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State Budget and Budgetary Process in the Czech Republic during joining the EU

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Introduction

In the present period there are two main areas of concern regarding the budgetary policy in the Czech Republic. First, the gradual changes of the budgeting from the centralised–planning model into a modern process which leads into improvement of the public sector management and ensures efficiency while fulfilling the social and economic goals. Second, the co-ordination of relations with the EU and connecting our public budgetary system with the EU budget.

For introduction it is useful to mention some facts which were important for the development of the presented scope in the Czech Republic in the last decade. Since the 1990 the role of the state has changed dramatically. These changes were obviously reflected in the public finance system and in the state budget. In 1990 the state budget was for the first time compiled with the aim not to intentionally decrease the transparency of this document, as was commonly practised so far. The new principles on which the state budget was based remained unchanged for the several following years. The state budget was prepared in order to have anti-inflationary impacts. Therefore a surplus was planed and some expenditure cuts were realised, especially in the area of defence, security and subsidies to companies. The volume of redistribution decreased and the decentralisation process (especially of the revenues) was commenced. In 1993 in connection with dividing of the Czech and Slovak Federal Republic and establishing of the Czech Republic the fiscal relations between the different governmental levels were simplified.

The European agreements between the Czech Republic and the European Communities and the individual member states were signed on 4th October 1993 and came in force on 1st February 1995. The Czech Republic applied for the EU membership on 23rd January 1996. The negotiations got under way in 1998.

The European atreements form the legal framework for association between the applicant countries and the European Union and cover their political and economic relations. Their objective is to provide an appropriate framework for the applicant countries' gradual integration into the Community. The Agreements cover the main areas in which the Community *acquis* is to be adopted. They should help the applicant countries prepare schedules for incorporating the *acquis communautaire* and transposing the Community's legal rules into their national law prior to accession.

The preparations for the EU entry concerning the financial and budgetary provisions include following three areas: (1) state budget and the ability to co-finance the EU programs, (2) own resources of the EU budget and their calculation and (3) the administration of their collection. This paper will deal only with the first one.

Although there does not exit for the EU budget the *acquis communautaire*, which would have to be bindingly transpon into the national legislature, the compliance with the EU´s budgetary and financial control standards is required. It is because of the importance of the whole budgetary area for the smooth course of the economical and monetary union and for connection of the EU budget with the budgets of the individual countries. Therefore the recommendations of the EU concern not only the narrow domain of the mutual co-ordination but also some modifications of the national budgetary procedures.

The present paper first reviews requirements and suggestions about the scope of the state budget in the transition period and during the pre-accession process. Than it deals with two main legal changes: Budgetary Classification and the new Budgetary Rules. The draft of the new Budgetary Rules has already been approved by the government and submitted to the Parliament. The most important changes in point of view of EU joining are described. In this context examples of regulation of the same issues from the Netherlands and from Austria are included. I have chosen Austria, as it is one of the most recent EU members. Austria, during its preparation for joining the EU, had to adopt the *acquis communautaire* as well. But regarding the existing budgetary system that was in compliance with the budgetary standards in the EU countries no major legislative changes were undergone. The Netherlands was chosen because it places special emphasis on the multi-annual budgeting.

The goal of the Czech government about the public finance presented in the Policy Statement of August 1998 is to achieve long-term balanced public budget system and to reform the system of the public finance. This includes the new Budgetary Rules of the Republic and the tax reform in connection with establishing of the regions and the tax harmonisation with the EU.

The National Programme 99 for the Preparation of the Czech Republic for Membership of the European Union was approved by the government on 17th May 1999. It suggests as the most important aims to identify and analyse all sorts of the fiscal risks and to prepare the multi-annual estimates, which make possible to evaluate the sustainability of the today's policies and to see the priorities in accordance to the middle-term economical strategies.

During the passage towards the market economy it is necessary to promote sufficient transparency and accountability. Therefore the budget should be formulated in the context of a macroeconomic framework with recognition and assessment of the linkages between the budget and the economy with reasonable assessment of prospective income and what can be achieved at what cost. (Premchand and Garamfalvi (1992))

Legal regulation

The state budget is currently regulated by the Law on the State Budget for the given year and by the Budgetary Rules of the Republic. This regulation is in compliance with the Constitution of the Czech Republic, which claims that the government submits the draft of the State Budget Law and the draft of the State final account to the Chamber of Deputies. The second phase of the budgetary process (i.e. the parliamentary discussion and approval) is also influenced by the Law on the rules of procedure of the Chamber of Deputies. In the Czech Republic there are two chambers of Parliament, but in the budgetary process only the Chamber of Deputies is involved.

