

Debt relief of individuals in five regions of the Czech Republic

M. Randáková, J. Bokšová, O. Buben, J. Maixner

Abstract— This paper presents the results of an ongoing research of personal bankruptcies in the regions of the Czech Republic. Five regions were examined and compared so far: the South Bohemian Region, the Prague Region, the Liberec Region, the Usti Region and the Central Bohemian Region. The research is focused on successful proposals for debt relief and various factors influencing its success across these regions. The option of undergoing a debt relief is possible in the Czech Republic since 2008 when a new Act No. 182/2006 Coll. came into force and, as there is growing awareness of this possibility among Czech population, the number of proposals was significantly increasing ever since. The research thus compares debtors according to the success rate of their proposals, their age, gender, income, the total amount of debt, the structure of creditors as well as university education level.

Keywords—Czech Republic, Debt Relief, Insolvency, Personal bankruptcy

I. INTRODUCTION

THIS article presents the results of analysis of debtors from the South Bohemian Region, the Prague Region, the Usti Region, the Liberec Region and the Central Bohemian Region. The main aim of this research is to analyze debtors who successfully submit a proposal for debt relief in each region in the Czech Republic. Each debtor is examined for various factors influencing its successful proposal for debt relief.

As the amount of household loans rises every year, and the financial literacy is still deficient, it is not surprising that the number of personal bankruptcy increases by 30% annually (see Fig. 1) [1]. The research of the Czech Bank Association came with some interesting conclusion as the financial literacy was stagnating for last nine years and more than 78% of population does not have any financial reserves. There are three main categories of insolvency: lack of knowledge, economic climate and inaccessibility to debt [2]. We believe that especially lack of knowledge and lack of financial literacy have the biggest share in insolvency among people. They are not always able to foresee the consequences arising with taking loans and they

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take one even though they will not be able to repay it. Banks usually refuse to process a loan when debtor is in a bad financial situation and anticipate its inability to repay the debt, but this market gap is filled by non-financial institutions which benefit from that. Then there is only a small step towards insolvency. For this reason and many others, the possibility of debt relief is very important nowadays.

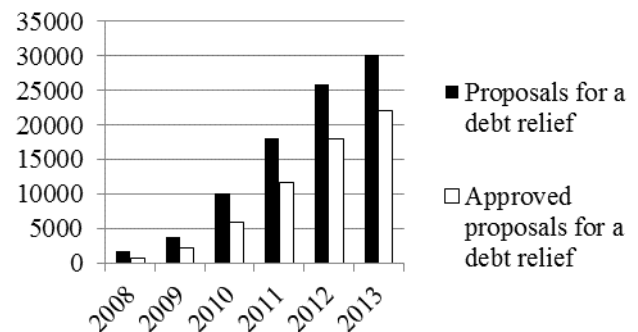


Fig. 1 development of personal bankruptcies in the Czech Republic

II. THEORETICAL BASIS

A. Insolvency legislation in the Czech Republic

Although the Czech Republic has a long history of solving bankruptcy, which goes back to 18th century with the Josephine bankruptcy order, it used to be the most outdated part in the Czech legislation until the recodification in 2008. Since January 1st 2008 when new Insolvency Act came into force, also non-entrepreneur entities have been able to solve insolvency by personal bankruptcy. Therefore it is rather new opportunity for individuals in the Czech Republic to declare bankruptcy and this research focuses on those who need it. In the past debtors could not have debts out of the business when applying for debt relief, but according to current case law it is possible for debtors to have some business liabilities if they obtain the agreement, which declares that it is possible to repay business liabilities through the debt relief, from their creditors [3]. The Act No. 182/2006 Coll. was inspired abroad, mostly influenced by our neighboring country Germany and partly by American legislation whose principles can be found even in European law [4].

B. Debt relief

Debt relief is meant for those whose debts are more than 30 days overdue and has at least two or more creditors [5].

