

THE PROCESS OF BUDGETING AND ISSUES OF INDEBTEDNESS IN THE CZECH REPUBLIC

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Abstract: *The proposal of state budget is based on the medium-term outlook and expenditure framework, which are adopted in the year preceding the year for which the budget is drawn up. Draft documents are presented by the Ministry of Finance to the government for approval. Consideration of the legislation is entrusted to the Chamber of Deputies. During the approval procedure, the State Budget Act undergoes three readings and after its approval it represents basis for state's management in a given year. The public expenses are represented not only by the budgetary expenses, but also by the expenses of state funds, expenses of regional administrative units, or expenses of other public entities. Management of public funds is connected to problems of indebtedness that are being solved in different ways and should be solved through a special legislation governing budgetary responsibility in the future.*

Keywords: *budgetary process, budgetary outlook, expenditure framework, public entities, regional administrative units, indebtedness*

1. DRAWING UP THE STATE BUDGET

According to article 42 (1) of the Constitution of the Czech Republic the State Budget Bill is submitted to the Chamber of Deputies by the Government.

Under section 8 (1) of Act No. 218/2000 Sb. stipulating budget rules and changing certain related laws (Budget Rules), as amended (hereinafter “Budget Rules”), the State Budget Bill is drawn up by the Ministry of Finance (hereinafter “the Ministry”) in cooperation with budget chapter administrators, regional administrative units, voluntary alliances of communities, Regional Councils of Cohesion Regions and state funds.

The bill is based on a medium-term expenditure framework adopted in the year preceding the year for which budget is being drawn up. The State Budget Bill for the relevant year as well as the proposed medium-term expenditure framework is submitted by the Ministry of Finance for Government approval. The medium-term expenditure framework consists of the total expenditures of the state budget and state funds for every year of the medium-term outlook, and it is determined upon a motion of the Government by the Chamber of Deputies in its resolution on the State Budget Bill submitted by the Government; the medium-term expenditure framework is always determined as a single amount and does not contain individual defined expenditures.

The medium-term outlook is drawn up simultaneously with the State Budget Bill and contains the expected revenues and expenditures of the state budget and state funds for individual years of the outlook, it follows the budget structure and provides the assumptions and intentions that form the basis of the expected revenues. The work on creating the medium-term outlook is managed by the Ministry. If the medium-term outlook predicts a budget deficit, it contains also the expected manner of funding the deficit. The

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medium-term outlook is drawn up for the period of two years following the year for which the state budget is submitted. It contains the indicators for the year for which the state budget is submitted. In case of expenditures for programmes and projects co-financed from the European Union budget the period of medium-term outlook is identical with the period of financing of such programmes or projects. In terms of obligations of the state arising from approved concession contracts the period of medium-term outlook is identical with the period of duration of the obligation. With respect to loans where state guarantee was provided the period of medium-term outlook is the same as the period of repayment. The medium-term outlook is drafted by the Ministry in cooperation with the chapter administrators, regional administrative units and state funds and it is submitted to the Government together with the State Budget Bill.

The Government discusses the draft medium-term outlook simultaneously with the State Budget Bill and after it is approved it is submitted by the Government (as a separate document) to the Chamber of Deputies at the same time with the State Budget Bill. The Government must submit the State Budget Bill to the Speaker of the Chamber of Deputies at the latest three months before the commencement of the budget year. Amendments to such bill may be submitted no later than 15 days before the commencement of the session of the Chamber determined for the first reading of the bill.

2. CONSIDERATION OF THE BUDGET BILL AND THE POSSIBILITIES OF AMENDING IT

Under article 42 (2) of the Constitution of the Czech Republic the State Budget Bill is considered only by the Chamber of Deputies in public session and the resolution on the bill is adopted only by this chamber (as opposed to all other laws where the Senate is also involved). The state budget is approved in the form of a law. The consideration of the State Budget Bill is governed by part thirteen of Act No. 90/1995 Sb. According to this act the Government submits the State Budget Bill to the Speaker of the Chamber of Deputies at the latest three months before the commencement of the budget year. Amendments to such bill may be submitted no later than 15 days before the commencement of the session of the Chamber determined for the first reading of the bill. The Speaker refers the State Budget Bill to the budget committee for consideration. The State Budget Act must not include any changes, amendments or repeals of any other acts.

