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**PROBLEMS IN THE FUNCTIONING OF THE
PENSION SYSTEM IN SOME COUNTRIES OF
SOUTHEAST EUROPE**

Abstract

Many countries in Europe and in the world are facing problems in the pension system. The problems that may arise in the pension system are as diverse as the industrialized countries and countries in transition and development. But these problems are less pronounced in industrialized countries than in the countries in transition.

Some of the factors that led to the emergence of problems in the pension system are the demographic factor, and the ratio of active workers to pensioners insured. Besides these two important factors, another factor that can cause problems is economic growth and rising unemployment.

This paper will analyze the pension systems of several countries of Southeast Europe, presenting a short history of the pension reform, and the problems that have arisen.

Key words: pension system, Southeast Europe, pension reform

INTRODUCTION

Pension insurance is a fundamental element of social protection and security of citizens. Social security is provided by the state through its program of social security and social protection programs. Pension insurance is accomplished by way of contributions. The system of pension insurance is important in the context of social security of any individual or society in which it is located. Their financing is one of the facts that determine the living standards of every pensioner or his financial and social security. Maintaining the stability of the system of pension insurance is today one of the main problems for most countries in Southeast Europe and most countries in the European Union and the world.

The provision of pensions and the pension system face great difficulties and the main reasons for this are the growing number of pensioners compared to the number of employees, i.e. working population, whose revenue is necessary for retirement. These problems, in many countries, are largely resolved by reforming the pension system. For this purpose, it is necessary to make a complete investigation of the real situation in the country, the current conditions for taking new, modified steps, and the reasons that led to the need for reforming or changing their way of functioning (Bjelic, 2002: 57).

New terms of providing pensions opened the door to exit the crisis in which the pension system works on the principle of intergenerational solidarity. The solution for the crisis that endangers the functioning of the financing of pension payments on the principle of intergenerational solidarity can be made, primarily in flux in terms of number of employees and retirees as well as dwindling of workers in terms of the number of pensioners.

Regarding the problems of functioning of the pension system in a particular country, usually the main factors that have a key role in the problems of functioning of the pension system in a particular country are: high unemployment, presence of gray economy, expressed in non-restrictively regulations governing the right of retirement, consequences of economic and political developments in the country in the last ten years, which also reflected the functioning of the pension system, and the pension and disability insurance (Basic, 2004: 89).

Analyzed from the economic aspect, the pension system is an important area of economic life which is characterized by a net cash flow of payment and payment, and which extends throughout the year. Consequently, it is necessary to find the key institutional and economic factors that predominantly affect the establishment of the balance of the election of financing pension funds and payment of pension benefits.

Southeast Europe is a particularly interesting region for conducting research on the current state and trends of the development of the pension system, especially

in terms of promoting certain issues and challenges that are currently arisen. First of all, it comes to countries that in the recent past have passed or still spend a period of transition, and countries that have managed to set up a stable structure of functioning of the pension system and thus provide an example to other countries. Therefore, it is particularly broad theme that within the paper will be viewed in a simplified way. The experience of the following countries will be considered in the paper: the Republic of Macedonia, Slovenia, Serbia, Bosnia and Herzegovina and Croatia.

PENSION SYSTEM: ESSENCE OF FUNCTIONING AND FUTURE CHALLENGES

Pension occupies a central place in the social security system in many countries. In European countries there are two basic models of retirement: a model of pension insurance (Bismarck model) and a model of universal pension (Beveridgeov model). In practice there are also mixed models that combine two basic models of pension insurance. In the first model, the pensions are insured on the basis of payment of contributions in working life, while the other model involves the provision of pensions of persons older than the determined age whose payment of pensions is done from the state budget and money for payment of pensions from the state budget. All outstanding issues such as an aging population and high unemployment, are directly endangering the functioning of the pension system. Faced with these problems, a number of European countries have undertaken significant reforms aimed at building a sustainable pension system. These changes and reforms taking place under the influence of the World Bank, which offered more-speed model for the establishment of financial balance and the creation of social security for pensioners (Van Horn, 2002: 12).

