Chapter 3

Czech Republic: Limited Constitutional Fiscal Policy and Public Finance Regulation

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Abstract

This chapter focuses on the fiscal policy in the Czech Republic. It introduces the theoretical approach to public finance according to leading authors and experts in the field. From the legal perspective, it is necessary to highlight the constitutional foundations of public finance and budgetary institutions. However, public finance does not have a crucial role in the Czech Constitution and is not regulated in the Constitution in detail. The following section deals with the budget law, which is strongly connected to state fiscal policy. While fiscal policy as such is the responsibility of the entire government, the central state body upon which attention is focused in the area of public budgets is the Ministry of Finance. The most important laws in the area of fiscal policy include laws on the state budget and budgetary rules for the state budget and local self-government budgets. These are complemented by laws on the issuance of state bonds and the state bond programme. Most recently, the Act on the Rules of Budgetary Responsibility was introduced to regulate fiscal policy. The chapter presents several insights into state debt issues and fiscal deficits. It also analyses the Czech Republic's crisis management in the context of crisis management at the European Union level. Finally, the main findings are summarised, and several *de lege ferenda* recommendations are offered.

Keywords: *Czech fiscal policy, Czech public finance, Czech budget law, budgetary responsibility, state debt, fiscal deficit, crisis management in the Czech Republic*

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1. Czech public finance – selected theoretical approaches

Public finance combines knowledge from several scientific disciplines, including sociology, politology, economics, and last (but not least) law. It is a very dynamic discipline with many topical circumstances, relations, and functions. This diversity dictates how individuals perceive public finance. There are two main groups of opinions on public finance in society: whereas the first group prefers an intensive role in public finance (a robust state, a redistribution mechanism, high levels of taxation, powerful supervising bodies, etc.), the second tries to eliminate public finance and its role. This group believes that a laissez-faire system is the best option for every state and society and that transactions between private groups of people should be free from any form of economic interventionism, such as regulations or subsidies. Though the opinions of society and scientists on the role of public finance differ, one conclusion is clear to all experts: public finance played, plays, and will continue to play a crucial role in the economy, both at the national and international levels. Even if it is not always immediately clear, public finance greatly influences individuals' behaviour.[1]

Public finance in the Czech Republic, as in the rest of the world, is defined as specific financial relations in the economic system between public law authorities (public bodies and institutions) and other subjects (natural persons, legal entities, etc.).[2] There are several areas of interest related to public finance: public financing (basic principles and main fiscal functions), the effectiveness of using public interventions, the influence of financial tools and public expenditures on individual behaviour and decision-making, the characteristics and typology of public revenues and expenditures, public budget deficits, and public debt.[3] The main aim of public finance is to identify the most effective way to allocate sources, that is, how to achieve maximal benefits with limited sources.[4] The content of public finance is to secure certain estates, assure the financing of transfers, and stimulate economic subjects to undertake specific forms of behaviour.[5]

Naturally, public finance is connected with the activities of the state; in other words, one part of the public finance relationship is always the state or any other public law authority. This fact is also evident in the principles of public finance: (i) Irreversibility (non-refundability) – the entity who paid the money (usually the taxpayer or the paying agent) does not have any legal right to its return or the realisation of a counterclaim; there is no individual right to draw money raised by tax collection; (ii) Non-equivalence – the share of money drawn from the public budget is not equivalent to the amount of taxes paid by the taxpayer; (iii) Involuntariness

1 Tomášková and Pařízková, 2015, p. 9.
2 Tomášková and Pařízková, 2015, p. 11.
3 Peková, 2005; Tomášková and Pařízková, 2015, p. 12.
4 Tomášková and Pařízková, 2015, p. 12.
5 Hamerníková and Kubátová, 2004; Tomášková and Pařízková, 2015, p. 12.

– the state has the power to collect taxes (established in the relevant Act) because, otherwise, in the case of voluntariness, nobody would be willing to pay taxes.[6]

With increasing globalisation, public finance now extends beyond national territories. This results in the creation of many international economic groups aiming for stabilisation, support, and cooperation. For these activities, financial sources at the national level are necessary. The most typical example of such an international budget is that of the European Union (EU). This budget is derived from national public finance and, at the same time, has an autonomous scope. The efforts of more centralised EU public finance have been evident in recent years, and it can be assumed that the EU will have further ambitions to influence public finance in its Member States.[7]

The main functions of both national and international public finance are allocation, redistribution, and stabilisation. The basis of the allocation function is to assign financial sources and correct market failures using budget revenues and spending. The redistributive function aims to secure a fairer distribution of incomes and wealth in society. The issue is to define the precise limits of redistribution. Several tools can be used to achieve redistribution, including progressive taxation in both income and property taxes, higher taxation of specific goods, and targeted cash transfers (subsidies) to low-income individuals and families. The stabilisation function seeks to secure minimal economic fluctuations within the economic cycle. Such a state economic policy influences the economy to ensure economic stability.

