2006 by 5.6%.
- **Government Decree No. 462/2006 Coll.** - effective from 1 January 2007. The decree set the general assessment base for 2005 (CZK 18,809), raised the reduction limits to CZK 9,600 and CZK 23,300 respectively, and set the conversion coefficient for adjusting the general assessment base for 2005 (1.0707).
- **Act No. 152/2007 Coll.** - effective from 1 July 2007. This Act reflected into the legal regulation the ruling of the Constitutional Court of 6 June 2006 promulgated under Ref. No. 405/2006 Coll. A change in the legislative regulation consists basically in the fact that the time (period) of care needs to be proved by all insured persons, i.e. both men and women in the same manner, namely by an affidavit submitted together with the application for pension (under previous legislative

- **Government Decree No. 256/2007 Coll.** - effective from 1 January 2008. As of January 2008 the basic amount of pensions was raised to CZK 1,700 and the percentage-based assessment for paid out pensions by 3%.
- **Government Decree No. 257/2007 Coll.** - effective from 1 January 2008. The decree set the general assessment base for 2006 (CZK 20,050), raised the reduction limits to CZK 10,000 and CZK 24,800 respectively, and set the conversion coefficient for adjusting the general assessment base for 2006 (1.0753).
- **Act No. 261/2007 Coll.** – effective from 1 January 2008. The Act extended the scope of persons participating in the basic pension insurance through the institute of non-contributory insurance periods, namely for people caring for a person under the age of 10 who is dependent on the care of another person, degree I.
- **Act No. 178/2008 Coll.** – effective from 28 May 2008. The Act provided for the condition for raising the pensions in an extraordinary term already if prices increase by at least 5% (previously, this provision applied only if prices increased by at least 10%). At the same time, the Act stipulated that in 2008 pensions would be increased, apart from the regular term, from the pension benefit payment due in August 2008.
- **Government Decree No. 211/2008 Coll.** – effective from 1 August 2008. As of August 2008, the basic amount of pensions granted before 1 August 2008 was increased to CZK 2,170; basic amount of pensions granted after 31 July 2008 was CZK 2,170 per month.
- **Act No. 306/2008 Coll.** – effective basically from 1 January 2010. Under the Act, in particular measures containing parametrical changes to the basic pension insurance were incorporated into the legislative regulation [for more details see Part (B) Approved Conceptual Changes].

(B) Approved conceptual changes to the basic pension insurance prepared as part of the 1st stage of the pension reform and further continuation of the pension system reform

Act No. 306/2008 Coll., amending Act No. 155/1995 Coll., on pension insurance, as amended, Act No. 582/1991 Coll. on social security organization and implementation, as amended, and certain other Acts, was approved by the Parliament on 17 July 2008 and will come into effect, basically as from 1 January 2010.

The most important approved changes, compared to the current legislation include:

- gradual extension of the insurance period required for entitlement to the old age pension from 25 years to 35 years, including non-contributory periods[8] or to 30 years without non-contributory periods,

- gradual limitation on crediting of non-contributory insurance periods also for entitlement to the old-age pension to 80%, except for these periods due to personal care for a child up to the age of 4, or care for a person who is dependent on care of another person and former compulsory military service,

- uninterrupted continuation of gradual increasing of the retirement age to 65 years for men and women who have not brought up any child or one child and 62 to 64 years for women (according to the number of brought up children), if they have brought up at least two children and in this connection also the age limit for entitlement to the old-age pension if shorter insurance period is acquired,

- gradual extension of the period for early retirement from three to five years,

- cancellation of the condition for entitlement to the payment of the old-age pension benefits, in addition to income from gainful activities which consists in negotiating the employment for a period of at least one year,

- increasing the percentage-based amount of old-age pension for a period of gainful activity after becoming entitled to old-age pension, with concurrent receipt of this pension in full amount, namely by 0.4% of the calculation base for every 360 calendar days or in the case of receipt of half the amount of this pension, namely by 1.5% of the calculation base for every 180 calendar days,

- change of full disability pension to old-age pension in the same amount when reaching the age of 65,

- unification of the existing fixed age limit for “permanent” entitlement of women to widow pension (currently at the age of 55) and men to widower pension (currently at the age of 58) to the age by 4 years lower than the retirement age for men with the same date of birth,

- new definition of disability (introduction of a three-degree disability), with "permanent” protection of the amount of previous partial disability pensions in cases where the 2nd degree of disability is changed to the 1st degree (previously, there

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[8)] Non-contributory periods are periods that are counted (credited) for the purposes of basic pension insurance, despite the fact that neither premiums are paid, nor other payments are contributed during such periods – e.g. the period of care for a child up to the age of 4, the period of personal care for a person dependent on the care of another natural person, time of "registered" unemployment, etc.

were two types of disability pensions: full disability pension and partial disability pension),

- unification of the age limit, for which the so-called additional recalculated period [9)] is ascertained for the purpose of determining the amount of the percentage-based assessment of disability pension for men and women (for men and women the retirement age set for women with the same date of birth who have not brought up any child),
- cancellation of the period of studies acquired in the period after the effective date of the Bill as a non-contributory insurance period, except for considering the entitlement to disability pensions

- increasing the reduction of the percentage-based assessment in the case of early retirement, starting from the third year.

The adoption of the above measures was preceded by the conclusion of the Coalition Agreement between the Civic Democratic Party (ODS), the Christian Democratic Party – the Czechoslovak People's Party (KDU-ČSL) and the Green Party after the election for the Chamber of Deputies of the Czech Parliament in 2006. The policy programme part of this agreement and the subsequently adopted policy statement contain, inter alia, also the intention to implement the pension reform in three stages.

By way of the above legislative regulation, the 1st stage of the pension reform which has been prepared by the MLSA with a view to contributing in particular to better financial sustainability of the basic pension insurance and eliminating some microeconomic inefficiencies and thereby ensuring its long-term stability, is being implemented. The relevant changes pertain to the expenditure side of the basic pension insurance and can be divided into a part relating to the insurance period and the non-contributory period (the period for which no premium is paid), a part relating to the amount of pension, a part relating to the conditions for entitlement to payment of pension and a part relating to a change in the definition of disability.

As far as the 2nd stage of the pension reform is concerned, changes were prepared and will continue to be prepared in respect of both the public basic pension insurance (in particular the creation of a reserve for the pension reform) and private pensions (separation of the assets of shareholders and clients, introducing the option of providing pension plans with various focus, boosting incentives for higher contributions, increasing the participation of employers, support for drawing annuity pensions from the supplementary pension insurance). The Government on 27 June 2008 discussed the document prepared by the Ministry of Finance and the Ministry of Labour and Social Affairs which informed about fufilment of the tasks within the 2nd stage of the pension reform and charged the Minister of Finance with the task to secure, in collaboration with the Minister of Labour and Social Affairs, drawing up of principal points for drafting of the new Act on Supplementary Pension Insurance and

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[9)] Additional recalculated period is the period from the date of entitlement to full disability or partial disability pension to reaching the retirement age – this period is counted (credited) in the same manner as the insurance period on account of gainful activity.

submit them to the Government by the end of September 2008 (Government Resolution No. 737).

As part of the 3rd stage of the pension reform intensive negotiations will be held with the aim to reach consensus on diversification of resources for income for older people, with the option of reallocating a small portion of mandatory payments of premium for the basic pension insurance based on a voluntary decision of the insured person into the private system (introducing the possibility of opting-out). Insured persons would be given the opportunity of choosing whether their pension will be derived from the state basic pension insurance only or partly also from the new savings pillar of the pension system. Consequently, the insured persons would not choose whether they will pay contributions to the old-age pension insurance or not but only what sources of financing for their future pensions they will use.

A.2.2. SICKNESS INSURANCE

(A) (A) Legislative changes that have come into effect

- **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.

- **Government Decree No. 588/2006 Coll.** –effective from 1 January 2007. This Decree adjusted the amounts for determining the daily assessment base as follows:
  - the amount of CZK 510 was increased to CZK 550, and
  - the amount of CZK 730 was increased to CZK 790.

- **Act No. 261/2007 Coll.** – effective from 1 January 2008. The changes consist in particular in:
  a) the establishment of participation in sickness insurance of employees in the employment relationship since also the day before commencing their employment, for which they are entitled to wage (salary) compensation or for which their wage or salary is not reduced is considered to be the day of commencement of their employment,
  b) introducing the waiting period for the provision of sickness benefits, i.e. the provision of no sickness benefits for a period of the first three calendar days of temporary sick leave or the ordered quarantine,
  c) not increasing reduction limits for the adjustment of the daily assessment base for 2008,
  d) retaining the reduction of income up to the level of the first reduction limit for the calculation of sickness benefits and family member care benefits even after the 14th day of duration of the social event, for which there is entitlement to these benefits,

e) adjusting the percentage rates of the daily amount of sickness benefits and family member care benefits; sickness benefits after reduction of the daily assessment base, from the 4th day to the 30th day of temporary sick leave (quarantine) amount to 60% of the daily assessment base (DAB), from the 31st to 60th day 66% of the DAB and from the 61st day 72% of the DAB, family member care benefits amount to 60% of the daily assessment base after its reduction,

f) reducing the supported period for which sickness benefits are provided to beneficiaries of old-age and full disability pensions on account of sick leave due to sickness or other than industrial accident, from 84 to 81 calendar days,

g) limiting the supported period for the provision of sickness benefits and family member care benefits for employees who are beneficiaries of old-age or full disability pensions, for a period of the duration of employment,

h) reducing the protected period; the general length of the protected period of 42 calendar days was reduced to 7 calendar days,

i) cancellation of entitlement to family member care benefits from the protected period,

j) cancellation of entitlement to maternity benefits on account of seeking a job; job-seekers are not participating in sickness insurance on account of being kept in the register of job-seekers with the Labour Office and therefore are not entitled to sickness benefits, but rather to the state social support benefit or parental benefit,

k) cancellation of the lone status as a necessary prerequisite for extension of the provision of maternity benefits from 28 to 37 weeks,

l) using the daily assessment base determined for the calculation of the previous maternity benefits for the calculation of further maternity benefits; as a necessary prerequisite, a female employee must start next maternity leave while the same employment lasts at the time when her previous child is not older than 4 years and her previous daily assessment base before reduction is higher than the daily assessment base determined for further maternity benefits.

- **Act No. 305/2008 Coll.,** amending Act No. 187/2006 Coll., on Sickness Insurance (the Sickness Insurance Act), as amended and certain other Acts,

  – effective from 1 September 2008 introduces in particular the following changes:

a) decreasing the rate for calculation of sickness benefits for the first three calendar days of sick leave from 60% to 25%,

b) insured persons are entitled to sickness benefits even in the case of a quarantine shorter than 4 days,

c) regular soldiers and members of security corps are entitled to sickness benefits for the first 3 calendar days of incapacity for service

  – Effective from 1 January 2009:

a) the Sickness Insurance Act in particular simplifies the implementation of sickness insurance and removes legislative discrepancies,

b) under “special regulations“ in particular wage (salary) compensations for bonuses, reduced salaries and bonuses for the first 3 working (or calendar) days of duration of the ordered quarantine are awarded.

(B) <u>Approved conceptual changes</u>

The MLSA drafted in compliance with the Government Policy Statement of August 2002, new Bill on Sickness Insurance.

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

c) securing economically active citizens with short term monetary benefits in certain short-term situations,

d) uniformity of the system whereby participation will be obligatory for employees and voluntary for the self-employed,

e) limiting solidarity amongst persons with higher and lower incomes (reinforcement of insurance elements),

f) limiting solidarity between employers by partially (gradually) privatizing the system,

g) strengthening the protective elements of the system to prevent its abuse,

h) revenues from premiums and expenditure on benefits will essentially be balanced,

i) employers will also contribute to financially securing employees during sick leave,

j) 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:

k) 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,

l) decreasing the rate for sickness insurance premiums for employers from 3.3% to 1.4%,

m) 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,

n) transferring the implementation of sickness insurance from large organizations to sickness insurance authorities,

o) strengthening protective elements against abuses of the system,

p) decreasing the penalty rate by half (from 0.1% to 0.05%).

The CSSA’s preparations for implementing the Act will necessitate an increase in personnel and funding.

Under Act No. 585/2006 Coll., the effective date of Act No. 187/2006 Coll., was deferred by one year and therefore it had to come into effect on 1 January 2008. However, the Act did not take effect, since under Act No. 261/2007 Coll., its effective date was deferred again, namely to 1 January 2009.

A.2.3. PREMIUMS

(A) (A) Legislative changes that have come into effect

On 1 January 2007 **Act No. 264/2006 Coll.** (the accompanying act to the new Labour Code), that has significantly changed the criteria for crediting the income of employees into the assessment base for the payment of premiums for social security insurance, came into effect. The following earnings will be credited into the assessment base:

q) earnings that the employer attributed to the employee in connection with the employment covered by sickness insurance, and

r) are subject to personal income tax on employment-related activities, and

s) are not included on the list of non-creditable income (e.g. severance pay, compensation for damage).

Under Act No. 261/2007 Coll., on stabilization of public budgets, effective from 1 January 2008 further changes were made to creditability of income into the employee's (and hence also the employer's) assessment base for payment of premiums for social security and contribution to the state employment policy. From 1 January 2008, included in the employee's assessment base are also incomes that prior to 1 January were excluded since such incomes were not attributed (settled) by the employer to the employee, i.e. the value of supplies was not recorded in the relevant employer's accounts as an expense or outflow of resources. Furthermore, incomes not creditable to the employee's assessment base were further supplemented and specified.

Effective from 1 January 2008, the maximum annual assessment base for the payment of premiums for social security and contribution to the state employment policy for all contributors was set at 48 times the amount of the average wage in the national economy. For 2008, this maximum assessment base amounts to CZK 1,034,880.

(B) Approved and proposed changes

Approved changes

Changes in premiums will be made in connection with

- the new Sickness Insurance Act (Act No. 187/2006) whose effective date has been deferred to 1 January 2009 (see Chapter A.2.2)
- the Bill to amend Act No. 187/2006 Coll., on Sickness Insurance, as amended (the Sickness Insurance Act), under which it has been proposed to reduce premiums for sickness insurance, in particular for employees and the self-employed by 0.1 percentage points whereby the non-provision of wage compensation or another supply over a period of the first 3 calendar days of

sick leave due to sickness or other than industrial accident or the ordered quarantine is compensated for.

Proposed changes

- together with the proposed tax changes, it has been proposed to reduce with effect from 1 January 2009 premiums for social security and contribution to the state employment policy for employees and the self-employed by 1.5 percentage points.

PART B

EVALUATION OF THE BASIC INDICATORS OF SOCIAL INSURANCE DEVELOPMENTS

B.1. PARAMETERS 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

Since 2003, there was a gradual acceleration in the rate of economic growth whereby between 2005 and 2007 there was the greatest rate of real GDP growth in the history of the independent Czech Republic amounting to 6.3%, 6.8%, or 6.6%. The Ministry of Finance is expecting a slight decline in the rate of growth for 2008 to a level of 4.6%[10].

Table 2 GDP development

Year	GDP	Annual growth rate in fixed prices	Rate per inhabitant (calculated using the purchasing power parity)	
	(CZK billion)	(%)		EU 12 = 100
2003	2,577	3.6	15,200	66
2004	2,815	4.5	16,300	68
2005	2,984	6.3	17,100	69
2006	3,216	6.8	18,400	71
2007	3,551	6.6	20,300	74

Source: MF

For the first time since 1990, in 2003 there was a year-on-year decrease in the price level. Hence, the average inflation rate reached 0.1% in 2003 and was the lowest since 1987. In following years, inflation ranged from 2.5% to 2.8%, except for 2005 when it reached the level of 1.9%. It is expected that there will be an increase in the price levels in 2008 up to 6.1% due to extraordinary developments at the end of 2007 and administrative changes relating to the Act on stabilization of public finances.

[10] Macroeconomic forecast for the Czech Republic – July 2008

Nominal value of the average gross wage in the national economy[11] (civilian sector, i.e. exclusive of wages of employees of the Ministry of the Interior and the Ministry of Defence) grew year-on-year in 2003 – 2007 by 6.7 %, 6.7 %, 5.2 %, 6.6 % and 7.4 %. However, due to the above growth in prices, **the real value of the average gross wage** in the national economy grew by 6.6 % in 2003 and in subsequent years by 3.8 %, 3.3 %, 4.1 % and 4.5 %. The growth in the real value of the average wage in the national economy was since 2004 lower 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
2003	16,769	12,807	6.7	6.1
2004	17,882	13,601	6.7	6.1
2005	18,809	14,252	5.2	4.8
2006	20,050	15,506	6.6	8.7
2007	21,527	16,509	7.4	6.5

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 premiums for health and social insurance.

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 the stagnation in 2001-2003, since 2004, this proportion has further gradually risen. **The demographic development after 1990 was relatively positive in terms of economic burden on the productive element of the population, even though the share of persons aged 65 and more increased and the population as a whole aged.** However, the economic burden index[12] continued to fall steadily in this period up to 2006 from a value of 50 in 1991 up to 40.4 in 2006. In 2007, it amounted to 40.5.

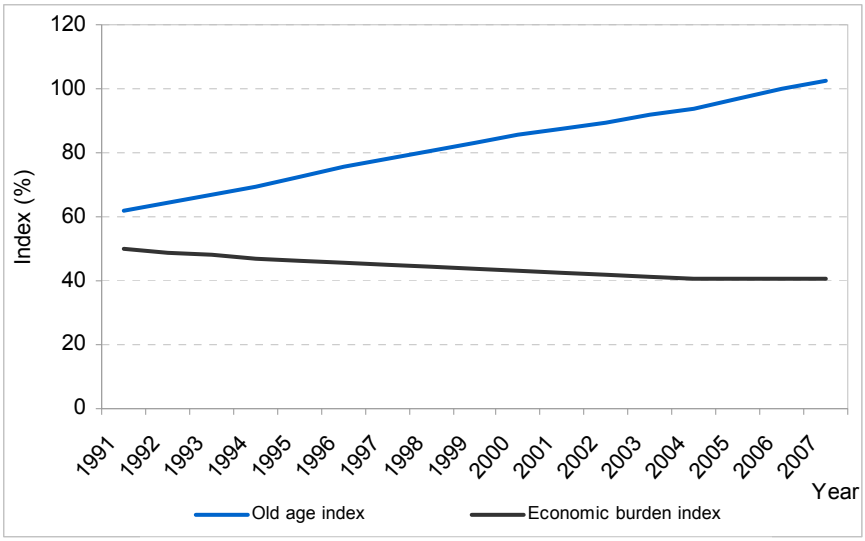
Table 4 Age structure of the population

Year	Age group 0-14 years		15-64 years		65 and more years		Total
	(thous. pers.)	(% of pop.)	(thous. pers.)	(% of pop.)	(thous. pers.)	(% of pop.)	(thous. pers.)
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	14,6	7,293	71.2	1,457	14.2	10,251
2006	1,480	14,4	7,325	71.2	1,482	14.4	10,287
2007	1,477	14,2	7,391	71.2	1,513	14.6	10,381

Source: CSO

[11] The average gross wage is further defined as the general assessment base (Section 17 para 2 of Act No. 155/1995 Coll.) promulgated by Government Decree in the amount of the average monthly wage in the national economy, as ascertained by the Czech Statistical Office (average monthly wage for economic entities having 20 and more employees in the commercial sector and in all organizations of the non-commercial sector, excluding armed forces). For 2007, the amount of the general assessment base is estimated.

Graph 1. Old-age index and economic burden index[12]



Source: ♠CSO

The total demographic structure is affected especially by a low birth rate and increases in life expectancy. While life expectancy at birth for 2003-2007 for men grew by 1.7 years (1.4 years for women), upon reaching the age of 60 it was 1.2 years for men and 1 year for women and upon reaching the age of 65 it was 1.2 years for men and 1.1 years for women. The effect of foreign migration on the structure and size of the Czech Republic's population is marginal.

Table 5 Total fertility rate, life expectancy

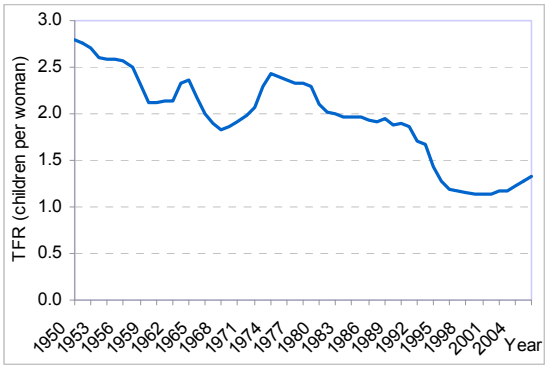
Year	Total fertility rate	Life expectancy (number of years)					
		At birth		At 60 years		At 65 years	
		Men	Women	Men	Women	Men	Women
2003	1.18	72.0	78.5	17.2	21.3	13.8	17.1
2004	1.23	72.6	79.4	17.6	21.6	14.2	17.5
2005	1.28	72.9	79.1	17.8	21.7	14.4	17.6
2006	1.33	73.5	79.7	18.2	22.1	14.8	18.0
2007	1.44	73.7	79.9	18.4	22.3	15.0	18.2

Source: CSO

At the turn of the 20th and the 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.

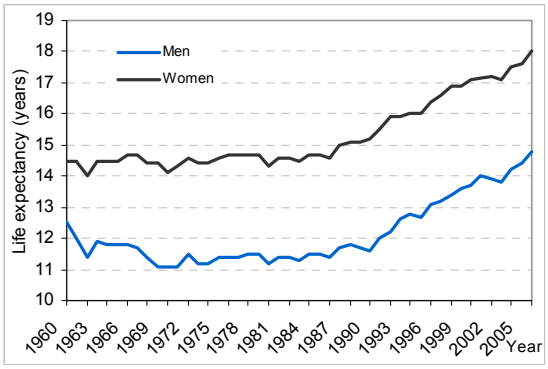
[12] Old-age index = number of persons aged 65 and more per 100 persons aged 0– 14.
Economic burden index = number of persons aged 0-14 and 65 and more per 100 persons aged 15 – 64

Graph 2. Developments in total fertility rate



Source: MLSA

Graph 3. Developments in life expectancy at 65



Source: MLSA

B.1.3. EMPLOYMENT DEVELOPMENTS

An important aspect of employment in the Czech Republic is the fact that the population is ageing while this ageing process is, for the time being, reflected in the growth of the number of persons of an economic active age. However, this trend is significantly affected by a decreasing participation rate, which has been gradually falling since 1999 to almost 69% for men and approximately 50% for women. A positive shift has, however, occurred with the older age groups where the participation rate has begun to increase significantly since 2000.

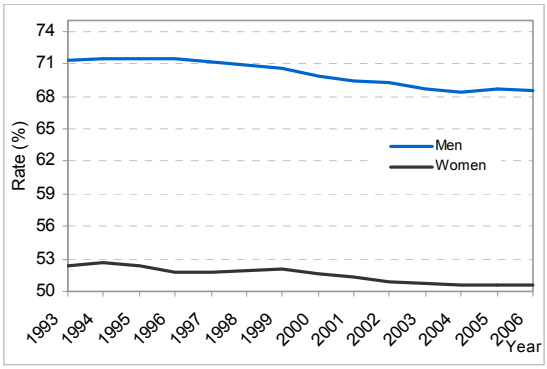
Table 6 Participation rate

Year	55-59 years	60-64 years	55-64 years	Total	Total Men	Women
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
2006	66.7	23.8	47.7	59.3	68.6	50.5
2007	66.9	26.4	48.2	58.8	68.3	49.8

Source: CSO

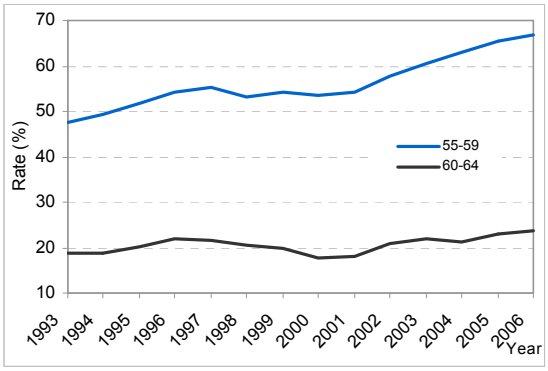
According to the Labour Force Sample Survey, the unemployment rate has been after 2004 **gradually decreasing** while the rate of lowering the unemployment rate has been increasing. In 2007 the unemployment rate was 5.3% (compared to 8.3% in 2004). In subsequent years the trend of declining unemployment rate should further continue.

Graph 4. Participation rate – in total



Source: CSO

Graph 5. Participation rate of older persons



Source: CSO

B.2. SOCIAL INSURANCE INDICATORS

B.2.1. PREMIUMS

Revenues from premiums for social security and contribution to the state employment policy constitute about 35% of all state budget revenues and cover approximately 70% of all social 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 has had a rising trend since 2000. In 2006, the number of contributors increased by 50,000 (year-on-year increase by some 1%) and in 2007 by 92,000 (about 2%). The ratio of the self-employed to the number of insured persons has been decreasing over the last two years from 15.3% in 2005 to 14.6% in 2006 and 14.4% in 2007.

Table 7 Number and structure of insured persons

Year	Employees			Self-employed	Total
	Total	Organizations	Small organizations		
			Number (thousands persons)		
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
2006	4,162	3,194	967	714	4,876
2007	4,254	3,267	987	714	4,968
			Proportion of the total number of insured persons (%)		
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
2006	85.4	65.5	19.8	14.6	100.0
2007	85.6	65.8	19.9	14.4	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 the 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 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 incurred to generate, assure and maintain such income and it may not be lower than the prescribed minimum, which is determined as ¼ of the general assessment base in the year preceding by two years the year for which it is determined, multiplied by the conversion coefficient. In 2008, the minimum for the

self-employed carrying out main activities amounted to CZK 5,390 per month and for the self-employed carrying out secondary activity (i.e. for part- -time self-employed) it was CZK 2,156 per month. The self-employed shall pay their premiums always, whereas the self-employed carrying out secondary activity do so, if their annual income less expenses is higher than 2.4 multiple of the general assessment base for the year preceding by two years the year for which it is determined multiplied by the conversion coefficient (CZK 51,744 in 2008).

