Statement of the Czech Fiscal Council on the Draft State Budget for 2024

On 27 September 2023, the Czech government approved the draft state budget for 2024, which assumes a deficit of CZK 252 billion. The Czech Fiscal Council (CFC) comments on this proposal as follows:

1. The CFC notes that the draft budget presented by the Ministry of Finance of the Czech Republic implies a general government's deficit of 2.2% of GDP in 2024. The CFC considers this estimate to be reasonable and credible given the current state of information and forecasts of future developments.
2. Even if all the assumptions about the performance of local governments and the health insurance system are not met, the overall deficit should be below 2.5% of GDP. This marks a remarkable improvement on this year's expected deficit of 3.6% of GDP, and an improvement on 2022, which was positively affected by unexpectedly good corporate tax revenue for that year, which will probably eventually reduce the deficit to 3.2% of GDP (compared to the 3.6% of GDP originally projected).[1]
3. Last year, the CFC warned that the parameters of this year's budget were based on the expectation of a structural deficit of 3.1% of GDP, which means not only a significant structural imbalance but also a conflict with the wording of Act No 23/2017 Coll., on the Rules of Budgetary Responsibility ("Act").[2] This is why the CFC pointed out the need to launch consolidation efforts that will gradually bring public budgets back on a sustainable path and in line with the Act. And in this context, the consolidation contained in the government's proposal currently under consideration in the 3rd reading in the Chamber of Deputies seems to bring this movement in a more sustainable direction (the draft law on the state budget for 2024 is based on the assumption of the approval of this package).
4. However, looking at the larger detail of the fiscal parameters of the budget, it is clear that a large part of the consolidation effort will be absorbed by new expenditure that is approved by the government separately in time from the consolidation package or as a result of the increase in debt. Thus, the structural deficit, which is expected to reach 2.2% of GDP next year, shows only a slight improvement compared to this year where a final structural deficit of 2.3% of GDP is expected. Thus, a strong structural imbalance remains built into the public finance system, which will have to be addressed in the period after the full implementation of the current package, i.e. after 2025.
5. The CFC also draws attention in particular to the non-standard course of adjustment (increase) of the expenditure framework of the state budget and state funds. In accordance with the relevant provision of the budget rules[3], the expenditure framework approved in May in the Budgetary Strategy of the Public Institutions Sector of the Czech Republic for 2023-2025 was increased by CZK 40 billion in the draft state budget and medium-term outlook at the end of August. This increase was dominated by additional tax and social security contributions revenues, which were assessed and duly approved by the Committee on Budgetary Forecasts on 31 August 2023. However, during September, the expenditure framework was further increased by almost CZK 19 billion, partly by additional tax and social security contributions revenues. The CFC considers that the above procedure disturbs the proper budgetary process,

[1] The change is likely to be confirmed by the Czech Statistical Office in the October deadline for the notification of the government deficit and debt.

[2] See the Vyjádření NRR k návrhu státního rozpočtu na rok 2023 z 6. října 2022 [‘The Czech Fiscal Council's Statement on the Draft State Budget for 2023 of 6 October 2022; available in Czech only].

[3] See Section 8, paragraph 2, Act No. 218/2000 Coll., on Budget Rules and on Amendments to Certain Related Acts (Budget Rules).

as foreseen by the relevant laws[4], for the following reasons: a) the increase in revenue is not based on a change in expected macroeconomic developments, b) there is no reason to assume that substantial new information on expected tax and social security contributions revenue in 2024 emerged during September that was not available at the end of August, c) the change in expected revenue was not considered by the Committee on Budgetary Forecasts at the time the draft state budget was approved by the government. The increase in the expenditure framework thus made is non-transparent and sets a dangerous precedent for future years.

6. In the context of the above-mentioned change in expenditure frameworks, the CFC also points out that non-tax revenues are growing in importance in the state budget. In recent years, this has been the case in particular for revenues from the sale of emission allowances or revenues from the holding of assets (dividends and profit shares). However, estimates of these revenues are not considered by the Committee on Budgetary Forecasts, which the CFC considers risky. In this context, it can also be noted that part of the increase in the expenditure framework for 2024 is made up of an increase in these revenues.

7. In connection with the revenues from the sale of emission allowances (approx. CZK 41 billion), the CFC also draws attention to the current EU regulation which requires that these funds be used to limit the negative impacts of climate change. Therefore, it cannot be used to finance standard operating expenditure. In the context of this year's problem with the use of the Modernisation Fund and the growing fiscal importance of this revenue, the CFC believes that this issue needs to be given increased attention.

8. In the submitted proposal, the government again (similarly to the approval of the state budget for 2023) transfers part of the deficit to off-budget funds. The dominant item is the State Fund for Transport Infrastructure which is expected to record a deficit of CZK 18 billion.[5] The CFC continues to believe that this approach significantly reduces the transparency[6] and manageability of public budgets. The imbalance of public budgets at the central level should be dominantly concentrated in the state budget.

9. Last but not least, the CFC feels the need to comment on the planned austerity measures on the expenditure side of the state budget. The government has announced that a substantial part of the cuts will take place in the so-called national subsidies, to the extent of approximately CZK 45 billion. The CFC has warned from the outset[7] that it would be very difficult, if not unrealistic, to achieve the announced savings in the area of state subsidies, and that the main "subsidy" to be reduced would be the transfer of the payment of the renewable energy levy back to households and businesses, as was the case before 2023. The government's draft budget for 2024 largely confirms this thesis. The pass-through of the renewable energy levy will also lead to an increase in the composite tax rate.

10. Further year-on-year savings in government subsidies result from the abolition of energy price caps, including the reimbursement to firms and households in 2023 of electricity distribution and transmission charges paid exceptionally from the government budget. However, these are one-off and temporary measures, so their reduction will not have any impact on the reduction of the key structural deficit indicator.

    Nevertheless, the CFC considers passing these charges back to end consumers to be an economically and fiscally rational step. Of course, the social impact of the decision must also

[4] In particular, Act No. 23/2017 Coll., on the Rules of Budgetary Responsibility, and Act No. 218/2000 Coll., on Budgetary Rules and on Amendments to Certain Related Acts (Budgetary Rules).

[5] However, the State Fund for Transport Infrastructure may show an even higher deficit in the following year as it is expected that part of this year's EIB loan (approx. CZK 10 billion) will be spent only in 2024.

[6] One of the consequences of this is that it is not possible to make a fair comparison of government balances over time. Using the above procedure, the government balance improves optically, but the public finance situation does not improve materially.

[7] See Vyjádření NRR k návrhu konsolidace veřejných financí z 11. 5. 2023 [Statement of the CFC on the draft consolidation of public finances of 11 May 2023; available in Czech only]

be taken into account, but this cannot be clearly calculated at this stage. The exact distribution of the levy between households and businesses has not been definitively decided.

About the Czech Fiscal Council

The Czech Fiscal Council is an independent expert body whose main task is to assess whether the state and other public institutions comply with the rules of Budgetary Responsibility set out in Act No 23/2017 Coll., on the Rules of Budgetary Responsibility. The activities of the CFC also contribute to the sustainability of the public finances of the Czech Republic and reduce the risk of excessive state indebtedness. The members of the Czech Fiscal Council are Mojmír Hampl (Chairman), Jan Pavel and Petr Musil. More information can be found at https://www.rozpoctovarada.cz/en/

Media contact:
Anna Urbanová, Head of the CFC's Office
+420 774 370 366
media@unrr.cz