Public finance also has other, secondary functions. The control function concerns the control of all public revenues and spending. In addition, the regulative function buffers adverse effects in the economy that affect production, unemployment, or prices. The opposite of the regulatory function is the stimulatory function, which motivates subjects toward investments or savings.[8]

From a legal perspective, the legislative function and corresponding regulatory function must also be taken into account. The legislative function aims to create a legal environment for the whole society, from constitutional regulation through legal regulation up to sub-statutory rules. The regulative legal norms are focused on individuals (natural persons, legal entities, and other subjects) to regulate their behaviour, rights, and obligations.[9]

1.1. (Limited) constitutional foundations of public finance and budgetary institutions

The Constitution sensu lato in the Czech Republic is also called the 'constitutional order'. This is because, unlike in other countries, there are two main constitutional

6 Tomášková and Pařízková, 2015, p. 13.
7 Týč, 2000; Tomášková and Pařízková, 2015, pp. 24–25.
8 Tomášková, 2006; Tomášková and Pařízková, 2015, pp. 13–16.
9 Tomášková, 2006; Tomášková and Pařízková, 2015, p. 17.

Acts. The first is the Constitution of the Czech Republic.[10] However, this Constitution sensu stricto does not include the list of fundamental rights and basic freedoms that is typical of most constitutions around the world. The legislator has chosen to create a separate Constitutional Act called the Charter of Fundamental Rights and Freedoms,[11] which is part of the Czech Constitution sensu lato (in the broad sense).[12]

In an honest assessment, and again in comparison with other EU Member States, public finance does not have a crucial role in the Czech Constitution and is not regulated in the Constitution in detail (sensu lato): neither the Constitution sensu stricto nor the Charter of Fundamental Rights and Freedoms includes a specific part concerning public finance. The Constitution sensu stricto in its structure more or less echoes the division of powers (legislative, executive, and judiciary powers) and adds two, or even three, more powers in the state. A specific part of the Constitution on the Supreme Audit Office could be called ‘control power’, whereas a specific part on the Czech National Bank might be referred to as ‘bank power’. The bank power could also be easily transferred to the financial power, with the other (however rare) financial institutes named in the Constitution.[13] The sixth power in the state could, then, be considered to be local self-government power as it deals with the fundamental aspect of local self-government units.

Analysing specific areas of public finance, the current Czech constitutional regulation is limited only to several branches of financial law and several financial institutes.[14] The constitutional regulation of the tax law is very limited: only one sentence in the Charter of Fundamental Rights and Freedoms states that taxes and fees can be imposed only by Acts. The term ‘taxes and fees’ is broader as it covers all taxes, sensu lato (taxes, fees, charges, duties, levies, tolls, and other terms used for public payments to public budgets). All taxes sensu lato must be imposed by legal Acts; alone, municipal generally binding ordinances, governmental decrees, or ordinances issued by ministries would not be enough to assure the constitutionality of the tax. Interestingly, this principle, called ‘*nullum tributum sine lege*’, is set in Art. 11 of the Charter of Fundamental Rights and Freedoms, which deals with ownership rights protection. According to the principle *nullum tributum sine lege* set in Art. 11 para. (5), taxes then limit ownership rights. The missing constitutional principles must be supplemented by the decision-making activity of the Constitutional Court. The court mainly considers extreme disproportionality (the so-called ‘choking effect’) and non-accessory and accessory equality.[15] More about taxation in the Czech Republic is presented in the chapter on tax policy as a part of Czech fiscal policy.

In the area of public subsidies law, the Charter of Fundamental Rights and Freedoms guarantees the free provision of public goods in the field of education.

10 Act no. 1/1993 Sb., the Constitution of the Czech Republic, as amended.
11 Act no. 2/1993 Sb., the Charter of Fundamental Rights and Freedoms, as amended.
12 Radvan, 2016, p. 517.
13 Hulkó and Radvan, 2022, p. 62.
14 Ibid.
15 Constitutional Court, Pl. US 29/08; Hulkó and Radvan, 2022, p. 62.

It also establishes the existence of public health insurance, that is, the creation of specific public monetary funds and the right to the free provision of healthcare as a public good.[16] In addition, the banking law is regulated at the constitutional level – in the Constitution sensu stricto. The Constitution states that the Czech National Bank is the central bank of the state and defines that the main objective of the bank's activities is to ensure price stability. The activities of the Czech National Bank may be interfered with only based on law.[17] More about the national bank in the Czech Republic is available in the chapter on monetary policy.

The budget law is likely the most comprehensively regulated at the constitutional level. The Constitution sensu stricto includes the basic principles for public budgets, setting out that the state budget is a legal Act. The government has a monopoly on drafting the state budget and the final state account, while the Chamber of Deputies of the Parliament of the Czech Republic has sole responsibility for discussing these proposals. This means that the Senate has no rights in this field. The management of state property and the implementation of the state budget is controlled by the Supreme Audit Office. Meanwhile, the Constitution guarantees the budget autonomy of local self-government units. However, there are no constitutional guarantees for fiscal federalism at the constitutional level.[18] The following section examines budget law in the Czech Republic in more detail.

1.1.1. Budget law regulation in the Czech Republic

The budget law is strongly connected to the fiscal policy of the state. While fiscal policy as such is the responsibility of the entire government, the central state body upon which attention is focused is the Ministry of Finance. The most important laws in the area of fiscal policy are those on the state budget and budgetary rules for the state budget[19] and local self-government budgets.[20] These are complemented by laws on the issuance of state bonds and the state bond programme. Most recently, the Act on the Rules of Budgetary Responsibility was introduced to regulate fiscal policy.