Minimum premiums for social security and the contribution to the state employment policy for the self-employed are set out in the following table:

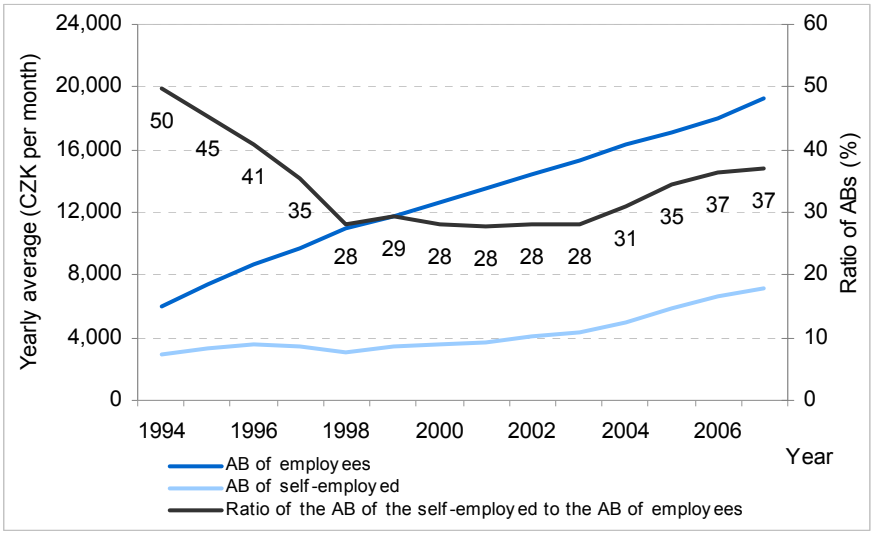
Table 8 Minimum premiums for social security and the contribution to the state employment policy for the self-employed

Year	Minimum assessment base	Minimum premium for			
		pensions	employment	pensions and employment	sickness benefits
		28.0%	*1.6%*	*29.6%*	*4.4%*
Self-employed MAIN ACTIVITY					
2004	3,368	944	54	997	149
2005	4,024	1,127	65	1,192	178
2006	4,709	1,319	76	1,394	208
2007	5,035	1,410	81	1,491	222
2008	5,390	1,510	87	1,596	238
Self-employed SECONDARY ACTIVITY					
2004	1,684	472	27	499	75
2005	1,789	501	29	530	79
2006	1,884	528	31	558	83
2007	2,014	564	33	597	89
2008	2,156	604	35	639	95

Source: MLSA

A comparison of developments in the amount of the assessment base for premiums of employees and the self-employed for the period 1994 – 2007 is reflected in the following graph.

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



Source: CSSA
Note: AB = assessment base

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 since 2004 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 and in 2007 was at 37.1%. The change of the premium amount is supposed to, inter alia, also raise the level of benefits so that some self-employed are not at risk of poverty in old-age.

The average assessment base for the payment of premiums (Table 9) is consistently lower than the average wage. In 2006 and 2007 the assessment base for the payment of premiums of employees of organizations was approximately 5% lower than the average wage. 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 2007, the average assessment base of employees of organizations and small organizations from which premiums were paid amounted to CZK 19,274, which was CZK 1,261 (7.0%) more than in 2006. In 2007, the self-employed paid premiums on average from an assessment base of CZK 7,149 which is 8.6% higher than in 2006 when the assessment base amounted to CZK 6,580.

The growth of the assessment bases from which premiums are paid together with changes in the number of contributors (in 2006 by 1.0% and in 2007 by 1.9% resulted in a year-on-year increase in the amount of premiums by 7.4% in 2006 and 10.1% in 2007.

Table 9 Average assessment base for premiums

	2003	2004	2005	2006	2007
Average assessment base for employees (CZK/month)					
- employees of organizations	16,178	17,213	18,045	19,013	20,373
- employees of small organizations	12,553	13,321	13,936	14,714	15,636
- employees in total	**15,334**	**16,300**	**17,081**	**18,013**	**19,274**
- self-employed insured under pension insurance	4,300	5,028	5,914	6,580	7,149
- self-employed insured under pension insurance/employees in total (%)	28.0	30.8	34.6	36.5	37.1
Average wage in the national economy (CZK/month)	**16,769**	**17,882**	**18,809**	**20,050**	**21,527**
Difference in the average assessment base of employees and the average wage in the national economy (CZK/month)	-1,435	-1,582	-1,728	-2,037	-2,240
Proportion of the average assessment base of employees and the average wage in the national economy (%)	91.4	91.2	90.8	89.8	89.6

Source: CSSA, MLSA

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

In 2007, the total prescribed premiums including fines and penalties amounted to CZK 353.5 billion and total revenues including fines, penalties and premium surcharges (accessories) amounted to CZK 357.2 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 2007, the contribution compliance amounted to 101.0%, which is by 0.2 percentage points more than in 2006, when the contribution compliance exceeded 100 % as a result of the recovery of outstanding receivables.

In 2007, CZK 357.2 billion was collected in premiums, excluding fines, penalties and premium surcharges. Of this amount, 82.9% (CZK 295.9 billion) was earmarked for pension insurance, 12.4% (CZK 44.3 billion) for sickness insurance and 4.7% (CZK 16.9 billion) for the state employment policy. The total amount of prescribed premiums, excluding fines and penalties for all three areas of social insurance was set at CZK 353.8 billion.

In 2007 write-offs of waived penalties and write-offs of bad debts were significant. For this reason, the amount of prescribed premiums, including fines and penalties was lower than the amount of prescribed premiums, excluding fines and penalties. In order to ensure an objective evaluation of the contribution compliance, the total contribution compliance needs to be adjusted for written-off bad debts. Such write-offs reduce the total amount of prescribed premiums for a given year despite the fact that old receivables are concerned. The contribution compliance that would reflect written-off receivables would be by 1.0-1.5 percentage points lower.

Table 10 Comparison of prescribed premiums and payments from 2003 to 2007

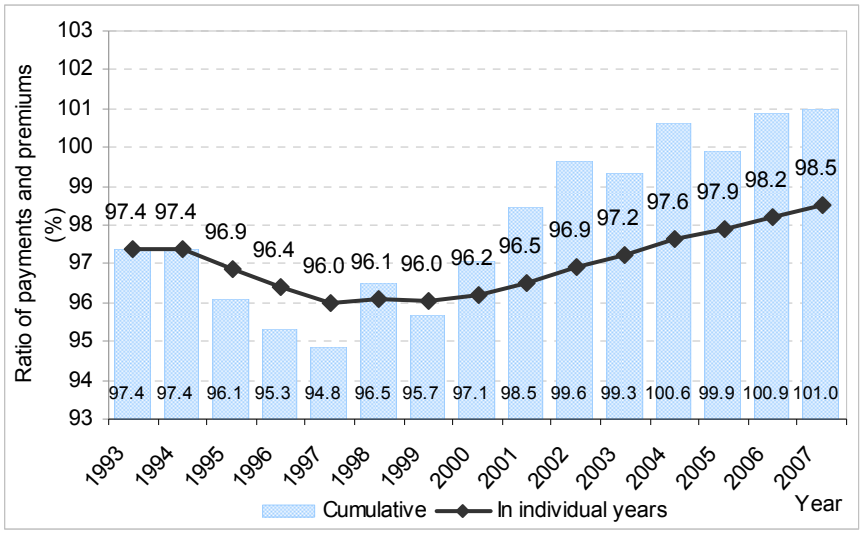
Year	Premiums including fines and penalties			Premiums excluding fines and penalties		
	Prescribed (CZK billion)	**Collected** (CZK billion)	**Contribution compliance** (%)	**Prescribed** (CZK billion)	**Collected** (CZK billion)	**Ratio of collected/ prescribed** (%)
2003	265.9	264.2	99.4	262.2	262.1	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
2006	321.4	324.3	100.9	321.8	324.3	100.8
2007	353.5	357.2	101.0	353.8	357.2	101.0

Source: CSSA

In 2006, fines, penalties, premium surcharges and other revenues amounted to 59 million and in 2007 to CZK 41 million, therefore, the data on the contribution compliance, including fines and penalties, on one hand and excluding fines and penalties on the other do not differ much.

The reported data assess contribution compliance in respect of the submission of statements and payments of the already registered companies and the self-employed. They disregard potential significant number of employees/workers who are not registered, or, where appropriate, organizations that employ their employees illegally or undervalue wages and salaries of their employees.

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



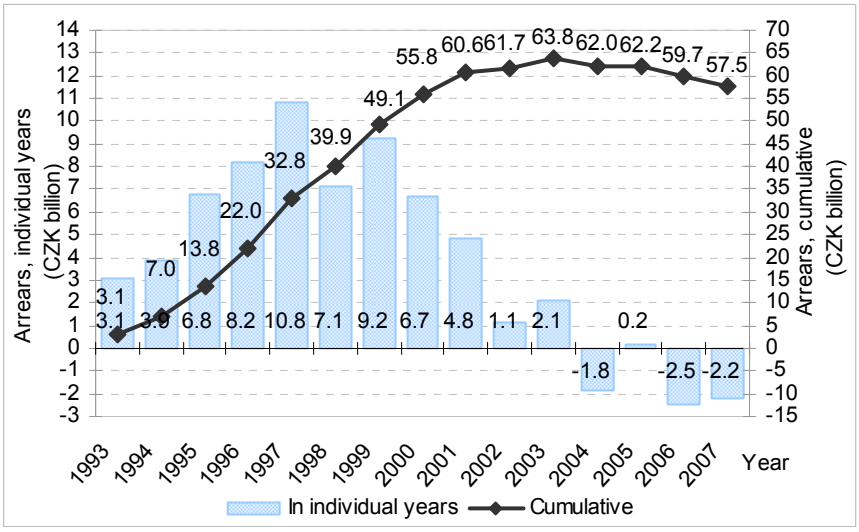
Source: CSSA

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 1993[13] to December 2007, a total of CZK 3,427 billion in premiums (including fines and penalties) was prescribed. In the same period, the balance of arrears (including fines and penalties) amounted to CZK 57.5 billion. Therefore the amount of debt was approximately 1.7% of the total amount of prescribed premiums and 1.6% of the GDP in 2007. In 2006, receivables dropped by CZK 2.5 billion compared to previous year and in 2007 decreased by additional CZK 2.2 billion. The above reported amounts reflected also write-offs of waived penalties and write-offs of bad debts.

Graph 8. Development in arrears (CZK billion)



Source: MLSA

Structure of receivables from contributors

As at 31 December 2007 receivables from deregistered entities amounted to CZK 35.3 billion. (61% of total receivables), receivables from current contributors CZK 21.4 billion (37% of total receivables), and receivables in approved instalments amounted to CZK 0.8 billion (2% of the total).

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

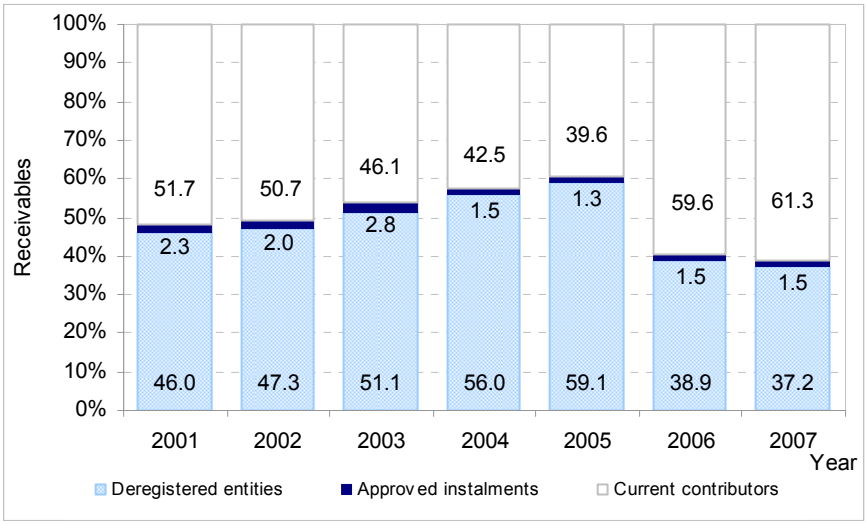
[13] On 1 January 1993 Act No. 589/1992 Coll., on Premiums for Social Security and Contribution to the State Employment Policy came into effect.

Table 11 Structure of receivables from contributors (CZK million)

Balance of receivables as at 31 December	2005	2006	2007
Total	62,180	59,721	57,488
Deregistered contributors	36,777	35,604	35,261
Approved instalments	781	917	873
Current contributors	24,622	23,199	21,354

Source: CSSA

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



Source: CSSA

B.2.2. PENSION INSURANCE[14]

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:

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

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 equation no. 1 as follows, the relationship for the main parameters of balanced accounts may be obtained: the contribution rate, the replacement ratio (the relation between the average pension and the average

[14] More detailed data are available from the Statistical Yearbook in the field of pension insurance published by the CSSA.

wage in the national economy) and the relation between the number of insured persons and the number of pensioners

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

The development of 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. This section discusses in particular the development of expenditure on pension insurance, relations between revenues and expenditure, development of the number of pensioners and pensions, pension amounts and their differentiation.

B.2.2.1. Revenues and expenditure[15]

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%. Significantly lower surplus of revenues over expenditure in 2006 (in Chapter 313 of MLSA) was caused by the fact that in this year, an increase in the number of insured persons was lower, the number of pensioners increased significantly and there was also a significant increase in the balance of advances paid to post offices, since the CSSA failed to pay to the Czech Post at the end of 2005 the usual advance for payment of pensions in the first days of 2006 and this expenditure (in the amount of some CZK 4 billion) was reported only in 2006.

Table 12 Pension insurance revenues and expenditure on pensions (CZK billion) (Chapter 313 – MLSA)

Year	Revenues [1)]	Expenditure [2)] on benefits	Revenues - Expenditure [3)]
2003	202.8	220.3	-17.6
2004	235.8	225.2	10.6
2005	250.1	241.2	8.9
2006	268.4	266.2	2.2
2007	295.9	282.6	13.3

Source: State final accounts
Notes: [1)] Including fines, penalties and voluntary supplementary insurance.
[2)] Not including advances paid in the previous year but including advances paid for the following year, excluding operating costs.

Pension insurance revenues and expenditure on pension insurance benefits in Chapter 313 – MLSA affect significantly the level of funds recorded in the special pension insurance account (see part A.1.3). In 1997 – 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,

[15)] The annual expenditure on pensions is tracked statistically in two ways. For budgetary purposes it is stated including the balance from advances to post offices for the payment of pensions at the beginning of the year (Table 12). The figures do not include such advances for the purposes of comparing developments in real expenditure on the payment of pensions in a given year (Table 14).

2005 and 2007 surpluses of the pension insurance system were calculated and transferred to this special account. In 2006, no surplus of the pension insurance system was reported and therefore the balance of funds recorded in the special pension insurance account was not subject to any changes that might arise from the management of the system of pension insurance; but was reduced by CZK 9.31 billion used for increasing state budget expenditure for 2006 allocated to pension insurance benefits (under Act No. 584/2006 Coll.).

Table 13 Special pension insurance account (CZK million)

Year	Special account	Difference between revenues and expenditure	Revenues on the pension insurance	Expenditure on the pension insurance	Of which expenditure on	
					pensions	administration
1996	4,384	4,384	133,927	129,543	126,797	2,746
1997	4,384	-6,516	146,333	152,848	150,231	2,617
1998	4,384	-12,493	156,338	168,831	166,119	2,711
1999	4,384	-19,445	161,827	181,272	177,849	3,423
2000	4,384	-19,658	170,457	190,115	186,852	3,263
2001		-18,501	185,953	204,454	201,111	3,343
2002		-18,909	198,424	217,333	213,648	3,685
2003		-19,912	209,624	229,536	225,833	3,703
2004	8,326	8,326	243,276	234,950	230,897	4,053
2005	14,886	6,560	258,327	251,767	247,390	4,377
2006	5,576	-864	276,913	277,777	272,911	4,866
2007	15,473	9,897	304,934	295,037	289,855	5,182

Source: State final accounts.

The highest share of expenditure on pension insurance is allocated to 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. Also the proportion of partial disability pensions is steadily rising which stems from their increasing number and from the fact that 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. A steadily declining share of expenditure occurs in the case of widow pensions due to the fact that the number of separately paid widow pensions (for more details see part B.2.2.2.), that are not reduced due to their concurrent receipt together with another pension is declining.

Whereas in 2003 – 2004 expenditure increased in the year-on-year terms by 3.7%, in 2005 – 2007, when higher valorization of pensions occurred, expenditure rose by 7.4%, 7.3% and 8.2%, respectively. The year-on-year increase in expenditure in 2007 was the second highest, next to 1998. The basic parameters that affect expenditure on pension insurance are the number of pensioners, or pensions and the amount of pensions influenced in particular by the valorization of pensions.

Table 14 Expenditure[1)] on pensions by type of pension (Chapter 313 – MLSA)

Year	Type of pension						
	Old-age	Full disability	Partial disability	Widow	Widower	Orphan	Total
	Expenditure (CZK billion)						
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
2006	188.9	37.2	11.8	18.9	1.8	2.7	261.5
2007	203.9	40.4	13.3	20.4	2.0	2.9	282.9
	Expenditure (% of total)						
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
2006	72.3	14.2	4.5	7.2	0.7	1.0	100.0
2007	72.1	14.3	4.7	7.2	0.7	1.0	100.0

Source: CSSA
Notes: [1)] Net expenditure not including advances to post offices for the payment of pensions.

B.2.2.2. Number of pensioners and pensions

The total number of pensioners significantly increased in 2006 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). Whereas 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 almost doubled, however in subsequent years it has been steadily declining. These developments are connected with 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). The increase in the number of pensioners receiving partial disability pension continued over the whole period. Also the number of pensioners receiving full disability pension increased, but in 2007 after 6 years their number declined again. In 2004 – 2007, a decline in the number of women receiving separately paid widow pension and a decline in the number of orphan pensions continued. A decline in the number of separately paid (solo) widow pensions stems from the fact that women make use of the option of early retirement and solo widow pension is then paid out only to women who are not yet entitled to retire or women caring for children (however, the number of these women is declining, similarly, as the number of orphan pensions).

Table 15 Number of pensioners [1] by type of pension (thousands)

Year	Type of pension									TOTAL
	Old-age				Proportionate	Disability		Widower		
	Total	Not reduced[3]	Reduced permanently[4]	Reduced temporarily[5]	old-age[6]	full	partial	and widow[2]	Orphan[2]	
					TOTAL					
2003	1,891.6	1,639.5	225.9	26.1	22.6	380.4	173.6	67.4	55.2	2,590.8
2004	1,923.7	1,648.7	250.7	24.4	21.2	384.2	179.2	63.4	54.0	2,625.7
2005	1,942.1	1,656.9	270.9	14.3	19.8	385.1	184.9	60.6	52.5	2,645.1
2006	1,976.7	1,667.6	295.3	13.7	18.7	385.8	194.3	57.4	51.0	2,683.8
2007	2,011.3	1,677.4	323.3	10.6	17.6	383.9	202.8	54.2	49.4	2,719.2
					MEN					
2003	657.8	559.3	87.4	11.1	1.1	190.5	96.6	7.5	25.5	978.9
2004	670.0	563.1	96.6	10.2	1.3	193.0	99.2	7.5	24.8	995.7
2005	679.1	568.2	104.8	6.1	1.3	193.8	101.7	7.7	23.9	1,007.5
2006	694.7	572.6	115.5	6.5	1.4	194.5	106.2	7.8	23.0	1,027.5
2007	710.1	576.7	128.1	5.4	1.5	193.7	110.0	7.6	22.1	1,045.1
					WOMEN					
2003	1,233.8	1,080.2	138.5	15.1	21.5	190.0	77.0	59.9	29.7	1,611.9
2004	1,253.8	1,085.6	154.0	14.2	19.9	191.2	80.0	55.8	29.2	1,630.0
2005	1,263.0	1,088.7	166.1	8.2	18.5	191.3	83.2	52.9	28.7	1,637.6
2006	1,282.0	1,095.0	179.8	7.2	17.2	191.3	88.1	49.7	28.0	1,656.3
2007	1,301.2	1,100.7	195.2	5.2	16.1	190.2	92.8	46.6	27.3	1,674.0

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 separately (not concurrently with old-age, disability or partial disability pension).
[3] Not reduced = old-age pension upon reaching the retirement age.
[4] Permanently reduced = up to 3 years before reaching the retirement age pursuant to Section 31 of Act No. 155/1995 Coll.
[5] Temporarily reduced = up to 2 years before reaching the retirement age pursuant to Section 30 of Act No. 155/1995 Coll.
[6] Proportionate old-age pension = old-age pensions granted pursuant to Section 26 of Act No. 100/1988 Coll. and pursuant to Section 29 (b) of Act No. 155/1995 Coll. (a short insurance period).

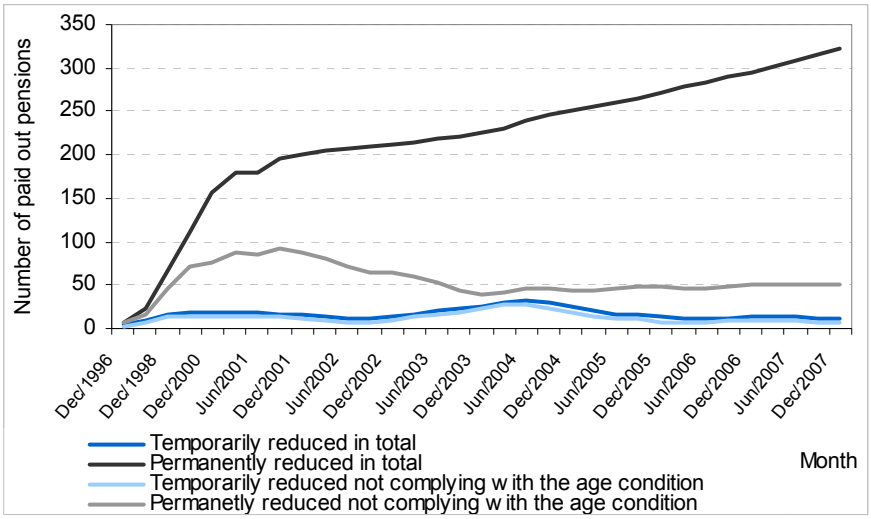
The number of pensioners to whom reduced old-age pension is paid out as a result of retirement before reaching the retirement age also includes pensioners who have already reached the retirement age. The ratio of these pensioners to the total number of pensioners receiving reduced old-age pensions is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

Table 16 Proportion of old-age pensioners receiving reduced old-age pensions after reaching the retirement age to the number of all pensioners receiving reduced old-age pensions

Year	2003	2004	2005	2006	2007
Share (%)	75.9	77.2	80.2	80.3	82.9

Source: MLSA

Graph 10. Number of old-age pensioners receiving reduced old-age pensions



Source: MLSA

In 2003 – 2007, the total number of pensioners increased by 5% and the greatest increase occurred in the number of pensioners with permanently reduced early old-age pensions (43%). This is due to the specific structure of this group of pensioners. Because of their relatively small numbers, increases in new pensioners are more obvious. An increase in the number of pensioners with permanently reduced early old-age pensions accounted for 81% of an increase in the number of all old-age pensions. The number of pensioners receiving partial disability pension increased by 17%.

Table 17 Increases in the number of pensioners during 2003-2007 (%)

	Type of pension									
	Old-age				Proportionate old-age[6)]	Disability		Widower and widow[2)]	Orphan[2)]	TOTAL
	Total	Not reduced[3)]	Reduced permanently[4)]	Reduced temporarily[5)]		Full	Partial			
Total	6.3	2.3	43.1	-59.4	-22.3	0.9	16.8	-19.6	-10.5	5.0
Men	8.0	3.1	46.5	-51.2	29.8	1.7	13.9	1.4	-13.0	6.8
Women	5.5	1.9	40.9	-65.4	-25.1	0.1	20.5	-22.3	-8.3	3.9

Source: MLSA
Notes: see Table 15

The average age of pensioners usually changes only after the elapse of several years (statistics provide data for whole years). An increase in the average age of beneficiaries of reduced old-age pensions reflects the fact that the reduction of pensions continues even after reaching the retirement age. Hence, an increase in the proportion of older pensioners affects these groups of pensioners more significantly. The average age of beneficiaries of solo widow pensions is falling slightly as women are making use of the option of taking early retirement which is paid out concurrently with the widow pension. Solo widow pension is then paid out to younger women only who are not yet entitled to retire.

Table 18 Average age of pensioners [1)]

Year	Type of pension									TOTAL
	Old-age				Proportionate	Disability		Widower		
	Total	Not reduced[3)]	Reduced permanently[4)]	Reduced temporarily[5)]	old-age[6)]	Full	Partial	and widow[2)]	Orphan[2)]	
					MEN					
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
2006	70	71	63	61	73	56	49	52	16	63
2007	70	72	64	62	73	56	49	52	16	64
					WOMEN					
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
2006	69	70	60	57	80	58	47	58	17	65
2007	69	70	60	58	80	58	47	58	17	65

Source: CSSA
Notes: [1)]Age reached by pensioners whose pensions were paid out in December; does not include pensions paid abroad.
See notes 2) – 6) for Table 15

In 2003 and 2007, 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 to 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 2007 to 54.7%.

Table 19 Number of pensioners in relation to number of insured persons

Year	Number of persons (thous.)	Number of pensioners (thous.)	Ratio of the number of pensioners to number of insured persons (%)
2003	4,666	2,591	55.5
2004	4,767	2,626	55.1
2005	4,826	2,645	54.8
2006	4,876	2,684	55.0
2007	4,968	2,719	54.7

Source: CSSA

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

$$NP = NPs - WP_{concurrence} - OP_{concurrence}, \qquad [3]$$

where NP is the number of pensioners, NPs is the number of pensions, $WP_{concurrence}$ is the number of widow or widower pensions paid out concurrently with a direct

pension and $OP_{concurrence}$ is the number of orphan pensions paid out concurrently with a direct pension.

The number of pensions paid out continued to rise steadily whereby the highest year-on-year increase (1.3%) occurred in 2006. 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 full disability pensions has been decreasing.

Table 20 Number of pensions paid out [1] (thousands)

Year	Type of pension							
	old-age full	old-age proportionate	full disability	partial disability	widow	widower	orphan	Total
2003	1,892	23	380	174	603	86	55	3,212
2004	1,924	21	384	179	600	88	54	3,250
2005	1,942	20	385	185	595	89	53	3,269
2006	1,977	19	386	194	593	91	51	3,310
2007	2,011	18	384	203	590	92	49	3,347
	as a % of total							
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
2006	59.7	0.6	11.7	5.9	17.9	2.7	1.5	100.0
2007	60.1	0.5	11.5	6.1	17.6	2.8	1.5	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 is **paid out abroad**. The proportion of pensions paid out abroad to all pensions paid out is increasing slightly.

Table 21 Pensions paid out abroad

Year	2003	2004	2005	2006	2007
Pensions paid out abroad	32,520	33,935	37,788	43,255	48,457
Share of all pensions (%)	1.00	1.03	1.14	1.29	1.43

Source: CSSA

The total number of pensions paid out up to the end of the year T (NPs(T)) is comprised of the total 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

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

The development of the number of paid out pensions is affected by the development of the **number of newly granted pensions**[16]**.** In 2007, the number of granted pensions was almost the same as the number of pensions granted in 2004 (190,000.). In the year-on-year terms the total number of granted pensions decreased in 2005 by 13,019 and increased by 11,295 in 2006 and by 1,839 in 2007. The annual decrease in the number of granted pensions occurred after 2004 in the case of deferred old-age pensions (i.e. after years of service beyond the retirement age, in the case of orphan and widow pensions and, except for 2006, in the case of full disability pensions. On the other hand, every year the number of old-age pensions granted upon reaching the retirement age and permanently reduced early old-age pensions was increasing. To a certain extent, this trend is caused by demographic developments, i.e. an increase in the number of persons who are at possible retirement age.

