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Control of State Debt in the Czech Republic

Abstract: This article focuses on control of state debt in the Czech Republic. State debt contributes the most to the public debt. Although the Czech Republic is one of the countries with the smallest state debts in the European Union, it has also been the country whose debt has grown fastest year-on-year in the last two years. The aim of this article is to investigate the possibilities to improve control of state debt in the Czech Republic. It works with the hypothesis that control of state debt is problematic in the Czech Republic and needs some amendments related to state debt regulation. The article is divided into two parts. First, a theoretical overview of state debt is included, regulation *de lege lata* is summarized and the current situation relating to state debt during the Covid-19 pandemic is stressed. Second, research findings mentioned in the first part are analysed. By synthesizing these research findings, I suggest amendments *de lege ferenda*.
Keywords: Covid-19 pandemic, Czech Republic, rules of responsibility, state debt

Introduction

Control is a part of management which can check errors in order to take corrective action. It helps to minimize deviation from standards and ensure achieved goals. However, if the control is to be carried out effectively, set objectives must be met. In the business sector, setting a goal is easier than in the public sector. Goal classifications are diverse, differing according to their contextual, functional, structural and temporal characteristics.[1] The question is what goals are set in the public sector, espe-

1 O. Ogbeiwi, General Concepts of Goals and Goal-Setting in Healthcare: A Narrative Review, 'Journal of Management & Organization' 2018, vol. 27, no. 2, pp. 1–18.

cially as time for fulfilling the goals is often lacking. It is obvious that it is easier to define goals at municipality than state level; however, absence of these goals at the state level cannot be taken as an argument.

State (or government) debt is absolutely crucial to public debt, which even leads to imprecise confusion of these terms. State budget deficits are the primary source of state debt. Public debt includes not only state deficits, but also the deficit of the entire public sector, including deficits of municipalities and regions, and also the deficit in the economic management of certain state institutions, which is not transferred directly into the results of state budgets but is covered by different means for which the state only takes over a guarantee.[2]

The aim of this article is to investigate the possibilities to improve control of state debt in the Czech Republic. Attention is aimed only at state debt as it is a crucial part of public debt. The Czech Republic was chosen for its abnormal increase in state debt in the last two years. Compared to 2020, when the coronavirus pandemic began to hit the economy, the budget deficit of EU member countries fell from 6.8% to 4.7% of GDP in a year. However, the Czech Republic was one of the few countries where, on the contrary, there was a sharp increase in the state debt due to an abnormal state budget deficit.[3] Last year's Budget deficit of 2022 exceeded the worst result of 2020, and the Czech Republic ranked among the countries with the lowest economic growth rate in the EU. The share of public debt in relation to GDP increased by 4.2 percentage points year-on-year 2021 which was the highest of any EU country. Mandatory and quasi-mandatory expenditures already absorbed almost 94% of state budget revenues in 2021.[4] Based on these facts, I work with the hypothesis that control of state debt is problematic in the Czech Republic and needs some amendments related to state debt regulation.

To confirm or disprove this hypothesis, I have decided on an Introduction, Methods, Results and Discussion structure for the paper. The research part is divided into two: first, the text includes a theoretical overview of state debt and summarizes regulation *de lege lata* and the current situation relating to state debt during the Covid-19 pandemic. Second, all research findings mentioned in the first part are analysed. Synthesizing these research findings, I suggest amendments *de lege ferenda*.

2 L. Smrčka, M. Arltová, Debt in Relation to the Standard of Living Enjoyed by the Population of Developed Countries, 'Prague Economics Papers' 2014, vol. 23, no. 1, pp. 84–107.

3 ČTK, Vládní dluh zemí EU se loni snížil. V Česku se naopak zvýšil, i tak patří k nejméně zadluženým, E15.cz, https://www.e15.cz/byznys/finance-a-bankovnictvi/vladni-dluh-zemi-eu-se-loni-snizil-v-cesku-se-naopak-zvysil-i-tak-patri-k-nejmene-zadluzenym-1389470 (8.03.2023).

