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## **THE TRENDS IN THE PENSION SYSTEM IN POLAND SINCE 1999**

### **1. The pension system in the public sector**

A retirement protection of citizens is the constitutional duty of the country. Article 67 of the Constitution of the Republic of Poland says that “A citizen shall have the right to social security whenever incapacitated for work by reason of sickness or invalidism as well as having attained retirement age.”[4] That is why the security of the pension system and to protect the interest of the insured - present and future retirees - are among the most important tasks of the government. The expenditure for this purpose in Poland, as in most European Union countries, is one of the most important items of expenditures in the public sector and unfavorable demographic trends of aging population are, potentially, the source of a further increase the charges of economy of this expenditures. Therefore, the efficiency of system solutions in the sphere of pension security is one of the most important factors determining the condition of the public finances sector. On the other hand, the pace of economic development is also important as the current and future state of public finances, which are critical to the security of the pension system and the quality of life of future retirees. So we can say that we are dealing with strong dependencies and the correct identification of this interaction is the most important element in the assessment of the pension system. Only on this basis we can actually identify the main weaknesses of the system, and how to remove them. The awareness of existing risks has become a cause of making actions in Poland in recent years, that were aimed at increasing the stability and efficiency of the pension system. The purpose of this article is to present changes introduced in the pension system in Poland since 1999 and their importance to the public finance sector.

## **2. The pension system in Poland**

In 1999 the reform of the pension system was carried out in Poland, which consisted in changing the pay-as-you-go system (PAYG) on PAYG – capital system. Two compulsory pillars were created: the first (larger, representing more than 3/5) PAYG (within the Department of Social Security) and the second (lower) capital in the form of Open Pension Funds (OFE) - managed by Pension Companies (PTE). A key change was the replacement of the defined benefit system with a defined contribution system for both pillars of the new system [3, p. 49]. Thanks to this, it was possible to dependent the size of future pension on the amount of all contributions and a further life expectancy. Additionally, a third pillar of voluntary insurance was introduced, which gives the possibility of voluntary pension insurance and was the signal for the insured, that the role of the country reduces in the regulation of the pension system, and the amount of future pension will be affected private savings discharged voluntarily Individual Retirement Account (IKE), and since 2011 also on the Individual Retirement Account Protection (IKZE). In the current system of voluntary savings in future pension they can also be collected as a part of employees pension schemes (PPE), which have existed since 1997.

This reform had two main aims. The first of them was to encourage a longer stay on the labour market, because postponing the decision to retire, can significantly increase benefits through defined contribution formula. The second aim was to increase the responsibility of the insured themselves for their income after retirement years. Moreover it expected changes in perception of pension contributions - not as a tax but as a form of saving for future retirement.

It should be emphasized that despite a thorough reform of the pension system in 1999 the current pensioners, as well as those born before 1949 take or will take a pension on the basis of pre-reform [3, p. 51]. Parallel operation of both pension systems (old and new) is the main source of imbalance of income and expenditure the Social Insurance Fund (FUS) managed by Social Insurance Institution (ZUS), as a result of which still require grant from the country budget. The present deficit of FUS is a liability today's working generation towards generation of retirees from the old system. One of the basic reasons for the lack of that balance was to create a pillar of

the capital, which was not accompanied by an increase in premiums. As a result, the contributions paid to pension funds have reduced funds for the payment of current pensions, and this difference must be financed by increased grant from the budget, which is a very important source of income Social Security Fund (in 2010-2014 more than 20% of income). Deficiency of funds in the pension system also resulted from the lack of consistency in implementing the reforms that formed its basis. The global financial crisis that began in 2007 even more highlighted the imperfections of the reform.

**3. Changes in the pension system after 1999 - previous experiences and future challenges.**

Since the implementation of the pension reform in Poland numerous changes was introduced in this system. The functioning of the reformed pension system, however, shows that corrections and modifications to the system are not always aim at improving the finances the social insurance fund. The most important of them, having an impact on financial condition of the Social Security Fund and, therefore, the situation of the public finances sector, see the table below.