However there are some other conditions that must be fulfilled to successfully propose for debt relief. Debtor must specify how he has got insolvent and prove that he is able to pay at least 30 % of its current debts to creditors. The proposal has to include at least this information:

- Personal information
- Expected income in following five years (salary, pension, donation)
 - Proof of income of the past three years
 - A preferred method of debt relief
 - A list of all valuable assets

If all conditions are met the regional court will most likely permit the debt relief. The court assigns insolvency administrator who secures maximum satisfaction of creditors and also protection of debtor against other charges. It is essential to remember that everyone can submit the proposal just once in life.

Insolvency Act defines two different methods of debt relief. One of them is a repayment plan. If the court approves resolving personal bankruptcy by the repayment plan, the debtor is obligated to pay every month a specified amount of money for the following five years, so that at least 30 % of total debts could be repaid. An amount exceeding subsistence minimum, which the debtor gains, has to be used for repaying debts. In the Czech Republic, this method is the most common. But there is also another option of debt relief and it is the method of monetization of debtor's assets. If the debtor has valuable property, the insolvency administrator can sell it and use the money for the repayment of the debts. In this case debt relief does not have to last for five years. Both methods can be combined. This option is also used when the debtor does not fulfill the repayment plan properly [6].

C. Creditor's demands

Creditors who are applying their claim against the debtor are participants in the insolvency process. There is no limitation which means that it does not matter whether it is a legal entity or individuals. All of them can sign their claim, unless none of their receivables could be satisfied. Creditors participate in deciding which kind of debt relief the debtor will undergo, they oversee the activity of insolvency administrator and advise him how to treat with their receivables [4].

III. METHODOLOGY

This section of the paper will describe the process of obtaining all the information that was necessary for the research as well as the methodology and further usage of the data. All of the data used in this research were acquired from the Czech Insolvency Register. Firstly all of the proposals for bankruptcy of debtors listed in the Czech Insolvency Register under České Budějovice Regional Court, Prague Regional Court, Liberec Regional Court, Ústí nad Labem Regional Court and Central Bohemian Regional Court were extracted from the register and put into alphabetical order for every region. It is most important to emphasize that for the first two regions - South Bohemian Region and Prague Region – was

used 100% data sample, because there was no way to estimate the proper sample to work with and still acquire valuable information without analyzing at least one entire region. Therefore two regions were completely analyzed before estimating sample to ensure high quality results. The extensive analysis was made over the acquired data and ten percent sample for other regions was established. Due to differences in sample sizes and due to different size of regions, it is essential to compare the result in relative values and not in absolute values. For a purpose of this paper, it is referred as Sample one for first two regions and as Sample two for ten percent sample. A systematic selection was made and every tenth debtor's proposal was selected for elaborate examination for other regions. The time period of bankruptcy proposals selected for this research was from 1st of January 2012 until 31st of December 2013.

In order to make sure the outcome of this research is not biased, some adjustments had to be made. At first, the selected debtors were analyzed whether they really filed for a personal bankruptcy or for another form of insolvency. Most common were individuals who proposed for a debt relief more than one time. That means their first proposal was unsuccessful. Only the very last proposal for a debt relief of such debtors was considered relevant for this research and only proposals that were filed before 31st December 2013. Another very common group of debtors were people who had personal debts as well as business debts. In such cases debts from business activities were taken out of this research and only personal debts were considered relevant. Married couples were considered as two separate individuals and duplicating individuals were cleared out of the list of debtors.