Budget law is a set of legal norms regulating the relationships arising in the creation, distribution, and use of financial assets in public budgets, as well as the system and content of public budgets, fund management, and the budgetary process. Budget law must regulate these relationships because the redistribution of resources from resource-creating entities to those that do not create resources but are an integral part of society is undertaken through public budgets. Budget law is commonly classified into three main parts. The general part defines the general terms of budgeting, the various types of public budgets, budgetary principles, and budget functions. The

16 Hulkó and Radvan, 2022, p. 62.

17 Ibid.

18 Radvan, Mrkývka and Schweigl, 2018; Radvan, Mrkývka and Schweigl, 2021; Hulkó and Radvan, 2022, p. 62.

19 Act no. 218/2000 Sb., Budgetary Rules Act, as amended.

20 Act no. 250/2000 Sb., Act on Budgetary Rules for Territorial Budgets, as amended.

special part focuses on the special rules regarding individual public budget types, such as the state budget, budgets of state funds, and budgets of local self-government units. Finally, the procedural part contains the procedural rules of budget creation, time limits, and sanctions.[21]

The Czech Republic is a unitary state. According to its Constitution, the country is divided into municipalities, which are basic territorial self-government units, and regions, which are higher territorial self-government units. These central and local levels are also replicated in the levels of public finance and public budgets. At the central level, there are the state budget and state funds budgets. The state budget is the most important public budget; its purpose is to create a financial plan to reallocate the state's funds to certain state tasks in the following year. From an economic perspective, the state budget is a monetary fund that collects the state's revenues so that these can be further used to cover its expenditures and functions. This type of budget is characterised by its irreversibility, non-voluntariness, and non-equivalence, whereby revenues and expenditures are used for the needs of the state.[22] From a legal perspective, in accordance with the Constitution, the state budget is a legal Act. The State Budget Act must be approved each year through the legislative process specified in the Budgetary Rules Act. The Budgetary Rules Act also regulates, *inter alia*, the functions and content of the state budget and the state final account, the revenues and expenditures of the state budget, the financial management of the organisational units of the state, financial control, conditions for the establishment of state funds, and the methods of managing the State Treasury and state debt. The state funds are established by special Acts as legal entities for the financial security of specially defined tasks.

The draft Act on the state budget is prepared by the Ministry of Finance in cooperation with chapter administrators (central state administration bodies and other organisational units of the state), local self-government units, voluntary associations of municipalities, and state funds. The state budget is based on the medium-term outlook, which contains the expected revenues and expenditures of the state budget and state funds for the two years ahead. The medium-term outlook is prepared simultaneously with the draft Act on the state budget. The Ministry of Finance then submits the draft to the government for approval. Thereafter, the government submits the draft to the Chamber of Deputies at the latest three months before the start of the financial year. Amendments or abolitions of other laws cannot be part of the draft. The proposal is discussed in a public meeting and decided only by the Chamber of Deputies, not the Senate.

In the Chamber of Deputies, the draft Act on the state budget is referred to the Budget Committee for consideration. In the first reading during the general debate, the Chamber of Deputies discusses the basic parameters of the draft state budget, including the amount of revenues and expenditures, the balance, the method of

21 Bakeš, 2012, p. 83; Marková and Boháč, 2007, pp. 41–42; Hulkó and Radvan, 2022, p. 73.

22 Marková and Boháč, 2007, p. 3; Hulkó and Radvan, 2022, p. 74.

settling the balance, the overall relationship to the budgets of higher territorial self-government units and municipalities, and the scope of the executive authorities' powers. The Chamber of Deputies approves the basic parameters or recommends changes to the government and sets a deadline for submitting a new draft. If the Chamber of Deputies approves the basic parameters of the draft state budget, they may not be changed during its further consideration. At the same time, the Chamber of Deputies resolves to assign the individual chapters of this draft budget to committees. The Budget Committee considers the resolutions of the other committees and adopts a resolution thereon.

At the second reading, a detailed debate on the draft state budget and the Budget Committee's resolution on it is held, during which amendments or other proposals are presented. The third reading is a debate in which only corrections of legislative-technical errors, grammatical errors, or clerical errors may be proposed. At the conclusion of the third reading, the Chamber of Deputies votes on amendments. The Chamber of Deputies then decides whether it approves the draft Act on the state budget. Unless the draft Act for the relevant budget year is approved by the Chamber of Deputies before the first day of the budget year, the organisational unit of the state shall manage its budget according to the indicators of the budget provision. As stated above, the Senate has no powers concerning the draft Act on the state budget. An approved Act on the state budget is signed by the president.

The chapter administrator is responsible for managing the state budget resources and other state financial resources in its chapter. The government is accountable to the Chamber of Deputies for the implementation of the state budget, and after the half-year end, submits a report to the Chamber of Deputies in which it assesses the development of the economy and the implementation of the state budget. Furthermore, the Ministry of Finance continuously assesses the performance of the state budget and reports on it to the government after the end of the first and third calendar quarters, with the government submitting it to the Budget Committee of the Chamber of Deputies. State property management and the state budget implementation are also controlled externally by the Supreme Audit Office.

No later than 30 April of the year following the financial year under review, the government submits the draft of the state's final accounts to the Chamber of Deputies. The state's final accounts contain data on the results of the budgetary management of the previous year and a proposal for the use of the budget surplus or the payment of its deficit. It is drawn up by the Ministry of Finance in cooperation with chapter administrators, local self-government units, voluntary associations of municipalities, and state funds. After discussion in the Chamber of Deputies, the Ministry of Finance must publish the state's final accounts, together with the opinion of the Chamber of Deputies, on the Internet.

