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Original research article

Development of the state-contributory supplementary pension insurance in the Czech Republic

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ABSTRACT

The state-contributory supplementary pension insurance is a popular product in the Czech Republic. According to the Association of Pension Funds of the Czech Republic, as at 31 December 2012 ca. there were 5.15 million registered participants in pension funds (as at 31 December 2011 it was ca. 4.60 million of participants) who had deposited ca. CZK 246.594 billion (as at 31 December 2011 it was ca. CZK 232.052 billion). Pension funds have been showing stable management, however, at the cost of low income. Since its reform was enforced by the government in 2013, supplementary pension insurance has remained a part of the pension scheme. It has become a so called ''Pillar III'' and the law describes it as *supplementary pension savings*. The Amendment to the State-Contributory Supplementary Pension Insurance Act, whose target is to reinforce the role of supplementary pension insurance in the creation of total savings for retirement age contains a number of positive elements. The question is whether the amendment will actually meet expectations, i.e. to make the supplementary pension insurance a functional ''Pillar III'' of the pension scheme as the state-contributory supplementary pension insurance does not fulfil its primary function yet and de facto it is not even capable of competing with life-cycle mutual funds or with other substitutes offered on the financial market without being significantly supported by the state.

Introduction

The amount provided by retirement pensions in the Czech Republic is considered to be adequate by 23% of citizens. On the other hand, 77% of citizens consider the amount to be inadequate and 45% of them regard the pension amount as ''definitely'' inadequate.

The state-contributory supplementary pension insurance implemented in the Czech Republic within the scope of the

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voluntary private pillar, was to help citizens when they retire by adding a certain amount to the state pension. It is therefore completely understandable that high expectations were laid on pension funds created in the Czech Republic in 1994. The media were competing with each other in publishing various specialists' and analysts' commentaries predicting not only a quick development of this sector but also a tempting return of at least 2–3% above the inflation rate. Interesting supplementary pensions (necessary also due to the decrease of the pension value by ca. 15% caused by price liberalisation in 1992) were also expected within 20 years at the latest after the start of the pension funds. Therefore, it is not surprising that after the first licenses were awarded in November 1994, pension funds attracted the general public extraordinarily.

However, the reality is somewhat different. Although the state contribution and tax relief helped the product to be used by more than 5.15 million active participants (60% of citizens between 30 and 60 years of age are saving these days – more than 80% of all economically active citizens – which means that the Czech Republic is now among world's top countries for participation of its citizens in savings), the average monthly contribution of participants (excluding the state contribution) does not even amount to CZK 600. This situation has not been significantly improved even after it was made more advantageous for companies contributing to their employees' supplementary pension insurance. It is therefore quite logical that participants' savings are low and insufficient for the payment of a regular pension amount (the vast majority of participants receives a lump-sum settlement; a regular pension is exceptional).

In a way, the state-contributory supplementary pension insurance is a peculiar Czech phenomenon. Its characteristics are those of life insurance, but that is not what it is. It seems to be a regular investment, but it does not follow investment principles. It simply functions under completely special rules.

Materials and methods

The aim of this study is to present the development, issues and perspectives of the state-contributory supplementary pension insurance (supplementary pension savings) as Pillar III in the Czech Republic. The grounds for the development assessment were the data published by the Association of Pension Funds of the Czech Republic [1,2], by the Ministry of Finance of the Czech Republic [3,4] and by the Czech Statistical Office [5]. Time series obtained from these data were furthermore analysed and conclusions were made based on these analyses.

Results and discussion

State-contributory supplementary pension insurance was implemented in the Czech Republic under Act No. 42/1994 Coll. on State-Contributory Supplementary Pension Insurance and Amending Certain Acts Related to its Introduction, as amended [6].

Under the above mentioned Act, state-contributory supplementary pension insurance means the collection of financial contributions from participants in supplementary pension insurance and from the state as provided for the benefit of the participants, management of such financial contributions, and the payout of supplementary pension insurance benefits. Supplementary pension insurance cannot be carried on by any persons other than pension funds.

A natural person may become a participant if he is over 18 years of age and has permanent residence in the Czech Republic. Participation in the supplementary pension insurance is established by the execution of a **supplementary pension insurance policy**.

The State-Contributory Supplementary Pension Insurance Act stipulates the following two types of pension plan:

- contributory pension plan;
- benefit pension plan.

The pension plan can be conceived of as a defined-contribution pension plan where the size of pension benefits is dependent on the sum of the contributions remitted in the participant's favour, on the participant's share of the pension fund's revenues, and on the age from which the pension benefits are to be provided.

The nature of a defined-benefit plan is that the pension sum is pre-determined and is not bound directly to the contributions made (when stipulated terms and conditions are met, the pension fund guarantees the agreed pension sum).

Significant support to the supplementary pension insurance is provided by the state (excluding the state contribution) as it offers tax relief [7,8], for **employees** as well as for **employers**.

We may define the system, which may be referred to as Pillar III of the pension security scheme in accordance with a common world practice, by the following parameters [9]:

- voluntariness;
- state contribution;
- governed supervision.

State-contributory supplementary pension insurance in data

There are 10 pension funds operating actively in the Czech Republic (over time, the number of pension funds has decreased from the original 44 to the current 9 funds) where a foreign shareholder with high capital has gained a key position almost with all pension funds. Their basic economic characteristics and positions on the supplementary pension insurance are shown in Table 1 of selected indicators as at 31 December 2012.

At the end of 2012, the number of participants in the supplementary pension insurance reached 5.150 million. Supplementary pension insurance is, therefore, still expanding, despite its downward trend (Tables 2 and 3).

The reasons for the slackening of interest in supplementary pension insurance in the years 2009–2011, presented by a downward number of newly concluded contracts, may be that, apart from the stagnation in economical performance, the unemployment rate was high, income growth was low, and the state did not have a clear strategy of reform of the pension scheme. The market-saturation factor also played an