4 Supreme Audit Office, Stanovisko NKÚ k návrhu státního závěrečného účtu České republiky za rok 2021, https://www.nku.cz/cz/publikace-a-dokumenty/stanoviska-nku-ke-statnimu-rozpoctu/stanovisko-nku-k-navrhu-statniho-zaverecneho-uctu-cr-za-rok-2021-id12708/ (8.03.2023).

1. Research

1.1. Theoretical view of state debt

Issues related to state debt are included under public finance. In scholarly studies, state debt tends to be analysed according to its impact on economies above all, whereas public finance is also a theoretical discipline. First, it is necessary to determine the term 'public finance' for better understanding the term 'state debt'. There are a lot of definitions of public finance. One of the most mentioned is by Mrkývka, who offers a view of legal and economic considerations as well. According to him, public finance is related to financial law and can be understood as social relationships which arise and are implemented during the creation and use of monetary funds. Monetary funds (1) concentrate public money; (2) are created in the public interest; and (3) are supposed to meet public needs.[5] This definition has since been extended. Public finance has five main characteristics: (1) it is a comprehensive category for social relations *sui generis*, which are part of monetary relations; (2) public money is the object of public finance; (3) the content of public finance is based on monetary transactions through which public funds are created and distributed, as are the rights, authorisations and obligations associated with it; (4) public finance is still related to the public sector; and (5) the existence of public finance is aimed primarily at the satisfaction of the public interest.[6]

One of the current requests for public finance is transparency – that public authorities inform citizens on the process of collecting and spending public sector income; however, it is not specified which way of reporting is the best. Salachna and Tyniewicki (2017) mentioned that the principle of the substantial transparency of public finances has been inadequately implemented, and it might be incomprehensible from the social addressee's perspective.[7]

The next requests of public finance are economy, efficiency and effectiveness.[8] Efficiency in the public sector makes it possible to (1) increase legislative simplification of administrative rules and procedures; (2) decrease bureaucracy; (3) in-

5 P. Mrkývka, Úvod do teorie finančního práva [Introduction into Theory of Financial Law], Brno 2006.

6 P. Mrkývka, I. Pařízková, E. Tomášková, Veřejné finance a fiskální právo [Public Finance and Fiscal Law], Brno 2014.

7 J. M. Salachna, M. Tyniewicki, The Principle of Substantial Transparency of Public Finance and the Creation of the Active Citizenship, (in:) M. Radvan, J. Gliniecka, T. Sowinski, P. Mrkývka (eds.), The Financial Law Towards Challenges of the XXI Century: Conference Proceedings (1st ed.), Brno 2017.

8 Effectiveness is based on the 'achievement of the final aim' while efficiency 'measures the quality'. Effectiveness is influenced by efficiency because it depends on the knowledge and qualifications of the personnel. N. Kjurchiski, Public Administration Efficiency in Resource Economies, 'The Russian Presidential Academy of National Economy and Public Administration (RANEPA)' 2014, p. 8, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2440725 (8.03.2023).

crease budgetary and fiscal transparency and accountability; (4) extend the use of electronic means of information in the development of processes; (5) implement improvement programmes at local public administration level; and (6) orient the efficiency of the public sector in relation to social needs and the satisfaction of provided goods and services.[9] The last request is the stability of public finance. Implementation of a budget stabilization is associated with lower revenue forecast bias and thus greater fiscal transparency.[10] Legal solutions are not a warranty for protection against over-indebtedness of municipalities, which is how it is stressed in some countries.[11] It is also necessary to continue to emphasize the control of public finances in terms of transparency, economy, efficiency, effectiveness and stability.[12] One particularly concerning area is the ever-growing debt issued by public authorities, which until recently has been largely hidden from public view.

