THE IMPORTANCE OF UNIVERSITIES FOR SOCIETY AND ECONOMY THE EXPERIENCE OF RESEARCHERS FROM THE VISEGRÁD GROUP

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CHAPTER 11

The Consolidation Package and Its Impact on the Business Sector and Universities as Key Educational Institutions

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Abstract: The Parliament of the Czech Republic has approved the Act on Consolidation of Public Budgets. The consolidation package introduced substantial changes on the expenditure and revenue side of the budget with the aim of stabilising public finances and reducing the government debt deficit. These measures will have an impact on the public sector, businesses and households, both internationally and regionally. The importance of universities as a key factor for the country's economic development and competitiveness is emphasised.

Keywords: Czechia, consolidation package, business sector, universities, public finances

11.1. Introduction

Czechia's debt ratio and budget deficit are rising. The associated standard of living, especially as perceived by society, is declining, hence the recovery of public finances is important for both fiscal (with implications for the monetary sphere) and social reasons. All governments know and have known about this long-term problem. Attempts at remediation can be traced in the period c. 2014-2019 (see Fig. 11.1), or even in the years after 2008. However, it was not until the turn of 2023 and 2024 that some major changes in Czechia's economic policy took place. The measures adopted affected mainly the area of taxation, but also some related facts. A consolidation package was adopted, approved at the level of a generally binding legislation, which was Act No 349/2023 Coll., amending certain acts in connection with the consolidation of public budgets (Zákon č. 349/2023 Sb). It was set to take effect globally on 1 January 2024, but some selected provisions will come into power in subsequent years (2025-2027).

In recent history, Czechia has been trying to consolidate public budgets since January 2008, when it adopted the first ever law that tried to stabilise (consolidate) public budgets. This was Act No 261/2007 Coll., on stabilising public budgets, which, among other things, raised electricity tax, gas tax and the tax on solid fuels (Zákon č. 261/2007 Sb). These taxes are generally referred to in the Czech tax system as ecological taxes.

The main reasons for the adoption of the consolidation package in 2023 were:

- efforts to consolidate public finances (i.e. reduce the national budget deficit),
- to address the consequences of high government budget deficits, which had an impact on the downgrade of Czechia's rating (before the consolidation package was adopted); after the adoption of the package, Moody's and Fitch affirmed Czechia's rating at Aa3 with a stable outlook,
- help tackle high inflation,
- eliminate the loss of tax efficiency (i.e. address the higher cost of tax collection).

11.2. Background

The performance of the general government sector in 2022 was largely influenced by developments in the security and geopolitical situation in Europe. At the same time, public finances were burdened by measures that significantly and permanently reduced the tax burden during the pandemic. The government's deficit management was reflected in the level of debt, which was estimated to increase by 2.6% to 44.6% of GDP in 2022. The National Budget Council states on its website a debt figure of 44.2 (Národní Rozpočtová Rada [NRR], 2024).

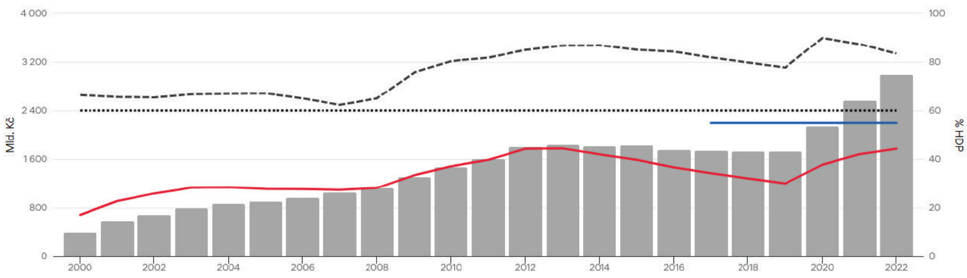
Nevertheless, Czechia's public finances were the seventh (some sources say ninth) least indebted in the EU in 2023, with debt estimated at 45.8% of GDP. At the end of the first quarter, Greece (168.3%), Italy (143.5%), Portugal (113.8%), Spain (112.8%) and France (112.4%) had the highest debt-to-GDP ratios, while Estonia (17.2%), Bulgaria (22.5%), Luxembourg (28%) and Denmark (29.4%) had the lowest (Kahánek, 2023). However, it should be remembered that Czechia is a small open and pro-export oriented economy and does not have as strong an economic potential as more indebted countries such as France or Germany, whose public debt-to-GDP ratio is about 66.1% (NRR, 2024), the so-called debt brake.