The State Budget Bill is introduced by the sponsor followed by a speech of the rapporteur member of the budget committee. The Chamber of Deputies considers in general debate within the first reading the basic data of the State Budget Bill including the revenues and expenditures, the balance, manner of settlement of the balance, overall relationship to the budgets of higher regional administrative units and communities and the scope of authority of the executive bodies. The Chamber either approves the basic data of the State Budget Bill or recommends to the Government to make some changes – in such a case a deadline is set for the Government to submit the revised bill. The deadline for submission of the revised bill must not be less than 20 days and more than 30 days after delivery of the resolution of the Chamber to the Prime Minister.

The provision of section 102 (4) of Act No. 90/1995 Sb., the Standing Rules of the Chamber of Deputies, as amended (hereinafter “the Standing Rules”) stipulates that if the Cham-

ber of Deputies approves the basic data of the State Budget Bill, such data may not be changed in the course of further consideration of the bill.

At the same time the Chamber of Deputies adopts a resolution to refer individual chapters of the State Budget Bill to committees. The committees consider the referred chapters of the State Budget Bill and submit their resolutions to the budget committee within the time limit stipulated by the Chamber. The minimum period for consideration of a referred chapter of the State Budget Bill is five days. The provision of section 103 (3) of the Standing Rules stipulates that a committee may propose changes only to that chapter of the state budget that was referred to that committee. If the committee wants to achieve a change in another chapter, it must request that the proposed change should be considered by the committee to which the chapter was referred. The committee has the duty to request the opinion of the chapter administrator concerning all proposed changes. This becomes the framework within which every deputy may introduce motions to amend the State Budget Bill or other motions in the course of clause-by-clause debate during the second reading of the Bill (section 105 (2) of the Standing Rules). The resolutions of the committees and opponent reports, if any, concerning individual chapters of the State Budget Bill are considered by the budget committee in the presence of rapporteur members of individual committees and the budget committee adopts a resolution. The resolution and also the opponent report or record of the committee meeting, if any, is submitted by the budget committee to the Speaker of the Chamber of Deputies. The resolution of the budget committee and any opponent report or record of the committee meeting is delivered to all deputies no later than 24 hours before the commencement of the second reading of the State Budget Bill. The same must be done with a resolution of a committee if such committee adopts a dissenting resolution with the resolution of the budget committee, in accordance with the rules stated above.

In the second reading the State Budget Bill is introduced by the sponsor followed by a speech of the rapporteur member of the budget committee. The State Budget Bill and the budget committee report are debated clause-by-clause and motions to amend as well as other motions are submitted in the course of this debate. A summary of the submitted motions to amend and other motions submitted is delivered to all deputies and to the sponsor.

The third reading of the State Budget Bill may be commenced at the earliest 48 hours after the end of the second reading. In the course of the debate within the third reading it is only possible to submit motions to correct legislative technicalities, grammatical errors, clerical and typographical errors, motions to make changes logically arising from the submitted motions to amend the bill, or to submit a motion to repeat the second reading. At the end of the third reading the Chamber of Deputies takes a vote on motions to amend and on any other motions. Then the Chamber adopts a resolution stating whether it consents to the State Budget Bill.

As the relevant constitutional law does not exist, it is practically impossible to review the compliance of the State Budget Act with the Constitution in proceedings before the Constitutional Court (proceedings under article 87 (1) (a) of the Constitution of the Czech Republic regulating repeal of an act or individual provisions). The only possibility (already put to practice) is to review the compliance of the process of adopting the State Budget Act with the Constitution. A motion to repeal the act cannot, however, be submitted by

an individual, it must be submitted by persons defined in section 64 (1) of the Constitutional Court Act, for example by the president, a group of at least 41 deputies or a group of at least 17 senators.

The Constitution of the Czech Republic does not forbid the possibility of drawing up a budget with a deficit.