Six main criteria for every selected debtor were analyzed. Firstly it was analyzed whether a proposal was successful or not. If a debtor was unsuccessful, he or she was examined further in order to acquire information whether he or she filed for a debt relief any other time and if so, when. If a debtor's last proposal was filed after the 31st of December 2013, the necessary data were taken out of the proposal that fitted the time period being examined. The selected debtors were then divided into six different age groups. These age groups were all compared to each other and percentage based number of each group was carried out. Another criterion analyzed was the proportion of men and women. Results of this criterion were also carried out according to the six different age groups. Every debtor was then screened for their income. Income of each debtor consisted out of three categories – social contributions (including gift covenants), gross earnings and net earnings. Gross earnings were adjusted with a simple formula based on the Czech social welfare and taxation system onto net earnings. The size of debt of every selected debtor was analyzed as another criterion and here too the debtors were divided into six groups. The size of debt was measured in the Czech koruna currency. Lastly the debtors' creditors were analyzed. They were divided into three groups – Banking institutions, Non-Banking Financial Institutions and Other

(including state institutions, insurance companies and individuals). Banking institutions were selected based on a List of Monetary Financial Institutions in the Czech Republic administrated by the Czech National Bank for the year 2013. If a financial institution was not on this list, it was considered a Non-Banking Financial Institution.

IV. RESULTS OF THE RESEARCH

The primary aim of the data collection was to compare South Bohemian Region, Prague Region, Liberec Region, Usti Region and Central Bohemian Region mainly in relative level due to different population density. The legislation framework combines the qualitative and quantitative conditions to let the justice allow the insolvency process. According to national statistical service, in the end of 2014 the population of the Liberec Region was approximately three times lower compared to the Central-Bohemian Region and the Usti Region had about 60 % of the Central-Bohemian Region population. Following table shows the absolute demographic data of the targeted regions that are used as a base for conclusions of the research.

Table I Demographic distribution of population (sample 2) [7]

		Liberec Region	Central Bohemian Region	Usti Region
Total population		438 851	1 315 299	823 972
Age group	0 - 14	68 701	220 787	129 480
	15 - 64	292 832	874 701	553 949
	65 and more	77 318	219 811	140 543
Gender	males	215 413	649 245	408 283
	females	223 438	666 054	415 689

There is a huge difference between the regions, therefore the results cannot be compared in the absolute numbers, but rather in relative values. The second table demonstrates the percentage of successful proposals and unemployment rates disaggregated by three regions.

Table II Successful proposals and unemployment rates (sample2) [7]

	Liberec Region	Central Bohemian Region	Usti Region
The proportion of successful proposals	86%	90%	91%
Unemployment rate	7,77%	6,52%	10,89%

One can say that the proportion of (un)successful proposals will be positively correlated with the macroeconomic indicator of unemployment rate. Positive correlation is not proven because the Usti Region with the best proportion of successful proposals also has the highest unemployment rate (which is the highest in the country). It is necessary to mention that insolvency process for the individuals is not primarily intended for unemployed people. As it will be shown further, about half of debtors has the month net income in the amount of 15 to 25 thousands CZK which is below average wage in the Czech Republic.

Table III Successful proposals and unemployment rates (Sample 1) [7]

	Prague Region	South Bohemian Region
The proportion of successful proposals	82,7%	89,9%
Unemployment rate	4,19%	4,7%

To compare Prague and South Bohemian region with other three regions we can realize, that these two regions have much lower unemployment rates. Prague and South Bohemian regions belong amongst regions with lowest unemployment rate. As mentioned above there is no significant correlation between these two measurements and reasons for lower amount of approved proposals should be sought somewhere else. The cause which most often affect the approval of the debt relief is the lack of formal information that debtor must provide.

Table IV Age and gender based portion of insolvent population (sample 2)

		15-24	25-29	30-34	35-44	45-54	55+	Total
Liberec Region	Men	0%	5%	9%	21%	8%	11%	54%
	Women	1%	3%	3%	20%	8%	12%	46%
Central Bohemian Region	Men	2%	5%	7%	11%	10%	10%	44%
	Women	1%	5%	6%	19%	15%	11%	56%
Usti Region	Men	0%	4%	5%	16%	11%	12%	49%
	Women	1%	4%	4%	13%	14%	15%	51%

It seems that women in Central-Bohemian and Usti regions submit a proposal for debt relief more often than men. But if we compare our outputs with gender distribution in those regions according to Czech statistical office, we come to the conclusion that debtors' distribution is the same for those who submit a proposal and whole population of the region. On the other hand, in Liberec Region there is a considerable difference between number of men and women submitting the proposal, when men seem to need debt relief much more than women. Considering age, most debtors are 35 years old or older. It is probably due to the fact, that people younger than 35 years either did not have time to make a lot of debts, or usually think that their financial situation is not as bad as it seems and believe to handle it in the future. Maybe even by taking another loan.