One of the dominant demographic characteristics of modern societies is the aging population. The development of medicine and science, and improving living and working conditions contribute to the continuation of human life. At the same time, in most societies there is a decline in the birth rate. The projection for the future shows that the duration of life will be longer, the aging process will be continuous and intense, while the birth rate will be low. In these conditions the insurance risk of old age becomes more and more significant on individual and societal level. Ensuring the reliable sources of income and decent standard of living after his life is important for each person. At the same time, demographic characteristics are important for the functioning of the pension system as an aging population directly threatens this system regardless of the model of pension insurance.

Commonly adopted model of pension system, should be adopted through a process of reform within the countries where they observed certain problems of functioning pension system with three poles. The first pillar is the state mandatory pension insurance, which would continue to be financed by contributions of employees and employers,. This first pillar actually represents the current financing system of the right of pension payment on the principle of intergenerational solidarity, etc. funds financed by the general distribution. The other pillar also would be a mandatory pension insurance, etc. additional pension insurance which is based on voluntary individual savings capitalization. The two pillars would be based on pension funds, whose financing works on the principle of capitalization.

The transformation of the pension system of systems that consist only of the first pillar to the construction of all three pillars of the new system can be divided into two phases. The first phase would include reform of the existing first pillar of the pension system, which would extend the conditions for retirement in parallel with the rationalization of the calculation of the salary. In this area, in the first phase it is commonly suggested: increasing the age limit for retirement and its equalization of men and women, increase the minimum period necessary for obtaining the pension insurance with appropriate proportional reduction of the pension for each year missing , reducing the use of beneficial length of service, minimizing the possibility of a temporary departure in retirement, determining the pension foundations since earnings over the whole of service, reducing the percentage for determining the amount of pension, changing the way of the revaluation of pension in terms of price growth and wages, gradually reducing risk in the amount of pension in the direction of their equalization (down), guaranteeing to all persons in an appropriate minimal pension (Schmahl and Horstman, 2002: 56).

The second phase of reform (improving the functioning) of the pension system shall encompass the following of a gradual transformation by creating a private insurance scheme which would be fully based on capitalization. The main proposal in this context would be the private insurance to be compulsory for all employees and new employees who are not at the end of service. It is assumed that this way of investing funds underlines the appropriate tax relief and exemption from the state. The rights based on private pension insurance would be determined solely on the basis of previously paid contributions and contributions realized through investment and not on the level of earnings as the largest practice of functioning pension systems. The funds would be managed separately by private agencies on a competitive basis, with precise and rigorous control by the competent state bodies (Vaughan, 2000:13).

The pension system, or the programs that are part of this system, represent the most important part of the social security system in almost all countries worldwide.

National pension system depends on a number of factors, among which are the following: the tradition, the development and goals of the system and the level of economic growth and development. Demographic change significantly affects the functioning of the pension system is founded on the model of the current distribution. An aging population, which is characteristic of a number of European countries, threatens this system because it undermines optimal terms of number of employees and retirees. Despite this problem, an additional problem is the rising unemployment due to the economic crisis. In these conditions it is difficult achievement of social policy objectives of the pension, which requires quality reforming the pension system.

FUNCTIONING OF THE PENSION SYSTEM IN SOUTHEAST EUROPE: OPPORTUNITIES AND PERSPECTIVES

In the nineties, the economic situation in Southeast Europe has significantly worsened, leading to a decline in employment over the years so that current revenues were insufficient to cover expenditure, with the payment of pensions already provided many years of donation from the state budget, as a guarantee for payment of the pension.

Pension funds in insurance organizations in developed countries are taking the biggest institutional strength of the capital market. For countries in transition, however, in common is that the early nineties of the last century, the pension system was a social category under state protection. Within the state there was a pension system operating on the principle of international solidarity. Changing the economic structure inevitably causes problems in the pension system. It happened to perform high unemployment as a result of the termination of employment of a number of factories and enterprises, due to high costs for pension and disability insurance, as well as evasion of income tax, more employers resorted to payment of earnings “on hand.”