All requests of public finance mentioned above are related to state debt as well; however, transparency is in first place. Free and fair elections and competition between parties in democratically elected legislatures contribute to higher levels of budgetary disclosure.[13] One particularly concerning area is the growing level of debt, whereas the causes of the increase of this debt are not widely presented by public authorities.[14] State debt should have a high level of interest for the public, because a heavy reliance on debt could raise concerns among citizens about intergenerational equity. State debt would have a negative impact on the government's capacity to fulfil all important future service needs and obligations.[15]

To sum up, state debt may indicate threat. Countries with a high level of debt have to solve different type of problems. These can be divided into six groups: (1) economies can lose more output in a crisis; (2) economies may spend more time with zero or low growth ; (3) economies are more heavily influenced by spillover effects

9 P. Florina, Elements on the Efficiency and Effectiveness of the Public Sector, 'Ovidius University Annals: Economic Sciences Series' 2017, vol. 17, no. 2, pp. 313–319.

10 S. Rose, D. L. Smith, Budget Slack, Institutions, and Transparency, 'Public Administration Review' 2012, vol. 72, no. 2, pp. 187–195.

11 A. Zalcewicz, Legal and Financial Aspects of Financing Tasks of Local Government Units from Financial Resources Obtained on Banking and Non-Banking Markets: Issues Connected with the Negative Impact of Current Provisions of Law on the Stability of Public Finances (Polish Case), (in:) M. Radvan, J. Gliniecka, T. Sowinski, P. Mrkývka (eds.), The Financial Law…, *op. cit.,* pp. 246–257.

12 E. Tomášková, I. Pařízková, Evolution of Public Finance in the Czech Republic, (in:) P. Mrkývka, J. Gliniecka, E. Tomášková, E. Juchniewicz, T. Sowinski, M. Radvan (eds.). The financial law towards challenges of the XXI century (conference proceedings), 1st edition. Brno 2002, pp. 93–107

13 J. Wehner, P. de Renzio, Citizens, Legislators, and Executive Disclosure: The Political Determinants of Fiscal Transparency, 'World Development' 2013, vol. 41(c), pp. 96–108.

14 B. Zhao, W. Wang, Transparency in State Debt Disclosure, 'Federal Reserve Bank of Boston Working Paper' 2017, no. 10.

15 J.L. Mikesell, Fiscal Administration: Analysis and Applications for the Public Sector (8th ed.), Boston 2011.

(negative impact a domestic event has on other parts of the world such as e.g. an earthquake, stock market crisis); (4) economies can face a crowding-out of private debt in the short and long term; (5) governments have less scope for counter-cyclical fiscal policy; and (6) economies are adversely influenced in terms of potential (long-term) output.[16] All these problems related to state debt could have been avoided if there had been adequate regulation. The regulation of state debt, and the whole of public finances in general, should be properly thought out and should primarily emphasise transparency, stability and accountability. Nor should there be frequent changes to this legislation. Only in this way can control of public debt be helped and, by extension, can public finances be effective and not a threat for the future.

1.2. State debt regulation *de lege lata*

Act No. 218/2000 Coll., on Budgetary Rules (hereinafter referred to as the 'Budget Rules') is marked like one of the most important regulations of budgetary law in the Czech Republic. This Act deals with the issues of medium-term budgetary frameworks, the state budget, the state final account, the income and expenditure of the state budget, financial assets and liabilities, the management of organizational units of the state and the state contributory organizations, the conditions for the management of state funds, etc. The budgets of territorial self-governing units are regulated by Act No. 250/2000 Coll., on the Budgetary Rules of Territorial Budgets. This Act regulates the issue of income, expenses and other monetary operations, as well as the issue of the creation and use of funds in municipalities and regions. Both these regulations are covered by the constitutional Act No. 1/1993 Coll., the Constitution of the Czech Republic. This Act consists of the fundamental postulates and limits on public institutions.[17]