Regarding the relation between the Czech state budget and the EU budget, the own resources system and the financing of the EU budget are governed by Council Decision 2014/335/EU, Euratom of 26 May 2014 on the System of Own Resources of the European Union. Expenditure indicators for programmes or projects that are co-financed from the EU budget are referenced to draft the Act on the state budget. For European financial resources, the National Fund was established. The National Fund is the sum of the financial resources entrusted by the EU to the Czech Republic for the implementation of programmes or projects co-financed from the EU budget through the Structural Funds, Cohesion Fund, European Maritime and Fisheries Fund, and European Union Solidarity Fund. The financial resources concentrated through the National Fund must be used in accordance with the principles of the budgetary outlook and the obligations arising for the Czech Republic from EU law or international treaties.

There is a close relationship between the central state budget and the budgets of local self-government units (regions and municipalities). As stated above, the draft Act on the state budget, the medium-term outlook, and the draft of the state's final accounts are prepared in cooperation with local self-government units. The state budget pays for grants and repayable financial assistance to local authorities for activities other than those related to business. The state budget also includes subsidies provided for the budgets of local self-government units. The criteria for calculating the amount of subsidy assigned to regional budgets are generally determined annually by the State Budget Act. Subsidies from the state budget to the budgets of municipalities, with the exception of subsidy investment actions, are typically provided through the region in which the municipality is located.

Local self-government in the Czech Republic and the existence of autonomous local units are guaranteed by Art. 8 the Constitution. The other provisions dealing with local self-government in the Constitution are rather strict. Art. 99 states, 'The Czech Republic is subdivided into municipalities, which are the basic territorial self-governing units, and into regions, which are the higher territorial self-governing units'. Regions were created in 2000 by the Constitutional Act.[23] There are 14 regions; however, their borders do not correspond to the historical borders of lands or any previous territorial units. The regions are regulated by the Regions Act,[24] while the Municipalities Act governs the rights and duties of municipalities.[25] The regulation thereof is complex and detail-oriented, especially considering the extremely high number of municipalities in the Czech Republic (almost 6,300). The capital city of Prague has a specific status regulated by the Act on the Capital City of Prague:[26] as a region sui generis, Prague is not divided into separate municipalities but city districts.[27]

Art. 101 para. (3) of the Constitution states that local self-government units are public corporations that may have their own property and manage their own budgets. Unfortunately, this is the only constitutional rule concerning the financial aspects

23 Constitutional Act no. 347/1997 Sb., on Creation of Higher Local Self-Governing Units, as amended.
24 Act no. 129/2000 Sb., Regions Act, as amended.
25 Act no. 128/2000 Sb., Municipalities Act, as amended.
26 Act no. 131/2000 Sb., on the Capital City of Prague, as amended.
27 Radvan, Mrkývka and Schweigl, 2018, p. 897.

of local self-government. Moreover, while the Czech Republic ratified the European Charter of Local Self-Government in 1999, it also declared that it does not consider itself bound by certain provisions of this charter, specifically, the third, fifth, and sixth paragraphs of Art. 9. The provisions in these paragraphs grant local authorities the possibility of introducing local taxes, protect financially weaker local authorities, and grant local authorities the right to be consulted in matters that concern them, respectively. The reason behind the country's decision not to commit itself to at least the latter two paragraphs can be found in a typical Czech feature: the extreme fragmentation of municipalities, which could potentially cause serious complications while implementing the given provisions.[28]

Concerning local self-government budgets, the primary legal source is the Act on Budgetary Rules for Territorial Budgets. This Act regulates the formation, status, content, and functions of the budgets of local self-government units (both municipalities and regions[29]) and establishes rules for the management of these units' financial resources. The financial management of a local self-government unit is governed by its annual budget and medium-term budget outlook. The medium-term budget outlook is a local self-government unit instrument for the medium-term (as a rule, 2 to 5 years following the year for which the annual budget is drawn up) planning of its financial management. This outlook is drawn up on the basis of the contractual relations concluded and commitments entered into.

The annual budget of a local self-government unit is prepared based on the medium-term budget outlook. No legal form is established for local budgets in Czech law; the budget is defined as the financial plan that governs the financing of the activities of the local self-government unit during the budget year (which is the same as the calendar year). As a rule, the budget should be drawn up as a balanced budget. It may also be adopted as a surplus if some of the revenue of a given year is intended to be used in subsequent years or if it is intended to repay the principal of loans from previous years. In addition, it may be adopted as a deficit budget, but only if the deficit can be covered with funds from previous years or a contractually secured loan, credit, repayable financial assistance, or the proceeds from the sale of the local self-government unit's municipal bonds.

The revenues of municipal budgets mainly consist of incomes from own property and own activities, revenue from local charges,[30] shared taxes (e.g. personal income tax, corporate income tax, value-added tax, gambling tax) and own taxes (immovable property tax), incomes from the municipality's own administrative activities (in particular, administrative charges), and subsidies from the state budget and regional budget, etc. The revenues of regional budgets are more or less the same, with the

28 Radvan, 2017, p. 19; Pál and Radvan, 2022, pp. 1160–1161.

29 As well as associations of municipalities.

30 Municipalities have the right to adopt the local bylaw and collect dog charge, charge for stay, charge for using public places, charge on entrance, charge for permission to enter selected places by motor vehicles, charges on communal waste, and charge on evaluation of building land.

exception of subsidies from the regional budget. Czech regions also do not have any own taxes.