The functioning of the pension system: the case of the Republic of Croatia

In Croatia, the pension system is based on compulsory pension insurance which in the late eighties and early nineties of the last century was divided into:

- * Fond of employees with 86% and 91% of insured pensioners,
- * Fond of independent retailers with 6% and 2% of insured and pensioners
- * Fond of individual farmers insured with 8% and 7% pensioners.

The decline in industrial production, the closure of enterprises and the

growth of unemployment in the 90s are the reasons that the ratio of the working population and retirees in 1998 was 1.48: 1 contrast ratio of 4:04 from 1980. Lack of funds from pension funds is compensated by the state budget which in 1999 amounted to 14% of GDP. There was a notable decline in pension benefits, which in the period 1987-1990 year amounted to 75% of the average wage, while in the period from 1979 to 1998 had fallen to 47% of average earnings (Bejakovic, 2000: 17-18)

Because of these problems the Republic of Croatia has acceded to reform the pension fund. The former approach of calculating pension - from ten best year's income, and indexation of pension compensation - pension harmonization with the rise in earnings was abolished. The law stipulates that the base for calculating the pension fee /it cost/ is the income during the entire length of service so that pensions also grow 50% in terms of earnings and 50% on the cost of living.

The next step in reforming the pension insurance was after 1999, when the Croatian parliament adopted a new concept of reform, which is based on three pillars:

- * Mandatory pension insurance
- * Mandatory capitalized pension insurance
- * Voluntary pension insurance based on individual calculations.

The second and third pillars are regulated by law. The application of these acts had been planned in 2000 and the reform started in 2002. However, due to poorly developed national economy, there was a delay in this process.

The first pillar pension insurance "pay as you go" system is the basis on which current employees fund the pension benefits of current retirees through the payment of contributions. In the second pillar of compulsory pension insurance are included all employees younger than 40, and for those who are 40 to 50 years of age, membership in the Fund is voluntary. The contribution is 5% of gross earnings. The third pillar represents voluntary pension insurance in Croatia is completely voluntary. The individuals who choose to access independently make their choice.

The functioning of the pension system: the case of the Republic of Slovenia

Like other countries that emerged from the breakup of Yugoslavia, Slovenia has gone the way of transition, but reforming the pension fund began earlier. However, the reform has not been implemented to the end, because it had not passed on the application of the second and third pillar pension insurance. The reform of the pension insurance is aimed at tightening the conditions for retirement, modification of the pension insurance principle of calculation of the pension and its increase.

Based on data from 1992, when the Law on Pension Insurance was adopted, the age limit for retirement was 58 for men and 53 years for women and pensions were to be financed from the budget of 4% of GDP (Puljus, 2003:23).

In the period from 1993 to 1999, the government of the Republic of Slovenia, with the help of the program PHARE, Ministry of Labor, Family and Social Security and the World Bank worked on changes to the system of pension insurance.

Act of 1999 pointed to sharper conditions for retirement, so that working men involved, according to this law can retire with 63 years and women 61 years. Besides the age, certain requirements had to be met in terms of service for which contributions are paid, which is at least 15 years of service and a maximum length of service is 40 years for men or 38 for women. The amount of the pension is determined based on the average of 18 best net incomes in the valorization coefficient which decreases annually by 1.5% for each year of service.

Through reforming their pension insurance, the Republic of Slovenia has turned to compulsory pension insurance - the first pillar.

The functioning of the pension system: the case of the Republic of Serbia

In the second half of the eighties and first half of the nineties of the last century there was a crisis in the social security of the Republic of Serbia, so the state had to undertake appropriate measures. In 1970 year it had to cover costs of the gross national income which amounted to 6.3% while in 1990 the figure was 13.7%. The crisis is particularly amplified in the nineties when the civil war broke out, leading to the disruption of the current economic situation in Yugoslavia.