Under section 8a of the Budget Rules the Chamber of Deputies stipulates in its resolution upon a motion of the Government a medium-term expenditure framework in the form of a total amount. The medium-term expenditure framework represents the total expenditures of the state budget and state funds for every year of the medium-term outlook (which is drawn up for two years following the year for which state budget is submitted), with the exception of subsidies to state funds. The amount of the medium-term expenditure framework for the first year of the medium-term outlook is based on the amount of the medium-term expenditure framework for the given year stated in the medium-term expenditure framework in the resolution of the Chamber of Deputies concerning the Government State Budget Bill for the current year to the extent that the amount of the expenditure framework may be increased or decreased to reflect the following:

- a) Substantially different development of consumer prices than that expected when the amount was stipulated;
- b) Changes arising from the Tax Revenue Allocation Act if the changes result in increasing or decreasing the state budget expenditures and if these consequences were not taken into account when stipulating the amount;
- c) Changes in the amount of incoming resources from the European Union budget and from financial mechanisms that were expected to be in different amount when the expenditure framework was stipulated;
- d) Changes amounting to up to two per mil of this amount if it is necessary to take into account the impacts that were not considered when the amount was stipulated;
- e) Extraordinary situations that were not taken into account when the amount was stipulated.

When drawing up the State Budget Bill for the following year the amount of the medium-term expenditure framework stated in the resolution of the Chamber of Deputies concerning the Government State Budget Bill for the current year is adjusted for the purposes of the amount that is to be stated as the total expenditures of the state budget for the following year. A similar procedure is applied also when drawing up the State Budget Bill for the following year when the amount of the medium-term expenditure framework stated in the resolution of the Chamber of Deputies concerning the Government State Budget Bill for the current year is adjusted for the purposes of the amount that is to be stated as total expenditures of the state budget for the following year with the exception of the adjustment that is applied in case there were changes due to extraordinary situations that were not foreseen when stipulating this amount and when an adjustment is made in the maximum amount of one per mil.¹

If the amount of the medium-term expenditure framework for the first year of the medium-term outlook proposed by the Government is not identical with the amount of

¹ MARKOVÁ, H., BOHÁČ, R. *Rozpočtové právo*. Praha: C. H. Beck, 2007.

the medium-term expenditure framework for the same year that was stipulated by the Chamber of Deputies in its resolution concerning the Government State Budget Bill for the current year as the amount of medium-term expenditure framework for the second year of the medium-term outlook, the Government must draw up reasoning for such change. The Government draws up reasoning for the change in the amount of the medium-term expenditure framework also for the following year of the medium-term outlook in accordance with the proposed amount of the total expenditures of the state budget for the following year. The reasoning for these changes is submitted by the Government to the Chamber of Deputies simultaneously with the State Budget Bill for the following year.

3. OPTIONS TO RESTRICT STATE DEBT AND PROPOSED WAYS OF RESTRICTING INDEBTEDNESS

One of the possibilities that may lead to state debt is providing guarantees for certain persons. However, the Czech Republic provides state guarantees only if it is stipulated by a special act. For the state guarantee the debtor pays into the state budget 0,5% of the guaranteed amount within 30 days of the date of effect of the act stipulating provision of that guarantee.

The Ministry of Finance sets up a state guarantee fund for expenditures related to realisation of state guarantees. When drawing up the State Budget Bill a list is created of all payments representing realization of state guarantees that the Ministry may be obliged to make in the following year including an estimate of the likelihood of having to make the payment as a result of realization of the state guarantee for every such item on the list. The budgeted expenditures in the State Budget Bill then include the percentages of the individual payments reflecting the percentage likelihood of realization of the guarantee. In the following year the Ministry transfers from the state budget into the state guarantee fund an amount that is the total of all such amounts. Under the Budget Rules (section 3) the realization of state guarantee means payment of the guaranteed amount by the state instead of the debtor whose debt was guaranteed by the state, to the creditor on the basis of a contract of guarantee concluded between the state and the creditor for the benefit of the debtor, or on the basis of a statement of a guarantor or letter of guarantee issued by the state to the creditor for the benefit of the debtor, or on the basis of an act imposing the guarantor duty on the state. This definition restricts the possibility of creating certain types of debt.

In terms of other state expenditures that may have impact on creating state debt, under the Budget Rules section 24 (1) (a) the Government or the Minister of Finance based on authorisation granted by the Government may consent to implementation of necessary expenditures not provided for in the state budget, on condition that the payments will be balanced by savings in other state budget expenditures. Such expenditures are though limited to a maximum of 5 % of the total volume of approved expenditures of the chapter where the adjustment is being made and to a maximum of 10% of the total volume of the binding indicator in the chapter where the adjustment is being made.