Another important law is Act No. 243/2000 Coll., on the Budget Allocation of Revenues of Certain Taxes to Territorial Self-Governing Units and Certain State Funds (hereinafter referred to as the 'Act on the Budget Allocation of Taxes'). Also important are Act No. 219/2000 Coll., on the Property of the Czech Republic and its Conduct in Legal Relations and the annually re-adopted Act on the State Budget, which for 2020 was Act No. 355/2019 Coll. Other regulations are individual laws establishing state funds. Related laws regulating the management of municipalities are Acts No. 128/2000 Coll., on Municipalities and 129/2000 Coll., on Regions. The area of control of budgetary discipline is regulated by Act No. 320/2001 Coll., on Financial Control in Public Administration and Act No. 420/2004 Coll., on the Review of the

16 P. Burriel, C. Checherita-Westphal, P. Jacquinot, M. Schön, N. Stähle, Economic Consequences of High Public Debt: Evidence from Three Large Scale DSGE Models, 'European Central Bank Working Paper' 2020, no. 2450.

17 M. Koziel, New Rules of Budgetary Responsibility and their Impact on Public Finances, (in:) I. Pařízková, E. Tomášková (eds.), Interaction of Law and Economics, Brno 2017, pp. 125–137.

Management of Territorially Self-Governing Units. The list of regulations is longer and is extended by a number of pieces of subordinate implementing legislation, regulating, for example, the legal regulations of the European Economic regulations.

The EU tried to solve state debt in EU countries in the Stability and Growth Pact, which was established in 1997 and amended in 2005 and 2011. Countries whose debt-to-GDP ratio exceeded 60% of GDP had an obligation to reduce their debt levels. Accordingly, the average rate of decline of the debt compared to GDP was determined as 1/20th of the difference between the actual level of the debt share in GDP and 60% of GDP. The Stability and Growth Pact obliges signatories to incorporate into national law the rule of balanced general government budgets. To sum up, the annual structural balance of the general government is at its country-specific medium-term objective, with a lower limit of a structural deficit of 0.5% of GDP at market prices. However, these rules were not adhered to. Since the end of the first decade of the 20th century, the EU has increasingly fought public indebtedness and budgetary irresponsibility. The European Union has mechanisms to enforce the fiscal rules onto the legal orders of Member States: first, the Directive of the European Council 2011/85/EU of 8 October 2011 on Requirements for Budgetary Frameworks of the Member States; second, through political pressure to ratify the so-called Fiscal Pact – the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union; third, directly used regulations of the EU. In the Czech Republic, Decree No. 323/2002 Coll., on the Budget Structure is one of the most important regulations of the budget structure. The requirement for budgetary responsibility is stated by Act No. 23/2017 Coll., on the Rules of Responsibility, which regulates all subsectors of general government on contingent liabilities with potentially large impact on public budgets. The rules of budgetary responsibility were thus adopted by the Czech Republic last, and moreover only in the form of an ordinary law, although the government originally submitted a draft constitutional law to parliament. The reasons for this were caused by (1) government crisis; (2) the subsequent resignation of the government in 2013; and (3) the fact that the new government did not have a sufficient negotiating position to approve the constitutional law and failed to get enough votes for the constitutional majority.

According to Act No. 23/2017 Coll., on the Rules of Responsibility, the total expenditure of the public sector must correspond to the sum of (1) a medium-term budgetary objective of no more than 1% of GDP; (2) the cyclically adjusted forecasted total revenue of public institutions; and (3) the amount of expenditure allowed by the escape clause (some countries have more or help less with one-off measures, especially on the revenue side, to meet criteria of the Stability and Growth Pact, e.g. sale of non-financial assets).[18] If, after deducting the cash reserve in the financing of government debt, the debt of the public sector amounts to at least 55% of nominal GDP,

18 Act no. 23/2017 Coll., as amended, § 10.

territorial self-governing units must approve their budget for the following year as balanced or in surplus. Other public institutions, after a period of debt of at least 55% of GDP, may not enter into new commitments under contracts leading to an increase of public sector debt for more than one calendar year, with the exception of commitments relating to projects co-financed by the EU budget or commitments necessary to comply with a court or public authority.[19]