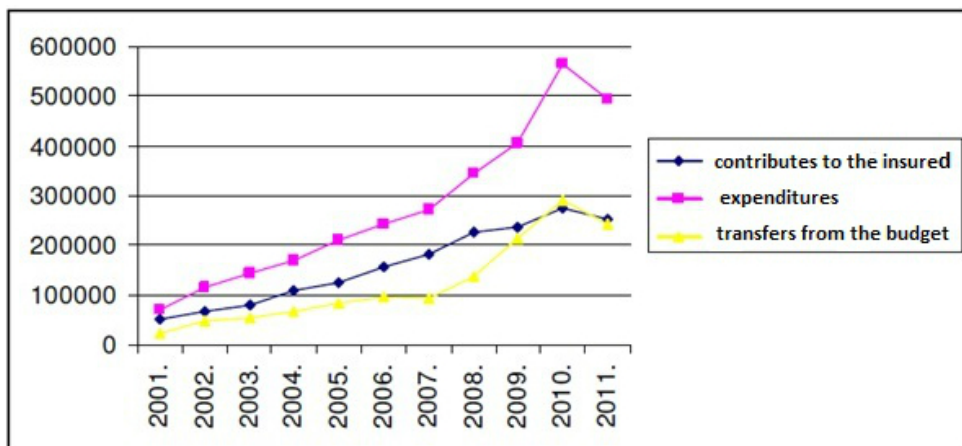
For that period it is characteristic that there was an increase in the number of pensioners. Only in 1991 in the Republic of Serbia 120 501 people retired. The proportion of the working population and the number of pensioners in 1981 was 6.6: 1 while in 1990 the difference was reduced to 3.18: 1st what is most worrying is that there is a constant trend of decline in employment in 2001 and increase in the number of retirees. In fact, the problem is that employees now cannot earn enough to settle the necessary funds for the payment of the pension, and for that reason the state donated 40% of the necessary funding to the fund for pension and disability insurance. Particularly lax requirements for retirement (especially disability) and the large presence of corruption influenced the increase in the number of pensioners, mainly disability pensions. Besides increasing the number of retired, changed and their structure. Namely, the number of old age pensioners is relatively lower compared to other countries and 45% of the total number of pensioners. On the other hand, the number of disability pensioners is 30%, and family 25% of the total number of pensioners, which is above the usual indicators

in other countries. For comparison, we can say that in most countries the number of pensioners is 60-80%, the number of disability pensions 10% of the total number of pensioners while others are family pensioners.

In 2003, the Law on pension and disability insurance was adopted, was significantly amended in 2005. A significant shift in the development of insurance in Serbia occurred with the adoption of the Law on voluntary pension funds and pension plans in 2005, which entered into force in 2006, when it introduced voluntary pension insurance. Today the Republic of Serbia has two systems of insurance: compulsory pension insurance and voluntary pension insurance.

Despite the economic self-sufficiency, the public pension system and disability insurance, the average pension benefits (pensions) are not sufficient to cover the minimal subsistence of the majority of pensioners.

Chart 1. *Expenditure on pension and disability insurance contributions of insurers and transfers from the budget (in thousands of dinars) 2001-2011*



Source: Republic Fund for Pension and Disability Insurance, <http://www.pio.rs/cir/> (accessed 8 August 2015)

The predicted values (described in figure 2) may be valid only under the assumption that the factors that acted in an observation period continue to operate the same way without significantly adding additional factors.

This forecast is a warning that in the future there will be even greater difficulties related to the proper functioning of the existing public system of pension and disability insurance, if appropriate changes are not made.

In September 2013 the number of employees, not taking into consideration the employees in the army and police in Serbia decreased to 1,705,256 persons, which is comparable with the number of employees in 1976. Average number of pensioners in 2013 was 1,711,699, although at the end of the year reached 1,722,649 persons. Relative to 1976, the number of pensioners increased by 3.9 times. Belgrade and Novi Sad have a particularly favorable relationship for the benefit of employees, compared to the rest in Vojvodina and in the Republic of Serbia, the cities of Novi Sad and Vojvodina have a relatively favorable opportunity for financial sustainability if the same would spin and split off from the rest of Vojvodina and the southern part of Serbia.