A transfer between binding indicators or a change of an indicator of the state budget within a chapter exceeding 10% of each indicator may be approved according to the

Budget Rules only by the budget committee of the Chamber of Deputies (section 24 (3)). Such a budget measure of the budget committee is not put to vote in plenary session of the Chamber of Deputies. However, the Government must inform the Chamber of Deputies of all budget measures in reports on adherence to the state budget or any time the Chamber of Deputies requests it (section 24 (7)).

The issue of restricting indebtedness is to be addressed by a new constitutional act “con. law” to regulate budget responsibility that was discussed in the Chamber of Deputies before it was dissolved.² At present it will be necessary to submit the bill again. If the constitutional law is adopted in some form, it will be necessary to adopt or amend the wording of specific rules of its implementation in a separate law. Such separate bill had been in the stage of discussion in the legislative bodies before the Chamber of Deputies was dissolved and now it is questionable whether and, if so, when an act regulating these issues will be adopted.

It is also worth noting that the current legal regulation addresses the issue of budget management and covering of necessary and unforeseeable expenditures of the state by creating a budget provision for the Government. The Government budget provision is created in the minimum amount of 0,3 % of the expenditures of the state budget for the relevant budget year and it is the Government, and, to the extent defined by the Government, the Minister of Finance who decides on the use of this provision. The Government reports to the Chamber of Deputies on the use of the Government budget provision in the reports on adherence to the state budget.

Legislative restriction of the overall amount of debt on the state level has not been in fact put in place so far. It should be addressed by the above mentioned constitutional law to regulate budget responsibility and the law to regulate in detail certain provisions of this law. However, in the current effective legislation there are some rules regulating budget responsibility applicable to financial management of regional administrative units in Act No. 250/2000 Sb., stipulating budget rules for regional budgets, as amended (see below).

The current legislation does not make it possible on the national level for the Chamber of Deputies to approve in an extraordinary majority vote that a debt be created or the stipulated limits be exceeded.

The proposed legal regulations included regulation of public indebtedness. They were supposed to emphasise long-term sustainability of public finance and maintaining of a certain level of debt to GDP ratio in the long run. A new instrument in the form of the so called debt brake should be introduced. It should play the role of a correction mechanism returning public finance into a position that should have a positive impact on financial stability and should maintain the amount of public debt in relation to the convergence criterion of the proportion of gross government debt to GDP in current prices (60% of GDP). The concept of the debt brake rule assumes application of the public debt definition introduced for the purposes of the excessive deficit procedure in the European Union (Protocol No. 12 on the excessive deficit procedure) and of the Stability and Growth Pact. The amount of public debt in the proposed documents is defined as the proportion of the

² MARKOVÁ, H. Rozpočtová odpovědnost. In: SEHNÁLEK, D., DÁVID, R., VALDHANS, J. (eds.). *Dny práva – 2010 – Days of Law: 4. ročník mezinárodní konference pořádané Právnickou fakultou Masarykovy univerzity: the conference proceedings*. Brno : Masarykova Univerzita, 2010, pp. 691–700.

debt of public institutions, i.e. the total gross debt of the sector of public institutions in nominal value, consolidated within and among subsectors of the public institutions sector unpaid as of the end of year, expressed as a percentage proportion of nominal gross domestic product. Public institutions debt consists of the categories of debt obligations such as current money and deposits, securities other than participating interests with the exception of financial derivatives, and loans. The constitutional bill proposed the principle of limits on debt connected with automatic correction mechanisms performing the function of a debt brake. The constitutional bill stipulated five debt brackets, but the values of those brackets were subject to political debate which has not been resolved. The bill also does not address how such restrictions would be enforced, who could challenge breach of these rules, who would assess such breaches and in what type of proceedings, etc. In this context it is also necessary to address the issue of the nature of the debt including the question whether a debt arising in breach of the stipulated restrictions is void. Neither the effective nor the proposed legislation provides the answers to these questions.