As we have a look at another two regions, it become obvious that women fall into need of declaring bankruptcy slightly more often than men. This fact is now supported by 4 out of 5 observed regions. Additionally it is much clearer that a person become more susceptible to fall under bankruptcy pressure when crossing the age of 35. Basically every group with age 35+ has double digits of the portion of the insolvent population, except the Liberec region that has 8% for men and women between 45 and 54 years. This lower numbers are probably caused by high numbers in preceding group. In general all five groups evince the same development of the relative amount of people that fall under bankruptcy depending on their age and gender.

As we observed the highest digits in age group of 35 – 44 years of age, we also try to explain why this group becomes the most endangered by the necessity of proposing a debt relief. As people in Czech Republic wait with building a family and becoming married. It can very much be the fact

why troubles with debts hit the older group than we could assume (instead of group 25 – 34 years of age the group 35 – 44 gets hit). There are many ways how to measure an average age of getting married, but we should take into account that only first marriages make the difference, because if a person has already been through the divorce, then most likely will not have kids again; will not build a family again. This leads into the fact that mostly first time marriages will produce children. Therefore we come up with the need of going debt for these families. The pressure is even stronger when Czech Republic does not support new families adequately nowadays. As the Czech Statistical Office reports the average age of getting married, we easily see the link between the most indebted age group and this relatively high average of entering a marriage. The average age reported is 32, 3 for men and 29, 8 for women. Whether they have children right after the marriage or not, the problems with repaying loans come to them usually few years later. This above mentioned fact might be one of the driving forces why the group of age 35 – 44 is the most often seen under problems with indebtedness.

Fig. 2 shows the insolvent individuals related to their monthly net income. The debtors with the income lower than 5 thousands CZK a month are not the most frequent ones among those who successfully submit a proposal. There are two possible explanations. First, with such low income banks do not usually loan money and if you cannot borrow money, you cannot fall into insolvency. Second reason is that non-banking institutions which take advantage of people with very low income and offer them loan for higher interest rate and more often add additional cost of debts (fees, penalties), but with such a low income it is almost impossible fulfill the necessary condition of repaying at least 30% of its debts.

Table V Age and gender based portion of insolvent population (sample 1)

		15-24	25-29	30-34	35-44	45-54	55+	Total
South Bohemian Region	Men	1%	5%	6%	14%	10%	11%	48%
	Women	1%	4%	6%	15%	14%	13%	52%
Prague Region	Men	0%	5%	6%	15%	11%	10%	47%
	Women	1%	5%	6%	16%	13%	12%	53%

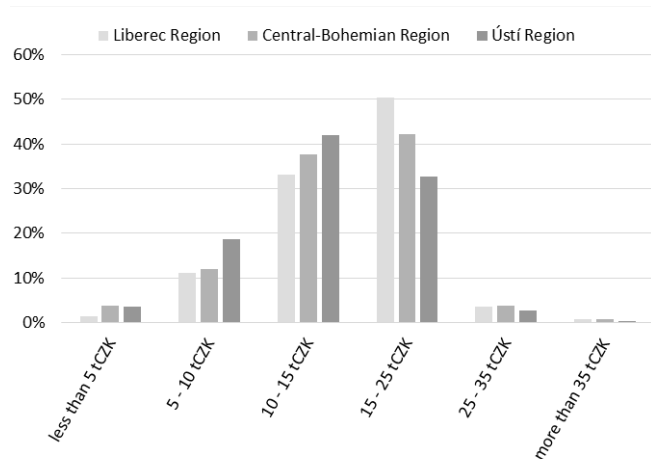


Fig. 2 debtors according to their monthly net income (sample 2)

On the other hand people with income over 35 thousands CZK do not usually need a debt relief, because their income is big enough to handle extra expenses or even to pay the debts. Also people with higher income have most likely good financial literacy as well. Most debtors who successfully submit proposal have income between 10 and 25 thousands CZK, which is just below the average wage in the Czech Republic. There is no significant difference between the regions.