Reforming the pension system in Serbia started, but to establish a stable economic pension system a lot of work remains to be done. Almost fifty years after the end of World War II until the early years of the twentieth century in Serbia there was a system of compulsory pension insurance. The initial programs of reform of the pension system aimed at stabilizing the pension funds, payment of overdue pensions and providing regular, monthly payment and reimbursement.

The model of pension reform "three bulb" was created by the World Bank, and is accepted by countries in all continents. The model is particularly acceptable in Southeast European countries that pass through the transitional period.

The process of reforming the pension system in the Republic of Serbia, as in most countries in transition, is going in the direction of combining the pension system. In the first phase of the process is twofold: further reform of the mandatory pension insurance and introduction of voluntary pension insurance in the form of the third pillar. In the second phase when the conditions are met, realistically expected introduction of mandatory private pension insurance, etc. second pillar.

In Serbia there are currently about ten pension funds managed by ten companies. The assets of the voluntary pension funds at the end of 2013 were 19 billion dinars (about 165 million) at the end of the third quarter of 2013 were 4.4% (800 million dinars) higher than in the past quarter, while growth last year was 26%. The total number of users of voluntary pension funds which pay benefits until the end of September 2013 was 183,547. They have a total of 244 306 contracts signed for membership in voluntary pension funds in the third quarter the number of users increased by 2878.

In the Republic of Serbia, in fact the formation of several pension funds benefits the maintenance of the pension system, thereby increasing competition. The voluntary pension insurance needed developed economy, developed capital market that also omitted in this country. The economic crisis has happened, and as an active participant in the financial market, pension funds have remained immune to the adverse developments throughout the past years, so in 2008 the average contribution of the voluntary pension funds was negative.

The improvement of the pension system is a precondition for economic progress. It is necessary to build a new system, economically sustainable, which will increase individual savings and will intervene to improve economic development. At the same time, there is great dissatisfaction among citizens over the continuation of life, because it increases unemployment, which is a problem that the state must take into account in the future. The economic prospects of the development and sustainability of the pension system in this country are looking to further economic and legal equilibrium in order to provide secure payment of the pension.

Functioning of the pension system: the case of Bosnia and Herzegovina

The first forms of pension insurance in the area of Bosnia and Herzegovina appeared in the late nineteenth century. In the recent past, through the Law on Fundamental Rights of Pension and Disability Insurance in 1982, basic solutions have been set (Gnjero, 2007:25):

- Basics of the pension system, where the workers were to be provided compulsory insurance under the principle of solidarity and expired labor demand, in order to provide material and social security in case of reduction or loss of work ability, age, and compensation in case of death of family members;
- Basic rights of pension insurance:
 - Entitled to a pension based on age;
 - Right on schedule another suitable job, position, retraining, additional training and the right to adequate compensation;
 - Right to disability and family pension and allowances;
 - The right to compensation in case of physical damage.
- Special conditions for national liberation fighters or recognition of time spent in the war as a special experience.
- Determining pension plan depends on the amount of pension benefits.
- Implementation and use of pension and disability insurance.

The latest amendments to the legislation to the Law on Pension and Disability Insurance Fund were done in 1998. This Law is the grace of amending the Pension and Disability Insurance in Bosnia and Herzegovina (Vukovic, 2005: 15).

Through the mentioned Law, changes have been made in the pension and disability insurance. Significantly reduced the requirements for retirement, or moved the boundary of years. The boundary pension is set at the 55 years for women and 60 years for men. Also the percentage of the amount for pension benefit decreased to 85% in 2000 and 75% by 2005. Changes to the basis of the mentioned Law have

been made through the abolition of the rights having a social character, such as the right to protection of foreign assistance and care, the right to part-time on the basis of disability and so on. All changes are intended to make the pension and disability insurance of Bosnia and Herzegovina financially durable. In recent years, the goal is somewhat achieved, given that the payment of retirement allowance is regular and transfers of the budget intended to cover the deficit of the Institute for Pension and Disability Insurance are reduced. However, to make the realization of long-term financial durability of the system is necessary to implement a comprehensive reform in the longer term, which will include the introduction of the principle of individual capitalization, new forms of pension insurance, voluntary pension insurance.