4. EXPENDITURES OF PUBLIC BUDGETS AND THE ROLE OF PUBLIC PERSONS

Not all public expenditures in the Czech Republic form part of the state budget. The expenditures of administrative units – the communities and regions – form part of their own budgets, the expenditures of state funds form part of the individual budgets of these funds.³

The expenditures of health insurance companies for healthcare (healthcare services) are expended also outside of the state budget, in accordance with the rules stipulated by Act No. 48/1997 Sb., to regulate public health insurance and to amend certain related laws (part five regulates the conditions of provision of healthcare services paid from public health insurance).

The expenditures for pension insurance benefits (including expenditures for retirement pensions), sickness insurance benefits, accident insurance benefits, state social support benefits, other social welfare benefits, expenditures for unemployment benefits, benefits paid out during requalification and for active employment policy are on the other hand paid from the state budget.

State funds are off-budget funds formed on the basis of separate laws which stipulate the nature of expenditures covered from the relevant state fund. The budgets of state funds are approved by the Chamber of Deputies in relation to discussion and approval of the state budget for the relevant year. Currently the following funds exist: State Environmental Fund of the Czech Republic, State Fund for Transport Infrastructure, State Culture Fund of the Czech Republic, State Filmmaking Fund, State Fund for Housing Development and State Agricultural Intervention Fund. The expenditures of these funds are always defined in the law forming the fund and are related to the budget of the relevant fund.

The issue of expenditures of public budgets is related to the issue of public persons. Even the definition of the concept of public person is problematic as it differs in various Czech laws depending on the purpose for which the definition is to be used (statistics, access to

³ MARKOVÁ, H. Rozpočtové výdaje, jejich povaha a členění. In: Radovan Dávid, David Sehnálek, Jiří Valdhan (eds.). Brno: Masaryk University, 2009, pp. 1187–1195.

information, etc.). A more suitable definition of the concept for budget purposes is to be included in the law regulating the budget responsibility rules. It would be better to define the concept so that it can be used for all purposes, but that right now seems to be unrealistic. It is assumed that the new constitutional law or the related law will define the sector of public institutions that will consist of institutions having features of government sector (in accordance with Council Regulation No 2223/96 of 25 June 1996 on the European system of national and regional accounts in the Community) as it is defined by the Czech Statistical Office. Under the submitted constitutional bill a public institution is to be registered in a register of economic persons as a unit of this sector of national economy. The sector of public institutions is to include structural components of the state, state facilities having similar position to structural components of the state, organizations formed by a public institution and receiving contributions from the state budget, state funds, regional administrative units, voluntary alliances of communities, Regional Council of Cohesion Region, organisations receiving contributions from regional administrative units or voluntary alliances of communities, legal entities of public nature such as health insurance companies, public research institutions or public universities. It should also include legal entities of public nature founded or formed for a particular purpose of satisfying needs of general interest having market character that are funded primarily by the state, regional or local bodies or other public persons managed by the state, regional or local bodies or other public persons. This group should also include persons whose administrative, managing or supervisory board has more than a half of members appointed by the state, regional or local bodies or another public person. Public persons as a whole are included in the state budget, they are not off-budget persons and as such cannot generate budget deficit.

There is no explicit state liability for the debts or solvency of public persons stipulated in the form of law, there is only a special provision of section 47 of the Budget Rules, whereby the state is liable for the obligations of organisations receiving contribution from the state budget arising in relation to carrying out their principal activity. Again the proposed legal regulation purports to address state debt. The budget strategy of the sector of public institutions should serve as a starting point for drawing up the state budget and the budget of state funds and it should be submitted by the Government for consideration in the Chamber of Deputies. The detailed contents of the budget strategy of the sector of public institutions should be stipulated by the act to regulate the rules of budget discipline. This document should also become the foundation of compliance with the requirements of Directive No. 2011/85/EU in the field of medium-term budget framework covering the entire sector of public institutions and illustrating planned medium-term policies with impact on the sector management.

5. BUDGET MANAGEMENT ON THE LEVEL OF REGIONAL ADMINISTRATIVE UNITS

a) Position of the budgets of regional administrative units and the process of adopting the budgets

Under article 101 (3) of the Constitution of the Czech Republic the regional administrative units – communities and regions – are public corporations which may own property and manage their own budget. The budgets of regional administrative units

do not form part of the state budget, rather the budgets of regions and communities are separate.