*Table 1*

**Changes in the Polish pension system introduced after 1999**

Decrease of income / increase of expenditures	Year	Increase of income / decrease of expenditures
	1999	INTRODUCTION SOCIAL INSURANCE REFORM
	2000	
	2001	
	2002	
exclusion from public pension system uniformed services	2003	
	2004	limit the fees charged by the PTE **
extension of the possibility of acquiring the right to earlier retirement by the end of 2007.	2005	
the introduction of pensions for miners	2006	

extension of the possibility of  
acquiring the right to earlier  
retirement by the end of 2008.  
reducing pension contribution\*

2007

2008 introduction of bridging old-age  
pensions since 2009.

2009 introduction of compensatory  
payments for teachers

limit the fees charged by the PTE\*\*

2010

2011 reduce the amount of contributions  
transferred from ZUS to OFE (from  
7.3% to 2.3%) and the introduction of  
sub-accounts in ZUS

increase the retirement age

2012 increase pension contribution\*

reform pension for uniformed services

2013 adopt the act regulating the thorough  
reconstruction of the second pillar of  
the pension system (OFE)

amortization 51.5% of the units of  
account in the account of each  
member of OFE (ie. liquidation of part  
of the bond OFE)

introduction of voluntary for the  
transmission 2.92% pension  
contributions to pension funds or ZUS

2014 reduction of fees charged by PTEs  
(institutions managing OFE) - the  
maximum level of contribution fee  
may be 1.75%.\*\*

the introduction of the so-called  
'security slider' which assumes that 10  
years before reach a standard  
pensionable age collected funds in the  
account a member of OFE will be  
gradually transferred each month to  
Social Security and recorded on the  
individual sub-account of the insured  
person.

reduction in the fees charged by ZUS

for the transfer of contributions to pension funds from 0.8% to 0.4%.

\* The changes concerned the pension contribution, but had an impact on the level of income and expenditures Social Insurance Fund.

\*\* A change didn't have a direct impact on the income and expenditures of the Social Insurance Fund, but the fees will affect the size of the funds in the accounts by members. of the pension funds.

*Source:* own study based on *Przegląd funkcjonowania systemu emerytalnego. Bezpieczeństwo dzięki zrównoważeniu*, Ministerstwo Pracy i Polityki Społecznej oraz Ministerstwo Finansów, Warszawa 2013, page 14.

The above table clearly shows that the decisions taken in 2003, 2005 and 2007, giving additional privileges to certain groups of work, increased costs of the pension system, and - by reducing pension contributions - reduced income. Only in 2008 so 10 years after the pension reform, it began to realize its other assumptions, limiting the right to early retirement, raising the retirement age and, though only partially, reforming the pensions for uniformed services. The effects of some of these changes were visible immediately after their introduction in the revenues and expenditures of FUS. The results of some of them will be postponed. In the case of modifications made to the pension system you can also identify those that have immediate effects and long-term nature. As a result of limitations of pension contributions transferred to private pension funds, obtained not only a significant reduction in borrowing needs and the pace of increase of public debt, but also to improve the result sector general government and local government according to EU methodology. A sector deficit of the general government according to the methodology of the EU decreased from 7.9% of GDP in 2010 to 3.9% in 2012 - an increase of 4 percentage points GDP [1, p. 18]. Similar effects had changes made in 2014 in the pension system, including the amortization of treasury bonds with a nominal value of 130.2 billion PLN which were assets of pension funds. In this case, there was a significant decrease in public debt - at the end of 2014 public debt (national definition) stood at 48.1% of GDP compared to 53.1% at the end of 2013 (definition of EU - debt decreased from 55.7% of GDP to 50.4% of GDP) [2, p. 7].

The reduction of the capital of the pension system and the simultaneous increase in the part of PAYG leads to an increase in the so-called hidden debt, which is an obligation to future generations. Although there has been a decrease in the level of so-called explicit public debt and reduced the amount grant from the country budget to FUS, however, in the long term is difficult to speak of a sustained improvement in public finances. There are even fears that these actions cause the postponement of the appropriate reforms. In this context, it should also be noted that the proposed changes in the reduction of the retirement age significantly contribute to the deterioration of the financial security of the pension system. They are not only a negation of the efforts in the reform of the pension system in recent years, but also questioning the basic principles of the 1999 reform.

Solutions introduced in the following years should concern not only the current prospects seem most socially troublesome, but also create a stable foundation for the functioning of the system for at least several decades which allows for the construction of efficient systems of retirement security.

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