The other two regions show very similar numbers, most of the people that ask for debt relief belong amongst groups of 10 – 15 thousands CZK and 15 – 25 thousands CZK of their income. In case of the region of capital city, we can see a slight difference in amount of people asking for debt relief. As this region has higher incomes in general, also people struggling with debt here do have a higher income. Nonetheless the Liberec region reaches the highest number in the group of 15 – 25 thousands CZK of income, but Prague has almost the same amount here and reaches more than any other region in group of 25 – 35 thousands CZK of income.

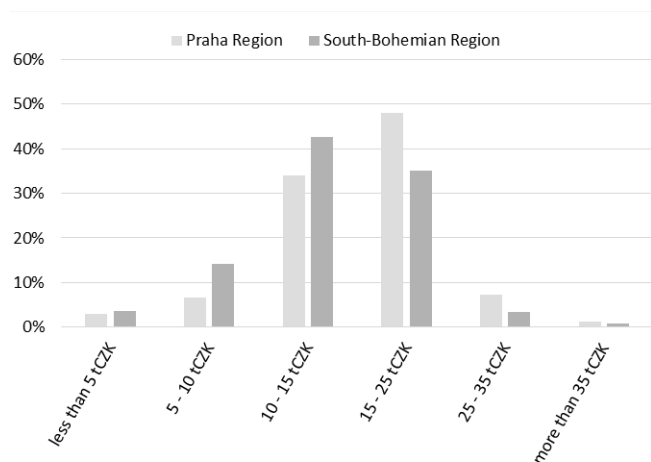


Fig 3 debtors according to their monthly net income (sample 2)

In next step, we analyzed debtors according to their debts and as with the income, the results of regions are very similar. There is just around 10% of those with debt below 200 thousand CZK in all regions. It is mainly caused by the need for the debt relief itself. Most people are able to repay this debt and do not need to submit the proposal. On the other hand, there is opposite with debts over a million CZK. It is also the small proportion of proposals for debt relief, but it is due to inability to pay at least 30% of debts.

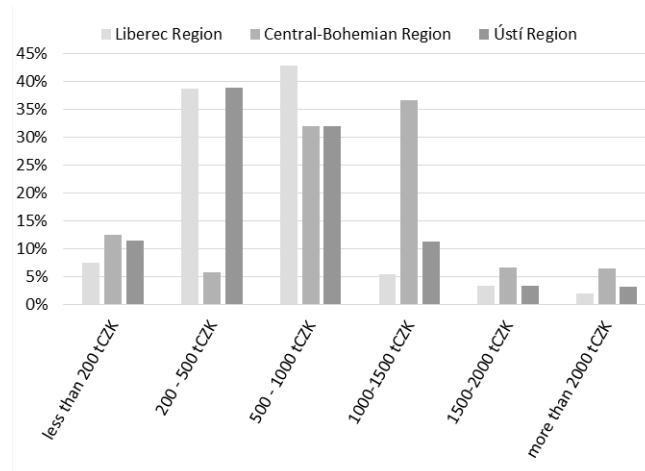


Fig 4 Average debt value (sample 2)

The debt average value of each approved debtor does not differ from region to region. As it was mentioned above, about 8 out of 10 debtors owe amounts between 200 and 1000 thousands CZK. Basically if lower than bottom bound the person does not need to ask for debt relief. Oppositely not many institutions are willing to loan more when a person is already heavily indebted. Our assumption was that higher income should allow a person to reach a higher value of taken debt. This is supported by the willingness of either banking institutions or non-banking institutions to loan more if a person earn more each month. In another words, the upper limit of total debt for a higher income individual is set higher comparing to lower income individuals. Controversially this has not been confirmed. The Prague Region, that reaches the highest average income in whole country, does not differ at all with the debt average value from other regions. We realize that the bounds we set up might be too wide to catch such a difference in total value of debt that would be caused by relatively small difference in incomes in other regions than Prague.