Drawing up, position, contents and functions of the budgets of regional administrative units as well as the rules for financial management of regional administrative units are provided in Act No. 250/2000 Sb., stipulating budget rules for regional budgets, as amended. The provision of section 2 (1) of this act goes beyond the framework of the Constitution of the Czech Republic to stipulate that financial management of regional administrative units (communities and regions) and alliances of communities is governed by their annual budget and budget outlook. A regional administrative unit draws up its annual budget in relation to its budget outlook and on the basis of data from the breakdown of the valid state budget or the provisional state budget, whereby the state budget defines its relations to the budgets of regions or individual communities and the regional budget defines its relations to the budgets of communities within that region. The budgets of communities and regions are approved by their bodies – the council of the community and the council of the region. The region as well as the community may receive subsidies from the state budget and state funds, and the communities may receive subsidies also from the regional budgets.⁴

Drawing up of a balanced budget is a rule under the law – the law provides that the budget is drawn up as a balanced budget. However, it may be approved as a surplus budget if some revenues of the given year are determined to be used in the following years or if they are allocated for repayment of the principal of loans from previous years. The budget may be approved as a deficit budget only providing that it is possible to pay for the deficit

a) using financial resources of previous years, or

b) by contractually ensured loan, credit, repayable financial aid or income from sale of municipal bonds of the regional administrative unit, for all of which the act uses the term repayable resources.

A positive balance of financial resources of budget management for the current year is transferred for use in the following year to cover budget expenditures or it is transferred into monetary funds. Under section 4 (7) of the above mentioned act the deficit of financial management must be paid from financial resources of the past years or is covered from repayable resources that must be repaid from the budget in the following years. The provision of section 16 (4) stipulates that if there is a danger of budget deficit, obligatory budget measures must be taken. A budget measure is defined as:

a) Transfer of budget resources where individual revenues or expenditures influence each other without changing their overall volume or approved difference between total revenues and expenditures;

b) Use of new revenues not foreseen by the budget to pay for new expenditures not included in the budget which means that the overall volume of budget will increase;

Tying of budget expenditures if covering the expenditures is jeopardised by failure to fulfil budget revenues; this measure reduces the volume of the budget.

⁴ MARKOVÁ, H. Územní samosprávné celky a jejich majetková a finanční samostatnost. *AUC Iuridica*. 2010, č. 4, pp. 21–28.

With the aims of achieving budget discipline of regional administrative units, restricting long-term deficit management funded from debit accounts and strengthening shared responsibility for the development of public finance, the prepared constitutional law proposes a principle of budget management stating that the amount of debt of a regional administrative unit may not exceed 60 % of the average of its actual total revenues for the last four years.

The regional administrative unit checks its financial management against the budget. Breach of duties in drawing up the budget, checking management against the budget, changing the budget and in other cases is an administrative delict and the regional administrative unit is liable under section 22 (a) of the above cited act. Such administrative delicts of the communities are considered by the relevant regional authority within their delegated powers and the delicts of the regions are considered by the Ministry of Finance.

Review of financial management of regional administrative units as well as the management of metropolitan districts of the Capital City of Prague, voluntary alliances of communities and Regional Councils of Cohesion Regions is governed by Act No. 420/2004 Sb., to regulate review of financial management of regional administrative units and of voluntary alliances of communities, as amended. This act also stipulates the subject matter of review, the aspects, procedure and rules of the review. Under section 4 (1) of this act the communities and voluntary alliances of communities are obliged to request by the 30th of June of every year the regional authority to carry out a review, the Capital City of Prague has the duty to request review by the Ministry of Finance or they must notify within the same time limit the relevant authority (the reviewing authority) if they instead decide to hire an auditor or an audit company to carry out the review. The metropolitan districts of the Capital City of Prague proceed in accordance with the Capital City of Prague Act No. 131/2000 Sb., as amended in a similar manner with respect to the Metropolitan Authority of the Capital City of Prague. The review in case of regions is carried out by the Ministry of Finance.

Under section 4 (2) of the quoted Act No. 420/2004 Sb., the reviewing authorities draw up time schedules of reviews for the period from the point of drawing up the plan to the 30th June of the following year. One-off reviews may be carried out by the regional authority in communities that do not have economic activities and where the number of citizens does not exceed 800 persons.