The pandemic, the adopted anti-epidemic measures and their accompanying effects have had an impact on the state budget and thus on the overall increase in the need for financing in 2020 and 2021. The state debt increased by CZK 825.5 billion from CZK 1,640.2 billion (at the end of 2019) to CZK 2,465.7 billion (–at the end of 2021), due to the increased emission activity during these years.

In relative terms to GDP, it increased from 28.3% in 2019 to 40.4% at the end of 2021, i.e. by 12.0%. In 2022, the government debt increased to CZK 2,894.8 billion, namely by 42.7% relative to GDP.

For 2023, an increase in the government debt of CZK 3 191.3 billion (43.7% of GDP), was foreseen. The government debt represents the indebtedness of central government budget organisations in the form of government-issued bonds, government borrowings and loans or issued bills of exchange at the end of the year. If the liabilities of local governments, health insurance companies, extra-budgetary funds and other institutions belonging to the public budget system are added to the national debt, the amount of public debt (also known as 'government debt' or 'general government debt') is obtained. For the interpretation as to how countries and governments are coping with their debts, it is useful to compare the debt-to-GDP ratio in addition to the absolute amount of debt. This shows how high the debt is compared to the size of the country's economy.

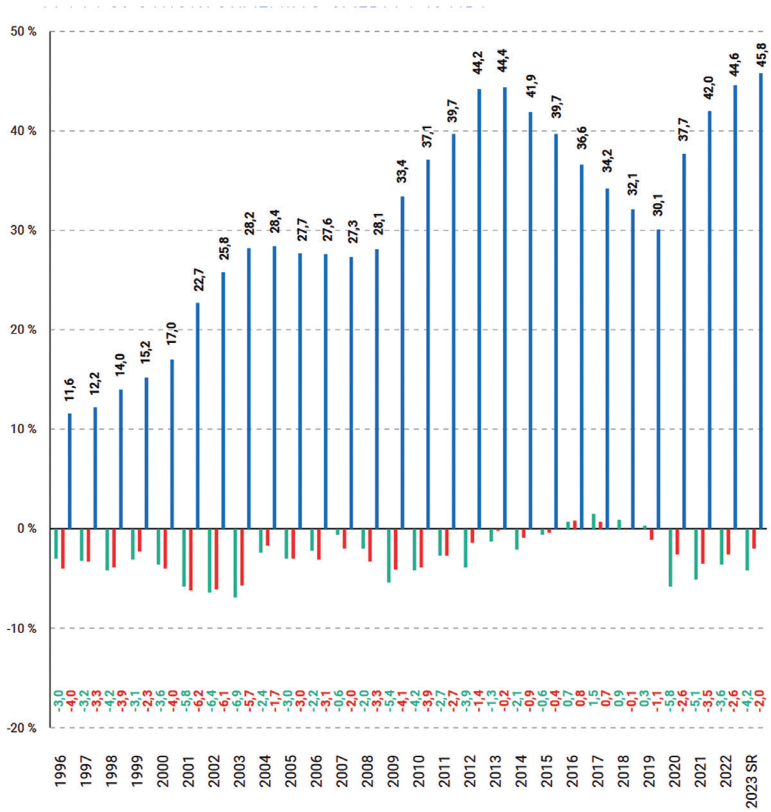
However, the important indicator is not only the level of debt to GDP, but also its dynamics. Countries like Czechia may appear relatively less indebted when debt to GDP is expressed, yet there is often talk of public finances being in tatters. The reason for this claim is precisely the debt dynamics – i.e. the significant debt growth and the lack of planned fiscal consolidation (NRR, 2024).



Explanatory notes: grey bars – debt of the Czech government sector (CZK billion – left axis); red curve – general government debt (% of GDP, right axis); blue curve – debt brake applied in Czechia (55% of GDP, right axis); grey dashed line – average debt of EU governments (% of GDP, right axis); dotted line – Maastricht debt criterion (60% of GDP, right axis).

Fig. 11.1. Public debt (general government debt)

Source: (NRR, n.d.).



Explanatory notes: green bars – general government balance; red bars – structural balance; blue bars – general government debt.

Fig. 11.2. Evolution of general government debt and balance as % of GDP and evolution of the structural balance as % of GDP

Source: (NRR, 2024).