If the debt of a territorial self-governing unit exceeds 60% of the average of its income for the last four years, it is obliged to reduce the debt by at least 5% of the difference between the current amount of debt and the 60% average. Failure to comply with this obligation may lead to the suspension of the transfer of tax revenue to the amount of 5% of the difference between the amount of the debt of the territorial self-government unit and 60% of the average of its income for the last four years.[20]

The Budget Responsibility Act talks about the medium-term budgetary objective; this means the target structural budget balance of each Member State relative to GDP that each country should achieve within a certain period of time. The medium-term budgetary objective requires Member States' budgets to be close to equilibrium or in surplus. It also contributes to ensuring that Member States comply with the requirement to keep government debt below 60% of GDP and government deficit below 3% of GDP, and that their public finances are overall sustainable. The medium-term budgetary objective is set for each country individually every three years. It may also be reviewed more frequently if a Member State implements structural reforms that have an impact on its public finances. On the basis of this review, a budgetary strategy for the public finance sector in the Czech Republic is being developed. The budgetary strategy of the public institutions of the Czech Republic is based on macroeconomic and fiscal predictions, the probability of their fulfilment being evaluated by the Committee on Budgetary Forecasts. The key output of the strategy is the binding expenditure frameworks of the state budget and state funds; compliance with the law and the implementation methodology is assessed by the Czech Fiscal Council.

1.3. State debt during Covid-19

As mentioned above, the spending frameworks for the state budget and state funds in the Czech Republic are based on the statutory structural deficit. The law in its original version set its amount at a maximum of 1% of GDP. With the Covid-19 pandemic and the need for a flexible response by economic policy, Act No. 23/2017 Coll., on the Rules of Responsibility was amended. First, Act No. 207/2020 Coll. increased the scope for fiscal expansion and made it possible to derive spending frameworks for 2021 corresponding to a structural deficit of 4% of GDP. Second, the further

19 *Ibidem*, § 14.
20 *Ibidem*, § 17.

development of the epidemic situation and the adoption of stimulus measures under Act No. 609/2020 Coll. necessitated an increase in the permitted structural deficit, which for 2023 may amount to a maximum of 5.1% of GDP. For the following years, the maximum structural deficits must be reduced by 0.5 percentage points each year. According to the government, this should ensure a gradual return to the full functioning of the standard spending frameworks at the level of the medium-term budgetary objective.

The Budgetary Strategy of the Public Institutions Sector of the Czech Republic sets binding medium-term expenditure frameworks of the state budget and state funds for the years 2023 to 2025. The strategy was approved by the Government of the Czech Republic on 11 May 2022 as a starting document for the preparation of the draft state budget, state fund budgets and their medium-term budgetary frameworks. Expenditure frameworks may be updated during the preparation of the state budget only by a new macroeconomic forecast and the subsequent forecast of state budget revenues and state funds, revenues from the budget of the European Union and financial mechanisms, or measures necessary to cover exceptional events, such as a state of emergency, a state of threat or a major natural disaster.[21]

These changes in regulation have a big impact on state debt. In the Czech Republic, government debt increased from 30.1% of GDP in 2019 to 41.9% of GDP in 2021. However, the Covid-19 pandemic had a significant impact on public finances in all countries. In the EU, government debt increased from 77.5% of GDP in 2019 to 88.1% of GDP in 2021, and in the Euro area it increased from 83.8% of GDP in 2019 to 95.6% of GDP in 2021 (see Table 1).

21 Ministry of Finance of the Czech Republic, Rozpočtová strategie sektoru veřejných institucí České republiky na roky 2023 až 2025, https://www.mfcr.cz/cs/verejny-sektor/statni-rozpocet/rozpoctova-strategie/2022/rozpoctova-strategie-sektoru-verejnych-i-47360/ (09.03.2023).