Compliance with the principle of responsible budget management of regional administrative units will be assessed every year if the above mentioned constitutional law is adopted. Act No. 420/2004 Sb. should be amended to include that the report of the review of financial management must include an opinion of compliance with the principle of responsible budget management. The body reviewing the financial management of the regional administrative units should have the duty to inform the Ministry of Finance of those units that failed to comply with this principle. If the regional administrative unit does not comply with the principle of budget management, i.e. the overall amount of debt exceeds 60 % of the average of its actual total revenues for the last four years, it will be required to reduce its indebtedness by at least 5 % per year of the difference between the actual amount of debt and the amount of debt representing 60 % of the average of its actual total revenues for the last four years. It is assumed that the Ministry of Finance will assess compliance of the regional administrative units with the principle of budget management on

the basis of data it will receive from the authorities reviewing management and on the basis of accounting and financial data submitted to the Ministry by the units under other legal regulations. The Ministry of Finance will publish the list of regional administrative units that failed to comply with the principle of budget management. If the unit fails to comply with the principle of budget management, the Ministry of Finance will verify the following year whether the debt of the unit exceeded 60 % of the actual total revenues of the regional administrative unit and whether the debt was reduced as required by the constitutional law. If the units do not comply with the duty imposed by the constitutional law, the ministry will decide to withhold the unit's share of tax revenue allocation (value added tax and income tax under the Tax Revenue Allocation Act). The withheld share should equal 5 % of the difference between the total amount of debt and 60 % of the average of actual total revenues for the last four years. The withheld proceeds of taxes will be released by the tax administrator exclusively for the purpose of repayment of debt obligations of the regional administrative unit. Taking into account the current political situation, it is quite uncertain whether the described measures will be implemented.

b) Indebtedness of regional administrative units

The budget of a regional administrative unit may be approved as a deficit budget only in the cases stipulated by law (see above). These restrictions are based from the legal point of view on Act No. 250/2000 Sb., stipulating budget rules for regional budgets.⁵

The rules for creation of obligations of regional administrative units from loans, credits and other legal titles are governed by general rules of private law. Special rules for financial management of regional administrative units are defined primarily in the Communities (Local Government) Act No. 128/2000 Sb., as amended (especially sections 38 to 44), Regions (Regional Government) Act No. 129/2000 Sb., as amended (especially sections 17 to 23), the Capital City of Prague Act No. 131/2000 Sb., as amended (especially sections 34 to 43). As opposed to the rules set forth in private (civil) law the following restrictions arise from the above laws:

With certain exceptions specified by law, the regional administrative units are prohibited to provide guarantees for obligations of third parties - if this ban is breached the legal act breaching the ban is void;

General duty to dispose of its property in an efficient and economical manner, the duty of care and the duty to control financial management of the property of regional administrative units.

The risk of creation of debt due to issued municipal bonds is under the Bond Act No. 190/2004 Sb., as amended, restricted by the statutory requirement of previous consent of the Ministry of Finance with issuing of the municipal bonds (s. 27 (2)).

The constitutional concept of regional administrative units in the Czech Republic is based on the fact that the communities and regions are public corporations, legal entities of public law distinct from the state, separate also in terms of property.⁶ The provision of section 38 (5) of the Communities (Local Government) Act No. 128/2000 Sb., as amended,

⁵ KOPECKÝ, M. *Právní postavení obcí a krajů - základy komunálního práva*. Praha: Wolters Kluwer, 2010.

⁶ MARKOVÁ, H. Fiscal Decision-making of Self-governing Regional Authorities. In: *Public Finances-administrative autonomies*. Győr: Universitas-Győr Nonprofit Kft., 2012, p. 371.

means that the state is not liable for the financial management and obligations of the community unless the state enters into a contract taking on such obligation. The same is provided by section 17 (5) of the Regions (Regional Government) Act No. 129/2000 Sb., as amended, in terms of liability of the state for financial management and obligations of the region. Neither regions nor communities are mutually liable for their obligations unless they entered into a contract taking on such an obligation.