Regarding Fig. 11.1, it is worth noting that for general government debt it is useful to look not only at the debt-to-GDP ratio (red line), but also at the amount of debt in billions of kroner (grey bars). In the case of monetary terms, it can be seen that in times of declining debt-to-GDP ratios, the value of debt in kroner has not declined much. In 2021 and 2022, the increase in the ratio was dampened by the high inflation rate increasing nominal GDP (compare the increase in debt in billions of CZK and in %). Even so, it is clear that the increase in the debt ratio in Czechia in 2021 and 2022 was significant compared to the evolution of the average debt ratio of EU countries, where it tended to decrease (NRR, 2024).

11.3. The Consolidation Package and Its Contents

Act No. 349/2023 Coll. came into force in January 2024, implementing the so-called consolidation or austerity package (hereafter referred to as the CCA) (Ministerstvo Financí ČR [MF ČR], 2024). This should ensure a reduction of public budget deficits by approximately CZK 151 billion in the period 2024-2025 alone, thanks to a CZK 78 billion reduction in expenditure and a CZK 72 billion increase in taxes and other public budget revenues, and this should halt the growth of the national or public debt.

The planned CCCT addresses savings in a relatively complex way, namely by limiting the expenditure financed from public budgets, and by increasing the revenue side of public budgets, both by changing the taxes levied within the tax mix applied in Czechia, but also by changing (abolishing) some exemptions that were applied to the levied taxes until the end of 2023. However, some measures can be considered as introducing more rationality in proving tax facts.

On the expenditure side, the following measures:

- reduction of national subsidies,
- 5% reduction in operating expenditure in each department,
- the abolition of certain territorial offices of the Financial Administration,
- reduction of public sector salary levels,
- a slowdown in the rate of growth of salaries of constitutional officials,
- reduction in the Cultural and Social Needs Fund (FCNF),
- compensation for temporary sick leave and its reimbursement from the salary cap,
- changing the conditions for unemployment benefits,
- reduction of state support for building savings for existing and new contracts,
- adjusting national funding for EU projects,
- abolition of stamps,
- increase in the price of the vignette and its regular valorisation,
- integration of debt recovery,
- reduction of the tax credit for one's spouse,
- abolition of school fees,
- abolition of the student tax credit.

On the revenue side, these are:

- increase in corporate income tax,
- bookkeeping in the functional currency,
- taxation of corporate income on exchange rate transactions,
- increase in the sickness insurance rate for employees,
- increasing the real estate tax and leaving 100% of the tax revenue to the municipalities,

- adjustment of the real estate tax on agricultural land,
- limitations on corporate income tax exemptions,
- limiting the exemption of non-cash benefits to employees,
- abolition of the exemption for over-the-limit meal vouchers,
- reduction of the exemption limit for raffle and gambling income,
- abolition of the exemption for staff apartments,
- elimination of the deduction for union dues,
- abolition of tax deductibility of silent wine as a gift of up to CZK 500 for representation,
- abolition of the deduction of payments for examinations verifying the results of further education,
- repeal the exemption for mining wage settlements and severance payments to miners,
- consolidation of selective exemptions into a general non-purpose limit of up to CZK 50 000 per year,
- repeal of the aviation fuel exemption,
- determination of refunds for so-called green diesel according to standards,
- adjustment of the levy burden on self-employed persons,
- abolishing exemptions from energy taxes,
- increasing the tax on tobacco products and heated tobacco and introducing a tax on alternative products,
- increase in gambling tax and change in the budget allocation of gambling tax,
- valorisation of the minimum tax on gaming machines,
- shifting the 23% personal income tax threshold,
- capping the levy relief for work performance agreements,
- simplifying the registration of work performance agreements,
- increase in the tax on alcohol,
- increase in mineral extraction fees,
- VAT rate reductions and tax cuts,
- restrictions on exemptions for the sale of securities and shares in companies.

11.4. Consolidation Package and a Company

Clearly, the CPR is very complex and amends several dozen generally binding legal regulations. Not all the measures that have been adopted have an impact on business entities, or the enterprise(s) as the basic representatives of legal entities. From the overview of the measures taken to consolidate public budgets, at least two areas can be identified that have or could have an impact on the financial flows in the enterprise.

These can be divided into the main factors affecting the enterprise and additional or sub-factors.

Main Factors Affecting a Company

The following two can certainly be considered as possible main factors:

- corporate income tax is now set at 21% instead of 19%,
- property tax – an average increase of 80% (see below).