In addition to referencing the medium-term budget outlook, local self-government units draw up their budgets based on data from the state budget schedule, through which the state budget determines its relations to the budgets of regions or individual municipalities. Municipalities must also consider data from the regional budget, whereby the regional budget determines its relations to the budgets of the municipalities. The budget of the local self-government unit is adopted by the municipal assembly. The public is involved in the process: the local self-government unit must publish the draft budget on its website and its official notice board at least 15 days before the day on which it is to be discussed at the assembly meeting so that citizens can submit comments on it, either in writing or orally during the discussion at the assembly meeting. The approved budget is published on the local self-government unit's website. If the budget is not approved before 1 January of the financial year, the budgetary management of the local self-government unit is governed by the rules of budgetary provisionality until the budget is approved.

Budgetary management (i.e. the management review) is controlled both internally and externally. Internally, budgetary management is carried out by the financial and control committees. Externally, the municipality has the right to choose to be reviewed by the regional office or auditor. Regions and the capital of Prague are reviewed by the Ministry of Finance. A report on the result of the management review forms part of the final accounts. The discussion of the final accounts at the municipal assembly concludes with a statement of approval of the annual accounts without reservations or approval with reservations. In cases where reservations are raised, the local self-government unit must adopt the measures necessary to correct the identified errors and deficiencies. The same rules apply for publicising the final accounts as for the draft budget.

To summarise this discussion on the Czech budget law, both the central (state) budget and local self-government unit budgets display several common basic features, which can be considered as the budgetary principles underlying the preparation, adoption, management, and control of public budgets. The principle of annuality sets out that public budgets are prepared and approved annually, and that they are valid for one year (with the exception that the carryover of funds to the following year is possible only to a limited extent). The principle of the timeliness of public budgets states that public budgets must be approved and published before the beginning of the financial year, except for budgetary provision. In addition, the principle of the time-limited use of funds expresses that only revenues gained and expenditures allocated during the actual calendar year are included in the budget, and that budgetary units need to spend their allocated funds by the end of the financial year. The rule that public budgeting should be based on an analysis of economic processes and real numbers is called the principle of reality and veracity of public budgets. Meanwhile, the principle of the completeness of public budgets means that the public budget should offer complex coverage of all revenues and expenditures over a given territory.

The principle of the unity of public budgets states that a uniform qualification and classification of revenues and expenditures in public budgets is required. Further, the budgetary structure should be clear, simple, and comprehensible as expressed in the principle of the clarity of public budgets. In addition, the principle of the non-earmarking of revenue and earmarking of expenditure establishes that budget revenues should not be earmarked for predetermined purposes, and conversely, that expenditures should only be used for a predetermined purpose (with the exception of local charges as these compulsory payments are usually paid in return for a public service). The principle of the long-term balance of public budgets expresses that from the long-term perspective, public budgets should be drawn up as balanced. The rule that public budgets are made publicly available in an appropriate manner that allows citizens to comment on the published draft budget is represented in the principle of the publicity of public budgets. Moreover, the principle of gross budgets establishes the need to draw up public budgets containing total revenue and total expenditure. The principle of the efficiency and economy of public budgets defines that public funds should not be wasted. The principle of expenditure over revenue states that expenditures should serve economic growth, for which adequate resources should be provided; to achieve this goal, it is necessary to have objectives for which expenditure is needed and to provide the required revenue to achieve them. Finally, the principle of the identification of the budgetary implications of legislation means that the expected impact of new legislation on public budgets should be quantified.[31]

Many of these principles are set out in the Act on the Rules of Budgetary Responsibility,[32] which contains the core of the regulation, and in the Act Amending Certain Acts in Connection With the Adoption of the Legal Regulation of Budgetary Responsibility, which is an amendment Act.[33] The Act on the Rules of Budgetary Responsibility incorporates EU law,[34] in particular the requirements for timely and regular public access to fiscal data for all subsectors of general government. Specifically, the Act stipulates that state, territorial self-governing units, and other public institutions must comply with the rules of transparency, effectiveness, economy, and efficiency in the management of public finances during the performance of their activities.

The Czech Fiscal Council is the key body for evaluating whether the state and other public institutions comply with the rules of budgetary responsibility. This independent expert body also contributes to the sustainability of the Czech Republic's public finances and reduces the risk of the over-indebtedness of the state. Its opinions and reports serve as inputs for the Czech government, Parliament, and local

31 Hulkó and Radvan, 2022, pp. 73–74.

32 Act no. 23/2017 Sb., on the Rules of Budgetary Responsibility, as amended.

33 Act no. 24/2017 Sb., Amending Certain Acts in Connection with the Adoption of the Legal Regulation of Budgetary Responsibility.

34 Council Directive 2011/85/EU of 8 November 2011 on requirements for budgetary frameworks of the Member States, OJ L 306, 23.11.2011., 41–47.

and regional authorities so that they can plan and implement fiscal and budgetary policies.[35]

The Czech Fiscal Council has several tasks, as follows. The Fiscal Council should

> evaluate the implementation of numerical fiscal rules and … draw up and submit reports on their implementation to the Chamber of Deputies. Examples of such rules include the debt limit, the determination of the total expenditure of the public institutions' sector, or the derivation of the state budget and state funds' expenditure framework.