Under section 4 (1) of Act No. 420/2004 Sb., to regulate review of financial management of regional administrative units and of voluntary alliances of communities, as amended, the communities and voluntary alliances of communities have the duty to request by the 30th of June every year that the regional authority review their financial management or they must notify within the same time limit the relevant authority (reviewing authority) if they instead decide to hire an auditor or an audit company to carry out the review. The metropolitan districts of the Capital City of Prague proceed in a similar manner with respect to the Metropolitan Authority of the Capital City of Prague under the Capital City of Prague Act No. 131/2000 Sb. The financial management of the region is reviewed under section 20 of Act No. 129/2000 Sb. by the Ministry of Finance. The regional authority (within delegated powers) or the Ministry of Finance, or the financial office authorised to do so, carries out control of financial management of communities or regions also under Act No. 320/2001 Sb., to regulate financial control in public administration and to amend certain other laws (Financial Control Act), as amended. Under section 10 of the Financial Control Act the control of communities carried out by the regional authorities within delegated powers is limited to legal compliance, verification whether they dispose of the resources provided from the state budget or other state resources or resources from state funds in an economical and efficient manner.⁷

Under section 13 (1) and (2) of Act No. 420/2004 Sb. the regional territorial unit has the duty:

a) To adopt measures to correct errors and defects listed in the minutes of partial review immediately after learning of them and the duty to inform, including provision of information to the reviewing authority on completing the measures during final review;

b) To adopt measures to correct errors and defects listed in the report on the result of review of financial management drawn up by the reviewing authority or by the auditor and to inform of that in writing the relevant reviewing authority no later than 15 days after consideration of this report together with the final account in the bodies of the regional unit.

The above described information provided by the regional unit must also include a time limit within which it will submit to the reviewing authority a written report on performance of the adopted measures; it must send the report to the reviewing authority within that time limit. The reviewing authority is entitled to control performance of such adopted measures.

A regional administrative unit that fails to adopt measures to correct errors and defects listed in the report on the result of review of financial management, or in the minutes of

⁷ KOPECKÝ, M. K zárukám transparentnosti a hospodárnosti při nakládání s komunálním majetkem. *Právní rozhledy*. 2010, č. 7, pp. 239–246.

partial review, or fails to inform in writing the relevant reviewing authority within 15 days of consideration of the report together with the final account in the bodies of the regional authority, is liable to a procedural fine of up to CZK 50000 under section 13 (1) (b) of the act. The procedure on imposition of a procedural fine under this act is conducted by the relevant reviewing authority. The fine may be imposed within 60 days of the first day of the breach of duty imposed by this law. The fines are collected and enforced by the reviewing authority. The decision imposing the fine may be enforced within two years after lapse of the time limit stipulated for payment of the fine (section 18 (1) (3) (5) of the act).

Under section 20 of Act No. 420/2004 Sb. the review is subject to supervision by the state in case it was carried out by a regional authority or the Metropolitan Authority of the Capital City of Prague or by an auditor. The Ministry of Finance is competent to supervise the reviews, it provides guidance in terms of the methods of review and coordinates the review with financial control carried out by the Ministry of Finance in accordance with Act No. 320/2001 Sb., to regulate financial control in public administration. When supervising the reviews carried out by a regional authority or by the Metropolitan Authority of the Capital City of Prague the Ministry of Finance proceeds in accordance with sections 87 to 89 of the Regions Act, and sections 106 to 116 of the Capital City of Prague Act (section 20 (2)) respectively.

APPLICABLE LEGAL REGULATIONS:

The Constitution of the Czech Republic – No.1/1993 Sb.

Act No. 90/1995 Sb., the Standing Rules of the Chamber of Deputies, as amended

Act No.218/2000 Sb., stipulating budget rules and changing certain related laws (Budget Rules), as amended

Act No.250/2000 Sb., stipulating budget rules for regional budgets, as amended
Communities (Local Government) Act No. 128/2000 Sb., as amended

Regions (Regional Government) Act No. 129/2000 Sb., as amended

The Capital City of Prague Act No. 131/2000 Sb., as amended

Act No. 320/2001 Sb., to regulate financial control in public administration and to amend certain other laws (Financial Control Act), as amended

Act No. 420/2004 Sb., to regulate review of financial management of regional administrative units and of voluntary alliances of communities, as amended

Government draft of constitutional law to regulate budget responsibility – Chamber of Deputies print ref. no. 821/0 – including explanatory report – www.psp.cz

Government bill to regulate budget responsibility - Chamber of Deputies print ref. no. 1097/0 – including explanatory report – www.psp.cz