Table 22 Number of newly granted pensions and their development

Type of pension	Number of pensions granted				Change from previous year (%)		
	2004	2005	2006	2007	2005	2006	2007
Total old-age	93,855	86,631	97,322	96,777	92	112	99
Total after the retirement age	62,439	58,142	62,657	65,565	93	108	105
at the retirement age	39,895	43,764	50,403	54,826	110	115	109
deferred	22,544	14,378	12,254	10,739	64	85	88
Total early	31,416	28,489	34,665	31,212	91	122	90
temporarily reduced	4,795	4,645	6,678	1 506	97	144	23
permanently reduced	26,621	23,844	27,987	29,706	90	117	106
Porportionate old-age	265	282	262	265	106	93	101
Total full disability	26 353	23,613	24,207	23,354	90	103	96
from youth	587	594	536	561	101	90	105
other	25,766	23,019	23,671	22 ,793	89	103	96
Partial disability	24,088	22,571	24,718	26,932	94	110	109
Widow and widower	39,840	38,708	36,956	38,206	97	95	103
Orphan	5,666	5,243	4,878	4,648	93	93	95
T O T A L	190,067	177,048	188,343	190,182	93	106	101

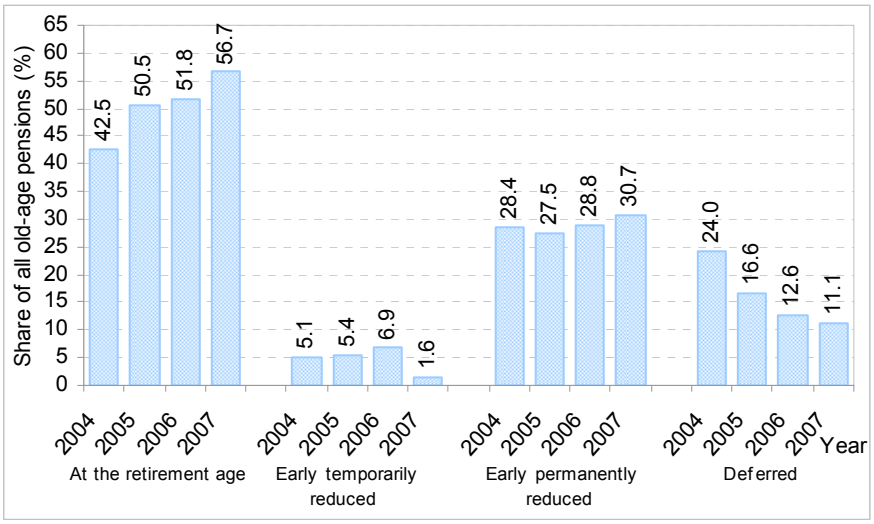
Source: CSSA

Notes: Does not include pensions paid out abroad.
Deferred = old-age pensions increased by additional activities after reaching the retirement age without receiving a pension.
Early temporary = up to 2 years before reaching the retirement age pursuant to Section 30 of Act No. 155/1995 Coll.
Early permanent = up to 3 years before reaching the retirement age pursuant to Section 31 of Act No. 155/1995 Coll.
Proportionate old-age = old-age pensions granted pursuant to Section 29 (b) of Act No. 155/1995 Coll. (a short insurance period).
Disability in youth = disability pensions pursuant to Section 42 of Act No. 155/1995 Coll.

[16] The statistical monitoring of information on newly granted pensions has been carried out since 2002 on the basis of a new methodology. Information is now categorized according to the date when the pension was granted as opposed to the old methodology under which it was categorized by the date from which the permanent payments of the pension benefits started to be made (these dates may differ even by a few months while such difference depends on the length of proceedings on granting pension and the administrative and technological procedures of processing the application for pension). The new methodology corresponds exactly to the granting of the pension and thus provides more objective information, since e.g. the amount of the pension is influenced by reduction limits whose amounts change as of 1 January of each year.

The development of the proportion of the number of granted individual types of pensions to the total number of granted pensions was affected most markedly by a decline in the share of granted deferred old-age pensions, i.e. those increased for gainful activity after reaching the retirement age without receiving the old-age pension. In 2007, these pensions accounted for 11% of all granted old-age pensions, whereas in 2004 their share was 24%. This lower interest in deferred pensions was apparently influenced by cancelling of the condition limiting the payment of old-age pensions concurrently with gainful activity in the first two years following entitlement to such pension and by conditions in the labour market. These conditions seem to be one of the reasons why 32% of old-age pensions in 2007 were granted prior to reaching the retirement age. The proportions of granted disability pensions to the total number of granted pensions reflect opposite development trends. While the proportion of full disability pensions is declining, the share of partial disability pensions is rising and in 2006 it has already exceeded the proportion of full disability pensions. In 2007, granted full disability pensions accounted for 12.3% and granted partial disability pensions accounted for 14.2% of all granted pensions.

Graph 11. Developments in the number of newly granted old-age pensions



Source: MLSA

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

Table 23 Average retirement age

Year	Type of pension							
	Old-age				Proportionate old-age	Disability		Widow and widower
	total	not reduced	reduced permanently	reduced temporarily		full	partial	
	MEN							
2004	61	61	59	59	65	49	48	69
2005	61	61	59	59	65	49	49	69
2006	61	61	60	60	65	49	49	69
2007	61	61	60	60	66	49	48	70
	WOMEN							
2004	57	57	55	55	65	46	46	65
2005	57	57	56	56	65	46	46	66
2006	57	57	56	56	65	46	47	66
2007	58	58	56	57	65	46	46	69

Source: CSSA
Notes: Not reduced = old-age pension upon reaching the retirement age.
Permanently reduced = up to 3 years before reaching the retirement age pursuant to Section 31 of Act No. 155/1995 Coll.
Temporarily reduced = up to 2 years before reaching the retirement age pursuant to Section 30 of Act No. 155/1995 Coll.

In 2007, the average retirement age was 61 for men and 58 for women. The age for retiring thus did not significantly differ from the prescribed retirement age in these years.

Table 24 Retirement age in 2006 and 2007

		2006		2007	
		retirement age	for those born in the period	retirement age	for those born in the period
Men		61y+6m	7/1944-12/1944	61y+8m	5/1945-12/1945
		61y+8m	1/1945-4/1945	61y+10m	1/1946-2/1946
Women with number of children	**0**	59y+8m	5/1946-12/1946	60y	1/1947-12/1947
	1	58y+8m	5/1947-12/1947	59y	1/1948-12/1948
	2	57y+8m	5/1948-12/1948	58y	1/1949-12/1949
	3 and 4	56y+8m	5/1949-12/1949	57y	1/1950-12/1950
	5 or more	55y+8m	5/1950-12/1950	56y	1/1951-12/1951

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 65 for men and 62 -65 for women according to the number of children brought up. This retirement age will be reached by men in 2030 and by women in 2027 to 2031.

Table 25 Year in which entitlement to pension arises for a given age

Retirement age	Men	Women with number of children					
		0	1	2	3	4	5 or more
54							1999
55					1999	1999	2003
56				1999	2003	2003	2007
57			1999	2003	2007	2007	2011
58		1999	2003	2007	2011	2011	2015
59		2003	2007	2011	2015	2015	2019
60		2007	2011	2015	2019	2019	2023
61	2002	2011	2015	2019	2023	2023	2027
62	2009	2015	2019	2023	2027	2027	2031
63	2016	2019	2023	2027	2031		
64	2023	2023	2027	2031			
65	2030	2030	2031				

Source: MLSA

In 2007, a total of 155,292 pensions **terminated** for various reasons, i.e. about 35,000 less than the number of pensions newly granted. Of all terminated pensions, 75% occurred due to the death of the pensioner and 15% due to the granting of a different type of pension.

Table 26 Number of terminated pensions

Year	2004	2005	2006	2007
Total of terminated pensions	148,009	162,224	151,592	155,292
of which: old-age	65,449	76,601	67,020	69,936
full disability	22,626	23,925	23,994	25,769
partial disability	16,112	17,239	19,500	18,018
Reason of termination				
- due to granting of another pension	15,764	27,351	23,781	23,001
- death	117,798	120,338	113,093	116,035

Source: CSSA

B.2.2.3. Amount of pensions

The average amount of the pensions paid out is affected foremost by the increasing 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 valorized due to the termination of the pensions paid out to older pensioners, which are on average lower than pensions that are newly granted[17].

[17] The average amount of terminated pensions has for several years no longer been recorded by the CSSA.

Table 27 Average monthly amounts[1)] of solo paid out pensions (CZK)

Year	Type of pension									TOTAL
	Old-age				Proportionate old-age[6)]	Disability		Widow and widower	Orphan	
	total	not reduced[3)]	reduced permanently[4)]	reduced temporarily[5)]		full	partial			
					TOTAL					
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
2006	8,200	8,437	7,241	7,091	3,859	7,962	4,847	5,385	3,998	7,653
2007	8,761	9,040	7,699	7,646	3,994	8,496	5,161	5,705	4,278	8,176
					MEN					
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
2006	9,168	9,401	8,170	7,932	3,503	8,538	5,133	4,358	3,977	8,419
2007	9,796	10,077	8,687	8,503	3,664	9,094	5,457	4,668	4,254	8,990
					WOMEN					
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
2006	7,444	7,668	6,586	6,259	3,942	7,243	4,492	5,546	4,016	7,002
2007	7,952	8,217	6,985	6,652	4,080	7,750	4,800	5,875	4,298	7,484

Source: CSSA
Notes: [1)] The average amount of pensions paid out in December; does not include pensions paid abroad.
Solo = only pensions paid out separately (not concurrently with survivor pensions).
[3) – 6)] see notes to Table 15

Under the Act, paid out pensions are as of 2003 increased 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.

Table 28 Overview of increases to paid out pensions

Month and year the increase came into effect	January 2004	January 2005	January 2006	January 2007	January 2008	August 2008
Increase in the basic amount of pension (CZK)		90	70	100	130	470
Increase in the percentage-based assessment						
old-system pensioners	2.5%	5.4%	6.0%	6.6%	3.0%	3.0%
new system pensioners			4.0%	5.6%		
Basic amount of pension (CZK)	1,310	1,400	1,470	1,570	1,700	2,170

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

Increases in paid-out pensions carried out in 2006 and 2007 exceeded the minimum statutory level of increase by 1.9 percentage points. Other increases in paid-out pensions carried out in 2003-2008 exceeded the minimum statutory level of increase by 0.1-0.3 percentage points.

Pensioners to whom a pension was paid out in June 2004 also received a one-off allowance in the amount of CZK 1,000 as a one-off assistance to meet the costs incurred in respect of changes made in the amount of value added tax. This allowance does not constitute a pension insurance benefit, nor is the expenditure on its payment included in the pension insurance expenditure.

The growth of the average amount of paid out pensions was, except, for 2005, slower than the growth of the average wage in the national economy, and therefore **the replacement ratio** (the second parameter that affects the balancing of pension insurance accounts) **kept falling in the year-on-year terms** and the average old-age pension in 2007 amounted to 40.6% of the gross wage and to 52.9% of the net wage. The discrepancy between the rate of growth of pensions and the rate of growth of the average wage stems in particular from the fact that only 1/3 of the growth of real wages needs to be reflected in increases in pensions; however, it is also influenced by the fact that increases in pensions are determined with regard to the increase in wages in the period of the calendar year which precedes by two years the year in which pensions are increased and which usually differs from the growth of wages in the year in which the replacement ratio achieved is evaluated.

Table 29 Replacement ratio

Year	Average pension[1)]	Average wage		Total replacement ratio	
		Gross	Net[2)]	Gross	Net
	(CZK)	(CZK)	(CZK)	(%)	(%)
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	18,809	14,252	41.1	54.2
2006	8,173	20,050	15,506	40.8	52.7
2007	8,736	21,527	16,509	40.6	52.9

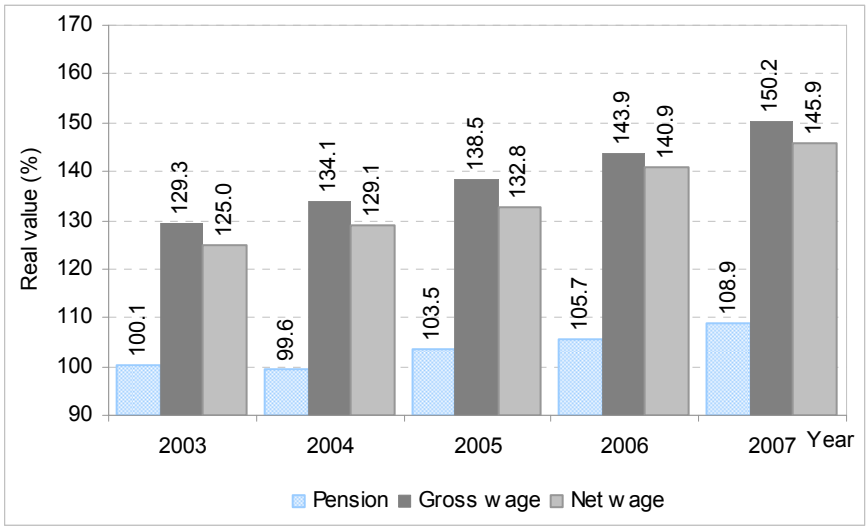
Source: MLSA

Notes: [1)] The average pension is the average monthly solo old-age pension paid out in a given year.

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

The development of the relation between the average paid out old-age pension to the wage may be deemed "positive" in terms of its effect on the development of the balance of revenues from and expenditure on pensions (with the same rate of premium, revenues from pension insurance grow faster than expenditure on pensions insurance), however, not in terms of the development of the standard of living of pensioners, 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.** Such development is usual in pension systems of other states, however in the Czech Republic this fact is more important for the standard of living of pensioners because pensions are here almost an exclusive source of income for pensioners.

Graph 12. Developments in the real value of the average paid out old-age pension and the average wage as percentage of their values in 1989



Source: MLSA

The real value of average paid out old-age pension decreased over the period of the last five years only in 2004,namely by 0.6% (the calculation does not include a one-off allowance paid in June 2004 since not all pensioners were eligible for it); in other years it increased by 2.1% up to 4.0%.

Table 30 Developments in the real value of the average paid out old-age pension

Year	100% in the year			
	2003	**2004**	**2005**	**2006**
2003	100.0			
2004	99.4	100.0		
2005	103.4	104.0	100.0	
2006	105.5	106.1	102.1	100.0
2007	108.7	109.4	105.2	103.1

Source: MLSA

The average amount of the paid out pensions also depends on the year when they were granted. Basically, the rule applies that the longer the pensions are paid out, the lower is their amount in relation to other pensions. Such differences are caused by wage developments, changes in the method of calculating the newly granted pensions and valorization of pensions.

Table 31 Average amount of solo old-age pensions paid out by the period they were granted (pensions paid out in December 2007, in CZK)

Year granted	Total	Not reduced	Early reduced	
			permanently	temporarily
-1988	8,348	8,348		
1989-1995	8,648	8,648		
1996-1999	8,586	8,992	7,795	7,559
2000	8,366	9,250	7,700	7,075
2001	8,655	9,376	7,565	6,426
2002	8,949	9,480	7,080	6,607
2003	8,941	9,478	7,276	6,759
2004	9,076	9,659	7,367	7,371
2005	9,264	9,791	7,708	7,156
2006	9,374	10,078	8,015	7,732
2007	9,361	9,946	7,973	8,539
Total	8,762	9,041	7,699	7,647
Old-system pensioners	8,534	8,534		
New-system pensioners	8,894	9,481	7,699	7,647

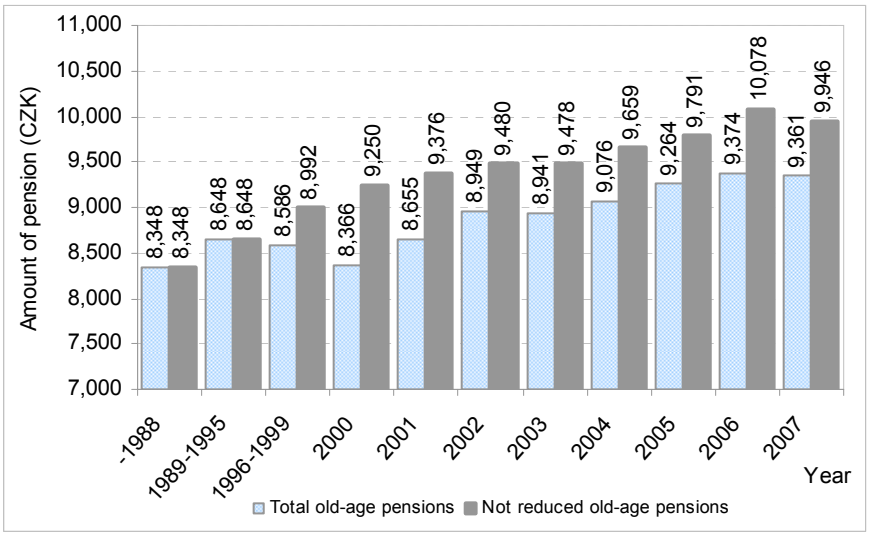
Source: CSSA

Notes: Not reduced = old-age pension upon reaching the retirement age.
Permanently reduced = up to 3 years before reaching the retirement age pursuant to Section 31 of Act No. 155/95 Coll.
Temporarily reduced = up to 2 years before reaching the retirement age pursuant to Section 31 of Act No. 155/95 Coll.

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 lower than those of the new-system pensioners (pensions granted after 31 December 1995). This situation persists even though the pensions of the old-system pensioners were adjusted seven times between 1998 and 2007 more advantageously than those of the new-system pensioners. In the given period pensions of the old-system pensioners were valorized by 80% and pensions of the new-system pensioners by 54% in the aggregate. Nevertheless, a difference between the average amount of old-age pensions of the old-system pensioners and the new-system pensioners paid out in December 2007 was CZK 360, i.e. 4.2%.

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 2007 it amounted to CZK 947, i.e. 11.1%.

Graph 13. Average amount of solo old-age pensions paid out that were granted in various years

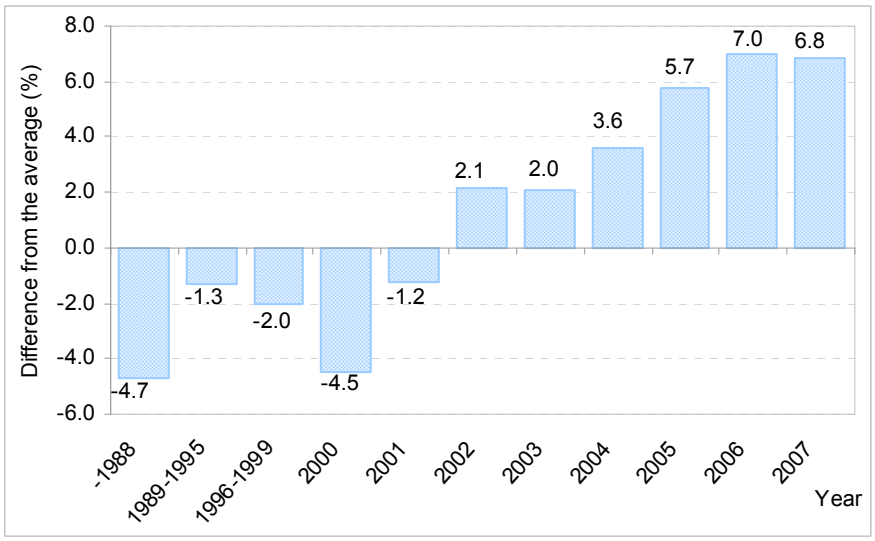


Source: MLSA

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 provided for under 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.

Hence, there are not only differences between the pensions of the old-system pensioners and the new-system pensioners, but also between the amounts of pensions granted at the time when the same regulations were in force (for the new-system pensioners). While a difference between the average amount of pensions of the old-system pensioners and the new-system pensioners is CZK 360, a difference between old-age pensions granted in 2003 and 2007 is CZK 420 and between pensions granted in 2000 and 2006 even CZK 1,008. Therefore, the natural development of the pension system results in certain differences between more or less comparable pensions. The focus on specific differences between the old-system pensioners and the new system pensioners was justified at a certain development stage. Currently, however, these issues are not extraordinary to an extent that would justify further the need for an extraordinary solution in the form of more advantageous valorization. Due to more advantageous valorization of pensions of old-system pensioners, for instance, pensions granted in the six-year period before 1 January 1996 are higher than pensions granted in the six-year period after this date.

Graph 14. 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 (%)



Source: MLSA

The number of old-system pensioners is gradually decreasing; their share of the total number of pensioners fell in the period 2003-2007 by almost 15 percentage points.

Table 32 Developments in the proportion of old-system pensioners to the total number of pensioners

Year	2003	2004	2005	2006	2007
Share (%)	60.2	56.1	52.4	48.7	45.1

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 (crediting) of earnings decisive for the calculation of the pensions.

Table 33 Reduction limits for the calculation of pension amounts

Year	2003	2004	2005	2006	2007	2008
First reduction limit (CZK)	7,400	7,500	8,400	9,100	9,600	10,000
as % of the average wage	44.1	41.9	44.7	45.4	44.6	43.0
Second reduction limit (CZK)	17,900	19,200	20,500	21,800	23,300	24,800
as % of the average wage	106.7	107.4	109.0	108.7	108.2	106.6

Source: MLSA

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.

Except for 2005 and 2006, the first reduction limit increased slower than the average wage in the national economy so the band of earnings that are fully credited to the amount of pensions was becoming smaller (in relation to the average wage). The second reduction limit grew in 2003 – 2008 somewhat faster (by 3.4 percentage points) than the first reduction limit. As a result, the band of earnings that are credited by 30% to 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 earnings are fully credited to 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 then again after 2006.

Table 34 Developments in the relation of newly granted old-age pensions to wages in 40 years of being insured and at different wage levels (%)

Multiple of the average wage	Old-age pension granted in the year				
	2003	2004	2005	2006	2007
0.7	55.6	53.6	55.4	55.7	55.2
1.0	44.3	42.9	44.2	44.4	44.0
1.5	32.1	31.2	32.2	32.3	32.0
2.0	25.6	24.9	25.6	25.7	25.5
2.5	21.7	21.1	21.7	21.8	21.6
3.0	19.1	18.6	19.1	19.1	19.0

Source: MLSA

Table 35 Average amount[1)] of newly granted old-age pensions

Type of pension	CZK				as % of the average gross wage			
	2004	2005	2006	2007	2004	2005	2006	2007
Total old-age	7,760	8,391	8,855	9,321	43.4	44.6	44.2	43.3
total after the retirement age	8,489	9,092	9,565	9,958	47.5	48.3	47.7	46.3
at the retirement age	7,968	8,693	9,201	9,585	44.6	46.2	45,9	44.5
deferred	9,410	10,306	11,062	11,859	52.6	54.8	55,2	55.1
total early	6,308	6,960	7,571	7,983	35.3	37.0	37.8	37.1
temporarily reduced	6,404	6,836	7,550	8,610	35.8	36.3	37,7	40.0
permanently reduced	6,291	6,984	7,576	7,951	35.2	37.1	37,8	36.9
Proportionate old-age	2,366	2,489	2,526	2,665	13.2	13.2	12.6	12.4
Total full disability	7,740	8,396	8,950	9,371	43.3	44.6	44.6	43.5
from youth	5,979	6,483	6,908	7,344	33.4	34.5	34.5	34.1
other	7,780	8,446	8,996	9,420	43.5	44.9	44.9	43,8
Partial disability	4,451	4,809	5,137	5,404	24.9	25.6	25.6	25.1
Widow and Widower	4,659	4,961	5,245	5,594	26.1	26.4	26.2	26.0
Orphan	3,778	4,050	4,296	4,538	21.1	21.5	21.4	21.1
T O T A L	6,916	7,458	7,945	8,315	38.7	39.7	39.6	38.6

Source: CSSA

Notes: Does not include pensions paid out abroad.

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

Early temporary = up to 2 years before reaching the retirement age pursuant to Section 30 of Act No. 155/1995 Coll.

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

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

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

1) Amount of pensions not reduced for concurrence with another pension.

B.2.2.4. Reduction of pensions due to early old-age retirement

In the case of early old-age retirement, the amount of the percentage-based assessment of the old-age pension is reduced and the level of reduction depends on the remaining time to the retirement age and the amount of the calculation base. Given the different importance accorded to the basic amount of pensions for those pensioners with varying insurance periods and amounts of assessment bases, this reduction has a different impact on the total amount of the old-age pension. The greatest relative reduction 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 insurance period and a high assessment base, which is caused by the great impact of the reduced percentage-based assessment and the relatively large weight of this assessment in relation to the total pension. In contrast, such a reduction has the lowest impact on persons with low assessment bases and long insurance periods.

Table 36 Reductions in early old-age pensions permanently reduced by 1 year*) granted in 2007 (%)

Personal assessment base (CZK)	Number of years being insured				
	25	30	35	40	45
5,000	-5.2	-4.7	-4.3	-3.9	-3.6
10,000	-6.7	-5.9	-5.2	-4.7	-4.3
15,000	-7.0	-6.1	-5.4	-4.9	-4.4
20,000	-7.2	-6.3	-5.5	-5.0	-4.5
25,000	-7.4	-6.4	-5.6	-5.0	-4.6
30,000	-7.4	-6.4	-5.7	-5.1	-4.6

Source: MLSA
Note: *) 360 days before reaching the retirement age (i.e. 4 x 90 days).

In the case of increasing the basic amount pension, a smaller reduction in the early old-age pension occurs due to the increase in its weight in relation to the total pension, while this is most obvious for persons with a low assessment base and a short insurance period. For instance, an increase in the basic pension amount from CZK 1,570 (in 2007) to CZK 2,170 would affect cases set out in the Table by 0.2 to 0.8 percentage points. An increase in the basic pension amount apparently also influenced the fact that the proportion of the average amount of newly granted permanently reduced old-age pensions to the average amount of non-reduced old-age pensions granted upon reaching the retirement age between 2004 and 2007 increased from 79% to 83%.