The Fiscal Council must also 'determine the amount of the debt and announce it the way laws are announced, i.e. within one month of the first publication of the public institutions' sector's debt for the previous calendar year by the Czech Statistical Office'. With regard to the Chamber of Deputies, the Fiscal Council prepares

> a report on the long-term sustainability of public finances, including an assessment of how the direct long-term effects of planned government policies will likely affect the sustainability of public finances. In drawing up this report, the Council shall consider economic and social development, employment, and intergenerational cohesion.

The Fiscal Council must also 'monitor the development of economic management of the public institutions' sector' and 'formulate an opinion on the calculation of the corrective component, which serves to adjust the deviation of the actual economic result of the public institutions' sector from the expected result'.[36]

2. State debt issues: How far is the debt brake threshold?

EU Member States are most often inclined toward rules at the level of the government sector, especially those limiting the size of the general government balance. In addition, rules setting a limit on the size of government debt or government expenditure are also used. Rules limiting government revenues are rather the exception. The rules imposed on local governments (i.e. municipalities) are significantly represented. Again, these rules most often comprise a limit set for the municipal budget balance and, less often, a limit set for municipal debt. Very sporadically, they

35 *The Czech Fiscal Council* [Online]. Available at: https://www.rozpoctovarada.cz/en/cfc/the-czech-fiscal-council/ (Accessed: 21 November 2023).

36 *The Czech Fiscal Council* [Online]. Available at: https://www.rozpoctovarada.cz/en/cfc/the-czech-fiscal-council/ (Accessed: 21 November 2023).

stipulate a limit on municipal spending. There is no limit on municipal revenues. Central governments and social security funds also use revenue limits more often than other types of public budgets. Regional governments use the fewest types of rules, with only a limit placed on budget balance and expenditure.[37]

As mentioned above, the state debt is regulated by the Act on the Rules of Budgetary Responsibility, which was originally established in accordance with EU criteria. The requirements imposed by this law can be summarised as follows. The demands are linked to greater transparency in the management of public funds. Public institutions are obliged to publish not only the draft budget and the draft final account, as in the past, but also the newly approved draft and approved wording of the medium-term budget outlook, the budget, the final account, the rules of the provisional budget, and the budgetary measures implemented. The Ministry of Finance of the Czech Republic has also been given a new agenda, which, according to the given schedule, is to publish data on public institutions' compliance with the rules of budgetary responsibility. At the same time, this ministry is obliged to quantify contingent liabilities, the ownership interests of public institutions, estimates of tax relief, overdue liabilities, and other aspects. The Czech Ministry of Finance also prepares a budgetary strategy for the public institutions sector, which includes the Convergence Programme and expenditure frameworks for the public institutions sector, respectively, for the state budget and state funds.

One of the main rules is the debt brake. If the level of public sector debt rises above 55% of GDP, various measures will be applied in the next calendar month. For the government, this involves preparing a draft and medium-term outlook for the state budget and the budget of state funds, which aims to lead to the long-term sustainability of public finances. At the same time, the government submits proposals for balanced budgets for health insurance companies, which may be deficit only in cases allowed by law, to the Chamber of Deputies. The municipalities must approve their budget for the following year as balanced or in surplus. Other public institutions are not allowed to make new commitments outside of projects co-financed by the EU. These measures are not applied when there is a significant deterioration in economic development, in the event of a state of emergency or war, during a period of emergency measures announced by the government to increase the state's defence capability owing to a deterioration in the security situation, or in the event of high expenditure in response to natural disasters.

If the public sector debt rises above 60% of nominal GDP, the government will seek options to reduce it. The phrasing of this rule has several critics. The measures the government must take to activate the debt brake are very vaguely worded. They also do not oblige the government, for example, to run a balance or surplus, but only to act in accordance with long-term fiscal sustainability, which can be interpreted in different ways. Conversely, in such a situation, municipalities are obliged to propose a balanced or surplus budget.

37 Dvořáková, 2018, p. 29.

Another rule at the municipal level is the fiscal rule concerning the gradual reduction of the existing debt in the event that the current debt of the municipality exceeds 60% of the average income for the last four years. In the following calendar year, the municipality is obliged to reduce the amount of its liabilities by at least 5% of the difference between the amount of debt and the average of its revenues for the last four financial years. If the municipality fails to do so, or if it continues to violate the fiscal rule during the next audit, the Ministry of Finance has the option to suspend the transfer of its share in the tax revenue. For the purposes of the Act on the Rules of Budgetary Responsibility, the municipality's debt includes liabilities from issued bonds, issued bills of exchange, loans received, loans and repayable financial assistance, and the realisation of payments from guarantees.[38]

It should be noted that the general government debt of the Czech Republic consists mainly of the state debt, which has long accounted for more than 90% of the total. In this context, starting in 2028, when, according to our projections, the debt will breach the debt brake threshold, the growth of the debt would be accelerated compared with the baseline scenario. In 2042, the debt would become unsustainable, and the Czech Republic would fall into a debt trap as the implicit interest rate would exceed the growth rate of nominal GDP.[39]