At first glance, a two percentage point increase in corporate income tax is not a significant increase. For example, a company with a pre-tax profit of CZK 10 million will not have to pay more than CZK 10 million. At CZK 1.9 million in tax before the increase, now it will pay CZK 200 thousand more. The question will be whether this increase in income tax will be reflected in the final price for the customer. It is logical to consider that a business will not be willing to bear the increased tax costs from its own resources. Finally, the practice of including draught beer from the second reduced tax rate of 10 to 21% had a very clear impact on the final price. However, it is a fact that this indirect tax is inherently price-sensitive and is always paid by the consumer as a taxpayer; the business is only the taxpayer. What it collects, it pays into the state budget. However, the reasoning behind reflecting the increase in income tax in the price so that the business 'still has the same' is relatively logical.

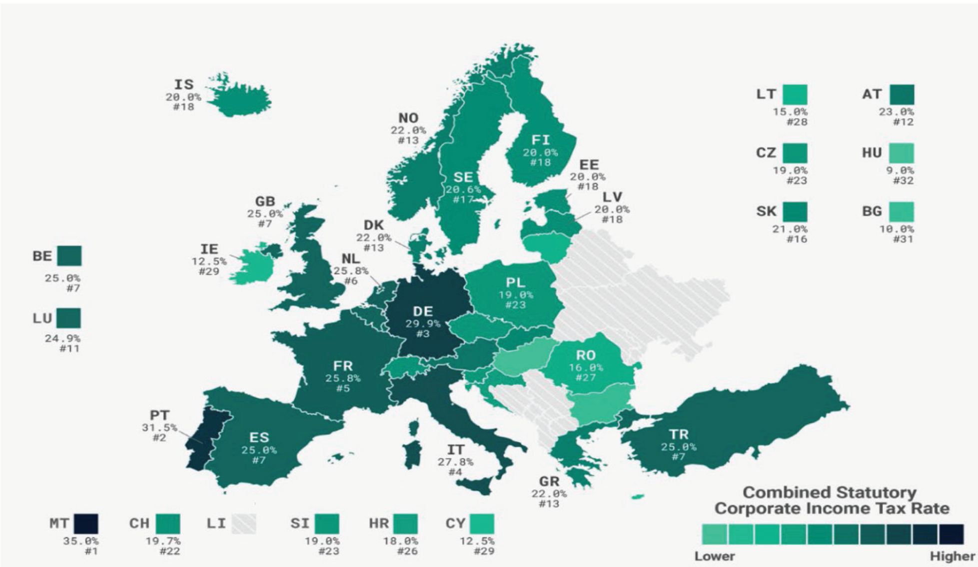


Fig. 11.3. Corporate tax rates in selected European countries

Source: (Tax Foundation, n.d.).

Looking at the corporate income tax rates in selected European countries, one can see that even after the increase of this tax, Czechia remains among the countries with a lower tax burden in this respect (Fig. 11.3).

The adjustment of property taxes is only a logical consequence of the increase in these direct taxes, which are among the lowest in Europe. In Czechia, the ownership of immovable property prevails over the rental of immovable property. Nevertheless, real estate tax revenue accounts for only 0.5% of total tax revenue (including social security and health insurance) in Czechia, before the January 2024 change. Only Austria, Luxembourg and Malta have a lower share; the EU average is 3% (Hypoindex, 2023). The tax burden in terms of property tax was very low in Czechia, 24th among EU countries in the share of property tax revenue in total tax revenue. Therefore, this tax is now being increased.

The changes to the property tax reflected in the consolidation package were primarily aimed at:

- tax increase,
- introduction of an inflation coefficient,
- comprehensive adjustment of the coefficients by which municipalities can influence the revenue from this tax,
- clarification of some problematic issues arising in the administration of the real estate tax, adjustment or removal of unsystematic exemptions,
- an effort to link to the cadastre of real estate and the terminology according to the cadastral law,
- reduction of excessive tax burden on difficult to use land of the type in other areas.

Property tax rates were to increase by an average of 80% from 1 January 2024. For buildings, the tax rate increased by CZK 0.75 for each floor above ground, now it is CZK 1.40. The tax on non-residential space used for business purposes was also increased from CZK 2 to CZK 3.50 per 1 m^2. The new tax increase will also apply to those taxpayers who provide accommodation in a residential building or in flats – these taxpayers will have to file a tax return and declare this fact to the tax administrator. Municipalities could increase the coefficient by a generally binding decree. The current coefficients for 2024 can be found on the website of the Tax Administration (2024).