The lack of existence of the relationship between the insurance premiums, etc. paid contributions received pension benefits, and uncertainty in the complicated way of calculating the pension, led to the contribution to be understood as a tax. Moreover, there is a difference between what the employee was willing to pay, driven by the expected income and what had to make based on the law. Such a difference is a sort of invisible income, however this condition causes three phenomena that are directly associated with jeopardizing the economy of Bosnia and Herzegovina (Lovrinovic, 2002: 45):

- Reducing employment
- Reducing the current salary
- Employment becomes more expensive.

Based on the foregoing, it can be concluded that the current pension system has a negative impact on employment in Bosnia and Herzegovina, where employment growth has been one of the main macroeconomic objectives of each country in general. Also, the system acts to reduce the current pay, and it directly reduces the standard of living and at the same time entertain the national economy as a whole. In Bosnia and Herzegovina, the development of the pension system is largely determined by:

- * Demographic movement
- * The development of the national economy
- * Legislation.

In this country there is a decrease in the birth of infants, which makes the country incapable to meet the average level of reproduction, which requires replacement of generation requiring 2 to 2.1 newborn per one woman. The decrease in the birth of children is a consequence of the economic crisis and military developments in the country. However, the awnings will continue in the future, what happens in other countries in transition, regardless of movement in economic development. When it comes to mortality, it is growing after the war, but the duration of life in general is

growing, not only in this country but also in other countries in transition.

The low levels of pension benefits indicate small payments of contributions and avoid paying them or work illegally.

The main conclusion is that the way of investing the collected funds for pension and disability insurance must be changed. Moreover, it is the responsibility shifted to policyholders. So, the risk of the venture would be adopted individually.

To ensure the development of the new pension system is necessary to ensure very formal, legal, institutional and other assumptions, such as:

- * Preparation of a consistent strategy for pension reform, a document subject to public debate;
- * Identification of interest groups such as pensioners, unions, tax authorities, etc.;
- * The establishment of expert groups to reform the pension system.
- * Identifying the legislation is necessary to adapt, and thus be harmonized and amended in accordance with the achievement of efficiency of the pension system.
- * The establishment of supervisory and regulatory authorities for a new pension system.

Functioning of the pension system: the case of the Republic of Macedonia

With the adoption of the Law on amendment to the Law on Pension and Disability Insurance, in March 2000, in the Republic of Macedonia was established multi-pillar pension system. As one of the main reasons for introducing the new system are the difficulties in the functioning of the current pension system and pension insurance, which will be particularly pronounced in the coming years as a result of poor demographics. During the years 1997-98, two employees financed pension compensation to a pensioner, and in 2000, 1.4 employees.

The newly established pension system in the country, besides the system of intergenerational solidarity, includes the system of fully funded pension insurance and consists of three pillars:

1. Compulsory Pension Insurance which operates on the principle “pay as you go “,
2. compulsory pension insurance which is based on capitalizing on savings and
3. Voluntary pension insurance is based on capitalizing on savings and can now be obtained under the offer of insurance companies.

Regarding the analysis of the pension system of the countries in Southeast Europe, particularly the countries of former Yugoslavia, the following data shows:

-In most countries, the percentage of disability pensions in relation to the total is above the EU average ratio of 10% while in some countries the figure is

doubled: 18.60% in Serbia, Bosnia and Herzegovina 20%, Republic Srpska 16%, and Montenegro 26 % and 24.70% in Croatia.