3. The Czech fiscal deficit in numbers

The Czech Republic's Fiscal Responsibility Act is not a constitutional law, although five proposals have been submitted. This fact had a negative experience in 2020 when two significant amendments[40] were made despite a number of experts. The root causes were the external shock of COVID-19 and an inappropriate approach to the fiscal rules, and from this time onwards, Czech public finance cannot be considered sustainable. Within the framework of these laws, the fiscal discipline that had been required until that point decreased. The first amendment was passed in April 2020, along with an increase in the government deficit in the year 2020 and an increase in the structural deficit limit from the original 1% of GDP to 4% for 2021. Simultaneously, a year-on-year consolidation of at least a rate of 0.5% of GDP was selected. According to the first amendment, the structural deficit should be returned to 1% in 2027. Changes to personal income tax were made in the autumn of 2020, with the Czech Parliament approving the abandonment of taxation of the super gross wage and simultaneously keeping a 15% marginal tax rate. Parliament also increased the basis of taxpayer relief in 2021 and 2022. The impact on public

38 Act on the Rules of Budgetary Responsibility.
39 Czech Fiscal Council, 2022.
40 The first amendment was Act no. 207/2020 Sb., and the second was Act no. 609/2020 Sb.

finance was calculated as CZK 100 billion in 2021 and CZK 120 billion in 2022. However, approving these changes in public revenue would have significantly impacted the structural deficit for 2021 (4% of GDP, as stated above). Consequently, the second amendment to the Act on the Rules of Budgetary Responsibility was appended to this law. This amendment brought a complete release of the structural deficit for 2021, with the result that the limit was not determined and the estimated structural balance for 2021, improved by 0.5% of GDP, was to be used to derive the expenditure frameworks for 2022. As such, the structural deficit of 1% is likely to be achieved again only from 2031 unless further legislation is made. Although the Czech Fiscal Council made several comments on these two amendments, both were passed and entered into force. According to the Fiscal Council, the strategy and expenditure frameworks for the government budget and state funds budgets should be consistent with the targets presented in the Convergence Programme submitted to the European Commission in the spring of 2022. However, these amendments are not aligned with the rules stated by the Convergence Programme.[41]

4. Crisis management at the EU level and its relationships with crisis management in the Czech Republic

The EU has offered some instruments to support economic recovery through fiscal policy in times of crisis. The European Commission activated a general escape clause from 2020 to 2022. It was stipulated that that this clause should have a neutral setting in 2023 and that it should be deactivated in 2024. A NextGenerationEU instrument permits the allocation of over EUR 800 billion, which allows the EU Member States to respond flexibly to the current economic situation. In 2023, the EU Member States were required to inform the European Commission of how their fiscal policy would ensure compliance with the public deficit benchmark of 3% of GDP and their ongoing efforts for debt reduction or debt sustainability.[42]

In February 2021, the Pandemic Act[43] was approved to amend the state of emergency during the COVID-19 pandemic and provide the government and the Ministry of Health with expanded powers to deal with the situation with effect for one year. Before and after the adoption of this law, the activities of the state, especially the Ministry of Finance, were extensively criticised. At the beginning of the pandemic, the Ministry of Health did not prepare information support for epidemic management. According to the Supreme Audit Office, '[t]his meant that the regional public health authorities were not prepared to deal with epidemic situations. Until the second half

41 Czech Fiscal Council, 2022.
42 Ministry of Finance of the Czech Republic, 2023.
43 Act no. 94/2021 Sb.

of 2020, they lacked over 900 workstations and laptops'. The Supreme Audit Office also claimed the Ministry of Health had known about the lack of IT equipment at the Regional Hygiene Stations since at least mid-2017. A system that would allow unified departmental communication was also lacking. This system was originally supposed to be completed in 2019; however, the Ministry of Health postponed the deadline three times, and it was not ready when the COVID-19 pandemic was declared. After the declaration of the pandemic, the Ministry of Health did not respond according to the Pandemic Plan of the Czech Republic but, instead, created new bodies to manage the fight against its spread. According to the Supreme Audit Office, the responsibilities and competencies of these bodies were not clearly defined, or their activities were duplicated; for example, the newly established central management team was tasked with the same activities as the already existing Central Epidemiological Commission.[44]

The total amount of funds paid for personal protective equipment and medical supplies (to a total of 148 suppliers) was CZK 7.5 billion. Funds directly spent on the air and rail transport of material to the Czech Republic, including the related services, totalled CZK 0.987 billion.[45] As a result of the pandemic, companies had the opportunity to draw a compensation bonus between 2020 and 2022. This compensation bonus is a tax bonus to compensate for certain economic consequences related to health threats, for example, the emergence and spread of COVID-19. The aim of this measure was to mitigate the effects of the pandemic and provide those affected by it with support to compensate for the resulting economic consequences. The initial requirement for implementing this measure was primarily speed and ease. The compensation bonus was assessed and paid via an application, and the total amount paid out came to approximately CZK 48.3 billion.[46]

In addition to the above, two other programmes have been established. The first was a targeted employment support programme ('Antivirus') aimed at covering employers' wage costs. In total, this programme covered 80% of wages in the event of forced restrictions on operations and quarantine and 60% in the event of related economic difficulties. The estimated cost of this programme was CZK 17.1 billion. Another programme that was announced was the waiver of minimum social security and health insurance advances for the self-employed. The estimated costs amounted to CZK 15 billion.[47]

According to the Supreme Audit Office, the expenditure related to the COVID-19 pandemic amounted to CZK 543 billion.[48] However, only part of these funds was used for the real fight against the pandemic: the Supreme Audit Office claims that almost 90% of the increase in total expenditure in 2021 was unrelated to expenditure

44 *IT řešení pandemie: Stát připravený nebyl. Následné budování IT provázel chaos a improvizace*, 2022.