Even after this tax increase, Czechia will still be one of the countries with the lowest tax burden in this tax. This will certainly have an impact on business, as many companies are based in their own real estate. If businesses were renting, it can be expected that the increase in this tax will be reflected by the tenants in the prescribed rent. Again, it can be expected that this cost will be reflected in the final price of the product or service to the end customer, which is often the consumer.

Additional Sub-factors

The sub-factors listed below can be considered as not having a significant direct impact on the financial flows of the company, but still need to be addressed by the company. They will, however, have an impact on the employees and indirectly on the enterprise. These include the following:

- limiting the exemption of non-cash benefits to employees,
- the amount of benefits provided to the employee up to the limit of half of the average wage will be a tax-deductible expense (i.e. half of the average wage = CZK 21,983),
- the amount of benefits provided to the employee above the limit of half of the average wage will be a tax deductible expense,
- abolition of the exemption for excess meal vouchers (the main impact will be on employees),
- limitations on corporate income tax exemptions and other measures listed above, depending on what each company uses according to its production programme.

11.5. The Importance of Universities for Society and the Economy

Universities are of undeniable importance to society and the economy. They provide high-quality education that prepares students for demanding jobs in a variety of sectors. The research projects and innovations that take place in universities open up new opportunities for technological development and economic growth. Higher education fosters the development of critical thinking and analytical skills, which are key to innovation and competitiveness in the labour market. Graduates often bring new ideas and perspectives to the workplace, stimulating entrepreneurial activity. An educated and continuously learning workforce is also key to adapting to changes in technology and global economic trends. Universities also play an important role in maintaining cultural identity and fostering the development of social awareness and civic engagement. Investing in education thus pays off in the long run as a means to promote sustainable economic and social development.

Universities play a key role in addressing economic and societal challenges. Their research activities contribute to the formulation of effective policies and measures for economic recovery. Graduates acquire the knowledge and skills needed to compete in the labour market and have the ability to analyse and solve complex problems. Collaboration between universities and government and other institutions contributes to effective governance. Higher education thus makes a key contribution to the sustainable development of the economy and society.

Case study of the University of Finance and Administration

The College has a number of experts who have been involved, directly or indirectly, in the process of drafting the Public Finance Consolidation Act. Students have been introduced to the progressive development, but especially to the rationale and meaning of the Act in several courses that are relevant and quite fundamental to the practice. The information was mainly related to the following subjects: Tax System in Czechia, Tax Law, Tax Theory and Policy, Public Finance, Public Budgets, Theory of Public Finance, Financial and Budgetary Law, Accounting, Corporate Finance, Enterprise and Taxes, Financial Analysis of Enterprise (Vysoká škola finanční a správní [VŠFS], n.d.). The process of teaching and education was designed according to their consistency, from courses on tax issues to courses on public finance issues to courses involving direct impact on practice.

Participation in the process and implementation in education was through the involvement of VŠFS teachers (commenting on the legislative process, membership in chambers of auditors, accountants, etc.), internal grant agency projects, student involvement in projects, seminars, and workshops. The educational process is designed so that students gain a comprehensive understanding of how these legislative measures impact the economy and society, and how they can contribute their knowledge and skills to their effective application in practice.

The importance of educating students in topical areas, here the issue of the consolidation package, is shown in Figs. 11.4 and 11.5. This is a survey taken from the media, where Czech citizens were asked whether they understood the importance of the consolidation package and to what extent they agreed with some of the proposed measures.

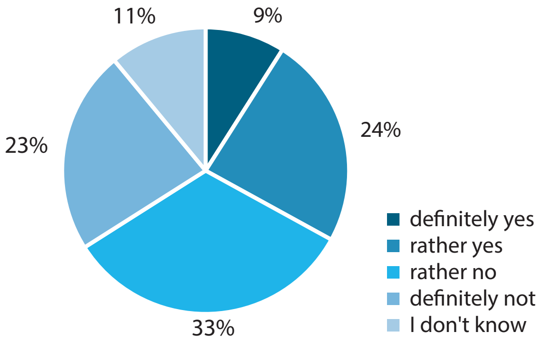


Fig. 11.4. Question: Do you understand the government's key financial measures (the so-called consolidation package) and their concrete impact on the lives of people in Czechia?

Source: (iRozhlas, 2023).