B.2.2.5. Differentiation of pensions by pension amount[18]

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

a) developments in the differentiation of newly granted old-age 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,
b) 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),

[18] Quantiles and the characteristics derived from them will be used for the measurement of the differentiation of old-age pensions by pension amount. A quantile is the amount of income/earnings (e.g. pension) which a certain percentage of pensioners earns. For example, 10% quantile is the amount of income (earnings) indicating that 10 % of the people have income (earnings) up to this amount. A 50% quantile is referred to as the median and in cases of normal distribution is equal to the average. The basic characteristics will be the width of the interval in earnings around the median expressed as a percentage of the median in which there are:

- **20 % of pensioners**: the respective characteristics is marked as **M(20)** = 100 x($k_{60} – k_{40}$) / median,
- **50 % of pensioners:** the respective characteristis is marked as **M(50)** = 100 x ($k_{75} – k_{25}$) / median,
- **80 % of pensioners**: the respective characteristics is marked as **M(80)** = 100 x($k_{90} – k_{10}$) / median,

where k_x marks the x% quantile.
The greater the numbers M (XX), i.e. the greater the interval in which there is the respective share of pensioners, the larger the difference.
Calculated according to data on solo old-age pensions.

c) developments in the ratio of the basic pension amount to the total pension amount,
d) valorization of pensions and the differentiation of their amounts for old- system and new-system pensioners,
e) 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 2003-2007, the differentiation continued to grow slowly foremost as a result of a slightly faster growth in the higher pensions of women.

Table 37 Basic characteristics of differentiation in the amount of solo paid out old-age pensions

	Year	2003	2004	2005	2006	2007	Change 2001- 2005
M(20)	Men	6.8	7.0	7.2	6.9	6.9	0.1
	Woman	6.0	6.3	6.7	6.8	7.1	1.1
	Total	9.0	9.4	9.5	9.7	9.8	0.8
M(50)	Men	17.1	17.9	19.8	18.7	19.2	2.1
	Woman	17.3	18.3	19.2	19.7	20.3	3.0
	Total	23.7	24.7	25.3	25.4	25.7	2.0
M(80)	Men	36.3	37.5	38.4	37.9	38.7	2.4
	Woman	38.3	40.3	41.5	42.4	43.4	5.1
	Total	44.5	46.6	48.8	48.3	49.1	4.6

Source: MLSA

The developments in the differentiation of paid out old-age pensions by their amounts are also influenced by the growing importance (weight) 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 38 Characteristics of the differences in the amounts of old-age pensions paid out in December 2007 by method of reduction

		Total	Not reduced	Reduced	
				permanently	temporarily
M(20)	Men	6.9	6.6	5.7	6.8
	Woman	7.1	7.1	7.8	7.8
	Total	9.8	9.9	10.5	11.9
M(50)	Men	19.2	19.1	16.2	18.3
	Woman	20.3	19.6	21.1	21.0
	Total	25.7	25.2	26.5	29.1
M(80)	Men	38.7	38.3	34.2	37.7
	Woman	43.4	40.1	43.2	43.4
	Total	49.1	46.9	48.5	51.2

Source: MLSA

The differentiation is clearly higher for the early old-age pensions of women than for the old-age pensions of women granted upon the retirement age; however, in contrast, for men it is lower. Apparently, they are mostly men with lower incomes who 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 insurance period relates to the number of children brought up.

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

Table 39 Basic characteristics for differentiating newly granted old-age pensions (solo) by their amount

	Year	2004	2005	2006	2007
M(20)	Men	8.0	7.0	8.7	8.4
	Woman	12.1	10.4	9.6	9.1
	Total	12.4	11.8	11.1	11.0
M(50)	Men	22.5	21.3	21.4	21.0
	Woman	31.9	28.4	26.2	25.5
	Total	31.9	30.0	28.6	28.0
M(80)	Men	44.7	42.3	41.7	41.6
	Woman	59.5	55.8	50.4	50.4
	Total	58.0	56.6	52.9	52.9

Source: MLSA

B.2.3. SICKNESS INSURANCE

Sickness insurance, like pension insurance, is based on the PAYGO method under which the financial balance is balanced out each year if 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 total revenues, DB as the average daily sickness benefit, NDS the number of calendar days of sickness and EOB expenditure on other sickness insurance benefits. The EOB is not outlined in greater detail given that sickness insurance accounts for the greatest share of expenditure on sickness benefits. Hence, 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:

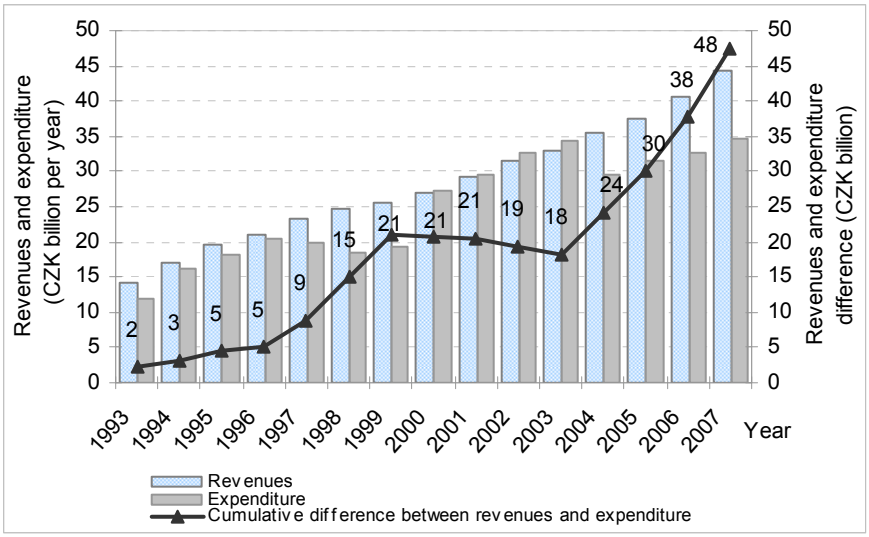
$$CR \times CC \times (1 - AC) \times p = DB/\ AA \times NDS/\ (NDCY \times NC), \quad [7]$$

whereby DB/AA is the relation of sickness benefits to earnings to date (replacement ratio) and characterizes the level of sickness benefits, and NDS/(NDCY x NC) is the average 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 on 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. Operating costs are assessed in Chapter B.2.5., which also covers both pension and sickness insurance.

Since 1993, when in connection with the tax reform premium for sickness insurance was introduced, annual differences between revenues from premiums for sickness insurance and expenditure on sickness benefits range from CZK - 1.3 billion to CZK + 9.7 billion. The deficit occurred for the first time in 2000 when the impact of an increase in the first reduction limit for determining the daily assessment base (DAB) from CZK 270 to CZK 360 and the introduction of the second reduction limit for determining the DAB in the amount of CZK 540 became apparent. It was only the reform of public finances in 2004 that led to surplus between revenues from premiums and expenditure on sickness benefits, namely in the amount of CZK 6.1 billion. The highest difference between revenues and expenditure (CZK 9.7 billion) was recorded in 2007. Originally, the new Sickness Insurance Act had to come into effect on 1 January 2005 and during its drafting emphasis was put on the balanced relationship between revenues from premiums and expenditure on sickness benefits. Due to the deferral of the effective date of the Act and the implementation of the approved changes the system of sickness insurance is not balanced in financial terms. The following graph shows differences between revenues from sickness insurance premiums and expenditure on sickness benefits. Cumulative difference between revenues and expenditure since 1993 amounted to CZK 47.5 billion in 2007. which is by 37% more than the funding required for benefits in 2007. Under the budgetary rules in force, however, premiums for social security and contribution to the state employment policy constitute state budget revenue and as a “a sort of tax", they are used to finance also other benefits falling within Chapter 313 of the Ministry of Labour and Social Affairs.

Graph 15. Development of revenues and expenditure on sickness insurance



Source: MLSA
Note: Expenditure is exclusive of administrative expenses.

In 2006 revenues from sickness insurance were by CZK 7.8 billion higher than expenditure on sickness benefits, in 2007 revenues were higher by CZK 9.7 billion than expenditure on sickness benefits, which for the first time dropped below the level of 1% of the GDP.

Table 40 Revenues and expenditure on sickness insurance (Chapter 313 – MLSA)

Year	Revenues[1)] (CZK billion)	Expenditure (CZK billion)	Revenues - Expenditure (CZK billion)	Expenditure (% of GDP)
2003	33.3	34.3	-1.0	1.34
2004	35.7	29.6	6.2	1.07
2005	37.7	31.7	6.0	1.06
2006	40.5	32.8	7.8	1.01
2007	44.4	34.7	9.7	0.98

Source: CSSA
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 has been gradually increasing, whereas the number of voluntarily insured self-employed persons has been decreasing.

Table 41 Developments in the number of persons insured under sickness insurance*) (in thous.)

Year	Sickness insurance			Pension insurance
	Employees	Self-employed	Total	Self-employed
2003	4,020	295	4,315	646
2004	4,040	279	4,319	727
2005	4,085	251	4,337	740
2006	4,162	230	4,392	714
2007	4,254	216	4,469	714

Note: *) Average number in a year

In 2007 the year-on-year increase in revenues from sickness insurance premiums was by 3.6 percentage points higher than the increase in expenditure (revenues increased by 9.4%, expenditure by 5.8%). The average daily amount of sickness benefits (expenditure on sickness benefits / the number of calendar days of sick leave) increased in 2006 compared to 2003 by 6.9% to CZK 283 and in 2007 increased in the year-on-year terms by 4.7% to CZK 296.

The greatest portion of expenditure on sickness insurance benefits represent sickness benefits which in 2005 amounted to 80% of all expenditure. Expenditure on maternity benefits accounted for 17% of the total expenditure and expenditure on family member care benefits comprised 3% of the total expenditure. 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.

Table 42 Expenditure on sickness insurance (Chapter 313 – MLSA)

Year	Sickness benefits	Family member care benefit	Pregnancy and maternity compensation benefit	Maternity benefits	Total
			In absolute terms (CZK billion)		
2003	29.523	1.004	0.006	3.774	34.307
2004	24.704	0.730	0.005	4.123	29.563
2005	26.258	0.819	0.004	4.579	31.660
2006	26.963	0.825	0.004	4.981	32.773
2007	27.881	0.893	0.004	5.893	34.671
			In relative terms (% of total)		
2003	86.06	2.93	0.02	11.00	100.0
2004	83.56	2.47	0.02	13.95	100.0
2005	82.94	2.59	0.01	14.46	100.0
2006	82.27	2.52	0.01	15.20	100.0
2007	80.42	2.58	0.01	17.00	100.0

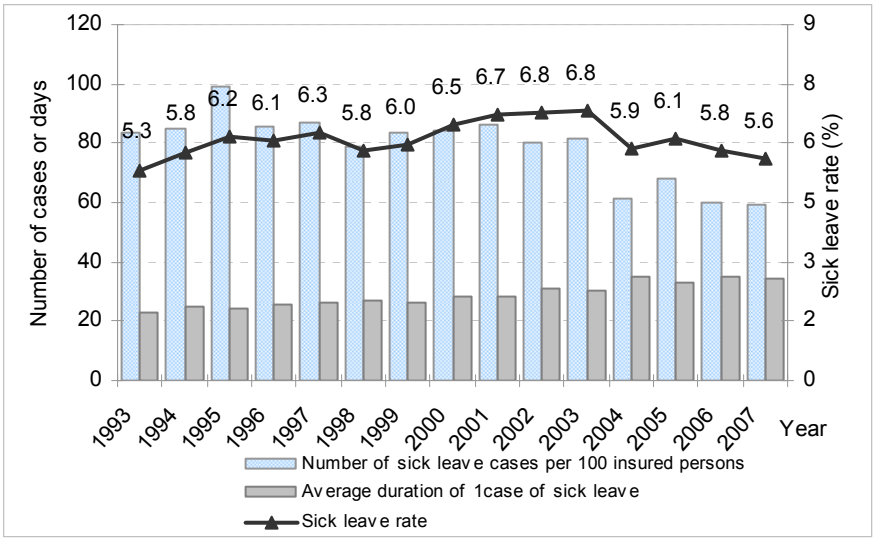
Source: CSSA

Development in sickness is characterized by the average 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

Sick leave rate = Average duration of 1 case of sick leave x number of cases of sick leave per 100 persons insured under sickness insurance / number of days in the calendar year [8]

Average duration of 1 case of sick leave x number of cases of sick leave per 100 persons insured under sickness insurance gives the number of days on sick leave. In 2006 this indicator was 95.4 million calendar days and in 2007 dropped to 94.3 million calendar days.

Graph 16. Developments in the general indicators of sickness insurance



Source: CSO

The lower sick leave rate in 2004 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. Since 2005 declining sickness rates were recorded.

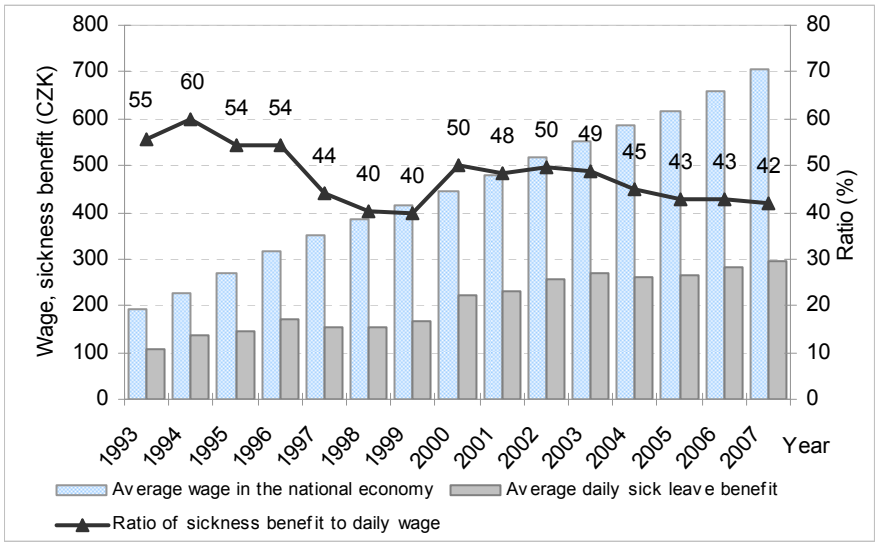
The amount of the sickness benefits depends on the earnings achieved and on the prescribed reduction limits of the daily assessment base for calculating sickness benefits, which from 2000 to 2002 were adjusted annually as at 1 January in accordance with developments in wages. With respect to the cost savings measures taken due to the floods in 2003 and in 2004 and 2005 within the framework of public finance reforms, the valorization of the reduction limits was not undertaken. Only in 2006 and 2007 the reduction limits were again raised to CZK 510 and CZK 790, respectively as of 1 January 2007.

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

Period of validity of reduction limits	Reduction limit (CZK)		Reduction of creditable income				Maximum daily assess-ment base (CZK)	For period of sickness	Maximum daily amount of benefit	
			income from amount up to (CZK)	reduced to	income from amount (CZK) over-up to	redu-ced to			rate of benefit	amount of benefit (CZK)
	first	second								
from 1.1.1993 to 31.12. 1993	190		190	not reduced			190	1st-3rd day	50%	95
								from 4th day	69%	132
from 1.1.1994 to 1.10.1999	270		270	not reduced			270	1st-3rd day	50%	135
								from 4th day	69%	187
from 1.10.1999 to 31.12.1999	360	540	360	not reduced	360-540	60%	468	1st-3rd day	50%	234
								from 4th day	69%	323
from 1.1.2000 to 31.12.2000	400	590	400	not reduced	400-590	60%	514	1st-3rd day	50%	257
								from 4th day	69%	355
from 1.1.2001 to 31.12.2001	430	630	430	not reduced	430-630	60%	550	1st-3rd day	50%	275
								from 4th day	69%	380
from 1.1.2002 to 31.12.2003	480	690	480	not reduced	480-690	60%	606	1st-3rd day	50%	303
								from 4th day	69%	419
from 1.1.2004 to 31.12.2005	480	690	480	90%	480-690	60%	558	1st-3rd day	25%	140
								4th-14th day	69%	386
			480	not reduced.	480-690	60%	606	from 15th day	69%	419
from 1.1.2006 to 31.12.2006	510	730	510	90%	510-730	60%	591	1st-3rd day	25%	148
								4th-14th day	69%	408
			510	not reduced	510-730	60%	642	from 15th day	69%	443
from 1.1.2007 to 31.12.2007	550	790	550	90%	550-790	60%	639	1st-3rd day	25%	160
								4th-14th day	69%	441
			550	not reduced	550-790	60%	694	from 15th day	69%	479
from 1.1.2008 to 29.6.2008	590	790	590	90%	590-790	60%	639	1st-3rd day	0%	0
								4th-30th day	60%	384
								31th-60th day	66%	422
								from 61th day	72%	461
from 30.6.2008 to 31.8.2008	550	790	550	90%	550-790	60%	639	1st-3rd day	60%	384
								4th-30th day	60%	384
								31th-60th day	66%	422
								from 61th day	72%	461
from 1.9.2008 to 31.12.2008	550	790	550	90%	550-790	60%	639	1st-3rd day	25%	160
								4th-30th day	60%	384
								31th-60th day	66%	422
								from 61th day	72%	461

Source: MLSA

Graph 17. Developments in the average daily sickness benefits, average daily wage and their ratio

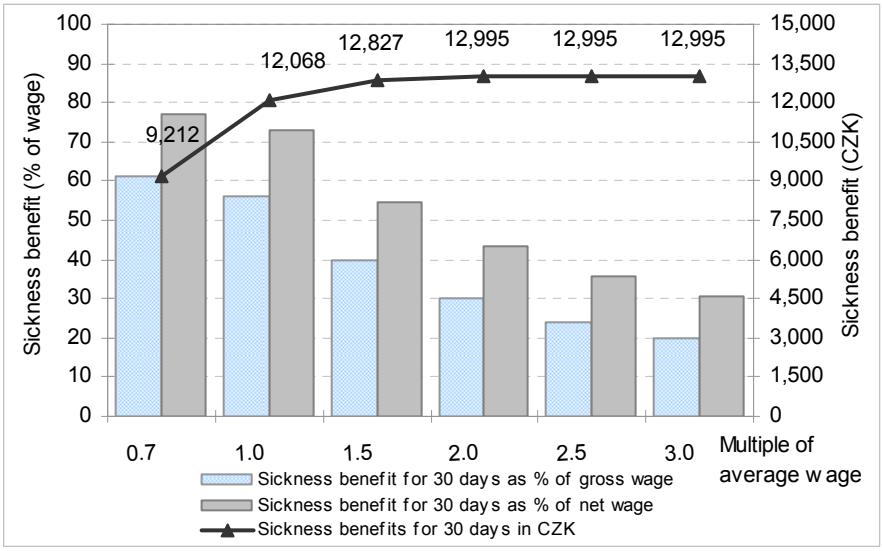


Source: MLSA

The relation of the average daily sickness benefits to the average gross wage has dropped since 2000 by 8 percentage points primarily due to the fact that reduction limits were not increased and in 2007 was only 42%.

A consequence of the effect of the reduction limits is that the replacement ratio decreases when wages increase (Graph 18). Therefore, there is a relatively large solidarity in the sickness insurance system between insured persons with high earnings and those with low earnings.

Graph 18. Amount of sickness benefits for 30 days in 2007 and its ratio to the gross and net wage for various wage amounts

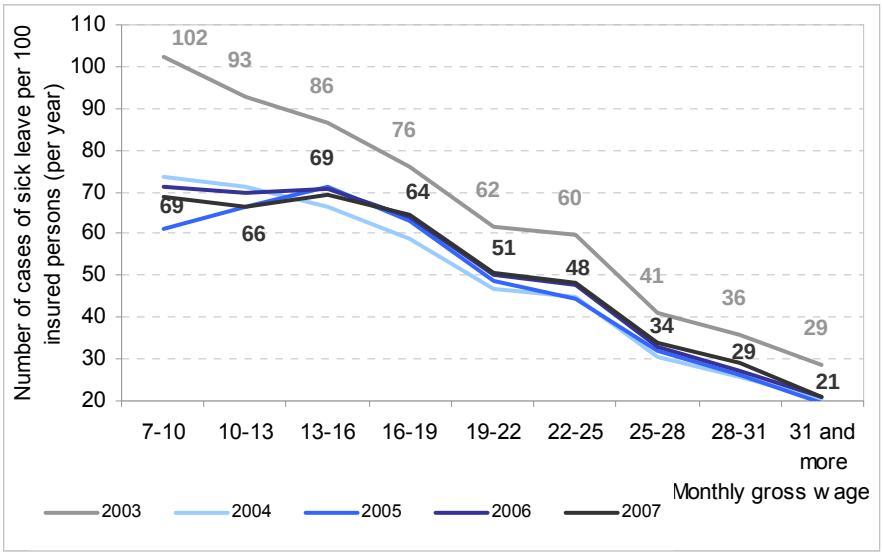


Source: MLSA

Sickness rate of insured persons by amount of earnings

For the purposes of determining the amount of sickness benefits, earnings over the second reduction limit are not taken into account and therefore all insured persons whose earnings are higher than about CZK 24,000 per month will receive maximum amount of sickness benefits. According to the statistics of employees of small organizations, in 2007 there were about 8% of cases of sick leave where sickness benefits were calculated from earnings higher than the maximum amount that was taken as the basis for the calculation of the amount of benefits, while there were about 14% of insured persons (payers of premium) whose earnings were in excess of the above amount. The fact that insured persons with higher earnings are on a sick leave more frequently than those with lower earnings is shown in the following graph that is based on CSSA data on sickness rate of employees of small organizations in 2003 – 2007.

Graph 19. Distribution of the sickness rate of insured persons by amount of earnings



Source: MLSA

The above data on sickness rate of insured persons per 100 insured persons confirm that the public finances reform that reduced in 2004 the level of sickness benefits also resulted in lower sickness rates. The decrease was more marked for insured persons with lower earnings. A similar (but less significant) trend can be expected also from the public budget reform in 2008. However, by reducing sickness benefits and thereby the sickness rate, about three quarters of expenditure on sickness insurance may be influenced. Expenditure on maternity benefits, which accounts for about one fifth of total expenditure and partly also on care benefits, is resistant to sickness rate and depends on other indicators.

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 January 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 levels of the 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 ILO 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 ILO Convention No. 128 requires a replacement 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 beneficiary.** A typical beneficiary is considered to be an insured person (with a dependent wife) 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). As in the Czech Republic, pensions are taxed only from amounts over CZK 198,000 and the state pays for the pensioner's health insurance, the ILO accepts for the Czech Republic the setting of the **ratio to the net wage.**

Table 44 Fulfilment of the ILO Conventions for old-age pensions during 2005 - 2008

Year	Wage Skilled labourer (CZK/month)		Old-age pension Amount (CZK/month)	As % of wage of a skilled labourer	
	Gross	Net		Gross	Net
2005	18,717	14,551	6,574	35.1	45.2
2006	19,507	15,103	6,971	35.7	46.2
2007	20,801	16,398	7,403	35.6	45.1
2008	23,002	17,824	7,959	34.6	44.6

Source: MLSA

The replacement ratio for newly granted old-age pensions dropped in 2008 under 45% to 44.6% and the Czech Republic ceased to fulfil criteria of the ILO Convention No. 128. The Czech Republic continues to fulfil the criteria contained in the Code. The main reason for a significant decline in the replacement ratio, even under the limit required by ILO Convention No. 128 is the increased level of net

income of the individual defined above due to tax changes[19].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 the following years the Convention was fulfilled only when using the average wage of the skilled labourer (which is lower in the Czech Republic).

- **Full disability pension and survivor benefits**

The ILO Convention No. 102 and the Code require **the replacement ratio of 40% for these benefits.** For newly granted full disability pensions and survivors benefits, a typical beneficiary is an employee with a wage equal to 1.25 multiple of the average wage in the national economy or a wage of a skilled labourer with two children. For this reason, for calculation purposes, into the employee's and pensioner's income also benefits for two children are included into the calculation. Similarly, as in the case of old-age pensions, for evaluation of fulfilment of the Convention, the ratio of benefit to net wage is decisive.

Table 45 Fulfilment of the ILO Conventions for disability pensions during 2005 - 2008

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
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
2007	20,801	17,398	1,216	7,403	8,619	39.1	46.3
2008	23,002	18,824	1,220	7,956	9,176	37.9	45.8

Source: MLSA
Note: with child benefits = including benefits for two children

Table 46 Fulfilment of the ILO Conventions for survivor pensions during 2005 - 2008

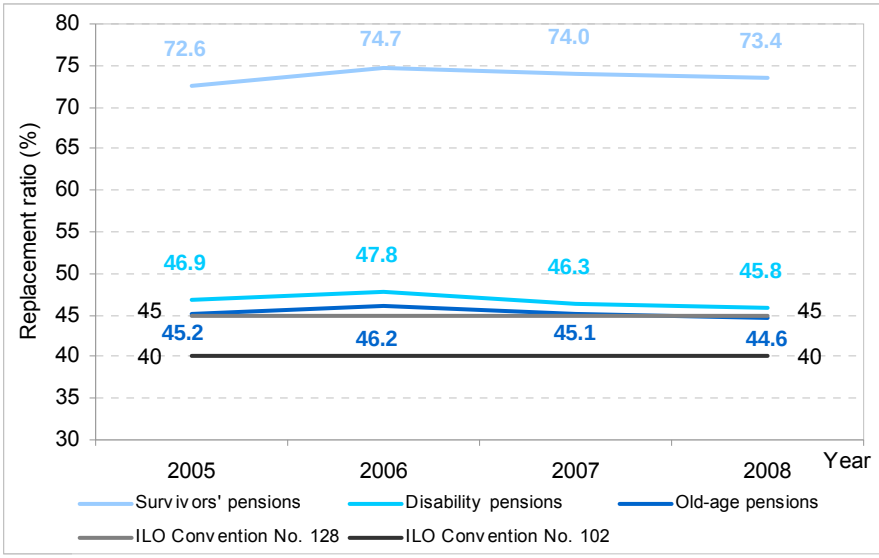
Year	Wage of a skilled labourer (CZK/month)		Benefits for 2 children (CZK/month)	Widow and 2 orphan pensions (CZK/month)	Widow and 2 orphan pensions with benefits		
					amount (CZK/month)	as % of wage of a skilled labourer	
	Gross	Net				Gross	Net
2005	18,717	15,551	1,342	10,927	12,269	61.2	72.6
2006	19,507	15,883	1,193	11,563	12,756	61.6	74.7
2007	20,801	17,048	1,216	12,295	13,511	61.4	74.0
2008	23,002	18 474	1,220	13,234	14,454	59.7	73.4

Source: MLSA
Note: with child benefits = including benefits for two children

[19] This involves in particular increasing tax allowance (tax credit) for a dependent wife or husband.

The Czech Republic **has always fulfilled the ratified Convention** with respect to **full disability pensions** and survivor pensions. The required minimum level (40%) of newly granted full disability pensions in 2004-2006 was met and in the case of net wages of a skilled labourer surpassed the required level in 2007 approximately by some 6.3 percentage points. The ILO Convention No. 102 requires a replacement ratio of 40% for survivor pensions. The level of **survivor pensions** granted **greatly exceeds** the required level both in terms of gross wages and of net wages; the replacement ratio reaches 60-74.7%.