Table 1. Public balance and general government debt in the EU. Source: Eurostat[22]

Public balance and general government debt, 2018-2021 (¹)
(% of GDP)

	Public balance (net borrowing / lending of consolidated general government sector)				General government debt (general government consolidated gross debt)			
	2018	2019	2020	2021	2018	2019	2020	2021
EU	-0.4	-0.6	-6.8	-4.7	79.6	77.5	90.0	88.1
Euro area	-0.4	-0.7	-7.1	-5.1	85.8	83.8	97.2	95.6
Belgium	-0.9	-2.0	-9.0	-5.5	99.8	97.7	112.8	108.2
Bulgaria	1.7	2.1	-4.0	-4.1	22.1	20.0	24.7	25.1
Czechia	0.9	0.3	-5.8	-5.9	32.1	30.1	37.7	41.9
Denmark	0.8	4.1	-0.2	2.3	34.0	33.6	42.1	36.7
Germany	1.9	1.5	-4.3	-3.7	61.2	58.9	68.7	69.3
Estonia	-0.6	0.1	-5.6	-2.4	8.2	8.6	19.0	18.1
Ireland	0.1	0.5	-5.1	-1.9	63.1	57.2	58.4	56.0
Greece	0.9	1.1	-10.2	-7.4	186.4	180.7	206.3	193.3
Spain	-2.6	-3.1	-10.3	-6.9	100.5	98.3	120.0	118.4
France	-2.3	-3.1	-8.9	-6.5	97.8	97.4	114.6	112.9
Croatia	0.0	0.2	-7.3	-2.9	73.3	71.1	87.3	79.8
Italy	-2.2	-1.5	-9.6	-7.2	134.4	134.1	155.3	150.8
Cyprus	-3.6	1.3	-5.8	-1.7	98.4	91.1	115.0	103.6
Latvia	-0.8	-0.6	-4.5	-7.3	37.1	36.7	43.3	44.8
Lithuania	0.5	0.5	-7.3	-1.0	33.7	35.9	46.6	44.3
Luxembourg	3.0	2.3	-3.4	0.9	20.8	22.3	24.8	24.4
Hungary	-2.1	-2.1	-7.8	-6.8	69.1	65.5	79.6	76.8
Malta	2.1	0.6	-9.5	-8.0	43.7	40.7	53.4	57.0
Netherlands	1.4	1.7	-3.7	-2.5	52.4	48.5	54.3	52.1
Austria	0.2	0.6	-8.0	-5.9	74.1	70.6	83.3	82.8
Poland	-0.2	-0.7	-6.9	-1.9	48.8	45.6	57.1	53.8
Portugal	-0.3	0.1	-5.8	-2.8	121.5	116.6	135.2	127.4
Romania	-2.8	-4.3	-9.3	-7.1	34.7	35.3	47.2	48.8
Slovenia	0.7	0.4	-7.8	-5.2	70.3	65.6	79.8	74.7
Slovakia	-1.0	-1.3	-5.5	-6.2	49.6	48.1	59.7	63.1
Finland	-0.9	-0.9	-5.5	-2.6	59.8	59.6	69.0	65.8
Sweden	0.8	0.6	-2.7	-0.2	38.9	34.9	39.6	36.7

(1) Data extracted on 21.04.2022
Source: Eurostat (gov_10dd_edpt1)

eurostat

It must be noted that in 2021, many countries tried to reduce the high increase in government debt in 2020. Only seven countries show an increase in government debt, namely Bulgaria, the Czech Republic, Germany, Latvia, Malta, Romania and Slovakia. In the Czech Republic, the state budget deficit reached about CZK 420 billion in 2021. This is about CZK 52 billion higher than in 2020, although economic restrictions related to the Covid-19 pandemic in 2021 were not as high as in 2020.[23]

There was no improvement in 2022. At the beginning of 2022, it was clear that it was necessary to repay the state debt of CZK 273.5 billion.[24] In addition, it was necessary to finance the state budget deficit in 2022, which has increased rapidly due to the development of the situation in Ukraine. The government has not created any

22 Eurostat, Public Balance and General Goverment Debt, 2018–2021, https://ec.europa.eu/eurostat/databrowser/view/sdg_17_40/default/table?lang=en.