According to the survey, not only the elderly, but also the university-educated, the employed and the unemployed do not understand the consolidation package and its impact on life in Czechia. In all these categories, the level of misunderstanding is around 60%. Overall, only a third of the surveyed understands the government's financial measures, and 33% said they understood the consolidation package. A large percentage of those who do not know what to think about the consolidation package can also be seen in the survey. Among the groups that understood the government's actions, most were young people under 29, but even among those only 33% of the respondents understand the meaning of the consolidation package. More than half answered that they do not believe in the positive impact on the economy. Interestingly, more than half of students and almost half of people with primary education believe in a positive impact.

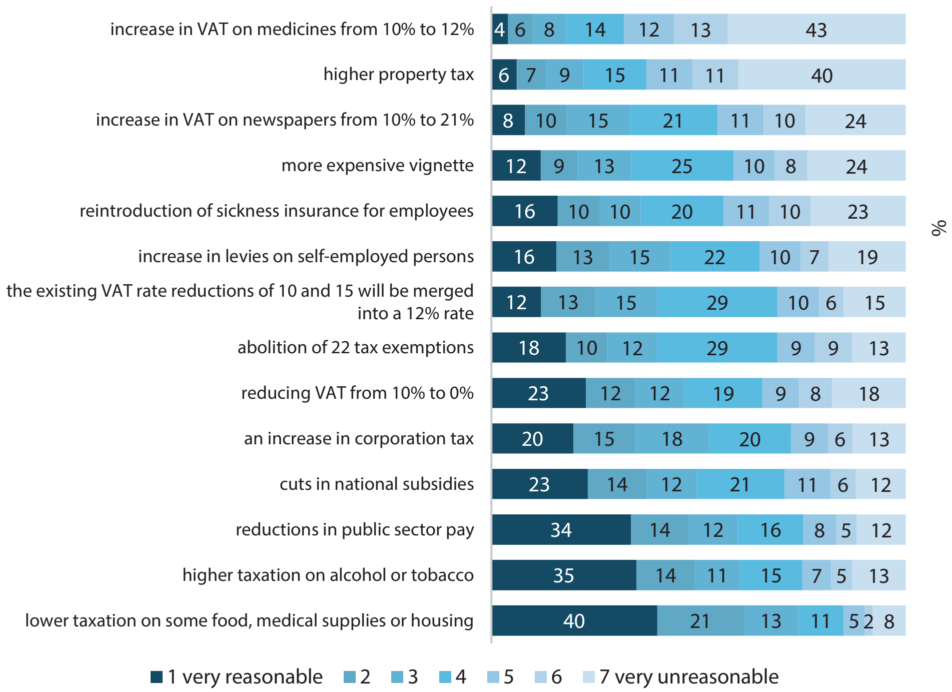


Fig. 11.5. Rating of specific government consolidation package proposals

Source: (Aktuálně.cz, 2023).

The survey produced findings that were not surprising. When it came to measures that will be spent by households, the respondents expressed a degree of disagreement. If it was a measure where there will be savings from the state, it was viewed positively by the public. Czechs understand the need to save, but most disagree with tax measures.

11.6. Conclusions

The tax mix in Czechia has undergone important changes with the adoption of the consolidation package, which has been in force since January 2024. This package has made a number of changes in both the revenue and expenditure areas of the public budgets, with the aim of reducing the deficits of these budgets, starting to reduce the growth dynamics of the public deficit and the national debt, and of consolidating the public budgets in order to sustainably finance the needs of the state in the medium and long term.

The selected changes will have a short-term impact on the business sector, but it can be assumed that the business sector should adapt to the new conditions, unfortunately to the detriment of the end users of products and services, especially consumers. Nevertheless, it must be also assumed that in the medium and long term the consolidation package will provide a sustainable basis for the gradual reduction of government or national debt and thus for the overall consolidation of public finances, which are mainly represented by public budgets.

Universities are an integral part of sustainable economic and social development through the provision of quality education and the promotion of innovation. Their research activities and the training of skilled graduates contribute to the formulation of policies for economic recovery. Collaboration between universities, government and other stakeholders, such as professional associations, strengthens the capacity to address economic and social challenges, thereby promoting the sustainable development of society. An educated workforce is a key factor in adapting to changes in technology and global economic trends, which has a positive impact on a country's competitiveness. Investments in human capital and education thus represent a strategic means for the future prosperity and stability of Czechia.

The consolidation package will have an impact in all areas, affecting the public sphere, the corporate sector and households. The impact will be both international and regional. For this reason, educating the public is also essential.

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