Graph 20. Development of the criteria for fulfilling the conventions for the minimum level of pensions



Source: MLSA

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 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 47 Fulfilment of the ILO Conventions for sickness benefits in 2004-2008

Year	Wage of a skilled labourer (CZK/month)		Benefits for 2 children (CZK/month)	Sickness benefits (CZK/month)	Sickness benefits with child benefits		
					amount (CZK/month)	as % of wage of a skilled labourer[1)]	
	Gross	Net				Gross	Net
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
2007	20,801	17,398	1,216	11,786	13,002	59.1	69.6
2008	23,002	18,824	1,220	11,160	12,380	51.1	61.8

Source: MLSA
Note: [1)] Including child benefits.

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 47 demonstrates that the Czech Republic fulfils these requirements.

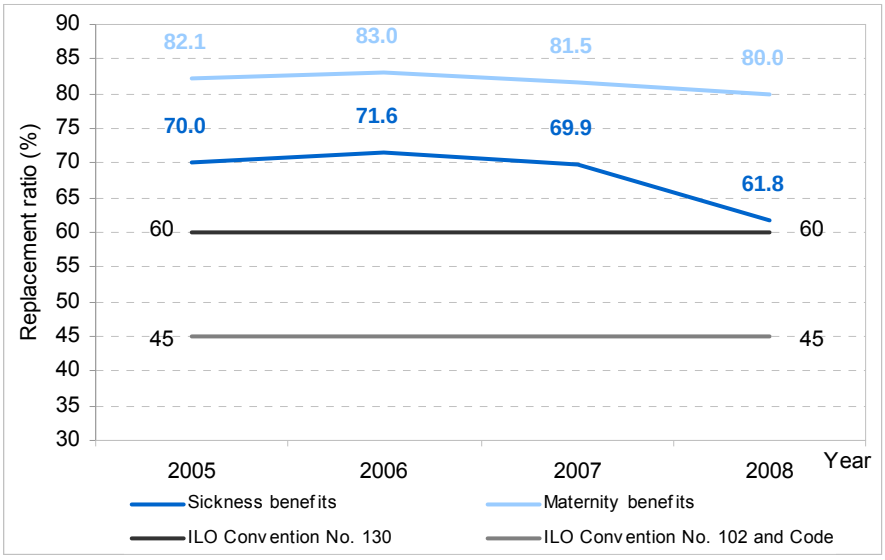
The ILO Convention No. 102 and the Code require that the ratio of the amount of maternity benefits and previous earnings of a typical recipient amount to 45%, which the Czech Republic greatly exceeds.

Table 48 Fulfilment of the ILO Conventions for maternity benefits in 2004-2008

Year	Wage of a skilled labourer (CZK/month)		Maternity benefits		
			amount (CZK/month)	as % of wage of a skilled labourer	
	Gross	Net		Gross	Net
2004	17,682	13,446	11,310	64.0	84.1
2005	18,717	14,171	11,640	62.2	82.1
2006	19,507	14,743	12,240	62.7	83.0
2007	20,801	16,048	13,080	62.9	81.5
2008	23,002	17,474	13,980	60.8	80.0

Source: MLSA

Graph 21. Development of the criteria for fulfilling the conventions for the minimum level of sickness benefits



Source: MLSA

In conclusion, it may be stated that the replacement ratio, which is the criterion 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 2006 and 2007 enabled the replacement ratio to be increased in order for the Czech Republic to fulfil the given criteria. Reduction limits for the calculation of pensions should not be increased less than would

correspond to the increase in wages, otherwise the Czech Republic might cease to be able to meet the ratified conventions for old-age pensions.

The Czech Republic fulfils the criteria of the ILO Convention No. 102 and the Code, which are less stringent. The replacement ratio for old-age and disability pensions is slightly above the level required by the ILO Convention No. 102, whereas the replacement ratio for survivor pensions greatly exceeds the amount required.

The Czech Republic, for the time being, fulfils the required level of the replacement ratio for sickness benefits. When calculating the level of sickness benefits, the fact that Conventions permit a three-week waiting period (the amount of benefit is calculated only from the fourth day of sick leave) has been taken into account.

The decrease in the replacement ratio of sickness benefits was caused primarily by the fact that the reduction limits for setting the daily assessment base were not increased and in 2008 by reducing the percentage rate for setting the daily amount of sickness benefits.

B.2.5. OPERATING EXPENCES

Operating expenses are included in the overall balance of the social security system. Operating expenses of the CSSA, i.e. investments, wage costs, including associated expenditure and material expenses, are relatively low.

Table 49 Operating expenses (CZK million)

		2003	2004	2005	2006	2007	Index 2007/2003 (2003 = 100) nominal	real
Total operating expenses		4,700	5,290	5,580	6,195	6,131	130.4	118.1
Total investments [1)]		544	924	828	1,110	945	173.7	157.3
Of which:	**building and machinery**	500	634	442	384	398	79.6	72,1
	computer technology	44	290	386	726	547	1,243.2	1,125.6
Total administrative costs		4,156	4,366	4,752	5,085	5,186	124.8	113.0
Of which:	**wages and other**	1,601	1,689	1,875	2,129	2,239	139.9	126.6
	premiums and the Cultural and Social Needs Fund	592	625	694	787	830	140.2	126.9
	postage	**578**	**582**	**562**	**582**	**569**	**98.4**	**89,1**
	net material expenditure	**1,385**	**1,470**	**1,621**	**1,587**	**1,548**	**111.8**	**101.2**
Operating costs [2)] **(%)**		1.78	1.85	1.85	1.91	1.71	96.1	87.0
Performance indicator [3)] **(%)**		0.9	0.97	0.97	0.99	0.91	101.1	91.5

Source: CSSA

Notes:

[1] As of 2005, the value of the indicator "*Total investments*" is equal to the value *"Total financing of asset replacement*", and it is subdivided by subprogrammes to building projects and ICT projects (computer technology).
Financing of asset replacement also includes current expenditure, whereas up to 2004 inclusive, the values in Table reflect really only investment (capital) expenditure.

[2] The ratio of total operating expenses (including investment expenditure) to total revenues (%).

[3] The ratio of total operating expenses (including investment expenditure) to the sum of total revenues and expenditure on benefits.

In the year-on-year comparison in 2007 compared to 2006, operating expenses dropped by 1% (due to reducing investments by 15%) and in 2006 compared to 2005 operating expenses increased by 11% (of which investments

increased by 34%). The amount of postage remained in recent years almost unchanged due to the rising share of direct debit and due to the fact that decisions are not delivered to addressees only. 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 current operating needs of the CSSA for ensuring the carrying out of social security.

The CSSA performs extensive tasks both in the field of state income (representing approximately 35% of state budget revenues) and in the field of expenditure (approximately 30% of state budget expenditure). In 2007, its performance indicator amounted to 0.91%. The share of total operating expenditure (including investments) to total income in 2006 reached 1.91% which is the highest level since 2000 (and the same as in 1999). The value of this indicator dropped in 2007 due to an increase in income and decline in operating expenditure to 1.71%.

The comparison of the ratio of administrative costs to the collection of premium for 2001-2005 performed under the project of the Research Institute for Labour and Social Affairs[20] showed that effectiveness of CSSA's premium collection is significantly higher than that of health insurance companies. According to the project's findings, it is difficult to make international comparison in particular due to the different structure of individual insurance systems and the level of insurance premiums, the scope of further activities of premium administrations and uncoordinated methodology for data collection and reporting.

[20] Prušvic, D. et al. Comparison of the collection of premiums and taxes (Research project Ref No. HR 149/06). Prague: Research Institute for Labour and Social Affairs, 2006.

PART C

SOCIAL INSURANCE PROJECTIONS

C.1. PARAMETERS INFLUENCING THE DEVELOPMENT OF SOCIAL INSURANCE

C.1.1. DEVELOPMENT OF BASIC MACROECONOMIC INDICATORS[21]

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 population ageing.

Table 50 demonstrates that the average annual growth rate of real GDP is strongly influenced by the development of employment and hence indirectly in particular by the population's demographic structure. The growth rate of real GDP is significantly 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 the anticipated demographic developments. An absolute decrease in the number of employed persons 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.

Table 50 Development of basic macroeconomic indicators[22]

		2010 -2020	2020 -2030	2030 -2040	2040 -2050	2050 -2060	2060 -2070	2070 -2080	2080 -2090	2090 -2100
Economic level										
GDP, fixed prices	*growth in %*	2.8	2.2	1.6	1.4	1.6	1.7	1.6	1.7	1.8
GDP per capita	*growth in %*	2.7	2.2	1.7	1.6	1.8	2.0	1.8	1.8	1.7
Labour productivity	*growth in %*	2.8	2.5	2.3	2.1	2.0	1.9	1.9	1.9	1.8
Labour market										
Employment	*growth in %*	0.0	-0.3	-0.7	-0.7	-0.4	-0.2	-0.2	-0.1	-0.1
Unemployment rate	*%*	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
Average real wage	*growth in %*	2.8	2.5	2.3	2.1	2.0	1.9	1.9	1.9	1.8
Prices										
Inflation rate	*%*	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5

C.1.2. DEMOGRAPHIC DEVELOPMENTS

All projections of the social insurance system are based on demographic forecasts developed by the Faculty of Natural Sciences of Charles University[23] that

[21] The method used is the same as the one which was used for the work of the Executive Team.
[22] The development to 2010 is based on the Macroeconomic Forecast of the Ministry of Finance (January 2008)

have a horizon of 2065, which was extended by a demographic projection for 2066 - 2100. The horizon of the projection determined in this way enables to demonstrate the developments after overcoming the peak of the demographic shock.

Table 51 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	1.70	1.72	1,73
Life expectancy										
Men *years*	74.1	76.5	78.7	80.4	82.0	83.4	84.6	85.8	86.9	88,0
Women *years*	80.3	82.4	84.0	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: Forecast of the Czech Republic's population developments for 2003 – 2065, Projection of the Czech Republic's population developments for 2066 – 2150

C.1.3. DEVELOPMENTS IN THE PARTICIPATION RATE

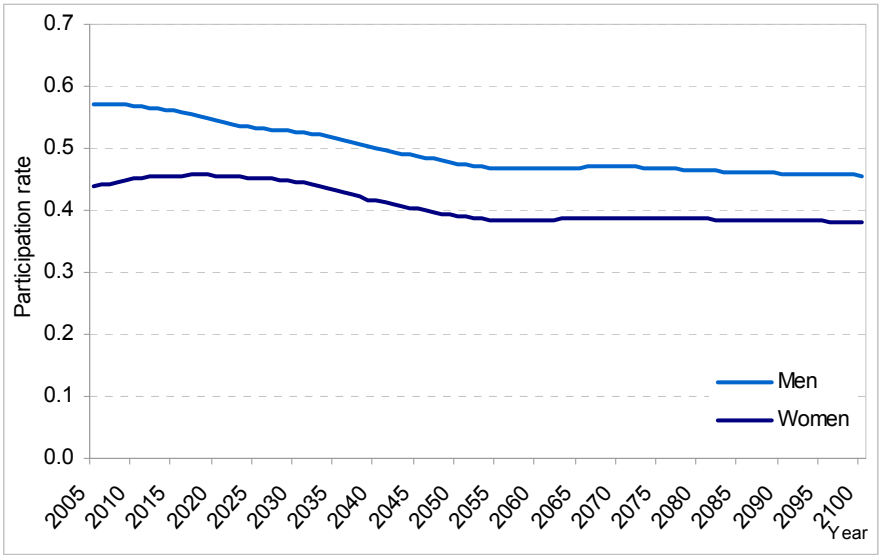
The dynamic method was used for estimating the future rate of participation, which reflects different behaviour of various generations as reflected in the decreasing participation of lower age groups and, on the other hand, the growing participation of higher age groups. The decrease in the rate of participation 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 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 market in contrast with the older generations due to, inter alia, their higher level of education.

[23] The projection of the Faculty of Natural Sciences was completed in September 2003 and is based on the result of the population census carried out in 2001. It was selected as it has the longest horizon which is extremely important for pension system projections.

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

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 22).

Graph 22. Total participation rate in the 15+ age group



Source: Final Report of the Executive Team

C.2. PENSION INSURANCE[24]

C.2.1. PROJECTIONS OF BASIC INDICATORS

The basic indicators of the pension insurance system include:

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

In contrast with the last published report, no measures were taken in the pension system that would have a significant impact on the projections.[25] At the same time, no revisions or updates were made to the demographic prognoses. Given the above, no circumstances occurred that would affect the trends stated in the projections published in the last report. Hence, the following text is only a brief summary of the already mentioned projections and the conclusions ensuing therefrom. Projections are updated but only with regard to actual developments and anticipated short-term macroeconomic developments.

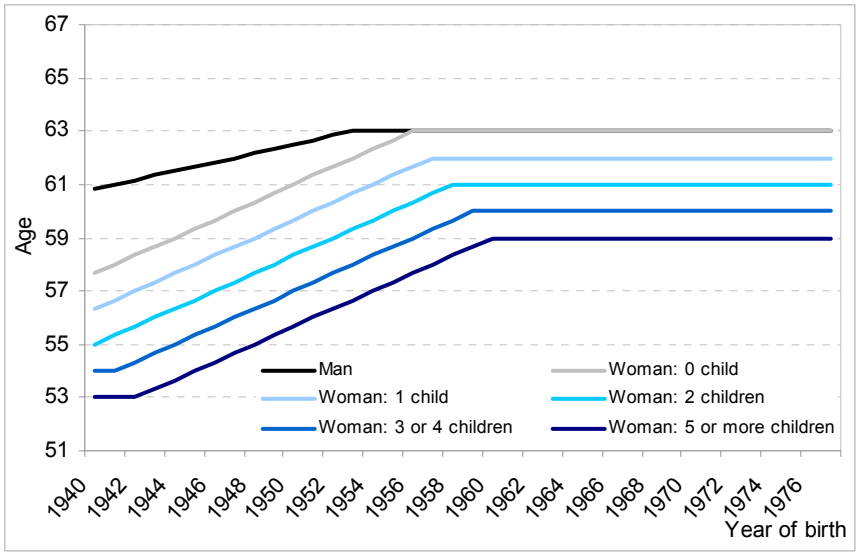
C.2.1.1. Developments in the number of contributors and pensioners

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 pension age (Graph 23), which determines the potential number of old-age pensioners. Other factors, such as the rate of disability do not have in the case of relatively slight increase of the pension age such crucial impact[26].

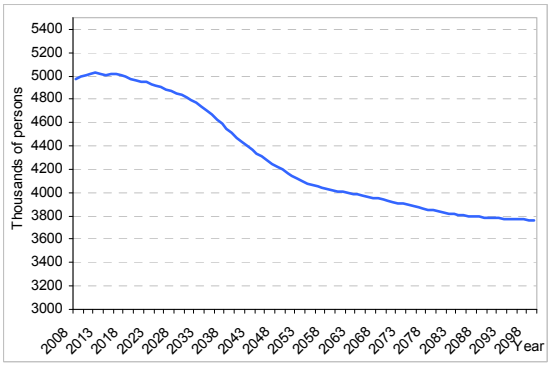
[24] All calculations are based on the status as at the end of 2003 and reflect adjustments to the reduction levels and the valorizations of pensions in 2004, 2005 and 2006.
[25] Except for the proposal for the 1st stage of the pension reform which is discussed in a special chapter.
[26] In the event of a more marked growth in the retirement age, the models show a greater impact also on the number of pensions other than old-age.

Graph 23. Developments in the retirement age



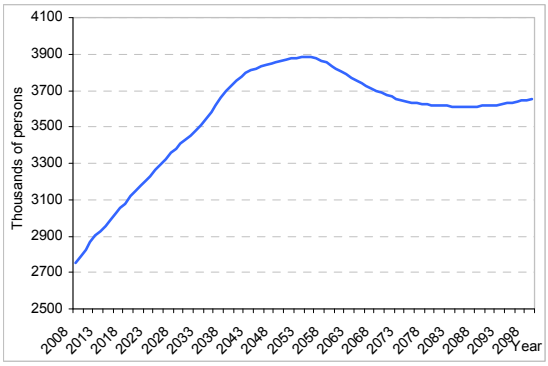
Source: MLSA

Graph 24. Number of contributors



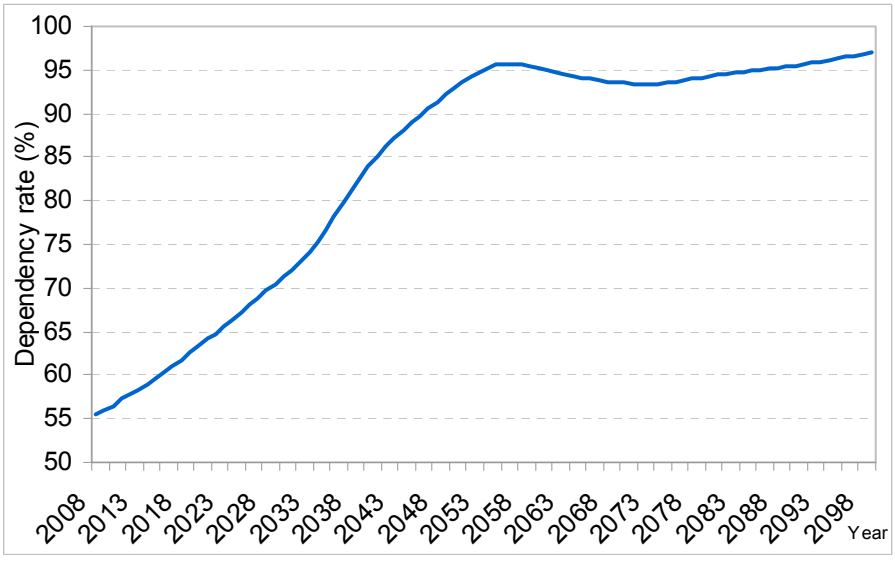
Source: MLSA

Graph 25. Number of pensioners



Source: MLSA

Graph 26. Dependency rate



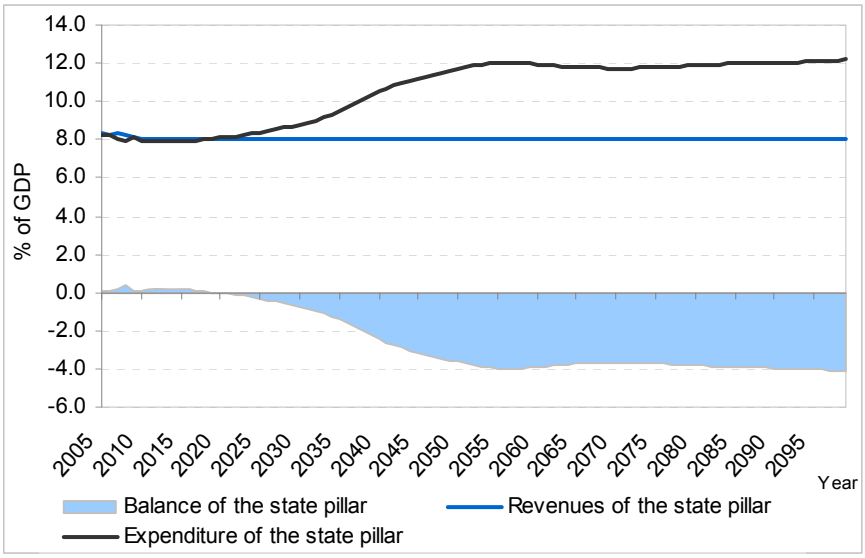
Source: MLSA

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. Development of expenditure and the total replacement ratio [27,28]

The expected change in the demographic situation, to which, under the current setting of the various parameters, the pension system essentially does not react, is reflected in the developments of expenditure and balances of the pension system The system is getting into permanent deficits which are in the range of about 4% of the GDP. After 2020, following rapid growth, expenditure will stabilize at about 12% of GDP. Even though this system is not financially sustainable in the long-run (Graph 27), it is to a great extent dependent on valorization of the pensions paid out only at a minimum statutory level. Failure to fulfil this condition will result in a significant growth in total expenditure.

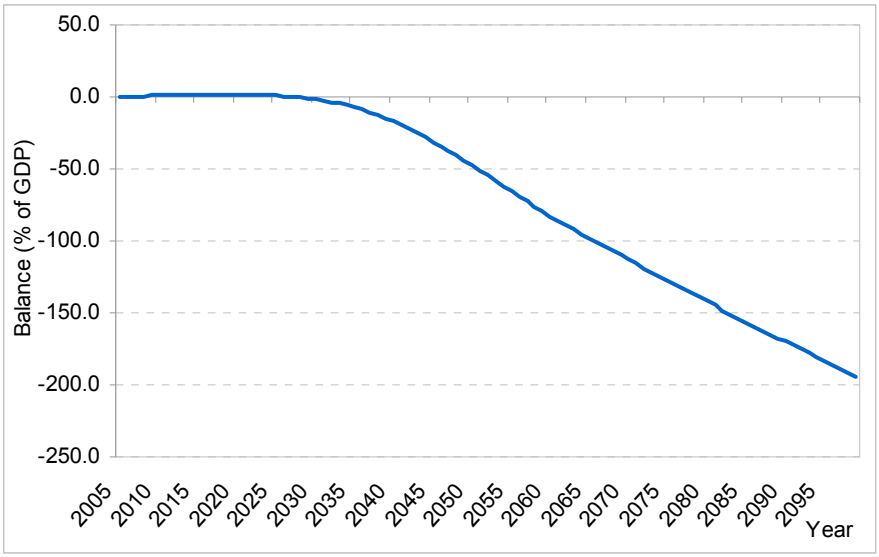
Graph 27. Development of revenues, expenditure and balance of the pension system as a % of GDP[29]



Source: MLSA

[27] The total replacement ratio is the ratio of the average old-age pension to the average wage.
[28] All scenarios do not reflect the prepared extraordinary valorization of pensions from August 2008 that will have no impact on long-term projections.
[29] Under the assumption that the valorization of paid out pensions is carried out only at the minimum level provided for under law.

Graph 28. Cumulative balance (% of GDP)30



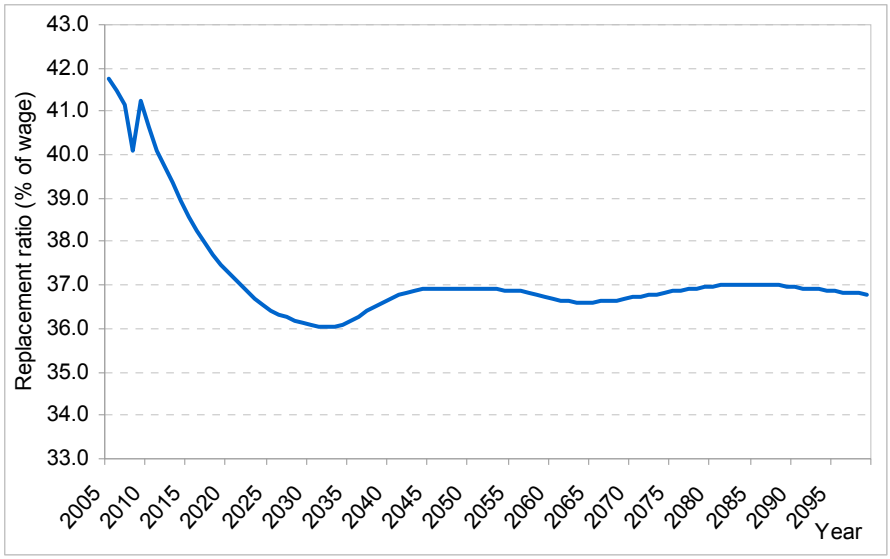
Source: MLSA

The total replacement ratio for about the next 20 years will reflect a growth in the proportion of early 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 replacement ratio. At the same time the higher increase in prices in 2008 will result in an extreme increase in the replacement ratio in 2009[31].

[30] It is expected that accumulation of surpluses will be placed on the capital market within a portfolio of 50 % of shares and 50 % bonds, i.e. with respective returns and that created debt will be covered by government bonds, i.e. with respective interest. 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 of the GDP on interest rates for government bonds.

[31] The projection does not reflect the impact of an extraordinary valorization in 2008 which slightly moderates the shape of the replacement ratio curve.

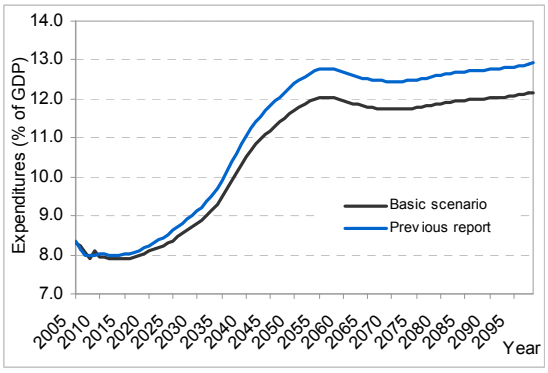
Graph 29. Total replacement ratio (%)



Source: MLSA

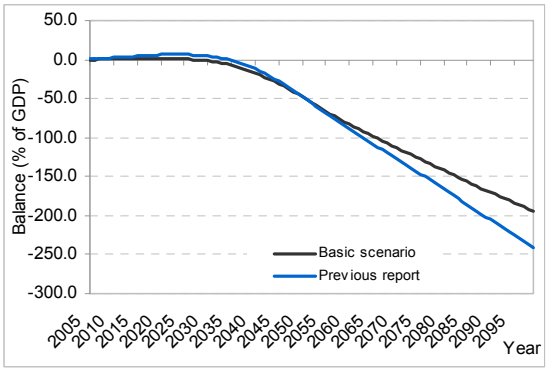
Compared to the previous report there were certain shifts in projections that were caused by different economic developments (higher growth of the GDP and wages and lower unemployment) and also a different (compared to the assumption for long-term projections) setting (or adjustment) of parameters of the pension formula (reduction limit and basic amount) and valorization of pensions, last, but not least, also the by introduction of the maximum assessment base for premiums. The comparison shows that differences occur in particular with respect to future development where a lower level of total expenditure and the total replacement ratio is expected which stems primarily from more rapid anticipated growth of wages to 2010. .