Since the 1st January 1997 the new Budgetary Classification has been valid. The system allows comparable reviewing of revenues, expenditures, budget balance and its financing in the system of public budgets in the Czech Republic. The Budgetary Classification is based on the following pillars:

- unification of all public budgets and of all public monetary transactions
- cash accounting
- consolidation of the individual budgets
- three types of classification: economical, functional and by chapters

The most important expected change is the preparation of the new Budgetary Rules, which should come in force from 1st January 2001. The government approved the draft of this law by its Resolution No. 1186 of 15th November 1999.

The new Budgetary Rules reflect the main requirements of the EU on the state budget:

1. multi-annual budgetary framework
2. same treatment of both Czech and EU resources
3. financial control and discipline

In addition, the draft changes the regulation of issuing of the state guarantees (4.), redefines the legal status of the public agencies and modifies the relations with the local budgets.

1. Multi-annual budgetary framework

In the Czech Republic the introduction of the multi-annual budgetary framework is very important for beginning of the pre-structural operations. The programs realised in the framework of the pre-structural operations i.e. currently for instance ISPA, SAPARD and PHARE cover longer period than one year and therefore for the assessment of the individual programs multi-annual budgeting is required. At the same time the multi-annual estimates will become a basic document about the intentions and goals of the budgetary policy in a longer period and by providing information to the public will decrease the uncertainty caused by unexpected governmental decisions.

The new Budgetary Rules introduce the duty to elaborate the multi-annual estimates for the total revenues and total expenditures of the state budget, capital expenditures on selected programs approved by the government and an overview of the credits, where the state guarantee has been issued. If the state budget deficit is expected, the suggested way of its financing must be included. The estimates are elaborated for the next two years, for the investments for the whole period of their financing.

In 1999 the Ministry of Finance prepared the multi-annual budgetary framework of the state budget till 2002. This framework was discussed by the government, which got acquainted with it by its Resolution No. 382 of 27th April 1999. Presented estimates are not compulsory integrated into the annual budget negotiations between the Ministry of Finance and the line ministers yet. However, the government recommended the line ministers to use them as the base for the preparation of the state budget for 2000.

Since 1995 a register of investments with data for a period longer than a year has already been compiled. This register gives a multi-annual overview of the capital expenditures.

In Austria the multi-annual estimates are prepared for the next four years. They include the size and structure of the revenues and expenditures accordingly the classification by chapters and the economical classification. The multi-annual estimates contain information about the impacts of extra budgetary operations on the budget and about the public debt and its expected development. The Ministry of Finance submits the multi-annual estimates to the Parliament together with the draft of the state budget.

In the Netherlands the multi-annual estimates are elaborated for the next four years as well. They contain the expected revenues and expenditures for each budget chapter. Individual line ministries compile the multi-annual estimates for each paragraph. There are also included non-monetary revenues, expenditures and internal transfers. The multi-annual estimates do not have to be formally approved, but they must respect the budgetary norms valid in the particular government's term of office.

Comparing the regulation of the three countries it is obvious that the multi-annual estimates in the Czech Republic cover shorter period and are less detailed. Nevertheless, the EU requirement is to be fulfilled as soon as the new Budgetary Rules are approved by the Czech Parliament.

2. Same treatment of both the national and the EU resources

The new Budgetary Rules introduce the National Fund, which concentrates all resources from the EU, from the state budget and other sources intended for the common programs. These financial means can be transferred into the next fiscal year on contrary to the rest of the state budget. The Ministry of Finance co-ordinates through the National Fund the management of the financial flows and the realisation of the common programs of the Czech Republic and the EU.

For the National Fund the same regulations of the budgetary discipline are applied as for the rest of the state budget. The Czech Republic guarantees that all the misused funds including the penalties or interests will be returned/paid to the EU budget.

Neither the Austrian nor the Dutch Budgetary Rules (Bundeshaushaltgesetz Nr. 213/1986 and Comprabiliteitswet, Stb. 1996, 387) mention explicitly the relations to the EU budget.