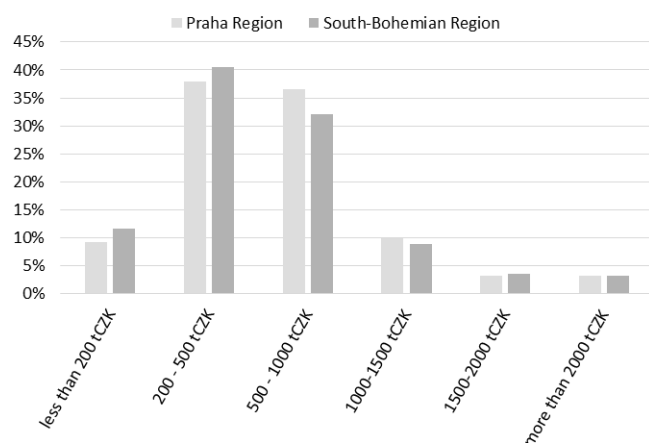


Fig 5 Average debt value (sample 1)

Finally, one of the most important conditions of the insolvency process is the plurality of the creditors. Every debtor must have at least two. In table 5 is shown whether debtor owes only to one type of creditor or more. Only very few have debts just to one type of creditor. Those are usually mortgages in combination with consumer loan provided by banks or many consumer loans from different non-banking institutions. The debtors have mostly even all three types of creditor group. It is common to use loans provided by non-banking institutions to repay other debts – energy, rent, mortgage, etc.

Table 5 Quantity of creditors group

	Liberec Region	Central Bohemian Region	Usti Region	South Bohemian Region	Prague Region
1	5%	3%	4%	5%	5%
2	36%	45%	44%	40%	43%
3	59%	52%	52%	55%	52%

The last table shows very clear dependence of debtors' levels of education on the very fact of being a debtor. In all of the researched regions more than 98% of debtors had no university degree. Debtors with a university degree were represented in every region only in few percentages with Prague Region being the region with the highest percentage of university educated debtors. This is most probably caused by higher financial literacy, higher income and overall better positions in the labor markets of university educated people. Although there exist university educated debtors, having a university degree thus significantly reduces the risk of becoming a debtor.

Table VI University Education level

	University Degree	without University Degree
Usti Region	0,80%	99,20%
Central Bohemian Region	1,10%	98,90%
Liberec Region	2,10%	97,90%
South-bohemian Region	0,90%	99,10%
Prague Region	3,00%	97,00%

V.CONCLUSION

According to the outcomes of this research we can assume there is often strong dependence on certain variables such as net income or total amount of debt. Comparing the five regions in the Czech Republic showed some very similar results in some categories for all regions. The success rate of a debt proposal is very high in all of the regions. Another result similar for all regions are the debtors' net incomes. The most indebted people are among those whose income is between 10 and 25 thousand CZK. Gender distribution among debtors in the regions showed one interesting fact. While the proportion of men and women in Central Bohemian Region and Usti Region corresponds with total amount of men and women indebted in these regions, this proportion does not correspond in the Liberec Region. Liberec Region is the only region where more men proposed for a debt relief than women during the examined time period. The most common debtor in the regions announces bankruptcy before his or her total debt reaches one million CZK. On the other hand, most of all debts are higher than two hundred thousand CZK. The majority of debtors in all regions are indebted towards non-banking institutions whereas the least represented creditor group is Others. It is then to no surprise that in every of the examined regions more than half of the region's debtors are indebted towards all creditor groups. Lastly, according to the results of this research, the risk of becoming a debtor significantly falls if an individual has a university degree.

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