Graph 30. Expenditure on the pension system



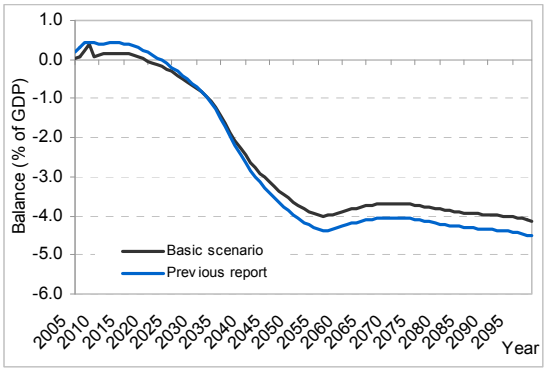
Source: MLSA

Graph 31. Cumulative balance



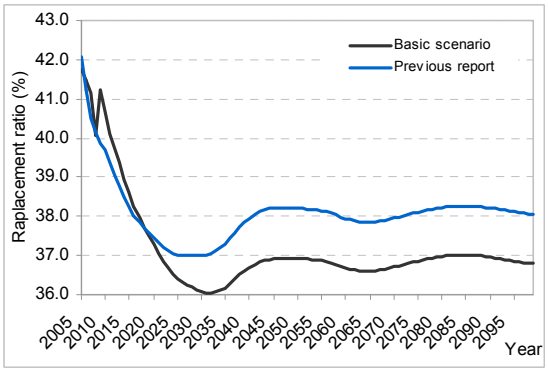
Source: MLSA

Graph 32. Balance of the pension system



Source: MLSA

Graph 33. Total replacement ratio



Source: MLSA

C.2.2. EVALUATION OF DEVELOPMENTS IN KEY INDICATORS

The expected ageing of the Czech population characterized 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 will go into retirement (the post-war and the 1970s generation). Post-war generations do not appear to be such a problem for the pension system as precisely the large 1970s generations 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 transition of these generations from being economically active to retirement will lead to a significant rise in expenditure on pensions in relation to GDP, which may be seen between 2030 and 2050[32].

After 2060, expenditure will become stabilized, however, thereby a deficit of approximately 4% of the GDP will occur in the system each year. Changes to the system should therefore aim to eliminate such expected deficits, while temporary increase in expenditure associated with large generations of the 1970s should be provided for (covered) by a reserve created in advance on the basis of their participation in the labour market.

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 2035. This decrease is seen despite an expected stable relative level for newly granted pensions. The main reason for such a decrease is the increasing proportion of reduced early (i.e. lower) pensions to the total number of old-age pensions. The expected valorizations at the minimum level provided for under the law (i.e. 100% growth in prices and 1/3 growth in real wages) also had a limited impact. After 2035, a slight increase in this relation should occur and should stabilize at a level around 37%. 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.

[32] Dynamics of the growth of expenditure in relation to the GDP is strongly influenced by setting the parameters of the pension system, in particular the pension age (see Chapter C.2.3.1)

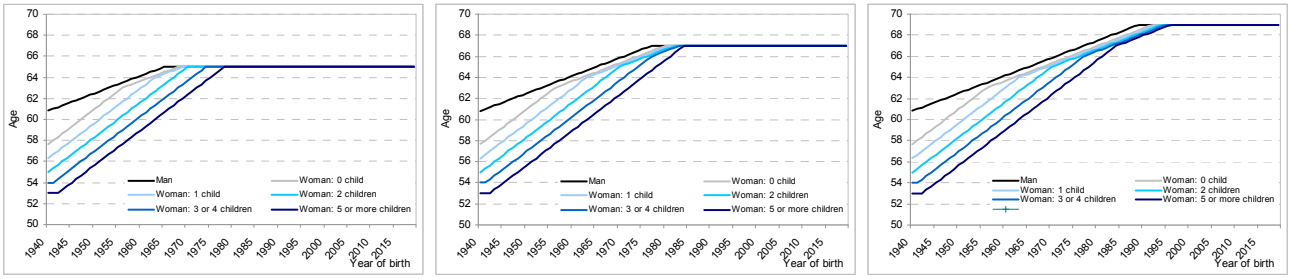
C.2.3. SENSITIVITY OF BASIC INDICATORS OF THE PENSION INSURANCE SYSTEM TO CERTAIN PARAMETERS

In terms of the current or future discussions on changes to the pension system in connection with anticipated impacts of the population ageing, effects of certain basic parameters on the overall future system stability need to be presented, under various sensitivity scenarios that assume a change in one specific parameter only and do not constitute comprehensive reform measures. The parameters that most significantly affect the development of the pension system or its balance include the setting of the retirement age (or its adjustments) and the manner and level of valorization of the pensions paid out.

C.2.3.1. Additional increases in the retirement age

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

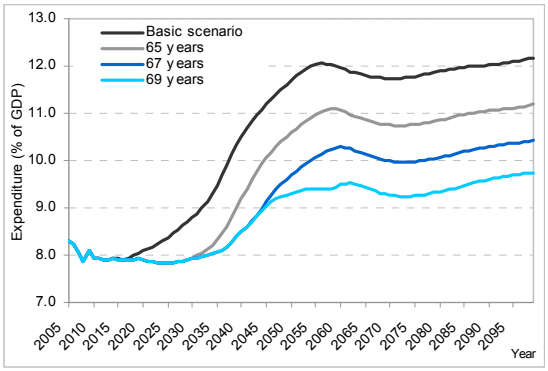
Graph 34. Process of increasing the retirement age to 65, 67 and 69 years



Source: MLSA

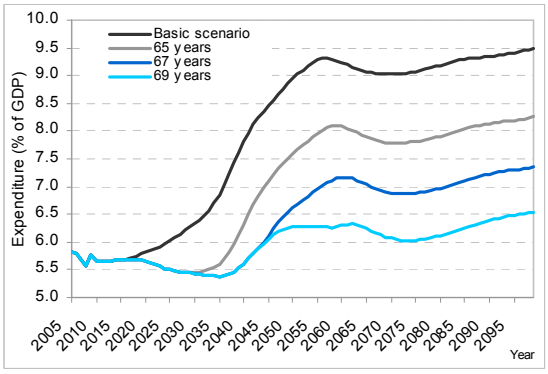
Of the basic indicators, expenditure on pensions (as a proportion of the GDP) is the most sensitive to the retirement age. Under the basic scenario, the expenditure grows in the long-term to 12% of GDP. Increasing the retirement age to 65 (from 63 under the basic scenario) reduces expenditure in the pension system in the long-term to 11% of GDP. Additional gradual increases up to the age of 67 would result in a long-term stabilization of expenditure on pensions at a level of about 10% of GDP. If such increases were to continue up to an age of 69, then expenditure on pensions would, in the long-term, be in the region of 9.5% of GDP.

Graph 35. Expenditure on pensions (% of GDP)



Source: MLSA

Graph 36. Expenditure on old-age pensions (% of GDP)

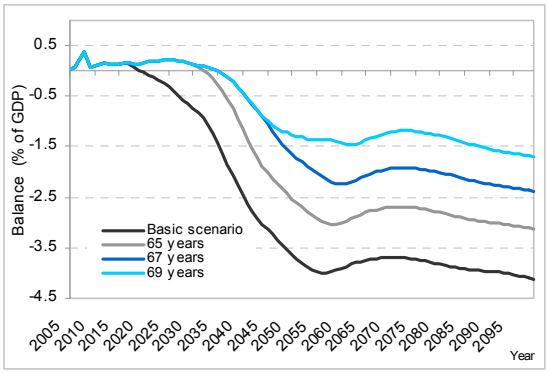


Source: MLSA

Under scenarios with higher retirement ages, the growth of expenditure other than old-age pensions is also seen very markedly (especially in disability pensions).

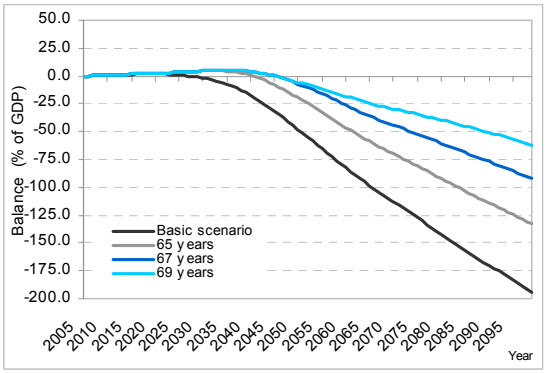
Taking into account the projected stability of revenues of the pension system in relation to the GDP (which ensues from the structure of the macroeconomic scenario) the development of expenditure is key for balancing the system. In comparison with the basic scenario, all scenarios with an increase in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

Graph 37. Balance of the pension system (% of GDP)



Source: MLSA

Graph 38. Cumulative balance (% of GDP)



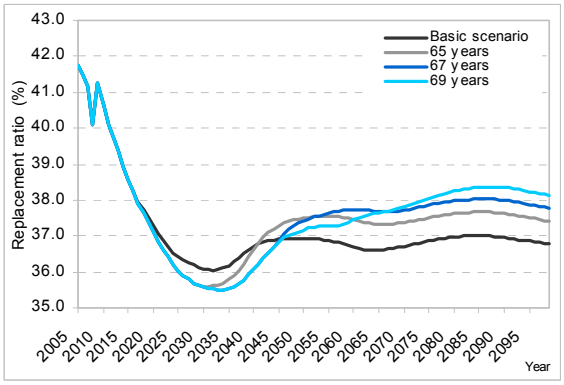
Source: MLSA

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 by 140% of the GDP lower than under the basic scenario, reaching still significant 60% of the GDP.

The scenarios using 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 completion of the process of increases to the retirement age, the replacement ratio will be slightly

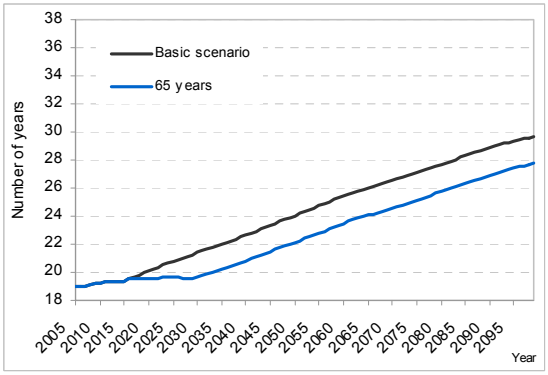
higher than under the basic scenario as pensions are paid out for a shorter period of time, i.e. relatively in relation to the average wage their level decreases less by valorization (lower than wages).

Graph 39. Total replacement ratio (%)



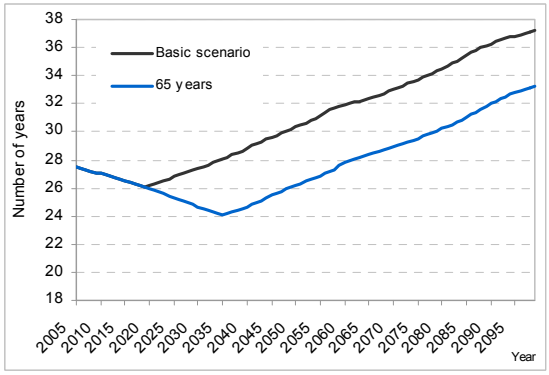
Source: MLSA

Graph 40. Average pension drawing time (number of years) - men



Source: MLSA

Graph 41. Average pension drawing time (number of years) – women



Source: MLSA

Table 52 Life expectancy at 60 and 65 years

	2005	2010	2020	2030	2040	2050	2060	2070	2080	2090	2100
Life expectancy - men											
at 60 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	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	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	20.9	21.6	22.9	24.1	25.5	26.9	28.4	29.5	31.0	32.8	33.9

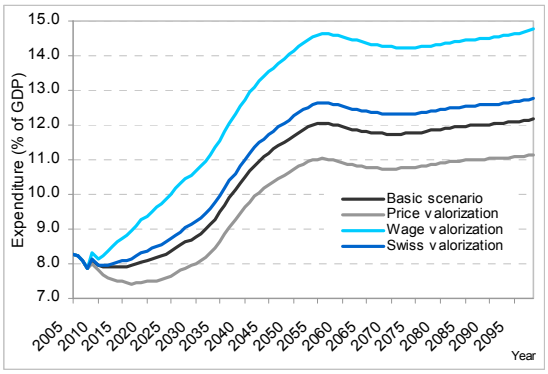
Source: MLSA

C.2.3.2. Method of valorizing pensions

In order to demonstrate the sensitivity 4 additional scenarios where chosen: valorization only reflecting the growth in prices (CPI), valorization reflecting the growth in prices and 1/3 of the growth in real wages (the minimum valorization under 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.

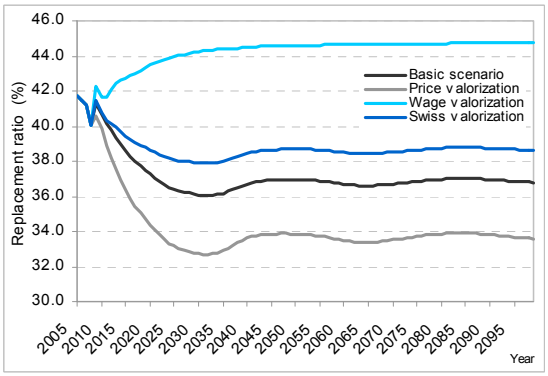
Changes to the valorization scheme affect expenditure on the pension system only through its effects on the relative amounts of the pensions paid out. No changes are made either to the number of pensions granted or paid out, or to the amount and the replacement ratio of newly granted pensions. Differences in the amounts of expenditure under the individual valorization scenarios may be fully explained by comparing them with the total replacement ratio.

Graph 42. Expenditure on pensions (% of GDP)



Source: MLSA

Graph 43. Total replacement ratio (%)



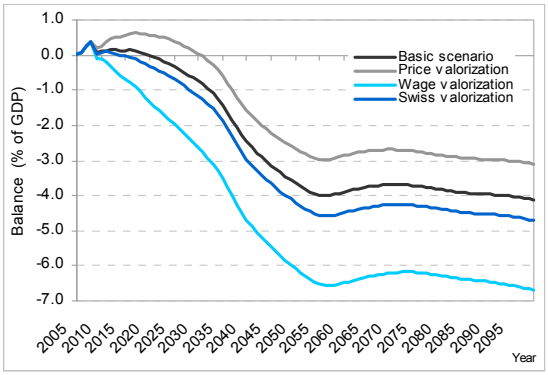
Source: MLSA

Expenditure on the pension system is the lowest one under the least generous valorization option which is the price valorization. In contrast, wage valorization and Swiss valorization (at 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 this year on the debt of the system cumulates, which at the end of the projected period may be at almost 350% of the GDP. The high debt of the system is a direct result of high long-term deficits which amount to about 6.5% of the GDP annually. Similarly, under the Swiss valorization the temporary cushion created from the restructuralization of the insurance rate in 2004 is drawn down sooner than under the basic scenario. From 2014 onwards, the pension system will have permanent deficits. Their amount will be stabilized in the long-term at the level in the region of 4.5% of the GDP. Under this scenario, surpluses of the pension system will be used up in 2020, 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 230% of the GDP.

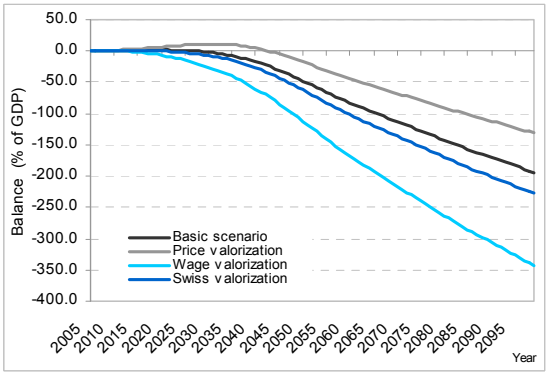
Price valorization defers up to 2031 the moment when the pension system will go into deficit. Up to this year, the pension system will have surpluses of up to 1% of the GDP. However, even this scenario has, in the long-term, large deficits which amount to 3% of the GDP. Not even limiting the growth of pensions in applying price valorization is capable of preventing the rapid growth of expenditure after 2030. Up to 2030 the cumulated surpluses would amount to about 10% of GDP. Such surpluses would permit financing of deficits of the pension system up to 2043. However, at the end of the horizon of the projected period there would be a projected debt reaching almost 130% of the GDP.

Graph 44. Balance of the pension system (% of GDP)



Source: MLSA

Graph 45. Cumulative balance (% of GDP)



Source: MLSA

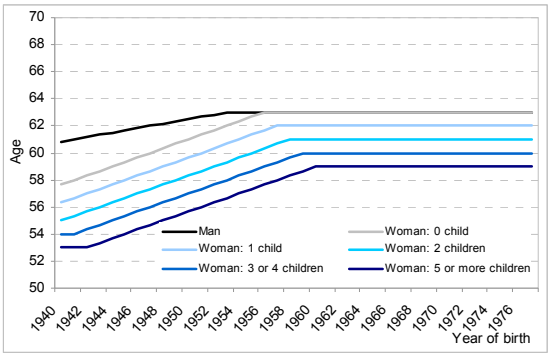
C.2.4. PROJECTIONS OF IMPACT OF PARAMETRICAL CHANGES ON THE DEVELOPMENT OF BASIC PENSION INSURANCE INDICATORS

As noted in subchapter A.2.1., within the first stage of the pension reform proposed parametrical changes to the basic pension insurance have been approved. These changes include in particular continuation in the process of gradual increases in the pension age to 65 years for men, childless women and women who have brought up one child and to 62-64 years for other women, gradual extension of the insurance period required for entitlement to the old-age pension from 25 years to 35 years, including non-contributory insurance periods, limitations on crediting of non-contributory insurance periods and measures in support of gradual retirement. In connection with gradual increases in the retirement age also the period for early old-age retirement will be gradually extended, namely up to 5 years for the retirement age of 65 years. The extended scope of an early old-age retirement will be also associated with various levels of reduction in the percentage-based assessment of pensions that will depend on the length of the period of an early old-age retirement. Furthermore, inter alia, also an administrative change of the full disability pension to the old-age pension upon reaching the age of 65 will be introduced, disability will be newly defined based on three degrees and the age limit for the "permanent" entitlement to the widow and widower pension will be introduced.

C.2.4.1. Expenditure and balance of the pension system

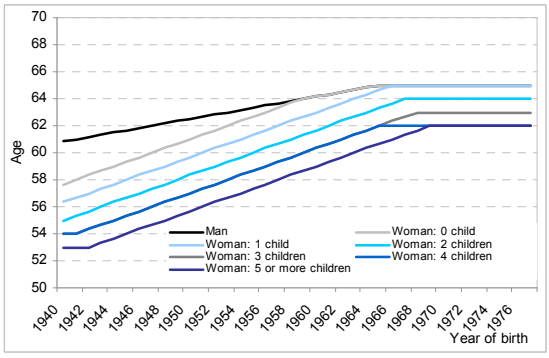
Changes (approved) within the 1st stage of the pension reform will contribute significantly to improving financial sustainability of the basic pension insurance. The implementation of all these measures should result in the medium and long term in gradual decrease in total expenditure on pensions by about 1% of the GDP. In terms of **economic impacts**, the key measure is to continue the process of increases in the retirement age.

Graph 46. Increasing the retirement age – current status



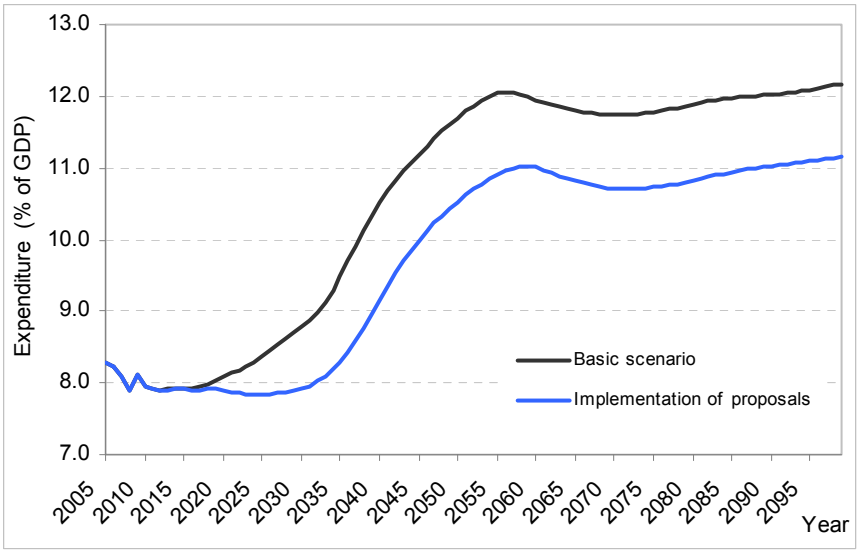
Source: MLSA

Graph 47. Increasing the retirement age – approved changes



Source: MLSA

Graph 48. Expenditure on pensions (% of GDP)



Source: MLSA

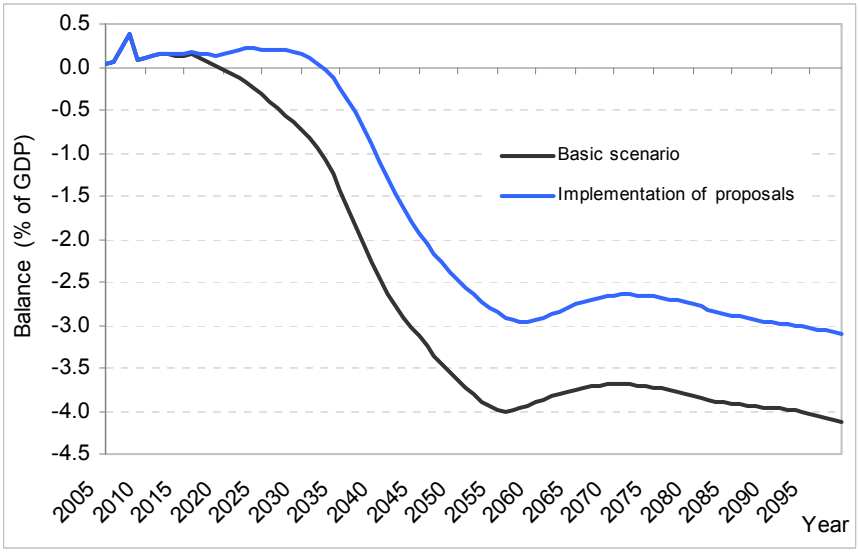
According to the projection of the Economic Policy Committee (EPC) and the European Commission of 2005[33] the Czech Republic ranked among the countries with the highest anticipated increase in expenditure on pensions from the public pension systems and the tenth highest expenditure on these pensions in the EU (excluding Greece) in 2050. It may be anticipated that the measures taken within the first stage of the pension reform will improve the Czech Republic's relative position compared to other EU Member States.[34] Parametrical changes (adjustments) will allow to balance out the pension system up to closely beyond 2030 (Graph 49). Delaying the moment when expenditure in a given year exceed revenues from

[33] Economic Policy Committee and the European Commission (2006): The impact of ageing on public expenditure: projections for the EU25 Member States on pensions, health care, longterm care, education and unemployment transfers (2004-2050).

[34] New projection will be published in the first half of 2009.

premiums for pension insurance will create the scope for the preparation and implementation of possible additional measures. The need for further changes is indicated by the long-term projection which shows that the system despite improved balance will end in deficit of about 3% of the GDP.

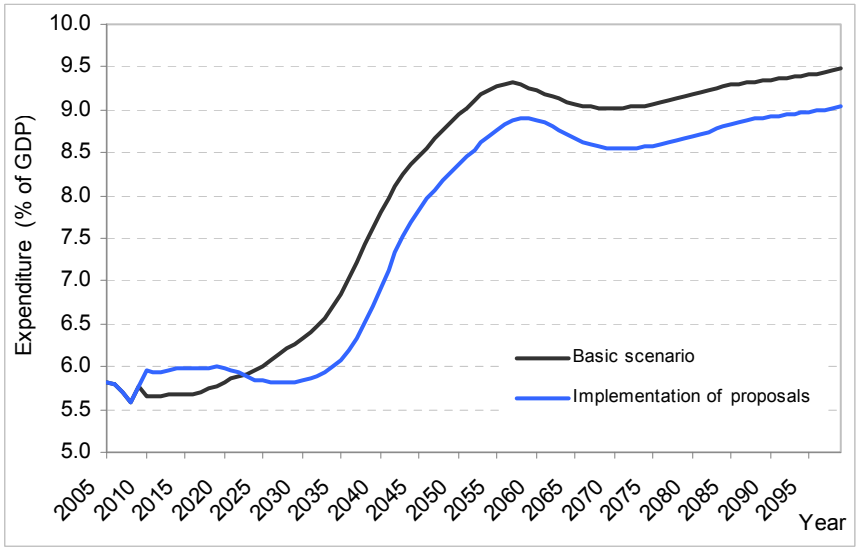
Graph 49. Balance of the pension system (% of GDP)



Source: MLSA

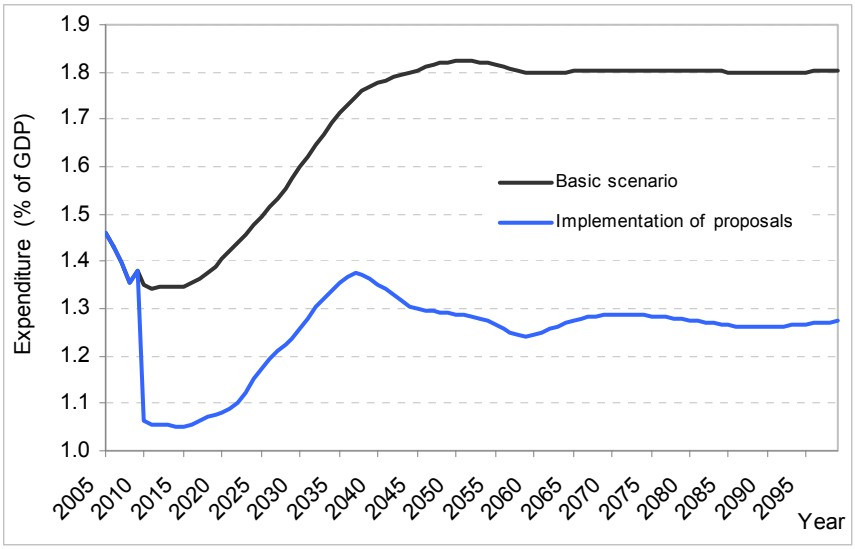
Expenditure within subsystems of old-age pensions and disability pensions, apart from further increases in the retirement age, will reflect an "automatic" change of the full disability pension to the old-age pension after reaching the age of 65 years. This measure results in an extreme increase in expenditure on old-age pensions and corresponding decrease in expenditure on disability pensions.