23 Supreme Audit Office, Hospodaření ČR v roce 2021: rekordní schodek státního rozpočtu, nejrychleji se zadlužující země v EU a ekonomický růst jeden z nejnižších, https://www.nku.cz//cz/pro-media/tiskove-zpravy/hospodareni-cr-v-roce-2021:-rekordni-schodek-statniho-rozpoctu--nejrychleji-se-zadluzujici-zeme-v-eu-a-ekonomicky-rust-jeden-z-nejnizsich-id12710/ (9.03.2023).

24 Ministry of Finance of the Czech Republic, Strategie financování a řízení státního dluhu České republiky na rok 2022, https://www.mfcr.cz/cs/verejny-sektor/rizeni-statniho-dluhu/publikace/strategie-financovani-a-rizeni-statniho-/2022/strategie-financovani-a-rizeni-statniho-47086/ (9.03.2023).

reserves from which it would be possible to repay state debt from previous years. The problem is solved through the issuance of medium- and long-term government bonds.

In this context, the Czech Fiscal Council has declared concern about the sustainability of public finances. According to the Council, public budget revenues have decreased in recent years, while expenditures have been increasing. The structural deficit (which arises regardless of whether the economy is doing well or not) is currently around 3% of GDP, which corresponds to about CZK 220 billion. This is a significant medium-term imbalance that cannot be solved by economic growth alone; rather, the revenue and expenditure sides of the state budget must be adjusted. The enactment of the so-called tax package in 2020 (Act No. 609/2020 Coll., Amending Certain Acts in the Field of Taxation and Certain Other Acts) which, among other things, reduced the tax burden on income from dependent activities, thus losing public budgets about CZK 120 billion per year, had a significant negative impact on this situation. The 2020 tax package has been criticized for three reasons: 1) it came at the wrong time; 2) it was macroeconomically counterproductive; and 3) it contributed to an increase in inflation in the Czech Republic (it is one of the highest in the EU).[25] Act changed Act No. 243/2020 Coll., on the Budget Allocation of Taxes as well. The Act No. 609/2020 Coll. was supposed to bring additional revenues to municipalities and regions after reducing the tax burden on income from dependent activities.

After consolidation, territorial budgets ended with a surplus of CZK 41.3 billion and increased by CZK 27.3 billion year-on-year. The balance on the bank accounts of local authorities amounted to CZK 367.5 billion at the end of 2021 and increased year-on-year by CZK 47.4 billion. According to the report of the Supreme Audit Office, the question is whether local government needs to have such a high reserve in bank accounts at the current inflation rate.[26]

The Ministry of Finance of the Czech Republic presented the Czech Republic Funding and Debt Management Strategy for 2022 – Second Half Update (amending Act No. 57/2022 Coll., on the State Budget of the Czech Republic for 2022) in July 2022. According to this Act, the planned total expenditure is CZK 595.8 billion in 2022, i.e. approximately 9% of GDP.[27]

25 Czech Industry, Propast mezi příjmy a výdaji rozpočtů se zvětšuje. Obrat směrem k udržitelnosti není na obzoru, www.casopisczechindustry.cz/products/nrr-propast-mezi-prijmy-a-vydaji-rozpoctu-se-zvetsuje-obrat-smerem-k-udrzitelnosti-neni-na-obzoru/.

26 Supreme Audit Office, Hospodaření ČR…, *op. cit*.

27 Ministry of Finance of the Czech Republic, The Czech Republic Funding and Debt Management Strategy for 2022 – Second Half Update, https://www.mfcr.cz//en/themes/state-debt/publications-and-presentations/funding-and-debt-management-strategy/2022/the-czech-republic-funding-and-debt-mana-48068 (09.03.2023).