In Austria the flows of funds between the national budget and the EU budget is organised as follows: All EU receipts correspond to the national expenditures. Their estimation and accounting are regulated by the Austrian legal norms and undergo full budgetary control. The EU expenditures are allocated to budget lines (EAGGF-Guarantee, EAGGF-Guidance, social fund and regional development) of the specific co-financing federal ministries or directly to the individual states. All receipts from the EU are handled within the federal budget and are subject to full budgetary control.

3. Financial control and discipline

Generally the financial control in the centralised-planing economies was very fragmented; it was executed by many institutions with overlapping spheres of control on selective basis. The EU has set strict requirements on management and control of its own resources provided by the public administration of its member states and on control of the expenditures financed from the EU budget. Regarding the Czech Republic the European Commission requires for instance development of the financial control system including special internal control bodies in each institution. This system must include control ex ante, ongoing and ex post of all budgetary operations and their management together with the decision-making mechanism.

The financial control contains evaluation of conditions important for providing a subsidy or guarantee and assessment of the efficiency and economy of using of the state resources and resources from the National Fund. The manager of the budgetary chapter (mostly the line minister) is responsible for the management of the state resources in his chapter and he has to develop a system of financial control for his chapter. The new Budgetary Rules define cases of misusing of the funds and the penalties in detail.

The Austrian law defines generally the internal control during and after the fiscal year, accounting and factional control. On the contrary, in the new Czech Budgetary Rules there are not included any penalties.

The regulation in the Dutch Budgetary Rules is completed by The Rules on the Budgetary Discipline. In case the estimated ceiling of the expenditures is overstepped, there must be immediately provided measures given by the rules of the budgetary discipline. For determining an overstepping of the estimated ceiling of the expenditures of each of the tree sectors (the kingdom's budget, the social security and the social help) so-called ijklijn is used. Estimated expenditures resulting from valid commitments can be overstepped only if the total cash paid/received follows the estimated cash paid/received and the multi-annual estimates. Overstepping of the estimated expenditures has to be prevented by suitable and early action. If the overstepping occurs, the minister of finance and the Council of Ministers have to be informed as soon as possible. In this case overstepping has to be compensated while respecting the given end of the year marge (1 % of the total expenditures of the budget can be removed in the next year) and between the year's compensations (till the end of the government's term in office). Following the rules of budgetary discipline there must be first done compensations in the frame of the ministry. This is the so-called specific compensation. Subsidy from other resorts or sectors (the so-called general compensation) must be approved by the Council of Ministers and can be used only in case the increase in expenditures was caused by the exchange rate changes or other exogenous factors.

4. State guarantees

One of the main sources of uncertainty in the Czech public finance system is the high amount of the credit guarantees issued by the government. The new Budgetary Rules limit the amount of guarantees which can be issued on 6% of the state budget revenues in the given year. In total the guarantees should not exceed 40% of total state budget expenditures in the given year. Following the data published by the World Bank (1999) the total guarantees outstanding in 1998 were 284,8 bill. CZK (i.e. 50,9% of the state budget expenditures). It is expected that up to 107 bill. CZK of these guarantees will have to be realised from the state budget till 2030. Therefore some experts require more strict and meaningful limitations.

The Austrian Budgetary Rules do not give such a limit, but they contain a detail regulation of the relations between the state, the debtor and the creditor. The Dutch Budgetary Rules does not regulate the state guarantees.

Conclusions

In my contribution I have discussed the recent developments in the area of the state budget in the Czech Republic for instance in regard to joining of the EU. It is very important to regulate the financial and budgetary relations between the Czech Republic and the EU and to ensure the same treatment of both the national and the EU resources. Other presented topics are more related to the continuing transformation process, which is, however, importantly influenced by preparations for the entrance in EU.

The negotiations on the EU joining of the Czech Republic are in progress. The new law on the Budgetary Rules was designed in accordance with the EU recommendations so that as it will be approved by the Parliament without major changes, our legal framework in this scope will be fully in compliance with the EU.