Graph 50. Expenditure on old-age pensions (% of GDP)



Source: MLSA

Graph 51. Expenditure on disability pensions (% of GDP)

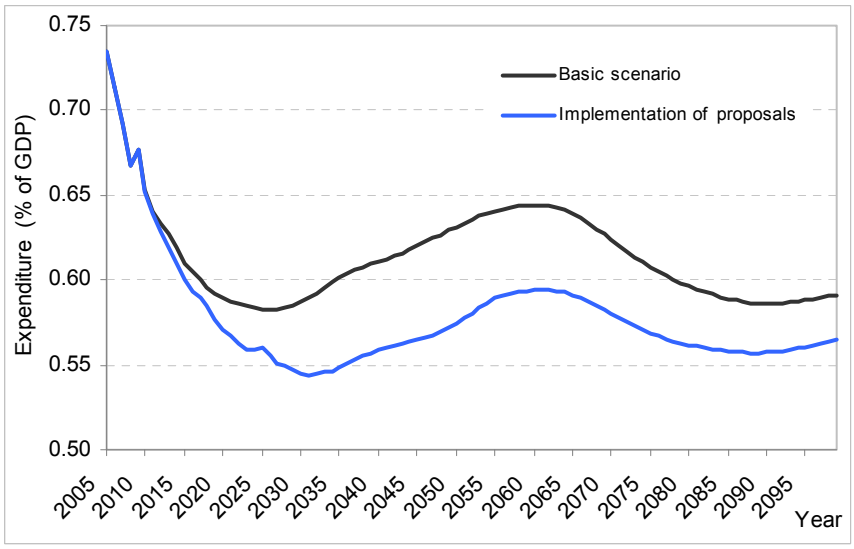


Source: MLSA

Graphs 50 and 51 show that “shift in expenditure“ will in the first year when the Act comes into effect amount to about 0.3% of the GDP and will gradually increase over time, while in the long-term it will amount to 0.5 – 0.6% of the GDP. This increase stems from the rising number of persons receiving the full disability pension who are older than 65 years. Expenditure on disability pensions gradually reflects positive impact of the introduction of disability based on three degrees.

Expenditure on survivor pensions is affected by unification of the age for "permanent“ entitlement to widow or widower pensions and its increase which corresponds to the increase in the pension age. Due to a low share of expenditure on survivor pensions as % of the GDP and a relatively minor change, savings arising from this measure are negligible, although they increase over time and around 2050 reach about 0.06% of the GDP. Subsequently, the impact is reduced and values of about 0.03% of the GDP are indicated.

Graph 52. Expenditure on survivor pensions (% of GDP)



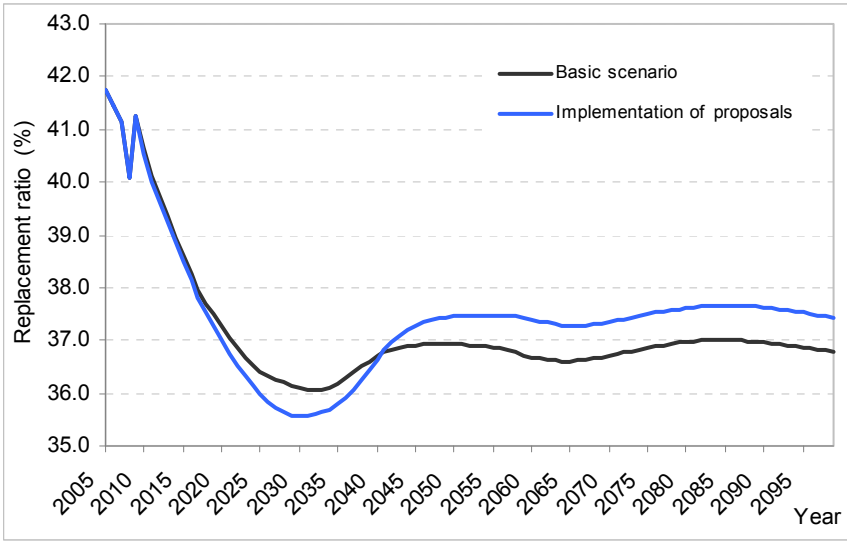
Source: MLSA

C.2.4.2. Replacement ratio

The development of the total replacement ratio is influenced also by the development of the retirement age. It is obvious that further increases in the retirement age result in the short term in an additional decline in the total replacement ratio (below the level of the basic scenario), while subsequently the replacement ratio rises even above the level reached under the basic scenario.

A change of a part of full disability pensions to old-age pensions has a certain, though negligible impact on the total replacement ratio, approximately by 0.1 percentage points. This stems from the fact that full disability pensions paid out after reaching the age of 65, are on average lower than old-age pensions, including early old-age pensions. The total replacement ratio will reflect also higher coefficient for reducing early pensions, but its effect will be only negligible since the proportion of persons who retire by more than 2 years earlier prior to reaching the retirement age is only about 10%. The impact of extending the period for early retirement will depend on the extent to which this option will be used by insured persons.

Graph 53. Total replacement ratio (%)

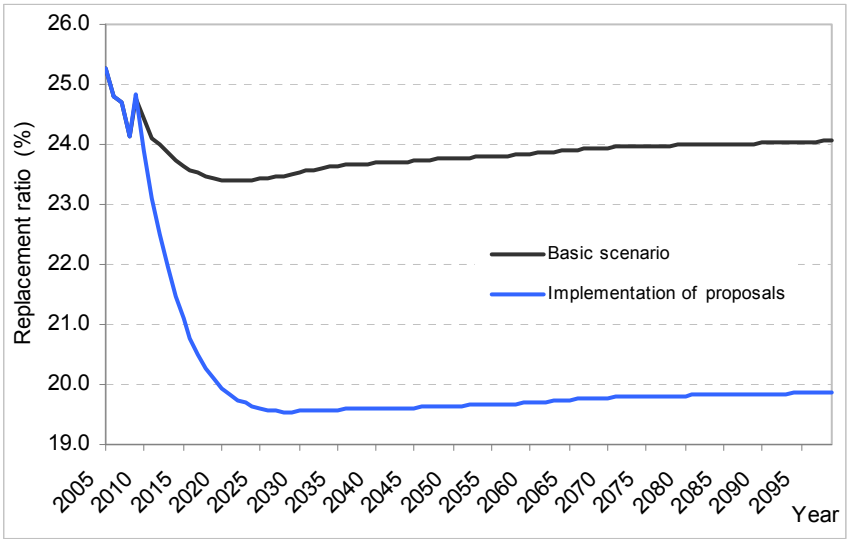


Source: MLSA

The replacement ratio within the subsystem of partial disability pensions that will be gradually changed to the 1st degree or the 2nd degree disability pensions, will decline due to the lower amount of newly granted 1st degree disability pensions. Model calculations show that the transitional period from the current system of the 1st degree and the 2nd degree partial disability pensions should last about 20 years, i.e. beyond 2030.

The target status then envisages a relative decline in the level of pensions paid out within this subsystem in relation to the average wage in the national economy by about 18%.

Graph 54. Replacement ratio for partial disability pensions or the 1st degree and the 2nd degree disability pensions (%)



Source: MLSA

C.2.5. CONCLUSIONS

Parametrical changes implemented at the first stage of the pension reform will be necessarily followed up by additional changes, in particular those targeted on the retirement age

As the updated projections show, the pension system, in terms of setting of its parameters, is financially unsustainable in the long term prior to the implementation of the steps envisaged within the first stage of the pension reform. Even if relatively restrictive assumptions are met[35] around 2020 the system would plunge into permanent deficits that would reach 4% of the GDP in the long-term: the long-term financial unsustainability of the pension system and its deficit trends are caused in particular by the anticipated demographic developments associated with the population ageing whose distinctive feature is the rising number and share of persons in higher age brackets. The changes envisaged within the first stage of the pension reform, in particular in respect of the retirement age, but also in the area of disability pensions, respond to these anticipated demographic developments and boost short-term and long-term sustainability. Nevertheless, even after the implementation of these adjustments, the pension system remains to be financially unsustainable in the long term, with anticipated deficits of 3% of the GDP. However, the moment when expenditure will exceed revenues from premiums has been deferred, by about 13 years beyond 2030. Consequently, this is the period of the following about 25 years which is basically the time for which the retirement age will be increased, while these positive effects are to a large extent contingent upon the above restrictive policies in particular in respect of valorization of the pensions paid

[35] This is in particular the assumption that the valorization of paid out pensions is carried out only at the minimum level provided for under law.

out[36].The above analyses imply that the performed parametrical changes are not sufficient in the long term and further changes will necessarily follow, in particular in the area of the retirement age. On the other hand, the question is whether it is appropriate to make already now definitive changes to the retirement age (entrenched in legislation), beyond 2030, since with longer period the level of uncertainty in demographic forecasts is growing. Nevertheless, it would be beneficial if the specific proposal for a legislative regulation of the retirement age for the following period be supplemented with a long-term concept explaining the context of its setting that would be revised on the basis of current demographic forecasts and that would serve as the basis for further changes.

In connection with the setting of the retirement age there are certain trends geared towards "automation" of the process of its changes, with no need for a political debate on it. This automation may be either direct (change to the retirement age based on demographic data – e.g. Denmark) or indirect based on linking the amount of the newly granted pension to life expectancy or the introduction of contribution defined schemes (Notional Defined Contribution, NDC or Financial Defined Contribution, FDC). This automatic approach, however, may result in higher uncertainty of participants in the system when they will be allowed to retire (i.e. what retirement age will be set or when their pension will be sufficient for DC schemes).

Parametrical changes need to be supplemented with a reform leading to the diversification of the system

Even though increases in 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 reform. Such a reform should be targeted at diversification of both revenues and 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**
  Possible strengthening of the equivalence of pensions is due to the possibility of lowering the pension levels for lower income groups.[37]. The room for differentiation of pensions is given by the differences in the minimum pension granted and the average pension. The possibilities of differentiating pensions depend also on the level of premium limits which in a way determines to what extent differentiation in the system of basic pension insurance should be dealt with. In case of relatively low limits of premiums, the differentiation will be the task of rather supplementary schemes. In contrast, with a high level of premium limit or its non-existence such differentiation must be dealt with within the system of basic pension insurance. Increasing the equivalence, while

[36] Implementation of e.g. wage valorization instead of the minimum level would drive the system into deficit already around 2010, i.e. sooner than changes made in the 1st stage of the pension reform would show any effect whatsoever.

[37] Generally, also the option may be envisaged that would retain the current level of pensions for insured persons in lower income brackets and strengthen the equivalence by increasing revenues (by higher rate of premiums) which is, however, given a very high level of premium in the Czech Republic, currently amounting to 28 %, only hardly acceptable.

maintaining the level of total system costs and the existing protection against the risk of poverty in old age, should be achieved for the middle and higher income groups at the cost of strengthening the levelling of pensions 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 allocated to covering a minimum pension and the remainder is allocated to the equivalency (ideally DC) scheme. 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 part of the premium is allocated to the equivalent (ideally DC) scheme. Both of the above-mentioned options would enable the introduction of funding elements of financing.

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 (contributors) and beneficiaries of benefits are not a basic indicator for projections of 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 for employees and the self-employed, two groups of insured persons exist: employees and the self-employed. The proportion of the voluntarily insured self-employed to the total number of the self-employed covered by pension insurance has gradually decreased from 51% in 2000 to 37% in 2007. 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 premiums for pension insurance. However, the absolute total number of persons covered by sickness insurance will be lower by the number of the self-employed who choose not be insured under sickness insurance (at the moment these are approximately 500,000 people).

Revenues from premiums for sickness insurance depend on the number of contributors, the amount of the assessment base, the contribution 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.2.1.2., Graph 27), however their absolute amount will vary according to the prescribed amount of the contribution rate.

New measures will have effect on **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. **For this reason, short-term projections are preferred.**

C.3.1.1. Changes in sickness insurance made in 2008

C.3.1.1. Stabilization of public budgets

Under Act No. 261/2007 Coll. on the stabilization of public budgets, as at 1 January 2008, the following changes were made to the manner of determination of the amount of sickness benefits.

a) for 2008 reduction limits have not been increased;
b) for determination of the amount of sickness benefits and family member care benefits, only 90% of the amount of the daily assessment base are counted into the first reduction limit even after the elapse of the first 14 days of sick leave or the need to care for a family member;

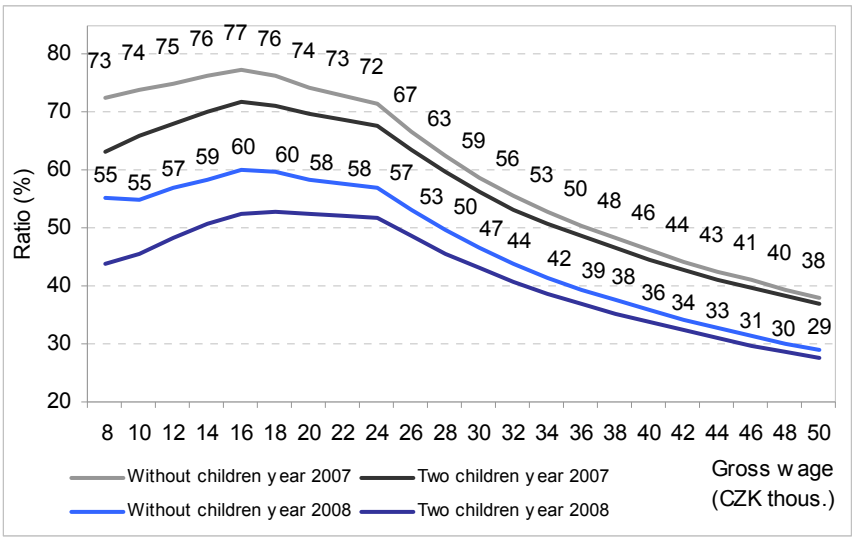
c) for the first three calendar days of sick leave insured persons are not entitled to sickness benefits (wage compensation);
d) the amount of sickness benefits (for calendar day) is calculated at the rate of 60% of the daily assessment base, if this is the 4th to 30th calendar day of sick leave, at the rate of 66%, if this is the 31st to 60th calendar day of sick leave and at the rate of 72% from the 61st calendar day of sick leave;
e) the amount of family member care benefits (for calendar day) will be calculated at the rate of 60% of the daily assessment base.

Financial impact on insured persons

The decrease in the level of sickness benefits is shown in the following graph that compares the ratio of sickness benefits to net wage in 2008 and in 2007.

While in 2007, the replacement ratio for insured persons receiving wage up to CZK 24,000 per month exceeded 70%, in 2008 this is by about 15 percentage points less. For insured persons with income amounting to double the average wage in the national economy, the replacement ratio dropped to about 36% only. The ratio of sickness benefits to net wage for insured persons with children is lower because net wage also includes the amount (CZK 890 in 2008 and CZK 500 in 2007) for each child.

Graph 55. Ratio of sickness benefits for the first 30 days of sick leave to net income



Source: MLSA

Evaluation on the basis of CSSA statistics – mostly for sick leave in January to June 2008.

- The number of reimbursed days of sick leave was by **7.8 million days, i.e. 18% lower**, than in the same period of 2007. Compared to 2007, the number of reimbursed days decreased in all months of 2008. The highest decrease in the number of reimbursed days (by almost ¼) was recorded for sick leave in February and June.
- **Expenditure on sickness benefits (per 1 benefit)** amounted to **mere 83% of the amount** reimbursed in the same period of the last year and hence was by CZK 2.5 billion lower. Expenditure in January 2008 (mostly for sick leave of 2007) was even by 13% higher than in January 2007, however, since February a

significant decrease in expenditure has been recorded. The highest decrease occurred in respect of sick leave in February when by 26% less funds were paid than in the same month of the previous year. It needs to be noted that a decrease in expenditure occurs only in the case of sickness benefits, whereas expenditure on maternity benefits has been steadily rising.

- With respect to employees of small organizations **cases of sick leave** for the first three months of 2008 dropped by almost one third (from 186,000 to 123,000). The highest decrease was recorded in cases with duration less than 14 calendar days. For instance, the number of cases with duration of up to one week decreased from 28,000 to 14,000, i.e. by one half.

The introduction of the waiting period (the period for which sickness benefits are not provided, i.e. for the first 3 calendar days of sick leave or quarantine) was intended as a measure conducive to the responsible approach of insured persons towards sick leave, reduction of cases of its abuse during short-term sick leaves where it is impossible to prove objectively whether they are justified or not. This purpose has been met.

3.1.1.2 Ruling of the Constitutional Court

In April 2008 the Constitutional Court cancelled with effect from 30 June 2008 the institute of the so-called waiting period**.** The Constitutional Court justified its decision also by reference to the breaching of the insurance principle in sickness insurance, since an employee remains for the first 3 days of sick leave without financial means, whereas his obligation to pay premium remains unaffected. As the Constitutional Court set the effective date of the ruling in such a manner that the Government, the Parliament and the President could not approve within the legislative process with effect from 30 June 2008 the appropriate legislation reflecting the Court's ruling, employers and sickness insurance authorities had to change shortly after the effective date of the Court's ruling the system of calculation of sickness benefits. The above decision means that until 29 June 2008 sickness benefits were provided only from the fourth calendar day of sick leave. Since 30 June 2008 the amount of sickness benefits to the 30th day of sick leave was 60% of the daily assessment base.

Evaluation on the basis of CSSA statistics – mostly for sick leave for July and August 2008.

- **The number of reimbursed days of** sickness was in the period under review by 620,0000, **i.e. 5% lower** than in July to August of 2007. The trend of decreasing number of the reimbursed days of sick leave in 2008 slowed down by 13 percentage points, but despite this the recorder number of days was the lowest one of all July and August periods since 2003.
- **Expenditure on sickness benefits** (**per 1 benefit**) amounted to **96% of the amount** paid out in the same period of 2007 and hence was by some CZK 150 million lower. The favourable developments in the decrease of expenditure also slowed down by 13 percentage points.

As a result of the ruling of the Constitutional Court, state budget expenditure on sickness insurance increased not only due to the fact that sickness benefits were again provided for the first three days of sick leave, but also because favourable developments of decreasing sickness rate were now slower.

Also expenditure on implementation of sickness insurance for employers and sickness insurance authorities increased. As the effective date of the ruling of the

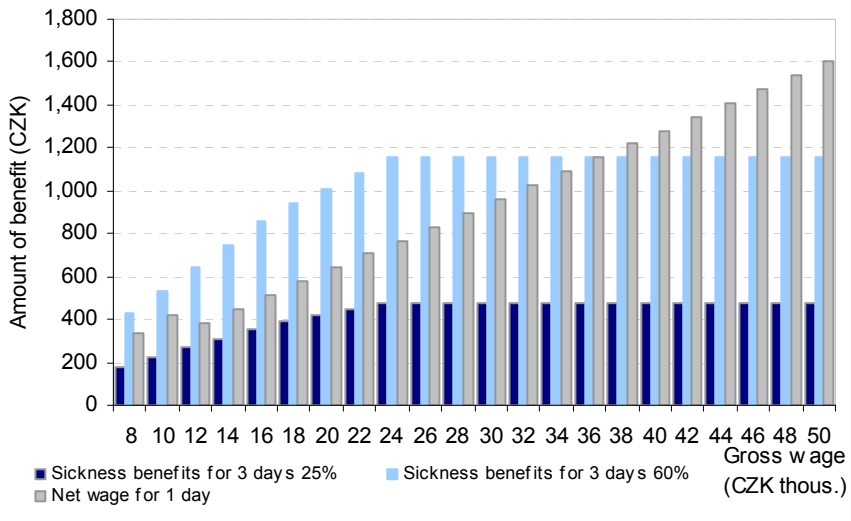
Constitutional Court was set for 30 June 2008, the programmes for calculation of sickness benefits had to be adjusted also for a part of June.

3.1.1.3 Changes as from 1 September 2008

Since 1 September 2008 under Act No. 305/2008 Coll., the rate for calculation of sickness benefits for the first 3 calendar days of sick leave has been decreased from 60% to 25%.

In order that the sickness benefit for the first three days of sick leave be lower than net wage for one day, the rate of daily sickness benefits should not exceed 35%. In the case of sickness benefits at the rate of 60% of the daily assessment base for the first three days of sick leave, it is advantageous to draw sickness benefits for a three-day period commencing on Friday or Saturday for all income categories with gross wage of up to CZK 36,000 per month. The following graph shows that insured persons with monthly income between CZK 14,000 and 24,000 in case of sick leave from Friday to Sunday at the daily rate of 60% will receive in addition half or up to two thirds of their net daily wage, compared to the situation if they were not sick at all. Individual cases differ not only by the amount of wage, but also by the number of working days in a month.

Graph 56. Comparison of the amount of sickness benefits for 3 days of sick leave and net wage for one day



Source: MLSA

The lower ratio of sickness benefits for the first three days of sick leave to net wage for one day in the first two mentioned zones is caused by the tax legislation of 2008. The calculated 15% tax is lower than basic personal tax credit per taxpayer because this credit (CZK 2,070 per month) is reflected fully only in incomes over CZK 12,000. Radical change for both curves occurs in the zone of reduction limits for determining the daily assessment base for the calculation of the amount of sickness benefits.

A summary of changes to the parameters for calculating the amounts of sickness benefits in 2008 is set out in the following Table:

Table 53 Parameters for calculating the amounts of sickness benefits

		Legal Act	Act No. 54/1956 Coll.	Reform of public budget Act No. 261/2007 Coll.	Ruling of the Constitutional Court Act No. 166/2008 Coll.	Amendment of Act No. 54/1956 Coll.
		Effective	to 31. 12. 2007	from 1. 1 .2008 to 29. 6. 2008	from 30. 6. 2008 to 31. 8. 2008	from 1. 9. 2008 to 31. 12. 2008
				Change	Change	Change
Reduction rate						
Sickness benefit	1st-14th day	to 1st RL	90% DAB			
		to 2nd RL	60% DAB			
	from 15th day	to 1st RL	100% DAB	90% DAB		
		to 2nd RL	60% DAB			
Care benefit	1st-14th day	to 1st RL	90% DAB			
		to 2nd RL	60% DAB			
	from 15th day	to 1st RL	100% DAB	90% DAB		
		to 2nd RL	60% DAB			
Maternity benefit		to 1st RL	100% DAB			
		to 2nd RL	60% DAB			
Rate for daily benefit						
Sickness benefit	1st-3rd day		25% RDAB	0% RDAB	60% RDAB	25% RDAB
	4th-30th day		69% RDAB	60% RDAB		
	31th-60th day		69% RDAB	66% RDAB		
	from 61th day		69% RDAB	72% RDAB		
Care benefit			69% RDAB	60% RDAB		
Maternity benefit			69% RDAB			

Source: MLSA
Note: RL = reduction limit, DAB = daily assessment base, RDAB = reduced daily assessment base

C.3.1.2. New Sickness Insurance Act

As from 1 January 2009 new Act on Sickness Insurance No. 187/2006 Coll. (Sickness Insurance Act) will come into effect. The original effective date of this Act (1 January 2007) was deferred by Act No. 585/2006 Coll., to 1 January 2008 and then deferred again by Act No. 261/2007 Coll. In connection with the new Act, also changes to other Acts following up on the new Sickness Insurance Act will take effect, in particular in the Labour Code (wage compensation) and in the Act on premium for social security and contribution to the state employment policy.

The new Act introduces a number of changes compared to the existing legislation. The key changes are outlined below:

- Comprehensive regulation of the system, except for insurance premiums. The Act governs insurance of employees, members of the armed forces and the self-employed.
- Involving employers more extensively in sickness rates of their employees. Sick employees are entitled to sickness benefits only from the 15th calendar day of sick leave. For the first 14 calendar days of sick leave the employer provides wage compensation.

- Implementation of sickness insurance has been delegated from employers to district social security administrations.
- The amount of benefit depends more on income earned due to the introduction of the third reduction limit. New parameters for the structure of benefits under the new Sickness Insurance Act (after the public budget reform) are given in Table 54)

Table 54 Parameters for calculating the amounts of sickness benefits

Act No. 187/2006 Coll.		Effective from 1. 1. 2009		
		to 1st RL	from 1st to 2nd RL	from 2nd do 3rd RL
Reduction rate				
Wage compensation	1st-14th day	90% ADE	60% ADE	30% ADE
Sickness benefit	from 15th day	90% DAB	60% DAB	30% DAB
Care benefit	from 1st day	90% DAB	60% DAB	30% DAB
Maternity benefit		100% DAB	60% DAB	30% DAB
Daily benefit rate				
Wage compensation	1st-3rd day		0%	
	4th-30th day		60% RDAB	
	31th-60th day		60% RDAB	
	from 61th day		66% RDAB	
	1st-3rd day		72% RDAB	
Care benefit	from 1st day		60% RDAB	
Maternity benefit			70% RDAB	

Source: MLSA
Note: RL = reduction limit, DAB = daily assessment base, RDAB = reduced daily assessment base, ADE = average daily earnings

Since 1993, when in connection with the tax reform premium for sickness insurance was introduced, annual differences between revenues from premiums for sickness insurance and expenditure on sickness benefits range from – CZK 1.3 billion to +CZK 9.7 billion. It is anticipated that cumulative difference between income and expenditure will exceed in 2008 already CZK 60 billion which accounts for 15% of total cumulative expenditure. Based on the legislation in force as at 1 January 2008 income and expenditure of the system of sickness insurance in 2008 – 2010 would develop as shown in Graph 57.

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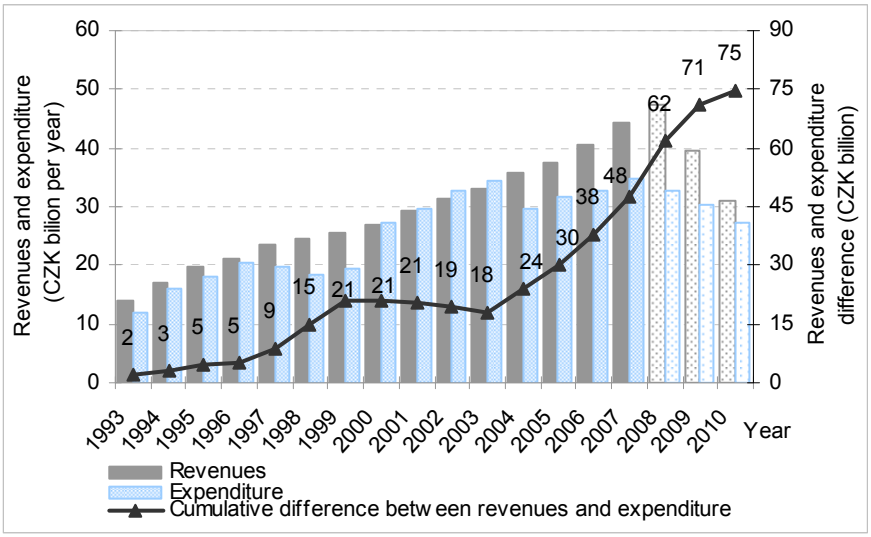
Graph 57. Development of revenues and expenditure on sickness insurance



Note: Expenditure is exclusive of administrative expenses.
Source: MLSA

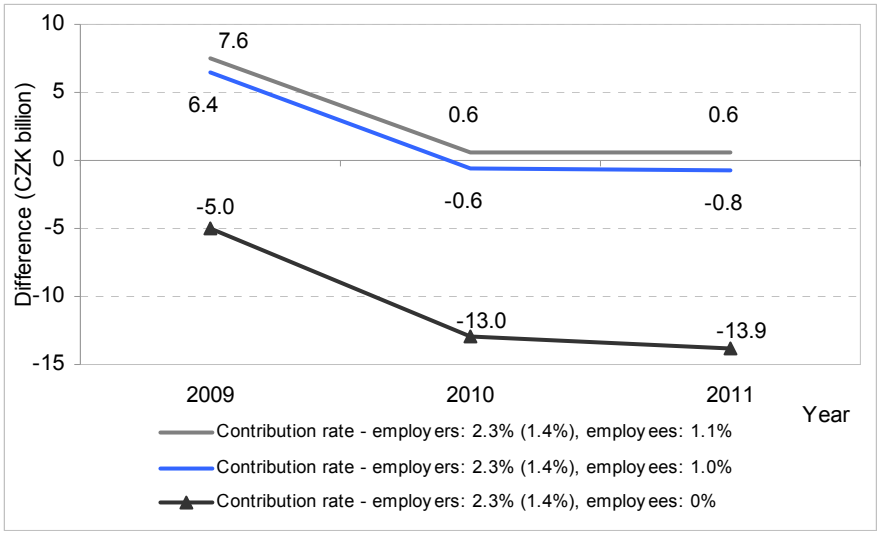
For the state budget, there is no balance of the revenue and expenditure side of the system of sickness insurance as in the case of pensions for which a separate account exists. Premiums for sickness insurance are a part of state budget revenues and sickness benefits constitute state budget expenditure. The system evaluates separately revenues and expenditure.