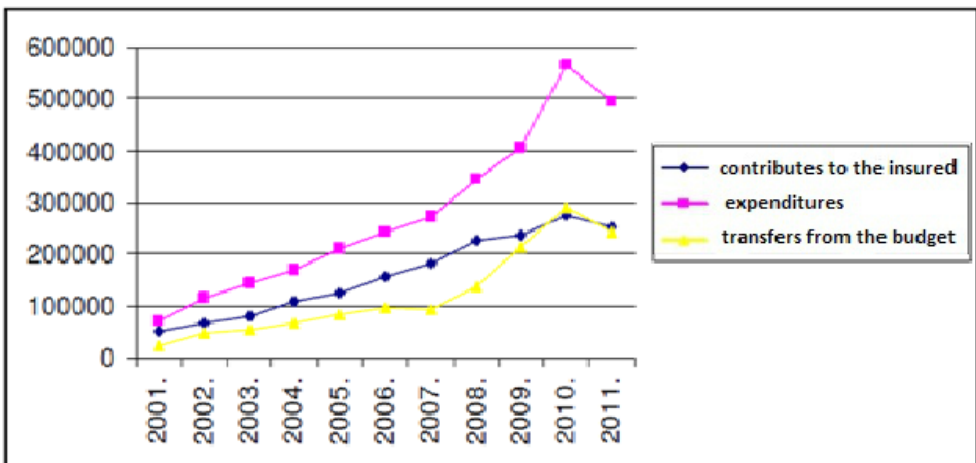
-When it comes to the differences in terms of the average pension which is significant in terms of the average wage in the countries of former Yugoslavia the following information are obtained: pensions over 50% of salary - Slovenia (56.60%), Montenegro (55.51%) and Macedonia (57.17%); pensions below 50% of salary - Serbia (46.30%), Croatia (40.00%), Bosnia and Herzegovina (40.80%), Bosnia and Herzegovina - Republic Srpska (40.80%), Federation of Bosnia and Herzegovina (44.40%).

These percentages reflect the social sensitivity in these countries.

In terms of the share of contributions to the inflow of funds, they move in a range of 53-88%, respectively:

Lowest in Macedonia 53.4%, Serbia 58% and Croatia 61% in Slovenia and Montenegro, a little more - about 66% and 70% in Bosnia and Herzegovina far the most: Republic Srpska 78.4% in the Federation of Bosnia and Herzegovina as 88%.

Chart 2. *Average pension in the countries of former Yugoslavia*



CONCLUSIONS

Pension insurance is subject to discussion and analysis in almost all countries in the world as a stable pension system is one of the prerequisites of economic growth and development. Therefore, it is important to have confidence in pensions,

regardless of whether the system can provide the revenue that would be sufficient for socially acceptable standard of living and proper funding.

The process of globalization has engulfed the pension system as an essential element of the economy (public finance). It is in this segment that used to be considered that there is no alternative in its financing, but it suggests that the maturity of time contributes to the emergence of new solutions and new concepts. As one of the solutions are pointed to partial or complete privatization of the pension system.

The problem of an aging population, the decline in fertility leads to unfavorable terms of number of employees and the number of pensioners. If to all this is added the economic crisis in the last decade, causing problems in the functioning of the national economy, it affects the increase in the contribution and the issue of payment of pensions. These aspects contribute to irregular payment of pensions and increasing impoverishment of pensioners due to small amounts of pensions often does not provide coverage to their existential needs.

All these reasons suggest that the countries of Southeast Europe, most of which were developed in detail in this paper, it is necessary to reform the pension system because the existing becomes financially unsustainable which also points to the need to introduce additional pension fund and voluntary pension insurance.

The following parameters are analyzed in this paper:

- * striving to reduce public spending and the budget deficit
- * solving the problems of aging of the population
- * Prevention of early retirement
- * the need for a wider range of insurers.

In this paper I analyzed the historical and current condition of the pension system of the countries of Southeast Europe. The states (especially in transition) go through a transformation of its system of financial, demographic and economic reasons. Also mentioned is that each country should, through its characteristics, shape its pension system and to impose the use of a mixed pension system as standard (as specified by the World Bank) for better circulation of the internal situation in this domain.

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