Literature:

Budgetary Rules:

- Czech Republic – current: Act. 576/1990 Coll. (Zákon o pravidlech hospodaření s rozpočtovými prostředky České republiky a obcí v České republice), ministerial regularion 205/1991 Coll. (o hospodaření s rozpočtovými prostředky státního rozpočtu České republiky a o finančním hospodaření rozpočtových a příspěvkových organizací)
- Czech Republic – new: draft approved by the government by its resolution No. 1186 of 15th November 1999 (Zákon o rozpočtových pravidlech a o změně některých souvisejících zákonů)
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Annex 1: General government budgets[1)] in 1993 - 2000

	1993	*1994*	*1995*	*1996*	*1997*	*1998*	*1999 Prelim.*	*2000 Estim.*
Consolidated general gov. revenues	43,8%	42,6%	41,9%	40,3%	39,4%	38,8%	41,9%	40,5%
Consolidated general gov. expenditures	41,2%	41,8%	41,5%	40,6%	40,6%	40,3%	42,7%	44,0%
Overall general gov. surplus/deficit[4)]	2,6%	0,8%	0,3%	-0,3%	-1,2%	-1,5%	-0,8%	-3,5%
Consolidated outstanding debt (end of the year)[6)]	18,8%	17,6%	15,3%	13,1%	12,9%	13,2%	.	.
Total expenditure non-consolidated								
State budget including SFAL[2)]	33,7%	31,6%	31,3%	29,7%	30,0%	30,0%	31,5%	33,9%
Health insurance	4,7%	5,7%	5,7%	5,7%	5,8%	5,8%	6,1%	6,1%
Extra-budgetary funds[3)]	-0,5%	1,0%	0,2%	-0,1%	0,4%	0,6%	0,2%	-0,7%
Local governments	8,8%	9,5%	9,6%	10,9%	8,9%	8,6%	9,3%	9,0%
Total expenditure non-consolidated								
State budget including SFAL	34,2%	32,9%	31,0%	29,3%	28,9%	28,6%	29,5%	29,6%
Health insurance	5,2%	5,5%	5,3%	5,5%	5,7%	5,8%	6,1%	6,1%
Extra-budgetary funds	0,9%	0,7%	1,1%	0,6%	0,5%	0,4%	0,3%	0,2%
Local governments	9,0%	9,5%	9,4%	10,4%	8,6%	8,6%	10,3%	9,0%
Surplus/deficit[5)]								
State budget including SFAL	0,5%	1,3%	-0,2%	-0,3%	-1,0%	-1,4%	-2,0%	-4,2%
of which state budget				-0,1%	-0,9%	-1,6%	-1,6%	-1,8%
Health insurance	0,5%	-0,2%	-0,3%	-0,2%	-0,1%	0,0%	0,1%	-0,1%
Extra-budgetary funds	1,4%	-0,3%	0,9%	0,6%	0,0%	-0,2%	0,1%	0,9%
Local governments	0,2%	0,0%	-0,2%	-0,5%	-0,3%	0,1%	1,0%	-0,1%
Consolidated outstanding debt	18,8%	17,6%	15,3%	13,1%	12,9%	13,2%	.	.
State budget including SFAL	15,6%	13,7%	11,2%	10,3%	10,3%	10,6%	.	.
Health insurance	0,0%	0,1%	0,0%	0,1%	0,1%	0,1%	.	.
Extra-budgetary funds	2,9%	2,8%	2,9%	1,4%	1,0%	0,8%	.	.
Local governments	0,3%	1,2%	1,5%	1,8%	2,1%	2,3%	.	.
Tax quota[7)]	38,5%	37,7%	37,0%	36,2%	36,2%	36,3%	36,3%	36,3%

Source: Czech Republic - Macroeconomic Forecast, Ministry of Finance of the Czech Republic, January 2000

Notes: 1) Based on current GFS (Government Finance Statistics - IMF) methodology
2) SFAL - State financial assets and liabilities
3) Extra-budgetary Funds: Czech Land Fund, National Property Fund, State Fund for Culture, State Fund for Environmental Protection, State Fund for Soil Fertilisation and State Fund for Support and Development of Czech Cinematography.
4) In 2000 the overall balance differs from the state budget draft figure because the redemption of National Property Fund bonds (15 bill. CZK in 2000) is classified as financing operation bellow the line (differently from national methodology).
5) The consolidated general government balance does not equal the sum of balances of individual parts of government due to credits inside government sector.
6) Excluding indirect debt of transformation institutions (Konsolidační banka, Česká inkasní jednotka, Česká finanční).
7) With consolidation of social security contributions of government employees