2. Discussion

It must be stated that unfortunately, the published government documents do not contain or indicate appropriate steps that would contribute to the improvement of the current situation. According to the Czech Fiscal Council, the draft medium-term budgetary framework of the Ministry of Finance of the Czech Republic for 2024 and 2025 envisages a structural deficit of 2.9% of GDP. From this, it can be concluded that no systemic reforms are planned.[28]

The biggest problem with the regulation dealing with budgetary responsibility in the amended version of Act No. 23/2017 Coll., on the Rules of Responsibility is its illogicality and ambiguity. The Ministry of Finance deduces that it has enough space and time from a legal point of view for consolidation of public finance. On the opposite side, the Czech Fiscal Council states that the provision amending the structural balance rule, namely the setting of expenditure frameworks, clearly only covers 2022. Since the legislation for 2023 and subsequent years is missing from the amendment, the structural balance rule of -1% of GDP is to be applied again from 2023, according to the Fiscal Council. A return to this rule would therefore mean that the deficit for 2023 would have to be about CZK 140 billion lower.

In 2021, the general government debt-to-GDP ratio reached 42%, rising by 4.4 percentage points year-on-year. According to the Czech Fiscal Council, the debt brake would be removed in 2028. Compared to the previous report, this will be four years later, so this is a partial improvement. This result has two reasons. First, the balance of public budgets in 2021 was better than was expected. Second, the economy of the Czech Republic is characterized by high inflation, which reduces the public debt-to-GDP ratio.

Public finance suffers from long-term imbalances; the so-called tax package in 2020 has significantly worsened the situation, but it was not the cause, which can be seen in the behaviour of Czech governments in previous years. If, in times of economic growth, reserves had been created for the event of a crisis, the current situation would not be so alarming. The current problems are not solved, especially those relating to reform of the pension system. Reforms are currently being postponed, leading to a shift in the financial burden to future generations. This situation was described in literature a few years ago.[29] Creating long-term debt to fund current expenditure, or delaying funding for public pensions, lead to future fiscal problems.

28 Czech Fiscal Council, Propast mezi příjmy…, *op. cit*.
29 B. Zhao, W. Wang, Transparency…, *op. cit*.

Conclusion

It was the stated hypothesis that control of state debt is problematic in the Czech Republic and needs some amendments related to state debt regulation. This hypothesis was confirmed. It is possible to see four issues which have to be solved. First, there is only a medium-term budgetary objective; a long-term budgetary objective is still missing. Moreover, there is no will to determine a long-term budgetary objective. Second, budget responsibility rules budget responsibility rules should be approved by constitutional law. It was a big mistake that this did not happen when the Budget Responsibility Act was ratified. This Act can be easily changed according to the current development of the situation and can also be of a populistic nature; this was especially obvious in 2020, before the election in 2021. It was supposed that budget responsibility rules in the Czech Republic do not improve sustainability, but they can be changed by government majority at any time. In the case of the approval of the fiscal rules at a constitutional level, it would contribute to higher stability.[30] Third, obligations in the Budget Responsibility Act primarily affect the income of municipalities. The government's obligations and its accountability for public finances should be strengthened; governments should be more accountable and transparent in their decisions. Fourth, opinions and reports published by the Council serve as a basis for the government, the Chamber of Deputies and territorial self-governments, among other things, to be able to plan and implement fiscal and budgetary policy. However, it would be appropriate if the Council could also have more powers.

Recent developments in public finance do not indicate that the situation will get better. On the contrary, interventions in the energy market will place an additional burden on public budgets. It is very difficult to stop the large-scale compensation of energy prices. This expenditure may become another significant mandatory expenditure of public budgets. In addition, the compensation programme will allow energy prices to stay at higher levels.

The imbalance of public finance has reached such a point that it can only be eliminated by increasing tax revenues and decreasing mandatory expenditure. These reforms at national level, together with planned reforms at the EU level, have to be implemented in a timely way to ensure risk reduction and to enable the key issues about indebtedness to be solved. It is possible to conclude that the health of public finance is influenced by the level of state debt.

30 M. Koziel, New Rules…, *op. cit*.

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