45 Supreme Audit Office, 2023.

46 Supreme Audit Office, 2022.

47 Hlaváček and Pavel, 2020.

48 Šulc, 2022.

incurred in connection with the fight against COVID-19. During this period, current expenditure continued to increase enormously, while investment expenditure increased only slightly.[49]

Although the Czech Republic had a relatively low public debt before 2020, this debt has increased significantly in recent years. Experts are calling for the consolidation of public finances. The Czech government aimed to reduce the state budget deficit by at least CZK 70 billion in 2023. Unfortunately, the requirement for the consolidation of public finances contained in the Act on the Rules of Budgetary Responsibility is insufficient: this Act does not determine a specific method for achieving the medium-term budgetary objective, which is a structural general government deficit of -0.75% of GDP. Public finances reached a deficit of 3.6% of GDP in 2022, mainly due to the government budget deficit. For 2023, the public finance deficit was forecast at 3.5% of GDP, with the largest share again being the state budget deficit. The deficit will increase the total state debt, which was expected to be 43.5% of GDP in 2023.[50]

5. Conclusions and *de lege lata* recommendations

Public finance in the Czech Republic is defined in the same way as in the rest of the world: it comprises specific financial relations in the economic system between public law authorities (public bodies and institutions) and other subjects (e.g. natural persons and legal entities).[51] The main functions of public finance are allocation, redistribution, stabilisation, control, regulation, and stimulation.[52] From a legal viewpoint, the legislative function and corresponding regulatory function must also be taken into account.[53]

In comparison with other EU Member States, public finance does not have a crucial role in the Czech Constitution and is not regulated in detail in this Constitution, sensu lato. Neither the Constitution sensu stricto nor the Charter of Fundamental Rights and Freedoms includes a specific part concerning public finance. However, a specific part of the Constitution for the Supreme Audit Office could be called ‘control power’, and another specific part for the Czech National Bank might be referred to as ‘bank power’. The bank power could also be easily transferred to the financial power, with the other (however rare) financial institutions named

49 *Nejvyšší kontrolní úřad: Koronavirus byl jen za 10 procenty nárůstu loňských výdajů státního rozpočtu*, 2022.

50 Ministry of Finance of the Czech Republic, 2023.

51 Tomášková and Pařízková, 2015, p. 11.

52 Tomášková, 2006; Tomášková and Pařízková, 2015, pp. 13–16.

53 Tomášková, 2006; Tomášková and Pařízková, 2015, p. 17.

in the Constitution.[54] The sixth power of the state could, then, be viewed as local self-government power as it deals with the fundamental aspect of local self-government units.

The constitutional regulation of the Czech tax law is also very limited, being covered by a single sentence in the Charter of Fundamental Rights and Freedoms, which states that taxes and fees can be imposed only by Acts. Interestingly, this principle, called '*nullum tributum sine lege*', is set in Art. 11 of the Charter of Fundamental Rights and Freedoms, which deals with ownership rights protection. According to the principle *nullum tributum sine lege* set in Art. 11 para. (5), taxes then limit ownership rights. The missing constitutional principles must be supplemented by the decision-making activity of the Constitutional Court. The court mainly considers extreme disproportionality (the so-called 'choking effect') and non-accessory and accessory equality.[55]

As concerns public subsidies law, the Charter of Fundamental Rights and Freedoms guarantees the free provision of public goods in the field of education. This charter also establishes the existence of public health insurance, that is, the creation of specific public monetary funds for this purpose and the right to the free provision of healthcare as a public good.[56]

The budget law is likely is the most comprehensively regulated at the constitutional level. The Constitution includes the basic principles for public budgets, setting out that the state budget is a legal Act. The government has a monopoly on drafting the state budget and the final state account, whereas the Chamber of Deputies of the Parliament of the Czech Republic has sole responsibility for discussing these proposals. This means the Senate has no rights in this field. However, there are no constitutional guarantees for fiscal federalism at the constitutional level.[57]

De lege ferenda, it would be reasonable to be inspired by other (e.g. Polish) constitutions. It would also be advisable to adopt the principle that the state and local self-government units should be assured sufficient public funds for performing the duties assigned to them. This is connected with the rule that everyone shall comply with their responsibilities and public duties, including the payment of taxes, as specified by statute. Further, it would be appropriate to guarantee the revenues of local self-government units in the form of local taxes and charges at the constitutional level. The budget law is generally well regulated under the condition that the budgetary principles underlying the preparation, adoption, management, and control of public budgets are followed at both the central and local levels.

54 Hulkó and Radvan, 2022, p. 62.
55 Constitutional Court, Pl. US 29/08; Hulkó and Radvan, 2022, p. 62.
56 Hulkó and Radvan, 2022, p. 62.
57 Radvan, Mrkývka and Schweigl, 2018; Radvan, Mrkývka and Schweigl, 2021; Hulkó and Radvan, 2022, p. 62.

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