In 2009 employers will pay premiums amounting to 2.3% of the volume of assessment bases and they will receive a refund of half of the paid wage compensation. As from 2010, for employers employing more than fifty employees and for those who will not register for the so-called supplementary pension insurance, the contribution rate will be set at 1.4% and these employers will pay wage compensation to their employees in full.

As part of the process of reducing tax burden and in connection with the ruling of the Constitutional Court in 2009 premiums for employees will be reduced by 0.1 percentage points and therefore they will pay premiums in the amount of 1% of the volume of the assessment base. Another option that has been proposed by the Government, suggests that a part of expenditure on sickness benefits be paid by employers only, whereas employees would not contribute to sickness insurance at all. Then one part of expenditure would be borne by employers and the other one would be paid from other sources of the state budget.

The following graph shows the balance of the system of sickness insurance for 2009-2011 for various rates of premiums set for employees.

Graph 58. Estimate of the difference between revenues and expenditure on sickness insurance for 2009-2011



Source: MLSA

In 2009, employers will pay the premium at 2.3% of the volume of assessment bases and in the case that **the same contribution rate as in 2008 applies to employees, i.e. 1.1%,** then revenues from premiums for sickness insurance would exceed expenditure by some CZK 7.57 billion. As from 2010, when employers will pay premiums in the amount of 1.4% of the assessment base and only those employers with more than 50 employees who will register for "supplementary pension insurance“ will receive the refund of wage compensation, the surplus of revenues over expenditure would amount to about CZK 0.5 billion.

The already approved **reduction** of the insurance rate for employees by **0.1 percentage points** (the rate for employers will be 2.3% in 2009 and 1.4% in 2010) means in 2009 the surplus of revenues over expenditure by some CZK 6.4 billion and in the following years a deficit in the region of 0.5 – 1 billion.

In the event that **employees would not pay premiums for sickness insurance** at all, expenditure on sickness benefits would be higher than revenues from premiums – in 2009 by CZK 5 billion and in 2010 by some CZK 13 billion.

C.3.2. CONCLUSIONS

So far, there were two limits within the system of sickness benefits that limited creditable income for the amount of benefits and premiums were paid by the same percentage from non-reduced income. Thereby, funds were redistributed significantly between insured persons in high income and low income brackets. At the time when the new Sickness Insurance Act that had set new parameters for the structure of sickness benefits came into effect, due to the introduction of three new reduction limits the amount of benefit is more than previously dependent on previous earnings (wage) of insured persons from which insurance premiums are paid. As of 2008, insurance premiums are paid from the limited amount of income. By reducing the level of solidarity between insured persons in high-income brackets and low-income brackets, the system equivalence will be strengthened.

If premiums for sickness insurance were paid only by employers in the amount of 1.4% of the volume of the assessment base, revenues from premiums

would not be sufficient for covering expenditure and sickness benefits would have to be paid also from other sources than from premiums.

APPENDIX

I. EXAMPLES OF BENEFIT CALCULATIONS

A. EXAMPLE OF A PENSION CALCULATION

Case example

A man born on 1 November 1945, after completing the compulsory nine years of schooling in 1961, studied at secondary school and university until 30 June 1969. After completing his studies, he was continuously employed up until 31 December 2007. 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 2008, he was granted an old-age pension under Section 29 of Act No. 155/1995 Coll. (a "normal" old-age pension).

Calculation

1. **Determining retirement age**
   The retirement age was reached on **1 July 2007.**
   The age limit of 60 was reached on 1 November 2005, i.e. in the tenth calendar year after 1995, therefore the retirement age amounts to 60 +10 x 2 months, i.e. 61 years and 8 months (Section 32 of Act No. 155/1995 Coll.).

2. **Determining the insurance period acquired up until becoming entitled to old-age pensions**
   The acquired insurance period amounts to 45 full years.
   Included in the insurance period is in full period from the beginning of studies at secondary school up to 18 years (1 September 1961 - 31 October 1963), i.e. 791 days and the duration of employment (1 July 1969 – 31 October 2007), i.e. 14,002 days. The duration of studies after the age of 18 (1 November 1963-30 June 1969) is included at a rate of 80%, i.e. 1,656 days (2069 x 0.8). Hence, the total insurance period amounts to 16,449 days, i.e. **45 full years** and 24 days (16,449: 365).

3. **Determining the reference period**
   The reference period for determining the personal assessment base will in this case be 22 years and will include **the years from 1986 to 2007** (2007 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 reference 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 case example,
   - for each of the calendar year "t" of the reference 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 conversion coefficient (hereinafter "CvC"), whereas for the calculation of the pension granted in 2008 CvC_{2006} = 1.0753 is set by Government Decree No. 257/2007 Coll.,

- for the individual calendar years of the reference period <u>set the coefficient of the growth of the general assessment base</u> (hereinafter "CGGAB"), whereby the following applies:

$$CGGAB_t = \frac{GAB_{2006} \; x \; CvC_{2006}}{CAB_t}$$

- to set <u>the annual assessment bases</u> for each calendar year of the reference period (hereinafter "AAB") whereby the following applies: AABt = ABt x $CGDAB_t$).

The method of calculation is seen in the following table:

Year	AB_t (CZK)	EP (days)	GAB_t (CZK)	$CGGAB_t$	AAB_t (CZK)
1986	28,000		2,964	7.2739	203,669
1987	30,000		3,026	7.1248	213,744
1988	31,000		3,095	6.9660	215,946
1989	33,000		3,170	6.8012	224,440
1990	35,000		3,286	6.5611	229,639
1991	41,000		3,792	5.6856	233,110
1992	51,000		4,644	4.6425	236,768
1993	63,000	10	5,817	3.7063	233,497
1994	75,000	20	6,896	3.1264	234,480
1995	96,000		8,172	2.6382	253,267
1996	112,000	15	9,676	2.2282	249,558
1997	131,000		10,696	2.0157	264,057
1998	146,000		11,693	1.8438	269,195
1999	161,000		12,655	1.7037	274,296
2000	175,000		13,490	1.5982	279,685
2001	193,000		14,640	1.4727	284,231
2002	211,000		15,711	1.3723	289,555
2003	229,000		16,769	1.2857	294,425
2004	249,000		17,882	1.2057	300,219
2005	266,000		18,809	1.1462	304,889
2006	289,000		20,050	1.0753	310,762
2007	315,000		21,527	1.0000	315,000

<u>Note:</u> 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 2007 =

$$= \frac{\text{Sum of AAB}_{1986 \text{ to } 2007}}{\text{No. of days} 1986 \text{ to } 2007 - EP} \times 30.4167 = \frac{5714432}{8035 - 45} \times 30.4167 = \textbf{CZK 21,754}$$

Given that there were days when sickness benefits were received (i.e. excluded periods), the total number of days of the reference 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: up to 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 2nd reduction limit 10% of the PAB is included. For pensions granted in 2008 the reduction limits are provided for in Government Decree No. 257/2007 Coll. in the amounts of CZK 10,000 and CZK 24,800.

   CB = 10,000 + (21,754 - 10,000) x 30% = **CZK 13,527**

7. **Setting the percentage-based assessment** (hereinafter "PA").
   The amount of PA for each entire year of the insurance period acquired until entitlement to the old-age retirement is 1.5% of the AB, i.e. 45 x 1.5% AB = **67.5% AB**, therefore 67.5% of CZK 13,527 = **CZK 9,131** per month.

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

8. **Increased** percentage-based assessment **by the period** of gainful activity carried out **after entitlement** to the old-age pension.
   The increase is for every complete 90 calendar days (not including periods of sickness) and amounts to 1.5% for the period acquired after 30 June 2001 and 1% for the period prior to 1 July 2001. From 1 July 2007 to 31 December 2007, i.e. for 184 calendar days, there is an entitlement to an increased percentage-based assessment of the pensions by 2 x 1.5% of the AB, i.e. 3.0% x 13,527 = **CZK 406,** and therefore

   total PA = 9,131 + 406 = **CZK 9,537 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.

9. **Setting the basic amount** (hereinafter "BA").
   BA = **CZK 1,700** per month (provided for by Government Decree No. 256/2007 Coll.).

10. **Valorization increase** pursuant to Government Decree No. 256/2007 Coll. **does not apply.**

11. **Total amount of the old-age pension**

    P = BA + PA = CZK 1,700 + CZK 9,537 = **CZK 11,237 per month**

***Other examples** of sample calculations of pensions and information on some terms are available from the website of the MLSA: http://www.mpsv.cz in the section Důchodové pojištění - Kalkulačky.*

B. EXAMPLES OF SICKNESS INSURANCE BENEFIT CALCULATIONS [38]

The following **four benefits** are paid out of sickness insurance: sickness benefit, family member care benefit, maternity benefit and pregnancy and maternity compensation benefit.

Legal status in the period from 1 January 2007 to 31 December 2008

Calculation under Act No. 54/1956 Coll.

B.1. SICKNESS BENEFITS

Case example

An employee became incapable of work on 2 January and sick leave lasted until 31 January (i.e. 30 calendar days).

His creditable income in the months from January to December amounted to **CZK 21,527:**

1. **Reference period** (365 calendar days)

year 2007	*January – December 2006*
year 2008	*January – December 2007*

[38] GENERAL NOTE - Definition of terms

- **Reference period** is as a rule the period of 12 calendar months preceding the calendar month in which the incapacity for work occurs (quarantine, need to care for a family member or maternity leave).
- **Daily assessment base** (DAB) Creditable income (all income subject to the payment of premiums for social security and contribution to the state employment policy assessed to an employee in the reference period) divided by the number of calendar days in the reference 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 2007 and 2008, the first reduction limit is CZK 550 and the second reduction limit is CZK 790.

Year 2007 For sickness benefits and family member care benefit (FMCB) for the first 14 calendar days of sick leave 90 % of CZK 550 is included, 60 % from the amount above CZK 550 to CZK 790 and any amount above CZK 790 is not taken into account. From the first 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 550 are included in full, 60% from amounts exceeding CZK 550 up to CZK 790, amounts exceeding CZK 790 are not taken into account.
Year 2008 For sickness benefits and family member care benefits, 90 % from the amount above CZK 550 are included, 60% from the amount above CZK 550 to 790 and any amount above CZK 790 is not taken into account. From the 1st day of maternity benefits, the amount up to CZK 550 is included in full, 60% from the amount above CZK 550 up to CZK 790 and amounts exceeding CZK 790 are not taken into account.

- **Daily benefit set by a percentage rate:** Year 2007 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. Year 2007 Sickness benefits for the first three days of sick leave amount to 0 % (60% and 25%) of the DABr, for the 4th and subsequent day of sick leave they amount to **60 %** of DABr; maternity benefits amount to **69 %** of the DABr; family member care benefits amount to **60 %** of the DABr.

2. Daily assessment base

year 2007 and 2008

Creditable income	CZK 258,324	12 x 21,527
Daily assessment base	***CZK 707.74***	258,324 / 365

3. Reduction of the daily assessment base [39]

year 2007

1st – 14th day of sick leave
CZK 590 550 x 90% + (707.74 - 550) x 60%

from the 15th day of sick leave
CZK 645 550 x 100% + (707.74 - 550) x 60%

year 2008

from the 1st day of sick leave
CZK 590 590 x 90% + (707.74 - 550) x 60%

4. Daily sickness benefit [38]

from 1 January to 31 December 2007

1st to 3rd day of sick leave	***CZK 148***	590 x 25%
4th to 14th day of sick leave	**CZK *408***	590 x 69%
from the 15th day of sick leave	**CZK *446***	645 x 69%

from 1 January to 29 June 2008

from 4th to 30th day of sick leave	**CZK 354**	590 x 60%

from 30 March to 31 August 2008

from 1st to 30th day of sick leave	***CZK 354***	590 x 60%

from 31 August to 31 December 2008:

1st to 3rd day of sick leave	***CZK 148***	590 x 25%
4th to 30th day of sick leave	***CZK 354***	590 x 60%

5. Amount of the sickness benefit for a sickness of 30 calendar days [38]

From 1 January to 31 December 2007	***CZK 12,068***	3 x 148 + 11 x 408 +16 x 446
From 1 January to 29 June 2008	***CZK 9,558***	27 x 354
From 30 June to 31 August 2008	***CZK 10,620***	30 x 354
From 1 September to 31 December 2008	***CZK 10,002***	3 x 148 + 27 x 354

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

B.2. FAMILY MEMBER CARE BENEFIT

Case example

A worker cares for a sick child and family member care support lasted from 4 January to 12 January (9 days, i.e. the maximum period for one case for a non-single parent). Her creditable income from January to December amounted to **CZK 21,527** per month.

Calculation

1. **Reference period** (365 calendar days)

   year 2007 — *January – December 2006*

   year 2008 — *January – December 2007*

2. **Daily assessment base**

   year 2007 and 2008

Creditable income	CZK 258,324	12 x 21,527
Daily assessment base	***CZK 707.74***	258 324 / 365

3. **Reduction of the daily assessment base** [40]

   year 2007 and 2008

   from the 1st day
   CZK 590 — 550 x 90% + (707.74 - 550) x 60%

4. **Daily benefit** [35]

   year 2007

   for each day of receiving the FMCB ***CZK 408*** — 590 x 69%

   year 2008

   for each day of receiving the FMCB ***CZK 354*** — 590 x 60%

5. **Amount of the family member care benefit** for the 9 calendar days [40]

   year 2007 ***CZK 3,672*** — 9 x 408

   year 2008 ***CZK 3,186*** — 9 x 354

B.3. MATERNITY BENEFITS

Case example

A woman went on maternity leave which lasted form 4 January to 18 July (196 calendar days). Entitlement to maternity benefits is for 28 weeks. Her creditable income from January to December amounted to CZK 21,527 per month.

Calculation

[40] The calculation is rounded up to the next whole Czech crown.

1. **Reference period** (365 calendar days)

year 2007	*January – December 2006*
year 2008	*January – December 2007*

2. **Daily assessment base**

year 2007 and 2008

Creditable income	CZK 258,324	12 x 21,527
Daily assessment base	***CZK 707.74***	258,324 / 365

3. **Reduction of the daily assessment base** [40]

year 2007 and 2008

from the 1st day
CZK 645 550 x 100% + (707.74 - 550) x 60%

5. **Daily maternity benefit** [36]

year 2007 and 2008

per each day of receiving maternity benefits ***CZK 446*** 645 x 69%

6. **Amount of maternity benefits for 196 calendar days**

year 2007 and 2008 ***CZK 87,416*** 446 * 196

B.4. PREGNANCY AND MATERNITY COMPENSATION BENEFIT

Case example

A worker was assigned to different work due to pregnancy on 1 February and went on maternity leave on 1 May 2007 (2008). Her creditable income in the months February 2006 (2007) – January 2007 (2008) amounted to CZK 21,527 per month and after the transfer in every month it amounted to CZK 15,070.

Calculation

1. **Reference period** (365 calendar days)

year 2007	*February 2006 – January 2007*
year 2008	*February 2007–January 2008*

2. **Daily assessment base**

year 2007 and 2008

Creditable income	CZK 258,324	12 x 21,527

Daily assessment base ***CZK 707.74*** 258,324 / 365

3. Reduction of the daily assessment base [41]

year 2007 and 2008

CZK 645 550 x 100% + (707.74 - 550) x 60%

4. Average daily amount per calendar day after the transfer [42]

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

February	**CZK 538.20**	15,070 / 28
March	**CZK 486.13**	15,070 / 31
April	**CZK 502.33**	15,070 / 30

5. Daily pregnancy and maternity compensation benefit [41],

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

year 2007 and 2008

February	**CZK 107**	645 – 538.20
March	**CZK 159**	645 – 486.13
April	**CZK 143**	645 – 502.33

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

year 2007 and 2008

CZK 12,215 107 x 28 + 159 x 31 + 143 x 30

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

It is possible to calculate the amounts of sickness benefits according to the legal status in 2008 and 2009 using the calculator available on the website of the Ministry of Labour and Social Affairs: www.mpsv.cz /nemocenské pojištění/ kalkulačka pro výpočet dávek v roce 2008 a kalkulačka pro výpočet nemocenských dávek v roce 2009.

[41] The calculation is rounded up to the next whole Czech crown.
[42] The calculation is rounded up to the next whole Czech crown.

II. OVERVIEW OF MAIN MEASURES ADOPTED SINCE 1990

A. PENSION INSURANCE

- **1990 to 1992**
  - ✓ Discrimination of the self-employed was eliminated (in particular social security of the self-employed was placed on equal footing with social security of other gainfully employed persons) and preferential treatment in the pension system was cancelled (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 was unified (sickness insurance was transferred from the remits of trade unions, the Czech Union of Manufacturing Cooperatives and district national committees and was organizationally unified with pension insurance under one state authority – the current Czech Social Security Administration – coordinated by the Ministry of Labour and Social Affairs.).
  - ✓ The rules for regular valorization of pensions were implemented - the first systematic valorization measures were adopted which provided for the conditions and method of regularly increasing pensions.
- **in 1994**
  - ✓ The passage of the Act on Supplementary Pension Insurance with State Contribution. Hence, the Czech pension system is comprised of two pillars - the basic compulsory pillar defined benefit and PAYGO and a second supplementary pillar defined contribution and funded by capital with state subsidized contributions, which also includes private life insurance.
- **in 1995**
  - ✓ Passage 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 in the territory of the CR) and complies with EC law.

- **in 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.

- **in 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.

- **in 1999**

  ✓ An amendment to the Act on Supplementary Pension Insurance with State Contribution 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 reliefs for participants - employees and for the contributing employers, the setting of stricter conditions for supplementary pension insurance.

- **in 2001**

  ✓ The actuarial rules (an increase in the reduction of the percentage-based assessment for the early old-age retirement and the deferred retirement was made more advantageous) were taken more into account in setting the pension amounts.

- **in 2002**

  ✓ The regular increasing of pensions as of 1 January of every year (in January 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 only on the basis of final statistical data and not just on estimates of these indicators with the possibility of raising pensions in exceptional circumstances outside the regular term when greater price increases occur.

- **in 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, for the time being, 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 the

employment relationship for a maximum of one year (previously, there was no such requirement),

- 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 State Contribution was approved whose aim was primarily to achieve harmonization with EU law.

✓ The system of reducing partial disability pensions or the suspension of their payment due to exceeding the set levels of income from gainful activity was cancelled with effect from 1 February 2006.

- **in 2006**

✓ The amount of widower pensions or permitting their payment was adjusted if the reduction of the amounts of these pensions or their non-granting occurred under legislation in force prior to 1 January 1996 due to “concurrent maximums”

- **in 2007**

✓ Change in the legislation consisting in the arrangement whereby the period of care for all insured persons, i.e. both men and women needs to be proved in the same manner, namely by an affidavit submitted together with the application for pension.

- **in 2008**

✓ A condition for valorization of pensions outside the regular term was changed (i.e. even if prices increase by at least 5%).

✓ A single reserve account for the pension reform has been established.

- **approved changes effective as from 1 January 2010**

As part of the first stage of the pension reform changes to the basic pension insurance were approved with effect as from 1 January 2010. The key measures adopted include:

- gradual extension of the insurance period required for entitlement to the old-age pension from 25 years to 35 years, including non-contributory periods or to 30 years without non-contributory periods,
- gradual limitation on crediting of non-contributory insurance periods also for entitlement to the old-age pension
- uninterrupted continuation in gradual increases in the retirement age to 65 years for men and women who have not brought up any child or one child and 62 to 64 years for women (by the number of the brought up children), if they have brought up at least two children and in this connection also the age limit for entitlement to the old-age pension if shorter insurance period is acquired,
- gradual extension of the period for the early retirement from three to five years,

- cancellation of the condition for entitlement to the payment of the old-age pension concurrently with income from gainful activities which consists in negotiating the employment relationship for a maximum period of one year,
- increasing the percentage-based assessment of the old-age pension for a period of gainful activity after becoming entitled to the old-age pension, with concurrent receipt of this pension in full or receipt of half the amount of the pension,
- change of full disability pension to the old-age pension in the same amount upon reaching the age of 65,
- unification of the existing fixed age limit for “permanent“ entitlement of women to widow pension and men to widower pension,
- new definition of disability (introduction of three degrees for disability classification)
- unification of the age limit for which the so-called additional calculated period for the percentage-based assessment of disability pension for men and women is ascertained,
- cancellation of the duration of studies acquired in the period after the Bill was enacted as non-contributory period, except for assessment of entitlement to disability pensions
- increasing the reduction of the percentage-based assessment in the case of early retirement, from the third year onwards.

B. SICKNESS INSURANCE

- **in 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.
  - ✓ 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 benefits, birth grant and funeral grant into the system of state social support; apart form sickness benefits, three other benefits continue to be provided under the sickness insurance system, which include family member care benefits, maternity benefits and pregnancy and maternity compensation benefits.
  - ✓ Compulsory sickness insurance of the self-employed was changed to voluntary.
- **in 1999**
  - ✓ The introduction of reduction limits for calculating the amount of sickness benefits and their regular valorization (annually as of 1 January).

- **in 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).

- **in 2003**

  ✓ Effective from 1 January 2004:
  - the reference period used for determining the daily assessment base for calculating sickness insurance benefits was extended from a calendar quarter to 12 calendar months,
  - the daily assessment base for the calculation of sickness benefits and family member care benefits for the first 14 calendar days of sick leave (quarantine) or for the purposes of family member care was decreased,
  - sickness benefits for the first three calendar days of sick leave were reduced
  - the period during which the reduction limits of the daily assessment base will not be increased will also include 2004 and 2005

- **in 2006**

  - New Pension Insurance Act was passed. However, its effective date was deferred to 1 January 2009 (see below).

- **in 2007**

  Changes were adopted effective as of 1 January 2008, in particular
  - introduction of the waiting period for the provision of sickness benefits, i.e. non-provision of sickness benefits for a period of the first three calendar days of temporary sickness or the ordered quarantine,
  - not increasing reduction limits for the adjustment of the daily assessment base for 2008,
  - retaining the reduction of income up to the level of the first reduction limit for the calculation of sickness benefits and family member care benefits even after the 14th day of duration of a particular social event, for which these benefits are to be granted,
  - adjustment of percentage rates of the daily amount of sickness benefits and family member care benefits,
  - reduction of the protective period,
  - cancellation of the “lone/single status” as a prerequisite for extending the provision of maternity benefits.

- **in 2008**

  ✓ The Constitutional Court by its ruling abolished non-provision of sickness benefits for the first 3 calendar days of sick leave.

  ✓ Effective from 1 September 2008:
  - the rate for calculation of sickness benefits for the first 3 calendar days of sick leave was reduced from 60% to 25%,
  - insured persons are entitled to sickness benefits even if the quarantine is shorter than 4 days,

- regular soldiers and members of security corps are entitled to sickness benefits for the first 3 calendar days of incapacity for service

- **approved changes effective as from 1 January 2009:**

✓ The new Sickness Insurance Act and relating Act provide in particular for:
- involves employers in the development of employee sick leave by the arrangement under which employers will pay wage compensation for the first 14 days of sick leave,
- ensures that the amounts of sickness insurance benefits are more proportional to premiums for sickness insurance paid by insured persons by increasing the number of reduction limits for the calculation of the daily assessment base from two to three,
- transfers the implementation of sickness insurance from large organizations to sickness insurance authorities,
- strengthens protective elements against abuse of the system,

C. PREMIUMS

- **in 1993**

✓ Premiums for social security (pension insurance and sickness insurance) and contribution to the state employment policy were introduced in connection with the tax reform as special payments outside the tax system which form revenue of the state budget at a total rate of 36% of the assessment base (4.8% for sickness insurance, 27.2% for pension insurance and 4% for the state employment policy).

✓ Effective from 1 January 1994, the total rate of premium for social security and contribution to the state employment policy was 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).

- **in 1995**

✓ Effective from 1 January 1996, the total rate of premium for social security and contribution to the state employment policy was 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).

- **in 2003**

✓ Effective from 1 January 2004:
- the rate of premium for pension insurance increased by two percentage points (from 26% to 28% of the assessment base) and at the same time the rate of contribution to the 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 2004-2006 from 35% to 50% of the difference between income earned 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 activities; those carrying out 'main' independent gainful activities always participate in the pension system and therefore must pay advances for premiums regardless of the amount of their income and also have a higher minimum assessment base then those carrying out 'secondary' independent gainful activities.

- **in 2006**

✓ The new Sickness Insurance Act and accompanying Act were adopted amending certain Acts in connection with the adoption of the Sickness Insurance Act. Effective from 1 January 2007:

- the rate for premiums for sickness insurance for employers was decreased,
- the rate of penalty was decreased.

- **in 2007**

✓ Effective from January 2007 and 2008 changes were made to creditability of income of employees into the assessment base for payment of premiums for social security and contribution to the state employment policy.

✓ Effective from 1 January 2008, maximum annual assessment base for the payment of social security premiums and contribution to the state employment policy for all contributors was set at 48 times the amount of the average wage in the national economy.

- **approved changes effective from 1 January 2009:**

✓ Reduction of the rate for payment of premium for sickness insurance for employers from 2.3% in 2009 and 1.4% from 2010 in connection with the fact that the new Sickness Insurance Act comes into effect.

✓ Reduction of premium for sickness insurance for employees and the self-employed by 0.1 percentage points whereby non-provision of wage compensation or other supplies for the first 3 calendar days of sick leave due to sickness or other than industrial accident or the ordered quarantine is compensated for.

- **proposed changes effective from 1 January 2009:**

✓ In connection with the proposed changes in the tax area, it has been proposed with effect from 1 January 2009 to reduce premium for social security and contribution to the state employment policy for employees and the self-employed by 1.5 percentage points.

Additional information on pensions and sickness insurance benefits is available from the website of the Ministry of Labour and Social Affairs and the Czech Social Security Administration at
www.mpsv.cz
www.cssz.cz